



APPEARANCES:

COMMISSIONERS PRESENT:

CHAIRMAN PAT WOOD, III, Presiding

COMMISSIONER NORA MEAD BROWNELL

COMMISSIONER WILLIAM L. MASSEY

ALSO PRESENT:

DAVID HOFFMAN, Court Reporter

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

(10:25 a.m.)

CHAIRMAN WOOD: Good morning. This open meeting of the Federal Energy Regulatory Commission will come to order to consider the matters that have been duly posted in accordance with the Government in the Sunshine Act for this time and place.

Please join us in the pledge to our flag.

(Pledge of Allegiance recited.)

CHAIRMAN WOOD: My love affair with living on the East Coast suddenly dissipated.

(Laughter.)

CHAIRMAN WOOD: With 16 inches of snow, and thank God for Advil. That's a stock we can invest in, actually.

COMMISSIONER BROWNELL: Think of how good it was for you to spend that quality bonding time with your children in the house, locked in for three or four days, the aerobic exercise of shoveling.

COMMISSIONER MASSEY: I was reading Orders.

(Laughter.)

COMMISSIONER MASSEY: The entire time.

CHAIRMAN WOOD: I was giving them, but unfortunately, nobody was listening.

(Laughter.)

CHAIRMAN WOOD: It's good to get back to work.

We have a good, full meeting today. There are a few items that have been pushed off for various purposes, from today's vote. We've moved a number of those, notationally, in the interim.

There are a couple that, due to my recusal from my prior job, I will not be able to vote on until we have a quorum that can vote. That's for a couple of those Orders, so we will see those when Mr. Kelleher and perhaps another Commissioner get here.

Until then, let's move forward with these other important, good items.

SECRETARY SALAS: Good morning, Mr. Chairman, good morning Commissioners. The items that have been struck for the agenda since the release of the Sunshine Act Notice on February 14th are as follows: E-15, E-19, E-34, E-39, E-46, E-49, E-51, E-59, G-24, and H-3.

Your consent agenda for this morning is Electric Items E-1, 3, 4, 11, 14, 17, 18, 22, 23, 24, 25, 26, 27, 32, 33, 36, 40, 41, 42, 44, 47, 50, 52, 53, 55, 56, 57, and 58.

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Gas Items: G-1, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 18, 19, 20, 22, 26, 28, 29, 30, 31, and 32.

Hydro Items: H-5, and H-6.

Certificates: C-1, 2, 3, 4, 5, 6, 7, 8, 9, and C-10.

Specific votes for one of these is G-4,  
Commissioner Brownell dissenting and Commissioner Massey  
votes first today.

COMMISSIONER MASSEY: Aye.

COMMISSIONER BROWNELL: Aye, noting the dissent  
on G-4.

CHAIRMAN WOOD: Aye.

SECRETARY SALAS: The first item for discussion  
this morning is a joint presentation of Items E-2, Illinois  
Power Company, and E-3, ITC Holdings Corporation, with a  
presentation by Melissa Lord. Melissa will be accompanied  
by Joyce Kim, Lodie White, Michael Donnini, Phil Nicholson,  
and Wayne Guest.

MS. LORD: Good morning, my name is Melissa Lord.  
With me at the table are Wayne Guest, Mike Donnini, Phil  
Nicholson, Janice McPherson, and Joyce Kim.

My presentation involves Items E-2 and E-3. The  
draft Order for E-2 addresses an application by Illinois  
Power Company, Illinois Electric Transmission Company, LLC,  
and TransElect, Inc, seeking authorization for the  
following: For Illinois Power to transfer its  
jurisdictional transmission facilities to Illinois Electric  
Transmission, an independent transmission company and  
subsidiary of TransElect, to Illinois Power, to continue to  
operate and maintain those facilities for a minimum period

of five years after the transfer, and for Illinois Electric Transmission to charge certain rates for access to the purchased transmission facilities.

The proposed rates reflect, among other things, a gross plant levelized return. As part of the application, Illinois Electric Transmission commits to make all necessary filings with the Commission to facilitate the transfer of functional control of its system to Midwest ISO.

The draft Order finds that the transmission rate proposal may result in significantly increased rates that may not be justified by the benefits associated with the transactions.

Accordingly, it establishes hearing procedures to develop a more complete factual record concerning the rate impacts and the benefits associated with the proposal.

Concerning Illinois Power's continued operation of the subject transmission facilities, the draft Order finds that while there could be valid reasons for an interim arrangement to ensure a smooth transition to new ownership, the services agreement may result in the operation of the transmission system not being completely independent of market participants.

Therefore, the draft Order limits the period for Illinois Electric Transmission's contracting with Illinois Power to one year from the service commencement date.

The draft Order indicates that the Commission's expectation is that after this one-year period, Illinois Electric Transmission would have staff and other resources necessary to operate as a transmission business entity.

However, if Illinois Electric Transmission determines that it continues to need to contract for support services after the one year, the draft Order requires that future contracting result from a competitive bidding process and results in the services being provided by a non-market participant.

The draft Order for E-3 addresses an application by DTE Energy Company, Detroit Edison Company, ITC Holdings Corp., and International Transmission Company, seeking authorization for the following: For DTE Energy to transfer its jurisdictional transmission facilities in International Transmission Company to ITC Holdings, Corp.; for Detroit Edison, to continue to provide engineering and system operation services for average terms of two years, and construction and maintenance services for a six-year term after the transfer, and for Midwest ISO to charge certain rates for access to the purchased transmission facilities in International Transmission's pricing zone.

The draft Order authorizes proposed transfer of jurisdictional facilities to ITC Holdings Corp. The proposed rates include, among other things, an ROE adder of

100 basis points above that approved by the Commission for the participation in MISO, as well as the recovery of an amount equal to the balance of accumulated deferred income taxes on International Transmission's books.

At the transaction's closing, the draft Order accepts the proposed ROE adder and the ADI treatment, and finds, among other things, that International Transmission's proposed business model will bring an additional layer of structural independence.

Concerning Detroit Edison's continued operation of the subject transmission facilities, this draft Order reaches the same conclusions as that in E-2. Today's Orders will encourage seamless regional transmission organization development in the Midwest, lessen the potential for the exercise of undue discrimination, and the provision of transmission services and encourage the development of competitive markets.

This concludes my presentation. Thank you.

COMMISSIONER MASSEY: Thank you for that presentation. These are very important cases. In both of these cases, we have a proposal by a utility to sell their transmission assets to an independent company.

In one of the cases, Illinois Power Company -- well, as I understand it, we find -- I suppose that in Illinois Power, we don't make that finding, but we find in

the ITC case, that the transaction meets our independence standards, sufficient to justify some rate enhancements.

Can you or a member of the panel describe what the rate enhancements are for this Company?

MS. LORD: I will tackle that. The first is an ROE adder of basically 100 basis points above the 12.88 percent ROE or return on equity that was approved for participation by a transmission owner in the Midwest ISO.

The second is an ADIT treatment, very similar to that that was in the TransElect, consumers TransElect Order. It is to recover --

COMMISSIONER MASSEY: Could you describe what ADIT is, please?

MS. LORD: Accumulated Deferred Income Taxes. The specific rate treatment here is to recover a portion of the capital gains associated with the sale of the transmission facilities.

Mike Donnini might be a better person to talk about this in detail.

MR. DONNINI: The ADIT adjustments that were approved for TransElect, would just allow rate recovery for the purchaser of an amount equal to the deferred taxes that come due with the sale of the transmission facilities. The deferred taxes are due to the prior use of accelerated depreciation and other effects that result in a different

depreciation or deduction for tax purposes than for ratemaking purposes.

So that's essentially what the deferred taxes are. It's limited to just the difference, the basis difference between tax basis and book basis, and it's not tied to the purchase price of the assets.

COMMISSIONER MASSEY: Okay, were you finished in describing the treatments?

MS. LORD: Yes.

COMMISSIONER MASSEY: What is our conclusion in this Order with respect to the level of independence that this filing facilitates for the ownership of these transmission facilities?

MR. NICHOLSON: Basically, the independence issue was raised with respect to one owner of International Transmission. That was KKR. We found them not to be a market participant. There will be no ownership whatsoever, active or passive, in this independent transmission company by a market participant.

So I hate to use the word, pure, but obviously it's another layer of independence above what existed before, because Detroit Edison, which owned -- DTE Energy, which owned the transmission system before, would have been considered a market participant.

COMMISSIONER MASSEY: KKR has a fund that holds

4.9 percent of the total voting rights of Dayton Power and Light. And they have warrants to purchase up to 25 percent of Dayton's common shares.

What is the treatment in this Order of those issues, the issues raised by those two points?

MR. NICHOLSON: With respect to the 4.9 percent ownership of voting preferred securities, that's below the level that we would deem KKR to be an affiliate of a market participant. There is a market participant here, and that's Dayton Power and Light, DPL, which is a holding company which owns Dayton Power and Light.

We basically find that that does not rise to a level sufficient to make KKR a market participant. The warrants to purchase 25 percent of the common equity, what we do in the Order is to say that if they exercise those warrants, which would raise the level of their voting interest, we would withdraw the incentive rate treatment.

COMMISSIONER MASSEY: So, essentially, what we conclude here is that the limited partner, KKR's ownership of 4.9 percent of the total voting rights of Dayton Power and Light does not make it a market participant?

MR. NICHOLSON: Essentially.

COMMISSIONER MASSEY: But if they were to exercise these warrants to purchase up to 25 percent of Dayton's common shares, that would create a problem?

MR. NICHOLSOLSON: That would create a problem, and I believe we so indicate in the Order.

COMMISSIONER MASSEY: Okay. I just had some questions, Mr. Chairman. Go ahead and allow for comments that anyone else has.

CHAIRMAN WOOD: We've got all day.

COMMISSIONER MASSEY: Let me ask a question about the Illinois Power Company Order. The rate treatment in that case, in contrast, is set for hearing. Why is that the proposed recommendation?

MR. DONNINI: Our preliminary analysis indicates that the premium above book value that would be recovered through the rate proposal would significantly exceed levels that we'd approved previously for TransElect, and we're considering in the proposed pricing policy statement, we find that given the nature of their proposal, we need to have a quantified cost or a quantification of the rate impacts and of the benefits associated with the transaction.

While the applicants have filed a cost/benefit study, the benefits they've quantified don't come close to justifying the rate impact that we quantify and we're setting it for hearing in the Order to develop a more complete record as to the rate impact and the benefits associated with the transaction.

COMMISSIONER MASSEY: Is the primary issue the

levelized gross plant original cost?

MR. DONNINI: It's the primary driver to the rate premium.

COMMISSIONER MASSEY: That is the primary driver that would increase the cost; that's what you're saying?

MR. DONNINI: Yes.

COMMISSIONER MASSEY: And that raises a concern. What about the 50/50 capital structure for rate purposes; is that part of the concern as well?

MR. DONNINI: That's not as much part of the concern. We don't have a basis right now to find -- to quantify what the impact is, associated with that. We don't know what the actual capital structure would be.

COMMISSIONER MASSEY: Other than the rate treatment in the Illinois Power case, which we set for hearing, as I look at this transaction, it's a fairly clean deal. The purchaser is not a market participant; is not affiliated with a market participant.

Do we reach that conclusion in our Order? Anybody? Do we reach any sort of conclusion?

MR. LARCAMP: Commissioner, the way I read that, we deferred on that, pending the submission of some agreements that have yet to be negotiated.

COMMISSIONER MASSEY: I see the partnership agreement.

MR. LARCAMP: The partnership agreement itself is not yet negotiated, so Staff very carefully reviews that documentation when it comes in, to make sure we understand what's going on with respect to the ownership structure, so there is no finding on that in the Illinois Power case.

COMMISSIONER MASSEY: As I see these cases, there are really two big issues: Number one, what level of independence is being facilitated by these transactions? It is my hope that both of these transactions are creating independent transmission companies that have a high level of independence from market participants, if not absolute, total independence, at least 99.9 percent of it.

The second issue is the rate treatment, because it seems to me, what we're incentivizing with more generous rate treatments, is a very high level of independence for market participants.

So, these two Orders have my full support. I want to congratulate the parties for moving forward to create these independent transmission companies. They've both made commitments to participate in RTOs as well, and this is the market direction that the Commission would like to see in the future.

And as has been made clear by our proposed policy statement on transmission pricing, the Commission is willing to be somewhat more generous in its rate treatments in order

to encourage the market to move in this direction and I

think these two Orders achieve that result.

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COMMISSIONER BROWNELL: I agree with Commissioner Massey that these models certainly represent the goal of the Commission, and it was interesting to work on these because the very questions that you raised, Commissioner Massey, I think are new questions that we will have to answer as clearly as possible as quickly as possible.

One of the I think more interesting aspects of the discussion of independence is we now have players in the marketplace with different structures than we had before, so the organizational charts that, thank you very much, the staff was able to provide for us to explain who owns what, I think is something that was very informative and something that I hope this sort of provides clarity about as we have many different funds and many different entities now investing in the marketplace. And we certainly want to encourage that.

So the issue of independence which some of the parties raised I hope the clarity given here will provide some guidance. I also think that we and the MISO will need to be vigilant in making sure that we fully understand that independence.

The second independence issue I think that we have given clarity here today to is that we are willing in fact to give some extra financial consideration to new independent models but there must be a value that is

returned to the customers. And continuously we've said we're looking for independence and innovation because we must be sure that we're paying for a value to the end use customer. And I just want to keep that thought in mind and encourage the market participants as they are going into these deals that that's what we're looking for and that's what our obligation is to the customers.

I think in our recent transmission policy we've done that, and we've done that in a very responsible way. I think there has been some concern that we're throwing money. I think we're giving money to those who bring value, when you think of the transmission system and all that it can enable in terms of generation efficiency. So I think these are two good cases that represent a good beginning in terms of defining the policy and defining what we consider important but also what we consider our obligation are to customers.

So I endorse these and look forward to lots more.

CHAIRMAN WOOD: I can't add much to that other than to say that the one thing we did in both cases, amend as part of our approval, was the continuing involvement of the prior owner of the facilities. And I think that there was in the Illinois power case an expectation that Illinois Power would continue to be there kind of under contract for five years, which we revised down to one, with an RFP option

to extend that. And then the E-3 item, which was the ITC Detroit, had a continuing involvement for two years plus I think a six-year construction.

It's important to go ahead and make the clean break here. I think ownership of the assets is an important attribute, but it's just as important that the employees know who they're working for, because the day-to-day type of issues that we enumerate to some length in our Notice of Proposed Rule that we put out last July really relates to the day-to-day types of discrimination that can happen by a transmission owner whose corporate cousin or corporate affiliate is in the generation or in the power sales business.

And so getting those employees as well as the ownership and the operation over to an independent entity are all equally desirable goals. And so I think it was important. It's something I hope that future applicants view as an issue that we take very seriously. Certainly the rate treatment is important I think, making sure that there are not disincentives for existing utilities who recognize that, due to the policies of this Commission and the Federal Power Act, that these are no longer strategic assets. They're money-making assets, yes, but they're not strategic assets that can be used to leverage returns in other lines of business.

To incent those people to go ahead and sell if they choose to do so, we do have to take some steps to neutralize the tax impact, and I do think that the ADIT, while an accounting technique among many others, is workable, I do hope that Congress is going to continue as they did last session to consider ameliorating the tax impact of the capital gains on the sale even further through the proposed language that I think was agreed to last session. I hope that can come through.

So I do think it's pragmatic, the kind of approaches that we take here, in recognizing that independence is worth something, probably worth many times over the something we have awarded it here, due to the long-term benefits to the customers from having a competitively operated market. So this is a good step.

I appreciate, Bill, your long advocacy for this type of corporate model, and I can't be happier than what we've got here today. I do think where the Illinois Power issue, while we sent that to hearing, I do think that we've got two data points out there now with the ITC case and with the Consumers TransElect case, that indicate kind of the ballpark that people can talk about.

And certainly these first three in the door here I think probably do merit some consideration for being first. I'm not sure that the subsequent folks on down the

line -- it doesn't get better. I don't think it gets a whole lot worse, but I think the first three through the gate do get the better enhancements. And I think there's some room there to get a negotiated outcome before a settlement judge on E-2 so that that one can get back on track.

So I support these and appreciate everybody's hard work, you folks till late last night. And you folks.

COMMISSIONER MASSEY: I just have one more comment. Although I'm willing to conclude that KKR's ownership of -- passively -- of 4.9 percent of the total voting rights of Dayton Power & Light, does not make them a market participant.

If they had two deals like that, if they owned 4.9 percent of Dayton Power & Light and 4.9 percent of another utility, I might have a different opinion about it. If they had three or four. I mean, at some point I think I would become concerned that it was not the level of independence that we had in mind that we're willing to pay a premium for. So I wanted to make that point clear.

Am I correct in assuming -- I'm sure it's in the orders, but I don't remember -- that both of these companies agree to participate in -- are they both participating in MISO? Am I right about that? They will be participating in MISO under these proposals?

MS. LORD: Yes. The International Transmission Company's transmission assets are currently controlled by Midwest ISO.

COMMISSIONER MASSEY: Right.

MS. LORD: And in the other case, those transmission facilities would be transferred to Midwest ISO on subsequent filings.

COMMISSIONER MASSEY: And they would both come in under Appendix I, is that right? Under MISO Appendix I?

MS. LORD: I believe that's correct.

CHAIRMAN WOOD: The point you made first about if there's more than one 4.9 percent ownership, we've captured there in a footnote that was I think put in there last night, footnote 37. We note that the Commission's analysis of an applicant with voting interests in more than one market participant even if below the 5 percent threshold, may result in a different conclusion. And I would concur with your thoughts on that as well.

COMMISSIONER MASSEY: Okay. Shall I vote?

CHAIRMAN WOOD: You shall.

COMMISSIONER MASSEY: Aye.

COMMISSIONER BROWNELL: Aye.

CHAIRMAN WOOD: Aye, on both orders. Thank you all again.

SECRETARY SALAS: The next item for discussion is

E-5, Midwest Independent Transmission System Operator, with a presentation by Helen Dyson, accompanied by Jesse Hensley, Penny Murrell, Udi Helman, and Jennifer Shepherd.

MS. DYSON: Good morning Chairman and Commissioners. My name is Helen Dyson, and seated with me at the table are team members Jennifer Shepherd, Jesse Hensley and Penny Murrell.

The draft order presented for discussion concerns the Petition for Declaratory Order filed by the Midwest Independent Transmission System Operator, or Midwest ISO, which seeks Commission approval of the general direction of three proposed market rules.

The Midwest ISO's proposed market rules would provide for a security constrained, centralized, bid-based scheduling and dispatch system; financial transmission rights for hedging congestion costs; and market settlement rules.

Recognizing that the Midwest ISO's filing represents an important first step in moving toward functional competitive bulk power markets in the Midwest, the draft affirms the general direction of the proposed market rules.

In addition, because there is a broad overlap of issues in the proposed market rules and in the Commission's recently issued Notice of Proposed Rulemaking on Standard

Market Design or SMD NOPR, the draft discusses the Midwest ISO's filing in light of the requirements in the SMD NOPR, approves or conditionally approves various elements of the filing accordingly, and provides guidance in areas found to be inconsistent with the basic principles of SMD NOPR.

More specifically, the draft provides guidance on issues related to congestion management, seams between control areas, resource adequacy, marginal losses, initial allocation of financial transmission rights, and the auction allocation method.

As stated in the draft, unless indicated otherwise, the Commission would take all appropriate steps at the final rule stage of the SMD rulemaking proceeding to ensure that, to the extent it has already approved or conditional approved RTO elements, including general aspects of the proposed market rules, the approvals would remain intact.

In addition, the draft order would provide the Midwest ISO with a reasonable time in which to change its market design if there are substantial changes in the Commission's final SMD rule.

Thank you.

COMMISSIONER MASSEY: I think my own view about this filing is that MISO is generally moving in the right direction, and our declaratory order finds that that is

true. They're going to propose a security constrained, bid-based dispatch, day-ahead market, locational marginal pricing.

There was a concern raised by a party about locational marginal pricing. I think the order lays out some good arguments for why the Commission believes that locational marginal pricing is the most efficient way to price in these markets. So we reject the concern that is raised about it.

There is a concern that is raised by this filing, though, that our order underscores, and that is MISO will continue to operate with 40 control areas in the region. And I was here when we voted on the original MISO order. I think it was back in 1998, and raised a concern about that then. That was when the proposal was simply to create an ISO in the region.

And our order directs MISO to take a look at this and to give us a report on whether this is the most efficient long-term way to operate the RTO with 40 different control areas within it. It is certainly something that I hope MISO will take a good, hard look at and, you know, put on their green eyeshade and give us a really solid report on whether this is the most efficient way to operate within this RTO, because it did raise some concerns with me.

The other issue that I'd like to highlight is the

allocation of FTRs. When I look at our proposal under Standard Market Design for firm transmission rights, which we call CRRs in SMD, I want to make sure that the load-serving entities have enough of these to provide a really solid hedge for congestion costs. So tell me how we deal with that issue in that order, whoever is responsible for that. Is that you, Jennifer?

MS. SHEPHERD: I guess that's me. What we do in this order on the issue of initial allocation of FTRs is we accept the Midwest ISO's answer that they're going to work with states on this issue and work with all of the stakeholders to try and come to some consensus and we accept that commitment.

We also -- I've lost my train of thought.

COMMISSIONER MASSEY: Well, as I understand it, we tell them that we still want some work on this issue of initial allocation, because we want to make sure that these rights are allocated in a manner that is similar to historical uses, so that there aren't any big surprises here.

I know that one of the concerns that has been raised in the context of Standard Market Design has to do with these rights, and are they going to be a complete hedge or congestion costs, will they be allocated or will they be auctioned? If they're auctioned, will those that need them

be assured that they can get them at a reasonable price?

So as I read this order, we say to MISO, you still need some work on this issue. You're headed in the right direction, but we lay out a number of concerns about the allocation of these rights and express some of the concerns that I've raised here and tell them that they need to come back to us.

MS. SHEPHERD: Yes.

COMMISSIONER MASSEY: And this is an extremely important issue for the Commission as we move forward. Do I have that roughly right?

MS. SHEPHERD: Yes, you have that correct. We're requiring them to come back when they file their tariff to institute these energy markets and file all of the information on who will get FTRs, what their existing rights are, and if there's any pro rataing of those rights.

We also direct them to make that kind of informational filing well before they come in and file their tariff with us. Really we would like to see it as soon as possible. We're aware, Staff is aware that the Midwest ISO is performing this type of modeling already, and we would like to see that as soon as possible, but certainly no later than two months prior to their filing of the tariff. And that would be an informational filing.

COMMISSIONER MASSEY: Well, my view is that MISO

is headed in the right direction. I'm glad they made this filing and gave us an opportunity to give them some policy direction here.

I think that if they put in the work that is necessary in consultation with their state commissions and other market participants, I feel confident that they can come to a very reasonable conclusion about the allocation of firm transmission rights, and I would encourage MISO to take a good, hard look at this control area operation issue and report back to us. And I think the order, if I'm correct, the order directs that kind of report. Am I right about that? Yes.

Thank you, Mr. Chairman.

COMMISSIONER BROWNELL: It's good to follow Commissioner Massey because he's a smart guy and he picks on all the right issues. So I would simply say that I particularly am interested in the outcome of the control area report, but I'm also glad that we're finally going to have an opportunity to address many of the concerns that have been raised by the co-ops and the munis, and that is the allocation of FTRs, getting accurate information in terms of the modeling, well before we put this into implementation, looking at the historical usage so we can make sure whatever allocation method is used that there isn't some cherry-picking by those who understand the system

better than others.

So I think it's really important that everyone have the same information and begin to understand what opportunities and what responsibilities they'll have in the marketplace.

So I thank MISO once again for being the laboratory. I look forward to the work and I think -- I hope it really does begin in a more meaningful way than we've been able to in the past to respond to some of the very legitimate concerns that we've heard during the development and discussion on Standard Market Design.

So I'm happy to support this order. And I thank all of you guys I know for working at the eleventh hour to add some of the bells and whistles that we felt were important to get the answers that we needed.

CHAIRMAN WOOD: I do note that MISO had proposed this day two market design well before we came out with the SMD NOPR. And the concepts that we're looking at here today and giving approval to: Having independent operator, of course; voluntary energy markets; both real-time and day-ahead, know they're going to phase in the day-ahead in a couple of sequences then add ancillary service markets subsequent to that; locational pricing and financial rights of a number of flavors. It does kind of have a Baskin-Robbins attraction to the array of options that we proposed

in the SMD NOPR but didn't require here.

This very robust process has led to a panoply of tradable products that I think will give a lot of rationality and efficiency to the market.

I do note, and it's one that I've been scratching my head over as I've watched people coming to terms with LMP across the country, one thing that people don't I think use as the correct baseline is that in fact congestion today is all being through a very opaque system sent to people today.

So what we're talking about the congestion costs that would be the unhedged costs that exist, to the extent there are any, are in effect added to whatever the lowest possible rational economically efficient rate would be, then the cost of congestion. If we allocate the rights correctly, then all of that is exactly what people are paying today. And if we allocate the transmission rights as the Commission orders here in this or encourages MISO to continue to do with its stakeholder-driven process, then people should be roughly bearing -- not roughly, pretty much closely -- bearing what they're bearing today.

So we start really at the same place where we were yesterday, but we're doing it in a very honest and transparent method that says here's the underlying cost in an efficient market that has sufficient amounts of transmission and has well-located generation. Then here's

the increment that is the result of our inefficient design  
of its system. That together is what we're paying today.

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So when we talk about unbundling this, we're not unbundling it and adding a bunch more costs. We're unbundling it so that people see what the costs today are and break an amount. It's very important to get it right, so that really day two is the same as day one and day zero, as far as overall costs.

And we do need to set this up. I think this market design will clearly do towards that inefficiency cost that's driven and purged from the system altogether.

So I think they get it right, as have New England and others in the '02, moving in the correct direction.

I think there are certainly regulatory tools, both at the wholesale level and at the retail level, that can be done to ameliorate the impact of moving from a system where that's all bundled and hidden, to a system where it's out in the open.

I do think the direction needs to be clear and measured, but I do think there are certain steps, as we have taken, for example, in New England, to encourage in a five-year window, that we continue to build transmission to unclog the congestion, and that that will, in fact, will be in for that period of time, after which it would not be.

Those would allow for a transmission solution to happen in the front end, and I think that's actually a good template for us to think about as we're pulling together the

white paper.

Are there any kind of measured glide paths from where we are today with opaque systems, to a more unbundled, transparent system? Are there kind of glide paths that could be taken for implementation of LMP?

And I want to encourage the parties here at MISO to think through that, because, as we know, there are congestion points across that grid as there are in others. It's just that they happen to be transparent in MISO because of the unbundling.

I do think the maximum preservation of existing transmission rights, which Bill laid out, is the key issue here. It's important to our colleagues at the state commission level; it's important to customers, so I do think what we do in this Order -- and I'm voting for it in that context, enthusiastically -- is providing the Midwest parties with certainty from us that they should continue to move aggressively forward with knowledge that there will be significant operational challenges, but with the knowledge that there's a lot of people working with good will to overcome their differences at the stakeholder-driven level that we at the regulatory support level will be active, vigilant, and swift.

I want to thank Staff. I know that this was filed on December 17th. This is a mere 63 days after that.

half of which were buried in snow. I do appreciate the nice, swift effort on y'all's part to give the people doing a lot of hard work out in the Midwest, some certainty as to the broad brush strokes, and some specific narrow brush strokes of their markets. Two thumbs up, and probably I would say three enthusiastic ones from us, but let's confirm that.

COMMISSIONER MASSEY: I'm really glad you made the point about congestion. It's not as if under these new market designs, all of sudden you're going to have congestion that you haven't had on the system all along.

The real issue is, are you going to make sure that the congestion is transparent on the grid, and, number two, who is responsible for paying for it or hedging against it? It's really those who put congestion on the system who ought to be responsible in some way. That's the theory of it.

I think some of the issue that are raised by this filing and are raised by standard market design, are just a matter of laying out the explanations of what we're doing, I think, in a very concise way.

Some of the proposals in the standard market design NOPR seem complicated and complex, but actually the current working of the electric system is also complex. It's not like we're creating and adding new complexity to

it.

Just for example, I think this is a very interesting point: We've had system operators that have operated the grid for years and years and years.

What they normally do is a security constraint dispatch, and they base the dispatch on least cost. They dispatch the least-cost generators first, and when they stack the bids, when they stack the generation, they use a least-cost system.

What we're proposing in standard market design is the use of a bid-based security constraint dispatch, which is not radically different. It's simply that you use the bids that come in, instead of the cost of the units.

But the dispatch is done, as I understand it, in roughly the same way. So, it sounds like it's a brand new system, and I suppose in many ways, that it is, but actually what we're doing is proposing to take the engineering of the system, as it's always been used, and change the way that the generation is stacked, and use locational marginal pricing to ensure that those who put congestion on the system, have to pay for it or hedge against it.

COMMISSIONER BROWNELL: Could I just add that I think this is an important discussion to have, because while we are not in many ways, dramatically changing the way we do business or, indeed, we're not adding costs, that isn't

fully understood.

And we're asking people to confront costs in a way that has financial implications for them, for their customers, and I think we need to have a transition period where it's fully understood, what those impacts are going to be, and make sure, as you've said, Commissioner Massey, that they have the tools to hedge against that.

I also think that we have in this country, largely been in denial about the problem that we're trying to solve, and I think one of our challenges has been that we're trying to create the next 20, 30, or 40 years when no one has really felt, because of that denial, and because of the opaque nature of the system, no one has understood the enormous costs that we're paying today because of congestion, because of, frankly, some uneconomic dispatch, some poor siting decisions of generation, particularly in the Southeast.

So, I think that we, and those in the marketplace, need to be clearer, not only about the fact that we're not adding costs, about the costs that people are paying today. The DOE study did a little bit of that; EPRI's, I think, exposed some of that.

But we need to be very, very honest with ourselves that there is a problem today. There are enormous costs today and they are growing today, and will continue to

grow without the economic signals to get the transmission built, to get the generation siting done in a more efficient way, and, in fact, to operate the system more efficiently and with greater integrity.

So I think we've got an additional challenge to define the problem more clearly, as well as to solve the problem.

CHAIRMAN WOOD: Amen to that.

COMMISSIONER MASSEY: Aye.

COMMISSIONER BROWNELL: Aye.

CHAIRMAN WOOD: Aye.

SECRETARY SALAS: The next item for discussion is E-7, PJM Interconnection, with a presentation by Jason Stanek, accompanied by Joseph Dees and Mike Goldenberg.

MR. STANEK: Good morning, Mr. Chairman and Commissioners. On December 24th, the PJM Interconnection filed amendments to its operating agreement to increase the size of its board from seven to nine members.

PJM also seeks to permit the election of board members by a simple majority, rather than a two-thirds majority of PJM voting sectors. Finally, PJM proposes to establish a nominating committee comprised of stakeholders and board members to choose candidates for vacancies on the board.

With respect to establishing a new nominating

committee, PJM states that this committee would retain an independent consultant that would prepare a list of persons qualified and willing to serve on the board. The nominating committee would then select one nominee for each vacancy on the board, and present the nominee to the PJM's membership committee for a vote.

In view of the details of PJM's proposal, the draft Order accepts PJM's proposed revisions to maintain and establish its governance structure, finding them to be just and reasonable. Thank you.

COMMISSIONER BROWNELL: I have a couple of questions. There were some concerns expressed by at least one consumer advocate, my friend, Sunny Popowski from Pennsylvania, about the addition of stakeholders to the nomination process. Could you just describe that a little bit for us?

MR. STANEK: Correct. The states of Maryland and Pennsylvania, their consumer advocates had some concerns about whether or not stakeholders would have more than input, but control of the nominating process.

As it stands, stakeholders would have the majority number of seats on the nominating committee. In addition, there would be two members of the board who would also be voting with these other five stakeholders for candidates for vacancies.

COMMISSIONER BROWNELL: And the process for putting together the slate, to hire an independent consultant, who hires that independent consultant, and how is it done? Is there an RFP process? Is it a consultant that's under some long-term contract? Do they report to the board? Do they report to management? Do they report to the nominating committee?

MR. STANEK: They report to the nominating committee, and they are selected by a simple majority of the seven voting members of the nominating committee.

COMMISSIONER BROWNELL: Is it kind of a one-time gig, or do we keep bringing back the same folks?

MR. STANEK: We don't have any details, if they select a new independent search firm every time a vacancy arises. That little detail was not in the filing.

COMMISSIONER BROWNELL: And if anyone wants to suggest a candidate, can they do so? Are they free to forward something directly to the search firm for consideration?

MR. STANEK: Yes, all the PJM members, as well as members of the nominating committee may suggest that the firm consider a specific candidate.

COMMISSIONER BROWNELL: Are there term limits on board members; do you know?

MR. DEES: There are not term limits. They have

proposed to not limit the terms of the members.

COMMISSIONER BROWNELL: The two additional places are really to reflect a broader representation they need from PJM West. Is that the reason? Most companies are shrinking their boards.

MR. STANEK: They said they would have these two additional board members in addition to a third member who would not be voting, but would be more of an advisor. These two members, the purpose of their seating on the nominating committee was to maintain consistency throughout the selection process.

COMMISSIONER BROWNELL: I watch with interest, probably more than most, the emergence of governance of the RTOs. I continue to be concerned and will spend time here, because I think we've seen in the last year, the price one pays for not paying attention to the appropriate governance structure, codes of conduct, independence.

I would encourage PJM and the other RTOs to take a good long look at all of the rules that the New York Stock Exchange has put in place for its members. I think the responsibilities of an RTO are as great as any of the member listed companies on the Stock Exchange.

I would ask them to pay particular attention to Sections 3-9 and -10, which really deal with independence and codes of conduct and full disclosure and how one sets

the characteristics one is looking for in a board.

So I can vote for this, but it is something that I'm going to pay close attention to. I know some people think that's intrusive, but we're creating organizations with enormous responsibility, and with oversight by us and oversight by the states, but nevertheless, a lot of responsibility.

I think we need to be sure that those boards are as good as we can get. Thank you.

CHAIRMAN WOOD: I'm fine with this Order, too.

COMMISSIONER MASSEY: Aye.

COMMISSIONER BROWNELL: Aye.

CHAIRMAN WOOD: Aye.

SECRETARY SALAS: The next item for discussion is E-8, Westar Energy, with a presentation by Jean Miller, accompanied by Janice Garrison and Julia Lake.

MS. MILLER: Good morning, Mr. Chairman and Commissioners. My name is Jean Miller. With me at the table are Janice Garrison and Julia Lake.

My presentation involves E-8, an Order that grants Westar Energy Inc.'s request to issue up to \$150 million of long-term, unsecured debt, subject to the following conditions: First, the proceeds of the debt must be solely for the purpose of retiring outstanding indebtedness.

Second, Westar must file quarterly informational status reports, detailing its financial condition and debt reduction efforts, within 30 days of the end of each calendar quarter.

Third, Westar must submit a report of securities issued, within 30 days after the sale or placement of the long-term unsecured debt.

Finally, Westar must abide by the following four restrictions that would be applied to all future public utility issuances of secured and unsecured debt: One, public utilities seeking authorization to issue debt that is secured or backed by utility assets, must use the proceeds of the debt for utility purposes only.

Two, if any utility assets that secure such debt issuances are divested or spun off, the debt must follow the asset and be divested or spun off as well.

Three, if assets financed with unsecured debt are divested or spun off, the associated unsecured debt must follow those assets. Specifically, if any of the proceeds from unsecured debt are used for non-utility purposes, the debt likewise must follow the non-utility assets, and if the non-utility assets are divested or spun off, then a proportionate share of the debt must follow the associated non-utility assets by being divested or spun off as well.

Four, with respect to unsecured debt used for

utility purposes, if utility assets financed by unsecured debt are divested or spun off, then a proportionate share of the debt also must be divested or spun off.

These conditions and restrictions are intended to prevent Westar and other public utilities from borrowing substantial amounts of money and using the proceeds to finance non-utility businesses.

The order puts public utilities on notice that these and other similar conditions and restrictions will be imposed on future issuances of debt in order to ensure that these issuances are compatible with the public interest, will not impair a public utility's ability to perform in the future, and will provide appropriate protections to ratepayers. This concludes my presentation; thank you.

CHAIRMAN WOOD: I know that our law splits between state and federal, some responsibility in this realm. Could you kind of walk through how that is and how the Order addresses that issue?

MS. MILLER: Our statute states that we have authorization over the issuance of securities, if the state doesn't have authorization. In this case, the Kansas statute has a similar statute in place whereby Kansas authorizes the issuance of long-term securities, if another state or federal agency doesn't have authorization.

So it can go in a circle, thus, Westar has filed

here, so we have jurisdiction. But in the future, the KCC has issued orders where they must file with the KCC for any future issuance of debt, and they won't have to file with us anymore; they'll just have to file informational copies of our applications.

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CHAIRMAN WOOD: Thank you.

COMMISSIONER MASSEY: I'm glad we're highlighting this case, because we've had commentators who have urged us to upgrade our policy with respect to Section 204 approvals of debt issuances, and so I am glad that we are in fact updating our policies.

These are new generic conditions, are they not, that we're announcing in this order?

MS. MILLER: Yes.

COMMISSIONER MASSEY: And they will apply to all applications that are in house now or that are filed in the future. Is that right?

MS. MILLER: Yes.

COMMISSIONER MASSEY: Okay. I recall that at our recent conference, in which we invited Wall Street representatives and a representative from MBIA, which was a fund that insures debt -- her name was Kara Silva -- recommended that the Commission upgrade its policy with respect to 204 applications.

Now, essentially what we're saying here is if you're going to borrow money and pledge utility assets as collateral, you've got to use that debt for utility purposes. That's the centerpiece of this, is it not?

MS. MILLER: Yes.

COMMISSIONER MASSEY: And if you spin off assets

at some point, a portion, the right portion of the debt follows those assets. Is that correct?

MS. MILLER: Correct.

COMMISSIONER MASSEY: Mr. Chairman, I think we have a good recommendation here from Staff as a way to tighten our policy on 204 filings. It's still a fair, reasonable policy. Utilities will be able to borrow the money that they need to finance their obligations, to finance their operations.

But a concern that had been raised is that utility assets were pledged as collateral for borrowings, and the debt was not used for utility purposes. It was used for other purposes, for nonutility purposes. And I'm glad we're addressing that concern here.

There's also language in the order that encourages state commissions to come in and tell us what they think when these filings are before us. And I think that is very important for the Kansas Commission or other state commissions that have a concern to come in and give us their recommendations when these applications are filed with us.

I think this is a good order. It's a reasonable outcome, although let me say that I have an open mind about this whole area of Section 204 filings. I think these new conditions are good ones. They're solid. I'm glad we're

going at least this far. If those in the marketplace, state commissions, want to recommend other conditions that we should consider on future filings, I have an open mind about them and would be happy to consider them as well.

COMMISSIONER BROWNELL: I think Commissioner Svonda as head of NARUC was with us during these discussions with the folks from Wall Street, and I think his take away was that indeed this was an important step for us to take, but that the states needed to take a look at this issue, and I hope that at the upcoming NARUC meeting, maybe this is be under discussion.

Because I think it's very important -- this is clear and straightforward and equitable and allows the companies to manage their businesses while giving the transparency that we need to fulfill our obligations. It would be I think helpful if the states responded in a way that we could get some consistency state by state, because we're clearly looking at multi-state entities today. I think when the market settles down, we'll have consolidation and convergence and we'll be looking more.

And so just to be sure that we're adding value for the customers and not getting in the way of the people to operate their businesses, I think the rules we adopt and the states adopt I would hope we would work together to make them as consistent as possible.

COMMISSIONER MASSEY: Aye.

COMMISSIONER BROWNELL: Aye.

CHAIRMAN WOOD: Aye. Thank you all.

SECRETARY SALAS: We continue now with E-30, Entergy Services Inc. This is a presentation by Diane Gruenke, accompanied by Penny Murrell and Gene Grace.

MS. GRUENKE: Good morning. This order addresses a complaint rehearing request and compliance filings related to four interconnection agreements to which Entergy is a party.

The order is a follow-up to a recent basket order, Pacific Gas & Electric, in which the Commission, acting under Section 206 of the FPA, required that certain existing interconnection agreements, including those with Entergy's interconnection customers, be amended to provide transmission credits for network upgrade facilities.

Furthermore, in Pacific Gas & Electric, the Commission stated that it would address the issues that were not addressed in that order at a later date. Accordingly, this order, E-30, addresses all of the remaining issues that were not addressed in Pacific Gas & Electric.

This concludes my presentation.

COMMISSIONER MASSEY: Mr. Chairman, I wanted to talk about this case to address what may be some confusion out in the industry and among state commissions about what

our existing policy is with respect to the cost of interconnection and where we're headed.

In these cases, as I understand it, we apply our existing policy, which is the so-called at-or-beyond test.

Am I correct?

MS. MURRELL: That's correct.

COMMISSIONER MASSEY: Okay. That is for these cases that have been pending for -- I don't know how long they've been pending -- but these are matters that are proceeding through the Commission's decisionmaking process right now.

Now the Commission has proposed a concept called participant funding for transmission upgrades. We proposed that in the context of the Standard Market Design NOPR. We also have a pending NOPR dealing with the interconnection -- we have two NOPRs, as I understand it, one dealing with the proposed interconnection standards for small generators, and one large generators. And all of these matters will end up addressing this question of how to allocate the cost of interconnection.

When I was out on the stump last week giving speeches, I got a number of questions about the orders that we issued on our last agenda. The question is, is the Commission backtracking on participant funding? Is the Commission going back to its old policy of at-or-beyond?

And my response to that is the existing policy right now is the at-or-beyond policy. We're simply applying that in these cases.

We have proposed a participant funding. I still like the concept of participant funding. We're getting a lot of good comments in the Standard Market Design proceeding on that issue. I have not myself backed away from that. I don't think the Commission as a whole has. It's simply a matter of how we sequence our decisionmaking process.

The existing policy is the at-or-beyond policy, which is a physical test for determining who pays. And in the future, we may adopt the participant funding test. But as I understand it, that requires two prerequisites: Number one, there must be in place an independent transmission provider or an RTO that's applying that standard. And number two, there must be a system of locational marginal pricing, neither of which exist in these cases or the pending matters where the Commission is applying our existing test.

So I wanted to make the record clear that I have not changed my mind on participant funding at all. I still think it's a very good idea. I'm glad the Commission is exploring it in our Standard Market Design NOPR. A lot of the comments we've gotten have been very helpful in

understanding how it ought to apply. We had a day-long conference on the whole series of issues that are raised by the participant funding concept.

So I just wanted to call these cases to say the fact that I am voting for our existing policy does not mean that I have backtracked or changed my mind. I don't think the Commission as a whole has.

MS. MURRELL: Commissioner Massey, I'm glad you called these cases and I'm glad that we're having the opportunity to discuss what is clearly a distinction between the existing policy and one that is proposed.

But I think it goes further than that. I think that participant funding means many different things to many different people. To some folks it means you pay for everything that I want you to pay for, and I pay for as little as I possibly can, in spite of many years of not upgrading my system.

I don't think that's what we intended when we talked about participant funding, and that is not the definition that is included in the Standard Market Design NOPR. So I think the problem this week and going forward is twofold. One is we do have an existing policy and we are applying it, and there was contract language in the original case that actually gave some rights that we preserved, as we must.

But more importantly, I think we need to be really very, very clear and we need to be clear when we're talking to folks in the marketplace about what it is we mean. And I would suggest others perhaps when they're having discussions about participant funding and commenting on what we mean and what we don't, probably take a look at SMD and look at that definition and say, if indeed they don't agree with that definition, then that's what they don't agree with. But to suggest that just because we're not agreeing with their definition we don't agree with participant is a slight misrepresentation.

So I think the problem is twofold, and I'm glad you gave us the opportunity to work on this. I think I would encourage everyone to look at exactly what we said about participant funding and kind of stick to that script until we say something more.

CHAIRMAN WOOD: In the interest of talking about a crisp concept, I did note with interest our sister commission in Louisiana on the round two comments did talk about participant funding and I think kind of encapsulated here a concept that I largely agree with. This is on page 12 of their comments:

The responsible utility or RTO/ITP et cetera, should determine each year what if any changes or enhancements are needed to the existing

transmission system to provide adequate reliable service to the historical and existing native load customers, including that needed for projected load growth for these customers. This annual planning process could also include enhancements that are economic in nature, if it is prudent to do so from the perspective of the retail native load. These costs would be rolled in subject to all necessary regulatory approvals, and these would be the only rolled-in costs. Any other transmission enhancements would have to be requested, financed and paid for by the party or parties requesting those enhancements.

I think I would agree with that with the caveat that Bill added that the determination of these issues should be done by an independent transmission provider operating within the context of a locational marginal pricing-type regime which is exactly what I think the two strongest utility proponents of participant funding, by whatever definition, acknowledged here at the Commission forum late last year, and in fact indicated that participant funding doesn't work unless it's done within the context of independent transmission service, locational marginal pricing, and actually I should add transmission rights, which are usually associated with the LMP concept but maybe

not necessarily.

I do think that I did hear those strongest advocates for participant funding acknowledge that that is really needed to make this work fairly, that that determination be done by an independent entity and that price signals be sent clearly as to where the transmission investment should occur.

So I would say that the discussion begin at that stage to crisply determine what we're talking about here. But that needs to continue at the level of specificity. And I do think when regional state commission groups come together in putting together RTOs and have a strong preference for whether to go this route, as the Louisiana Commission has suggested, or in other parts of the country that may draw the line differently between, you know, reliability and economic on one side and other -- that line may well be different in other parts of the country.

But I think we need to talk about clearly what types of investment are on what side of the line for rolled-in and what kind are for incrementally priced and that when we can get that sort of clarity, whether it be nationally, which I doubt, or on a region-specific basis, which is probably more likely, that we have it clear so that people can start that investment now and know how they're going to get their money back now. Because we're paying the price

for that.

Despite the fact it was affirmed by court yesterday, I do think long-term or current policy rule faces continued resistance if it's not more -- if we don't go more in the direction that I think, Bill, you've mentioned in the past and today, and that we've indicated an interest there because of the perceived cost shifting that could occur.

And I acknowledge that that's a valid point. But our policy on or pricing -- and pricing is pretty strong as well. And so we've got to maintain the equities on both sides of that equation. I think we can. I think this proposal, and to their credit, the Louisiana Commission articulated that pretty well. I think that gives us some ground to work from. But I do think it's going to help to see specific proposals with specific language, that is the kind of language you can go make investments based on. That's going to be how we get there.

So thank you for the conduit, Bill, for this Wrightsville order to do that.

COMMISSIONER MASSEY: Aye.

COMMISSIONER BROWNELL: Aye.

CHAIRMAN WOOD: Aye.

SECRETARY SALAS: Next for discussion is M-1.

This is a rulemaking proceeding on the treatment of critical energy infrastructure information, and this item will be

presented by Carol Johnson, who is accompanied at the table by Susan Court and Richard Hoffmann.

MS. COURT: Good morning. M-1 represents the final step in a process the Commission initiated after the terrorist attacks on September 11th, 2001 in order to protect critical energy infrastructure information, or CEII.

The Commission received over 40 comments in response to its Notice of Proposed Rulemaking. The vast majority of these comments supported the efforts the Commission is taking to protect CEII.

The draft final rule under consideration today attempts to strike an appropriate balance between the benefits of the free flow of information and protection of people and property. For that purpose, the rule establishes a mechanism for making available certain categories of information that would otherwise not be available under the Freedom of Information Act, or FOIA.

Specifically, the rule defines CEII as information about proposed or existing critical infrastructure that relates to the production, generation, transportation, transmission or distribution of energy; could be useful to a person in planning an attack on the infrastructure; is exempt from mandatory disclosure under the FOIA and does not simply give the location of the critical infrastructure.

The rule goes on to define critical infrastructure as existing and proposed systems and assets, whether physical or virtual, the incapacity or destruction of which would negatively affect security, economic security, public health or safety, or any combination of those matters.

The rule also elaborates on what types of location information qualifies CEII and what types do not.

The rule also instructs filers to submit non-CEII location information as non-Internet public information. This information will be publicly available in the Commission's Public Reference Room but will not be available on the Commission's Web site through FERIS.

In addition, the rule details how to submit CEII and how to request CEII outside of the FOIA process. To assist filers, the Staff has prepared guidance on how filers should submit non-Internet public and CEII information. That guidance will be available for downloading on the Commission's Web site shortly after the rule is issued.

Finally, the rule establishes a CEII coordinator and delegates to the coordinator authority to act on requests for information that is submitted as CEII.

In brief, the rule sets up a process in addition to the FOIA so that information otherwise not available under the FOIA can be obtained so the public can meaningfully

participate in Commission proceedings.

That concludes my presentation. Thank you.

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COMMISSIONER MASSEY: This is a final rule.

MS. JOHNSON: Yes, sir.

COMMISSIONER MASSEY: Suppose there's a pipeline, a new pipeline proposal under Section 7(c) and I'm a landowner that is affected by the route of this pipeline, and I want to know where this pipeline is going and how it's going to affect me. How am I affected by this rule?

MS. JOHNSON: Under the location information that's not considered to be CEII or a general location map alignment sheet, seven and a half minute topo maps, all of that information will be available through public reference. It will be available along the pipeline route, in reading rooms and things like that.

So that level of information is available to anyone in the public, including the landowners.

MS. COURT: Also, Commissioner, that's non-CEII information, so in brief, in response to your question, that person, that member of the public, will have access to the information that he or she needs in order to participate. Just general location information will be available. More detailed information than actually qualifies as CEII will also be available to that person through the process that's set up in this rule, where that person will demonstrate a need for the information.

So, in brief, that person will have access to all

the information he or she needs to participate.

COMMISSIONER MASSEY: So there's a category of documents that will not be made public; is that right?

MS. JOHNSON: Right. The CEII is not going to be routinely publicly available, meaning you can't get it on the Internet; you can't get it through the public reference room. You can file a FOIA request, but since the presumption that is that CEII, in order to qualify, if it actually is appropriately CEII, it's going to be exempt from disclosure under FOIA, which is why this new process is set up.

COMMISSIONER MASSEY: And this would be the most critical of information, more technical type specs and so forth; is that what we're talking about?

MS. JOHNSON: Diagrams of valve and piping details, flow diagrams, a diagram that shows critical parts of the system and other technical details; that type of information would be in the CEII category.

COMMISSIONER MASSEY: So the theory of this rule is that that level of detail, the technical specs, perhaps I, as a landowner, don't need to have available to me, and then that -- in balancing the equities, that is worth protecting.

MS. JOHNSON: Right, but, again, as Susan said before, if you decided, as a landowner, you did want that

information, you can follow the CEII process and request that information.

COMMISSIONER MASSEY: So if I follow the correct process, which is to make a filing here at the Commission --

MS. JOHNSON: Filing a request here, you identify who you are, you agree to abide by a nondisclosure agreement. Those are the types of things that you would have to do in order to get access to the CEII.

COMMISSIONER MASSEY: So I can get that information, but there are some checks and balances built into the system to make sure that it doesn't fall into the wrong hands?

MS. JOHNSON: Right.

COMMISSIONER MASSEY: That's my main concern, Mr. Chairman.

COMMISSIONER BROWNELL: Explain a little bit more about the process, because I think you've made it very simple. Landowners don't necessarily have access to the high-priced talent we usually see when people are making requests of the Agency, so could you describe the process a little bit? I think you have paid attention to making it simple and straightforward so that the average guy out there can get the access.

MR. HOFFMANN: Do you want me to take a shot at

that? I wanted to elaborate, just a little bit.

The new category that we have created of non-Internet-public will be a vehicle for landowners and agencies, local, state, or otherwise, to still get location information that would be included in the 7.5 minute maps, the alignment sheets, and the other sources of information which they typically are looking for to see where their rights-of-way are, how wide they are, where the workspaces are, whether the wetlands are affected and those sorts of things.

They will still be included. Maps of that nature, showing location, will still be included in our NEPA, Notice of Intent to Prepare an EA or an EIS. They will still be available in the reading rooms that the companies have to establish in each county along the route.

The landowner notice that the companies have to give to each person crossed, and a few other types of interested parties, will still have to be provided, three business days after the notice of application is posted by FERC.

Our NEPA documents will still include the typical 7.5 minute maps and other descriptions of the project that they normally do. The difference will be that the document that we post on FERIS won't have those sorts of maps in it, so we're removing the remote access capability that used to

be there.

Paper copies will still be accessible through the Public Reference Room. We can mail them to whoever. We're just removing that remote capability.

MS. JOHNSON: And if you're asking about CEII itself and how complicated it would be for a general citizen without a high-priced lawyer, I think it's really not that much more complex than filing a FOIA request. It has a little additional information. We ask for the date and place of birth and things like that, so that we can verify a little bit more about the identity of the person and why they want it, but it's really fairly similar to filing a FOIA request.

COMMISSIONER BROWNELL: I would suggest, because it's new, that maybe we test the customer in six months or a year or so and just get some feedback from people who have been through the process.

This is a very, very difficult issue that we're confront in many ways all over the country. For a country that truly believes in the principle of freedom of information, to have to balance that against a set of circumstances we never anticipated, is difficult, and I just want to make sure that we're checking ourselves along the way to make sure that there's some balance in what we're doing.

But I appreciate the job that you have all done.

I know that you have been working long and hard and that the commenters did, and I think you achieved the appropriate balance. I appreciate the outcome.

CHAIRMAN WOOD: As do I. I'm just sorry that we need a rule like this. But I'm sorry for a lot of things that happened in advance of its preparation. I do think it's very clear that information has become a weapon in our society, and one of the more vulnerable places for that is the very visible energy infrastructure that our Agency is charged, at least in part, with regulating.

I do look back and appreciate the swift effort that y'all did, particularly Carol and Susan, in your shop, to do with the interim process on FOIAs and the pragmatic response to that, which is this rule, which makes it easier, both on us and the requesting party, to actually get the appropriate amount of information.

I recognize that is a subjective call, but so are FOIA determinations, at their heart. This is no different than that, and I think it's fairer and I think it's more efficient. That's what good government should be about, because at the nub of this is information that would not be otherwise discloseable under FOIA.

I know from the comments that are summarized here in the preamble, that there are some people that question

that ruling. I read those thoughtfully, but I think we're correct that under the way FOIA is written, that information would be withheld and not be available to anybody.

What this rule does is allow information that is otherwise not available to anybody, to be available to people that have a proven or shown need to know. I do trust that we will charge the to-be-chosen CEII coordinator to use that subjectivity wisely and thoughtfully in light of the fact that our preference is that information is publicly available. That is our default presentation, and we want it to always be that way.

This is a well-done rule. Thank you for your efforts. I appreciate the participation of the Department of Justice, the FBI, the Department of Transportation, the TSA and OPS, the three of you all, and all the people behind you that made this final rule come together in such a swift timeframe. So we're there, and we appreciate the hard work of y'all getting us there.

COMMISSIONER MASSEY: I'm glad you made that point. As I understand it, we have heeded the advice of law enforcement in preparing this rule, and I think that's very important.

Aye.

COMMISSIONER BROWNELL: Aye.

CHAIRMAN WOOD: Aye.

SECRETARY SALAS: The next item for discussion is G-3, Five-Year Review of Oil Pipeline Pricing Index, a presentation by Harris Wood, accompanied by Andrew Lyon, Michael McLaughlin, and Robert Fulton.

MR. WOOD: Good morning, Mr. Chairman and Commissioners. Item G-3 is a proposed Order concerning the five-year review of the Oil Pipeline Pricing Index after remand to the Commission of a December 14, 2000 Order, in which it found appropriate, the continued use of a producer price index for finished goods, less one percent.

The proposed Order finds, after further data analysis, that the Oil Pipeline Pricing Index for the current five-year period should be the producer price index for finished goods, without the one-percent adjustment.

The Order further provides that oil pipelines may calculate the current ceiling rate using the producer price index for finished goods as though it had been the index in effect since July 1, 2001, the date of the first adjustment in the current five-year period, and that oil pipelines may file for rate increases to the ceiling so calculated to be effective 30 days after the date of their filing.

CHAIRMAN WOOD: I'm fine with the Order and the remand of a prior Order that went for review by the Court. It was appropriate for us to use the original methodology that was used several years -- I guess seven years ago to

generate the index price.

I do think, as shown on Appendix A, which is the deltas, based on both the middle 50 percent of the companies and the middle 80 percent of the companies, that really the appropriate index here more appropriately reflects that center of the bell curve of companies is the one that this orders. It was not the one that was up before the Court on review last year.

I think what we want to do is have an index that captures the costs, so that people aren't coming in on kind of the end run tariff proposals, which they have a right under the law to do, but let's get an index that tries to capture the bulk of everybody, so you don't have so many exceptions to the rule being sought.

I think that's something that's not only good for the companies, but good for the shippers as well, so we don't have to spend a lot of time down here, working through tariff filings, but can be out in the market, trying to keep our lights on, and keep the cars running.

I think this is the right outcome, and I hope it will lead to some more regulatory streamlining on our end. Thank you all for the nice work.

COMMISSIONER BROWNELL: Ditto.

COMMISSIONER MASSEY: Aye.

COMMISSIONER BROWNELL: Aye.

CHAIRMAN WOOD: Aye.

SECRETARY SALAS: The final item for discussion this morning is H-1, a rulemaking on the hydroelectric license regulations under the Federal Power Act. This is a presentation by Tim Welch, accompanied by Ann Miles and John Clements.

MR. WELCH: Good afternoon, everyone. On behalf of the Office of Energy Projects and the Office of General Counsel, I'm pleased to present to you today for your consideration, a Notice of Proposed Rulemaking that proposes sweeping changes to our regulations that govern the issuance of licenses for hydroelectric projects.

Before I get into an overview of what's in the Notice, I just wanted to take you through sort of our rulemaking journey and sort of where we've been and where we're planning to go.

We sort of began the whole process back in September of 2002 when we issued a public notice that set a schedule for a series of public and tribal forums that were cosponsored with the resource agencies that have involvement in the hydroelectric licensing process under the Federal Power Act.

We had those in October and November, and there we gathered comments and ideas about what people thought about what is needed in a new hydroelectric licensing

process. Now, we followed up those forums with a two-day stakeholder drafting session here in Washington, where we invited stakeholders from Indian tribes, non-governmental organizations, resource agencies, and members of the industry to come here to Washington to actually draft concepts and language, much of which you'll see -- many of the concepts that you will see in the Notice under the proposed rule today.

Following the stakeholder drafting session, in December and January 2003, we convened with our sister resource agencies, Departments of Agriculture, Interior, and Commerce, in drafting much of the language that you will see in the NOPR today.

Now, where are we going? Following today's Commission meeting, with the issuance of the Notice, once again we're going to take our show on the road and do a series of regional workshops where we hope to discuss the Notice with members of the public, and hopefully to identify any hot-button issues that people might have with the new process, and sort of discuss those issues.

Once again, we're going to follow that up in April with another stakeholder drafting session, where once again we'll invite stakeholders to come here to Washington for a four-day session this time to actually zero in on some very specific language and concepts that we will be

considering for the final rule.

Following that, in March and May, we once again reconvene with our sister resource agencies in drafting the language that will appear in the final rule. Hopefully, we anticipate that by July of next year, we will be here again, presenting you, a final rule for your consideration on this new licensing process.

The proposed rule does sort of two major things: Number one, and most importantly, it creates a brand new licensing process which we will refer to hereafter as the Integrated Licensing Process. And I will talk to you a little bit about that in a few minutes.

Now, we're also proposing to add some improvements to the existing process known as the traditional process, and I'll talk about those improvements a little bit later.

The Integrated Licensing Process will improve both the timeliness and efficiency of the licensing process. Now, we believe it will improve process efficiency by requiring that during application preparation, in other words, very early in the process, that the Commission will also conduct its NEPA scoping to collect the information that it will need for its NEPA document.

That's as opposed to the current regulations where the Commission does not conduct its scoping until

after the application has already been prepared.

The Integrated Process would also require coordination with other processes that may be going on in conjunction with the licensing process, most notably, the 401 Water Quality Certifying Process.

Also, the Integrated Process would increase public participation in the licensing process by requiring consultation of applicants with members of the public, in addition to resource agencies and members of the public, most notably, non-governmental environmental organizations.

Now, in regard to the timeliness of the process, we believe that the integrated process will improve timeliness by requiring early staff involvement in the process, early staff assistance with preparing the application. You will recall, as I said earlier, this is as opposed to the current traditional process where the Commission staff does not get involved in the application preparation, but becomes involved only when the application is filed here at the Commission.

FERC staff at that time will oversee what we're calling a process plan and schedule at the very beginning, at the NEPA scoping meeting, as one of the first initial meetings. FERC staff will introduce a process plan which will coordinate all the processes that will go on with the other agencies involved in the process, and will also

establish a schedule for getting things done in a timely and efficient manner.

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(Slide.)

MR. WELCH: One of the most effective changes, we think, is early study plan development, and informal and formal dispute resolution of studies.

So, right now, an applicant is pretty much on its own to develop its study plan. We're proposing that by the Integrated Process, that all the stakeholders and the agencies involved, including FERC Staff, are involved in that study plan development, very early in the process, so everyone's informational needs are out on the table at a very early time, and the study plan is formatted accordingly.

Also, we have a proposal in the proposed rule to implement both an informal and formal dispute resolution process for any disputes that arise concerning what studies the applicant is to perform when it's preparing its application.

Once again, that's in opposition to what's currently required under the current regulations where the dispute resolution process is not mandatory and quite frequently only happens after the application is filed here at the Commission.

(Slide.)

MR. WELCH: The next thing I'd like to show you is a graph that we prepared here that really illustrates the

timeliness of the Integrated Process. You can see the top bar there, which represents the amount of application processing time that Commission staff spends from the time the Commission receives the application to the time the Commission issues the license order.

So the time that we receive the application would correspond to zero on the X axis. You can see that, with the traditional process, as we reported in our 603 report, the median processing time was around 47 months, which is almost four years.

You can see that under the Integrated process, that time will be cut dramatically and that we anticipate the Integrated Process would take a processing time of about only seventeen months.

The other thing to note on this particular graph is that we've got marked, a timeline at 24 months. That is the two-year mark where the license would expire during the processing of the application, and, as you can see, with a traditional process, that quite often necessitates the Commission issuing annual licenses if the new license hasn't been issued by the expiration date.

Under the Integrated Process, we anticipate, in most cases, that the new license would be issued well before the expiration date, so we haven't precluded the necessity for the Commission issuing annual licenses.

(Slide.)

MR. WELCH: As I mentioned earlier, we also are proposing some modifications to the traditional process.

We've sort of chosen two of what we think are the biggest benefits of the Integrated Process. That's increased public participation; in other words, requiring consultation with not only resource agencies, but also members of the public and early study dispute resolution.

So we modified Parts 4 and 16 of the current regulations, the traditional process, in order to implement those measures into the traditional process.

(Slide.)

MR. WELCH: There are three sort of more global issues that I wanted to briefly go over with you that involve process selection, how you would select a process, cooperating agency policy, and how we propose to conduct tribal consultation.

(Slide.)

MR. WELCH: Now, with the implementation of the Integrated Process, there would be now three processes for obtaining a hydroelectric license: the Integrated, the traditional, and the alternative.

We're proposing in the Notice, that the Integrated Process, the new process, be the default. In other words, if an applicant wanted to use either the

traditional or the alternative, they would have to solicit public comment and let the Commission know their process selection and what comments they received in their Notice of Intent.

Following that, the Commission staff would then approve their use of the non-default process, either the traditional or the alternative.

CHAIRMAN WOOD: What if people are doing some pre-filing application activity today?

MR. WELCH: We have some transition provisions that are in there, and the effective date of the final rule would be three months after the issuance, just because people are sort of caught sort of in that in-between mark. We have, hopefully, accounted for that.

(Slide.)

MR. WELCH: The next slide on resource agency cooperation: Our current FERC policy does not allow a federal agency to be a cooperator on a NEPA document and be an intervenor in the process at the same time.

Our policy is that the Agency has to choose whether they're going to be a NEPA cooperator or an intervenor in the process. The Notice proposes to change that policy to permit an Agency to be a cooperator on a NEPA document and be an intervenor at the same time.

The second bullet, to address any concerns about

off-the-record communication, the Notice also proposes to modify the ex parte rule to require only disclosure of study information. That's specific technical information provided to Commission staff by that agency. That would still be required to be placed on the administrative record.

(Slide.)

MR. WELCH: Finally, I'd like to say a little bit about our efforts to improve tribal consultation. Under the proposed rule, the Commission would initiate very early discussions with any affected Indian tribe, in order to develop the consultation procedures that would be in place throughout the entire licensing process.

In order to do that, to facilitate that, we also are proposing to establish the position of tribal liaison here at FERC. That person would oversee all the tribal matters that the Commission is involved in.

That's all I've got.

CHAIRMAN WOOD: Oh, but you're modest. I haven't seen John since the last one of these. What was it, in November that we had the workshops?

This is, I think, a major step towards the creation of a more efficient and timely licensing process. I think your one slide, alone, showed that clearly. It envisions, as it should, that people of good will come together and advance and work through these issues in a more

collaborative format than certainly what I was surprised to find licensing has turned into when I got here.

We had the hearing back in November and December of 01, and learned about just the processes here. It's clear that there are some things that are outside our hands to do, but I would say that the rebuttable presumption is that this fixes as much on the process side as we can fix under our statutes, that should be fixed.

It balances the rights of the parties in an appropriate way, to make sure that we adhere to the laws, and also develop the resource, as appropriate. So I look forward to the process.

I think it's a good one that y'all have laid out, to go right on the hustings now and get feedback, explain what we're doing here.

Like another recent long NOPR, it is important to explain it and to explain it and to explain it again, and if they are walking out the door and need one more explanation, give it to them then, because there is a lot in here, a lot of detail, and I think it's needed and welcome.

I appreciate the effort that y'all and all the folks outside the agency put together to get us to this point. So I look forward to voting this out today and getting it on the street today, so that y'all can go get the comments and we can put this chart back on a straighter

path.

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COMMISSIONER BROWNELL: I think it's enormous testimony to the goodwill of the participants, including our Staff, and the staffs at Interior and Agriculture, that we have completed this work so quickly.

I want to particularly thank the National Review Group and the Interagency Hydropower Committee, who I think came together in a way that if you looked at the typical history of how we approached this, no one would ever have thought possible. And I really believe it made our job that much easier.

There are many elements to this NOPR that I think bear mentioning. You've mentioned several. I think the efforts made at reducing the redundancy in the reporting and the analysis are critically important. The up-front involvement of all the participants, the reduction of time, the increased public participation in the pre-filing phase, the special attention paid to some of the tribal and environmental issues, all are very positive. Will this satisfy everyone? Of course it won't. But I think the work that's been done so far demonstrates the discipline of the participants to kind of figure out what they need as opposed to just what they want. And I hope that that discipline continues, because I know everybody gave at the office on this one.

I'm also pleased that the other agencies in

conjunction with this process have looked at their own processes. Interior has announced or did announce in our first meeting that they intend to initiate an appeals process, one that is efficient and quick that does not add time to the process but really looks at some of the critical issues.

I commend them. I commend the other agencies who I think are also taking a look. While we can only control our own destiny, I think we've developed some working relationships that have grown over time that will allow us all to be focusing on the constant reengineering and reevaluation to get more and more efficiencies. Clearly this addresses administratively what we need to do.

We know that Congress, and we've certainly talked a lot to them, wants to address certain issues that are under their purview, and we will obviously work towards them. But we made a commitment when we came here in our nomination process, Pat, that this would be a priority. And I appreciate all the support we've gotten in fulfilling our commitments. And I particularly thank our Staff, who has really worked over time and gone out of their way to be responsive and to listen to the other participants in the process.

Because it's easy to sit behind our own desks and think that we kind of know how to solve all the problems of

the world, and it's amazing when somebody else has some good ideas. You've listened to those and incorporated those, and I'm grateful for that.

So I'm excited about the next couple of months and learning even more and getting it even better. I'm excited to vote for this.

COMMISSIONER MASSEY: Increased public participation, earlier Staff involvement in the process, early study plan development with a mandatory dispute resolution process. It almost sounds too good to be true. But I do think that this is a major revamping of our processes which virtually everybody seems to recognize needed some substantial modifications.

I like the way our Staff worked with the industry and the NGOs and others in putting this together. I very much like the way you worked with my office in kind of bringing us along in this complex area, telling us what you were thinking about and getting our feedback along the way. I want to tell you how much I really appreciate that.

As a result of that, I feel very, very comfortable with this proposal. I think it's a good idea. I want to commend Chairman Wood for taking a personal interest in this issue of the processing of hydroelectric cases.

I think you have been a catalyst for a lot of

good changes here by taking the bull by the horns and simply insisting that we improve our processes. I commend you for that.

Let me ask one question, though, in the area that it almost sounds too good to be true. What about the state? One of the issues we learned in these hearings we had in which Staff has come in and reported on the old or pending cases and why they're still outstanding, one of the issues that comes up time and time again is we don't have the state permits that we need to finalize. How is that dealt with in this ruling?

MS. MILES: The Water Quality Certification and Coastal Zone Management Act was not specifically dealt with, although we have changed -- well, we've got the timing slightly different than the traditional process. The timing for the request for it.

I think the answer is twofold. One is that the real goal is to have the states involved at the beginning with us as we work through this, and for them to lay on the table what their information needs are at the beginning so we can do the studies that are needed to get the information they need, and then they should be able to act in a timely fashion.

The other is they will be able to use our NEPA document. The way the rule is laid out, federal agencies

can be cooperating agencies. States are not. That's something I expect to look at a lot of comments on and see what people have to say about that. but we do anticipate that knowing that our NEPA documents would be able to have the information in it that the states would need to use it as they need it for their permits.

The other thing I think is, it's an area that we're going to need to work on as we go back out in our outreach sessions and see if there are more things that we can do to even integrate further with the states.

COMMISSIONER MASSEY: Yes.

MR. CLEMENTS: I just wanted to add one thing to that. The dispute resolution process is available to State Water Quality Certification agencies so that they can come to the Commission and if they're having a dispute with a potential applicant, they can have that resolved here.

There's no guarantee that the result of that will be for them to get the Commission to require the applicant to provide all of the data the state would like. It greatly increases the chances of that happening compared to what we have today.

COMMISSIONER MASSEY: We believe that the new processes we've set up here will make it more likely, even though we can't control what the states do, it will make it more likely that they will act in a timely fashion, that

they will have available to them the data, the information that they need early in the process. I also like the fact that our Staff would be involved at a much earlier period of time in the process.

Let me ask you one other question. This new Integrated Licensing Process is the default process as I understand it. Would it be safe to say it's the preferred process for licensing?

MR. CLEMENTS: Yes.

COMMISSIONER MASSEY: Now if I'm an applicant and I don't choose this process, what do I have to do again?

MR. CLEMENTS: A potential applicant that wants to use the traditional process or the ALP, has to get Commission authorization to do so. That's no different for the ALP. They have to do that now and they have to show that they have a consensus to support the use of that.

COMMISSIONER MASSEY: So they would have to make some showing that the use of the more traditional process is supported by a lot of the NGOs and other participants who've commented?

MR. CLEMENTS: We're looking for comment on what criteria might be appropriate for that. It's not entirely settled, but we'd like to hear more specifically about what criteria might best be applied if we're going to deal with an application to use the traditional process.

COMMISSIONER MASSEY: But we've created this new Integrated Licensing Process which even has a name that sounds more appealing. It would seem to me it's an integrated process that brings in a lot of early involvement by Staff and otherwise that would provide the necessary data and information that would allow all of the government entities that have to make decisions to make those decisions earlier and with better data.

But if I don't want to use that, I've got to make the case for use of one of the traditional processes?

MR. CLEMENTS: That's correct.

COMMISSIONER MASSEY: And the Commission has to approve that? Okay. Mr. Chairman, this proposed rule has my full support. I thank the Staff for an excellent presentation and for all their hard work.

COMMISSIONER BROWNELL: Aye.

CHAIRMAN WOOD: Aye.

COMMISSIONER MASSEY: Aye.

CHAIRMAN WOOD: Thank you, John, Tim and Ann.

What's the comment cycle on that, by the way?

MS. MILES: April 21st.

MR. CLEMENTS: Sixty days from today.

CHAIRMAN WOOD: That's the Battle of San Jacinto Day. That's a special day for Texans.

(Laughter.)

CHAIRMAN WOOD: It's a state holiday where I come from. Somehow they don't get it up here.

(Laughter.)

CHAIRMAN WOOD: We will have our Closed Session starting at 1:30 in Hearing Room 6. Meeting adjourned.

(Whereupon, at 12:25 p.m. on Thursday, February 20, 2003, the Open Session of the Commission Meeting adjourned.)