



COMMISSIONERS PRESENT:

CHAIRMAN PAT WOOD, III, Presiding

COMMISSIONER LINDA KEY BREATHITT

COMMISSIONER WILLIAM L. MASSEY

COMMISSIONER NORA MEAD BROWNELL

SECRETARY DAVID P. BOERGERS

## APPEARANCES (CONTINUED):

## FEDERAL ENERGY REGULATORY COMMISSION STAFF:

KENNETH P. NEIHAUS

THAN H. LUONG

KUMAR P. AGARWAL

MEESHA M. BOND

RAYMOND J. MONTINI

RONALD L. RATTEY

CAMILLA NG

JAMES L. AKERS

DAVID E. MEAD

RICHARD P. O'NEILL

KATHERINE WALDBAUER

LAWRENCE R. GREENFIELD

ALICE M. FERNANDEZ

WILLIAM A. MERONEY

BEVERLY A. MOWERY

DEAN WRIGHT

## ALSO PRESENT:

WENDY S. CASWELL, Court Reporter

DAVID L. HOFFMAN, Court Reporter

## P R O C E E D I N G S

CHAIRMAN WOOD: Good morning. I would like to start today's meeting, and all the others that we will have in the future, with the pledge allegiance to the flag.

If you would please stand silent for a moment for all the victims of the tragedy on September 11 of this month.

Thank you.

Also on behalf of all of us, I would like to recognize the heroic efforts of the people in the utility industry, those we regulate, Con Edison particularly, and those we don't regulate, Verizon in the telephone business and natural gas business who did a tremendous job in New York and Washington areas, Washington Gas, of course, in helping the recovery be as short as it was.

So the neighboring utilities really pitched in and showed how this industry works so well together. As the regulators, we want to thank all of them. The president told us to get back to work, so we will. But I would like to start off first by recognizing some visitors from overseas. Mr. Diego Baliano is head of the external relations for our sister regulators in Italy, the Italian electric energy and gas authority. He is assisted by the State Department translator, Professor Vitorio Solaccio. We would like to welcome them.

(Applause.)

CHAIRMAN WOOD: Consent agenda.

SECRETARY BOERGERS: Good morning. On the consent agenda today are E-6, 8, 9, 10, 11, 12, 16, 19, 21, 22, 24, 26, 27, 29, 33, 34, 35 and 37. G-1, 3, 4, 5, 6, 9, 10, 11, 12, 18, 19, 20, 24, 28, 31 and 32. H-1, H-2, C-1, 2, 4, 5 and 7.

On E-10, chairman is not participating. On E-33, Commissioner Brownell is not participating and Commissioner Massey goes first.

COMMISSIONER MASSEY: Aye.

COMMISSIONER BROWNELL: Aye, with the exception of E-3.

CHAIRMAN WOOD: Aye. All right.

COMMISSIONER MASSEY: Mr. Chairman, do we get to congratulate you?

CHAIRMAN WOOD: After about four years of work. I do have to say lots of changes in the past 2-1/2 months since we all met. Well, not 2-1/2 -- well, seems like forever, but been a long time since we met together. I guess I am a lucky guy because I still get to sit next to Linda, but I do want to recognize my predecessors, or Curt Hebert, who did a hell of a lot of good work and we had a good sendoff for him in August.

And I miss him and I fill his seat with probably

not as good a haircut, but at least some trepidation. But that would be true.

COMMISSIONER BREATHITT: Mr. Chairman, may I take this opportunity, before we proceed into the discussion items, to point out that I have an empty seat behind me on this side that is usually occupied by Michael Alexander. I think -- is Mike in the audience today, there is Mike.

As we say at the Commission, Mike has gone to the outside. I would like to thank you, Mike, for a job well done for almost four years. Mike came with me to the Commission from the Kentucky Public Service Commission. It's been a great experience, I know, for me to have you on board as part of my team. Thank you very much for a job well done, and I wish you -- to give you lots of congratulations and wish you wonderful good luck in your position with the Cinergy Corporation.

(Applause.)

COMMISSIONER BROWNELL: I would like to take a minute to introduce my new team, a great group of people who passionately believe in markets and a whole lot of other things, Jamie Simler, Mary Ann Morton, and Jim Peterson. Would you please stand.

CHAIRMAN WOOD: While we are doing that, I would also like to recognize my team that I just pulled together, Alison Silverstein, who joins me from my last job in Texas,

Andrew Soto, who's actually gone today, he had a personal loss in his family with the tragedy, Larry Crocker and Rob Gramwick. Rob is still in the audience because he is still on the other side of the fence for a few days.

(Applause.)

COMMISSIONER MASSEY: Mr. Chairman, I won't introduce my team. They are too tired and battle weary. I don't think they can stand up actually. They are all getting kind of old. But we are glad to be here.

CHAIRMAN WOOD: As am I.

One of the things that I want to do as chairman here is provide an opportunity for us to collegially discuss issues with each other, with our staff, with the parties, as those issues come up and in that light today I want to -- I guess it looks like we had consented a number of the regular agenda items, but some of the things come up in our regulatory enterprise. I hope in this meeting and future meetings we can use that opportunity to discuss policies in advance, discuss what we think about them with each other, hope we synergize off of each other's ideas and let the parties and the Staff know why we are going where we are going and not just where we are going.

So, first step on that is to have a game plan, and under item A-1, I have circulated, after a number of revisions that we have all made kind of seriatim, a

strategic plan, just to put in context for you all have done this, but for the audience and the Staff it's my firm sense that organizations and people work most effectively when there is a clear sense of direction and a game plan. Fortunately, there is already a process in place, as required by the agencies for U.S. government, to do what is called a five-year strategic plan.

What this is before us today is a revision to the existing plan plus a little bit more detail. The next step in the process would be to take this strategic plan and ask two independent Staff groups to look at the strategic plan and develop what I call a 12-month business plan. The business plan is actually a process where we take every task that we will be doing for the next 12 months in this agency, which is the government's fiscal year October 1 to October 1, and actually place under each of our objectives and strategies, as a Commission, these different tasks that we do, prioritize them by category 1, 2 or 3.

3 is also important, I had to endeavor to let people know that and put a date that we are going to get it done by so that we hold ourselves accountable to a time line, with a balance that doesn't have us falling over us every day to keep up with the work but to really plan ahead and run this like a well-run enterprise.

So this will be the first time that we see this

document. I expect we will bring it back quarterly to see if we are all comfortable with it, if there are new items that need to go on it based on changes in the outside world or changes in our priorities, we need to go ahead and recognize that in this document.

But by and large this was a process that, when I was kind of faced with a bunch of juggling balls down in the Texas Commission, then-Governor Bush told me to get with the business plan and he put me together with another agency head, who always did a good job of managing his agency well, so that's where this came from.

So anyway, I would like to put it out there for any discussions or feedback and request that after that we approve it as a body. So, anybody want to jump in?

COMMISSIONER BROWNELL: I would just like to say that I found the process enormously helpful. One of the things I think we have all heard, both internally and externally, is that there was concern about the lack of a vision and the lack of a blueprint.

I think the way this document evolved with really serious input from my colleagues and the development by you was enormously helpful for me to focus on what the priorities are. I hope for the rest of the world. I would hope people would certainly comment on the priorities that we have outlined here but understand that we are pretty

clear and determined in our focus.

COMMISSIONER MASSEY: Chairman Wood, I want to commend you for placing this before us, and forcing us to focus our attention on a document that is intended to succinctly summarize our regulatory priorities for the next few years. It's general in the sense that it's impossible to articulate those in much detail in a three-page document, but it is forceful and clearly stated, it uses language that everyone will be able to understand and has objectives that I find to be extraordinary and absolutely in the public interest and that I strongly support, such as standardizing interconnection of power generation plants, stimulating the use of new technology, advancing competitive market institutions across the entire country, assuring pro-competitive market structures and so forth. I commend it to all of you and I thank our new chairman for placing this before us.

COMMISSIONER BREATHITT: Mr. Chairman and colleagues, this was a process that we developed rather quickly, but it was still one that we were able to really build a consensus around from your initial document, Chairman Wood. It's a good document, it has features in it that I would like to point out such as building partnerships with our state colleagues, with other state officials and with governors. It says that we will

proactively address landowner and environmental concerns, which I think is important as we are looking at ways to enhance our energy infrastructure in the United States.

It also talks about improving our understanding of energy market operations. We have been doing that rather actively for a year but there's still a lot that we can improve upon and a lot to learn as the energy markets continue to unfold, and it also talks about assuring a pro-competitive market structure over the United States, which I also think is very positive.

So, it's broad, it's a good document because it does not tie our hands on individual cases that we will be dealing within the coming year because the business plan is for a year. So I can support it, it's a good document and thank you for placing this before us.

CHAIRMAN WOOD: I appreciate the process is a little difficult when you really can't sit down and work these things out all at one time. I appreciate the flexibility that you all gave me to do this one by one. It's part of making government work in the sunshine and sometimes you get a sunburn, but that's all right.

One of the things I would observe in here, Linda, you highlighted that in your comments, was an elevation of the market oversight role.

I think really, as far as the people were going

to redline against what was the old document and new document, the old document really had energy projects and competitive energy markets as a primary goal. Those are still, of course, principal goals. What this document does, from an optics point of view, is elevate the market oversight goal, market monitoring, market mitigation as we start going through in probably more detail than we want, in recent months, has elevated that to be a co-equal goal with the other two. Certainly permeating all of those goals is to be efficient as to how we administer these resources to do the other goals.

The details, I would ask Mr. Kadden to make that available on the Web page for outside parties. We will continue with our internal processes, but to probably bring back a business plan in two open meetings from now. We, of course, slipped a cycle with the cancellation of the September 12 meeting, but in any event, I would like to ask them for ratification by the full Commission of the September 25 revision B version of the making markets work strategic plan.

COMMISSIONER MASSEY: Aye.

COMMISSIONER BREATHITT: Aye.

COMMISSIONER BROWNELL: An enthusiastic aye.

CHAIRMAN WOOD: Put me down as well. A-1 is done. We will continue working through the Staff project

to generate a more concrete business plan. We have asked the senior Staff to begin collating their tasks to put under the different objectives on the paper. I have also asked as a control group, a group of nonsenior Staff, junior Staff and also some of the leadership of the FERC's union employees to also provide a look at the final business plan before it's ratified. So between now and the time you see it again, you will be going through those two processes, we will get the different feedback from each of the committees to each of you all.

Item A-2 is an item on infrastructure adequacy.

It really is just a follow-up to, really, one of the three primary goals. Of course, to make the markets work is that you have sufficient infrastructure, although we don't play a front-seat lead on every aspect of energy infrastructure, we have a bully pulpit, and we do have a good seat on energy infrastructure with regard to natural gas and hydroelectricity. With regard honestly to -- a lot of the policies we adopt on the electric side do have a serious impact on power lines and the transmission plants get better. We are a player here.

Nora and I had the opportunity right when we were both confirmed, the California Energy Public commission had a public hearing out there and discussed infrastructure in that particular state, but riding back on the plane it

became kind of clear to us this might be California's issue today, if we don't watch it, it could be a national issue coast to coast. Essentially, this is not a point lost on anybody from the president on down to people at Wall Street it's one thing to talk about it, another thing to do it.

In that light, based upon discussions with you all and Staff and outside parties, I would suggest that we bring our full Commission as an open meeting to four different regions of the country, to pull in appropriate parties from the state government and from the industry and from certainly any federal agencies that are involved, which would be varying around the country, to have an infrastructure work session.

The goal there would be to agree on what the facts are, basic analysis of what infrastructure exists today, what the projected demand for energy of all types would be, including any demand-side market programs that exist out in these markets and to get informed on other constraints such as environmental constraints, delivery of coal on the railways, et cetera, exist so that we get the issues out there in one concrete forum. No promises, saying that everything is hunky-dory, it really is but -- it is really an attempt to get the industry and have the other agencies who have a government role, as we do, focused on infrastructure issues and proactively doing

something about them.

So our first invitation was actually already extended from the Western group, the Western governors association is meeting November 1 and 2 in Seattle and have suggested that that might be a good forum to have a follow-on meeting with us to do the energy infrastructure adequacy workshops. So my recommendation to you all is that we do an open meeting out there in that time period and follow that up with one in the Northeast and perhaps December, and also or in the early spring and also do one in the South and in the Midwest in 2002.

Any thoughts or advice on feasibilities of that?

COMMISSIONER BROWNELL: I would like to add that the National Governors Association has been working on these issues. We hope to be working with them and NARUC and other interested parties. It's not enough to simply analyze what the hardware is or is not out there, but to really understand the local policies that may be interfering with or acting as barriers to entry to get new product on line as quickly as we can. So I think these will be very productive, and as our meeting in California was, we walked away knowing a whole lot more. So I fully endorse it.

COMMISSIONER MASSEY: I think this is a good idea, Mr. Chairman. It has my full support. I will

participate in any way that I possibly can.

CHAIRMAN WOOD: Then we will go set those up and work with Kevin Kadden through OEA to set those up and structure those.

The next is item 3 that Curt started and infrastructure of most immediate concern at that time and it continues, even though we had a wonderful, wonderful outcome in California for liability purposes. I tend to give the good Lord most of the credit for that, for weather issues, let's do our infrastructure. Update.

SECRETARY BOERGERS: Mr. Chairman, I think we have a presentation by Ken Niehaus.

CHAIRMAN WOOD: Good morning, Ken.

MR. NIEHAUS: Good morning, Mr. Chairman and Commissioners. At the prompting of the California staff, we sent letters to the CPUC for projects designed to enhance the state's natural gas infrastructure. The state's CPUC response described a number of local storage and transmission projects. In general, projects for So Cal Gas, San Diego Gas & Electric have been completed or are currently being constructed. PG&E targets have been targeted for a number of years. In providing a list, the CPUC made two points. First, the CPUC acknowledged for the state of California that the interstate delivery capacity exceeded the state's take-away capacity but not to the

level of 600 MMcf a day as used by Chairman Hebert.

Secondly, the CPUC maintains the intrastate take-away capacity into Southern California exceeds the certificated capacity for the interstates serving Southern California. Staff has compiled data used by EIA, the California energy commission and SoCal Gas. None of the state supports CPUC's admission regarding intrastate take-away capacity. On another front, Commission Staff has reported that California has recently put online nearly 2000 megawatts of new electric generation with more planned. These plants will exclusively burn natural gas as fuel. With this in mind, Staff believes that the continuing development of both interstate and intrastate systems serving California will be needed.

In closing, I would like to point out that the California energy commission issued its final committee report on the California natural gas infrastructure. That report was posted on their Web site on September 24. In order to match the growing use of natural gas as fuel for electric generation, that report also recommends expansions for both interstate and intrastate gas infrastructure serving California.

CHAIRMAN WOOD: Ken, what did it say how much intrastate, which is our jurisdiction, would be needed to keep up with production?

MR. NIEHAUS: They didn't really come out with specific numbers.

CHAIRMAN WOOD: That may be something we want to follow up in the Seattle meeting out there. Seattle is Northwest but we have to focus on the whole section out there. Thank you for the update. Any questions or thoughts or comments for Ken?

COMMISSIONER BROWNELL: I have a question. I am confused by the different calculations people did. To what do you attribute the difference between EIA's calculations and the California PUC's calculations?

MR. NIEHAUS: Yes, we looked at it. It was basically the different perspectives and there's different systems that originate, that really bring gas supplies into California versus the Mojave system. It starts at the California border but it's interstate so -- people looked at.

Another example was PG&E's line 300, which also serves and brings gas to So Cal system at the Kern River or Kern River meter station, so people treated those capacities different. So Cal Gas also included local production of supplies. All of these numbers were presented in different formats and looked at differently, but we were just trying to see if we could see any way any data that would support the CPUC's assertion.

COMMISSIONER BROWNELL: I didn't see the final report. Did the final report include an evaluation of any policies either at our level or at the state level that might be interfering with the development of projects there?

MR. NIEHAUS: They did make some assertions that things could be improved. I don't know if I want to go over and say whether I agree or disagree with them at this point.

COMMISSIONER BROWNELL: We won't put you on the spot. Thank you.

COMMISSIONER MASSEY: Does your report include any summary of the proposals that we now have before us to increase interstate capacity into California?

MR. NIEHAUS: The memo that we distributed doesn't, but we do have that information in that data.

COMMISSIONER MASSEY: Do you know it off the top of your head?

MR. NIEHAUS: No, I don't. I would have to go back and look at the spreadsheets we have done.

COMMISSIONER MASSEY: I would like to have a succinct summary of what is before us now to increase interstate capacity into California.

MR. NIEHAUS: Okay.

COMMISSIONER MASSEY: If we certificate those

projects and if there's no commensurate increase in take-away capacity, what does that do in the California market.

MR. NIEHAUS: One of the things, Commissioner, is that this electric generation, on where it is being sited, is basically, from what we can tell, it can be served directly by Kern River or it could be served by PG&E. That's generally where these new plants are being sited. So location plays a fact on where and what infrastructure needs to be expanded.

COMMISSIONER BREATHITT: Ken, is the Wheeler Ridge, the Wheeler Ridge border point still projected to be somewhat congested?

MR. NIEHAUS: Yes, Kern River filed their phase 3 expansion. They are bringing more shippers to that point and expanding the common facilities there, which are commonly owned by Kern River and Mojave. We have had protests on that point in that case. CPE 01422.

COMMISSIONER BREATHITT: Do you have any update on Topock?

MR. NIEHAUS: As far as expansions?

COMMISSIONER BREATHITT: As far as the constraints that have been there in the past.

MR. NIEHAUS: No. Basically, the data we saw that there's a match at Topock, the CPUC is claiming that

Ehrenberg, the SoCal system exceeds the capacity going into Ehrenberg but nothing, as far as Topock, nothing in the CPUC data seems to suggest there's a max of capacity in interstate.

CHAIRMAN WOOD: All right. Anything else on the California infrastructure item?

COMMISSIONER MASSEY: Is this reporting to be made public?

CHAIRMAN WOOD: It should be filed under docket 80-01-3. Can we do that. We will do that after this meeting. Thank you.

COMMISSIONER BROWNELL: Mr. Chairman, I would like to ask, will we get this report regularly so we can keep track of what is being done?

CHAIRMAN WOOD: I would like to. Is there any preference how often you would like that or what format?

COMMISSIONER BROWNELL: Quarterly.

COMMISSIONER BREATHITT: Quarterly is fine with me.

COMMISSIONER MASSEY: Can I get this update that I have talked about?

CHAIRMAN WOOD: Yes.

MR. NIEHAUS: Yes.

CHAIRMAN WOOD: We do have a lot of capacity issues that come out of 101 and see that integrated as a

whole, to make sure that we don't overcertify. If we do have needs on the interstate side, then the point of this is to make sure that we have got to do some pushing and pulling with our colleagues at the state level to get additional capacity certified on their side of the fence, we will do it. But that was such a critical part of the whole refund order and debacle that we had out in California over the past 12 months that we cannot really let that recede until we get past that. We will do a public presentation quarterly. If you will provide to all offices what Bill asked for, that will be great. Item A-4 up there.

I will let you know everything is not quite heavy at this time. A little levity is helpful. On the 8th of August of this month, there was, I have to confess, I'm sorry, my friends at the Post, but I wasn't a subscriber at the time, there was a little article by Al Kamen entitled "FERC, the solar panel." It had this interesting use of my name, I thought I ought to read it with Member Pat, third in line to become chairman in the next few weeks. "Some FERC watchers are wondering if this means the end for one of the best-kept secrets in Washington, the solar panels on the roof of FERC headquarters. Former Chairman Hoecker, Clinton appointee, had the panels installed just days before the Bush Administration began. The panels save 3

kilowatts of power, enough for three 60-watt light bulbs, then" -- said there was a little ceremony and a draft press release prepared, not sent out, nothing has happened since to take notes. Some uncharitable teams suspect this is because Bush team doesn't embrace new energy options. I am here to disabuse you have that. We don't have uncharitable teams here.

And Linda saw this yesterday, but I have a habit of liking to go to dedications of power plants, for those of you who need to know. I like shovels and I like toys that I can accept. This was one, I went to a few of these in my last job in Texas, but wind power, good. I am proud of this agency because I do believe that customers do have the right, should have the right to choose what they want. This customer, this building, chose the right, had the right to choose to have a solar panel on its roof.

I should add that maybe the more interesting story about the little article was that there was an assumption that it only powered 50-, 60-watt light bulbs. What is interesting, for those of who you don't look up at light sockets as often as I do, is that there are no 60-watt light bulbs in this agency. There are, in fact, a bunch of 15-watt exact fluorescent he is sent lights which use 1/4 the power of this, so, in fact, Hoecker's solar panels didn't replace 50 of these, they helped replace 200

of these, 4 times, 4 times 50.

MR. ROBINSON: 12 of them.

CHAIRMAN WOOD: You all do the math. Okay, anyway, the world is better off. I want to recognize here our architect Bev Mowery, Bev is right here. Her supervisor Tammy Semega, who we know and to give you a pat on the back for administering a very efficient building. As we have learned from the past, we learned in the West supply is important but also how we manage our demand. I appreciated this Agency long before I got here and had anything to do with it, making sure we steward wisely what we have on behalf of the people. I know you have some facts and figures. If you want to jump in. I will.

Linda, do you want to say something?

COMMISSIONER BREATHITT: If anybody bumps into Jim Hoecker on the street tell him he finally got his kudos for solar panels.

MS. MOWERY: Good morning, I am here to give everyone an overview of the consolidation of FERC headquarters into this energy-efficient building that we hope is also a healthy and pleasant place to work. First, I will describe the situation as it was in 1994, just before we moved into this building. I will talk about some of the goals we had for our new headquarters. Finally, I will discuss how we achieved those goals and achieved

success.

In 1994 FERC was occupied, occupied three buildings, 820 and 941 North Capitol Street and 810 First Street. The buildings were located several hundred yards of each other. Having Staff spread among these buildings presented logistical problems. In addition, the two buildings on North Capitol Street were constructed in the early 1970s and were not energy-efficient. The building at 825 North Capitol Street did have a wellness and fitness center and a day care center. These were not part of the original building and were added later.

The building at 810 was newer and energy-efficient but was not large enough to accommodate all Staff. Additionally, the lease on the 825 and 941 was expiring and the timing was right to take advantage of the opportunity to house everyone together in an energy-efficient, healthy and modern building.

As you can see from the slide, we took advantage of all of the energy efficiency advantages that we could find, and as I will discuss later, the savings have been significant. We also tried to ensure that the building's infrastructure reflected the latest building advantages, from improved air quality to improved wrist supports for keyboards. One of the problems we had May 25 related to ad hoc galleys, kitchens and coffee clubs with old,

inefficient refrigerators and other appliances brought in from people's homes. A more uniform, controllable approach was to provide galley providing energy-efficient appliances. The fitness center and child care center at 825 in this building, we planned them right from the beginning.

The effort to consolidate in one building was a success on many fronts, most noticeably with regard to energy savings. We now have all of FERC headquarters staff in one location. This has solved our logistical concerns. Also, we have begun to realize energy savings when compared to our previous locations, for example, our electric consumption at 825 North Capitol alone in 1994, year prior to move-in, was 3,778,250 kilowatt-hours. In 2000, our total electric consumption was 9,005,300 kilowatt hours. We have doubled our square footage by increasing electric consumption 7 percent.

Our building has won PEPCO's energy competition award for energy efficiency and was recently featured in an article entitled "Leading by example," published by American City and County in June 2001. We are not stopping here, however, we will continue to look for ways to improve energy efficiency and we will continue to stress conservation and recycling during Chairman Wood's term.

CHAIRMAN WOOD: Not your father's Republican

Party. All right. I do want to observe a fact here. An average office building in America uses 18.9 kilowatt-hours per square foot. FERC uses 11.3. So customer choice wins again.

COMMISSIONER MASSEY: May I make a comment, Mr. Chair?

CHAIRMAN WOOD: You may make as many as you want.

COMMISSIONER MASSEY: With regard to the solar panel issue, I would like to note for the record that I followed Chairman Hoecker as chairman of this agency, during that three days I recall that the sun shone very brightly, and I just wanted to make that point.

CHAIRMAN WOOD: Demand matters. I did gloss over A-2, infrastructure conference memo. We have been working with the Department of Energy to do a price responsive demand conference in mid-February to focus on the technology and the programs that are needed to allow customers to respond both into the retail and wholesale markets with demand reductions and response to price, which was an issue that we said in the June 19 order that could have enough support for continuing the California market.

I do have an, I think, angst about that, quite frankly, because I think that would have been a good fix but I will give the retail folks over there credit. They

responded in a way that did a lot of what we need doing, but that does take the heat off of us, to make sure that price demand works. That is for February. Also, to highlight a memo transmission technology, i.e., technology grid would also be a joint DOE conference in February. We will fill in details about that as we go forward.

On A-5, I think it's always good for a new time.

Thank you all very much.

COMMISSIONER BROWNELL: Thank you.

CHAIRMAN WOOD: I appreciate your stewardship of the building. On A-5, delegation of authority, I think always wise for a new team to look at items being handled on our behalf by our trusted OGP, OEC, OGNR and Office of the Secretary to let us know what items are being handled by delegated authority. I just want to see if anybody wanted to add, subtract and ask questions about anything on that list. If not, I don't see anything.

COMMISSIONER MASSEY: I have a question, does the general counsel have fairly unlimited authority in his or her discretion to issue subpoenas?

MS. MARLETT: Yes.

COMMISSIONER MASSEY: That has always been true.

MS. MARLETT: As far as I know.

COMMISSIONER MASSEY: There is no change here.

Okay.

CHAIRMAN WOOD: There was an increase to that. I believe, in the past, actually since I have been here, was there not, for -- Kevin had asked for one round of subpoenas.

MS. MARLETT: There may have been to a specific case, enforcement action that we had undertaken.

CHAIRMAN WOOD: Are you comfortable with that?

COMMISSIONER MASSEY: Yes.

COMMISSIONER BREATHITT: I am comfortable with the items that are delegated to Staff.

CHAIRMAN WOOD: Great. If not, it's our show to run. Let me know, we will talk to them. Okey-doke. If there are other items that could be delegated, we will consider that, too. I know you don't have to do as many copies of everything and it doesn't have to go through the agenda cycle. That can really expedite our ability to respond. We are open in either way to that issue.

Item M-1 is ORM-10, a proposed rule for standards of conduct.

MS. ANAS: Good morning. Mr. Chairman and Commissioners proposed one rulemaking on standards of conduct. You have before you two options, both options propose the following changes to the current standards of conduct. First, both options propose to adopt one set of standards of conduct to apply uniformly to natural gas

pipelines and electric utilities, referring to as transmission providers. The standards of conduct rely on two general principles. A transmission provider's transmission function must operate independently from its marketing and sales function, a transmission provider must treat all transmission customers, affiliated and unaffiliated, on a nondiscriminatory basis and cannot operate its transmission system to preferentially benefit an energy affiliate. Proposed standards of conduct would be codified.

Second proposed standards of conduct would broaden the definition of affiliate such that the relationship between transmission providers and all their energy affiliates, not just marketing affiliates, would be governed by the standards of conduct.

Third, the proposed standards of conduct would not apply to Commission-approved RTOs. If an electric transmission owner participates in a Commission-approved RTO and does not operate or control its transmission facilities, it may request an exemption from the standards of conduct. The only difference between the two options is how electric utilities would treat bundled retail native load employees. Under option A, the standards of conduct would maintain the status quo where the standards of conduct do not govern the relationship between the

transmission function of an electric utility and those employees may engage in sales or purchases solely on behalf of bundled retail native load.

Under option B, the standards of conduct would require a separation of the transmission function from all sales functions concluding bundled retail sales. Under option B, transmission buyers employees engaged in bundled functions for retail native load would have to be separated from transmission function employees and could no longer receive transmission information. This concludes my presentation.

CHAIRMAN WOOD: Thanks, Deme.

Bill, I think it's your turn to go first.

COMMISSIONER MASSEY: Let me ask a question, what we are doing is changing a definition of energy affiliate, the definition, that's the primary thrust of is it, is it not?

MS. ANAS: Yes.

COMMISSIONER MASSEY: Instead of an energy affiliate for gas pipeline, simply being the energy gas affiliate, an energy affiliate would include any energy affiliate of the pipeline; for example, engaged in financial transactions relating to energy would then be subject to the standards of consulting?

MS. ANAS: Yes.

COMMISSIONER MASSEY: Under this rule, are there any energy-type affiliates that would be exempt from the standards of conduct or would they all be covered?

MS. WOLFMAN: I think they are all captured. The way they are is they are focused on energy transmission providers and the rules for how the energy operations are done and the flow of information from the transmission function. So that the rules don't directly govern energy affiliates, but they govern the separation of transmission employees from other businesses.

COMMISSIONER MASSEY: So, the evil that the rules have always been designed to prohibit is the sharing of sensitive information that is gathered by the monopoly and disseminating that unfairly to a covered affiliate and they have monopoly transmission function; is that right?

MS. WOLFMAN: Right. The purpose has been to prevent market power transmission being extended into other businesses.

COMMISSIONER MASSEY: That standard, is that changed in any way here?

MS. WOLFMAN: No.

COMMISSIONER MASSEY: In other words, the codes of conduct that the industry, particularly pipeline industry, is very familiar with, other than a change in the definition of energy affiliate, are those tinkered with in

any way in terms of what conduct is prohibited?

MS. ANAS: The same types of conduct are prohibited. The language may have changed a bit and may be a little bit broader with certain specific types of things, but it's the same general principle, that the pipeline's affiliations with its affiliates are covered.

COMMISSIONER MASSEY: In terms of the open question, we have two drafts. One would apply separation requirement in the codes of conduct to provide the transmission provider from the bundled retail function, am I correct? I have stated it inartfully, but that's basically it?

MS. ANAS: Yes.

COMMISSIONER MASSEY: One draft would not provide that separation. That would be a major change, to provide that separation here. One of you give me your thinking of the pros and cons on that proposal.

MS. WOLFMAN: I don't want to preclude others who might weigh in here. It would make consistent the rules on all transmission functions, interstate transmission functions would have to be completely separate from all sales or marketing functions or other energy-related businesses, so it would be a consistency: I guess there is some thought it would not be a major change in operations for all companies since wholesale sales had to be separated

from interstate transmission and many companies have the same staff for all sales, so that, as a practical matter, it might just be codifying a practice that already exists but it would make clear that transmission information can't be preferentially used for a corporation's own sales versus competitive sales, so it would provide some greater balance.

COMMISSIONER MASSEY: All right. Let me ask a more general question. This would -- about the way this proposed rule works. Suppose I am an energy affiliate and I am engaged in financial transactions that relate to energy. And I am affiliated with a natural gas pipeline. In the course of my business, I gather very sensitive data about the market and I transfer that information to my pipeline affiliate. What is the pipeline's responsibility with respect to the data that I transfer to them?

MS. ANAS: There is no prohibition against information from the affiliate to the pipeline once the pipeline has the information. If it is transmission or customers' information, it would be prohibited from sharing that information with anybody else, or any of its energy affiliates.

COMMISSIONER MASSEY: What if it just posted it on the Web site?

MS. ANAS: Then it would be sharing it

contemporaneously with everybody so everybody would have the benefit of the information simultaneously.

COMMISSIONER MASSEY: Those are the two responsibilities, either don't share the information with everyone or share it with everyone.

MS. ANAS: Right.

COMMISSIONER MASSEY: That's always been true.

MS. ANAS: That's right.

COMMISSIONER MASSEY: So we don't change that.

MS. ANAS: Correct.

COMMISSIONER MASSEY: Thank you, Mr. Chairman.

COMMISSIONER BREATHITT: The energy market of 2001 is vastly different from 1997, or even five years ago on the '89 bill when you voted on those. The restructuring in these industries has transformed our energy markets. In today's energy markets, physical delivery of energy competes with virtual storage of gas and virtual transmission of electricity. Options and derivatives are now commonplace, so it is imperative to me that the standards of conduct promulgated by this Commission should reflect the realities of this new market. This NOPR's aim is to do just that.

Specifically we propose to broaden the definition of energy affiliate to include affiliates engaging in financial transactions relating to the sale of power or

electric energy. Proposal would prevent transmission to benefit affiliates engaged in trading such as asset managers. There is no reason that key information should not be made available to another party when it is shared with an affiliate.

One aspect of the rule, though, that Bill touched on that I have not become comfortable with is the requirement that employees engaged in a bundled sales function for retail native load be subject to the proposed standards of conduct. These bundled sales were specifically exempted from the orders of conduct in rule 889. I believe at a time when the Commission is seeking to build strong partnerships with states, I just don't agree with the timing of broadening the standards of conduct to include native load sales.

I haven't been given any compelling reasons or been stated any compelling problems that would require this approach at this time. There have been no complaints and there's been no evidence that requires this change.

Although the NOPR argues that this proposal doesn't translate into asserting jurisdiction over bundled sales transactions, I believe that state commissions may have some angst, maybe they won't, but I believe they may have some angst.

And there certainly will be other opportunities

even in the near future for us to do this. I do agree with the concept philosophically, I don't have a problem with that. I just don't like the timing. I think this can be done later on, after we do a little bit more bridge building with our state commissions; overall, I support the document. One approach that I don't know if I can garner support for would be to move this from making it a bona fide proposal to asking the question in order to give us a little bit of time with state commissions to explain why we think this is a necessary move at this time.

But I am prepared to -- I haven't made up my mind what my course of -- will be. In keeping with the open and frank exchange that we are having, I wanted to share my thoughts with my colleagues at this time on that one aspect and see if there was any support for asking it as a question as opposed to having it in the document as a concrete proposal.

CHAIRMAN WOOD: Nora, do you want to pipe in?

COMMISSIONER BROWNELL: I think Linda's comments are thoughtful. Linda, how would you suggest we go about asking that question. I mean, is it your suggestion that we adopt option A, somehow get the question out, get comments back and revisit it in the final rule?

COMMISSIONER BREATHITT: We ask a question in the document with respect to divestiture, for example, that's

not a proposal. We are just asking the question.

COMMISSIONER BROWNELL: Right.

COMMISSIONER BREATHITT: So it would be posed along those lines, treat it as a question, this is something the Commission is considering. It would give us a little time with our state colleagues, and it could be revisited in the final rule.

MS. WOLFMAN: The way we would do this is to amend the preamble section of option A to ask the question in that part of the document.

COMMISSIONER BROWNELL: The Staff seems to be leaning to option B. If we take this route, what kind of substantive answers to that question would persuade you that this is something that we ought not to do? There are always jurisdiction issues and concern, to be sure, but what kinds of things would be looking for in those answers?

MS. WOLFMAN: I am happy to defer to others.

MS. MARLETT: I am not sure I would characterize it as what we are looking for. My guess is the Commission will hear a lot from the competitors out there about the problems that we repeatedly hear about, albeit not for a formal complaint, Commissioner Breathitt, to use native load to give preference to one set of customers over another set. Back to the old phrase "everybody is

somebody's native load customer somewhere," it's simply a matter of ensure that we don't have preferences, undue discrimination. I think we will hear a lot.

COMMISSIONER MASSEY: I have a -- in that vein, is there a good operational reason why this change should not be made, Dan, can you or anyone else think of an operational reason why native retail load should be exempted from the standards of conduct?

MR. LARCAMP: As I recall the draft, if there are emergency operating circumstances as in the status quo, they can share the information to maintain reliability -- with a posting of that violation to maintain reliability, so candidly and to build on what Cindy said, a lot of the chatter we hear out there about the relationship with the generation that is supplying native load both in terms of interconnection and ATC, seems to be a fairly steady and recurring theme of unduly preferential treatment for one type of generator, affiliated generator, serving native load versus the independent, nonaffiliated generator that is trying to compete for, maybe not for the customer load there but competing on use of the interstate transmission system, so I think that's why Staff is leaning in the direction of recognizing that fact going forward.

COMMISSIONER MASSEY: The problem is right now, a transmission provider can house all of the same employees

that provided the transmission function with the employees that provide the retail native load, a purchasing function, without any situation whatsoever and without sharing and she can share information freely; is that the way it works right now?

MS. MARLETT: Yes. As it stands right now, if I work for the utility and I engage solely in purchasing on behalf of retail customers. Now "solely" is important, I can go into the control room and get all of the information I want, others can't have that. That's what it boils down to.

MR. CANNON: If I could add one thing. There is always the process, if there are systems or some operational reason that a reasonable entity ought to be exempt from this, our procedures would come in and allow them to seek that kind of way.

COMMISSIONER MASSEY: If there was a regional reason, we provide for that. If there is an emergency exemption, we provide for that.

MR. CANNON: Correct.

COMMISSIONER MASSEY: I must say, Commissioner Breathitt, I do understand the political issue here with respect to federal study relations, but I must say I think this is an opportunity for discrimination that ought to be eliminated. I would be willing to propose this today, and

let's get comment on it. That's my leaning.

CHAIRMAN WOOD: When I saw the early drafts on this proposal, I was pleased that the Dominion/CNG merger concept, which Linda, you outlined, as Deme did too, DE, core affiliates as opposed to having electric world and gas world and never the twain shall meet were important. I have two questions, I confess, not dealing with gas, in substantial part 889 compliance for the past six years.

I was surprised that bundled retail sales were not concluded from the control rule, and asked why, why the current rules are that way and the propensity for a very unequal weighing of the scales is there. I would prefer that, based on that appearance, that this ought to be separated. I would propose if we were to agree to do option B, that we would make pretty clear, though, that if we don't hear from people that they really want this separation, we ain't going to do it.

Knowing something philosophically and knowing it kind of apocryphally is one thing, but if they are not substantial costs and they are not outweighed by enumerated benefits by people who have participated here, then I would agree to pull it down as one who supported that part of option B.

I would prefer, my general preference is when I vote on a proposed rule, a rule I would like to see go

final if nobody told me any importance, so I would be leaning toward B, but I would add on page 13 of B the following concept.

Deme had described what the native load exception being repealed is. I would say at the conclusion of that rollover paragraph in the final role, the Commission may determine that this separation is not required. Parties are strongly urged to provide factual evidence on the costs and benefits of this proposal. Basically flagging which roles would come on that, so sticking with B, but making it clear this is an open question philosophically, I think definitely where Bill just said he was, it makes a hell of a lot of sense and I think practically, there should be a bifurcation, but may be explained otherwise if people have good reason.

COMMISSIONER BREATHITT: Option B is the one with the reg changes.

CHAIRMAN WOOD: Right. It would be the one you would have a preference to vote out, unedited. What I am suggesting is an edit to that that would say the final role of the Commission, we are not going to do this, parties provide factual evidence on cost and benefits of this if they can. That would be my counterproposal to your proposal.

COMMISSIONER BREATHITT: I would like to consider

that and see that.

CHAIRMAN WOOD: Why don't we after lunch break.

COMMISSIONER BREATHITT: I can reserve my vote for this afternoon.

CHAIRMAN WOOD: Why don't we. I will make a Xerox of this. We will look at it over lunch and come back to this at the end of the meeting.

Anything else that we want to talk about before we go to M-23? We will take up M-1 then after the break.

M-2 is docket RMO 111, electronic service documents. I don't think we need a presentation on this. I am fine with what this order does as to what it does. I just wanted to use this opportunity to share publicly what I have discussed with the Staff on this issue. What this order does is ask for comments on the advisability of allowing the Commission to serve documents on parties through electronic means from ourselves outward.

I would like to see us go a lot broader than that. Ferdinand, you and I have talked about this. I would like to see us require, any substantial documents meaning anything greater than 10 pages, will be required to be filed here electronic, period, no paper filing, particular types where Staff would need hard copies, certificate applications with map attached, environmental studies that 50 people are looking through, rate filings

and schedules that have data, that's fine, to have those be under the old rules. But interventions, motions for hearings, all the motions that we get in support of our decisionmaking here largely, I would suggest that we move as far and fast as possible toward -- electronic-only approach toward that.

If we need to hit the print key, if we need to get cheaper printers that don't have those toner cartridges, let's go out for bid, but let's have all the utilities make copies because they can make them cheaper than we do hitting the printers. But we do ask, of the 70 copies that we have filed, do we use more than five on hard copy. If so, those are the ones we need to keep. The others we need to e-file.

10 years from now we will be laughing about paper, but we are not there yet. I would like to hasten that day. I know people feel religious about paper issues so I wanted to put that first. I think it's a step in the right direction. I do know that it will be required in a law that will be in effect of October of '03 that we are required to do a number of things electronically. This is one step in that effort. So with that --

COMMISSIONER MASSEY: Are you proposing to amend this document in some way?

CHAIRMAN WOOD: No. I thought it was a good

platform for me to lay out there early and stake my claim on e-filing.

COMMISSIONER MASSEY: All right.

CHAIRMAN WOOD: Because I can.

COMMISSIONER BROWNELL: Have we created a monster here or what?

SECRETARY BOERGERS: Are you ready to vote on this item, then?

CHAIRMAN WOOD: Yes.

SECRETARY BOERGERS: Commissioner Massey votes first.

COMMISSIONER MASSEY: Aye.

COMMISSIONER BREATHITT: Aye.

COMMISSIONER BROWNELL: Aye, with the hope and prayer that our system is up to supporting this kind of venture.

CHAIRMAN WOOD: Dark clouds. Aye.

All right, E-1. Docket EX-01-1. This is a discussion item on the provision of adequate electrical capacity. I believe we have a presentation from a team on this. Bob.

SECRETARY BOERGERS: We have Kathy Waldbauer, Dave Byers and Dave Meek.

MR. AKERS: Good morning, Mr. Chairman, I will be making presentations this morning. To my right is Kathy

Waldbauer, Office of General Counsel. To her right, David Mead of the Office of Chief Economic Advisor, myself with market tariffs and rates.

The transition to competition in the electric utility industry has raised new questions as to the most efficient ways to ensure that needed electric generation facilities, including facilities that provide reserves, are built. Mechanisms that were appropriate under a title-regulated industry structure may not be the most efficient today.

The study team has addressed a question as to whether in today's world it is still necessary to take regulatory action to ensure that adequate reserve capacity is provided and if so, what is the most efficient method of achieving that goal.

In order to understand the concept of electrical roles, it is necessary to understand certain electrical facts. Electricity must be produced as it is consumed, that is, a fraction of a second before it is used by a load,. It has to be produced by a generator. There is no way to store large amounts of electric energy. Electricity must be produced equal to demand, consumers want electricity when they want it in the quantities when they want it without any advance notice.

Unlike other commodities, that service is not

available. Electricity cannot be directed from paths. Electricity cannot be directed from a generator to designated customer. Therefore, as the system is operated, in order for a electric supply to be reliable, the generation resources and the interconnection system must be reliable for the needs as the whole system, the electricity demand and supply, fluctuates. In the short term other events can unpredictably cause higher demand than expected. Generation plants can go out of service unpredictably. Long-term forecasts are made and generation committed based on assumptions of future conditions.

However, generation may not be dealt when expected. Demand might rise faster than expected. Since plants take several years to be built, available reserves are needed to take up the slack in all of these situations.

In the era of the fully regulated utilities, utilities were under a state-imposed obligation to serve their loads and had an obligation to have sufficient capacity to serve. Within power pools, those utilities that had capacity deficiencies made deficiency payments, were designed to incent the construction of new generation and discourage participants from leaning on the capacity of other participants. This system tended to keep supply in balance with demand and provided the necessary reserves.

Kathy Waldbauer will now take a look at how this has changed.

MS. WALDBAUER: When the three northeastern ISOs first formed, they used this mechanism Jim just discussed, but industry has changed, generation were separated and many became load serving, or LSE, focusing on energy-provided transmission and they sold much of their transmission, but they imposed a requirement on LSE and had ICAP charges or ICAP deficiency charges. As reserves grew tighter, the ICAP market sometimes showed market power being exercised. It appeared that ICAP holders were withholding in the hope they would receive greater revenue from risk-sharing in the deficiency charge revenues.

Recently the ISOs have attempted to address these problem; for example, New England has just instituted an operating mitigation measure, namely 5000 for ICAP. PJM has just required ICAP holders to commit capacity to PJM on a zonal rather than daily basis, both New England and PJM have made changes in the deficiency charge revenues so that now those revenues are not allocated to not just holders of ICAP, but also to LSEs who are compliant with ICAP requirements, but they do not tell you how effective they will be.

This leads us to the question: will we be able to rely solely on market forces to bring enough new

generation into the market to serve as a reserve so that demand will be met and shortages can be avoided? Our conclusion so far is that there are currently obstacles to the operation of market forces that caused some problems. First, most end users of electricity can't respond to real-time prices and curtail their own demand voluntarily because they don't see real-time prices. It is possible to do real-time metering, there are real-time meters, but they are very expensive, they are not widely available currently and it is our understanding that in some cases they would be prohibited by cost considerations.

If customers could see prices in real time and voluntarily curtail, then of course that would increase the amount of capacity available for customers who were willing to pay real-time prices, and in this way, hopefully there would be no or at least much less involuntary curtailment, but we are not there.

Second, end users cannot protect themselves and LSEs are not able to protect their own customers against involuntary curtailments by engaging in advance energy. If a grid operator has to curtail load, it may not have the necessary equipment to allow it or the distribution utility to target curtailments to particular end users or to the customers of a particular LSE. It has to curtail all customers within a contiguous area. So in a situation

where only some LSEs or some end users purchase forward contracts, those purchasers might never experience involuntary curtailment.

Again, there is technology to correct this problem, switching technology, but it is not widely in some places and expensive. Finally, the market does provide signals to incent production capacity reserves but it does so only at extreme volatility and price hikes and sometimes involuntary curtailments.

High energy prices can incent production of new energy but the construction of capacity largely or solely for reserve purchases, which may not supply energy very often and for us receive very limited income from energy sales, in some cases can only be incented through very high price spikes. This makes it very hard to obtain project financing. It's hard to get a letter to finance you if you say my project is only going to be selling energy during very short periods, we hope. Even then the long lead time between the appearance of market signals and the construction of new plants may mean that customers might have to tolerate price volatility and spikes and shortages for a period of years.

If we have decided that we do need to have a regulatory mechanism to provide sufficient reserve capacity, what mechanisms are available to the regulator to

address this problem. That's what Dave is going to talk about next.

MR. MEAD: Yes, as Kathy mentioned, I would like to talk about alternative mechanisms for enduring generation capacity on the one hand, capacity obligations to meet both capacity generation and returns or in turn, obligations to meet only reserves, demand-side mechanisms could be permitted to meet some or all of the demand side capacity obligation. One option is to require wholesale customers to acquire enough capacity to meet their peak energy demands plus reserves. The installed capacity or ICAP obligation used in the eastern ISO is one example of this type. The obligation is enforced by a deficiency charge which a customer must pay if it fails to meet its obligation.

Currently, the acquired capacity must satisfy relative modest requirements regarding availability, price and location, for example. Some critics maintain that these requirements don't provide adequate customer benefits.

Other requirements might provide greater benefits; for example, requiring the capacity to be available to produce energy on peak periods, requiring the capacity to be located in areas that deal with or take into account transmission constraints and limiting prices at

which energy can be sold from this capacity to take -- well, limiting the prices that the prices, that the prices from the energy from the capacity would be sold from.

Currently, customers must meet their capacity obligations near the date of the delivery period based upon the customer's actual peak demand, which is not known until after the fact. An alternative would be to determine a customer's obligation in advance. Customers would then have more supply choices since new entrants could compete with existing customers.

There have been complaints about market power and capacity markets; the Commission should monitor for market power and there are ways to reduce the potential for market power. For example, by establishing the obligation well in advance of the delivery date, so that new entrants can compete and -- by avoiding excessive deficiency charges. Next slide, please.

Another option is a capacity obligation to meet reserves but not the basic peak energy demand. The premise here is that energy market revenues can elicit enough capacity to meet peak energy demand but not necessarily to meet reserve requirements. After all, reserves by definition are utility capacity and rarely receive energy revenues.

One way to implement this option would be through

a board reserves contract, a type of call option for energy. Generators would be paid to be available on reserve and to produce energy only when the market energy price would exceed what is called a "strike price" established in the contract.

The strike price would be set at a relatively high level, for example, say, \$100 a megawatt-hour so that the generator would produce energy only occasionally during periods of extreme supply tightness. By procuring energy in advance, buyers would have more supply options than by procuring the capacity near real time. This would be the potential for market power. Also, capacity payments would be made under contract, would be targeted to generators that run infrequently. The option, this option avoids requiring capacity payments to all generators that receive substantial energy revenues in any event.

Under either of these capacity obligations, customers could be allowed to meet at least some of the capacity obligation through demand-side mechanisms, by demand loads that could curtail usage when directed by the grid operator. This feature could be enhanced so that customers would submit price-sensitive demand bids. Demand-side mechanisms would bring additional choices to the market and thus would reduce market power and price volatility in capacity markets. Of course, large-scale

implementation of demand-side mechanisms may require state regulatory approvals.

These are some of the broad options available to encourage adequate generation capacity. This concludes our presentation.

CHAIRMAN WOOD: We thank you and your team for that. This is a little backwards as to how it could have been, but because of how we don't meet in August I am not sure it's a tradition I want to keep. It's been so damn long since we got together and talked about these things. We were voting about an ICAP order in New England on August 25 or so that the Staff had done a great job helping me understand, it's a world you live and Nora, as state regulator, lives with, but I have not. I want to make sure. It's critical, in California, if we get capacity built ahead of time when you need it.

At the risk of learning from California, bad lessons, I want to know more broadly about how to fix this problem if we aren't faced with the crisis of 100 percent spot market that needs to be revised. So this broad presentation came after we had to vote on the order. The order itself said, I believe, come back with a forward contract, the second slide that Dave went over, come back with that, combined with the third slide you went over, but we put enough wiggle room in there because all of us knew

we hadn't fully engaged on substantive issue here yet but if that won't work, we will be open-minded to it.

This is our kind of chance to at least initiate that discussion about that critical issue of how do we harmonize a competitive market, that is, decentralized, and, you know, business-oriented from an obligation that we know we really ought to have there to be sufficient supplies, that force in excess was a current theme today. We talked about it from the California pipelines making sure you have in excess, not excess I guess, Linda, from our discussion, but enough room for competition to move its elbows to work and that's kind of what we are talking about, and if this is something that will not work, none of these mechanisms were used in Texas, if it's an anomaly, maybe the original question ought to be do we get involved and we have talked about this.

And as their trigger at which we get involved, I would like to throw that out for a question for us to kick around in the future, but at what level do we get involved to make sure that the build-ahead continues. That's the frame for the nice job that these guys did, thinking about the different types of options that we can use. We have seen a number of them already with the ICAP family of options in New England, but I want us to think outside the box as to what mechanisms could work better, could work in

a more competitive market than we have got.

I know there are not -- ICAP and LEP. It has some flaws of its own, it may be the best we have but I accept that. I want to address this issue at least early in the year so we can kind of not let it fall behind until the next ICAP order comes in the door. I am not asking for any vote or action I want to start engaging to see if people have thoughts, from Staff or folks that had to live with the policies we vote out of here and any questions you have for the team, feel free to jump right in.

COMMISSIONER MASSEY: I have some questions. Do you see an ICAP obligation that is primarily related to reliability or primarily related to the price mitigation aspects of having plenty of supply or both?

MR. MEAD: I will take one crack at it. It seems to me that ICAP has effects on both of those areas. Certainly ICAP encourages generation capacity, it improves reliability situation. Also to the market side, that there is more supply, that creates more downward pressure on prices and reduces market power. There may be other ways of addressing those problems and certainly there have been a number of market power mitigation proposals here -- some of which the Commission has approved in various cases -- that can also address market power. But the short answer to your question is it can have positive effects, I think,

on both of those areas.

COMMISSIONER MASSEY: Positive effects both -- clearly as a reliability measure. Clearly, we want plenty of supply so that the grid functions in a reliable way. Also, plenty of supply means that we are less likely to have huge price spikes and price swings. I know there will always be some price volatility, but would we agree that a reasonable policy with respect to reserves would make price swings that are politically intolerable less likely.

MS. WALDBAUER: Yes, I think that's definitely true. We see more generally price swings.

MR. AKERS: Actually, we are talking about the mechanism to support reserves, support the construction of reserves. If you do not have something like ICAP, which provides, in most cases, support for the carrying costs of the reserves, these units have to make up that price and the energy, and the few hours that they sell it, so therefore the price spikes during those hours have to be a much greater magnitude since they have to make their whole revenues from that than if they have a shot of ICAP revenues.

COMMISSIONER MASSEY: It seems to me that the reliability feature of this, and the mitigation of price volatility feature of this, sound to me like almost public goods that we ought to be creating. The benefits of

reliability are shared by everyone. If the system is unreliable, everyone suffers. The benefits of reasonable prices are shared by everyone. If prices are unreasonable, everyone suffers. Thinking about it, I realize your paper deals with the pros and cons of ICAP both as a mechanism and the pros and cons of other ways to achieve the purpose, obviously one of them is a very robust demand side response which I think is an excellent idea. We are just not there yet.

What do we do in the interim to get more perfect market. Do we get this mechanism -- will we always need this sort of mechanism even if markets are designed with a level of efficiency that we simply haven't seen now. What is your thinking about that? Is this some sort of mechanism to ensure that there are adequate reserves, some sort of mechanism set by, let's say, regulators or reliability standards? Will those always be necessary?

MR. AKERS: Certainly not, on the gas side there's not an immediate analogy to ICAP. Why is it this Commission, and state commissions as well, who typically require of their local distribution companies that they have a certain minimum amount of generation? What is the need for requiring that?

Kathy, I think, discussed that at in some length in her presentation.

Right now we don't have much, if any, demand side response; in the short run, if we find we are in a capacity shortage and price hikes, demand doesn't get curtailed. So, you know, in the absence of something else you may have involuntary curtailments or the crude word is "blackouts." Also, as Kathy mentioned, you know, individual customers right now who might want to protect themselves against involuntary curtailments through forward contracting may find that their efforts don't in fact protect them against involuntary curtailments because the grid operator can't curtail this one small group of customers and spare the other group.

Over time, it's possible that technology may allow for some of these advances, you know, for demand side price responsiveness and that sort of thing. We may find we don't need the regulatory imposition of capacity requirements, but we will have to see how things develop.

COMMISSIONER MASSEY: Thank you. It was a very good paper. I appreciate all of your work on it.

COMMISSIONER BROWNELL: I echo Bill's comments in that the paper was good. It is time that we thought about it. I think that reliability in energy is necessary.

I am not sure that ICAP is part of PJM. ICAP does not exist in ECAR; is that correct?

MR. AKERS: That's correct.

COMMISSIONER BROWNELL: Have we seen any reliability issues in there or lack of interest for new entrants to come in and build?

MR. AKERS: Let me just follow up on Jim's response. My understanding is, the ICAP notion has been developed in power pools where there is reserve sharing, often across state lines. It is my understanding that most state commissions have some type of analogous obligation that they impose on their own local individual utilities. Although I am not an expert on retail regulation, I believe that in the ECAR area most of the state regulatory commissions have this reserve requirement. Which at least in part encourages investment.

Now, is it needed to get the right amount of investment, that's, I suppose, an open question and --

COMMISSIONER BROWNELL: I guess it's a question we ought to pursue and get a better understanding of what the impact of different ways of handling this are in different markets. I personally believe that ICAP, and to the extent that it was useful in an old market, doesn't seem to be working in this market. An example I would like to share with you is that Pennsylvania, two-thirds of Pennsylvania is in PJM, one-third was in ECAR, we are forming PJM west, and I am advised because of the ICAP, now called ACAP in the hopes of nobody knows what is coming,

will add somewhere between 40 and \$50 million of cost to the end user. I am not sure that is what we intended when we open our market in Pennsylvania.

Have you taken a look at any of the swings you suggested, Kathy, that in fact ICAP may have presented some opportunities to exercise market power? Have you or anyone in the agency taken a good look and analyzed some of the swings in the ICAP cost in PJM, for example?

MS. WALDBAUER: I don't know if we have done that now. We certainly have some cases before us where those questions have been raised which we will be looking at. There is an appendix to our paper, the new version I sent around yesterday which addresses new cases, which this Commission will be looking at shortly, in which those questions had been raised.

MR. AKERS: I would also point out in the latest rounds of the ICAP orders that the Commission issued, the ISO is trying to address some of the ways that they did see some gaming of the system to provide -- to prevent that in the future, so I think it has tightened up in the past few months. I am not sure that it has totally eliminated any possibilities for gaming but I think it has tightened up.

COMMISSIONER BROWNELL: I would suggest that in view of the commitment of this agency to make markets work that we take a look at yet one more tool as we are looking

at other tools, and we pursue, I think, some of the options that you have suggested to do some modeling, perhaps, to get some comments to see how it would work. I am very concerned we are using an outdated rule, it's not having the effect that theoretically it is to have. Indeed, it's become a barrier to entry, and additional transaction costs are not yielding any definable benefit that I can see.

CHAIRMAN WOOD: Linda and I were mumbling over here from our days, we each add a 15 percent reserve requirement on the regulated side -- I think you were all saying regulated utilities in ECAR would have.

In Texas, that was effective through '01 and if that's the response that would cause them to have a build-ahead, people would quit building because there wasn't a customer -- I mean, the reserve margin is substantial there. I don't want to read too much into that fact, it may be a one-time blurb but I share, Nora, as you do, if in an open market, the closed market seems to be, if there are reserve requirements and they are enforced, that's sort of the second part. I presume the state commissions are doing that, then we are pretty much as kind of traditional. But as more and more states and markets, et cetera, open up, you don't want to have free riders on the system.

I guess that's where the ICAP, at least as it has

been attempted to go through New England and PJM, where we have seen those in a -- in some cases since I have been here, that seems to be most about the attempt to replicate the bill requirement, the 15 percent that some states had in the old world. It's a traditional device perhaps, maybe it isn't triggered until you get below 16 percent, something triggers it. If you are up above it, there's no requirement for everything.

Maybe that's an incentive for everybody to keep the markets built ahead because you don't get this regulatory burden upon you if you pierce the 16 percent floor. I think at the end of the day, Bill, you are right, you have to have something that is a fallback for reliability and for price security. That's kind of what we are banking our whole agenda on here: if you build it, they will come. We have to build it, make sure that happens and not wait, as unfortunately we did out West, for a rainy day to never show up.

I do have a little bit of angst about seeing six cases on our immediate agenda coming up without having us really thought globally about how to do something here that makes sense for transitioning markets particularly, and I would welcome any balm you can put on my open wounds, Jim. Maybe parties can file comments on this docket if they want to. I am not going to do a formal thing but the reason we

have docket numbers is so if people choose to react to things we are talking about, they can virtually insert themselves in the conversation.

MR. AKERS: Many of these dockets concern prior periods and practices that are no longer permitted, to that extent it would not go forward to the future. There are some things that we have to resolve about prior periods.

COMMISSIONER MASSEY: If I could comment also, there's another item that we are going to discuss regarding RTO market design and it seems to me that that's another area where we could take up this question. I think we ought to publish this paper and see what kind of comment we get. Let's let some smart people look at it and pick it apart or say this is a great idea, this is a bad idea, here is the way the Commission should balance all of these competing concerns, this is the way RTO markets ought to be designed.

MR. AKERS: We will also be getting a report from the ISO New England on December 3. In our last order we told them to look at, which they have done in the past, the concept of the forward market and reserves, to also look at their ICAP system, to see, in their opinion, what is superior. So we won't be getting that report December 3 and that would give us some indication. I think we should -- the suggestion in publishing this would be fine.

There are a number of people that have differing views on ICAP or other systems, so I think it would be good to get everyone's views. That has been one of the problems in each ISO. The participants have been so polarized on this issue it's been very hard to come together.

CHAIRMAN WOOD: I think we have a general agreement that we should put this paper out. Kevin, if we could, in our press release on that today and invite comments on that point in this docket number, which is EX 01-1. So it's not a contested case docket, it would be a policy statement, if we want to, so we can have open discussions about that with interested parties.

SECRETARY BOERGERS: Mr. Chairman, would you like a time period involved in obtaining those comments?

CHAIRMAN WOOD: Again, I want to keep this a little fluid. I think it's kind of an urgent thing and will not go away. Ultimately, Bill, the right solution would be in the global context.

COMMISSIONER MASSEY: We will be taking up with the market design questions. We are going to discuss that later in the meeting but fairly soon.

CHAIRMAN WOOD: Just say if anybody wants to react to this document, please do so by the 17th of October.

SECRETARY BOERGERS: Fine.

COMMISSIONER BREATHITT: Before we close out this conversation, I would like to point out that it's been a useful discussion for me and it points out the tension between the need to have sufficient generation supply in times of shortages, and as Bill says, the politically unacceptable price spikes and blackouts that we occasionally see versus the need to have easy entry of new generation and also in order keep prices low. I wasn't aware of the added costs that you mentioned in Pennsylvania, and that was important that you added that to the discussion because we have this good goal of wanting to have reliability in sufficient supply but it also comes at some cost, so we have this tension and I guess that's why we are having this discussion today, to try to figure out better ways to do this, better ways to assure sufficient supply, new entry, and do it at a cost that is reasonable and responsible.

Chairman Wood, I am glad that you have asked for input from those that are thinking about this also.

CHAIRMAN WOOD: And this is a standing invitation, unless it's in contested cases, I think we all benefit from as much feedback and information from the outside world as possible. I think that's how we make good decisions. I certainly learned that from working with you all during this short period of time and encourage the

parties to please feel included here.

We will file this document today in RIMS and also invite comments to it by the 17th of October then.

MR. LARCAMP: Would it be appropriate to strongly encourage executive summaries at the beginning of the document?

CHAIRMAN WOOD: Said like a man who has read that much paper in 10 minutes. Yes, those are always welcome, too.

We will talk again. Thank you for initiating the conversation. While they are transitioning to our next item, I would like to at this point recognize one of our employees. Would Patricia Morton aka "Pat" come forward. Pat Morton is this year celebrating her 30th year in federal service. She began as a clerk at the Interstate Commerce Commission hearings office in '71, and came over when a number of those duties were transferred to the federal power commission, sorry, to the FERC, in 1994 and has worked with the solicitor's office since then, paralegal in the solicitor's office. Her primary responsibility is to prepare the records of all of the underlying agency documents at the U.S. Court of Appeals. I should add that I know Ben Lane and his team would like to get credit for our success in the courts but I think I know who gets the vote. Thank you very much for all of

your hard work.

I would like to present this in appreciation for your 30 years of superior service, signed by Ms. Marlett.

We will continue.

SECRETARY BOERGERS: We have a presentation this morning by Cynthia Pointer and Kumar Agarwal.

MS. POINTER: I guess with five minutes to spare, I will say good morning to the Commission. My name is Cynthia Pointer. We are here to preview the electric transmission development statement that we are performing. The members of the team are myself, Kumar Agarwal, who will be speaking after me in presentation, Meesha Bond, Raymond Montini, Ron Rattey, Camilla Ng, Dean Wright and William Meroney.

The transmission constraint study will identify the significant constraints on the national grid and the additional costs to the customer associated with that constraint. Our estimated date of completion is November 7 of 2001, but that's highly contingent on the cooperation with NERC and the WSSC to provide necessary data we need to finish our analysis. There are two upcoming projects related to the constraint study. The first being western infrastructure assessment that is currently under development, and eastern infrastructure assessment. Next slide.

As an introduction to the transmission constraint study, it's important to know why constraints are important. Probably the most familiar and the one that everyone hears about is threat to reliability constraints in the transmission system, and secondly, an issue becoming more prominent in markets, increased cost of power due to those constraints. Reliability is reliability of the transmission provider to deliver uninterrupted power to the customer on demand. Relief of the constraint in the name of reliability has been the traditional purpose for relieving constraints.

However, most recently in markets, increased power costs has also become a primary reason for relieving constraints, because power cannot move to where it's needed, meaning the customer has to pay more. My colleague Kumar will continue the presentation with some examples of those additional costs.

MR. AGARWAL: Thank you, Cynthia.

Since this is a preview, let me demonstrate for you by way of examples the kind of product you should expect. While our team is in the process of compiling a significant list of transmission constraints, there are 15 in central California and in New York. This is a map of California, approximate location of path 15. Path 15 consists of 6 sets of transmission lines, high voltage,

some of them are 500 kV and two of them are 430 kv vote. The rating of this is 900 megawatt, and according to California ISO, this interface was constrained approximately 14 percent of the time in 2000. About a couple of years ago PG&E tried to upgrade this transmission interface but they were unable to obtain necessary approval.

Next slide, please, this is a map of New York and we see here central east interface in New York, which is from Marcy to Leeds. This consists of seven sets of high voltage transmission lines, two of them are 340 kV, and the remaining transmission lines, this was constrained in 1999 76 percent of the time, according to the New York ISOs.

Taking December 2000 as the example, the cost of constraints was \$17 million to customers. And the constraint costs on the central east interface was \$19 million for the month of August 2001. Next slide, please.

In conclusion, you should expect a transmission constraint study in two weeks and the infrastructure is underway.

CHAIRMAN WOOD: Thank you very much. Earlier, we spoke about infrastructure inadequacy and our intention to begin that discussion with the Seattle trip in November, which is part of the reason why the western infrastructure study is something that is important. Because if we have a

common set of facts -- as we saw from the California issue, those sometimes are a little hard to get. But if we have a common set of facts upon which we can make decisions or encourage others in another sphere of authority to act, then we make real good decisions. I do want to add that this effort you all have done on the transmission constraints is very critical. I know that the national energy plan or strategy has a request that DOE do a national study. I have offered that, what we have falling out of here for the large economic constraints, will be factored into their report as well. Our expertise on their economic side and our expertise on other issues can relate to a document with a lot of you mean if, I think we have a lot of oomph, and on some more details where we can perceive weak spots in the grid we can quibble, or we can put a top 10 most wanted transmission grid on hold and us and the states will rush like hell to make sure it gets filled.

I don't care who gets credit. That is the kind of MO I would like to do until and unless the Congress ever changes authority, then our job of looking after the interstate grid and state's job of looking at environmental and site issues works together. Identifying the need is real important. I appreciate you-all's efforts to do that.

COMMISSIONER MASSEY: What approval was PG&E unable to obtain to upgrade path 15?

MR. AGARWAL: I understand they were unable to get a CPN from CPUC. I tried to research it this morning on CPUC and PG&E side but I wasn't able to find the exact date.

COMMISSIONER MASSEY: Is the \$73 million for December of 2000, was that typical of all of the months in the year 2000?

MR. AGARWAL: The reason we picked December of 2000 was that when path 15 was most congested, transmission for the entire year is 40 percent, that month it was about 76 percent of the time. For recent months I think there is a decline in the amount of constraint cost.

COMMISSIONER MASSEY: But it could be in the range of several hundred million dollars a year?

MR. AGARWAL: That's correct.

COMMISSIONER MASSEY: Well, just this constraint, for example, but all constraints, as I understand the issue, there are at least three ways to relieve a constraint. One is a transmission investment, second is a generation investment or -- third is a demand response and/or a combination -- are you going to focus in your report on the various technically feasible ways to relieve particular constraints?

MR. AGARWAL: At this point in time, we do not have plans to address whatever generation would take care of this problem or -- economically or not. We are going to identify the transmission constraints. You are correct in pointing out, Commissioner, that there may be more than one solution, but I think it's up to the Commission to make a decision. We would simply identify and rank them there are various ways to rank those transmission constraints; one apparent way is to rank them by constraint cost, the second to rank them by frequency of congestion, third way is by duration, how many hours. We are looking into all those numbers. But generation or demand side management is not within the scope of our study.

COMMISSIONER MASSEY: I have another question. I understand there are new technologies, some of them are called fax technologies, high-risk technology, which I understand is a computer chip that allows the existing lines to be loaded with much more confidence, in other words, to a higher level. Yet, there isn't exactly a clamor for investing in those new technologies. Does anyone on Staff have any ideas about why not?

MR. AGARWAL: I think I can answer that.

COMMISSIONER MASSEY: Okay.

MR. AGARWAL: Path 15, California ISO has identified two plans. One plan would entail installing one

500 kV line which is 18 miles long and an additional installation of some fax devices. Those fax devices would increase the capacity by approximately 200 megawatts and this plan that California ISO has identified, they expect an investment of \$270 million. Actually, \$230 million would be required to increase the capacity of the path from 3900 megawatt existing to 5400 megawatt. So an increase of 1500 megawatt would be obtained and it has a mix of things that they want to do, and fax is one of them. But simply doing the fax device doesn't give them all the way they want to go. They want to get another 1500 megawatt.

MR. LARCAMP: Commissioner, to be a little bit more direct, every place you have a constraint, you have generation on the high side of the constraint that doesn't want lower price, competition on the low side of the constraint, into that market. There are a variety of reasons for that. There are a variety of solutions to that, making transmission more of a stand, alone and for-profit business as we are transitioning the competition, but to be real candid about it, you have some stakeholders that are in favor of the status quo because it protects their investment dollars on the high side of the constraint.

COMMISSIONER BREATHITT: Is it the notion, Dan, that some people say a little or a lot of congestion is a

good thing?

MR. LARCAMP: Well, obviously, I don't think the Commission wants, well, Commission may want, I would not recommend that we necessarily invest dollars to be unconstrained 8760 hours a year. There may be a cost-effective amount of constraint that is appropriate on any system, you have to run the numbers to see what level you tolerate both in terms of economic volatility, for example, as well as a reliability concern. But I think dollars drive a lot of these constraint issues with the existing stakeholders.

COMMISSIONER MASSEY: So even though the installation of a fax device might be effective might avoid the siting concerns that would arise from laying a wire, there are winners and losers in installing those devices and the political process is stymied.

MR. LARCAMP: I think that's an accurate statement, yes. I would note, though, that fax technology, there are some demonstration projects, I believe there's one in New York where they are going forward with this on a demonstration basis, but the entire infrastructure debate, I think we have got to keep focus that there are winners and losers. I think the Commission's job is to sort through the conflicting market rules, establish those and let the investment climate operate to build the

cost-effective infrastructure.

COMMISSIONER BROWNELL: When you say there are winners and losers, you are referring to the market participants themselves. The ultimate loser, if we do nothing, is end use consumer under any scenario.

MR. LARCAMP: Correct. The customers will be, I think, unequally benefited by removing some constraints. To the extent that lower price generation is not available to reach a broader geographic market, there may be temporal benefits to certain groups of customers, I think, over the long term. I think where Staff is committed with a market solution, over a longer term it is in all customers' interests to have the largest geographic markets we can operating for these energy commodities.

COMMISSIONER BROWNELL: I just have a couple of questions. That was a great presentation, I look forward to the full report. I think Bill has identified something important. While I wouldn't want to slow down the report, I think we want to add on some of the options at the top 10 constraint points about what different things could be pursued and maybe do that at a later date. I know we will have a conference on transmission technology. You mentioned that you would make the deadline for this report if all the parties cooperated in providing the data. Are you having any difficulty with any particular party in

getting that data and is there something that you would like us to do? You can name names.

MS. POINTER: I guess it's my understanding that so far American WSSC has been fully cooperative. We are still waiting, I believe, for a format that we can manipulate a lot easier from NERC. We are working with them now to get the data in a format we can work with. I don't believe we have come up to any problems with regards to that yet. Tom can add a little bit more to that.

MR. LUONG: In 2001, there's a tremendous amount of data as far as the transmission and allows us to do a meaningful analysis, so right now I would like to get the right format for us and we can get our own data. It would be a lot of data, take a lot of time, you know, to get it. It depends on how soon we get that data.

COMMISSIONER BROWNELL: I can't always speak for my colleagues, in this regard I suspect that I can. For those parties on whom we are waiting, I would make this a priority. It's an economic issue that our country really needs to grapple with. The longer we delay the greater the price is. Let us know if you need help in that regard.

MR. LUONG: Thank you.

COMMISSIONER BREATHITT: I would like to thank you for a great presentation and a compilation of all of this information as we really continue to focus on various

challenges and segments of the industry and transmission constraints and the need to improve our infrastructure is certainly one of them. Thank you for that. I am looking forward to the report.

CHAIRMAN WOOD: Ditto for me. Thank you very much. Hop on to item E-3, which is a discussion of RTO tariffs.

SECRETARY BOERGERS: I don't believe there is a presentation on this item.

CHAIRMAN WOOD: It's been more than two months since we did our RTO orders in early July. A lot has happened, both in our world and in the world, and I think based on my experience about how to get things done, it's important for us at this stage I think to get some additional focus and guidance to get this transition over with.

Overall goal I think articulated by the Commission very well in order 2000, I think really brought home to me the conference that you and I have talked about. This June 19 was one of those watershed days for me not because of the call that went out. But that's when I got to sit right there and we watched a number of parties, I think, with a couple of exceptions but a strong minority of exceptions, expressed exasperation. If there was ever a time for this agency to lead, it was on June 19 at the

conference here. So I would like us to, as we did in July and I think thoughtfully I done in July, but take it to another level and really get there.

It's been difficult for me to get in my mind a game plan for getting this transition over with, and I have been casting out and about to outside parties, to our fine Staff, to my wife, to help me focus on stuff that has nothing to do with work but to kind of think through a process, to get through a thought pattern here that we can all work on and that will be as inclusive as possible, not only for the four of us and our future colleagues but for the parties who have to live with the seeds that we sow.

So in that mind set I have gotten to a place, I want us to try to get together to a more crisper place but I want to throw out some thoughts.

The RTO effort appears to me to be two tracks. One is an organizational track. What organizations are going to be the conduits for this, what is hard to describe as anything else but a delegation of authority from us and for organizations like NERC and others to accomplish a lot of broad and important goals for this country. So organizational goal is one I think we did a lot on in June, July, excuse me, July 11 with some pushback, some feedback, pro and con, and I am open to thinking through how we do that. But the second track is one that we haven't really

frontally addressed but that's the substantive track. We set up these organizations, what is it they are really going to do when they grow up. We have done a lot of little discrete issues and orders as they come through. Largely the ones that I voted on since I have been here were, this is close but you are not quite there on constraint, congestion management, penalties on scheduling time frames, whatever, on market monitoring, there was a lot of pushback but it was in this awkward contested case format that allows us to say no and allows a party to try something. Sometimes the parties that are putting forward don't really speak for the broad slice of who will be affected by an RTO.

So I wanted to try to think of a way to get us out of what I consider to be a dead-end, slow, inefficient, one-sided rut and get it out into a process that I felt more comfortable with because this agency is the one that taught me how to do it in the gas end. Which is throw a real broad blanket and ride herd every day of the week until the job gets done and get the best ideas in the country to play.

So, with that in mind, my recommendation goes along this line. On the organizational effort, we have got a number of different procedural vehicles out there that are moving forward, Northeast and Southeast mediations have

had reports issued by the ALJs that we asked to see what could happen. I do, from my initial skimming -- that's going to be some more work I have to do personally because this is important, initial skimming. They took two different tacks. They both may work, they have two up and going in the direction where we can sink our claws in there in the next three to four weeks, as a Commission give them feedback. We are involved in the MISO Alliance settlement that brought in two large organizations throughout the middle of the country. I understand a status report is coming from where they are. They have gotten a little agitated. Didn't seem like all is well there. I want to have that to be something that we address on the merits. If we can have that in early November, or we better, so we can decide what, if any, tweaking needs to be done to that settlement.

I am not a judge, but I am pretty flexible as to the structure. What is important to me is that the guts of what they do is consistent. My intention is to, probably at our first or second meeting in October, put these efforts on for our discussion and hopefully some action by us as to what we have got. I think some guidance today on the western United States would be useful. First would be RTO West and Desert Star need to go ahead and marry up, flirtation is cute but we need to get serious here.

Although the weather was good, California is not healed yet. Nora had a good suggestion which she shared with us about doing audit of the operations of the ISO, Nora, I will let you talk about that in a second, and make recommendations to us about changes that are needed for that effort.

I do note with a lot of pleasure, there's an item on our agenda E-38 today that I held back only for the purpose of praising it, but it was an effort in the western systems coordinating counsel and the two RTGs that were set up under FERC prodding in the last decade to merge their efforts to become FERC reliability region and long-term resource planning region, which are two, in my mind, the most important. It's not as important to me, to be persuaded otherwise, I think the single western RTO be pursued today. I think we have to handle California on its own track, because it was an effort that we started several years ago that I think needs some further attention and help at this point, but encourage the good efforts that we looked at in RTO West and Desert Star to start building up for the rest of the west to see how broad we can get from there. That's my thought on where the maps are, but honestly I have to say my real salvation comes from the substantive docket I would propose that we do. Initiate, under Section 206, rulemaking on market design and on

market structure, to translate the eight RTO functions that you all outlined, and I think they have stood the test in time in order 2000, into concrete proposals for the RTOs.

I would lean strongly toward market design standardization but not be fully fixated on that. I am a big fan of standards but I think we also as regulators know there's some time for regional diversity on these things, and flexibility can certainly be part of that. I would make that a rebuttable presumption, that we try to have a coast-to-coast market standard design as much as possible so that we really do benefit in the long term of competition, that people can enter these markets, enter them in Oregon, Ohio, Oklahoma, and they will all be the same.

I appreciate our approvals to set aside the week of October 15 through 19 for some advance workshops to that NOPR, to focus with the brightest minds in the country and on our Staff on a number of issues that are critical to defining market design and market structure. Those include, but are not limited to, congestion management cost and investment in transmission-related facilities, market monitoring, transmission planning, business and reliability standards. What is the nature of transmission rights, what are -- would be the correct solution.

The Section 206 proceeding that this would be

would yield a new pro forma to replace OATT's on Order 888 and would require all public utilities on RTOs both.

That's kind of the process suggestion I have got. A couple of other thoughts I want to print out is have you -- Staff has thought a lot about the December 2001 date that was put in order 2000. I would recommend that date be changed to one by which all jurisdiction utilities elect to join RTO organization or have us review or have us revoke on a prospective basis their market base rate privileges. I think we would do that under 206 but I would be open to considering that as well. I would also recommend we don't do mergers. I understand from talking to Jan this was something you all decided not to do, so that would be something, if a majority of us want to do that. I would say mergers relating to entities who don't become part of an operational RTO ought to not be handled here.

I think at any stage, we have got to -- if a public utility under our jurisdiction is not part of these RTOs, I think we have to take a hard look at transmission rates in order to ensure that they remain just and reasonable in the context of a broader RTO weight that recognizes the interdependence of the power grid. That would be the stick to characterize that.

I think the success of the gas agenda was that agenda was -- they were not legally mandatory that you

become order 436 or, I'm sorry, if you did hold out, but I think there needs to be an old world and new world. The old world needs to have the new world sitting right next to the person who wants to stay in the old world. The new world needs to have the risks and rewards of the new world fairly borne by the people who choose that. I have taken to heart, Linda, your thoughts about mandatory and voluntary. Although I might disagree a little in what we did in July was mandatory, because I think people that aren't in the hunt weren't required to be in the hunt, the people who have opted to be in the, RTO that we start telling them how a RTO ought to look. I do that in interpreting our rules on scope. The Commission determined at that point that the scope was just not good enough when they were smaller and I am open on that. Quite frankly, you standardize what they do. You could have 100, but as long as they do the same stuff.

At this point to me, four is a good place to land, five if you count these overheads and Staff levels and these issues get to be pretty, they get to be pretty costly if you don't try to achieve some economies of scale. Mine honestly has been driven by the fact that a lot of these are expensive, more than by the substantive aspects. I think you do somewhat resolve things if you are in one umbrella organization that may not have to be dealt

with by the rule, but we won't be doing one coast-to-coast RTO. I think despite the urgings of some, that ain't going to happen. We have to be pragmatic about what we work but also recognize they all have costs to them.

I am willing to kind of keep working around that but I really prefer at this point to kind of focus on the arcane or much more important issues of what does an RTO do and how quickly we can get them up and operating to get them to do what we need them to do. It was depressing to me, since we met, I always told everybody what I do never appears on the front page so you won't understand it, I only talk about sports and weather but Washington Post, not only on one day but three consecutive days, ran the energy story so I had to change my shtick but it was a sad reflex, that the wholesale markets had functioning wholesale markets, California and Texas colored in, then the Northeast RTO, the rest of that map was white.

I will do that as my report card while I am here coloring the rest of that map. I am pretty open as to what colors were used out of the Crayola box, but I do think we have to get it, but I think we need to get the wholesale competition colored in.

We have some pending RTO filings here, I don't quite frankly need know what to do about that, but you can make a recommendation and get Staff. I think it's

important, I have heard Linda say this, Bill say this, cost-benefit studies are important for me. Quite frankly, you don't get a cost-benefit study for saying it's important that the sun come up and set but there are people not as immersed in the arcana of RTOs as we are that would yield customer savings. I think it's important we do, we look at the costs of the RTOs versus the existing structure and look at the benefits we achieved. I do note with pleasure a recent study by Merit for the Northeast RTO that I think actually upon reading was very credible. We look forward to responses, pro or con, and to more of those.

I think outside parties that support an RTO agenda have the resources to do that that this Commission may not have and I strongly encourage you to do so. But we need to do our own as well.

We talked about this a little earlier today, but I think the abruptness of our decisions in July on RTOs did cause some ruffled feathers from a number of our state colleagues. I would say that I got probably twice as many calls from people who were thrilled that we were stepping up to the mat, they are important colleagues to have in this transition because they are on the front line. Three of us have been there. Bill, you are the honorary one there already. But I think we have got to sensitize them and others for the way we move forward.

I think one important step to take on that is at the workshops, and in October have state commissioner colleagues be really the first in the line because, again, we are putting the markets together that ultimately affect their direct retail customers, and we want to be colleagues in that effort and open to their concerns, and I think some issues may be more of interest to them and others. Market monitoring, I know Dan, Cindy and Shelton went down to Florida and had a good meeting with Chairman Jacobs and Staff. I think market monitoring is important. We learned that from California that it is probably something we need to do more collegial work with and get done.

There are other issues, rate recovery is critical, cost recovery is critical, that's important from the utilities that they invest in RTO and get their money back. We can say a lot but quite frankly, the retail regulators are ones who have to do a lot in that regard, I wanted to say publicly we would do it in July. I am pleased with where we are going in direct, but sometimes there's a better way to get there than we did. I think we probably could have done that better. I know we all talked about that. I wanted to say it publicly in an hour and a half.

I just prefer a rulemaking context in general to close out. I think the congested case format has been extremely frustrating for me. There are so many issues that I want to talk to a lot of people in this room and the people watching from the home audience about, under the law cannot do and will not do. Any effort we can take to get these things into discussion format where we all have the give-and-take with each other, with our Staff, and with the parties, is one that I think will result in the best possible outcome for our policy. That's my thoughts on RTO progress, and I would welcome any suggestions or feedback or thoughts about where we want to go.

COMMISSIONER MASSEY: I thought about just sitting here and smiling like the Cheshire cat and not saying a word.

CHAIRMAN WOOD: That's okay too. It's lunch time.

COMMISSIONER MASSEY: I really appreciate how you're taking the bull by the horns on these very tough issues. Your plan has my wholehearted support. I think it's a very good idea. My only regret is that we couldn't have done it sooner. We ought to do it now and focusing on the market design issues, the guts of the RTO is an excellent idea.

I agree that we should perhaps create a strong

rebuttable presumption that certain market design features ought to be adopted all across the country. If someone can come in and make a complaint argument that those features should not apply in their region, we'll listen to it. As they said, a marketer or a seller in one part of the country ought to be able to move seamlessly to another region and understand the rules and to be able to trade. I think achieving this goal will help a lot of small businesses that want to emerge that simply don't have the resources to figure out eight different, ten different, 15 or 20 different sets of rules. So I commend you for taking the bull by the horns. This approach has my wholehearted support.

COMMISSIONER BROWNELL: I'm really excited, although I'm already tired thinking of that week but I think this approach makes sense from a variety of standpoints. One, we're dealing with the issues altogether so that when we finish the puzzle, we know that the pieces fit together. I know that some of the responses to creating markets have failed because they didn't figure out how those pieces ultimately would fit together. I think from that perspective, it's going to work.

From the second perspective, I think it will bring certainty, and for me, this is all about economics and at a time when we really need to stimulate our economy, I

think that getting the RTO issues resolved will bring investment not only into the incumbent utilities but into all of the new technologies and all of the growth opportunities that are going to be available. It's very clear from Wall Street. It couldn't be clearer.

So I would encourage the participants to come in a disciplined fashion and stick to the substance. I don't think we envision, nor will we tolerate this as a platform for debating whether we need RTOs or whatever other agenda items are out there. We are really going to focus on the issues, and hopefully collectively, with smart people, as you said, come up with standards, and whether it's the same answer for across the country or there are variations on the theme, we will walk away with some answers.

I'd like to talk a little bit about the western market. Upon reflection and based on some of the feedback we've seen, I think that while ultimately that is a goal and an important goal, the development of RTO West and Desert Star I hope to put on a fast track. I know the governors are putting some attention to having those developed without seams. We understand that California needs work and that people are concerned with whether they're ready to join that larger entity; hence, I think the call for the operations audit. We've asked the California ISO to do a lot in a short period of time.

They took on the responsibilities for the PX.

Many of the fixes that we have identified depend on the successful operation. So I would hope that cooperatively we would work on really taking a look at all of the processes, the protocols, the organizational structure, and come out with some recommendations, so all of the market participants can have confidence in that structure as being able to function successfully.

Ultimately, I think ongoing audits are probably a good idea for all of the RTOs so we can be sure they are capable of doing what we ask them to do, particularly in the market monitoring. I view that as kind of a positive step in the ongoing solution to create a real market in California so that in fact it is an attractive marketplace to their western neighbors.

COMMISSIONER BREATHITT: I don't know where to begin. Chairman Wood, this is a very ambitious document. I agree with my colleague, Commissioner Brownell, that we've got a lot on our plate and we need to be fortified for the week of October 17th, and also implementation of some if not all of these features in the memo. I just got this memo. Although you and I had had a pretty broad discussion of some of its features prior to that, but I haven't had a whole lot of time with it. I do appreciate your words about the July 12th Order. I agree with you that there needs to be

some flexibility on market design.

There was a reason we didn't standardize everything all at once. We did want to see various plans percolate and various plans actually at work, so that we could see good features as well as features that did not work so well. So now may be the time to approve some standards.

I would caution against one hundred percent hard and fast design rules all over the country, in order that we might still be able to have appear throughout the country some features that we don't want to stifle through having real hard and fast standardization of market design. But I don't think you had that in mind, stifling creativity. So I appreciate your points on flexibility.

With respect to the West, I think there is a delicate balance right now with RTO West. I would like to see RTO West move forward and be able to be implemented. I don't know much about the Desert Star effort. I think I'm going to hear from them in a pre-filing mode next week. So that will be informative for me.

Nora, I think your concept of an audit for Cal ISO will be beneficial and I hope will give us the results that we need to move forward with important things in their market, such as governance and independence.

I have to hand it to the staff of the ISO.

They've been under a huge pressure cooker for the last year and I think they've done a pretty terrific job under the circumstances that they've been in. I think your idea to be able to give them the support that they need going forward, and I'm sure the audit will produce that for us and for them, and for the market participants in California.

Since I haven't had this document but a day-and-a-half before today, I don't know if I can give tacit, unequivocal support to some of the recommendations in it, but you weren't asking us to vote, so I'm sure we can continue discussions on those.

I don't know really what it means to say that market-based rates would be prospectively revoked, whether that means any new applications that come in after December 15th requesting approval for market-based rates, or whether it means that all market-based rates by an entity could have the possibility of being revoked following a Section 206 investigation. Then I have questions on what do you replace that with. I'm assuming cost-based rates and how long would rate cases and what would you use in the interim.

So since I haven't been able to ask you those questions, I have those parts of the memo that I would like to further consider and ask you about. I also agree with you that the December 15th, 2001 date has always been

ambitious. It was ambitious when we voted out Order 2000 in December 1999. We haggled over whether it should be December 15th, 2001 or whether we should give a little bit more time and actually go into 2002. But we settled on that to keep feet to the fire, to keep progress moving forward. And we see that we do need a little bit more time to approve RTOs.

I am pleased that we're going to be, as Bill says, taking the bull by the horns and dealing with the issues in October with respect to the northeast and the midwest and the southeast. I do think we need to keep moving forward on these, but I don't have a definite idea in my mind right now of what to do in the midwest. I was very, very pleased when the settlement and all the efforts that that took came about, and hoped that that would prove to be the result that the midwest section of the country needed. I'm pleased that the SPP has made its decision because we left that open for them. I know all of that is not settled yet, but with respect to the southeast, the judge's report told us that we've gone from four entities to two and with the northeast, the judge's report on that put forth a business plan to result in an operational entity around the '03 time frame, maybe early '04.

So we have progress that has been made, progress that's being made, and with what we do in October, we'll

continue that. I do agree that it makes some sense to do a rulemaking on market design, but I'd like to also recognize that, as I said earlier there, I think there should still be some flexibility built into that so we continue to get good and new ideas. So those are my very quick thoughts on a document I haven't had a lot of time with.

I have not thought too much about the conditioning mergers. We've almost gone that far in certain mergers by saying that we expect entities to join RTOs. I think that's the latest language that we've used, isn't it? I certainly believe in looking at the record and mergers on a case-by-case, but if we find that there is a compelling reason to go forward in those orders, then I'll certainly consider that too.

I don't know if I've gone through everything but I've tried to hit the high points.

CHAIRMAN WOOD: I should add I think we do have another item that, in light of the late hour, we'll take up after lunch on market-based rates. That is again a discussion-only item today but in thinking through that item, and my stick, I guess there are a couple of different ways to get there, and I just wanted to put out there that I think it's a new world. There are new world benefits, and along with those benefits come some burdens. And if you want to stay in the old world, we can maintain that world

but the new world benefits don't accrue. And whatever those are -- and Bill I know you've thought about these longer than I have, and Linda, you've lived with them as well -- I just think FERC did a real good job on that in the gas side and we need to make it real clear that people can pick which side they're on.

COMMISSIONER BREATHITT: Before we conclude, I would like to make one more point. We still haven't seen a bona fide transco come to the forefront. I think that whatever we do going forward, I think it is incumbent upon us, if we agree that that is a legitimate business model, to make sure we don't disincent the formation of independent transmission companies to being able to form transcos as an RTO.

CHAIRMAN WOOD: I would hope that this would actually incent that to happen sooner rather than later. I know there's been a healthy debate on that. Unfortunately, I did not put that on today's agenda on transco versus iso caption, is there really a difference. But we have a long enough day ahead so I want to thank you all for your thoughts on that. Our next action on that, we will kind of have RTO out on probably every agenda for a while, but I want to keep this fresh and current so that we don't let ten weeks lapse while the outside world wonders what we think.

Nora?

COMMISSIONER BROWNELL: Can I just ask a couple of clarifying questions in terms of where are we?

We have agreed that we are going to have RTO week. We've agreed to go forward with the audit. And we've agreed that no matter how we handle it, that waiving that December date is not a free pass to be fooling around with this issue for the next 25 years, okay? I'm too old to wait.

COMMISSIONER MASSEY: On the 206 investigation on market design, would you propose some sort of 206 proposed document be voted on by the Commission before RTO week or after we gather the data analysis and information from RTO week?

CHAIRMAN WOOD: Do you have a preference?

COMMISSIONER MASSEY: It's probably a good idea if we could do the document, now that we've put everybody on notice, if we could get the input that week, and then formulate the document shortly thereafter.

CHAIRMAN WOOD: Let's do that. Great. We will not break for our closed session as was posted under the Sunshine Act, and also have a lunch break. So is that fine with you? We'll come back and pick up with E4, we'll also pick up M1 later in the day as well. I will let parties know that we won't come back to begin our open discussions any earlier than 2:00 o'clock. So please go have a nice

lunch in the neighborhood.

(Whereupon, at 12:55 p.m., the hearing was recessed for lunch, to reconvene in open session at 3:15 p.m. on the same day.)

## AFTERNOON SESSION

(3:15 p.m.)

CHAIRMAN WOOD: We're back on the record. Item M-1, which we've held over from this morning, we've talked about some language.

Linda, do you want to just read that into the record?

COMMISSIONER BREATHITT: Yes, I do. Let me find it real quick. I can't find that piece of paper, but it said, the new language has three new sentences, two of which were proposed by Chairman Wood, and one by me, and it says, in the final rule, the Commission may determine that this separation is not required. Parties are strongly urged to provide factual evidence on the costs and benefits of this proposal in their comments. And I think I'm resurrecting the right sentence. State commissions are also strongly urged to provide their views as well.

And that gets me on board and I will vote for the proposal.

CHAIRMAN WOOD: Which will be Option B.

COMMISSIONER BREATHITT: This had to do with requiring the separation of those employees that deal with bundled sales in the codes, so you worked your compromise well.

CHAIRMAN WOOD: Thank you for being open-minded.

I owe you one. I don't know when you're going to cash it in, but I'll wait.

COMMISSIONER BREATHITT: I'll remember that.

CHAIRMAN WOOD: David?

SECRETARY BOERGERS: Yes, if we could have a vote starting with Commissioner Massey?

COMMISSIONER MASSEY: Aye.

COMMISSIONER BREATHITT: Aye.

COMMISSIONER BROWNELL: Aye.

CHAIRMAN WOOD: Aye. Thank you. And now we're going to resume with Item E-4, I believe. And let me just identify the team that was part of the market-based rate study. It was Rahim Amerikal, Edward Gallick, David Unger, Ronald Lafferty, Debra Leahy, David Mead, Edward Morell, Debra Ott, Jerry Pederson, Jamie Simler, Joyce Kim, and I believe Jamie Simler has a presentation.

MS. SIMLER: Good afternoon, Mr. Chairman and Commissioners, and welcome to round two. Discussion Item E-4 is a staff paper setting forth options for the near term and the longer term for addressing generation market power for the purpose of selling power at market-based rates.

Wholesale electric markets have changed and expanded since the Commission's initial grant of market-based rates. Today, all utilities provide open access transmission service and many utilities have restructured

business operations. And in some regions, there are bid-based power markets. Concerns with assessing market power are widespread.

The study team sitting before you today revisited the assessment of generation market power for market-based rates and recommends a three-part approach for addressing generation market power.

First, the team recommends that the Commission adopt an interim method for assessing generation market power. This interim method could be used immediately to process the pending initial applications and tri-annual reviews.

Second, and coupled with this interim method for assessing market power, the Commission could issue a quick turnaround Section 206 initiative to explicitly prohibit anticompetitive behaviors that were implicit in the granting of market-based rate authority, and importantly provide refund protection against such behaviors.

Third, the study team recommends that the Commission institute a generic proceeding to formulate a longer-term approach to assessing market power. With regard to an interim method for assessing market power, the study team presented five options to the Commission. The options represent variations on the assessment of concentration or market share and supply and demand, and they are not

mutually exclusive.

The study team recommends that Option Two, the Supply Market Assessment Test, be adopted and implemented immediately for all new and pending applications. This option is a combination of several of the other interim options and should provide a better interim assessment of potential market power while long-term solutions are under study.

This supply margin assessment test builds off the existing hub and spoke test. It systematically factors in available transmission and measures an applicant's relative size against the actual reserve margin in the relevant market. This test would be applied only in non-ISO or non-RTO markets. All sellers into markets operated by an ISO or an RTO would be granted market-based rate authority subject to applicable market monitoring and mitigation.

In addition to the proposed change in the market power analysis, the study team recommends that the Commission institute a 206 proceeding to establish a refund effective date 60 days following publication of an order in the Federal Register, and seek comments on a proposal to amend all outstanding market-based rate tariffs and authorizations to prohibit anticompetitive behavior or the exercise of market power.

As for a long-term solution, we recommend a

series of outreach or market assessment meetings on the issue of market power; how to detect it, what the Commission should do when it is detected, and mitigation options. The data gathered from these meetings, coupled with the team's analysis on how to assess market power, will form the basis of a NOPR designed to introduce the Commission's preferred test for market power.

The study team is available to answer any questions, and I thank you.

CHAIRMAN WOOD: Bill?

COMMISSIONER MASSEY: Thank you for an excellent presentation, and we have before us a paper that outlines the various options that are open to us. It's a paper that I think is very well done and I thank all of you. It's no secret that from comments I've made time and time again from this table that I think our hub-and-spoke methodology is sorely out of date and needs to be modified.

What you are doing is proposing a pathway for the Commission not only to ensure that existing applications are treated in a more rigorous manner but that we end up with a long-term fix that is also consistent with the public interest.

So as I understand it, you have essentially got two parts here. Number one, agree on an interim solution that you would recommend that also includes two of six plus

proposed tariff changes, and I'm all for that approach.

It's an excellent approach. I'll sign on the dotted line.

Number two, meanwhile, we would let the world know that we are interested in a long-term solution, a long-term way to ensure that market power is effectively mitigated in the marketplace. Am I correct? Have I summarized that correctly?

MS. SIMLER: Yes.

COMMISSIONER MASSEY: So the question is what is the standard that we apply in the interim, and it seems to me that's question number one, and you proposed five different tests that could be used either individually or mix and match them in some way.

And the second issue is if we do choose to open a 206 and propose interim tariff changes that all sellers would have to comply with, what are those tariff changes, correct? All right.

Back on how we measure market power. As I understand the test you are proposing, it builds on the hub-and-spoke but also factors in transmission constraints based upon TTC, total transmission capacity, right? All right.

Then the question is, how do you measure the concentration that you would be concerned about. And as I understand it, simply stated is what you would propose is if the capacity of the seller involved is not necessary to meet

peak day demand, then that seller would not have market power.

Have I stated that accurately?

MS. SIMLER: Yes. I think Jerry Pederson can answer more fully.

COMMISSIONER MASSEY: Okay. Would you like to comment more on that, and why do you think that's the best test to use?

MR. PEDERSON: Well, I think what that test does is it brings in a couple of factors that we didn't see with the hub-and-spoke. The first one, as you pointed out, was the transmission capacity. So we're limited to the suppliers that can get to the market in a more realistic than perhaps our old study did.

The other thing we're looking at is we're bringing in the factor of demand. When you compare the total supply that can get to the market with peak demand, if the seller, as you said, is needed to supply some of that power, in other words, it has more capacity than the supply margin, that seller becomes a pivotal supplier in the market and he almost becomes a must-run unit. And if it's a must-run unit is a pivotal player, then that seller has market power. And if it has market power, what we would propose is then we would deny market-based rates for that entity.

COMMISSIONER MASSEY: Now you also list, as an

option, the delivered price test, I suppose which would be the methodology taken from the Appendix A, generally speaking from the Appendix A analysis to the merger policy statement of 1996, is that correct?

MR. PEDERSON: Yes, that's one of the options.

COMMISSIONER MASSEY: That's just a different way to define the scope of the market, correct?

MR. GALLICK: Commissioner, it's a little more than that. The hub-and-spoke and the options that are related, one and two, you can think of those, as Jerry just said, we're trying to make adjustments to make sure you get ideally the economic capacity that's available. We're trying to measure how much alternatives do we realistically have that we can rely on.

So one adjustment is in Option Two. What we're doing is adjusting for transmission because all the capacity that's available at the generator location can't always get to market. So that's one adjustment.

But the delivered price test goes an entire step further. And what it does is it asks the question, okay, we're only going to run the capacity you can actually get to market, but we're going to make another cut and eliminate more suppliers if those suppliers cannot get to market at a price that's competitive. It has to be a good alternative to customers. So I'd say that's the major distinction in all

these options, that we're trying to get, we're trying to balance the conceptual getting the right measure of alternatives and not be over burdensome in the process of doing the analysis.

COMMISSIONER MASSEY: And can you tell me why this group proposes the supply margin assessment rather than the delivered price test?

MR. PEDERSON: Well, I think one of the things about what we were trying to come up with on an interim solution is something that we could put forward on a quick basis. Staff's generally familiar with this type of approach. We have the ability to get in and get these numbers, and it's a test which we can do on a -- we're thinking in terms of a 60-day clock as well. And so we needed a test that we could process rather quickly while we're looking towards the long term.

COMMISSIONER MASSEY: And could someone explain to me, Option Four, you call it the "residual supply index" which sounds somewhat similar to the supply margin assessment but yet it's different. Can you -- the way we explained the supply margin assessment is first you take the hub-and-spoke methodology, you factor in transmission constraints, then you look to see if the seller's capacity is necessary to meet peak requirements, and if any of it is, then that seller fails the test.

Now tell me how the residual supply index test would differ from that test.

MR. GALLICK: Okay. There is some commonality between the two approaches. The short answer I think is, with Option Two, Option Two gives you a measure of aggregate demand supply conditions, and it's built on a foundation a particular way of defining the market and measuring the size of the firm. So it gives you a competitive analysis with a specific measure, and this measure's a reserve margin.

That reserve margin, in and of itself, as you said, actually mathematically it's almost identical to the residual supply index. And the way I would explain it is as follows. The supply margin assessment really asks the question, is the excess capacity greater than the size of the applicant of the firm in question. If you have so much excess capacity that you don't really need the supply of the applicant or the firm in question, then you don't really need that firm to meet market demand.

Move over now to Option Four. Option Four says is there enough supply by others to meet market demand. So in effect what we are saying is, if there's really so much excess supply that we don't need the supply of the firm in question, the supply of others is enough to meet market demand. So conceptually that measure, what we are really

trying to do is look at market demand and supply conditions, conditions that often are not looked at if you bore into delivered price test that looks at specific market share and maybe concentration measure, so they are complementary. Four is a complement to the other options, it's an adder.

So what we're saying is if you were looking at delivered price, or even if you're looking -- well delivered price is the easiest one. With delivered price, we specifically calculate market share in HHI. And you say, oh, that looks pretty good. You might have a low HHI, everything looks good. You say, but wait a minute, we're in the electricity industry. If we're in other industries, that might be all you need. But in this industry, we're worried. There's no, there's very little price responsiveness by customers to price increases. So what might happen is a seller may be less able and less willing to switch over and offer alternatives to customers of the applicant.

So this is a long way of saying what Four is doing is it is looking at aggregate concerns. If it turns out that there is just enough supply to meet demand, including the applicant, we don't have the confidence that you're going to get enough alternatives for the customers of the applicant. So that one measure in Four does not depend on a particular analytical framework. It's just a

computation, an adder, a complementary screen, if you will.

COMMISSIONER MASSEY: It's just a different measurement of market power once you've got the market defined, right?

MR. GALLICK: Yes and no. If you look at market power, we normally look at it from the firm's point of view, and the problem we would run into is that from the firm's point of view, we may think the firm has no market power, but then what we have to do is look at the overall market conditions to see, is this firm supply actually needed, because in electricity, with consumers not really responding very well to increases in price, alternative suppliers, instead of moving to the customers, try to rob the customers of the applicant, may decide just to raise its own prices. So you don't normally get the supply response that you get in non-electric markets.

MR. GELINAS: Bill, let me try to recap this just a little bit, and give you a little bit additional on how the team got to their options. I think the first two options in here, probably as a practical matter, produce very similar results but they're the closest and build the most on the hub-and-spoke. So from a point of view, Cindy, perhaps legally and otherwise, implementing them quickly without a NOPR, you have a lot less risk with those too.

The first one keeps the 20 percent market share

that we've all been familiar with but reduces the total capacity to the smaller of what the competing suppliers have to sell or the size of the interfaces' total transmission capacity. So it's a more stringent application of the 20 percent. In a sense, it deals with transmission up front in the application, rather than the way we used to with the hub-and-spoke, which would have been to set it for hearing, and we rarely did that.

The second option builds again on the hub-and-spoke but drops the 20 percent static market share and instead looks at the size of the supplier relative to the margin in the market, and it's really a factor of one. If the supplier is larger than the margin, then he's, as you said, Bill, he's required to meet load, he knows it, and he has market power.

The one we've been talking about on the residual supply, in a sense it changes the number from a factor of one, which is unity, is enlarged to 1.2. It moves the margin number a little bit higher up the scale. Each one of these gets a little bit further away from the hub-and-spoke and it has a little bit more bells and whistles to it, and a few more risks.

The choice the team made was to try to find one that builds as much on where we are so we could do it quickly but gives you folks the biggest bang for the buck

that we thought you could have.

COMMISSIONER MASSEY: And obviously the flow in all of them, and we all recognize this, is they are all snapshots.

MR. GELINAS: That's correct.

COMMISSIONER MASSEY: And if market conditions change like out west all of a sudden you had no hydro, that was a surprise, then it's very hard to factor that into a snapshot it seems to me.

MS. SIMLER: And that's why we were looking for something longer term. This was just an interim solution while we could take stock of where we are, talk to market participants, and get a plan for the longer term. Something that would be more dynamic and not take a static approach.

COMMISSIONER MASSEY: Now let me ask a few questions about, because the second part of the interim solution is the new tariff, proposed tariff conditions. Now I couldn't tell from the proposal whether the refund, the new refund condition that would be triggered by violations of the tariff, would say, would be triggered by a finding of an unjust and unreasonable price? There's some language it sounds like that's what you had in mind. Other language sounds like the refund condition is only triggered by bad behavior.

In other words, you could have a market that was

simply dysfunctional, there's no bad behavior, it's just a market that is not working well, and is producing unjust and unreasonable prices, would any sort of refund condition be triggered in that market where there was no bad behavior?

MS. LEAHY: If I could address that. I think that the intent is to, clearly in the first instance, address instances of bad behavior but it would also anticipate market dysfunctions so that the refund condition could attach if a showing was made in a particular case that rates were unjust and unreasonable.

COMMISSIONER MASSEY: Sort of like we found in the California orders. In the December 15th Order, we pointed no fingers at any particular sellers but we found a dysfunctional market that was leading to unjust and unreasonable prices. Is that what you're talking about?

MS. LEAHY: Yes. The way this is set up, we are eliciting comments. We would elicit comments within 15 days and then provide an opportunity for reply comments after that.

COMMISSIONER MASSEY: But what you would propose is tariff conditions that were triggered by either bad behavior or a dysfunctional market?

MS. LEAHY: That's right. That's right.

COMMISSIONER MASSEY: Thank you.

COMMISSIONER BREATHITT: The SMA, the supply

margin assessment, is that a word found in any legal textbooks, or is it one that we're using for this new methodology? Is it a new word?

MR. MEAD: Yeah, it's a new word.

COMMISSIONER BREATHITT: Okay.

CHAIRMAN WOOD: Did the team copyright it or is that still available?

MR. MEAD: We made it up.

COMMISSIONER BREATHITT: So the SMA. If that's the one that we decide to go to, or whatever one we decide to go to, did I hear in the presentation that this would be applied differently in RTO areas and non-RTO areas?

MR. MEAD: Basically, yes. Really the mechanics of the SMA, as it is described in the paper, really applied to sellers in markets that are outside ISOs and RTOs.

Option Five, which is in a broad sense, part of the Staff's recommendation, would be applied to sellers in areas operated by ISOs and, as you've read, the basic mechanics here are to grant market-based rates to any seller into an ISO or an RTO's bid-based market but to have those suppliers be subject to the market monitoring and mitigation measures that are in place in those markets.

COMMISSIONER BREATHITT: David, do they get an automatic approval?

MR. MEAD: For sales into the ISOs or RTOs bid-

based markets, yes, they get an automatic approval in the sense they get market-based rates, that is, they are exempt from cost-of-service regulation for sales into those markets.

However, you know, there is still the market monitoring and mitigation measures that are in place in those markets to address the market power problems.

COMMISSIONER BREATHITT: So this would be a new change. Heretofore, every applicant requesting market-based rates went through the hub-and-spoke test, correct?

MS. SIMLER: That's right.

COMMISSIONER BREATHITT: So this would be a change.

Then the other question I have is for sellers, if you take the eastern seaboard, for example, if you have a seller that wishes to sell into an area that is already an approved ISO, since we have no fully approved RTOs yet, we've conditionally approved ones, but for the purposes of my question, let's just say they're wishing to sell into an ISO but that same seller has generation that, on the same day, wishes to sell into an area on the eastern seaboard where the load is not in an ISO. Would that seller then need two different kinds of rate treatment or authorities to do so?

So in the second instance, if they are selling

into a load that is not in an already approved ISO or RTO, they would have to meet the hub-and-spoke test plus this addition that we are thinking about adding today to that? Help me understand this distinction.

MS. SIMLER: I believe the focus is on the market where you're selling, so your distinction is correct. If you're selling into the ISO market, you would be allowed to sell at market-based rates. You would be subject to the market monitoring and mitigation there, and the team didn't discuss, but I think you'd still be required to have a tariff on file for the provision of those services.

And if you were selling in the non-ISO market, you would be required to pass, if we decide here, it would be the supply margin assessment test, you would be required to pass that. And if it was decided that we would go forward with the 206, you would be subject to all the provisions of the 206.

COMMISSIONER BREATHITT: So the tariff that you're talking about, Bill, is the tariff that we talked about earlier today, or the existing tariffs that -- it would have to comply with which tariff?

COMMISSIONER MASSEY: As I understand, they are proposing, as an interim solution, a 206 proceeding in which all sellers that have market-based rate authority, their tariffs would be amended to include these new conditions on

an interim basis. Am I correct? They would apply to new applicants that are coming before us now for the three-year reviews and existing tariffs would be 206'd and amended?

MR. GELINAS: They would apply to everyone here now and coming to us for all their sales.

COMMISSIONER MASSEY: So it's like 994 of them?

MR. GELINAS: The whole thing.

MS. SIMLER: And the timing of when you would have to amend your tariff is something we talked about and we don't know that we necessarily would want to require everyone to amend their tariff instantly as a result of the 206, or amend it when you came in for another revision. But you would still be subject to the provisions of the 206.

COMMISSIONER BREATHITT: Well, that was confusing to me because everybody's operating under the OATT tariffs.

MS. SIMLER: I'm sorry. These are the market-based rate tariffs. They have separate tariffs to be able to sell at market-based rates, so that would be the 206.

COMMISSIONER BREATHITT: So when they come in for a new application or a pending application, this new test would get applied, depending on whether you were in -- well, really they would need both because sellers are going to sell all over the eastern seaboard I'm assuming. I don't know if, so that needs to be considered.

Also, I wanted to ask about the 206 itself.

Okay, go ahead, Dave.

MR. MEAD: If I could just step in for a second.

The provisions of the Section 206 would apply to sellers, to all sellers whether they are selling into ISO markets or non-ISO markets, so you know, the prohibition against any competitive behavior, however that's defined, would apply to sellers into the ISO markets, and you know, a similar condition has already been adopted for sales into the California and the west-wide markets.

COMMISSIONER BREATHITT: The second prong of this paper, which talks about the Commission issuing a country-wide 206 investigation, I have to state that with only having three working days to consider this paper, I have not fully considered the ramifications and the broad impacts of this, but the way I read it puts the transmission owners, it puts suppliers on notice all over the country that their rates are subject to refund. That gives me some pause because of regulatory risk, uncertainty, and what that would do to other items that we've been discussing today of great import, which is how to build needed supply and infrastructure and the cost of capital and the need for capital to do that.

So the tension there is protecting consumers but also realizing that if you have an open-ended 206, we have to recognize that there is regulatory risk that is assigned

to that, and that this is very open-ended. Does it have, do my colleagues or do the staff have a closure date?

MS. LEAHY: As presently conceived, there really isn't intended to be a closure date because the idea would be that your tariff would be conditioned upon you not either engaging in behavior that's unlawful, that was anticompetitive or that you should not be operating at market-based rates pursuant to a tariff if there are facts to show that the rates are not just and reasonable. So it's currently a brief on condition that would just be imposed and we certainly would like to provide as much certainty as possible to the industry, but the idea that we are trying to make it clear that when the Commission gives you authority to engage in sales at market-based rates, that authority is subject to certain agreements, that you're not going to be engaging in anticompetitive behavior, that the rates that you do negotiate are going to be just and reasonable.

MS. GRANSEE: I guess, could I just add a couple of things to distinguish here. What the order envisions is an actual tariff provision such that it would become a clear violation --

COMMISSIONER BREATHITT: What order are you talking about here, Cindy?

MS. GRANSEE: The 206. If the seller engages in

anticompetitive behavior. So it's not like an open-ended  
206. That will be part and parcel, and if they are found to  
withhold improperly, or engage in other anticompetitive  
behavior, it is a violation and the Commission would clearly  
have the authority to go back and remedy it.

I personally don't see a regulatory risk for that  
because no one should be engaging in anticompetitive  
behavior period. That's to me just a given. I think the  
area may be of more concern to you is -- and it's not  
totally clear in the order -- is that if we find there are  
market dysfunctions which make the rate become unjust and  
unreasonable, that then the Commission could go back, and  
there's no limit in that situation, the way this is drafted  
now.

Now in the California case, as I recollect, we  
initially conditioned continued market rate authorization on  
utilities agreeing to refunds but I think it was 18 months  
to two years, until we could get the market dysfunctions  
corrected, so we did put a limit there.

We then later further amended those  
authorizations on no anticompetitive behavior in perpetuity  
basically. So there are two pieces of it, I think one of  
which may pose the risk problem you're talking about. But I  
don't think the anticompetitive piece of it does because, as  
I said, no one should be engaging in that kind of behavior

to start with. We're just putting this in as a prophylactic.

COMMISSIONER BREATHITT: Well, any time that, you know, the Commission certainly has the ability to initiate a 206 whenever it wants to. I just think we would be putting on blinders and kidding ourselves if we didn't recognize that if we issue a country-wide 206, that there would be parties that would say there's regulatory risk out there and we just need to know that, whether it's because of poor market design, we should always deal with flaws and high prices, certainly regulators have to do that and we need to do that. But this is a big deal.

And Chairman Wood, I need a little bit more time to consider this than just the three days I've had.

CHAIRMAN WOOD: And I would not ask that this be put up for a vote today. I want us to talk about where we want to go.

COMMISSIONER BREATHITT: But I only had an hour briefing at 5:00 o'clock last night, and I need a few more to understand whether this really is the option that is the best one, although right now I favor Option Two, and I do agree that we need to add some components to the hub-and-spoke. I do agree that we need to come up with something permanent and longer-term. So there's a lot here to consider, and I'm glad we're having this conversation, it is

extremely important, it has a lot of facets to it, and I will be looking at this intensively in the next weeks as we continue to consider it.

MR. GELINAS: Commissioner, let me just raise one point with respect to what you said. One thing that you probably should consider is you could do the first part of this three-part package immediately if the 206 order and getting comfortable with that is something you want to take a little more time on, one thing you ought to consider is at least making the cut on the upgraded analytical tool because we've got 60-day applications, not to mention triennial updates, which don't depend on the behavioral conditions of cleaning up the existing tariffs on file, which is more what the 206 order goes to. And we're holding those back now, and there's a point where we're going to have a floodgate of filings that just need to be processed. So as you're thinking this through, you might want to keep that in mind.

COMMISSIONER MASSEY: Yes, but let me just say that my thinking on this is that the two parts are related. Since even the jazzed up hub-and-spoke is merely a snapshot, it doesn't eliminate all risk of unjust and unreasonable prices or market power, and so the tariff condition, to me, is hard for me to agree to a certain jazzed up hub-and-spoke type analysis without knowing what the tariff condition will be that goes along with it to provide the extra protection.

And I appreciate the comment you made, Linda. The other side of it is, by the time we -- and we move fairly quickly but by the time we got the complaint on California, acted on it, set the refund condition that was applicable 60 days hence, the date was October 2nd, and there had been, you know, soaring prices for June, July, August, and September, that we have now concluded we could not provide a remedy for. So I'm concerned about that.

COMMISSIONER BROWNELL: I just had a couple of questions and I actually thank my colleagues. I think they've asked the most important ones. But the exemption for those who are operating in ISOs or hopefully RTOs is founded on I think an assumption that everybody's market monitoring units are up to speed.

Are we comfortable with that? Is that something that at the same time we need to take a look at so that we are confident that that exemption is warranted?

MR. MEAD: Everything in life can be improved upon of course --

COMMISSIONER BROWNELL: Except the Commission here.

MR. MEAD: Of course, of course. And I think, you know, we need to look further at the way that ISOs, and later on RTOs, monitor for market power and the steps they take to remedy market power when they find it.

Having said that, the existing evidence suggests that the monitors in the ISOs have been very diligent and have not been shy about telling us about problems that they see. So my view is that certainly, as an interim measure, this would be a reasonable way to go. And certainly the alternative of subjecting sellers to cost-of-service rates and bid-based ISOs I think it not a very palatable one. These markets work better if market forces can be allowed to be brought to bear.

COMMISSIONER BROWNELL: I certainly agree with that, that's my mantra. But I think we just need to be sure that the market monitoring units are a) up to speed, and b) that the rules are similar so that we're not creating unequal playing fields from region to region. I just think that goes part and parcel if we go down this route.

Just two more suggestions, and I think both of them are being worked on. I think we need to be very clear when we talk about unacceptable behavior to suggest exactly what those behaviors are. We will never encompass all of the possibilities but I think that the market is going to look for guidance to us by what our tolerance for pain is, so I would encourage that.

I also think we need to be real clear. There's an attempt in here I think to give an example of what we deem to be a competitive market. Let's be sure that we

define that as well, or define it as functional market so that once again some days it's easier to get consensus when we leave gray areas but that only leads to more litigation and misunderstanding, so, you know, even if we take a stab at it and we are wrong, I feel certain someone will tell us we're wrong.

But you've done a great job and this is a very comprehensive report and I appreciate it.

MR. CANNON: Commissioner just one thing on your second point. We are a little vague here in terms of the exact types of behavior which are tabu. I think, at least my own thinking is that as we get into the longer term fixes, we're going to probably learn a lot more about the kinds of behaviors that we care about. And so it's almost purposely vague here so that we can give ourselves the latitude to try to put a little more flesh on those bones as we move forward, and get a better handle on exactly what kinds of behavior ought to be out of bounds.

COMMISSIONER BROWNELL: That's commendable and we're all learning as we go, but to the extent that we have learned some lessons, and I believe we all have, and we can identify some of those behaviors, I think that we would be doing a great service to the market participants by defining those. If I don't have the ten commandments, I can never sin, which I guess would be okay. But I think maybe we

found ourselves in that problem on occasion in the last six months or so, so I don't want to let it go. We can always build on it.

CHAIRMAN WOOD: I'll take that last point first. The three things we're talking about here are new tests for what's in the pipe or what's actually on the desk, and I lean toward the Option Two/Option Five. I think from the back-and-forth I had with the Staff yesterday, that certainly sounds like a sufficient interim fix.

For the 206 -- this came up a lot in our testimony to the Senate I believe in, was it late July? -- when we basically admitted we didn't have the hooks in the current certificates to go back and do anything even though there may have been something as egregious as withholding of production, we wouldn't have had the hook to go get it anyway. So I would definitely want to do a 206 to put the correct conditions in all the certificates but I do share Linda, yours and Nora's articulated concern that we be real clear about what the ten commandments are.

I think I would rather err on the side of doing nine commandments and somebody sinning go through, than do something over broad that we don't have anybody around to sin in the first place. So I would rather do nine that we know are sins, and then see if we can define the tenth if it ever shows up and then do that in a successive 206, than be

over broad at first.

I think one thing I would like to be, I'd like our Commission to be known for is being very clear about the rules, asking people to play by those rules, leaving them alone if they do, but if we in fact find out that we wrote the rules wrong, then we'll fix those rules as fast as possible prospectively so that we're constantly letting people know in advance what the game plan is and expecting them to play by it.

I do worry about an open-ended. I think the way it is drafted is open-ended, it will invite comment, it will elicit that comment. I would not vote on anything that was not crisp as to commandments one through nine, to carry the analogy to the bitter end, but we might could package that order more crisply up front so that our intentions are known to the outside world during the 60 or 90 days that we're getting comment, working on the order, and moving forward on the rest of our agenda.

So I would definitely want to see a crisper version of the 206 order initiating changes to all the existing tariffs be up here before we vote it out.

COMMISSIONER BREATHITT: Tell me again about the 60 to 90 days you just mentioned. That would be?

CHAIRMAN WOOD: Well, I think we have to, under the law, tell people how quick we're going to act on a 206,

just so there's some certainty out there. So that's what I'm saying is if we publish something that's at our next open meeting, a 206 that is cleaned up to get us all, you know, content with where it's going, we get comments in a 15-day cycle, reply comments in a 15-day cycle, that's 30. We have time over here at the Commission to respond to those comments and get the most crisp version of the tariff conditions that we are now inserting into everybody's market-based rate certificate over the next 30 or 60 -- I don't think it was in here at all, but just I assume we've got to move probably pretty aggressively if we want to have those conditions actually be applicable.

And Bill I think made a good case for why there is some sense of urgency on this because it was just during the shoulder months last year that we started to see, due more to market dysfunctions, but perhaps due to some discriminatory, anticompetitive behavior, perhaps that things started to go awry out west. And so I do want us to move forward hopefully at the next meeting to get this out, but I think we do need to give the industry some clarity as to where we're going pretty quick, so I wouldn't want it to hang around here long after the comments came in is where I'm going with that number.

COMMISSIONER BREATHITT: Debra, you were talking a little bit about time frames in your presentation. Is

that what you were referring to?

MS. LEAHY: That's right. In other words, the order would be issued, it would be noticed, we would allow, as currently proposed, we would allow 15 days from the date of issuance of the order for comments to come in. When comments are in, there'd be an additional 15-day period for reply comments. At that point in time, under 206, the Commission will generally indicate when it expects to issue a final order. And so the order that we would issue would give an expected date by which the Commission would issue a final order laying out the tariff conditions.

COMMISSIONER BREATHITT: So the first order that you're talking about, Chairman Wood, that you would like to go at at the next meeting would be an order initiating the 206? I'm seeing heads nod. And then there would be a subsequent that would be the actual new generic tariff or the tariff that -- would there have to be two? One for parties selling into non-RTO/ISO areas, and one for parties selling -- it would be the same one? I'm seeing heads nod.

You can tell I haven't had much time with this. I could be asking these questions in a private staff briefing too, but why not ask them here. I'm just trying to figure out the mechanics and understand this better.

MR. MURRELL: Commissioner, the first order would propose the general conditions that would be applied to all

of the market power tariffs. The comments would be addressing how well the Commission drafted those proposed conditions. And then the second order would address the comments, refine the language, and craft the final language that would then be imposed on the individual tariffs.

CHAIRMAN WOOD: I think what Linda's asking, though, is how do you incorporate, assume we go with Test Number Two and Test Number Five from the SMA, and the option five. How do we graft that into everybody's existing certificate? In other words, do we go back and review people who might have numbers greater than the SMA that we're looking at?

MS. SIMLER: I think what we are proposing to do is as soon as we have approval to go out with Option Number Two for assessing market power, we would begin using it immediately for processing all 60-day filings, and we would start looking at the tri-annual reviews that are pending.

Pardon me?

CHAIRMAN WOOD: You would not impose that new test, then, through a 206-type proceeding. You would do it in the tri-annual reviews.

MS. SIMLER: That's right. That's the current plan.

CHAIRMAN WOOD: Okay.

MS. SIMLER: And in the 60-day items that we need

to be processing now.

CHAIRMAN WOOD: Big stuff and three-year reviews?

MS. SIMLER: Yes.

CHAIRMAN WOOD: So what's in the 206 then are just the broad conditions of thou shalt not, list of nine, and one of those is market dysfunctions, so that thou shalt not also applies to a supply/demand imbalance as we saw in California, or out west, which was Bill's first question, I believe.

COMMISSIONER MASSEY: And then the long-term solution, if it's consistent with what you're proposing here would, since it's our intention for there to be only, for there to be bid-based RTO markets everywhere, would be to apply the same standard long-term, I would suppose. In other words, everyone would be selling into a bid-based RTO market, would they not?

MR. LARCAMP: I don't know that the Commission's reached that conclusion yet, have they? That you would be prohibited from selling in bilateral markets?

COMMISSIONER MASSEY: Oh, no, no, no, I don't mean that.

MR. LARCAMP: That are not RTO bid-based markets.

CHAIRMAN WOOD: That would be a minimum characteristic of an RTO market that allows you to basically avoid having the SMA test --

MR. LARCAMP: That would be a safe harbor.

CHAIRMAN WOOD: It's got to be an ISO or an RTO that has bid-based market at a minimum.

MS. SIMLER: And I think that's something that you know we would be looking to do you know through the outreach, the market assessment meetings, to get a feel for longer-term what type of tools we would use to measure different types of market power and what type of mitigation or other kind of tariff provisions we would want to include.

COMMISSIONER MASSEY: And if our efforts during RTO week are successful and lead to market design elements that are more likely to structure markets in a way that lead to just and reasonable prices and these markets would also have market power mitigation measures built into them, I'm assuming, must-offer provisions or something like that. Ex-anti-mitigation provisions.

And if, in fact, you know, my fondest dream is accomplished which is there's an RTO everywhere and a bid-based market everywhere, at least for imbalance requirements, then as those RTOs developed, the use of the hub-and-spoke would melt away. Is that right? The use of the jazzed up hub-and-spoke?

MS. SIMLER: Right. The longer-term does not have to have the jazzed up hub-and-spoke or anything else. I mean, it could be something that our assessment does

simulation modeling, something that would be more dynamic than static. It could be a list of indicators or tests to kind of capture the pulse of the market, where the market conditions are. That's where we are looking to explore for the longer term.

And as you've said, if we get sufficient infrastructure in the market design right and the market rules right, then a lot of what we're talking about here sort of becomes the fail safe.

COMMISSIONER MASSEY: Thank you.

MR. CANNON: Can I ask a question because I'm a little confused. In terms of the nine thou shalt nots that are sort of part of option 206, don't we still need those with regard to any of the sales that don't go through this real time balancing market?

CHAIRMAN WOOD: You need them either way. I think you need them under the RTO markets or under the non-RTO markets.

MR. CANNON: So those things don't disappear just because you happen to be participating in an RTO, correct? Okay, I'm clear.

CHAIRMAN WOOD: That's my understanding. I would think so. I think what is maybe a little confusing here is that these are all in the same proceeding because they are related but they really are two independent things that

we're doing. One is taking, we can leave hub-and-spoke alone and go back, because we did in California and the west, put these conditions in the east as well. So we could do this totally separate from this other discussion about revising hub-and-spoke. We're just having both discussions today because they are related.

MR. GELINAS: Could I raise one more quick thing. Linda, you asked about the name of Option Two, and I said we made it up. And on behalf of the team, I've been asked to ask our inspirational leader, Commissioner Massey, for on whose behalf we tried not to use the words hub-and-spoke, to please not call this the jazzed up hub-and-spoke.

(Laughter.)

MR. GELINAS: That's all I ask, Bill.

COMMISSIONER MASSEY: I would prefer to call it the jazzed up horse and buggy approach.

(Laughter.)

CHAIRMAN WOOD: I call it all let's get to an RTO fast approach if I'm reading between the lines.

COMMISSIONER BREATHITT: Chairman Wood, can I harp on one thing one more time?

CHAIRMAN WOOD: You may harp --

COMMISSIONER BREATHITT: And that's I heard Jamie, you or Don talk about the fail safe down the road, and I heard you, Chairman Wood, talk about crisping up what

we have before us as a draft. I guess I don't know the answer to my question yet of is this open-ended forever. Would there be a point in time in the near future where there would be no need and then would we have a regulatory action to end the two -- we don't have to answer this question now, but they're lingering questions, and I'll be asking those in the next couple weeks, so --.

MS. GRANSEE: If I could just very quickly, one option you could consider is keeping the nine thou shalt nots in for everybody forever because if thou shalt not, thou shalt not. In the tariff, you could consider the option on the market dysfunctions being subject to liability for refunds because of market dysfunctions that may come down the road. You could consider an end point on those because presumably if we get our market rules right, we do our RTO rulemaking, that should hopefully cure all the potential -- not all, but go a long way toward ensuring that you're not going to see market dysfunctions. So you could put an end point or at least reevaluate it once we get the rules in place.

COMMISSIONER BREATHITT: Do we have an end date in our California orders in September of '02?

MS. GRANSEE: We did on the open-ended refund condition, but I don't think we have any end date on the anticompetitive behavior condition.

COMMISSIONER BREATHITT: Okay.

MR. GELINAS: And one other, just to add onto that because I think it's a good suggestion, is the end date could be tied to what Commissioner Brownell asked of when is the market monitoring really up and functioning, and so there could sort of be a time certain there that once they get the Commission's good housekeeping seal of approval with regard to their market monitoring function, maybe that would be the end date with regard to the open-ended piece, not with regard to the nine commandments.

CHAIRMAN WOOD: Daniel?

MR. LARCAMP: Well, I just, maybe we're going to vote, I don't know. I'd like to make sure that, I mean, we've got cases that are on deck that need to be moved. Can we proceed to move those under the Option Two new approach that will come up in an order for voting by the Commission on the first one and we'll follow that on the second ones.

We are crisping up the 206, and we're proceeding on the longer-term NOPR but that's part of the business plan discussion about where we cite that in other things. Is that my understanding of what we're doing here?

COMMISSIONER MASSEY: Yes, I would be happy for us to use any higher standard than we now use in the interim, and so I would go along with that.

MR. LARCAMP: That's a significant margin

assessment, that's a really big one, Bill.

COMMISSIONER MASSEY: But I just want everybody to know that my ultimate happiness with the snapshot standard will depend I think in part on whether the new tariff conditions are satisfactory. That will give me more comfort.

CHAIRMAN WOOD: Let me just, I've been polling informally, but I believe, let me just say, I'm comfortable with using Option Two which is the supply margin assessment for processing in-house applications and I believe Linda and Bill and Nora --

MR. LANCAMP: And that includes the three-year updates, right?

CHAIRMAN WOOD: And the tri-annuals.

COMMISSIONER MASSEY: I'm comfortable with that.

COMMISSIONER BREATHITT: Yes.

COMMISSIONER BROWNELL: Yes.

CHAIRMAN WOOD: And then between now and next week, we could put up on for the following Friday for discussion through the pre-agenda process, the language on the 206 Order at least either with the non-thou shalt nots, or asking for the parties to help them draft them more crisply so that we can put that up on the October 11th meeting. Is that? Does that work for you, Linda?

COMMISSIONER BREATHITT: It works for me.

CHAIRMAN WOOD: And then we've also, in the business plan, as one of the tasks, we'll put the timeline on the, consult with the interested parties, format, publish a NOPR final rule for a broad inquiry as to how to do this longer term, not just what test do we do for what comes in the door but, and this may well fold into kind of where we go with market monitoring more generally, I would expect, but I would like it to be a stand alone because of, I mean, I think we need some direct focus on that.

Wonderful, thank you all for a thorough discussion and the nice preparation and great questions.

We have a few more and they will go swiftly.

SECRETARY BOERGERS: I believe we're up to E-13 and -14 which, Mr. Chairman, you wanted to discuss together.

CHAIRMAN WOOD: These were mergers and in light of our last discussion, I have nothing new to add, so I would recommend that for E-13, 14 and 15, we go with the most recent drafts as proposed. So I have nothing to add on those.

SECRETARY BOERGERS: Shall we take a vote then on both items.

CHAIRMAN WOOD: All three, and 15 as well.

SECRETARY BOERGERS: And 15 also.

Commissioner Massey?

COMMISSIONER MASSEY: Thirteen and 14 are the two

mergers and 15 is Suffolk?

SECRETARY BOERGERS: Correct.

COMMISSIONER MASSEY: Aye.

COMMISSIONER BREATHITT: Aye.

COMMISSIONER BROWNELL: Aye.

SECRETARY BOERGERS: That takes us to E-38, Mr. Chairman.

CHAIRMAN WOOD: E-38 I called separately.

SECRETARY BOERGERS: And we have a presentation, by Annette Marzin.

CHAIRMAN WOOD: That would be helpful.

MS. MARZIN: E-38 is a draft order forming the Western Electricity Coordinating Council as a reliability council for the west. The draft order grants a request by Western Systems Coordinating Council, Western Regional Transmission Association, and Southwest Regional Transmission Association to transfer their functions to the WECC. The order finds that the WECC by-laws, as modified by the order, are reasonable. The order directs the WECC by-laws and any changes to them to be filed with the Commission. Lastly, the order states that we will consider whether changes to the by-laws are necessary to ensure that the operations of the WSEC do not conflict with the authorized activities of an RTO.

CHAIRMAN WOOD: Thank you for that. I wanted to

just take this chance to do an attaboy for the parties out there on pulling together for the entire western interconnection, a body that I know from having been a western interconnect regulator. I'm the only one that gets to have been in all three in my last job. Knows that WSEC had a lot of respect from really broad diversity of the parties, and am pleased that that organization's combining with the RTGs that have existed out there to accomplish some pretty big goals. I look forward, and I'm going to hold them to a high expectation that they will deliver on good planning and great reliability on the whole interconnect out there, so I was pleased that this was proposed, and pleased at how fast we were able to move forward on it, and just wanted to publicly recognize what I think is a very good development out in a part of the country that could use a few good developments.

So I would support the order strongly.

SECRETARY BOERGERS: Commissioner Massey?

COMMISSIONER MASSEY: Aye.

COMMISSIONER BREATHITT: Aye.

COMMISSIONER BROWNELL: Aye.

CHAIRMAN WOOD: Aye.

And now that we are done with the electric agenda, I want to use the opportunity to thank Jan McPherson, a long-time friend. We worked together as

advisors for Jerry Langdon who has helped me with a lot of interesting and hard cases over the last four months, and importantly helped my new team break in, and know where all the bodies are buried.

So, Jan, thanks for all your help and friendship, and Alice gives you a rousing send off.

Okay, Gas.

SECRETARY BOERGERS: The first gas item was G-30, Mr. Chairman.

CHAIRMAN WOOD: I've resolved my questions on G-30 and would recommend that we support it.

SECRETARY BOERGERS: Commissioner Massey, would you like to lead the vote on G-30?

COMMISSIONER MASSEY: I would, aye.

COMMISSIONER BREATHITT: Aye.

COMMISSIONER BROWNELL: Aye.

CHAIRMAN WOOD: Aye.

COMMISSIONER BREATHITT: Thank you for walking up to the table.

COMMISSIONER MASSEY: Can we let Alice do something?

COMMISSIONER BROWNELL: I'm thinking the Commissioner wants to take you all to lunch.

(Laughter.)

SECRETARY BOERGERS: One other item on the gas

agenda was G-33. I believe there was a presentation from Mr. Mareholtz.

CHAIRMAN WOOD: We will pass the item till the next open meeting. That leaves us with?

SECRETARY BOERGERS: The last item is C-6, which, Mr. Chairman, you wanted to discuss.

CHAIRMAN WOOD: This is the El Paso Certificate case that in my first open meeting I got I guess the deserved reputation as a pain in the posterior on some of these gas certificate issues. As a result, this is the one where we asked for El Paso to do a little follow-on report to let us know what their plans were for the pipeline capacity.

I think some of their east-of-California shippers were concerned about adding a large, full requirements customer or taking a full requirements customer and greatly increasing that customer's capacity because it's affiliate added a new power plant that took a lot more gas out of the existing system. I saw the report here from El Paso dated July 9th, filed in Docket RP00-336, and have to admit that I remain concerned about how things are going to work there. I have to utter, on the altar of regulation here, that I am just not a fan and supporter of ten-year rate freezes or any extended rate freezes.

The world changes a lot when people agree to

stuff, and I understand there's a tremendous financial disincentive here because of that for needed expansions to occur, unless they are expansions that are done through incremental pricing or maybe things like that aren't so bad.

But the interplay here of having full requirements customers that seem to have an unbounded upper end, which I would love the opportunity to opine on if we ever get a contested pleading, to define exactly just how full full requirements can be. That interplay with the ten-year rate freeze with a growing part of the country, with the need to have increased generation makes this a very complicated pipeline scenario.

It's hard for me, as a lawyer, to find an excuse to grant rehearing here because this is not the appropriate docket to do that. I will concede, after four months of being brow beat into submission, it doesn't happen often but sometimes you've got to fold up. But I remain concerned about the interplay on this pipeline that I think, if we don't watch it and we don't engage in some long-term planning, can lead to a continuing bedsore scenario for the customers out there in the southwest. So I will reluctantly go along with the order denying rehearing but look forward very aggressively to a forum in which we can address these capacity concerns. I'm told that that is in the 637 proceeding. So I will wait with bated breath, recommend

approval.

COMMISSIONER MASSEY: Mr. Chairman, if you have reasonable recommendations for what to do that's different, I'd be willing to consider them.

CHAIRMAN WOOD: This case was one, Bill, that had -- where this was a jurisdictional deal where they went in, they filed to increase the capacity to serve, the affiliate power generator company of Arizona Public Service. Then -- I'm not going to link them, but after there was opposition to the proposal, El Paso came back and said actually part of this isn't jurisdictional anyway, and because the remainder of that is jurisdictional, it's below our threshold amount. It falls under is it blanket, blanket construction certificate and so it really doesn't in fact come before the Commission at all. Painful though that is, that is legally correct.

And on that very limited basis, I am willing to just go forward here, but the underlying problem is absolutely not resolved by this order. I am very confident that it will be resolved in our 637 proceeding, if not before. So thank you for that. I'll owe you one too.

COMMISSIONER MASSEY: Well, I didn't do anything.

CHAIRMAN WOOD: You indicated you would have. The virtual chip is almost as good as the real one.

(Laughter.)

COMMISSIONER MASSEY: I'll do that more often.

(Laughter.)

CHAIRMAN WOOD: Collegial Commission moves on.

All right, but thanks for asking.

COMMISSIONER BROWNELL: I don't have anything to offer. Can I get a couple of chips anyway?

(Laughter.)

SECRETARY BOERGERS: Did you vote?

COMMISSIONER BROWNELL: Aye.

COMMISSIONER BREATHITT: Aye.

COMMISSIONER MASSEY: Aye.

CHAIRMAN WOOD: Aye.

SECRETARY BOERGERS: Before we conclude, can I just make sure that the record is clear on the M-1 item that was adopted as revised with the changed language that was Option B that you all were voting on, Option B with the revised language?

CHAIRMAN WOOD: That's correct.

SECRETARY BOERGERS: In order to allow you to adjourn the meeting properly.

CHAIRMAN WOOD: All right, meeting adjourned.

(Whereupon, at 4:30 p.m., the Open Session of the Commission meeting was adjourned.)