

1 APPEARANCES CONTINUED:

2 HARVEY REITER, Partner, Stinson, Morrison, Hecker

3 LLP

4 RON WALTER, Executive Vice President -

5 Development, Calpine Corporation

6 ED COMER, Vice President and General Counsel,

7 Edison Electric Institute

8 TOM WELCH, Chairman, Maine Public Utilities

9 Commission

10 ELIZABETH BENSON, Energy Associates, CLECO

11 Independent Monitor

12 ERSHEL REDD, President, Western Region, NRG

13 Ted Banasiewicz, Principal, USA Power LLC

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P R O C E E D I N G S

(9:05 a.m.)

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3 MR. PEDERSON: Good morning. My name is Jerry
4 Pederson. For those of you that do not know me, I work in
5 OMTR as an Manager of the group that processes market-based
6 rate filings.

7 The topic of this morning's conference is issues
8 associated with solicitation processes, including
9 solicitations whereby public utilities sell to their
10 affiliates.

11 In Boston Edison-Edgar, the Commission held that
12 in analyzing market-based rate transactions between an
13 affiliated buyer and seller, the Commission must ensure that
14 the buyer has chosen the lowest-cost supplier from among the
15 options presented, taking into account, both price and non-
16 price factors.

17 The purpose of this conference is to address
18 proposals for the best practice competitive solicitation
19 methods or principles that could be used to ensure that
20 transactions filed with the Commission for approval, are the
21 result of an open and fair process.

22 This conference is being transcribed, and
23 transcripts will be placed in the public record, ten days
24 after the Commission receives the transcripts.

25 We have two panels this morning, so we'll take a

1 short break between the panels. We're also a little tight
2 on time, so panelists will be giving five- to six-minute
3 presentations.

4 We'll pause for clarifying questions, but before
5 opening the floor for a fuller discussion, we will have all
6 the panelists make their presentations, so we'll go through
7 the whole panel and then we'll have open discussion.

8 With that, I'd like to introduce our first
9 panelist, Mr. John Hilke. John is the Electricity Project
10 Coordinator from the Federal Trade Commission, Bureau of
11 Economics, Division of Economic Policy Analysis. Mr. Hilke?

12 MR. HILKE: Good morning and thank you for the
13 invitation. Before I begin, I would like to state the usual
14 disclaimer, that these are my personal views and they do not
15 purport to be the views of the Federal Trade Commission or
16 any individual Commissioner.

17 Another preliminary point is that the context of
18 my comments is the assumption that we're already in a market
19 situation in which affiliate relationships are a potential
20 way that transactions take place, because the full
21 divestiture has not already occurred.

22 In my few minutes this morning, I would like to
23 make two points about potential market distortions
24 associated with utility solicitation processes that result
25 in transactions with unregulated affiliates.

1 First, affiliate transactions, like the make-by
2 decisions of other firms, often enhance efficiency and
3 benefit consumers when they are based on objective analysis
4 and criteria.

5 Conversely, these transactions may reduce
6 efficiency and harm consumers, if they are based on
7 discriminatory analysis and criteria, because the
8 transactions may then allow the utility to exercise market
9 power by evading rate regulation or to allow the utility to
10 expand or prop up an unregulated affiliate by evading rules
11 against cost subsidization.

12 I'd also like to note that the issues involved in
13 assuring objective make-buy decisions are not really unique
14 to FERC or to the state utility regulators. I'll just
15 mention a couple of other examples where the FTC has been
16 active:

17 One is in privatization initiatives of municipal,
18 state, and federal agencies, and the other is the workshare
19 discounts offered by the U.S. Postal Service. Both of these
20 contexts are ones in which the same types of issues arise.

21 My second general point is that evasion of rate
22 regulation or cross-subsidization and solicitation processes
23 potentially create serious long-term inefficiencies in
24 wholesale and retail el electricity markets, above and
25 beyond the immediate price effects.

1 Given the short-term and long-term potential
2 harmful effects of discrimination, it seems to me that this
3 is a worthwhile topic for FERC to be investigating more
4 thoroughly as it seeks to assure that wholesale rates are
5 just and reasonable.

6 Having said that transactions between a regulated
7 utility and its unregulated affiliates need not pose a
8 threat to competition and may, in fact, enhance competition
9 and benefit consumers, I'd like to address the more specific
10 situations in which that might not be the case, in which
11 there is potential harm to consumers and to competition
12 through discrimination, and also mention some potential
13 approaches for detecting and discouraging such
14 discrimination in utility solicitation processes.

15 Let me start by talking briefly about evasion of
16 rate regulation: In a market with cost-based regulation of
17 prices, in which the regulatory utility has market power,
18 and some of which is not exercised, that is that the rate
19 regulation is binding, some mechanism is appropriate to
20 assure that transactions between an unregulated affiliated
21 generator and the parent utility, do not take place at
22 inflated prices.

23 Rate-regulated parent utilities with market power
24 have incentives to make such transfers and that the
25 mechanism here basically be that the inflated price is

1 passed along through the regulated rate.

2 A supply contract with an inflated price would be
3 a form of regulatory evasion because it would result in the
4 exercise of more of the potential market power of that
5 utility, with captive customers paying higher regulated
6 rates to cover the regulated utility's inflated costs.

7 The evasion of cost-based regulation could also
8 involve selling to an unregulated affiliate at below market
9 prices. That would also increase the prices in the market
10 and lead to higher profit margins for the unregulated
11 affiliate.

12 Hence, evasion of rate regulation may involve
13 both types of transactions, that is, both sales and
14 purchases. The same framework may also apply where a
15 wholesale customer depends on a regulated transmission
16 provider with generation assets in the same geographic
17 market to act as its agent in acquiring electric power or to
18 provide reliable access to generators from which to obtain
19 power.

20 In this scenario, the utility gains by arranging
21 for power supplied from its own generators or by inhibiting
22 access to non-affiliated generators. Here, the
23 discriminating utility evades the rate regulation that
24 applies to its customer, and so it's a secondary tier
25 effect, but one which is also potentially of concern.

1 One way to help prevent and -- to detect, and,
2 therefore, to prevent the evasion of rate regulation is to
3 develop methods of establishing market-based values for the
4 affiliate transactions, establishing estimated market values
5 for transactions is an important task in many contexts, as I
6 mentioned a few moments earlier.

7 There are several approaches which are used in
8 various contexts, and let me just mention a few of those:
9 One approach is to hold an open solicitation of bids with
10 announced objective criteria for selecting the winning
11 bidder.

12 This is the most direct and often the most
13 effective approach. Issues include obtaining several
14 bidders, so that you actually establish a competitive price,
15 assuring that bids are realistic from the affiliates, and
16 penalizing any bid reneging that occurs after the fact.

17 A second approach is for the regulators to check
18 the utility's selection of a supplier, after the fact or
19 before the contract is signed. And these don't necessarily
20 involve using a bidding approach. There are techniques
21 which use a list of comparables, there are various
22 econometric techniques for establishing values based on a
23 number of transactions in different areas, and all of those
24 are approaches that can be used and don't involve the direct
25 RFP type approach.

1 Another approach is to evaluate the profitability
2 of a prospective contract to the affiliate and to prohibit
3 bids by which the affiliate would earn a higher rate of
4 return than allowed for the parent utility. This
5 effectively expands the range of the cost-based rate
6 approach to the affiliate.

7 Existing prudency reviews are another approach,
8 although doing it after the fact risks not detecting things,
9 and, therefore, allowing a lot of it to go through which
10 might not otherwise occur.

11 Another thing about prudency reviews is if they
12 have sufficiently large penalties attached to them, they may
13 have deterrent effects, even if they don't catch all
14 instances.

15 A direct method of preventing discriminatory
16 contracts with affiliates is to utilize third-party analysis
17 to compare supply bids and to determine the winning bid.
18 This is much like the independence requirement for RTOs and
19 ISOs.

20 A modification of this approach would be to allow
21 the utility to select the winning bid, but to effectively
22 require that a third party review the bid, if they decide
23 that the affiliate is going to be the winner.

24 All of these approaches present challenges, but
25 they are likely to constrain at least the most blatant

1 potential discriminatory solicitation decisions of
2 utilities.

3 Cost subsidization is another issue. Here, the
4 concern is that you expand, effectively, the less efficient
5 suppliers. The techniques for cross-subsidization may
6 include buying from an affiliate at inflated prices, or
7 selling at a price less than the market value.

8 Other examples would include offering free goods
9 or services to the affiliate, or giving preferences to
10 supplying an affiliate when the service or product involved
11 is in short supply. A parent utility whose ability to
12 exercise market power is constrained by cost-based rate
13 regulation, may find it profitable to cross-subsidize an
14 unregulated affiliate.

15 Various examples are available. One of the most
16 pertinent is the possibility that that cost subsidization
17 will avoid a bankruptcy from the unregulated affiliate and
18 the costs associated with that.

19 Approaches to preventing cross-subsidization
20 include cross-subsidization include establishing market
21 values for transactions, much as in the case of the other
22 types of discrimination.

23 As FERC has heard from FTC staff before, we favor
24 a cost/benefit approach for considering alternative forms of
25 separation as a technique to prevent cross-subsidization,

1 but, again, the context here is one in which that structural
2 approach has been rejected.

3 Now, let me turn very briefly, as my last point,
4 to the long-term inefficiencies due to favoritism in
5 solicitations. I mentioned three potentially important
6 losses of efficiency associated with such favoritism.

7 The first adverse impact of discrimination in
8 solicitation is inefficient expansion of the market position
9 of the affiliates, resulting higher social costs, such as
10 higher average production costs, because a less efficient,
11 subsidized firm has a larger market share.

12 Another is slower diffusion of innovation because
13 the entry based on innovation is less profitable.

14 Another is less consumer choice, because some
15 suppliers are forced out of the market that would otherwise
16 be in the market, and there could be an average lower
17 quality because the lower quality subsidized firm has a
18 larger market share.

19 The second adverse impact that I'd like to
20 mention is increased concentration in wholesale electricity
21 markets, caused by the relative decline of stand-alone
22 suppliers. To the extent that a utility is the most
23 attractive customer in its distribution franchise area, and
24 the independent suppliers are foreclosed from doing business
25 with the buyer or face discrimination in selling to this

1 customer, the stand-alone suppliers are more likely to exit
2 or not to enter to begin with.

3 Increased concentration where concentration is
4 already high and entry is impeded, can contribute to an
5 increase in market power, either from unilateral
6 anticompetitive effects or coordinated interaction.

7 The third adverse impact stems from distortions
8 in wholesale and retail electricity prices, which send
9 inefficient investment signals to wholesale and retail
10 customers. Customers faced with inefficient price signals
11 are likely to make inefficient consumption and investment
12 decisions regarding energy conservation investment, location
13 of facilities, choices between production methods, and other
14 examples.

15 Since some of these investments are likely to
16 have long-term market presence, the inefficient price
17 signals initially result in some long-term changes and
18 basically inefficient choices on the demand side, which will
19 have longlasting effects.

20 In summary, both the evasion of rate regulation
21 and cross-subsidization are concerns when utilities engage
22 in transactions between the utility and its unregulated
23 affiliates. Although structural separation is the remedy
24 most likely to reduce the incentives to evade rate
25 regulation or to cross-subsidize, other approaches are

1 available.

2 All of these focus on detecting discrimination by
3 establishing market values for affiliate transactions. Open
4 market solicitations using third parties to analyze the
5 bids, are a potentially attractive approach, but techniques
6 that compare the proposed affiliate transaction to
7 comparable transactions are another option.

8 Inefficiencies that stem from discrimination in
9 solicitations include expansion of less efficient suppliers,
10 increased concentration, and distortion in pricing signals
11 and related investment incentives for customers, which my
12 have long-term effects. Thank you. That's the end of my
13 comments.

14 MR. PEDERSON: Thank you, John. Our next
15 panelist is Mr. Craig Roach, who is Principal of Boston
16 Pacific Company, and independent monitor of the Maryland RFP
17 process. Craig?

18 MR. ROACH: Good morning, everyone. Thank you
19 for inviting us, and thank you for having this proceeding.
20 We think that these competitive solicitations are as much a
21 marketplace as the spot markets.

22 They involve thousands of megawatts, sometimes
23 sales that involve multiple years, so they mean a lot to
24 consumers, so we really appreciate the attention being given
25 today.

1 Before I get to your eight questions, let me just
2 state a couple of principles: The principle that I use to
3 guide us in our thinking on solicitation is really simple.
4 Anytime we think about whether to have a solicitation or how
5 to conduct it, we have one goal in mind.

6 That goal is to get the best deal possible for
7 consumers in terms of price, risk, reliability and
8 environmental performance. We think, based on our
9 experience, that these solicitations can serve consumers.

10 Our involvement has ranged from being in several
11 Edgar cases here, to being in state cases across the
12 country, and, as Jerry mentioned, most recently, we were the
13 independent monitor for all of the Maryland solicitations.

14 So, with that introduction, let me try to give at
15 least short answers to your questions. Your first question
16 listed was, is Edgar enough? Is the Edgar precedent enough?

17 My answer is no. Now, it's not because I don't
18 like what's said in the Edgar precedent. There's a lot of
19 good concepts there, but my concern is that we can no longer
20 rely on after-the-fact, case-by-case enforcement of these
21 Edgar standards.

22 It's too expensive for intervenors and it's too
23 late, too late in the sense that harm to wholesale
24 competition has already been done. What I'd really like to
25 see the Commission do is give a very detailed, strong,

1 before-the-fact guidance on what is expected.

2 What I'd like to see is, out of the cases that
3 are now pending before the Commission, that the Commission
4 would come out and say, look, if you're going to bring an
5 affiliate transaction to us, we want it to be market tested
6 through a competitive solicitation and that competitive
7 solicitation must meet certain minimum standards.

8 One of your other questions asked about
9 jurisdiction. It's an important issue.

10 I think that with that method that I just stated,
11 I think that FERC is not telling the states what to do and
12 it should not tell the states what to do. What it's saying
13 is what the Commission will do if a docket is opened on a
14 transaction.

15 I think that if the Commission takes that
16 consumer point of view when it defines minimum standards,
17 then they are going to be in sync with the states and it's
18 going to be a basis for cooperative federal-state
19 partnership.

20 I mentioned minimum standards. Two of your
21 questions raise two minimum standards that I would certainly
22 include: One, you asked whether the solicitation should be
23 designed through a collaborative process? My answer is yes,
24 absolutely.

25 And it should not just be going through the

1 motions. If someone comes to you and says we use the
2 collaborative process, there should be evidence of
3 consensus, evidence of compromise.

4 You asked whether an independent monitor should
5 oversee the solicitation. Again, my answer is, yes,
6 absolutely. My preference is that that monitor be hired by
7 the state commission and work for that state commission.

8 Some of your questions asked about safeguards,
9 and, you know, I want to say up front that there is no
10 foolproof solicitation. Any solicitation can be abused by
11 affiliates and non-affiliates.

12 But there are ways to put safeguards in place,
13 and I want to close by mentioning three concepts: The first
14 is that the solicitation itself can be designed to minimize
15 the opportunity for abuse by any bidder. Clearly, the most
16 innovative solicitations in that respect are those that have
17 been held in New Jersey and Maryland.

18 Secondly, solicitations can involve safeguards
19 that target the areas that are most likely to be abused. We
20 know those now; we know from experience, what they are.

21 Again, two of your questions lead me to two
22 examples: You asked about transmission. I think this is
23 one of the most troublesome areas in solicitation outside of
24 RTOs, and within transmission, the most troublesome area is
25 network resource status.

1 One of the minimum standards I'd like to see come
2 out of the Commission is that every bidder should have
3 access to a network resource assessment on terms comparable
4 to that provided to affiliates. They all have to be done on
5 the same standards in the same way.

6 Another one of your questions talks about the
7 rules of the game or monopsony power, and, again, let me
8 give an example an area that's been troublesome. Let me
9 just explain it in basic terms:

10 What I've seen that I think is trouble, is that
11 I've seen utilities invite bids and they'll say, look, I
12 want a ten-year offer with fixed prices, a reliability or
13 availability guarantee, and I want you to guarantee
14 replacement costs.

15 They then receive those bids, and then proceed to
16 compare them to a cost-plus utility offer which has none of
17 those consumer protections. Again, another minimum standard
18 that has to be set is that all bids must meet the same
19 requirements, and all must be evaluated on the same
20 criteria.

21 My third and final concept on safeguards is to
22 say that there's a phrase that the Commission has been using
23 in its Edgar Orders or Hearing Orders. It says that Edgar
24 require the affiliate deal to be above suspicion.

25 I'd like to see that made functional,

1 operational, and with the notion that there are always ways
2 to get around whatever rules you set up. What I'd like to
3 see is the Commission set a requirement for an affirmative
4 effort that the buyer come in to show the Commission that
5 the process has been transparent, that they have taken an
6 affirmative effort to make it transparent and that they have
7 done all that needs to be done to assure that it's the best
8 deal for consumers.

9 With that, let me again thank you, and I'd be
10 happy to go into detail on any of those points.

11 MR. PEDERSON: Thank you, Mr. Roach. Our next
12 panelist is Harvey Reiter, a Partner at Stinson, Morrison
13 and Hecker, LLP. His practice has involved laying the legal
14 groundwork for competitive restructuring in the natural gas
15 and electric industries. Mr. Reiter?

16 MR. REITER: Thank you. I want to extend my
17 thanks to the Staff and to the Commission for inviting me
18 here to speak today and to express my views on the questions
19 posed in the Notice.

20 There are eight questions and I prepared some
21 written comments. I haven't addressed all of them, but I
22 think that my questions do address the central concern
23 expressed by the Commission, mainly, how to devise
24 competitive solicitation processes that are fair and produce
25 good outcomes, where affiliates, utilities and their

1 affiliates are involved.

2 I should give a disclaimer at the outset, too.
3 Much of my work has been on behalf of state public utilities
4 commissions, and so my world view is probably informed to
5 some degree by that experience.

6 But I'm here expressing my own views and not
7 necessarily those of my clients, regardless of how
8 persuasive and logical you may find them. I did want to say
9 -- and with a representative of the FTC here today, that I
10 didn't expect to be a more aggressive proponent of a
11 structural approach than someone else on the panel, but my
12 own preference in approach the questions that were posed is
13 to look for structural solutions that are legal and
14 politically viable to addressing affiliate relationships
15 with utilities, as opposed to more intrusive regulatory
16 procurement rules and regulations.

17 I think the Commission or any commission at the
18 state level interested in the subject can devise a pretty
19 good set of rules, but they will never be able to detect all
20 forms of discrimination, something that Craig mentioned, but
21 there are enforcement costs that go with any set of
22 guidelines.

23 And so even if you devised the best set of rules,
24 you need to devote sufficient resources to prosecute
25 violations. Those are problems that are avoided in large

1 part by structural solutions.

2 Let me tell you what I have in mind, though, by
3 structural solution. It's simply this: In competitive
4 solicitations by utilities seeking supply from affiliates,
5 what I would suggest is the following; that affiliates
6 interested in obtaining market-based rate authority, would
7 have to agree in advance that they are not permitted to sell
8 to their utility affiliates, except in instances where the
9 presence of the affiliate is necessary to provide a
10 sufficient number of bidders to produce a competitive
11 outcome in a bidding process.

12 I would add, too, that there are circumstances,
13 and the Commission, I know, is aware of it, where there
14 aren't enough bidders in the marketplace, even with the
15 presence of affiliate. And in those instances, I think the
16 answer is that the affiliate should be selling at a cost-
17 based, not a market-based rate.

18 Now, if the Commission decides not to pursue a
19 structural approach, I think there's still some structural
20 elements and alternatives. And even under -- the approach I
21 have suggested is that affiliates could sell into the
22 solicitation process if their presence was necessary to
23 provide a competitive outcome.

24 You needed a sufficient number of bidders. But
25 in those instances, and also if the Commission generally

1 concludes that affiliates should be eligible to participate
2 in the process, when there are some of what I would call
3 structural safeguards -- and both of the prior speakers have
4 touched on them -- mainly, that there ought to be some
5 independent party, both designing the bidding process and
6 conducting the evaluation.

7 That's a structural solution of sorts, and it
8 helps ensure that the process itself is neutrally devised
9 and implemented. I should add, though, that the concern
10 about structure -- I think my concern is somewhat less in
11 the context of sales by utilities to their affiliates in
12 instances where the utility may have excess capacity or
13 stranded capacity and where the sale of that excess power
14 helps defray the costs to ratepayers.

15 In that instance, what I think you're looking for
16 is the highest price that can be obtained through the
17 bidding process, and with a blind bidding process,
18 independently run by a third party, I don't see the same
19 kinds of concerns about structure as I would in the context
20 where the utility is buying from the affiliate.

21 In that case, if you had a blind bidding process,
22 independently conducted, adding additional bidders,
23 including affiliates, could benefit consumers.

24 I also wanted to touch on a couple of the
25 questions that were asked in the outline about the role of

1 state commissions, and I think a number of states have
2 addressed the issue of competitive bidding, both in the
3 context of purchases of power supply and other services and
4 goods from affiliates.

5 And the Commission, I think, should draw from
6 their experiences in designing its own rules. Some of them
7 have gone through these processes several times and they
8 have learned from their experiences, and the Commission
9 could learn from what those states have done.

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1 Last, I think that the Commission needs to
2 carefully tailor any rules that it adopts to ensure that it
3 doesn't interfere with efforts by states to avoid cross-
4 subsidization, something that our first speaker touched on.

5 I have addressed these topics in a little more
6 detail in the written comments, and hopefully in the open
7 discussion, we'll have a chance to talk about those in more
8 detail, but, again, I want to thank you for inviting me here
9 today.

10 MR. PEDERSON: Thank you, Mr. Reiter. Our next
11 panelist is Ron Walter, who is the Executive Vice President
12 of Development at Calpine Corporation. Mr. Walter?

13 MR. WALTER: Thank you, Mr. Chairman and
14 Commission Staff. It's my pleasure to have the opportunity
15 to provide a statement at this important conference.
16 Calpine is the largest independent power company in the
17 United States, and so we have some very specific views on
18 this subject.

19 The Notice of this technical conference, I think,
20 rightly focuses on assuring the lowest-cost supply of
21 electricity to consumers. This worthy goal has been the
22 primary focus of the Commission in doing competition over
23 the last decade.

24 You've taken some important steps to create a
25 level playing field, but the job is far from done. The

1 industry is straddling between the old and the new.

2 The old is the vertically integrated monopolies
3 that control wholesale supply, and the new era is
4 competitive suppliers trying to enter into markets. At this
5 critical juncture in this murky middle ground that we have,
6 the achievement of the Commission's goals is at severe
7 risk.

8 The current situation is untenable and sharply at
9 odds with the Commission's pro-competitive goals. It is
10 virtually impossible for an independent power producer to
11 finance the construction of a generation project without a
12 contract from a buyer in these days.

13 In most areas of the country, independent
14 companies do not have access to a fair process to get those
15 contracts. In addition, litigating at FERC, all these
16 disputes over biased or nonexistent procurement processes is
17 very costly, time-consuming, and leads to uncertainty among
18 all market participants.

19 Competitive suppliers like us, we don't have the
20 deep pockets or the captive customers to pass on these
21 litigation costs like the utilities do.

22 The Commission must adopt procurement standards.
23 The very foundation of the competitive wholesale markets is
24 at risk without Commission action, and customers will not
25 have access to the lowest-cost supply of power.

1 I'd like to give you some of our experiences that
2 we've seen out there in the marketplace. Given the downturn
3 in the market over the past several years, Calpine has seen
4 more and more utilities finding ways to use their monopoly
5 status to protect their own generation, or to assist their
6 affiliates.

7 In several regions of the country, we've
8 experienced the following examples of discriminatory conduct
9 and sham processes on competitive bidding: One, utilities
10 that deal only with themselves or their affiliates, with no
11 competitive procurement at all;

12 Two, utilities that use an RFP process that looks
13 good on paper. Some even have a, quote, "independent
14 monitor," for appearance purposes, but then choose their own
15 affiliate or a self-billed;

16 Three, solicitation processes where good-faith
17 bids are made, but the utility merely uses the bids as a
18 benchmark for a build/own transfer into their own system;

19 Four, utilities refusing to deal with competitive
20 suppliers, in turn, creating distressed assets that are then
21 bought by the utilities themselves;

22 Five, a variety of other preferences to utility
23 affiliates, including preferential sharing of information,
24 preferential access to transmission, preferential transfers
25 of fully-developed and permitted construction sites to their

1 affiliates; also devices such as a service company
2 arrangement to favor an affiliate and to circumvent the
3 standards of conduct.

4 A utility choosing itself, No. 7, or an
5 affiliated supplier to build it, and justifying it by
6 playing this reliability card in the wake of the August 14th
7 blackout last year, even though this is a false
8 justification.

9 I took a scorecard of some of the competitive
10 procurements that we've been involved with in the last 36
11 months. I've noted 17 separate competitions or flat-out
12 utility choices that exhibited one or more of the above
13 characteristics.

14 They are in 12 states: Georgia, Alabama,
15 Florida, Louisiana, Wisconsin, California, Utah, Idaho,
16 Nevada, Washington, Oregon, and Arizona. This represents
17 over 12,000 megawatts of opportunities denied to independent
18 power producers, and also denied access to the lowest cost
19 to the consumer.

20 Another scorecard that I took was to look at the
21 independent power companies themselves. Four years ago,
22 there was a growing number of IPPs and they themselves were
23 growing. Today, I took a look at 12 companies as a sample,
24 who subsequently failed in the business in that short, four-
25 year timeframe. Four have gone bankrupt.

1 Five sold all or a majority of their assets. One
2 sold out altogether. Two canceled their projects and exited
3 the business.

4 Now, I admit that some of these companies had
5 poor strategies and they would have died on their own, but I
6 contend that a number of these companies were not successful
7 because they didn't have good access to selling their power
8 to consumers and customers.

9 Since 1992, the independent power industry has
10 invested \$100 billion in new power plants, based on the
11 concept that we have access to customers. That simply
12 hasn't happened in a lot of areas of the country.

13 If I leave one point today, it's that now is the
14 time to act. Deliberating and litigating and extending this
15 process too much further into the future, there won't be
16 much to fix.

17 What are my recommendations? The Commission has
18 the obligation arising from the Federal Power Act, to ensure
19 that wholesale power is free from undue discrimination and
20 preferences, and the customers have the benefit of a market
21 that functions well.

22 While RTO development is important, it's been
23 slow. There are some things, in the meantime, that the
24 Commission should do to improve competitive markets:

25 First, permission to sell at market-based prices

1 is a privilege, not a right. Utilities that do not engage
2 in competitive wholesale procurement and fail to comply with
3 FERC standards prohibiting affiliate abuse, or erect
4 transmission or other barriers to entry, should be denied
5 this privilege.

6 Second, the Commission must strengthen Edgar.
7 Fair, competitive procurement should be the rule for
8 affiliate transactions. Edgar is all about making sure
9 affiliate abuse is not present in transactions among
10 affiliates.

11 And the competitive procurement process should be
12 made the standard, rather than some other benchmark.

13 Third, and, more generally, the Commission should
14 adopt competitive procurement standards. They should
15 include an independent evaluator, equal access to the
16 transmission system, openness and transparency of the
17 process. It should also include a specific definition of
18 needed products, so that people can respond.

19 Fourth, the Commission, without delay, should
20 implement the new standards of conduct for transmission
21 providers and closely monitor and investigate affiliate
22 abuses. Fair, impartial, and transparent wholesale
23 competition solicitation standards promulgated by FERC are
24 absolutely critical to continuing the progress towards
25 broader customer benefits and to help move this industry

1 forward, not backward.

2 I'd like to close with the comment that some who
3 support the old way of doing business and want to retain
4 vertical monopolies, will say that competitive procurement
5 is the business of the states and not the Federal
6 Government. I say that it's FERC's responsibility when we
7 see the level of discrimination that's taking place in many
8 areas around the country.

9 This development of fair and open competitive
10 processes can, and I hope will not end up being a battle
11 between the states and the Federal Government, but a
12 partnership, because, after all, the one thing we have to
13 remember is that we have the same goal of getting the
14 lowest-cost, most-reliable product to the consumer. So,
15 with that, I'll close. Thank you.

16 MR. PEDERSON: Thank you, Mr. Walter. Our fifth
17 and final panelist for this morning's session is Ed Comer.
18 He's Vice President and General Counsel for Edison Electric
19 Institute. Mr. Comer?

20 MR. COMER: Thanks very much. Let me just start
21 off with the point that I think is fundamental: All power
22 purchase and sale transactions have to be conducted in a
23 fair manner, without bias and without self-dealing that
24 favors affiliates. And the goal is to achieve the best deal
25 for utility customers with the best cost/risk balance.

1 The Edgar Standard provides three ways to
2 demonstrate that buyer has chosen the best supplier from
3 among the options, taking into account both price and non-
4 price factors -- and that's important.

5 Most folks this morning have talked about the
6 first of those standards of head-to-head competition, either
7 through a formal solicitation or an informal negotiation
8 process. That's probably what you're going to do for your
9 longer-term deals.

10 But Edgar has two other criteria that we think
11 are perfectly valid -- demonstration of prices that non-
12 affiliated buyers were willing to pay for similar services,
13 and benchmark evidence that shows prices, terms, and
14 conditions of sales made by non-affiliated sellers.

15 These certainly are going to make a lot more
16 sense in RTOs with liquid markets and other places, and
17 certainly for shorter-term transactions, and they continue
18 to be valid. Now, I recognize that when a utility chooses
19 an affiliate over other competitors as its supplier, there is
20 heightened concern about the potential for self-dealing and
21 about unfairness in the selection process.

22 But the choice of an affiliate, in and of itself,
23 may well be the best option in a given circumstance, so I
24 don't think you should just ban them or throw them out. In
25 fact, the Commission itself has a long history of approving

1 such transactions, and as long as the process is fair, any
2 proposal to prohibit or restrict affiliate transactions
3 could harm consumers.

4 Now, the ultimate goal of the solicitation
5 process is to enable the utility to balance both cost and
6 risk in providing the best service at the best price. Now,
7 sometimes the answer may be to build new generation.

8 These days, it may be to buy a distressed asset.
9 Other times, the best approach may be to enter into a
10 purchase power agreement with a power marketer or an
11 independent or an affiliated producer.

12 The big deficiency in the Edgar Standard is that
13 it fails to recognize that most of the competitive
14 solicitations that take place are issued by load-serving
15 entities for the purpose of serving native load. Most of
16 these entities are state-regulated.

17 The process is usually conducted with
18 considerable oversight and direction from the state
19 commissions, and it's always conducted with the full
20 knowledge that an imprudent condition can lead the
21 applicable state commission to disallow cost recovery, as
22 some utilities are regulated by multiple state commissions,
23 which further heightens the scrutiny of the procurement
24 process.

25 We believe the state involvement provides strong

1 assurances that the process will be conducted in a fair and
2 unbiased fashion, and will achieve the best results for
3 customers. In listening to Mr. Walter talk about 12 states
4 where there have been affiliate transactions, I personally
5 find it hard to believe that there will be 12 states that
6 are all not doing their jobs to decide what's the best deal
7 for their customers. I think it's strong evidence of the
8 fact that affiliated transactions could be very beneficial
9 for customers.

10 Now, why might there be an affiliate transaction
11 or why might an independent power producer's proposal be
12 rejected? In making the evaluation between building a power
13 plant, buying an existing power plant, or executing a long-
14 term power purchase agreement, you have to look at a variety
15 of factors:

16 Certainly these include a lot of factors that are
17 established by your state like renewable energy
18 requirements. You do have to look at the construction risk
19 of building a plant, you also have to look at the credit
20 risk of your counterpart.

21 You also have to take into consideration,
22 accounting standards dealing with direct or inferred debt,
23 and you also have to look at what S&P's and Moody's and the
24 bond rating agencies will say about the impact of debt,
25 long-term contracts as debt.

1 You have to look at transmission, reliability
2 issues, you have to look at the likelihood that your
3 regulator is going to approve the transaction, and that does
4 include FERC. And, of course, you have to look at the cost
5 to mitigate unwanted risks.

6 Now, at this point in the business cycle, there
7 is a surplus of distressed generation with assets at very
8 attractive prices in some markets, and, in comparison, long-
9 term contract purchase options can raise substantial
10 questions about the long-term financial health of the
11 entities involved.

12 This Commission is well aware of such credit and
13 default risk issues. Unfortunately, uncertainties about
14 some of these issues have been exacerbated by the Commission
15 itself's failure to resolve what constitutes reasonable
16 assurances when a party's credit rating is downgraded under
17 the Western Systems Power Pool tariff.

18 You can't solve all the credit issues, but you
19 can help clarify the rules and contracts. Given these
20 circumstances, generating asset purchases may well prove to
21 be the best business alternative.

22 The Commission should not exhibit a bias against
23 this choice when it proves to be the best alternative for
24 utilities and their customers.

25 Now, let's talk about the states. I agree, I

1 think, with virtually everybody on the panel who has said
2 that it's very important for this Commission to work closely
3 with the states in a cooperative manner. States have many
4 different competitive solicitation processes that they use
5 to determine the best way to serve their retail customers.

6 Some of the successful ones, very successful
7 ones, for instance, the New Jersey and Maryland programs
8 that were mentioned today. Other states are examining new
9 programs or looking to revise their programs. Some states
10 use an independent monitor, others don't. They believe that
11 their role is sufficient to assure fairness of the process
12 and to assure the adequacy of the process.

13 Frankly, I regret that you haven't invited more
14 states to this conference, because I think that a continued
15 discussion between the Commission and the states to develop
16 best practices and to understand how each approaches the
17 issues, would be very useful.

18 There is no one right solution or practice or
19 process common to all of the states. Each state may hold
20 differing views on the exact criteria and the mechanics
21 that a procurement process should possess.

22 It's also important to note that the parties
23 vying to sell power are very active in the state proceedings
24 that address procurement issues. They have a forum and they
25 have remedies in the states, if they are convinced that

1 those processes are not fair. Thus, when a state is
2 involved, FERC doesn't need to rely upon its own independent
3 monitor or other independent entity to evaluate fairness.
4 That's the state's role.

5 Now, for all these reasons, the Commission -- and
6 it does have a responsibility to review wholesale rates
7 under Section 205 of the Federal Power Act -- should still
8 defer to state commissions regarding how a utility best
9 procures power to serve its native load.

10 While the Act gives this Commission
11 responsibility over wholesale transactions, it preserves the
12 retail electric service responsibility for the states. And
13 it's the states' role to ensure adequate service, fair
14 procedures, no self-dealing, and just and reasonable terms
15 and conditions.

16 In addition, I'd like to point out, because we're
17 talking about affiliate transactions here, that the last
18 time Congress addressed this issue it clearly looked to the
19 states, not to FERC, to address the potential for affiliate
20 abuse in sales of power.

21 Section 32(k) of PUCHA, enacted in 1992,
22 prohibits sales of electricity from an EWG to an affiliated
23 utility, unless it is specifically approved by every state
24 commission having jurisdiction over the rates of that
25 utility. In conclusion, we urge the Commission to act in

1 concert with these provisions, and to modify its Edgar
2 approach in a manner that explicitly recognizes and
3 complements the responsibilities of state commissions.

4 We recommend continued cooperation and close
5 communication with state commissions. We urge the
6 Commission to avoid moving in a direction that requires a
7 uniform approach for all competitive solicitations.

8 I think a one-size-fits-all approach would
9 intrude upon state responsibilities for how jurisdictional
10 utilities, state jurisdictional utilities meet their retail
11 obligations to serve load, would also intrude upon the EWG
12 affiliate transactions under PUCHA that Congress told the
13 states to regulate.

14 We fear that any effort to force states into a
15 process that they don't feel comfortable with, risks that
16 the states will turn to resource solutions that are not
17 FERC-jurisdictional, so that their judgment would not be
18 second-guessed. This would not be in anybody's interests.
19 With that, thank you, and I look forward to our discussion.

20 20

21 MR. PEDERSON: Thank you, Mr. Comer. At this
22 point, I'm going to open up the questions and discussion for
23 the staff and the panelists as well. I encourage everyone to
24 participate.

25 The focus of this conference, I think, is to come

1 up with the -- we've heard a lot today. We've heard a
2 number of folks talk about fair and unbiased solicitations.
3 We've heard the differences in the way these solicitations
4 are being conducted. I think that one of the main things
5 that we want to get out of this conference is to start
6 establishing the criteria of what are the standards for a
7 fair and unbiased solicitation process.

8 That's kind of what I'd like to focus on, and I'm
9 going to direct my first question to Craig Roach.

10 To start this off, I guess that the first thing
11 that I would like to understand is if you could contrast a
12 solicitation process, an RFP that might be conducted within
13 an RTO area, versus a non-RTO area. What are the
14 differences between those types of approaches?

15 MR. ROACH: Well, they needn't be really
16 different. You just have to do things a bit differently.

17 You know, the Maryland and New Jersey approaches
18 are -- you know, we view them as innovative. They are
19 consumer-focused. In fact, the bids are to take
20 responsibility for a percentage share of a customer class
21 need. They are that consumer-focused, so they are
22 innovative in that sense.

23 They are designed to avoid any opportunity for
24 abuse because, in the end, they are price-only bids. You
25 literally get the bids on Monday and the session is over on

1 Friday. You can choose the bids.

2 And as to your question, I'll say that those
3 innovative solicitations are not by accident in the most
4 innovative RTO and in PJM. PJM helps tremendously. And
5 they're just willing to help, but they help tremendously in
6 areas like transmission assessments.

7 They help tremendously in prequalification. You
8 know, when you bid, you have to be accepted as a buyer and
9 seller in PJM. So there's a lot of accommodation or
10 infrastructure that the RTO provides that is truly
11 beneficial.

12 But when you're outside an RTO, you just have to
13 get that accommodation another way. If there's not an RTO,
14 for example, taking care of transmission, I think that
15 either an independent third party transmission assessor or
16 assessment has to be done or, at a minimum, the independent
17 monitor has to be capable of going toe-to-toe with the
18 utility transmission assessment. This is especially
19 important, as I mentioned, in network resources.

20 Another point thing in PJM or any RTO is that a
21 bidder has a spot market to turn to, a bidder can turn to
22 that to fill in and purchase power. A bidder can turn to
23 that spot market to lay off capacity, if they have too much,
24 especially as is true in Maryland and New Jersey where the
25 supplier is taking market risk.

1 Well, again, if you don't have that, you may want
2 to have an accommodation in a non-RTO location. And that
3 accommodation might involve transparency and economic
4 dispatch.

5 So, you know, I take your question and I agree
6 that perhaps my experience is that things go better in an
7 RTO, especially on transmission, especially on the spot
8 market access, but you can accommodate, you can create those
9 same accommodations outside an RTO, if all the parties are
10 willing to do it.

11 MR. PERLMAN: Can I ask a followup question on
12 that? I guess my experience and understanding is that in an
13 RTO, what you're really doing in bidding on the things like
14 Maryland and New Jersey, is, you're providing the economic
15 wherewithal to stand behind the default risk for the price
16 guarantee you gave, because there's fungible products in
17 ICAP, ancillary services, energy, what have you, and you
18 could, if you wanted to, lean on the spot market every day
19 for everything, and just pay the bill and the RTO would
20 effectively undertake the supply for you.

21 Now, that's probably not a good business
22 strategy, but you could do that. In a non-RTO region,
23 you're going to have to, like you said, get a network
24 resource that meets the test, that can do an integration
25 agreement, that can deliver, and that deals with the

1 transmission issue. There's much more physical orientation
2 than the RTO structure. Do you agree with that?

3 MR. ROACH: I think there's some truth in what
4 you're saying. I think that if you go out there and you
5 talk to state regulators, for example, in non-RTO states,
6 you will, as your question implies, talk more about asset-
7 backed solicitations, often meaning unit-contingent
8 solicitation.

9 It's a feeling, as implied by your question, that
10 they want to have a place to go kick the tires. They want
11 to see the power plant, so I think that's generally true.

12 At the same time, financially firm -- I think
13 that's what you're saying -- financially firm products like
14 firm LD sales, you know, summer blocks of power, they're
15 sold all over the country.

16 So, financially firm is accepted, too, but your
17 point is a firm one.

18 MR. PERLMAN: I guess the bottom-line question
19 is, does that cut down -- if you're in the more physical
20 world, does that cut down on the number of competitors you
21 might have to participate in that kind of arrangement, as
22 opposed to the RTO where anybody with an adequate balance
23 sheet can show up. They will have to sign up to the PJM
24 agreement or whatever, but they can play and they can be
25 effective.

1 MR. ROACH: I think it really depends. It
2 depends on the product. If you're in an area -- if you're
3 outside an RTO and you have a solicitation for a product
4 defined as unit-contingent gas-fired, combined cycle, I bet
5 you get a lot of bidders, just by the nature of the fact
6 that people own those power plants.

7 If you were to attempt to get system power, you
8 know, take a percentage share of a customer and take
9 responsibility for that customer class percentage share, I
10 think that would be difficult, outside of an RTO, although
11 accommodations could be made.

12 MR. PEDERSON: Continuing with that them, so,
13 what I'm hearing, I think, is that within an RTO, the RTO
14 can participate a little bit and help out on those
15 solicitations, especially on the non-price factors like
16 transmission and so forth.

17 I'd like to address a question to Ron on that, on
18 outside of an RTO. What kind of process needs to be -- what
19 kind of collaborative process needs to be developed so that
20 solicitations outside of an RTO can be reliable in terms of
21 when there is affiliate bidding in there?

22 What kind of collaborative process needs to be
23 established so that these non-price terms, non-price factors
24 are evaluated fairly?

25 MR. WALTER: This is our view: We think that in

1 the ideal world, that state commissions would tell their
2 utilities what standards they need to meet with respect to
3 reliable supply of electricity; in other words, establish
4 what a reserve margin ought to be for that particular state
5 and that particular area.

6 Then I think it would be the responsibility of
7 the utilities to design a process to acquire the necessary
8 generation to supply that, specify the timing, where it
9 should be, and how many megawatts.

10 And at that point, it's our view, in a non-RTO
11 situation, to create a fair and open and level process, is
12 to turn the solicitation of that new generation over to an
13 independent monitor, manager, entity, whatever you want to
14 call it.

15 A process would thereby be conducted where all
16 suppliers would have an opportunity to respond to that need
17 that's been established. And we're not saying that we don't
18 think affiliates should be allowed to bid in those
19 processes.

20 We're not saying that even in a case where a
21 utility might be able to bid in a rate-based asset at that
22 solicitation; all we're asking is that all the bidders, all
23 the potential suppliers, live under the same set of rules;
24 that they all have the same access to transmission; that
25 they all have the same access to whatever sites they want to

1 offer up; that they have the ability to include and the
2 independent monitor has the ability to evaluate all of the
3 factors, including credit, including financial stability,
4 including all of these non-price factors, and that they all
5 be treated equally and not preferentially, which we are
6 finding in these 12 states, that that is happening.

7 MR. PERLMAN: May I ask a followup question on
8 that as well? You had said earlier that you thought it
9 would be difficult to finance a project without a long-term
10 contract from the utility. Mr. Comer talked about the
11 balance sheet impact on that and how that's viewed as debt
12 by the rating agencies for the utility.

13 So, in the fair analysis you're talking about,
14 should the alternative supplier's bid be burdened with the
15 debt consequences that the S&P or Moody's is placing on the
16 utility by entering into what would be effectively a capital
17 lease or something like that, in their eyes in calculating
18 the results?

19 MR. WALTER: A couple of points on that: In
20 responding to a couple of RFPs, we've faced this issue of
21 debt equivalency. We have created a lease structure that
22 satisfies the rules, and we've gone to, you know, our
23 accounting agency and they have endorsed that.

24 So we have been able to figure out a structure to
25 make that work. But even more so than that, I think that

1 when you look at this whole debt equivalency issue and what
2 was created by S&P, what I would like to do is to ask you to
3 step back and look at the bigger picture.

4 A lot of the issues that S&P is worried about is
5 what happens after the fact? Does the Commission get along
6 with the utility? Are they going to disallow in the future?
7 Is there uncertainty related to recovery?

8 Now, in my view a contract has a lot more
9 certainty in the front end than a rate-based plant, or one
10 that's BOT'd and put into the rate base, because, as you
11 know, in a lot of cases -- and I will just mention Mountain
12 View here -- with that particular power plant, there are no
13 limitations or liabilities for late delivery.

14 They are allowed to overrun by \$30 million. They
15 are allowed to pass through all the environmental and
16 operational costs that may occur, that were unknown at the
17 time of the transaction.

18 And there is an opportunity later on for the
19 Commission to disagree with the utility on that, creating a
20 risk that -- so far, the S&P has only been focused on the
21 power purchase agreement side.

22 Our argument in the Mountain View case is that if
23 we were to enter into a power purchase agreement -- and this
24 applies to other cases, as well, and I didn't want to single
25 that out -- where we would enter into a power purchase

1 agreement, we would take full responsibility for
2 construction, for the cost of it, to schedule it.

3 We'd pay LDs if it didn't get done on time. We
4 would take on environmental risk, we would take on
5 operational risk, we would take on delivery risk, and in
6 some cases, providing replacement.

7 This creates a lot more certainty, in my view,
8 for the utility and their relationship with the Commission,
9 and perhaps a rate-base plan. I'm encouraging S&P and
10 Moody's and others -- and Moody's is looking at this, too --
11 to look at the broader picture of this whole debt
12 equivalency issues.

13 MR. PERLMAN: Was that a yes or a no?

14 (Laughter.)

15 MR. PERLMAN: I mean, it would seem to me that
16 you couldn't avoid having to burden this contract, if there
17 was, in fact, a cost of capital impact on the utility by
18 using up some of their debt capacity and being looked at
19 with their ratios and all that, for this contract. Would
20 you agree that that's something that, in a fair analysis,
21 should be considered as in --

22 MR. WALTER: Yes, as long as it's considered for
23 the alternatives, as well.

24 MR. COMER: Can I just say one thing there?
25 There are some utilities that would love to address this by

1 receiving an equity adjustment to help compensate for the
2 debt equivalency issue. That is a state issue, whether or
3 not the state decides to do it.

4 And that's one of the reasons, you know, the
5 state involvement in this and how you set it up is very
6 important.

7 MR. PEDERSON: Dick?

8 MR. O'NEILL: As a matter of fact, I agree with
9 you that the asymmetry between the purchase agreement and
10 the rate base treatment is a serious problem that needs to
11 be dealt with. Ed, I assume from what you said, that the
12 affiliates are winning these procurements because they have
13 some combination of the best technology, the best risk, the
14 best price, or whatever, in these procurements?

15 MR. COMER: I would assume so, too. And in some
16 cases, this may be the better credit profile. You know, I'm
17 not involved in the individual procurements. They are not
18 all affiliate-won by any means.

19 MR. O'NEILL: Well --

20 MR. COMER: There are lots of ones that --

21 MR. O'NEILL: -- affiliates --

22 MR. COMER: -- independent generators who are
23 either selling long-term contracts or selling their plants.

24 MR. O'NEILL: Right, maybe we don't have a
25 problem. I guess the statistics could bear that out, but if

1 we believe some of the other people here, especially Ron,
2 that it seems that the affiliates are winning a significant
3 portion of their own company's bids.

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1 If they are really the best, from some
2 combination of factors, why aren't they winning in other
3 procurements?

4 MR. COMER: Because they are fair procurements,
5 the states are involved.

6 MR. O'NEILL: But if they're offering the best
7 deals --

8 MR. COMER: You can look in New Jersey and there
9 are deals in New Jersey where sometimes the utility -- that
10 everybody sets up as, you know, a role model, sometimes the
11 affiliates win and sometimes they don't.

12 MR. O'NEILL: Those procurements are --

13 MR. COMER: Now --

14 MR. O'NEILL: -- than some -- I'm talking about
15 the longer-term procurements, you know, for long-term
16 capital assets.

17 I mean, it looks like the affiliates are winning
18 a huge portion of those procurements, and yet they are only
19 winning them when they're affiliates. And if they are
20 offering the best technology or the best of that litany of
21 issues that you gave, they should be winning in other
22 places, shouldn't they?

23 MR. COMER: Each transaction and each party is
24 different. I would not generalize across the board.

25 MR. O'NEILL: So there are no good producers;

1 there's no --

2 MR. COMER: I mean, I just don't know how you
3 generalize like that.

4 MR. REITER: Can I make a comment on that? I
5 mentioned before that I thought a structural solution was a
6 better one, and it was based on this thought that it's not
7 at all unfair where there's a sufficient market, where there
8 are enough bidders to say, well, affiliates, you're just not
9 going to compete in this market.

10 I go back to an example, I think, unfortunately,
11 where the government didn't take up on the communications
12 industry. When the first broke up AT&T, the Bell Operating
13 Companies said, you know, how about letting us offer long-
14 distance service in those regions of the country where we
15 don't have a local exchange network?

16 If we're good, we'll obtain the business, and if
17 we're not, well, then we'll fail on the merits. And the
18 settlement ultimately adopted, didn't allow them in at all.
19 Ultimately in '96, the Communications Act was passed and
20 they established this elaborate check list of competitive
21 conditions that had to be met before an operating company,
22 one of the historical ones, could enter into long distance,
23 but they could offer it in their own service territory.

24 Now, over time, the FCC has approved most of the
25 -- given permission to most of the companies that offer long

1 distance service, to offer them in their local territories,
2 and virtually overnight, they have obtained huge shares of
3 the long distance business in their own territories.

4 And it makes you suspicious. I mean, it may be
5 that they just won on the merits, but the concern is that if
6 there's enough competition out there without them
7 participating in the market, why not just say -- you know,
8 adopt a rule saying, well, okay, this is one area where
9 you're not allowed to compete, and if you're good, you'll
10 still make a lot of money in the other markets where you
11 would on the merits.

12 MR. O'NEILL: I would feel a lot more comfortable
13 in this debate if the affiliates were winning outside their
14 own territory, but that doesn't seem to be the case.

15 MR. PERLMAN: If the affiliates wanted to charge
16 sort of an under-market price, because they wanted to win
17 and were willing to accept a sub-optimal return, is that
18 something that regulator should be concerned about for your
19 competition issue?

20 MR. REITER: I think so, long-term. You know,
21 you get into an area in antitrust policy where it talks
22 about predatory pricing, and it's a difficult concept to
23 establish on the facts, that someone has entered into a
24 market, selling low-cost or below some average embedded cost
25 in order to obtain market share and then drive out

1 competitors, long-term.

2 In the short term, consumers are going to
3 benefit, but, long-term, it may make others who are
4 interested in entry, reluctant to participate, because they
5 figure, well, you know, this is just isn't worth my while.
6 If the utility's got staying power, they -- you know,
7 there's also the potential for cross-subsidization that may
8 make them be able to sustain that type of a strategy, longer
9 term than some other entity might.

10 MR. COMER: Dick, you just said something that I
11 want to make sure I understand. Are you saying that
12 affiliates are not winning outside their service territory?

13 MR. O'NEILL: Not in the same proportion that
14 they're winning inside their own.

15 MR. COMER: So you're saying that companies like
16 Constellation or Mission Energy or, you know, any of the
17 others that are, you know, affiliates --

18 MR. O'NEILL: There may be exceptions, and I can
19 feel very comfortable with the exceptions, but they're not
20 the rule.

21 MR. PEDERSON: Let me swing the questioning over.
22 We've got a question for Mr. Hilke regarding affiliates that
23 we've been discussing.

24 Has the FTC conducted any study or are you aware
25 of any study that has looked at the effect of affiliates

1 participating in competitive solicitations, whether it's the
2 electric market or other markets?

3 MR. HILKE: Well, we have, as I mentioned in my
4 opening remarks, looked at privatization as a general area,
5 and there, there is a clear concern about whether the
6 affiliate offer is a realistic one, and what sort of
7 guarantees there are that once the offer has been accepted
8 that it will be able to carry forward on that same basis.

9 The same issues have arisen in the federal
10 privatization efforts for the A-76 program, and in both of
11 those instances, the techniques which have been used to try
12 to make sure that the inside bid, essentially is a fair one,
13 have involved either some third-party assessment of that bid
14 or severe penalties for renegeing on the contract after it's
15 been signed.

16 MR. PEDERSON: That's after the fact.

17 MR. HILKE: No, in the case of third-party
18 review, it's before the fact; in the case of the renegeing
19 penalties, that's after the fact.

20 MR. PEDERSON: Okay.

21 MR. HILKE: So, both techniques have been used in
22 different contexts.

23 MR. PEDERSON: And, Mr. Roach, a question for
24 you: What demonstration needs to be made so that we could
25 be comfortable that the solicitation process is a good

1 process?

2 MR. ROACH: Well, again, I think there are
3 minimum standards. I think, first, that the design of the
4 process has to be done through a collaborative process. And
5 that's not just bumper sticker stuff.

6 You know, a good one is, we participated in
7 Arizona, and one of the approaches was, the first thing that
8 was done there was, we tackled the issue of product design,
9 which is hugely important in ensuring a fair solicitation.

10 The utility came into a meeting; it's off the
11 record; it's a lot of people that are in the market, you
12 know, a lot of consumer groups, suppliers, et cetera.
13 Anyhow, you tackle this first question on product design.
14 The utility brings in a forecast of their needs.

15 That's then discussed. Certain issues can be
16 resolved through consensus. If there are issues that can't
17 be resolved -- and there were -- the staff then opined
18 officially. It went to the Commission and the Commission
19 decided.

20 MR. PEDERSON: So the idea is, you go out with
21 the products, here's a proposal, get folks in, discuss it,
22 work out the details, get to an agreement to move forward,
23 so we have that set aside.

24 MR. ROACH: That's right, and then we tackle
25 transmission. In the West, there are lots of RMR issues.

1 The staff, again, the Arizona staff was really on top of
2 this, did some transmission -- they were in the middle of
3 transmission assessment, so we tried to tackle that issue
4 and we really tried to tackle the RMR issue.

5 Again, you know, there were issues that resolved,
6 some remained unresolved, and it goes to the Commission.
7 Then we took up the issue of the criteria. What's the RFP
8 going to look like? You know, what are the criteria?

9 Again, in a true collaborative process, a good
10 way to start is the buying utility comes in and says here's
11 my draft, and then lets all parties, all stakeholders, in a
12 multi-day meeting, say what they feel and try to resolve
13 issues. What's not resolved, goes to the Commission and
14 it's resolved pretty quickly.

15 That's a collaborative process that really, I
16 think, works, and, again, shows signs of consensus, shows
17 signs of compromise. I didn't mean to go off on that song.

18 But the second one of minimum standards is to
19 have an independent monitor. Again, I like it that the
20 monitor is hired by the Commission and works for the
21 Commission. That's the way it worked in Maryland.

22 That monitor has to be real, too. You know, I've
23 seen monitors that can't go toe-to-toe with the buying
24 utility. Well, you need that level of experience in your
25 monitor.

1 They have to have access to every part of the
2 solicitation, and they have to have the capability to go
3 toe-to-toe, and that includes transmission monitoring. So
4 you want an experienced independent monitor.

5 Thirdly, you want all bids evaluated on the same
6 criteria. And that sounds so simple, but, you know, again,
7 you're going to run into a difficult problem with cost-plus
8 versus pay-for-performance contracts, and you're going to
9 want to consider, if all bidders except the utility must
10 come up with fixed prices, reliability guarantees, you know,
11 payments for replacement costs, then everybody's got to do
12 it. There can be no exceptions.

13 Fourth, you've got to have equal access to
14 transmission assessments. I've talked about network
15 resources. We find that there is not a lot of
16 comparability.

17 I used to think that network resource status
18 could be defined pretty readily, but that's not the case.
19 We're seeing out there that there's lots of flexibility.

20 Sometimes some parties are given network resource
21 status, but it involves redispatch. Sometimes they are
22 given network resource status, but it involves an operating
23 guide, meaning you're a network resource, but if you don't
24 show up for these five hours, that's okay.

25 Sometimes we're beginning to see a utility say,

1 well, I have network resource for that power plant, but I'm
2 going to transfer it to another power plant. So there's
3 lots going on.

4 Whatever that utility buyer does for its own
5 affiliates, it must do for others, so that transmission
6 assessment has to be in there. And I know that there are
7 five, and I'm thinking of the fifth one.

8 By the way, everything I'm saying is in this
9 little pamphlet that you can get at bostonpacific.com for
10 free.

11 (Pause.)

12 MR. ROACH: Well, the fifth one is escaping me
13 right now, but I think those -- I'll add what is a sixth,
14 and maybe the fifth will come to me as I --

15 MR. PEDERSON: Let me ask a followup question.
16 Maybe you said this and I just missed it.

17 Referring to the independent monitor, who pays
18 that monitor? How is the compensation set and who pays?

19 MR. ROACH: You can do it any way. In Maryland,
20 we work for the Commission, but we're paid for by the
21 utilities. In Arizona, the monitor worked for the
22 Commission, the Commission staff, but was paid for by bid
23 fees.

24 MR. HILKE: Let me mention one other thing here.
25 Another comparable institution is sort of the arbitrator

1 groupings and various forms of certification and payment
2 systems that are used in that context. They are also
3 relevant to this type of concern.

4 MR. REITER: If I could, I just wanted to raise
5 one cautionary note about the collaborative process. I
6 don't disagree with Craig's suggestion about the importance
7 of that process, introducing consensus, but I think there's
8 a significant difference between producing consensus and
9 producing a neutral outcome.

10 And in my written comments, I made note that one
11 example that came to my mind was in Ohio where the utility
12 had, in the restructuring process -- and customers agreed
13 that it would be able to recover something like \$7 or \$8
14 billion in stranded costs, but half a billion dollars of
15 that would be put at risk, nominally, if within five years,
16 it wasn't able to achieve a switchover of 20 percent of its
17 customers to competitive suppliers.

18 The idea, in theory, was, you know, that this
19 would help ensure a neutral approach by the utility to non-
20 affiliated suppliers, because it would have to make way for
21 them. But, in fact, the way the collaborative process
22 defined competitive suppliers, it included affiliates, so
23 the utility got credit for meeting the 20 percent switchover
24 target by including in those switches, shifts to its
25 affiliate.

1 To me, that struck me as hardly a neutral
2 outcome. They was, I'm sure, give-and-take in the consensus
3 process, but ultimately I think that even though the
4 Agency's decision ought to be informed by collaborative
5 processes, the ultimate decision to ensure neutrality has to
6 be made by a neutral party.

7 MS. TIGHE: Just to follow on that idea of a
8 safeguard or a provision that provided at least no incentive
9 or disincentive for abusing the affiliate relationship,
10 Harvey, could you and Craig and really the whole panel, tell
11 us about the solicitation that you have been involved in, or
12 the processes that you've been involved, whether affiliates
13 were allowed to participate and what particular feature
14 assured you or the Commission, the person who had the
15 oversight, that there had been fair dealing for all
16 participants? Harvey, if you want to start?

17 MR. REITER: I guess you will probably hear more
18 from Tom Welch later, but I know that in Maine, they don't
19 permit affiliates to participate in the bidding process.
20 And in Vermont, they have adopted a program called
21 Efficiency Vermont, dealing with distributed -- not
22 distributed, but demand management services.

23 Utilities were excluded from bidding to offer
24 demand management services because the state concluded that
25 they had an inherent conflict in performing those services

1 and in selling power.

2 And the state found that it got a sufficient
3 number of bids from those willing to offer the services.
4 Those bidders, in turn, had to agree to another condition,
5 and that was that if at any point, the state decided to
6 adopt a retail access program -- and they don't have one in
7 Vermont, which is the exception in New England -- but, if at
8 any point they did, then entities who were contract to
9 provide these services in the state, could not also sell
10 power through any marketing division.

11 They'd have to make a choice. Either they
12 participated in demand management services or they offered
13 power supply. Again, it comes back to whether there's a
14 sufficient market for competitive solicitations, absent the
15 affiliate. And I think that in many instances, there are.

16 MR. ROACH: Again, I think some of the things
17 we've already mentioned. A lot of the potential for abuse
18 is worked out through the collaborative process, again,
19 product design, transmission, and evaluation criteria.

20 If those can be addressed up front, the
21 opportunities for abuse can be limited. Now, in the case of
22 Maryland, and, I believe, New Jersey, in that design, they
23 came up with a solicitation so that the evaluation was price
24 only, and that is very strong structural defense against
25 abuse because it's literally on bid day, just a comparison

1 of the prices.

2 So, driving towards price-only or price-mostly
3 bids through the collaborative process, is a good step.

4 Again, the independent monitor, having an
5 independent monitor that really can go toe-to-toe with a
6 utility buyer, I think is a good defense.

7 Beyond that, all the standards work, things like
8 codes of conduct. We'd run through every code of conduct,
9 we'd identify every point of contact, okay, on this issue.
10 Are you going to use corporate services on credit, for
11 example? Who was going to be the bid team? Do they have
12 any link to anyone in an affiliate who would bid?

13 Who would do the transmission? You'd just
14 literally run through all of those things. We've used
15 secure bid sites. We've gone to remote sites so that on bid
16 day, they are in remote sites, so there are a lot of common
17 sense things.

18 But, again, I think the collaborative process and
19 having the IM, goes a long way to creating a credible bid
20 and to combatting abuse by any party, really, not just the
21 affiliate.

22 MR. COMER: What I'm struck by, listening to
23 these questions and the answers to these questions, is that
24 there is incredible involvement from the states, and I think
25 that's good.

1 And there's clearly variety among the states. I
2 mean, when you look to New England and New Jersey and
3 Maryland, those are bidding situations in states with
4 greater degrees of retail competition and more liquid
5 markets. And those are different situations than you might
6 find in Arizona.

7 But I think what you're hearing here is that
8 there is a lot of involvement of the states, and, again, I
9 would encourage the Commission to have a collaborative with
10 the state commissions and hear their perspective about this
11 and share best practices and good practices.

12 I think the price-only auction in New Jersey may
13 not be a model for other portions of the country. I believe
14 the New Jersey ones are relatively small and relatively
15 shorter-term, but it would be useful to understand the
16 difference in the nature of the auctions and what purposes
17 they're supposed to serve.

18 MS. TIGHE: Thank you.

19 MR. WALTER: I agree with Ed, that I think the
20 state commissions obviously have been getting involved with
21 this, but I just look at the end results of a lot of these
22 where affiliates have been involved, because without an
23 independent monitor in an non-RTO situation, cross-
24 subsidization has gone on, preferential access has been
25 provided to the affiliate, replacement power alternatives

1 have been available to an affiliate and not to an
2 independent bidder.

3 And so the facts of the matter are that in spite
4 of the fact that these commissions have gotten involved,
5 these other aspects of preferential treatment have gone on
6 and will continue to go on without some competitive
7 procurement standards and guidelines that you all could put
8 together.

9 So I think that I would agree with Craig very
10 much, that having an independent entity looking at this
11 whole process to make sure everybody is treated fairly, is a
12 really critical part of it.

13 MR. PEDERSON: We have time for one more
14 question. Dave?

15 MR. PERLMAN: I guess that yesterday we had a
16 market-based rates conference and we talked about this topic
17 a little bit, and there was a FERC-oriented component of
18 that that's different than the state issues. And I'm
19 curious about each person's view on that.

20 It really just came up in the conversation with
21 Julie Simon of EPSA, and it was, if we have procurement of
22 long-term capital assets that effectively reintegrates by
23 contract, where the utility has control over a generator,
24 does that create competitive issue or issues in that
25 particular sense of market-based rates?

1 So, should there be a FERC criteria that relates
2 to the impact on wholesale markets and wholesale competition
3 of the outcome of these procurements? For example, is there
4 25 percent of the resources still free to trade? Or, can it
5 still be dispatched by the non-utility owner, or something
6 like that that we should keep in mind when we look at these
7 issues?

8 MR. ROACH: Just quickly, you know, I just want
9 to make the point again that your question sort of implies
10 that the wholesale market is the spot market. That
11 solicitation that was implicit in your question is as much a
12 wholesale market as the spot market and deserves as much
13 attention from state and federal commissions as the spot
14 market.

15 You know, my view, specifically on your question,
16 is that, yes, under -- if you sign a long-term PPA, under
17 Appendix A standards, that would be allocated to the
18 utility. But I would very much be willing to put that
19 aside, that issue aside, if that long-term contract was
20 competitively procured.

21 The competitive procurement is itself blocking
22 market power abuse for that wholesale market, for that big
23 transaction. So, I think that if the PPA is itself subject
24 to a market test, then I wouldn't allocate it to the
25 utility. I would say that that's been purged of market

1 power.

2 MR. PEDERSON: We're going to take one more
3 question. Sebastian?

4 MR. TIGER: I have a question for Mr. Comer. You
5 had mentioned that the Edgar standard was sufficient as it
6 exists today in regards to solicitations, but you made
7 another argument that utilities have to look at buying
8 distressed assets as another option to signing PPAs.

9 I was wondering whether that would suggest that
10 in evaluating solicitations, whether it was necessary to
11 look at the buy-first/build option -- buy/build versus PPA
12 option, and if you are doing that, as you noted, there are
13 distressed assets.

14 Do you have to look at why those assets are
15 distressed before allowing for that other option?

16 MR. COMER: Well, two things: One, when I say
17 the Edgar standard was sufficient, I did point out, I think,
18 that the Edgar standard needs to be supplemented by looking
19 very closely and giving deference to state determinations.

20 Where states are, as you have heard, we're
21 conducting, reviewing and being very involved in the
22 solicitations. In terms of -- are you saying apply Edgar to
23 the purchase option, you're really saying it's the lowest of
24 cost or market.

25 I think if there is an affiliate transaction and

1 you're purchasing it, you do want to have a sense that the -
2 - it puts you in a very funny position, and if the market is
3 lower than a cost-based rate, then the solicitation process
4 might give you better information.

5 MR. PEDERSON: I want to thank the panelists this
6 morning. I think we had a very good discussion. I hate to
7 cut it off at this point, but I think we need to --

8 CHAIRMAN WOOD: Jerry, hold on. We're going to
9 override you for just a second.

10 (Laughter.)

11 MR. PEDERSON: I'm sorry.

12 COMMISSIONER KELLIHER: I had one question: A
13 lot of the discussion this morning has been on how to make a
14 formal solicitation work, how to make it work well.

15 But Ed pointed out that Edgar provided three
16 means for a utility to prove the absence of abuse and self-
17 dealing, and I wanted ask -- Ed's position is clear. Ed
18 thinks all three means should be retained, but I wanted to
19 ask the other panelists, do you agree that we should
20 maintain all three means, or should we require a formal
21 solicitation process? Should there be only one means?

22 MR. WALTER: I think we should require a
23 competitive procurement process as a way to get to a
24 fullness of market consideration, instead of just using this
25 benchmarking, so I think it ought to be focused on

1 competitive procurement.

2 MR. REITER: I would agree. I think my concern
3 with the other two options, looking at benchmark purchases
4 and benchmark sales, involves quite a subjective judgment
5 about what constitutes a contemporaneous transaction or what
6 constitutes a similar type of sale, service, or product.

7 It opens up the process, I think, for potential
8 evasion and abuse. I mean, it's a second-best solution. I
9 think the Commission has applied it in judging affiliate
10 sales in the gas industry, historically, where there was a
11 pretty thin market, looking at only certain identical
12 transactions, but it is, I think, an inferior choice to a
13 competitive bidding process, and as I mentioned before, I
14 think it's inferior to a more structural solution.

15 MR. ROACH: I would agree that you should at
16 least have a preference for competitive solicitations, and,
17 just as a practical point, it's very hard to go out, and, as
18 Edgar requires, get comparable benchmarks and comparable
19 sales to others.

20 The best way to assure comparability is through
21 the solicitation.

22 MR. HILKE: As I mentioned in my opening remarks,
23 there are these other systems for finding comparables and
24 then are -- if you've got a common type of transaction,
25 there are econometric methods to look at the equivalency

1 question. So, yes, I would divide it into very, very common
2 types of transactions for which you probably can establish
3 ready benchmarks, versus more esoteric ones in which there
4 is so much art involved in it that you might not want to go
5 there.

6 I guess I'm most comfortable with the idea that
7 you have a preference for the competitive bidding situation,
8 but, again, you usually look at these things in a
9 cost/benefit framework. If it turns out that the costs of
10 that type of arrangement are, you know, astronomically high
11 compared to the others, and you can get these ready
12 benchmarks, then maybe you don't need to go that far.

13 MR. COMER: Commissioner, if I could clarify? I
14 don't know if you were here when I first spoke, but I did
15 say that the competitive solicitation process probably makes
16 more sense in the longer-term, more complex kinds of
17 transactions.

18 But if you have a short-term transactions and a
19 liquid market, I think the other elements of Edgar make
20 perfect sense. I mean, if you're doing a day-ahead
21 transaction in PJM, you don't need a competitive
22 solicitation, you have to buy from an affiliate.

23 COMMISSIONER KELLIHER: Thank you very much.

24 CHAIRMAN WOOD: Where is the line drawn? Is it a
25 year? I mean, we like bright lines because we've got put

1 stuff in boxes and run it through chutes, once it gets to
2 the door here, and these guys do all the hard work on it.
3 Contract of a year or longer, two years or longer, 90 days
4 or longer?

5 MR. COMER: I think you need to look at the
6 market and see what's commercially available out there. I
7 think you need to talk to the states and see what's out
8 there, as well.

9 A year is a reasonable benchmark, but that may
10 vary from market to market.

11 CHAIRMAN WOOD: Speaking of the states, my
12 question was, based on your collective experience -- and I
13 think that Ed has a good recommendation to continue that
14 dialogue, although we have the very erudite Chairman Welch
15 on the next panel, I know there are other states that are
16 dealing with different versions of solicitation. What would
17 be a good wish list for your dream panel to get a good cross
18 section of, I guess, best practices at the state level, that
19 we should discuss this with?

20 MR. ROACH: I depends on how you define "wish
21 list," but right now, for example, Pennsylvania and, after
22 yesterday, I believe, Ohio and Illinois are considering this
23 issue and have done some considerable homework on the issue
24 through a series of technical conferences.

25 I know, Mr. Chairman, you spoke at Illinois. I

1 spoke on that panel also, or later in the day.

2 So those three states, I think, are in the middle
3 of trying to decide. And they're tackling issues like,
4 should we look at the Maryland or New Jersey type of
5 process, or should we be at a process that looks more at
6 asset-backed unit-contingent? So, they're at least really
7 interested in these issues. It's very important for them
8 and they will be making decisions.

9 They might be good folks to have on this. I
10 think that beyond that, I thought the Arizona staff did a
11 great job, and they had a good, independent monitor, so they
12 might be someone, too.

13 MR. REITER: I guess I probably have some bias
14 with respect to my own clients, but certainly you'll be
15 hearing from Tom later, again, and I think Vermont has
16 looked at some structural issues in this process, and I
17 think you would get some good information from them.

18 I know that the State of Michigan has looked at
19 competitive solicitations and is developing sets of rules,
20 non-structural approaches with which they have had some
21 considerable experience, and I think that Bob Nelson would
22 probably be someone who would be interested in talking on
23 the subject.

24 MR. COMER: I would think you would want a mix of
25 states, certainly. Some have retail competition and more

1 liquid markets, but I think you also want a number of states
2 in the South and West that have more traditional structure,
3 because the issues they face may be a little different.

4 And I don't know that I would limit it to --
5 obviously, you want those that have the best practices, but
6 I think part of the usefulness of the session would be to
7 help educate state commissions about what their colleagues
8 are doing, as well.

9 MR. WALTER: I was just going to say that I agree
10 with Craig. I think some of the best processes we've seen
11 are developing in Maryland and Pennsylvania and in areas
12 like that. Beyond that, I do believe that Texas is working
13 well. It's a little different situation there, of course,
14 but I'd like to obviously export that from Maryland and
15 Pennsylvania and other areas.

16 I know that California has tried to take this
17 subject up, but they have a bit of a distance to go yet.

18 MR. PEDERSON: I'd like to thank this panel
19 again. Let's take a short, ten-minute break, and we'll
20 begin again at 10:50.

21 (Recess.)

22 22

23 23

24 24

25 25

1 MR. PEDERSON: Okay, we'll continue the
2 discussion from the earlier session, and I think we'll
3 proceed in the same manner. I'll ask each of the panelists,
4 in turn, to give a five- to six-minute presentation,
5 followed by questions and discussions. I'll ask that you
6 keep your comments within that five- to six-minute period.

7 And, with that, I would like to introduce Mr. Tom
8 Welch, Chairman of the Maine Public Utilities Commission.
9 Chairman Welch?

10 MR. WELCH: Thank you. I appreciate the
11 opportunity to be here. My comments are going to focus on
12 what I think is Maine's very successful experience with
13 obtaining or default supply, what we call standard offer.

14 But I think that even though the particular
15 product that we're seeking is a relatively limited one,
16 there may be useful lessons to be learned from what we've
17 done there in whatever procurement, whether it's a long-term
18 procurement for supply adequacy or some other purpose.

19 By way of background, Maine has a fully open
20 market. Any customer can enter into a bilateral contract
21 with a competitive electricity provider.

22 The T&D utilities were required to divest all
23 generation and have severely limited rights to market
24 energy. The T&D utilities have no load-serving obligation
25 and no prices for energy for any customer or set

1 administratively.

2 The customers who do not choose to enter the
3 bilateral market are served by the standard offer, and I'm
4 going to describe the process by which we obtain it, and
5 that's actually obtained by the Main Public Utilities
6 Commission itself through an open bid process.

7 I'll also note -- and I think this is a
8 precondition for the kind of process we have, that we are a
9 part of a robust market, the New England ISO, soon to be, I
10 hope, the New England RTO, which provides, I think, the
11 necessary competitive vigor and transparency that is really
12 essential, in our view, for any effective competitive
13 solicitation.

14 And I'll answer the questions more or less in
15 sequence. Our procurement is done by the competitive
16 solicitation. We issue an RFP outlining the
17 responsibilities of the winning bidder.

18 The selection process obviously has to be as
19 transparent as possible, either administered or supervised
20 by a disinterested party, for example, the State Commission.
21 The particular features of the solicitation process used in
22 Maine to obtain the standard offer of service, which is a
23 default, all-residual requirement service, load-following
24 service, is that we ask for bids by customer class, divided
25 into residential, medium-sized and large customers.

1 The bids are either for the entire residual load
2 within the class, that is, whatever the loads is, net of the
3 people in the bilateral market, or for 20 percent increments
4 of that entire load, whatever that happens to be. Following
5 the RFP, we take indicative bids and negotiate -- the PUC
6 itself negotiates the non-price terms such as security for
7 performance.

8 Final bids are requested, and then the selection
9 of the winning bidder actually takes place within three or
10 four hours of the final submission of the bid. We do it on
11 the same day.

12 The product solicited depends upon the customer
13 class. For customers with larger loads, the medium and
14 large customer classes, we seek bids for six months to a
15 year, with the intent of having that price follow the market
16 reasonably closely.

17 For residential customers, the bids are from one
18 to three years. We try to time the market a little bit, not
19 always successfully, and the prices are fixed throughout the
20 period.

21 In all cases, the obligation is for the entire
22 load, which is to say the supplier takes all the load risk.
23 The Maine Legislature has recently asked the PUC to consider
24 whether we should include asset-backed contracts with
25 suppliers with renewable energy as part of the solicitation,

1 and we haven't yet made a final determination on that.

2 Price is the most important selection element.
3 It really dominates all the others, but the strength of
4 security is vital.

5 There was a comment this morning that you could
6 rely upon the strength of the ISO as security for
7 performance. You might be able to rely on it to keep the
8 lights on; you certainly cannot rely on it for price,
9 because if the price rises in the spot market, the security
10 questions become intensely interesting, and we've had some
11 experience with that.

12 The affiliate of the T&D companies -- the T&D
13 companies are permitted to have marketing affiliates. They
14 can't own the generation, but they can market the product.

15 They actually are permitted to participate in the
16 bidding, but they are restricted by statute to providing no
17 more than 30 percent of the standard offer load within their
18 own territories.

19 As a practical matter, both because of our rules
20 against the T&D companies owning generation, and because we
21 have extraordinarily strict structural separation and codes
22 of conduct rules, none of the T&D companies have chosen to
23 market or to bid in our standard offer solicitation.

24 The regulatory oversight is direct. We actually
25 conduct the auction. We don't use any further independent

1 observer.

2 We did have some early cases where we permitted
3 the T&D utilities to conduct the auction because we didn't
4 get enough bids in the early days of our market to get the
5 procurement, and we had essentially hour-to-hour oversight
6 over their activity. Every decision they made was directly
7 reviewed by us.

8 There are no negotiations after the selection of
9 the winning bidder. The contract has to be in a form agreed
10 to by the PUC and the bidder, before the final bids are
11 submitted.

12 We generally release the RFP about two months
13 before the date for selecting the final bid, and there is a
14 period of time when the staff will answer questions about
15 the bids. We ask for indicative bids, and once we have a
16 short list, we'll negotiate more intensely with those to get
17 particular terms, and the security terms tend to vary from
18 bidder to bidder, and some of the other terms do.

19 As I said, typically we get the final bids by
20 10:00 a.m. and decide by 1:00 p.m., who the winner is. The
21 reason -- we started our process by actually allowing six
22 weeks between the submission of bids and when we decided.

23 And in conversations with the bidders afterwards,
24 they indicated that that put them at too much market risk,
25 and we were paying a high premium, so they want to be able

1 to lock in their supply, almost immediately after they
2 submitted a bid, so it's an interesting but important
3 feature.

4 We use both formal and informal rulemaking
5 processes to develop the rules for the standard offer
6 solicitation. It's extremely useful to have an open process
7 for developing the solicitation process itself.

8 In the early years, we spent a lot of time
9 talking to bidders after the bid to see what we could do to
10 improve the process, and really that's how we learned that
11 we were costing our ratepayers money by having this six-week
12 window during which we could ponder which bid to accept.

13 That has, frankly, driven us to depend almost
14 entirely on price in selecting it. We assume the other
15 things have a minimum threshold, and once those are met,
16 price is what determines the winner.

17 It is vital, in my view, to ensure that there is
18 no incentive or ability to favor one bidder over another.
19 Significantly, the bidders have told the Maine PUC that they
20 find our process to be the best or among the best in the
21 country, precisely because they do not fear that the T&D
22 utility can give preference to its own, for the simple
23 reason that the T&D utility has no role whatever in the
24 selection, and, for the most part, does not even compete in
25 the standard offer.

1 In my view, full structural separation is the
2 minimum that is needed to avoid the prospect and perhaps the
3 reality of discrimination, and I have a strong preference
4 for full divestiture with no participation at all by T&D
5 utilities.

6 One reason for -- my view has actually been
7 hardened because we did have one circumstance where the T&D
8 utility was marketing its own affiliate's product within its
9 own territory, and we were almost immediately confronted
10 with a bloody, inconclusive, and fact-intensive case about
11 whether or not the T&D utility was sharing important
12 information with its affiliate, so in the one case where the
13 T&D utility was active, we had precisely the case that we
14 feared. It was very difficult to resolve, and the end
15 result was that they have gotten out of the market.

16 Contrary to concerns raised by utilities prior to
17 the passage of Maine's restructuring law, we have found no
18 dearth of people interested in bidding for the Maine
19 standard offer supply.

20 To the extent that monopsony power is used to
21 favor an affiliate, that prospect alone will dampen bidding
22 interest. Frankly, we have been criticized by those selling
23 in the bilateral market, that the prices we obtain in the
24 standard offer solicitation are too low, because there is no
25 customer acquisition costs, but, frankly, our current view

1 is that the load risk undertaken by the standard offer
2 supplier, acts as a sufficient counterweight.

3 I think the Commission, the Federal Commission,
4 should ensure that a fully disinterested party, perhaps as
5 the Maine PUC, actually conduct the bidding process and make
6 the award, and the same disinterested party should have the
7 final say on the bidding process itself, after full
8 consultation with all interested parties.

9 If the state commission is unwilling or unable to
10 perform the role, any monitor or bidding administrator
11 should be at least as independent as the independent market
12 monitor of the New England ISO or New England RTO; that is,
13 the monitor must have no financial interest of any kind in
14 the particular outcome of the bid process.

15 The selection should be approved by at least the
16 relevant state regulators, and the monitor should have
17 reporting responsibilities to the same. As for best
18 practices, frankly, I think Maine is a best practice, and I
19 encourage people to look at it, and we'll obviously be
20 pleased to continue to work with the Commission. Thank you.

21 MR. PEDERSON: Thank you, Chairman Welch. Our
22 next panelist is Betsy Benson, Principal of Energy
23 Associates, and independent monitor of a number of
24 solicitation processes, including CLECO. Betsy?

25 MS. BENSON: Thank you very much. I'm going to

1 speak principally this morning about the experience in
2 Louisiana and being an independent monitor, because I think
3 that's probably the issue about which people are most
4 interested.

5 In Louisiana, there is no retail access, and the
6 independent monitor works in a situation where there is a
7 market-based mechanism required by the Louisiana Public
8 Service Commission, which requires bidding for all long-term
9 bids, and, in general terms, that means everything over a
10 year, although, of course, there are some exceptions to
11 that, and we can go into that later, if you are interested.

12 The independent monitor's responsibilities -- let
13 me speak first to how the independent monitor reports. As
14 the independent monitor, I am recommended by the company to
15 the Commission. The Commission has the right to either
16 accept or reject, in other words, to say we accept this
17 individual or you need to go back and get somebody else.

18 But the feeling in Louisiana is that the utility,
19 because of the close working relationship that would be
20 existent between the independent monitor and the utility,
21 should have somebody who would work well with the utility.
22 However, I do report, not the utility; I do report to the
23 Commission, and, in fact, work very closely with the
24 Commission staff. I also work very closely with the
25 utility.

1 Let me talk a little bit about the market-based
2 mechanism requirements, because, in fact, it is a highly
3 collaborative process, and that has been described here this
4 morning, although I think some of the issues that were
5 discussed this morning were really within states that do
6 have retail access, and this is a state that does not. So,
7 again, I think it provides another perhaps interesting
8 model, because, obviously, there are many states which have
9 not gone to retail access and are looking for long-term
10 bids.

11 There are competitive bid solicitations required
12 for, as I mentioned, for virtually every term of long-term
13 power supply. My responsibilities involve making sure that
14 there's no undue preference towards affiliate bids, but also
15 self-billed and self-supplied bids, which are often -- which
16 are usually factors in these solicitations.

17 The collaboration process itself is the process
18 of the utilities are required to submit forecast
19 information, essentially information to justify why it is
20 that they need more capacity, to provide information on
21 their existing resources, to provide information on their
22 self-billed options, if any; to provide an extensive RFP
23 draft for the market.

24 And then there is the process of collaboration,
25 which includes one or more technical and bidders'

1 conferences. That is an informal, non-litigated process,
2 but is conducted by the Louisiana Public Service Commission
3 staff in that context.

4 I do want to say one thing about the
5 collaborative process. Just as an interesting thing,
6 obviously it is as good as those who are asked to
7 collaborate make it. And I would say that there are many
8 bidders, many of whom are represented by independent power
9 producers who have already appeared here today, who do
10 participate in that process, and, I believe, have taken
11 seriously, their responsibility to comment during this
12 process, the process really being to try to make the RFP
13 better, the procedures better, the procedures more
14 transparent.

15 I would also tell you that I spoke just the other
16 day with a bidder who called me about a transmission issue
17 and who commented that, well, he usually liked to wait until
18 the final came out, before he paid much attention to it.
19 And I said, well, I think that's certainly your right to do
20 that, but the whole point of the collaboration process is to
21 have you have an opportunity to influence the way the
22 solicitation comes out.

23 So, what he chooses to do or not do -- and I
24 should also mention, obviously, that we are right in the
25 midst of the collaboration process right now for the

1 particular RFP, which is seeking possibly up to 1800
2 megawatts for CLECO Power, so it's a solicitation of some
3 note.

4 There is a Phase II of the market-based
5 mechanism, and that, of course, is the fully-litigated
6 portion of a certification process at the point at which a
7 utility will present a capacity deal, but this first deal
8 really is a collaborative process.

9 My own background and experience is that I
10 believe very strongly in competitive solicitations, and, in
11 fact, this is the fifth very highly competitive, long-term
12 solicitation that I've been involved with, not all of which
13 have been in the Southeast, but, actually, two others of
14 which were in the Northeast and the Mid-Atlantic Regions.

15 So I believe very strongly in them. I also am
16 very well aware of the complexities associated with
17 virtually every long-term deal, and I should say that I
18 started doing my first one in 1996, and the market has
19 certainly changed a lot since then as well. The issues have
20 certainly become more complex in many, many ways.

21 As far as what I do -- and I think this is
22 perhaps useful, because it was commented on earlier this
23 morning -- I am, as I think was termed this morning, all
24 over this thing, this solicitation with, in this case, CLECO
25 Power.

1 One of the things that this and many other
2 utilities have are all sorts of internal complexities in
3 terms of shared services, and those things need to be carved
4 out, made to identify who can work on what, what employees
5 are designated, who has access to what information.

6 You need to have -- in some cases, you need to
7 actually carve people out from non-involvement, because they
8 either have access to information that is going to be
9 commercially sensitive, and, frankly, will or could
10 potentially advantage an affiliate or not.

11 Also in the case of this and many other
12 companies, obviously, employees get assigned from time to
13 time from utilities to affiliates. So we really have a
14 fairly extensive process of that. We also require people to
15 adhere to a very extensive code of conduct with respect to
16 the RFP, which is in addition to anything that they are also
17 required to do by other codes of conduct.

18 We have training in protocol and everyone needs
19 to sign a confidentiality agreement that indicates that he
20 or she will adhere to the requirements of the protocol. We
21 channel communication, and what I mean by that is that at
22 this point, the RFP is out for comment, and as of the date
23 that the RFP was submitted in a draft form, all
24 communication from any potential bidder has to be channeled
25 to a designated representative at CLECO Power or to me or to

1 the Louisiana Public Service Commission staff, as may be
2 appropriate.

3 And the reason that we do that is really to make
4 certain, as much as we possibly can, that we stop
5 discussions that are sidebar discussions that could well
6 disadvantage the solicitation.

7 So there are all sorts of additional procedures.
8 I would also say that in terms of the independent monitor's
9 scope, in addition to monitoring these things and making
10 sure that as the solicitation itself is developed, and if
11 it's administered, I am also responsible for handling the
12 bids when they actually come in and making certain that they
13 are handled by a very small number of people, making sure
14 that they are secure, making sure that they are redacted,
15 making sure that the evaluation that is set up is
16 independent, monitoring that evaluation.

17 If, in fact, there are affiliates involved in a
18 short list that would come after a final bid procedure, I
19 would be involved with the negotiations for those
20 affiliates. So it's really a pretty intense, hands-on kind
21 of activity.

22 That said, I am not myself evaluating things
23 separately. I mean, the company is, in fact, doing that,
24 and that's something that I'll be very happy to talk with
25 people about, if you wish to talk about the pros and cons of

1 that, because I do have some opinions about that.

2 I would say that in the end, a very strong effort
3 has been made and is being made, and I would also say that
4 the Louisiana Commission has actually reevaluated its
5 market-based mechanism within the last year, and took the
6 monitor position, which was a voluntary position a year ago,
7 and made it a requirement, and then put the procedures in
8 place that I just alluded to very briefly, in terms of
9 managing.

10 I would just like to stop my comments by simply
11 indicating and echoing what a lot of people have said here
12 today. I think that any sort of effort to sort of tease out
13 the jurisdictional complexities that exist between states
14 and the Federal Government in power supply, can best be
15 aided initially by a serious evaluation of the many
16 different ways in which the states approach competitive
17 solicitations.

18 You've heard some good examples today,
19 principally, I think, from states that are already involved
20 with retail access and go through competitive auctions.
21 That also has been indicated here, and is quite distinct
22 from long-term supply in states that have not done that.

23 Obviously, there are many other models, as well,
24 and many increasing -- or many other models and many
25 examples of what might be termed best practices, but I would

1 indicate that I think it would be a wise thing for the FERC
2 to try to look at these things very seriously and very
3 intensely, and I'll stop here.

4 MR. PEDERSON: Thank you. Our next panelist is
5 Ershel Redd, President of the Western Region of NRG Energy.

6 MR. REDD: Thank you, and thank you, Mr. Chairman
7 and Commissioner Kelliher and the Staff for allowing me to
8 come and speak about the wholesale power industry and also
9 the procurement practices that we see, particularly as it
10 relates to new development projects and current capacity.

11 This Commission and other Commissions that
12 preceded you, have begun the process of replacing regulatory
13 controls with competitive forces. That's a major win for
14 this economy and also for the consumers as they are saving
15 billions of dollars.

16 The process of disaggregating the vertically-
17 integrated utilities has to continue. We do regulate to
18 shift the burden of stranded costs from the ratepayers to
19 the consumers -- I mean, from the ratepayers to investors
20 and shareholders, and it's working.

21 By placing generation in the hands of
22 entrepreneurs, you've unleashed the competitive forces and
23 the innovation of a rational and competitive market.
24 Competitive investment in the wholesale power sector has
25 drastically reduced the effective cost of converting the Btu

1 of energy into electricity, and, again, consumers are the
2 beneficiaries and they are saving billions of dollars.

3 While the spark spreads are at unprecedented
4 level and consumers are saving those billions, there are
5 some unhealthy risks that are currently surfacing.
6 Investment risk in this business today is high. The capital
7 markets that I have spent a lot of time with over the last
8 two years, are telling me that before they invest additional
9 funds in this sector, they need some assurances that their
10 loans will be repaid.

11 Encouraging the execution of longer-tendered
12 power purchase agreements is one of the important steps the
13 Commission can take today to ensure that capital flows into
14 this sector, such that the development of a healthy and
15 robust competitive market continues.

16 However, more critical will be the longer-term
17 development of capacity markets such as what we see in New
18 York. Today, for example, the California market is
19 precariously perched on the edge of another major energy
20 capacity problem, reminiscent of that which occurred in
21 2000/2001.

22 New generation needs to be built in California,
23 and it must be built competitively, rather than by the
24 inefficient, vertically-integrated utilities that operate as
25 monopolies where costs to consumers are not considered.

1 To be competitively built, host utilities should
2 issue requests for proposals that meet the basic standards
3 of the competitive marketplace. FERC must establish the
4 baseline standards.

5 Those standards must establish a fair and level
6 playing field for all participants, open and transparent
7 processes, and ensure discriminatory practices are not
8 employed. The RFPs must carefully and articulate the
9 products and services that are required, define and
10 articulate the processes themselves, also define and
11 articulate the bid evaluation standards, including weights
12 applied to price and non-price components of the RFP.

13 They also need to define and articulate
14 deliverability standards, and they must use a third-party
15 entity to run the solicitation and to conduct the evaluation
16 process to prevent affiliate abuses.

17 The evaluation process must give priority to
18 contracts that provide the lowest cost, but fully burdened
19 or all-in cost of the energy to the load center, and that
20 also meet strict deliverability standards during those hours
21 where the energy is needed the most.

22 Let me warn the Commission that the problem you
23 identified in 1991 in the Edgar case, still exists, and I
24 quote, "Where traditional utility is buying from an
25 affiliate not subject to cost-of-service regulation, the

1 buyer has an incentive to favor its affiliate, even if the
2 affiliate is not the least-cost supplier, because the higher
3 profits can accrue to the seller's shareholders," unquote.

4 This problem is particularly acute today, where
5 there don't exist, workable and independently operated
6 capacity markets. So that is almost everywhere, except New
7 York.

8 Why does it continue to exist? Because the host
9 utilities that contract for generation from an affiliate,
10 can pass fixed costs along to retail ratepayers and they
11 dump the wholesale power on the market at variable cost,
12 thus suppressing rational market price signals.

13 In effect, the host utility and the affiliate
14 enjoy private capacity rights that are recovered through the
15 utility's retail rates, while other suppliers are left with
16 only variable cost compensation or no incentive to stay in
17 the business. This creates an unhealthy situation where
18 innovative and competitive market participants are forced
19 out of the business and the consumers are left at the
20 economic mercy of the utilities.

21 Without the proper application of the Edgar
22 principles, the above-described situation can be blatantly
23 discriminatory, and without workable capacity markets, even
24 PPAs that pass that Edgar test, will depress prices, asset
25 values in a competitive market and continue to reinforce

1 barriers to entry that exist.

2 Let me now leave you with two recommendations:
3 One is rather short-term and it is to maintain the momentum
4 of regulation that you so dutifully began, and the other is
5 the longer-term solution to sustain the growth and
6 sustainability of the wholesale power market in this
7 country.

8 First, you must employ the Edgar approach to
9 ensure transparent, objective, and fair PPA bidding
10 processes are established up front and that will ensure the
11 competitive wholesale market will continue to attract
12 capital that they need to remain in this business.

13 Second, you must continue to pursue your quest to
14 introduce independently managed and efficient capacity
15 markets in this country that will ensure the long-term
16 security of the power market in this country. Thank you for
17 your time, and I look forward to the question and answer
18 session.

19 MR. PEDERSON: Thank you, Mr. Redd. Our next
20 panelist is Ted Banasiewicz, who is Principal of USA Power,
21 a development and acquisition advisory firm. Mr.
22 Banasiewicz.

23 MR. BANASIEWICZ: Thank you and good morning. My
24 comments will focus on a recent experience that my company
25 has had with a utility solicitation. I will address many of

1 the issues on your agenda.

2 USA Power is a power plant development firm
3 founded in 1997. We select specific site locations where we
4 believe a competitive advantage exist, as well as a
5 significant demand for generation resources.

6 We obtain all of the permits and approvals
7 required to begin construction, and then bring in project-
8 specific partners for the financing, construction, and
9 operation phases of the project.

10 USA Power recently participated in an RFP by
11 Pacificorp, which solicited peaking and baseload power for
12 delivery into its Eastern Control Area, with the Mona
13 Switching Station near Salt Lake City being identified as
14 the most preferred delivery location.

15 USA Power had anticipated a significant shortfall
16 of generation resources in that area, and began developing
17 our Spring Canyon Energy Facility, two years before
18 Pacificorp announced its RFP. We had previously chosen a
19 site less than a mile from the Mona Switching Station and
20 selected a 500-megawatt configuration with the flexibility
21 to provide either peaking or baseload power.

22 We obtained all of the permits required to begin
23 construction, including the air permit, water permits, and
24 interconnection agreements, being first in the queue for
25 transmission rights. The RFP sought approximately 500

1 megawatts of peaking power and 500 megawatts of baseload
2 power, and our project as a perfect fit to meet Pacificorp's
3 needs as identified in the RFP.

4 Our bid partners in the Spring Canyon Energy
5 Project include Quips Corporation of Amarillo, Texas, which
6 provides operation and maintenance services and its parent,
7 Utility Engineering, a power plant design and construction
8 company. We also have an equity partner in the Energy
9 Investor Funds, which is a Boston-based equity fund that has
10 invested more than \$ 1 billion in power plant generation
11 infrastructure since its inception in 1987.

12 In response to Pacificorp's RFP, we bid a project
13 that had all aspects and risks of the development phase
14 complete and our partners were able to provide the
15 construction, operation, and all of the equity required for
16 financing.

17 It is a very strong team which was put together
18 specifically for the Pacificorp RFP. We felt we had to
19 provide a very credible, experienced, and creditworthy team,
20 in addition to bidding the very best project in terms of
21 technology, operational flexibility, cost, and schedule.

22 Several months before Pacificorp announced the
23 RFP, they had approached us in an attempt to purchase our
24 Spring Canyon Project, which at that point consisted of a
25 project site and various permits and approvals. We

1 negotiated with Pacificorp for several months and shared all
2 project-related information with them, including contracts
3 for site acquisition, water agreements, all permits,
4 including the technical aspects of the air permit, all
5 technical design work, and all plant performance
6 information.

7 Three days after reaching an agreement for
8 Pacificorp to purchase our project, Pacificorp informed us
9 that upper management would not approve the purchase, and
10 that an RFP would be issued shortly. Although disappointed
11 by that news, we were confident that our project would
12 prevail amongst the competition for the RFP.

13 We put our bid team together and prepared our
14 response. We submitted bids for both peaking and baseload
15 portions of the RFP, and were short-listed for both.

16 During our short-list discussions, we were
17 informed that Pacificorp had submitted a self-billed option
18 that was more than very similar to our project. In fact,
19 they had picked a project site only one half mile from ours,
20 selected the exact technical configuration as ours, selected
21 the exact same 13-mile gas pipeline route, and they had
22 offered to purchase water at the exact same price that we
23 had spent months negotiating.

24 In every way, the Pacificorp bid was an exact
25 clone of the Spring Canyon Energy bid, despite the fact that

1 we had a valid confidentiality agreement in place which
2 prevented Pacificorp from utilizing our information for
3 anything but evaluating the purchase of our Spring Canyon
4 Energy Project.

5 Needless to say, we were astonished to learn of
6 these facts. Finally, Pacificorp announced that their self-
7 billed option was the winner because it provided the lowest-
8 risk and lowest-cost alternative to the ratepayers, and that
9 they would be seeking a Certificate of Convenience and Need
10 from the Utah Public Service Commission, which was required
11 to begin construction.

12 We initially intervened in the CCN process, not
13 because we felt that Pacificorp had violated our
14 confidentiality agreement, but because they stated that
15 their project was lower risk and lower cost. At that time,
16 we had a thorough understanding of their risk, however, we
17 did not have a thorough understanding of their cost.

18 They did not have an permits or approvals
19 required to begin construction, no air permit, no water
20 permits, and their application for these permits were being
21 fiercely challenged. We intervened because Pacificorp, in
22 its bid evaluation process, gave no credit to projects that
23 had secured permits, versus what they called virtual
24 projects such as their self-billed option.

25 It wasn't until well into the intervention

1 process that we learned just how far Pacificorp was willing
2 to manipulate the process to ensure that they won. Today,
3 I will give you just a few examples of their many ways.

4 MR. PEDERSON: Mr. Banasiewicz, I apologize for
5 interrupting you, but if we can wrap up, so we can get to
6 questions and answers?

7 MR. BANASIEWICZ: Absolutely.

8 Through the intervention process, we were able to
9 obtain the economic models that Pacificorp used to evaluate
10 its self-billed option and our Spring Canyon Energy Project.
11 We found two very different models.

12 These models were overly complicated and were
13 several hundred pages long. Models that we use to evaluate
14 projects are about 30 pages long. Models our partners use
15 are about 50 pages long. We had never seen models that were
16 several hundred pages long.

17 Our team spent many long days analyzing the
18 models, and we were astonished at the results of our
19 analysis. First, we found that models were conceptually
20 inappropriate.

21 Instead of looking at each alternative to
22 determine which provided the lowest cost, these models
23 calculated which alternatives make the most money by
24 including a revenue component. You would think that two
25 identical facilities, in an identical locatio, would have

1 the same revenue. Not when Pacificorp does the evaluation.

2 2

3 The two models used different pricing, and, to
4 compound the problem, Pacificorp elected to operate its
5 self-build option, 24 hours per day, whereas they elected to
6 operate our project for 16 hours a day.

7 Further compounding the problem, Pacificorp
8 evaluated its self-build option over a 38-year period,
9 versus limiting our economic evaluation to 20 years. The
10 RFP limited all bidders to 20 years, yet Pacificorp allowed
11 its self-build option the benefit of an additional 18 years.

12 The result of all of this is that even though the
13 two projects are identical, the Pacificorp self-build option
14 had more than double the revenue of our Spring Canyon
15 Project. This result is clearly absurd, especially when
16 revenue should not be a component of the RFP evaluation.

17 Digging further into the models, we discovered
18 that Pacificorp used incorrect values for the megawatt
19 output of our facility, incorrect values for the
20 availability, incorrect values for the heat rate, for the
21 capacity charge, and for the cost of operations and
22 maintenance.

23 Most troubling is that we never had an
24 opportunity to verify the actual inputs used in the
25 evaluation of our project, prior to them announcing

1 themselves as the winner. It was only because of the
2 intervention process that we were able to see these
3 manipulations.

4 We were able to deliver our project at a lower
5 cost than Pacificorp and we were willing to guarantee the
6 cost of the facility, the output, the heat rate,
7 availability, and the emissions. Pacificorp was unwilling
8 to guarantee any of these.

9 We had all the permits, yet they boldly claimed
10 that their project provided lower risk to the ratepayers.
11 That brings me to the world of the independent consultant,
12 which in this case was Navigant Consulting.

13 During the intervention process, we obtained
14 several e-mails which Navigant sent to Pacificorp, offering
15 instruction on how to make their self-build option score
16 better in the evaluation process. Navigant did not offer
17 this type of advice to us or any of the other bidders.

18 Also, during the hearings before the Commission,
19 Navigant sat with Pacificorp and drafted many questions for
20 Pacificorp's lawyers to ask of various witnesses. The
21 independent consultant was anything but independent.

22 During the course of the proceedings, we
23 developed the ability to run Pacificorp's models and we
24 concluded that when we ran the models with the correct
25 inputs, we win and we win by a huge amount. Our bid

1 provided a lower-cost product than did Pacificorp's
2 proposal, yet when Pacificorp runs the models, they claim
3 they win by a huge amount.

4 This makes no sense, and adds credence to our
5 assertion that their models are flawed. Remember that these
6 are identical facilities in the identical location. One
7 would think that this would be like a NASCAR race where you
8 had two good drivers in similar cars with similar cars with
9 the same horsepower, and after 500 miles, one wins by two-
10 tenths of a second.

11 However, in this race, Pacificorp, according to
12 their testimony before the Commission, would have you
13 believe that our Spring Canyon facility is four and one half
14 times less economical than their facility. Not only does
15 this not pass the common sense test, but it begs the
16 question of how do these models tell the public that the
17 process is honest and believable?

18 I have identified a few concerns with the
19 process. In my opinion, it was a disingenuous effort by
20 Pacificorp to manipulate the evaluation to ensure that their
21 self-build option would win.

22 We presented all of this to the Utah Public
23 Service Commission in seven day of hearings. The result of
24 those hearings was that Pacificorp was awarded the CCN that
25 it had requested, even though two independent consultants

1 hired by the ratepayer advocates also concluded that the
2 Pacificorp bid evaluation process was seriously flawed, was
3 skewed in favor of Pacificorp's self-build option, and could
4 not be relied upon to determine the lowest cost option.

5 Only the Division of Public Utilities concluded
6 otherwise, and they, by their own admission, did not do a
7 substantive analysis of its own, but, rather, relied on
8 Navigant Consulting.

9 We believe that the Utah Public Service
10 Commission and its staff are not in a position to be able to
11 evaluate economic models that are several hundred pages
12 long. And while they appeared interested and generally
13 concerned to do the right thing, they are not well versed in
14 the technical aspects of power plant operation and did not
15 grasp the importance of such mistakes.

16 To compound the problem, Pacificorp played the
17 blackout blackmail card very well. They claimed that
18 blackouts would occur if the Commission did not grant the
19 CCN. With Pacificorp and us claiming to be right, and with
20 the Commission under pressure to avoid blackouts and unable
21 to determine who was actually right, the Commission felt it
22 did not have any alternative but to issue a CCN.

23 Unless the Commission has a truly qualified and
24 truly independent evaluator reporting to it, rather than to
25 the utility, the utility can pull the wool over the

1 Commission's eyes every time.

2 In conclusion, I recently heard a politician
3 describe the U.S. foreign policy as the U.S. thinking it's a
4 hammer and all of its problems are nails. When I heard
5 this, I immediately thought of Pacificorp.

6 Unless the FERC gets involved, Pacificorp will
7 continue to believe itself to be the hammer, and all
8 independent power producers to be nails. I believe an
9 investigation by FERC regarding our allegation of
10 Pacificorp's behavior is most appropriate and necessary to
11 ensure the integrity of the RFP process in a regulated
12 environment. Thank you.

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1 MR. PEDERSON: Thank you, Mr. Banasiewicz. That
2 was some war story. We've heard a little bit about that
3 today, and I'd like to start the questioning.

4 If I could start with Mr. Redd, who mentioned in
5 his comments about the proper application of the Edgar
6 principles, which once we look into that a little more and
7 establish that a little more, that may help out on
8 situations like you just described.

9 So, Mr. Redd, can you discuss a little about --
10 when you mentioned proper application of Edgar principles,
11 can you expand on that? What is, in your opinion, the
12 proper application of that?

13 MR. REDD: I think one of my concerns is that the
14 Edgar principles ask the utility, particularly when they are
15 dealing with an affiliate, to do an ex post facto review
16 about whether or not there was any kind of discriminatory
17 practice.

18 That's kind of like sending the fox to the hen
19 house to gather the eggs. It just doesn't work.

20 I think that what you need to do is probably
21 establish even greater standards that you can affix to the
22 current Edgar standards that create a level playing field so
23 that you ensure that there aren't any discriminatory
24 practices; that the process is, as I had said, clearly
25 defined, the needs and resources are clearly articulated.

1 And then I think what you've got to do is
2 establish an independent monitor to -- or maybe an entity to
3 run the whole process and do the evaluation.

4 MR. PEDERSON: On the process itself -- and I'll
5 throw this out to the whole panel -- what do you envision
6 that process to be? We've heard collaborative process.
7 Specifically, if we were -- we look at filings, at least my
8 group does. What would that process -- what process should
9 we be looking at that is a collaborative process that would
10 work for everyone and avoid the kind of problems that we
11 might see out there?

12 MS. BENSON: Are you speaking about specifically,
13 what the Federal Energy Regulatory Commission would require
14 as a separate process, or in collaboration with state
15 commissions, or what?

16 MR. PEDERSON: In my mind, I guess, in
17 combination with the state process. What is the process
18 that will result in a fair and transparent RFP?

19 MS. BENSON: Well, you know, I will certainly
20 make a plug, not just for what Louisiana is attempting to
21 do, but what I see, having been involved in power
22 solicitations that have not been under any regulatory review
23 of the state because they initially involved municipal
24 utilities, which typically are not jurisdictional, but for
25 which it became very clear that in order to have the market

1 be as competitive as it needed to be, that everybody
2 participating in it, needed to feel that it was fair.

3 And in a regulated environment, that means that
4 they need to participate prior to, I believe, the
5 solicitation going live, if you will, in what that
6 solicitation is going to look like.

7 And I think there are examples. Arizona is
8 another one, and I think there are other examples around,
9 because there are many states that are trying variations on
10 this where the regulatory environments at the states has, in
11 fact, set up a formal, but non-litigated collaborative
12 process that simply says to people, these are the things
13 that you need to provide and these are the things that you
14 need to make transparent to the market, with appropriate
15 redaction of confidential information, of course, as
16 determined by the regulator.

17 And then rely upon the market, as I believe that
18 these gentlemen would indicate, to participate actively,
19 which was the point, of course, of my comments about the
20 gentleman that I spoke with the other day, who commented
21 that he would only wait until it was final, which, of
22 course, obviated his participation in a collaborative
23 process.

24 But that's his problem, and I think, to some
25 degree, that is, you know, a process step that independent

1 power producers who have been active in the market would see
2 as valuable. I think there are others of them that may not
3 see so, but in my view, it is trying to make that going-in
4 process as transparent as possible.

5 MR. WELCH: I think the critical feature is who
6 gets to make the final decision about what the process is
7 going to be, what the RFP is going to look like, and I think
8 it's absolutely critical that that -- that the person or the
9 entity that makes the final decision about the RFP, and who
10 makes the final decision about the winner, is a completely
11 disinterested party, perhaps, optimally, a commission, but
12 in any case, someone who has no ties of a financial variety
13 with any market participant.

14 I think that once you establish that, it will be
15 in the interest of that disinterested party, who,
16 presumably, has some public interest objective, to get as
17 much information from as many people as possible and will,
18 in the normal course of things, develop an appropriate
19 collaborative.

20 I think that if you think of a collaborative as
21 something where the parties must reach agreement among
22 themselves, that is a formula for failure. If you think of
23 a collaborative as something where the decisionmaker has an
24 appropriate opportunity to get all the information it needs,
25 that's a recipe for success.

1 So I think the focus ought to be on who actually
2 gets to make the decision and the financial links that that
3 particular entity might have.

4 MS. BENSON: And I just would comment that I
5 don't disagree with that, to the extent -- again, my
6 experience has been that at the end of the train, there is a
7 regulatory body that is legally responsible for making the
8 decision.

9 There are lots of side rails along that
10 particular train, but I certainly don't disagree with that.

11 MR. PERLMAN: Could you address the issue of
12 complexity that we heard about, where there is a regulatory
13 body that had to make the decision, but there is a
14 contention that the regulatory body wasn't adequately
15 sophisticated enough to wade through all these models and
16 make that kind of judgment, whereas, if they had been
17 involved in the process, as Mr. Welch seems to be saying,
18 and were making the decision, not as having something
19 presented to them, but as being part of a continuum of the
20 information flow and the structure going in, they would be
21 more efficient and effective in doing it.

22 That's what I hear him saying. Are you
23 disagreeing with that and saying that as long as there is a
24 regulator at the end of the line, that's good enough?

25 MS. BENSON: Obviously, I'm in no position to

1 comment upon the particular case that was described here
2 today, but if the facts as they are, there are regulators
3 and there are regulators. I mean, clearly these are very
4 complex decisions that have many working parts to them.

5 None of them, even in simple -- even simple ones
6 are not simple. So, obviously, there needs to be
7 individuals who are themselves fully capable of, as somebody
8 said this morning, going toe-to-toe.

9 And whether that is a combination of regulatory
10 staff or regulatory staff consultants, independent monitors,
11 but also there are clearly people who are actually running
12 these systems. In my view, to pull -- which is slightly
13 moving the bar on your question, but to take the
14 responsibility for evaluating a long-term power supply
15 proposal completely out of the hands of those who have
16 fiduciary responsibility for hundreds of millions and
17 billions of dollars, is not the solution, even though I
18 understand why those who feel that they have been badly
19 burned by the process feel so.

20 MR. GALLICK: If you don't evaluate or
21 participate in evaluating -- and I may not be using the
22 right words here -- if you don't evaluate the bids yourself,
23 how do you develop a confidence that the company is actually
24 doing it in a fair way?

25 MS. BENSON: I don't run the models, because I'm

1 not equipped to run them. You know, we all have our skills
2 and our talents, but I am not -- I don't know how to run
3 ProMod.

4 But I am not uninvolved in those particular -- I
5 understand how the models work, and I spend time with the
6 companies, understanding how those models work. In certain
7 instances in this particular case, the transmission
8 decisions are to some degree outside the immediate
9 decisionmaking of this particular company, because of the
10 way that particular area is configured.

11 As I'm sure you know, that particular company is
12 somewhat transmission-dependent on a larger not-to-be-named
13 company that --

14 MR. GALLICK: Oh, come on.

15 (Laughter.)

16 MS. BENSON: But that said, I mean, I mean I
17 wanted you to understand specifically, really, that I do not
18 -- I have to say I have participated in solicitations
19 previously where I was part of a small team of people who
20 basically did all the analyses and did all the evaluations.
21 We were employed by the utility, but we did them
22 independently.

23 And that model worked well, as well, but that
24 model is not this model, and I would say it just -- in this
25 case, I really am monitoring, but I do understand how these

1 models work, and I think I'm able to determine --

2 MR. GALLICK: Just as a followup, when you reach
3 -- I don't know if "disagreement" is the right word --

4 MS. BENSON: Could well be, yes.

5 MR. GALLICK: But if you really have a serious
6 issue, how do you go about resolving that?

7 MS. BENSON: Ultimately, I am charged ultimately
8 with making certain that any unresolved issue is made as
9 close to immediately, that the Public Service Commission
10 staff is aware that there's an unresolved issue.

11 I would say that in most cases, it has been
12 enough of an incentive to help us all reason wisely
13 together. But, again, you know, there are big issues and
14 then there are non-big issues, and, again, these are complex
15 things.

16 But, ultimately, I am charged with reporting any
17 unresolved issue immediately to staff, and if chooses,
18 obviously to the Commission.

19 MR. PEDERSON: Did you have a question?

20 MR. O'NEILL: Ms. Benson, would you care to
21 comment on what would have happened if you would have been
22 hired by Pacificorp?

23 (Laughter.)

24 MS. BENSON: A fair question?

25 (Laughter.)

1 MS. BENSON: Well, no, Utah is a lot drier than
2 it is here, and I -- truly, I mean, the way the process was
3 described here today, it sounds pretty horrific, but with no
4 one here to defend the other side, I'm in no position to
5 comment.

6 It seems as though there were a few process steps
7 possibly that they missed, and, you know, looking at a self-
8 build option as we do in Louisiana, I have learned that
9 self-build is potentially radioactive as affiliate issues as
10 well, so they need to be very, very carefully tended to as
11 well, for some of the reasons that were stated here today.

12 I'm sorry that that's really not an answer, but -
13 -

14 MR. O'NEILL: I only asked if you cared to. I
15 realize that --

16 MS. BENSON: Yeah, you're a bad guy.

17 (Laughter.)

18 MS. BENSON: And everybody knows it as well.

19 (Laughter.)

20 MR. BANASIEWICZ: When we prepare a bid response
21 to a solicitation, it takes the effort of several folks with
22 different types of backgrounds -- financial, technical,
23 transmission issues, and they all culminates into an
24 economic pro forma, if not a model that has a price attached
25 to it.

1 I would think that the independent evaluator --
2 and my biggest point is that it truly be independent and
3 truly be qualified. I don't see all of those talents
4 residing in one individual. I think the independent
5 evaluator is going to be a team approach that had that
6 combined talent.

7 MR. TIGER: If I may follow up with Ms. Benson,
8 maybe you could describe a little bit about the difference
9 in the way you would evaluate or how you do an evaluation
10 of self-build versus buy, buy through the PPA, essentially
11 It would seem that there are so many different variables
12 there that it would be hard to make it down to the price,
13 essentially, or the ultimate sort of -- how would you go
14 about trying to make sure that that's fair and reasonable,
15 ultimately, to the consumer, as opposed to, you know,
16 ultimately the shareholder of the utility.

17 MS. BENSON: Ultimately, really, my job is not
18 the shareholder; that's not my job. My job is the
19 ratepayer. So that -- I mean, in theory, that makes it all
20 crystal clear and simpler, but -- your question?

21 MR. TIGER: I guess that what I'm trying to get
22 at is, if you're trying to do some type of solicitation,
23 right, and there -- the variables are so different when you
24 consider the self-build versus PPA, you know, especially
25 when you -- unless you're giving, you know, some fixed price

1 to the ratepayer, I mean, most of the self-build, I would
2 imagine, are cost-plus.

3 There's no way it can be apples-to-apples, in
4 terms of comparison.

5 MS. BENSON: No.

6 MR. REDD: So, how do you -- how would you, as an
7 advisor, essentially to the ratepayers, be able to make
8 those apples to apples? If we were to be trying to figure
9 out whether a solicitation was a fair process, you know, to
10 evaluate a solicitation that has, you know, that huge
11 difference, how would you get there?

12 MS. BENSON: I mean, you know, essentially you're
13 asking the question, you know, all else equal, how do you --
14 you know, how do you evaluate something that a utility
15 wants to build itself, through something that -- and I
16 agree, it's difficult, and, to some degree, I'm going to
17 probably take -- give a very general answer and take a
18 specific pass, because this is a factor that existed in the
19 solicitation that I was involved with last year.

20 But it wasn't, frankly, a very serious self-
21 build option, so it really didn't end up showing in any
22 particular way. I think that that's less likely to be the
23 case this time.

24 I think that, again, it's -- you know, the
25 general terms are understanding how the numbers work, and,

1 you're right, there's a difference between a cost-based and
2 ultimately a rate-based model and something that's coming in
3 through the market.

4 In this particular instance, there are also
5 issues, again, related with being able to deliver, that are
6 real issues in this particular factor, but I have not, as I
7 sit in this part of the process, I have not yet looked at
8 any of the specific numbers in terms of the self-build, so
9 all I can say now is that it's an issue to which I am alert,
10 and I also know that the Commission staff is extremely -- is
11 very alert to.

12 And I believe that the company is, too,
13 increasingly. I think that they're -- this is -- this is,
14 I think, virgin territory for them, as well, to do this
15 within the context of a competitive solicitation. So that's
16 as good as I can do here this morning.

17 MR. TIGER: Mr. Redd, do you have any suggestions
18 as to how to -- how you would be able to show a sort of
19 counterfactual that if you were putting in a bid, or maybe
20 Mr. Banasiewicz as well, that it's even better, you know, in
21 that type of context, or do you have to wait?

22 I guess, ultimately, it comes back to post factor
23 litigation or that they made the wrong decision, which,
24 eventually, is not necessarily, from societal perspective,
25 the best way of getting there, I guess.

1 MR. REDD: Let me start out the comment by saying
2 that \$135 billion, by some estimates, is a legacy to that
3 utility monopoly model, and the regulators have regulated
4 them. I believe that a company like NRG or USA Power can
5 go head-to-head and be the utility any day, because we're
6 beholding to shareholders and we don't have a regulatory
7 cushion to fall back on.

8 I think if we leave the evaluation to an after-
9 the-fact evaluation, it's going to cost consumers a lot of
10 money. We've got to realize that, you know, the first thing
11 we need to start with is a well-defined and well-designed
12 market mechanism that has a good congestion management
13 system that is independently operated, where transmission
14 access and congestion are fairly priced and access is
15 equitable.

16 If you do that, then we can figure out exactly,
17 you know, where the ideal spot to put that plant is, and
18 then in terms of running the plant, we can run it a lot
19 cheaper, we can manage the risk a lot better.

20 So I think you've got to start out with a well
21 designed market. One of the problems that Betsy has is,
22 she's doing business down in Louisiana, and we have that
23 same problem.

24 (Laughter.)

25 MR. REDD: Bitterly, we --

1 MS. BENSON: It's very nice this time of year.

2 MR. REDD: I know, but we're sitting on a lot of
3 low-cost generation where we can't get transmission access
4 because that unnamed utility she was talking about wants to
5 dispatch a lot of units out of Merit, and it doesn't make
6 any sense. It's costing the ratepayers millions.

7 MS. BENSON: Can I just add one thing that maybe
8 is relevant? I mentioned the individual from the market who
9 chose not to comment during the collaborative period, there
10 have, however, been several potential bidders who are, I
11 think, specifically watching this self-build option, because
12 they see themselves as potentially competing against it, who
13 have chosen to comment quite actively on issues related to
14 concerns that they have that are somewhat along the lines
15 that you raised here.

16 And that's terrific, because they -- because they
17 clearly believe, similar -- I mean, they're clearly people
18 who are -- who need a sink in order to begin construction or
19 if they are in construction, I mean, they would like to have
20 some way to make their units pay.

21 And they have been quite specific in terms of
22 making it clear to all of us that they're looking very
23 closely at this particular aspect of it, not necessarily for
24 some of the reasons that you raised, but for some others
25 ones that have come up here today.

1 MR. BANASIEWICZ: Sebastian, one of your comments
2 about the utility bid may not be an apples-to-apples bid and
3 how do you deal with those differences, and from my
4 perspective, I don't know that they have to be different.

5 A utility typically does things on a cost-plus
6 basis, but I know of no reason that they couldn't do an EPC
7 contract, construction contract on a fixed cost basis, much
8 the way we do, and remove that risk in the same way that the
9 independent power producers have removed that risk.

10 But if they're not going to do it that way, then
11 at least the differences between the two of them need to be
12 identified and some independent process needs to evaluate
13 what is the potential for that risk to affect the ratepayer.

14 MR. O'NEILL: If I recall correctly, you said
15 that your project got downgraded because it was unreliable?

16 MR. BANASIEWICZ: I'm not sure what you're
17 saying.

18 MR. O'NEILL: I thought you said that it was
19 declared less reliable as part of the --

20 MR. REDD: Why was it turned down?

21 MR. BANASIEWICZ: The utility declared themselves
22 to be lower cost and a lower risk.

23 MR. O'NEILL: "Risk," meaning?

24 MR. BANASIEWICZ: We are still not sure what that
25 means. To me, that meant -- in previous occupations where I

1 worked for affiliates of utilities and was involved in
2 evaluating bids to determine which of them were legitimate
3 bids and which were not, that meant you have control of a
4 piece of property.

5 Do you have an air permit? Do you have water
6 permits? What is the reasonable chance that this project
7 will find its way to completion? And if you don't have a
8 site and you don't have an air permit and you don't have
9 water, in my view, that project presents a higher risk than
10 one that does have all of those.

11 MR. O'NEILL: So it was only a risk to
12 completion, not a risk in operation?

13 MR. BANASIEWICZ: Yes, that would be an accurate
14 statement.

15 MR. PERLMAN: Mr. Welch, I have a quick question
16 for you. I actually did participate in your process, and
17 was very impressed with the way it was run by the
18 Commission. My reaction was that because it was run by the
19 Commission, because it was open, because it had a lot of
20 opportunities for people to participate and feel like they
21 could succeed, you got a very competitive response.

22 And is that -- do you feel that the fact that you
23 have precluded the utilities from participating, pretty much
24 in most of the competitive types of activities in your
25 state, as I think I heard you say earlier, and you have run

1 this RFP process, has helped create a more robust
2 competitive response from the marketplace, and do you think
3 that if you hadn't, there would be less of a response?

4 MR. WELCH: Absolutely. In fact, one of the
5 critical components of the auction process is the exchange
6 of information between the utility about load and the
7 competitors. We've been told that that process runs more
8 smoothly in Maine than anywhere else, because the utility
9 has no incentive to conceal anything, and the bidders have
10 no reason to believe that the utility is concealing anything
11 for the benefit of their own affiliates.

12 So, I think the practical exclusion of the
13 affiliates from the process has been a very positive factor.
14 Now, granted, we're a small market, so we had to do more
15 than perhaps other people would have to do to attract
16 players, but typically we're get eight or ten big players
17 coming into our market, and all of them have indicated that
18 they're very happy with the fact that they don't feel as if
19 they have to be looking over their shoulder at possible
20 relationships between the T&D utility and its affiliate.

21 May I may a brief comment on one of the other
22 questions? It seems to me that if you -- that one of the
23 critical aspects, if you're dealing, for example, with a
24 long-term supply issue as opposed to the sort of things we
25 deal with in our bid, is defining a product which everyone

1 can offer.

2 And in a situation where you permit self-build by
3 a rate-regulated component of a utility, you've just
4 recreated PURPA. That is the description of PURPA.

5 You know, you figure out what that self-build is,
6 call it avoided cost, let people bid against, that's PURPA.
7 We had a very unhappy experience with PURPA in Maine, and it
8 actually went to the inability of regulators to figure out
9 what the self-build option cost. We missed by a factor of
10 ten.

11 That was not good. If you are going to believe
12 that you're going to get the benefits of competitive
13 solicitations, the products that everyone can offer,
14 including affiliates, if you let them into the market, have
15 to be identical, however you define that.

16 And you cannot have people operating under
17 different regimes in terms of cost recovery or in terms of
18 their ability to go out after money for the ratepayers,
19 without simply recreating something with which we had a
20 rather unhappy experience.

21 MR. PEDERSON: We have time for one more question
22 before we go to the audience. Dick?

23 MR. O'NEILL: I was just going to comment. I
24 don't think you were the only one that had that PURPA
25 experience.

1 MR. PEDERSON: Anything else?

2 (No response.)

3 MR. PEDERSON: At this point, I'd open it up to
4 the audience, if the audience has any questions, if anyone
5 has questions for the panel.

6 Please come forward, identify yourself and who
7 you represent.

8 MR. TAHLMAN: Thank you. My name is Mark
9 Tahlman. I work for Pacificorp. I'm Managing Director in
10 the regulated function, the commercial end of the business.
11 In fact, it's my responsibility to issue RFPs.

12 And I'd like to make some comments. I really
13 don't have any questions for the panel, but I do feel a need
14 to make some comments relative to the statements from the
15 gentleman from USA Power.

16 Certainly it is true that Pacificorp held an RFP
17 process, and it's also true that Navigant Consulting was our
18 independent evaluator that we chose. It's also true that
19 the Utah Public Service Commission thoroughly evaluated the
20 outcome of that RFP in a very detailed, arduous process, and
21 that I will just say that each and every assertion that the
22 gentleman from USA Power made today, was addressed by the
23 Utah Commission, and the Commission Order reflects their
24 opinion of his assertions.

25 It's all a matter of public record, and, in fact,

1 I have a copy of the Order with me. I'd be happy to make it
2 available to Staff.

3 The testimony that was filed during the
4 proceeding is also a matter of public record. It addresses
5 each and every assertion that Mr. Banasiewicz has made.

6 And I do feel a need to, I think, correct one
7 statement. Pacificorp never did agree to purchase their
8 project, in any way, shape or form, and there was no cloning
9 whatsoever that took place.

10 Now, as long as I have the microphone, I will
11 say, I think, in the context of today's proceeding, just to
12 help you understand the context of Pacificorp's solicitation
13 process, that no affiliates were allowed to bid on our
14 process, so they were barred from participation.

15 We did, as you know, retain an independent
16 consultant, Navigant Consulting. It was our desire to
17 retain a large nationally recognized firm. It was a blind
18 bid process where the consultant served as the communication
19 vehicle with the bidders, and the process itself was a
20 result of a collaborative process on the front end, that was
21 stipulated to between stakeholders and the Company and the
22 State of Utah.

23 Having said all of that, I will be here for the
24 balance of the day. Anybody that would like to have me e-
25 mail them the testimony and the Commission decision and the

1 Order, I'd be happy to do that, and I'd be happy to answer
2 any questions you might have.

3 MR. O'NEILL: Could you list the differences
4 between the project that won and the USA Power Project?

5 MR. TAHLMAN: Well, that's where life gets
6 blurry. The project that Mr. Banasiewicz refers to, that
7 was discussed for purchase, was not the same project that
8 they bid into our RFP process.

9 The projects are very similar, he is correct in
10 that respect, but there were no trade secrets stolen, there
11 was no cloning, and certainly USA Power doesn't have the
12 monopoly on how to design a combined-cycle combustion
13 turbine project, so -- and that, in fact, is included in
14 the testimony and is addressed.

15 MR. PERLMAN: Could you tell us who Navigant
16 reported to, how they were independent in this process? Did
17 they have a relationship only with Pacificorp? Did they
18 have one with the Utah Commission, and now was that
19 structured and how were they brought to the table?

20 MR. TAHLMAN: Navigant was retained by us through
21 a solicitation to find an independent evaluator. We went
22 out and did a mini-solicitation and we evaluated three
23 responding firms, and Navigant was chosen by us as what we
24 felt was the best candidate.

25 And Navigant was retained by us, paid by us, but

1 produces reports that are confidential reports that are made
2 available to the Commission. In Utah, there's effectively
3 three regulating bodies -- the Commission itself, the
4 Division of Public Utilities, and the Committee for Consumer
5 Services, all of which received the reports.

6 MR. PEDERSON: Thank you for your comments. Do
7 we have any other questions from the audience?

8 MR. McDONALD: Steve McDonald with AES. The
9 discussion on the CLECO RFP brought something to mind from
10 sitting in yesterday's discussions, that these two topics
11 are fairly closely related.

12 In the situation that you described with the
13 CLECO RFP, is there any special screens or analysis done
14 with relationship to an offeror's responses that might be
15 made from a marketing affiliate of an entity that controls
16 the transmission with which you are surrounded?

17 MS. BENSON: Actually, no, but there's nothing to
18 preclude it, and thus far it has not been an issue, but
19 that's an interesting question, and it's conceivably
20 possible, as you know.

21 MR. PEDERSON: We'll take one more.

22 MS. BROWN: Carol Brown from California, but not
23 representing the Commission.

24 But I heard a number of you talk about in the
25 solicitation process, trying to keep it transparent. How do

1 you balance transparency with the need to keep certain
2 information confidential, so that certain things can be
3 protected?

4 MS. BENSON: Well, I can tell you what is done in
5 Louisiana. There are a number of things that are filed
6 under redaction, but filed with the Commission. The
7 Commission receives the full material. Self-build is an
8 excellent example; the rules in Louisiana require that prior
9 to the bids being received, prior to the bid due date.

10 The utility will have to file its full self-build
11 analysis that will then be the full self-build analysis, but
12 it will be filed under redaction. They have provided useful
13 information to the market as to what it is they're
14 contemplating doing, and it's quite clear to me from the
15 responses that I have seen from potential bidders, that they
16 understand full well, what that is.

17 But in terms of the actual numbers and so forth,
18 those are filed under redaction. If that's responsive to
19 your question --

20 MS. BROWN: It is. Once the bidding -- once a
21 winner is announced, is the redacted information ever made
22 public?

23 MS. BENSON: My understanding of the process is
24 that they have to go through a certification procedure in
25 Louisiana, and then whatever the rules of the certification

1 would take.

2 MR. WELCH: In Maine, we actually have -- the
3 information concerning the RFP is obviously public. All the
4 load information is available to all the bidders, so it's
5 not sort of generally publicly available, but require the
6 utility to make it available to bidders.

7 There are private discussions with each of the
8 bidders with respect to non-price terms, typically security.
9 Those are not shared with other bidders, but the bidders
10 understand that we have a level playing field, and each one
11 can get pretty much what it wants, as long as it satisfies
12 the criteria.

13 The final contracts are public. The bid -- the
14 losing bids are never made public. The winning bid is made
15 public two weeks after -- or the amount is made -- the
16 amount of the winning bid is made public immediately; the
17 identity of the winning bidder is actually withheld for two
18 weeks so that they can go out in the market and cover their
19 positions.

20 MS. BROWN: Thank you.

21 MR. PEDERSON: Commissioner Kelliher and Chairman
22 Wood, do you have any comments or questions?

23 CHAIRMAN WOOD: Just thinking through the general
24 questions that are raised with the self-build option in our
25 jurisdiction, PPAs, purchasing of rate-based facilities,

1 which we'll talk about this afternoon -- or purchasing of
2 facilities to put into rate base, those truly invoke 2.05
3 and 2.03 of the Federal Power Act.

4 When you're dealing with a mix that includes
5 those two things, and then this third thing, which really is
6 a state rate base regulation issue, how does -- and Tom, I'm
7 going to start with you on this, because it is one that
8 we've tried to be very respectful of our overlapping
9 jurisdiction with states on these types of issues, but how
10 do you -- where's a forum to really hear that?

11 Does it start and stop at the state jurisdiction,
12 since they're regulating the purchaser and ultimate seller?
13 I mean, assume this self-build wins. If one of the others
14 wins, then it's filed here under 2.05 and goes through
15 whatever, but how -- it's awkward, and I'm wondering how
16 does -- in looking for the long-term health of a competitive
17 power market, which is what we do, how do we ensure that
18 there's a proper forum for those issues to get vetted? Or
19 has that forum, in fact, already been had at the state
20 level?

21 MR. WELCH: I think, as a practical matter, where
22 you have a situation -- I mean, the self-build option is
23 only going to be available where you have a vertically
24 integrated utility that's in some sense, price regulated.

25 And at that point, I think you sense the benefits

1 and detriments of that decision really flow to the retail
2 ratepayers. As a practical matter, you have to rely on the
3 state commission.

4 I think the issue of jurisdiction becomes a
5 little bit more tricky when you have -- and where I think
6 the Federal Commission has the critical role, is, to the
7 extent you are going to allow an affiliate to use market-
8 based rates, as opposed to rate-of-return-based rates, then
9 you have to be sure that the process by which they were
10 selected was absolutely fair.

11 I'm not sure that there's a way to solve, really,
12 from the Federal level, the former problem. If the state
13 commission gets it wrong, that's sort of the state
14 commission's problem, and I just don't see a way to avoid
15 that.

16 You can certainly make the -- you know, if a non-
17 affiliate wins the bid and it's filed here, you know, you
18 have all the existing review protections, but in a sense,
19 the fact that a non-affiliate wins already gives you some
20 comfort that there's --

21 CHAIRMAN WOOD: We just say file that quarterly,
22 right now, today. It's only when there's an affiliate
23 winner that that triggers potential hearings and such here.

24

25 MR. WELCH: Right, and, as I said, I think that's

1 -- if what the -- you know, going back to the Edgar case, it
2 seems to me that the weakness of that case is that it -- on
3 the one hand, it describes a process for selecting bidders
4 in a fully competitive market, which is a precondition for
5 having market-based rates, and then it say, oh, by the way,
6 if you don't have a fully competitive market to look at, you
7 can use these other measures.

8 I seems to me that that's an internal
9 contradiction. Either you have a fully competitive market,
10 in which case, you can run a bid process and actually select
11 a winning bidder, or you don't, in which case, you shouldn't
12 be talking about market-based rates.

13 CHAIRMAN WOOD: Thank you.

14 MR. PEDERSON: I want to thank the panelists
15 today and the audience for their participation, and with
16 that, this conference is closed.

17 (Whereupon, at 12:05 p.m., the technical
18 conference was concluded.)

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