

BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

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IN THE MATTER OF: :

CONSENT MARKETS, TARIFFS AND RATES - ELECTRIC :

MISCELLANEOUS ITEMS :

CONSENT MARKETS, TARIFFS AND RATES - GAS :

CONSENT ENERGY PROJECTS - HYDRO :

CONSENT ENERGY PROJECTS - CERTIFICATES :

DISCUSSION ITEMS :

STRUCK ITEMS :

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817TH COMMISSION MEETING

OPEN MEETING

Commission Meeting Room

Federal Energy Regulatory

Commission

888 First Street, N.E.

Washington, D.C.

Wednesday, January 29, 2003

10:34 a.m.

APPEARANCES:

COMMISSIONERS PRESENT:

CHAIRMAN PAT WOOD, III, Presiding

COMMISSIONER NORA MEAD BROWNELL

COMMISSIONER WILLIAM L. MASSEY

ALSO PRESENT:

JANE W. BEACH, Court Reporter

OPEN SESSION

CHAIRMAN WOOD: This is the open meeting of the Federal Energy Regulatory Commission will come to order to consider the matters which have been posted in accordance with the government and the Sunshine Act for this time and place. Please join us in the pledge to our flag.

(Pledge of Allegiance recited.)

CHAIRMAN WOOD: All right, folks. This is the first anniversary of our wonderful Secretary being at the Commission. We hope for many more. I want to just say we're in the process now of continuing the clean up on the Commission's backlog, and so over the next several weeks, several open meetings and notationally we're going to try to get caught up on as much we can all of the prior items that are just awaiting Commission action. So you'll see some of those in this meeting, and you'll see plenty of those at the next meeting. I just want to make an open invitation to the public. If by Easter you haven't had action on something you really care about, I want to hear about it, so please let us know.

Sorry we started late but we were able to get a few items put over to the consent agenda, so with no further adieu, we'll let the Secretary tell what those items are.

SECRETARY SALAS: Good morning, Mr. Chairman, good morning Commissioners. The items that have been struck

from the agenda since the issuance of the sunshine notice on January 22nd are as follows:

E-1, E-3, E-7, E-14, E-21, E-35, E-36, E-43, G-3 and G-6.

The consent agenda for this morning is Electric Items E-2, 4, 5, 6, 8, 9, 10, 11, 13, 15, 16, 19, 20, 23, 24, 25, 26, 28, 29, 30, 31, 33, 38, 39, 40, 41, and 42.

Miscellaneous items and one gas items. G-5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 17, 18, 19, 20, 21, 22, 23, 24, 25, 27, 28, 29, 30, 31, 32, 33, 34, 35, 37, 38, 40, 41, 42, 43, 44 and 45.

Hydro items H-1, 2, 3, 4, 5, 6, 7, 8, and 9.

Certificates C-2, C-3, C-4, C-5, C-6 and -7.

The specific votes for some of these items are as follows: E-40 Commissioner Brownell concurring. E-41 Commission dissenting. G-21 Chairman Wood concurring. H-9 Commission Massey dissenting, and Commissioner Brownell votes first this morning.

COMMISSIONER BROWNELL: I noting the concurrence on E-40 and the dissent on E-41.

COMMISSIONER MASSEY: I with my dissent on H-9 noted.

CHAIRMAN WOOD: And I with my concurrence without statement on G-21.

SECRETARY SALAS: The first item for discussion

this morning is A-4, it's a seams resolution presentation and our guest this morning for this presentation are as follows: From the RTO West Bud Krogh, also from RTO West Frank Afranji, Rich Bayless, Steve Walton, Dean Perry, Kristi Wallace. Also for this presentation from West Connect, Charlie Reinhold and Ed Beck. And from the California ISO Elena Schmid and Armie Perez.

Mr. Krogh will lead the presentation this morning.

MR. KROGH: I'm technologically challenged right at the start. Is that on now? Okay. Chairman Wood, Commissioner Brownell, Commissioner Massey, it's a pleasure to be before you again this morning. I want to thank you very much for giving us this opportunity to report to you today on the progress of the seams steering group western interconnection. This is the vehicle through which the three western RTOs are resolving seams issues in the west. Before getting into the briefing, just so you know who is here at the table before you. The list has been read, Elena Schmid from the Cal ISO, Charlie Reinhold from West Connect and Armie Perez to my far right from the California ISO. Rich Bayless and Frank Afranji from RTO west and Steve Walton from RTO west.

When we get to that portion of the briefing on planning, Dean Perry will be joining us on the table and on

market monitoring, Christie Wallace, also with us will be joining us at the table.

Let's see, we have the slides. Go to the next slide.

(Slide.)

The basic nature and structure of RTO west or rather SSG-WI has not changed since we first briefed you I believe it was in November of 2001, Mr. Chairman, in Seattle when you and Commissioner Brownell and we presented SSG-WI as it was in its sort of infancy at that point. Since that time we have been functionally actively as a seams discussion forum for the three western RTOs.

I wanted to be clear at the outset that SSG-WI itself is not a decisionmaking body, it is a discussion forum that has been set up by the three RTOs to enable each one of them to meet their function eight requirements under order 2000 which is interregional coordination. So as each of them deals with these seams issues as they arise in the development of those market designs for those RTOs, they refer the seams issues into the segue process. And Elena Schmid will go through the process as we have structured so you can understand how it works.

The other point that I wanted to make is that I know two weeks ago, you had before you some of the senior executives from the northeastern RTOs; I believe New York,

New England and PJM. They gave, as I understand it and having looked through their slides, some very detailed presentations on seams issues that they had been working with for some time. These RTOs or the ISOs in the east are mature. They've been operating for a very long time. They have a history of working together as I understand it, and they are able to go into details that the western RTOs are simply not at that point to present to you today.

The western RTOs are still in a development stage, all three of them. One the California ISO far in advance of the other two RTO west, and West Connect, but I think it's important to understand the different stages of development that we find ourselves in for those you came before you two weeks ago.

However, this also gives the western RTOs the opportunity to resolve seams issues as we move along, and before they become more difficult to solve later on. So there's some advantages being where we are today but we're simply not at the point where some of the other ISOs that have come before you to discuss seams are.

I think on the 8th of January you received our report to you which included the memorandum of understanding that was executed on the 5th of December by the three RTOs. This represents a strong commitment by the western RTOs to work through the segue process as the principal means for

addressing seams issues.

With the next slide, could we go back to the organizational chart?

(Slide.)

MR. KROGH: This basically is the same structure that was presented to you a year and a half ago. We have made a few changes in the number of work groups.

You can see that we have five workgroups that are currently in place: Transmission Planning, Market Monitoring, Price Reciprocity, Common Systems, and Congestion Management.

You have had some presentations here, I know, from Don Watkins, who is the Chair of our Common Systems Interface Committee. He's not with us today.

Frank will be able to respond to some of the questions that you may have about what CSIC is doing. We're still working our acronyms. He's got a subgroup called Business Architecture Development, and we told him to take BAD off of this.

So we have -- Don is not here today, but Frank can answer questions regarding CSIC. I'd like to make the point that these are the workgroups that we have in place today.

It may be that there will be issues that we need to address in the course of development that will require another workgroup to be set up.

The steering group itself, that's one of its assignments, in working with the RTOs, is to decide what workgroups do we need to set up, so that we can address these seams issues most effectively. These are the ones that we think do encompass most of the issues that we have to deal with in seams today.

Now, I'd like to turn to Elena Schmid, who can brief you on the process.

(Slide.)

MR. KROGH: I know that this chart looks a little complex, and there are a lot of arrows, but I think it will work out so that we can all understand it. Elena?

MS. SCHMID: I assume that you have the chart in front of you, since it's not now up on the screen, but I'll walk you through it as best I can, starting in the upper left, which is where we have the three RTOs, and as Bud indicated, they are the ones that make the final decisions.

So we will move around, basically in a circle, showing how we get feedback into the RTOs, but that it's the RTOs that make the final decisions.

So, Box No. 1, towards the center, shows the issues to be identified for discussion. Those issues are going to come from a variety of sources. They will come from the stakeholders; they will come from the steering group itself; they will come from the RTOs.

As we begin to look at the issues, begin to identify what may make a difference as we cross the seams, then it will go to the steering group to begin the initial discussion. And it's at the steering group that we move to Box No. 2, over on my right-hand side, where we had the initial formation and the ongoing direction.

So, at some point, we say, okay, there's enough here that it needs to go to a working group, the working groups basically being the technical groups who can begin to dive into the issues and to begin to look at the issues.

For the working groups, we'll do an initial cut at what is the issue, try to define the issue, give them some ongoing direction on the kinds of things that we're thinking about at that point, give them a schedule that says this is when we'd like you to come back with a recommendation or to at least lay out some options for us.

That then goes to the working groups. We'll also be the ones that appoint the chair of the working groups.

The working groups are public participation, wide open, anybody can go. We've actually had very good participation in most of the working groups.

They then will work through whatever issues that they see that come. If, in fact, they want to broaden it or they want to focus it from what the steering group has given them, because we ask for periodic reports, we go along with

them, we listen to what their concerns are, so it's an iterative process between the steering groups and the working groups.

Moving then over to Box No. 4, after due consideration amongst the working groups, they come back to the steering groups and make some recommendations, or lay out some options. It's at this point that the steering committee will do a couple of things:

We'll listen to what they've got to say, listen to the pros and cons of the options that are there, but we also have to keep in mind, the integration of the issues; that as one group will come forward, the Planning Group or the Congestion Management Group, we have to make sure that whatever recommendation they are coming forward with, fits into other things that are going on at the time.

So part of our responsibility is to do the integration of the issues at that point.

CHAIRMAN WOOD: Let me ask a question about the dynamic of those, having moved through those at ERCOT. It's an important dynamic at the level where a lot of key policy issues are getting hashed out.

In the room, is there a diversity of opinion that is driven by something other than the economic interests of the participant's employer? I'm trying to think, is this kind of stakeholder kind of California ISO Setup Part II, or

is it -- you went through that, didn't you, Elena?

MS. SCHMID: Sure.

CHAIRMAN WOOD: Is it similar to that and just bigger, or is there something qualitatively distinguishable?

MS. SCHMID: And you're talking about the working groups, or are you talking about the steering group?

CHAIRMAN WOOD: Well, the interplay of both. The process that's used to create a decision, is there kind of a west-wide perspective that's taken on the answer, or is it kind of the three of you all?

MS. SCHMID: I think it goes to probably the degree of experience. So, the Cal ISO probably brings some depth of experience, of operations experience to the discussion that is a little bit different than what other people bring.

So there's already immediately a diversity there. Everybody is going to come at it from their own point of view and from their own either experience of how it operates now or how they think it would operate under an RTO, so there is a different level there.

I think that we are in a little bit of a different situation since we have formulated the market design, and RTO West and WestConnect are still developing their's, and so there is a difference of how we approach the problems. That is sometimes where you can get into this is

as far as we've gone and we can't go any further on this particular issue.

So I think that there have not been a lot of issues that have come back to the steering group for final resolution, but in the iterative process of going back and forth, the discussions have been open. There have been a number of issues that have been put out there, but it's been difficult.

At this point it would be difficult to say exactly how the diversity is going to come about when we come to a final decision.

CHAIRMAN WOOD: So are the people participating, employees of the three RTO/ISOs, or are they stakeholders from the individual companies and other market participants, or a mix of both?

MS. SCHMID: If you're talking about the steering group, it is the representatives of the organizations, of RTO West, WestConnect, and Cal ISO. The chairs of the working groups always participate, but they also -- I think that at this point, they are all members of an RTO or employees of an RTO.

MR. KROGH: No, Wally is not.

MS. SCHMID: Wally is not, that's correct, so one is not.

And what they are doing is that they are also

bring, the chairs are bringing to the steering committee, the stakeholder comments, because we ask what was the discussion, what were the pros and cons, who put them forward, and that kind of thing, so that we're getting the stakeholder input via the chairs at that point.

CHAIRMAN WOOD: And as to -- as the RTO West and WestConnect participants on the steering committee, who are those folks. Are they still employees of a public utility?

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MR. KROGH: Yes, they are. They are employees of the respective utilities, like Frank is an employee of Portland General Electric, Rich is with Pacificorp, Akut Mansur, who is not with us today, is from BC Hydro.

Also, in terms of the stakeholder participation, Mr. Chairman, I will get to that in Slide 6. We have opened up the steering discussions to full stakeholder participation. I will get to it in a minute, but we did have a meeting where everybody attended.

And these are all interests; everybody is invited to come to those sessions.

MR. AFRANJI: If I may, I think that if you look at the workgroups, all the workgroups are open to all the market participants, so you have vendors, you have IPPs, you have state commissioner staffs. So the working groups are really open to the entire industry.

CHAIRMAN WOOD: And that's fine, but I think where I'm going is that I kind of want to make sure that there is somebody looking after something other than the individual interests of a company and just the individual interests of the RTOs, since what we're interested in and what kind of kicked off our, I think, attempt to empower SSG-WI to a higher level, was the thought that there might be a western market design, perhaps, that looked different than the one we were contemplating.

And, if so, is somebody looking at this is what's good for the west, as opposed to this is what's good for my organization?

MR. AFRANJI: At least I can speak for RTO West. For RTO West, the decision has been made internally that as we sit and discuss issues at the RTO West, we can bring up our individual company issues. But once a decision is made there, then when we go to the steering committee of SSG-WI, then we're representing the interests of RTO West, rather than our individual companies.

And I can't speak for the rest of the folks, but that's the situation in RTO West.

MR. KROGH: Your question, I think, Mr. Chairman, went more broadly to --

CHAIRMAN WOOD: That's the right direction.

MR. KROGH: That's the right direction. We're

moving from company to RTO, but then to the western perspective. Steve, would you like to add to that?

MR. WALTON: I think that in large measure, the individuals and the committees and the working groups that I have been on, have been thinking about how do we make this work across the system? How do we get a transaction that goes from here to there? What are the pieces that have to go together.

And certainly the marketing companies that are participating think in those terms, so I think that that's kind of what we're working towards as individual workgroups, is, how do you do the transaction that goes from a coal strip to California or from Arizona to the Northwest, or vice versa.

COMMISSIONER BROWNELL: But nobody -- picking up on Pat's theme, no one -- at best, you're getting three RTOs' vision, ISO vision of the world. There isn't the steering committee or a group that says a western market design might be preferable and it would contain the following elements; it's each of the design elements of the three RTOs have to be reconciled in some way.

MS. SCHMID: If I may, I think that that's right. I think that as we begin to formulate the Seams Steering Group, it was that if we want to maintain our individual designs and have integrity within our individual designs,

what is it that we need to do to ensure that the seams are not a barrier?

So we looked at it as either an overlay, an integration or whatever, but we looked at it as taking the three designs and trying to work in such a way that they can come together. And that was a different starting point than saying shall we start with a western market design and figure out how to make a western market design.

So I think those are two different starting points.

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MR. BAYLESS: We've got kind of a predicament in that we've got a lot of parties in the Northwest coming together under our DOS. They really can't afford to go to a whole other parallel performance. We have asked the stakeholders to figure out a way to do it such that there can be sort of a representative stakeholder input to the SSG-WI stakeholder process so we can get that fixed, so we're sort of walking in parallel with the RTOs doing their design, trying to come together and identify places where they need to fit on a SSG-WI level and not try to trample on the stakeholder processes that are very fragile and the RTOs that aren't done yet, sort of the dynamics we have to go through.

MR. KROGH: Charlie, you want to take on --

MR. RHEINHOLD: Certainly as far as the initial question from West Connect on the Seam Steering Group, we have two of the members are jurisdictional, represented as jurisdictional utilities. I work for the interim committee. I'm hired by the group which includes the Salt River Project as a non-jurisdictional entity as well.

So although I'm looking at my perspective is implementation of the RTO efforts. That also includes stakeholder views to the extent that they're made known through primarily the previous West Connect processes and we have yet to restart a formal stakeholder process following

the orders that we got from the Commission last fall.

CHAIRMAN WOOD: Just to set the pattern for the two that aren't set up yet, where are we on it seems to be getting aboard and getting some decisionmaking authority and getting a budget and all that is a good way to kind of facilitate getting decisions made. I'm looking down on the chart here. Well, it's gone. At item number 6, proposals from the Steering Committee go to the different RTOs, how do we get decisions made. I mean we've got a board and management there. But where are we, Bud, on that? I can't remember from the orders that we got.

MR. KROGH: With RTO West, we do have a filing utility group, we have a corporation that's designed to put together the filings to come to you. At present, when we would get a proposal from the steering group, it would go to that filing utility group for consideration. We would get stakeholder input on that, and that board or group would make a final determination. It does it in conjunction with the regional representatives group with is the stakeholder group in the Northwest that's been very actively engaged with us over the last two years. But it would come to that group. That's the final sort of decisionmaking point for RTO West at this point is that filing utility group.

And Charlie, I'd have to ask you to describe the interim committee for how that works with West Connect.

MR. REINHOLD: For West Connect, we have an interim committee composed of the five transmission owners that are funding the on-going efforts of West Connect formation. Through the name, we recognize they are an interim step for decisionmaking until the limited liability company is formed and we have a formal board of directors. And certainly they recognize the limitations --

CHAIRMAN WOOD: What's the time frame for that effort?

MR. REINHOLD: Frankly we're still trying to determine what the time frame is. We have a meeting of the chief executive officers of the transmission owners upcoming next week, and we expect to be a little more formalized in what that time line would be following that meeting.

CHAIRMAN WOOD: And just to kind of put on the table, my interest in, and my colleagues would probably, agree is that ultimately the balance market rules when they're developed and ratified through a process that meets our independents standard are a lot easier are to assume are going in the public interest direction. I think our experience with non-independents has been pretty unidirectional that's not where we want to go. That doesn't result in good decisions, good outcomes, and usually results in spending a lot more money than we need to.

So I'm really looking on down the line here after

we get through step five here and it goes back to the yellow boxes, our independent entities they're making those decisions with the best interest of not only the RTO but of the Western Interconnect in mind. If that is the answer to that is yes, than our job gets really simple. If the answer to that is, well, no we're not there yet, then our job is still to be pretty intrusive and pretty hands on here. So any progress we can make in all ISOs toward that kind of independent decisionmaking with a broad view toward the public interest and that starts to really make this process a whole lot more effective I think.

So that's kind of my mode of preaching and I'm sorry to interrupt your wonderful presentation.

MR. KROGH: Okay. Elena did --

MS. SCHMID: I think we're actually pretty close. We did five. That's when the working groups to have the reports or recommendations to the steering group, listen to that, take those then, bring it back to the individual RTOs for the decision. That then would mean that we would have to do the filings that the RTOs/ISO would do the filing individually and we would ensure that they're coordinated practices, coordinated rules that the implementation of whatever it is we filed for you is put in place. So that takes you complete circle all the way around.

MR. KROGH: Maybe we could move to the next

slide, and Charlie could talk about making it work.

MR. REINHOLD: Certainly. In my moment of rebuttal to the moment of preaching earlier, in the west we do have a history of getting together, even absent FERC direction, on some issues of trying to resolve critical issues throughout the West. And some examples that we have, certainly loop flow has been an issue in the West in the past and we put together the unscheduled flow mitigation program which was brought to the Commission by the Western Systems Coordinating Council for its approval. And that certainly deals with loop flow issues and operation of * throughout the West.

The formation of the Regional Transmission Associations was completed regionally and certainly in hindsight, a couple of years ago, we recognized that some adjustments were needed there and we've recently merged two of those regional transmission associations with WSEC to form the Western Electricity Coordinating Council.

Another issue that was brought to this Commission for approval was a reliability management system which was a contractual effort to ensure the reliable operation of the system throughout the West. So we do have some history of working together and finding solutions in the absence of a single cohesive organization throughout the West.

An additional point is that there is an inherent

feedback look between the SSG-WI efforts and the RTOs. Certainly we are us in working on these problems. Another critical issue we have facing us in the West is just the large preponderance of non-jurisdictionally owned transmission assets and we've got to find ways to accommodate that within all of these deliberations.

And as we're going on with this, what we do need from --

CHAIRMAN WOOD: Are they being included in the work groups and all?

MR. KROGH: Yes, they are.

CHAIRMAN WOOD: I don't know who they are. I mean I think they're in there. Is there something that you all have heard as people in the leadership of this effort from the non-jurisdictionals about this process? I mean are they positive, negative, neutral about the SSG-WI process as far as how to resolve these broader market design and interregional coordination issues?

MR. REINHOLD: Within West Connect, the non-jurisdictional entities participating with us are in fact are participating and they are enthusiastic in working towards resolution of the issues through the SSG-WI work groups.

MR. KROGH: And with RTO West and the Bonneville Power which is non-jurisdictional is a very active, major

part of the filing utility group. Participates in all of the work groups and Sid Burweger is an alternate on the steering group itself from Bonneville. We've also had strong support in terms of the work group work from a number of the large publics in the Northwest that are non-jurisdictional, the City of Seattle, Snohomish, a number of the public utility districts. They participate. I think they acknowledge that SSG-WI is the entity for trying to resolve these seams issues in the West but yes, they have come. And BC Hydro obviously yes. It's a huge entity, a very critical part of RTO West filing utility group, and they've been actively engaged for the last two years.

MS. SCHMID: And California ISO cannot have a meeting without the public's being present and participating actively.

MR. BAYLESS: The only concern we may have heard about in the Northwest is that we don't inadvertently get drug in to some market design that we haven't been able to come to agreement on in the Northwest through the SSG-WI process. We're having a very fine line. In that regard, especially as we talk about timing of the three RTOs developing.

CHAIRMAN WOOD: Is that most I guess of the five work groups in the congestion management side?

MR. BAYLESS: Yes, sir.

MR. KROGH: And we're going to go through each of the work groups so you can see.

MS. SCHMID: I think it also comes up in the systems in the CSIC part.

MR. KROGH: Charlie, you want to finish that slide?

MR. REINHOLD: The only other points I have on this particular slide is we certainly appreciate the flexibility that the Commission has given so far in allowing us to find a design that works in the West. Given your views on the need to continue to push prior to full independence governance of the RTOs, we certainly appreciate that and I think we need to continue to have the time and the ability to work through these issues.

And additionally we do have FERC Staff participating in some of our work group efforts. We certainly want that to continue and in fact expand into other work groups as the interest appears both from the Commission and I think is appropriate is the levels of issues are discussed within those work groups.

CHAIRMAN WOOD: They'll be there.

MR. KROGH: Okay, next slide.

(Slide.)

I think we've already addressed most of these points, Mr. Chairman, about the work groups being open to

all stakeholders. We had the first open meeting of the Steering Group January 21 in Las Vegas. We had 50 people attend in addition to the Steering Group, people from all over the West. We're going to rotate these meetings around the West so that we can have people can come to those meetings who maybe can't travel a very long distance, so this was in the relative Southwest area. We'll have some in California, some in Portland. We're going to be moving those around the West over the next few months.

Commissioner Brownell?

COMMISSIONER BROWNELL: I know that there's some state commission staff involvement on the working group meetings and then there's CREPC is kind of looking over the shoulder as the policies develop, reserving their rights to do what they need to do in their individual states.

I think there was a recent meeting of CREPC to talk about some of these issues. How did that go? What's the involvement of the state commissioners at this point?

MR. KROGH: Well we had a SSG-WI, had a meeting with CREPC last fall and it was well-attended. In terms of how they are going to represent the states, the state PUCs, I don't think it's been completely worked out just yet as to what kind of entity will do it. The members of CREPC, the Committee on Regional Electric Power Cooperation, told us that they're there representing themselves individually, not

CREPC as a group.

And I think there was a meeting in California a couple of weeks ago where Marsha Smith did describe -- one of the Commissioners from Idaho PUC -- some of the organizational efforts they're going through right now to structure state participating with SSG-WI when working out these seams issues. I haven't heard specifically how that is evolving but I know that's something that's on their list right now. You probably have heard more about that than I have.

COMMISSIONER BROWNELL: A little bit but I'm just trying to get a handle. Shelton, maybe you can tell us more about recent meetings and the involvement of state commissioners throughout the Western Region?

MR. CANNON: Well pretty much what I have heard dovetails very closely with what Bud just described that there's a sense that they want to participate but they haven't really defined how and I think there's this sense that they want to keep their powder somewhat dry in terms of subsequent decisions they'll be called upon to make in their PUC role.

That said, my reaction to the whole process chart is we need to try to figure out ways not only for this Commission to become involved at a staff level in helping, not to shape, but to make sure that we're comfortable in

giving whatever guidance we can in terms of how the process evolves, and I would suggest we also need to figure out a way to get the states to sort of play that same kind of role because as excellent as this process looks, I don't think it can be successful without a real firm sort of handshake between what we're trying to do and what the states are trying to do as well.

COMMISSIONER BROWNELL: So that when there are CREPC meetings and at the meetings where state commissioners are involved, there's full involvement from most of the states from different regions at the commissioner level?

MR. CANNON: That would be what I think we should be trying to aim at but I'm not sure we're there yet.

COMMISSIONER BROWNELL: Thank you.

MR. KROGH: Commissioner Brownell, just on that point, I think we can work together on how to engage the states with us because I think we acknowledge that we have to work, go forward in partnership with the states as best we can in this process.

The final point on this slide is that we asked the stakeholders to submit some proposals to us as to how they would like us to organize these open meetings of the steering group, and we've given them until this Friday to get reports back to us, proposals back to us. We're going to post those on our Web site, and then start working with

them to set up the next meeting. But I think that's underway and that was in response to direction that we got from you all on your September to RTO West.

Next slide.

MR. AFRANJI: I won't spend a lot of time on this slide because basically it summarizes the January 8th report that we have filed into you and we understand that you have taken a close look at it, so I'll spend about five seconds for the folks that didn't see this report.

What the purpose of that report was to basically highlight the seams issues that we're trying to address through SSG-WI in the West and to detail the work plans as to how we're going to address those seams issues. And to give somewhat of a timetable on when we're going to be addressing these issues. So you have that report.

Just in a nutshell, that report dealt with four different elements and those are to start with, we wanted to reiterate and emphasize the constant of SSG-WI and that is that SSG-WI is not the decisionmaking body and you've heard that already, but it's basically the entity where proposals are made and discussed and then sent back to the RTOs for decisionmaking.

The second part was we summarized the memorandum of understanding that was signed by all three RTOs and detailed some of the coordination to date with some of the

states such as the meeting that we had with CREPC and the various commissions.

The third is we basically provided you with a summary on the current activities and what we hope to deliver, what are the deliverables in the year 2003, this year. And there were many other issues that we basically, some incidental, some very important, that we detailed in that report.

MR. KROGH: I think getting into the details of implementation work during 2003, and we understood that that was main issues that you wanted us to address and I'd like Steve Walton to go through this next slide, is slide number eight, which are the milestones for 2003. Steve?

(Slide.)

MR. WALTON: Okay, there are more detailed layout of the milestones in the back of the report and beginning at about 28. This is a summary that indicates by quarter approximately what the major issues are. Of the five work groups, all of them are presently working. The congestion management group is intending to put out quarterly reports of each of the quarters.

The first quarter, the effort is focused on identifying what the issues are and we'll cover that more in detail later, and towards getting a common proposal by the end of the third quarter towards into the fourth quarter.

The planning work group and the others are also laid out here, and each of those groups, as they make reports this morning, will cover those issues.

(Slide.)

MR. KROGH: Okay. And then the next slide on sequencing development, Rich?

MR. BAYLESS: Okay, here's where we're sort of walking on top of the fence trying to figure out how to, at least in the two that aren't done yet, get the RTOs markets designed and set up. At the same time make sure that the three market designs are compatible where they need to be and standardized where they need to be.

Each of the other three RTOs has very distinct jurisdictional issues, percentage of non-jurisdictionals. We've a very large percentage in the Northwest, and we're striving to set up a market design that we can get voluntary participation from all and have them join. So we're focusing on getting those market designs done as best we can, and trying to retain the flexibility and the deference that we need for the individual RTOs as well as the way we make them all fit together in the west.

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What we are trying to do is do the individual market designs while at the same time the SSG-WI activities are looking at how they meet at the seams and where they're compatible and where they may need to be standard across the seams.

And that's sort of our sequencing problem with the timing of the individual RTOs. But we think it's the best way to proceed, and you'll hear from the work groups in a bit on how that's working.

I think that's pretty much all I need to say in this slide.

(Slide.)

What will happen out of the work groups is as they see and look at the three individual market designs and see how they fit, they'll be coming back to the policy group with recommendations on what needs to be fit together better, what's compatible and so forth with solutions. And we'll be taking those back to the RTOs and working on getting the designs to fit.

So we've sort of got a parallel process going on, one that's somewhat fragile in some of the areas, and that's sort of the sequencing problem we've got.

COMMISSIONER BROWNELL: So I just need to get clarity here because I've heard mixed reviews on the impact of the seams group on RTO development, and we don't want to

be dealing with unintended consequences here.

Is the seams process, which has been going on for quite some time, in some of its new responsibilities from us, delaying the RTO development? And any of you can comment on this.

MR. BAYLESS: I'm not sure it's delaying anything at the moment. We're a little concerned about what might occur as we get down the road on our timeline with the different rates the individual RTOs are going. I think we're moving on both parallel processes as fast as we can, so I don't believe it's delaying anything yet.

MR. KROGH: Commissioner Brownell, I know that you've addressed this question before and expressed --

COMMISSIONER BROWNELL: Endlessly it seems.

MR. KROGH: And concern that the SSG-WI process would somehow impede or delay the work of the respective RTOs. That is not our intent at all.

COMMISSIONER BROWNELL: Intent, I understand intent. In practice, is it happening?

MR. KROGH: I think I would let the individual RTOs speak to that. Elena?

MS. SCHMIDT: Well, certainly for California, we're marching forward as quickly as we can to get our implementation in place, market design having been thought although always iterations as we look at the implementation

details.

SSG-WI is not in any way that I have been aware of delaying the implementation of our work. We have some of the same people going to some of the working groups, but mainly we have different people going to the working groups. So even on a resource call, it is not impeding the work.

COMMISSIONER BROWNELL: Good. Thank you. I can sleep at night. Charlie, now the ball is in your court.

MR. REINHOLD: From WestConnect's perspective, our major efforts right now in formations are getting local approvals done.

I see the SSG-WI efforts as an iterative process as we reach agreements and understanding on the three different market designs and how they might meld together. We then will have to adjust what eventually will be the WestConnect market design. But at this point it's all still at the rather conceptual level, and we're not investing time and dollars in actual software/hardware design.

So I think the efforts will minimize in any redesign later on by dealing with it up front now on a conceptual level. And we frankly see a lot of meetings for the work group efforts from SSG-WI. We've got folks pretty much involved in that. But I think it will be productive in the final analysis, and at the end of the process in getting a cohesive WestConnect market design, however that might

change based on the decisions reached or conclusions, through the SSG-WI process.

MR. AFRANJI: From RTO West's point of view, I really look at it differently. Without SSG-WI, there isn't going to be a compatible market in the West. And in order to have a compatible market in the West, I think SSG-WI will reduce the time of getting the RTOs to move forward. Because otherwise we're going to end up with three incompatible systems possibly. And if that happens, then we're going to have to spend quite a bit of time trying to get to one compatible market.

So in essence, the way we look at it is it's really cutting down on the time that is going to create a compatible Western market. So my views are different on this.

COMMISSIONER BROWNELL: Certainly the issue of a compatible Western market has been a top priority for all three of us. But so we now kind of have it etched in stone that we won't see a filing from any of the RTOs in here saying we've got to delay because we're working on SSG-WI. I just wanted to be sure we all understood that.

MR. BAYLESS: We see SSG-WI as helping us get to a compatible market faster than we would if we all went to our corner. We just have to be careful not to get caught in a trap where we get drug into a market design that one of

the RTOs can't live with and some of the big parties that need to be a part of the RTO fall off. That's the only hazard we have.

COMMISSIONER MASSEY: Are you talking about getting dragged into an LMP-based market? Is that really what you're talking about?

COMMISSIONER MASSEY: Well, LMP is a very broad term. Its provisions under the market design, it may adopt certain provisions of LMP. There's a lot of wrinkles to it. But we have one party that's connected by a big river and they claim it's too little storage and they can be manipulated by other parties, and some parties believe they got too much storage and they can be manipulated depending on how you structure the day-ahead market.

And it's not necessarily the same in all the RTOs. And we just have to be careful that we can meet those. We believe we can, and that we don't get put into a position where one party can't live with all the terms.

MR. AFRANJI: If I may, let me just add one little point to give you an example of how in some cases it's speeding up the process.

For example, the folks that are working on the systems developments, there is cross-fertilization. There are entities that are ahead of other entities. So in essence, it's cutting down the time that's going to be

needed for system development and process development in those cases, because people are picking up the experience of the others. And in this case, this specific example, it really is reducing the time that is needed to get the RTOs up and running.

MR. KROGH: Mr. Chairman, I'd like to now, if we could go through the work groups, specifically the Congestion Management Work Group and the Planning Work Group, Market Monitoring, which are our three principal ones that we were going to emphasize today, and then we'll have some follow-up and price reciprocity in the common systems interface.

Steve, do you want to start with congestion management?

MR. WALTON: Yes.

(Slide.)

The first slide, Slide Number 10, lays out the purpose. But I think another way to shorthand that purpose is to say, at least from this work group, this particular work group, is focused on the notion that you have to be able to make transactions across the boundaries and they have to be executable. They have to be practically able to do it.

So the question we've been focusing on is how would a transaction occur, what steps would have to be. If

there are different congestion hedges in each one of them, what do they have to be, and how do they fit together. So we're really focused on trying to make these, how the transactions take place across the seams.

And we're conscious of this, because if you look at our flows on lines in the West, even during the crisis, you'll see energy moving back and forth on a daily basis from the Northwest to California and vice versa. Everyone I think for at least my whole working career, I've been dealing with how do we sell to buy from California back and forth in the various companies that I worked for.

(Slide.)

Turning to Slide 11, then, the framework of the work that we're doing as to congestion management is that each of the RTOs has conditional approval for the various approaches so we're attempting then to eliminate and mitigate those seams issues between them and figure out what matters.

The goal is a consensus proposal, but I think the question is what key issues matter? What issues have to be the same or where do we have to meet, and what things can be different? What differences can we have?

CHAIRMAN WOOD: What's the answer to that?

MR. WALTON: That's the next slide. Thank you.

(Slide.)

These are the three issues where we have focused on, trying to analyze where we think the key issues that we need to talk about. The first one is whether we -- and Slide 12 is the question of a mixed model. WestConnect is largely a physical model where RTO West and the California ISO are both operating on what we call the financial model, meaning that they're locationally priced, you can say LMP or locational prices, however you want to use the term. But they're based on those, which means that the rights in those two are based on spread of congestion price, and in WestConnect, they're trying to manage congestion based on schedules through them.

Now to some degree we've always had a mixed market in the system. We've always had a dual model because inside each individual control area, they made decisions on a price basis. They said inside of our control area, what do we dispatch next? How do we use this? Between them, we've used a physical model. Now we're actually compressing some of those up to where we have three systems.

And so the question has to be then for us is what are the implications of using the mixed model? Can we continue to stick with the mixed model we have, or is there a way that we can accomplish this that allocates the transmission efficiently that uses these two models? Is there a way to build connectors that can connect WestConnect

and RTO West together in such a way that we accomplish what we want to, even though we start from different models?

So that's the first issue.

The second one is to determine, to the extent that we need to use redispatch among ourselves, do we need to come to a single set of congestion clearing prices at the border.

One of the questions, even if the parties have different hedging instruments, if at the border they came to the same price, so that when I look South from Cobb or look north from Cobb, that I as a marketer would see the same price, then I can hedge up to that point with one instrument from the other -- there's another instrument, and it really doesn't -- it doesn't mean that I -- I just know what the rules are, then I can execute that as long as there's some way for me to control my risk across the seams boundary. Certainly that's an issue.

So we're looking at the question, is there a way to get to a single set of prices? Is that single set of prices needed? How do we pull them together? How do you get them to converge? This takes us back again then to the physical model. If they have a physical model, is there a way we could do a price overlay and address the seams issue on a price basis, or do we need to go to flow-based scheduling, which is a way to handle it on a flow basis?

So those are the two major threads of the discussion that's underway there.

And then finally we have another issue that goes to the physical model each party uses. It's referred to here as different granularity. But another way to look at it is when each system is looking at its own system and it's optimizing or doing its dispatch in its own system, how does it recognize the rest of the system? What physical model does it use when it looks outside of its system?

This is particularly important in the West because although we're actually, the number of interconnections, given the size of our load, is quite a bit higher. I think it's maybe two or three times as high, you know, when you measure the interconnections against the total load is there are in a lot of the other parts of the country. Because we only have about 120 megawatts of total load, but we have interconnections on the order of 10,000 megawatts among all the parties, or higher.

So it's a fairly high number. So we're all conscious of the fact that when you schedule from coal strip to NP-15 in California, that a certain percentage of that is going to go through WestConnect's system. Most of us cut our teeth arguing about loop flow back in the seventies, so this isn't new information to us. We're trying to find another way to attack the same problem that we've been

spending our careers at.

And so the question here is, for this last bullet, is how do you recognize that. And so I think we've all come to the conclusion that you have to have what we call the closed loop. You have to show the entire loop. So the question is how big should the model be? How do we get to a common model? Is there data exchange should occur from hour to hour or should it be done day ahead to line the systems up fairly close to each other day ahead and then allow them to individually dispatch into real time and minimize the amount of problems up front.

So that's another modeling area where we have the area. So those are the three primary areas where we've gone to look right now is the mixed model, the question of whether we need a single set of prices, if that will work, and then the issue of how do we get a model so that each of us looks at the world the same way.

CHAIRMAN WOOD: Let me step back to the prior page, the assumption that our conditional approval of differing CM approaches is kind of like etched in stone.

I think our thought was these look different. Let's get SSG-WI to put together as to what's the best approach. Is there one that works that accommodates the hydro of the north, that accommodates the long lines of the Southwest and of the Rocky Mountain West, and that

accommodates the difference in the California market, rather than trying to justify three different ones and iron them across, it looks like that it really is just looking at how to make decisions that quite frankly aren't that firmly made in any of the three.

At that point, that's why we thought SSG-WI quite frankly could be more helpful is that people weren't concreted down on the specific details of how the LMP should work, or how congestion management should work, that maybe a comprehensive method that doesn't require a whole lot of I guess page 12, I kind of characterized when I heard you describe them, Steve, is excuses, band-aids and workarounds. I mean, in software, that usually spells, you know, computer crash.

MR. WALTON: Well, yes. Especially if you do it after the fact. What we're trying to do in advance of this is say, for instance, if there's a way we can resolve the problem -- people have preferences for the way they'd like to go about it. WestConnect certainly has a preference for using a flow-based model.

If there's a way -- if we can find a solution that instead is an overlay that resolves the issue between them so that we have the best solution. If each individual optimizes on their own and then we put the three together, the likelihood it is everybody will be better off.

And certainly there's some work others have been working on along the same line. And so the intention is to acknowledge the fact that people have preferences but then to go out and look and see what's the best attack for bringing the three together. And the critical issue it seems to me is, is can you do a transaction? Can you do a reasonable transaction without a whole lot of headache? Do you have to do 14 steps, or can you have one step?

CHAIRMAN WOOD: But if you've got the three different grids and the overlay, you're paying for two systems per customer as opposed to keeping the cost down.

MR. WALTON: But the overlay isn't really -- when I use the term "overlay", it probably sent the wrong impression. What we're talking about is can we adopt a common approach to how we fit together? So that, for instance, if RTO West comes up with its redispatch in one way or its system model, California comes up with its, WestConnect comes up with its day ahead.

Then in the day ahead process we then exchange that information between ourselves, and the prices, and then iterate one time, do we come to a common set of prices? That's one approach.

There are three separate parties, but because they've agreed to become a process to share the data and exchange the data, it actually converges to the same number.

Now is that an executable possibility? Perhaps. But it really is -- there's no overlay involved so much except to the extent that you have this data sharing up front.

Everybody knows what lines are in service.

Everybody has the same physical model. They may have taken the details, their part of the system out, simplified and put their detailed back in, but they're going to get accurate representations of what happens in the outside of the network.

So it's the details of how to do that or the kind of process we might use to accomplish that that's on the table.

CHAIRMAN WOOD: Just back to the core decision, I mean, we looked kind of across the country and WestConnect's the only people that are really advocating a physical rights model. Why is that?

MR. REINHOLD: In large part, well, WestConnect is advocating is the stakeholder process we went through. The conclusion at the time was definitely a physical rights model was preferred.

It was preferred for the price certainty ahead of time, and it was also preferred in large part because by some of our larger nonjurisdictional entities, who felt that the sanctity of their own contracts, the way their systems were put together, were preserved by a physical rights model

much better than it would be in a financial model.

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CHAIRMAN WOOD: Why would we have not heard that elsewhere in the country? We're hearing it in a few places, to be fair to those that say, gosh, we've got a little problem with this.

But, it just hasn't been as dominant as it has been there. I'm just wondering, what's different about Arizona and New Mexico in that regard.

MR REIHOLD: I don't know what's different. I would think that some of the same issues would come up in other parts of the country. Certainly other PMAs have similar contracts, and the tax implications for private use certainly should be the same in other parts of the country as well.

CHAIRMAN WOOD: Elena, what is different between California and RTO West? I mean, certainly you've got a lot of hydro in California, maybe not as much, but you've got certainly, of anywhere else in the country, you are one and two.

What would necessitate a different approach toward a locational model on congestion pricing between the two?

MS. SCHMID: As I understand what RTO West is talking about -- and I do not know the details, but if I understand what they are talking about, it's probably a question of degree; that we're probably close in what we're

doing, but if we're going all the way to nodal and running it all the way through to the endpoint through real-time, sending the prices out at nodal and real-time, I believe that RTO West does not take it all the way forward.

It's a question of the degree that's being done.

I think we're actually very similar in what's going on.

MR. KROGH: Steven, did you want to respond?

MR. WALTON: Yes, in terms of the locational prices, we're the same. We're going to have a nodal system and nodal prices.

The question is the processes that come up to it.

For instance, in the Northwest, the hydro resource is really the marginal resource. The thermal resource is a baseload resource; it does not follow the load that hydro does.

And because that hydro is largely in the hands, or a lot of it is in the hands of non-jurisdictional, parties have legal implications, and we really need to have a voluntary process, and so there is some of the structure on how you build the market and what obligations are, how you measure market power, and what the requirements are for resource adequacy.

Those are the details where we have differences.

In accomplishing nodal prices, I think we're very close.

MR. BAYLESS: We're trying to stay more towards the transmission market in the Northwest to try to get

around some of these issues, as opposed to an energy market totally. We've got -- our one entity is 80 percent of the market, depending on how you cut it, which is a lot of market power.

Some are concerned about that, if they don't have a must-run provision, for example, because they can't, by statute.

So those are issues that we're trying to work around in our design for those reasons that may be different in California.

COMMISSIONER MASSEY: Am I hearing then really that the toughest issue, to get right down to it, is that WestConnect has such a different model from the others?

MR. WALTON: That's one issue. The other one is, in RTO West, we have not said that we would have a full day-ahead energy market. California said they will, so the question is, when we try to do this alignment, if we do an alignment day-ahead, how do we go about that?

That's where we go back to what I was saying earlier; is there a way that each one could come up with their dispatch, however, and then a common way to redispatch to get the best deal?

MR. BAYLESS: Now, we believe we're designing -- as people move in and actually have to implement and spend money on system and software, we believe we're getting the

design such that it can be flexible enough to adapt as we figure these things out and make them fit.

And that's one of the key pieces we're having to work with as a SSG-WI.

MR. WALTON: And if we can nail down a lot of these issues now, in the next 12 months or so, most of us won't be -- California is in a different position, but the rest of us won't be writing any software.

Certainly, as that system comes up, we will be building those software systems up with this in mind, and hopefully we're avoiding building incompatible systems.

Instead, we're trying to get the theory and philosophy common, so that as we build those systems, they actually work together at the end.

CHAIRMAN WOOD: That's good; that's the goal here.

MR. KROGH: Okay, Steve, do you want to finish these up here.

MR. WALTON: The last item on congestion management was just to mention the two work groups on Slide 13. We've broken it up into two subgroups:

One group is working on scheduling issues, transaction, how will a transaction occur, how do you put it together, what are the problems associated with that? What incompatibilities are going to be difficult, if we -- what

would we have to change?

The second group is looking at -- it's called Modeling, but it's really trying to come up with an example of the kinds of processes I mentioned earlier about how you would bring the systems together.

Those groups are also looking at the modeling issues. That's all.

MR. KROGH: Okay, thank you.

CHAIRMAN WOOD: Can those subgroups get the technical information back to the steering group on a timely basis?

MR. WALTON: What's happening there is that the subgroups, we're saying let's -- everybody can't work on the project. You work on this part; I'll work on that part.

The Congestion Management Group is meeting on about a monthly basis. We have a target to produce a quarterly report each quarter as we try to put up the options on the table, test the options, and so on, so that over the three quarters, we're at least targeting -- and it's optimistic -- to come to some sort of proposal, a rough proposal, by the end of the third quarter.

MR. KROGH: And, Mr. Chairman, those slides from 28 through will give you the schedule that we are proceeding on for each of the work groups, so that you can see what we're going to be meeting during the course of 2003.

I thought we could go quickly next to the Transmission Planning Work Group, which has been very active. Dean Perry has been the chair of that work group from the outset. Dean?

Also, I should say that Armie Perez has participated in that and can respond to questions as well.

MR. PERRY: I think that the planning area that we're working on under SSG-WI, is one of the areas that we can chalk up some successes in, because basically we are moving forward to institute a regional planning process prior to the RTOs getting up and running.

What we are doing is looking at the total western interconnection, looking to the future where there might be future congestion. We'll be looking at some possible alternative solutions to future congestion, and possibly making recommendations.

Really what we're trying to do is move forward and provide information to the marketplace and to those builders of transmission, and, again, we're starting this right now. We're actually implementing this process right now, this year, and we plan to issue our first report on our work in September of this year.

I did want to mention that our effort is a combined effort of not only those working on the RTOs, but there's probably actually more participants outside the RTOs

in our process. We are involving the folks, the coal, the gas, renewable resources, in helping us develop future scenarios that we're looking at.

We're looking at five and ten years into the future, and we're also actually looking at about 20 years into the future, a real long-range effort, so it's quite a concerted effort that we've started.

Many people are involved. I feel the effort, personally, as chairman of the group, is making a lot of successes and people are really cooperating in moving forward to do this. I feel personally very good about it.

We are in the initial phases of actually setting up a model for the western interconnection, a commercial model. Right now we're collecting the data and developing the database to run these studies, which we will be doing shortly.

The next slide, please?

(Slide.)

MR. PERRY: This just indicates some of the products that we have come up with, that we have developed so far. Initially, we have developed a draft of the planning process, and this was included with the January filing. It's our description of this.

Essentially, this process is describing the product that we are developing, and it's describing what

inputs go into developing the plan and that type of thing, how it interfaces with others that are doing planning. It just basically describes the planning process that we are embarking on.

And as I indicated, as we're developing the process, we're actually starting to do some of the studies this year and collecting the data. We're currently developing the database to do these studies right now.

CHAIRMAN WOOD: When I look at the chart on page 29 that shows a task of developing a SSG-WI transmission plan, is that going to actually have the recommended projects so that the state commissions can then take up or the federal agencies can take up?

MR. PERRY: In the first year, Mr. Chairman, we will at least list the alternatives that we are looking at. I'm not sure, by this September, that we'll be able to actually develop a consensus on recommendations, but at least we're going to analyze, and we'll be at least able to show where we think congestion will be occurring and what some alternative solutions are to that.

And we're trying to hold to the September date, I guess, as a matter of just getting some information out, so at least we'll get that far this year.

CHAIRMAN WOOD: So there will at least be then a professional staff's recommendation as to these are the

projects that are needed to bring the western grid up to snuff?

MR. PERRY: That's correct.

CHAIRMAN WOOD: And then it's up the states at that level and the RTOs as to how they get paid for and built?

MR. PERRY: Right. We're providing information, that's right.

CHAIRMAN WOOD: So it's not just the planning process that's going to be done by the end of September, but an actual first year's plan for the entire West?

MR. PERRY: Right.

CHAIRMAN WOOD: Great.

MR. PERRY: Again, it should include alternatives, but I don't think we're going to get, in all cases, to developing actual recommended projects.

CHAIRMAN WOOD: Now, this will include both the relief of congestion and, of course, the normal reliability kind of traditional planning that's gone on, or is that --

MR. PERRY: Our focus is going to be on the commercial part and what the market needs.

CHAIRMAN WOOD: Where is the reliability planning? Is that with one of the other agencies with a couple of letters?

MR. PERRY: I think that the reliability part is

coordinated through the WECC, Western Electricity

Coordinating Council.

CHAIRMAN WOOD: So you see that if you fix something for reliability, you might actually fix the commercial problem, too, so you don't need to recommend it separately? Why can't we just do all of that together?

MR. PEREZ: The main purpose of the RTOs will be to make sure that their system is reliable and compliant with the reliability criteria.

CHAIRMAN WOOD: Right.

MR. PEREZ: The main purpose of SSG-WI is to make sure that whenever there's an economic need for a line, that the line is brought to the RTOs for their consideration.

CHAIRMAN WOOD: Is it lines within RTOs, or just those between them?

MR. PEREZ: Lines -- for the economic priorities within RTOs and, in general, it will be the seams issue.

CHAIRMAN WOOD: So both, right?

MR. PEREZ: Both, right.

CHAIRMAN WOOD: Because you need something between Oregon and Idaho and then something between maybe Idaho and Nevada -- I guess that's not in RTO West -- Nevada and Arizona, those would all come out of this process.

MR. PEREZ: That's correct.

CHAIRMAN WOOD: Is the reliability planning

that's done at WECC, is that rolled into here as an assumption that those get dealt with and then those don't present any problems? My experience is that building a line sometimes results in a couple of problems.

MR. PEREZ: WECC, per se, doesn't have a reliability planning function. WECC, per se, is where the liability criteria is created.

CHAIRMAN WOOD: Right.

MR. PEREZ: And then the individual RTOs will make sure that their expansion planning is designed to meet that WSCC criteria.

CHAIRMAN WOOD: The two that aren't set up yet, who is doing that planning now for those areas.

MR. REINHOLD: The individual control areas are responsible for providing that initial planing within the same context that the RTO does in the California ISO case.

CHAIRMAN WOOD: So, just kind of clear up for me how does that planning that's done by either the control area RTO, depending on where we are, get integrated into the SSG-WI planing process?

MR. AFRANJI: Let me take a crack at it. The way reliability planning is done today, each transmission provider does their own planning, and then they take the plans to WECC, to the Western Electric Coordinating Council to make sure that they fit together, that they -- once they

meet with each other, it's not going to create an issue.

WECC reviews the plans and decides, you know, that looks fine, or they make some recommendations on how to coordinate better. My view is that in the future -- and that's my view -- is that you would have the reliability planning done at the RTOs and possibly then to coordinate the reliability piece of it at the seams, there would be a WECC/SSG-WI interaction to make sure that the reliability is well coordinated, as it is done today.

On the adequacy piece, you're looking at the SSG-WI looking at the adequacy of economic planning for the system as a whole. So that's the difference between the two.

One, on the reliability, there would be coordination like today at the seams, through WECC or an entity like it.

MR. REINHOLD: Mr. Chairman, to get back to one of my earlier points, the same people that are doing the reliability planning are working on the SSG-WI planning effort on the commercial side as well, so we have the same individuals working both sides of the problem.

MS. SCHMID: I guess I just want to give a little bit of a California perspective here. When we talk about reliability, the reliability decision on the decision on building a reliability line or upgrading a line for

reliability purposes, rests at the CPUC, rests at the California Public Utilities Commission.

When we talk about the economic transactions, which is what SSG-WI is looking at, we're looking at the high voltage lines and where is it that we need something to happen that will ease the commercial transactions throughout the West?

And, for me, that's a clear distinction between the two. Obviously they have to feed into each other, and they will share the information, as Charlie says, because it's basically the same people who are working on it, but it comes from different perspectives.

CHAIRMAN WOOD: Does the ISO in California do an analysis that they provide to the CPUC?

MS. SCHMID: We do, yes.

MR. PERRY: Yes, just a comment I might make on this discussion we've been having is that as in the SSG-WI planning process, as we model the system to look for future commercial needs or marketing needs, we are representing all the projects that individual owners may develop or that they take through this WECC process.

Our model already encompasses those projects that they planning, and so we're representing those in what we're doing. And then what we'll do is look and see whether those are sufficient, whether there might be additional problems

that we still need to address.

Another thing we might look at, I think, is if there are projects proposed, and then through this SSG-WI process, we may decide or we may feel that that project could be modified in some way to maybe make it a better project for the interconnection then as a whole, so that's where we would look for those kinds of things.

We're working closely with the WECC, as I think Charlie already mentioned. A lot of the members are already WECC members, but we're working with the WECC staff. We're using some of their data and things like that in what we're doing, so there's a close, good working relationship there.

(Slide.)

MR. PERRY: The last slide that I had is really just a summary of the issues that the Planing Work Group has identified that need to be worked on in developing our process. And those were already included in the filing. I don't need to go over those other than to just summarize quickly.

One would be that the process needs to identify the projects. We need to agree on how we're going to do that; we need to agree on how we're going to evaluate the cost effectiveness of projects. We need to take a look at what role SSG-WI might have in possible implementation of projects or how we would kind of fit into that process with

the states.

And, by the way, I wanted to mention that in the work that we're doing, the states are very actively involved in what we're doing in the planning part. Actually two of the commissioners have been participating, coming to working group meetings and actually participating with us, as well as many of their staff. So, we have established a good rapport, I think, with the states on an individual basis and with CREPC.

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I guess that's basically it. One of the main points I wanted to make was that we are embarking -- we're moving forward on setting this process up, and we're actually doing it, and we'll have a report out in September.

That's all I had.

MR. KROGH: Thanks, Steve. If we could move on to market monitoring, Mr. Chairman. Kristi Wallis is the chair of that work group. I know she was back here this last month for a technical meeting on market monitoring. Kristi?

MS. WALLIS: Good morning. The Market Monitoring Work Group has been a very active and productive group. It kicked off with a workshop, a regional workshop, in November of 2001 and started negotiating.

The group has been meeting actively since December of 2001. It's had very broad participation. There has been representation from each of the Western RTOs, but also from a wide range of stakeholders. We have had state participation, and what's been especially helpful, and I'd like to thank the Commission for this, is that we've had active FERC Staff participation, most recently from the Office of Market Oversight and Investigation, and that's been very helpful.

The group was initially tasked with developing a workable proposal for a single market monitoring entity that

would monitor all the Western RTO markets and would satisfy the Order 2000 requirements for the three Western RTOs. And the group actually prepared and presented to the Steering Group a set of recommendations to establish a single market monitoring entity, and those were presented in July.

Since July, there have been some questions about whether a single market monitoring entity is the right way to proceed or whether there could be a couple of other options that might work as well, including an umbrella organization that would be analogous to what you just heard with respect to planning, that it would be looking at seams issues. Or a third option would be coordination between three independent market monitoring entities for each of the Western RTOs.

The concerns that are prompting further discussion of these other options are responsiveness to local issues, the fact that you'll have three separate RTOs and three separate market designs, although they will be compatible, for a seamless Western market, but there will still be three separate tariffs.

And there has also been I think in California as well as in other ISOs across the country I think we heard from the market monitors that it's important to have people on the ground and have, although they're independent, have a close relationship with the operations folks. And so at

least some people are concerned if you go to a single West-wide, you might lose some of the benefits of that approach.

And so the steering group recently confirmed, reconfirmed its commitment to a Western, a West-wide market monitoring function, but they asked the work group to supplement the previous recommendations to bring in those other options to fully develop them, basically identify what they would be and then do an analysis, pros and cons. And I think we'll test to see if we can come up with a consensus or majority/minority opinions in the work group, but we'll be bringing that back to the steering group.

CHAIRMAN WOOD: When do you expect that to be done, Kristi?

MS. WALLIS: I think it will be probably by the end of the first quarter. I think it will be this spring we should be able to accomplish that.

I think that notwithstanding the addition of other options on structure, there are certain things that are fundamental to the work group, and I think they will stay in place. The first is the that the market monitoring function needs to be independent.

It needs to be independent of market participants and it has to strike the right balance of accountability with the RTOs, but it needs to be to a certain extent independent from the RTOs as well. And it's very important

that that market monitoring function have a direct relationship with the Commission.

And certainly one of the things that we're exploring, and once again it's very beneficial to have, different members of OMOI be involved in the discussions as to just what the relationship is going to be and the divisions of responsibilities.

I think also there was very strong consensus on what the responsibilities of the market monitor should be. It should be actively monitoring markets, seeing if there are any issues, if there's performance inconsistent with a competitive market, and then investigates the causes that could get into conduct as well as market design. They should be evaluated in market design and coming up with recommendations as to what would make a more efficient market.

And that also the market monitor would be monitoring compliance or application, trigger situations for FERC-imposed mitigation measures or RTO design and FERC-approved mitigation measures. So those are -- I think that those will still be in the final recommendations.

We've got a meeting set in February, a two-day session where we're really going to focus in on developing those other options, analyzing them and identifying pros and cons. We're also going to spend some more time talking

about collection of data information and confidentiality issues.

I think we're also going to need to take a look at whether the addition of structure options will require further modification or tweaking some of the other recommendations. But we have an optimistic schedule, and I think that certainly by this spring, we should have another set of recommendations.

The only potential complicating factor will be one of the things that we might need to do in detail in an umbrella organization is identify and specifically as between the individual RTO market monitors and the West-wide function, which entity has which responsibilities. And to the extent that we don't have final market designs for WestConnect and RTO West, it may be difficult to get into as many specifics as we need to. So a final decision may be delayed beyond this early spring.

But I think the work group should be able to come up with pretty comprehensive set of recommendations by this spring.

MR. KROGH: Okay. Anything else? Thanks, Kristi.

MR. HEDERMAN: We've been working well with them and I think it's been helpful in both directions so far.

MS. WALLIS: Thanks.

MR. KROGH: Frank, do you want to take on Common Systems Interface Committee?

MR. AFRANJI: As you all know, Don Watkins, the chair of this group, has appeared before you earlier and pretty much gave you a detailed description of the CSIC or the Common Systems Interface Group. So again, I'll try to walk through some of the description of that group very fast, and if there are any questions, I'll be happy to answer them.

That group's purpose is to share the information and coordinate the technical system development. What we're trying to do, we're trying to avoid having three RTOs develop the technical systems in vacuum and hopefully we'll end up coordinating in a close manner to avoid the pitfalls of creating three systems that cannot talk to each other.

They are really trying to achieve three goals. The first goal is to create the seamless interfaces between the RTOs so the systems are the keys to get that interface or seamless interface between the three RTOs.

The other one is clearly to lower the cost for the three RTOs. If we jointly create or work on those systems that we agree on at the end of the day, we can go to the vendors and hopefully get as similar of a system as possible so that we can avoid having to create additional patches to get the systems talking to each other.

And clearly, the third bullet is a long-winded way of just saying that we need reliable system that can talk and be with each other.

(Slide.)

The group has been pretty active and it's been on the scene for over a year. And here are some of the key products that they have brought to us to date. One is the single market interface. What they did is they recommended a methodology for developing this single market interface across the three Western RTOs early on in the process.

One of the more significant issues that they came up with is they addressed the back-up control center. Meaning they looked at how can the three RTOs back up each other when it comes to the back-control centers. The back-up control centers are a huge expense, and if each one of us will have their own back-up control system and back-up computer system to support that back-up control center, it would have been a tremendous expense.

So what they came up with is creating what amounts to bunkers as a back-up control center within an hour's drive of each RTO that would have limited computer capability but at the same time you would have, for example, the computer system of RTO West backing up the computer system of WestConnect or Cal ISO by having the system in RTO West in case of an emergency, instead of having a full

duplication at the bunker of Cal ISO. And that's really a large cost-saving device.

Also, they spent a lot of time on the communication infrastructure. The communication for back-up control centers are by far some of the most expensive elements of those back-up control centers. They pretty much have come up with some really innovative idea of how those communication systems are going to work and what are they and what have you. And if you recall, Don had given you very detailed descriptions of those.

Another area they looked at is the training. Instead of having each RTO train its dispatchers, nowadays a dispatcher really has to deal with a very limited set of dispatching responsibilities. When the RTOs are developed, they will have to look at dispatch issues of the other RTOs and the region as a whole. So the training requirements are really going to be revved up quite a bit. It's not going to be the same type of training that the dispatchers get today.

So they agreed on a process on the three levels of dispatch training and how they could work with each other to set up sort of a central training center for all three RTOs.

And the last item on this is the outlined, the open system for the wholesale electric transactions. What they're trying to accomplish here is almost like the airline

reservation systems. In essence, have a central system that can talk to each other across the West, which is really a lot more efficient than where we are today.

CHAIRMAN WOOD: What does the verb "outlined" mean?

MR. AFRANJI: Basically they just set up what needs to be done. I don't think they're at the stage where they started the process. They said here's what we'd like to accomplish, and they put more details on it.

MR. WALTON: This is an area where these two, the Congestion Management Work Group and CSIC need to -- haven't yet done this, but they need to come together because as we understand, develop transaction concepts. Then we'd work with them as to how you'd implement that. That's an interlink that hasn't yet happened.

COMMISSIONER BROWNELL: It would be interesting if somebody started to put pen to paper and do some cost estimates as you marry these two of the cost of having different congestion management systems, for example.

Because I think the participants may want to take a look at whether the costs of different systems are bringing them the value and recognizing the importance of those differences. It would be good to have some kind of disciplined financial analysis done, as decisions are made.

MR. AFRANJI: I think that's really valuable.

And just to add on what Steve had said, that's really not the only area where the Common System Interface Group and the Congestion Management Group are going to have to cooperate.

There is several areas, as I walk through this, that they will have to work very closely because they overlap on what they're trying to do.

Some of the key tasks going forward is what we call implementation, coordination. And by the way, if you look to page 31, there is sort of a timeline on when they propose to accomplish some of those issues.

To start with, implementation coordination. Again, here they're trying to help the Western RTOs keep current and take into consideration each other's system as they move forward, meaning our implementation timelines, as you all know, are different, and they're trying to coordinate those as closely as possible.

They're also going to try to work on simulating the coordination process. What they're afraid of, they could build this process, this coordination process, but unless you sit down and really go through a simulation, you're not going to find the gaps in the three systems. And they're hoping to bring somebody from the outside, like college students or what have you, sit them down in a room

and say, here are the systems and here is what we're trying to do, and simulate it on a board or however they're going to do it. And hopefully in the process, they'll discover the gaps.

They will do the same thing with the business modeling. They will try to model the process along the same vein by trying to make sure that there is a consistency between all of the systems.

The last issue that they're working on, and they already started the process, is look at other systems that are already in existence. For example, the group has already spent considerable time at PJM and went through their system, looked at their computer models and how they're interacting with the other New York ISO and what have you, and came back with detailed recommendations on what works in their opinion and what needs, you know, we need to work on, and what are the gaps and what have you.

So they're not just looking at the West. They're expanding their horizon to make sure that we get the learnings from other folks.

COMMISSIONER BROWNELL: Along that line, I was going to ask this question later, but while the West is different, and we know the West is different, so we don't have to have that conversation.

(Laughter.)

COMMISSIONER BROWNELL: Has the SSG-WI group and its members talked to the Northeastern groups to understand what they might have done differently were they developing today? How and what the costs are of various seams issues, how they've dealt with contract issues?

It seemed pretty obvious to me at least during our CRR technical conferences that people who had been through it in the Northeast had not talked to the people in the West, although the West is different, contracts tend to be similar I think. And so I'm must wondering if broadly those conversations are going on.

MR. WALTON: Well, the kind of discussion that Frank just described in terms of visits and so on have gone on. Some of us worked in both systems in our checkered past, and so we're conscious of that.

I think going forward, there is a desire to do more of that, but the primary difference, for instance, in transmission rights is that it is this question of the allocation and the structure and those sorts of things. So there's where the differences lie.

But we are conscious of trying to learn from there. It's always cheaper to buy Version 2.3 of anything than Version 1.0, plus it works usually by 2.3. So we're conscious of that.

We want to learn from what's done, but at the

same time, we have to keep in mind there's sort of a learning curve. There's a learning curve for our folks to begin to see how they're the same as well as different.

MR. AFRANJI: Let me just add this. I'm going to take this as a recommendation as well. I think some of the working groups have interacted and maybe I will take your words as a recommendation to rev it up and spend more time at the higher level, and that's probably a good recommendation.

MR. REINHOLD: And, Commissioner, the working group members did spend a week on the road in December and spent a day each in I believe four different control rooms of the IMO and a couple of the other RTOs in the East. So that effort has been undertaken, at least at the work group level.

COMMISSIONER BROWNELL: The reason I say it, I mean, I comment on the differences. The reason I say it is we're spending customers' money.

And to the extent that we don't need to reinvent the wheel or indeed there are lessons to be learned that would cause us to act more differently and efficiently, that is what is driving me.

So it's not to impose something that doesn't work. It's to just be sure we fully understand what's gone before and take advantage of that.

MR. KROGH: Mr. Chairman, we have a final report on pricing reciprocity. Charlie?

MR. REINHOLD: The Price Reciprocity Work Group was fairly active early on in the SSG-WI process, and has been a little less active as some of the pricing proposals have gained a little more solidity over the past couple of months.

Essentially this work group is investigating pricing barriers to trade throughout the Western Interconnection, while also fulfilling that mundane function of collecting sufficient revenues to pay for RTO operations and the use of the transmission owners facilities.

Next slide, please.

(Slide.)

MR. REINHOLD: Some of the products developed to date are four alternatives or options for further consideration have been identified. One certainly is no change to the existing RTO price structures, the no-action alternatives.

We also looked at some type of reciprocal waiver for the wheeling charges among RTOs; a transfer payment mechanism, which details would have to be worked out as this process moves a little further forward, and also the potential of a west-wide wheeling charge for any transaction occurring within the Western Interconnection.

The group currently is working on the evaluation criteria that will be applied to all of these options and the data that they produce, in order to give a common basis for evaluating which one might be better.

Some of the indicia that they will be looking at are eliminating trade barriers between or among the RTOs; mitigation of cost-shifting of the proposals; the equal treatment of all users of the system with any of these options; and certainly the simplicity and ease of implementation of whatever option the work group comes up with.

Some key tasks and key work that they will be working on here over the next year in Calendar 2003: They are currently identifying the applicable existing charges and making sure they document the magnitude of those costs to identify existing revenue streams and needs.

They will then be collecting data and creating a central database in which to analyze these various options. They will then move on to making their own determination and testing consensus within the work group of the option that seems to fit for them, and then, as you have seen through the process slide, bumping that back up to the steering group for its analysis, and eventually taking a recommendation back to each of the RTOs.

CHAIRMAN WOOD: Let me just observe something

because we have seen it in the place where we're dealing with interregional costs and the PJM MISO.

The ISO or RTO heads came to us and said these money issues really kind of pit us against our members. Is it really constructed for this to be dealt with honestly at the independent operator level? Or should we just put this in the 206 proceeding, as we did there, and as we probably will do in the Northeast, and just say this is a money issue and let's just get the right equities there?

I mean, if you're going to spend a full year -- I'm looking at the schedule, and to be honest, truth in advertising, it's all black and not red, so I think that's a good way to allocate resources. Rate pancaking is certainly, elimination of it is an important goal for us, as well.

I'm just wondering if it's really productive, because, you know, when we were there in November of 01, we really heard, I think, three of the four. And I'm wondering how constructive it is for you all to spend a whole lot of time and head-banging on that effort when everybody is just going to look at the bottom line, did my bill go up or not and not really care too much about what's the just and right thing to do when it comes down to it. That's really kind of our job. Should we just go ahead and get that going here?

MR. REINHOLD: I think that's a fair question.

What I would add is that some of the rate designs within the RTOs has changed since the late 01 timeframe that you referenced. Frankly, I would like to see some data collection and some analysis done before we kick it upstairs for the referees decision.

CHAIRMAN WOOD: I'm offering that as a friendly alternative, rather than y'all spending what looks like the balance of this calendar year, kicking this issue around. Collect the data and that will determine how much net flows there are between regions in the first place. I think there's an assumption in my mind that there will be exports from your two sides to your side, and it may be just a natural conclusion that, therefore, some of the dollars ought to go that way, as well.

But, you know, I don't know if that's borne out by facts or not. It would be interesting to see where in the past couple of years, the flow patterns have been, to estimate how the transmission constructions across the entire grid benefit different regions. But at some point, I'm just saying don't bang your head too long, because you won't get to an answer. And I doubt that your steering committee will, much less all three RTOs, accept it.

But if that happens, I'm bringing the champagne out there myself.

(Laughter.)

CHAIRMAN WOOD: But recognize that we've got a role to play there, and that's just what regulators do pretty well, is money issues. So, please use that.

MS. SCHMID: I do think, if I could add to it, that on a more generic level, I think that the money issue is the big issue that you probably are going to have to step in on on more than one account.

I mean, we're talking about pricing reciprocity here and wheeling charges, but I think, as we get to recommendations on transmission lines that we think should be built, maybe, in fact, they are going to be built within a single state, but they are going to benefit the west.

I think allocation of dollars there is going to be very important and very contentious, and I think it's something that FERC probably needs to look at. You know, you're going to get comments from the California ISO on the SMD, and one of the things that we're going to suggest is that maybe you should start looking at rate, allocation rate accounts, rate standards, whatever the correct terms are, for the ISOs in general, so that you don't have all of these individual 206s coming at you, but that you begin to have a generic bucket that we can begin to put our work into.

So I would take you up on your offer that I think that the FERC does need to begin to look at rates and allocation and how to spread them around.

CHAIRMAN WOOD: With that, you mentioned, Charlie, data collection exercises. What kind of timeframe do you have on that?

MR. REINHOLD: My recollection is that we're looking at --

CHAIRMAN WOOD: Is that Task No. 14?

MR. REINHOLD: First of second quarter of this year.

CHAIRMAN WOOD: Okay, that's that one? I think the point of allocation of new construction, we've heard that from really when we do our infrastructure tours around the country, is there's a lot of nodding that we need new infrastructure, but it's just who's standing when the music stops?

So everybody is going to stand at one song or the other, so, there needs to be a lot of thought toward that. But we can -- that's our job; I mean, we do that.

MR. KROGH: Mr. Chairman, that brings us to the conclusion of our work group reports, and just repeating, making it work, I think you mentioned earlier about just how engaged should the Commission be as we go forward over this next year with this SSG-WI processes and the different work groups.

My guess is, as one who is helping to coordinate this, I would say, to be very directly and actively engaged

with us in the work groups and the steering group meetings, so one of your representatives, Charles Faust, who was at our first open meeting of the SSG-WI steering group on the 21st of January, and I know there has been active participation in all of the work groups, right from the start.

I think we're still in a development phase right now. I think we need all the help we can get. There are going to be some issues that probably we won't get total, say, unanimity on at the first crack, and we might have to come back to you and have you assist in making some of those decisions with us.

So I view this as an ongoing partnership with you throughout this process over the next year and beyond.

CHAIRMAN WOOD: I met you right when I first came on the job, with RTO West, and then went on out there, in last June it was, I guess, again. But I appreciate your personal leadership and I appreciate. All of you, I have gotten to know through some way or the other. I don't think Mr. Perez and I have met, but I know this is not the lead item on your job description, and, quite frankly, that is a part of the worry, is that there's just not somebody whose job it is to bring this all the way home.

I think I'm going to keep an open mind on how we get there, but it's an impatience that we've got. When I

came to this job, as Nora did, we both started on the same day, your region of the country was the one that had just blown up, and while it's centered on California, it had ripple effects across the entire pond.

And we are committed to making sure that never happens again. But that involves a number of things. It involves getting sufficient infrastructure back, where needed.

It involves getting balanced market rules back in place or in place, and it involves a vigilant market oversight function that none of us were able to do independently, but together, we can all do a lot better.

So this brings together the entire FERC agenda in resolving this issue, so please know it is of critical importance to us that your calendars are aggressively set and aggressively met; that the formulation of recommendations through the entire process are such that all three boards, when constituted, which I hope will be soon, or three independent decisionmaking authorities in the three regions can say, yes, that is right, and, yes, we're ready to implement, and, yes, we're going to go either get the software or the employee or get the contractor, do whatever we need to do to implement that decision.

But it's of critical importance that the thoughtful decisions get analyzed, as I think you've clearly

set up here. Thumbs up on that, but that the follow-through process is equally as robust.

We are going to be committed to that, both in resources from our staff level, and from our attention as Commissioners to this effort, because it was a scarring episode for our Agency's history and for a lot of customers in your half of the country, and we don't intend for it to ever be repeated.

So thank you again for your leadership.

Colleagues, are there any further questions? This was a very helpful presentation.

COMMISSIONER MASSEY: Yes, to follow up on your earlier comment about teeing up some issues, I hope there is a way to ensure that there aren't certain issues that are just so tough that you can't resolve them and they don't ever get resolved; you just talk about them forever, and, despite your best efforts, you just don't make progress.

And I would like for us to have an early warning system about those, so that maybe they can be teed up and we can resolve them to keep this going, keep this moving along in a very sharp pace.

I appreciate all of your efforts, and I share your frustration that it takes so long to get this going and get this done. And I hope that if there are issues that we need to step up to the plate and resolve, that we will do

so, and I hope there is a process to let us know what those are early in the process.

CHAIRMAN WOOD: One important one was one that Bud and y'all have mentioned, and I think it was on the bottom of your slide that we've seen twice, assistance in issue resolution involves not just us sitting here at the end game, but our folks, through our staff, participating as Charles did last week, on the front end, to really just be the screen and kind of a vent.

When we were putting together the ERCOT model, staff from my prior commission was involved everywhere. They were not decisionmakers; they weren't even sitting at the table; they were almost in the confessional booth on the side so that people could come vent their steam, get it over with, and then kind of be told to go back into the game and keep playing, and then that, of course, got back to us and we knew who was really hot about what issues, so we could kind of work around them.

MR. KROGH: Mr. Chairman, there has been considerable venting with some of your staff's support and Mr. Cannon. I don't think that will be discontinued anytime soon.

CHAIRMAN WOOD: That's good; that's healthy, but a role that we can play -- and I want to encourage our staff to do this -- is when entities and y'all kind of set up to

do that, three kind of come in from different angles of the interconnect and may have different interests, maybe don't necessarily see that optimizing solution that works for all three.

And the staff person who is quick and on the outside can look at kind of the broader public interest, can say, gosh, this ought to solve all three of their things that they really care. It might make them a little bad on some peripheral issues, but this is an option.

So we're going to make sure that we get the kind of folks that can do that kind of thinking and be that kind of role there, but, again, I hope that that kind of role can also be home-grown as well, where folks in a seams process can step out of their own pecuniary interests and kind of look after the greater good, because that's really -- that's what we're trying to achieve through all of our agenda, is trying to set up an independence mandate that we're being very committed to, and through detailed tension to market design, are those balances, and to make sure that they work well for y'all's customers.

So, you're off to a good start. I appreciate the effort, and, as one who has been flying across the continent lately, thank you for doing that, to come here.

Without -- do you have anything?

MR. CANNON: Just that we certainly will make

ourselves available in any way we can to try to help this process and make it successful. And I would recommend that at some point, we may want to set up another dialogue between you all and some of your state colleagues from the West, to try to work through how do we best work together with them to try to make this effort successful?

CHAIRMAN WOOD: And that's what we were planing to do in November when it became clear from the Denver meeting that this is a useful process to get some of that up to a more refined level than just generalisms. Yes, it's time to talk specifics and not just process.

So, that's good, and I would look forward to exploring that also. Thank you all. We'll take a recess.

(Recess.)

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CHAIRMAN WOOD: After a short recess.

SECRETARY SALAS: Next on our discussion agenda, we will take up both G-1 Northern Natural Gas Company, and G-2 Tennessee Gas Pipeline Company with a presentation by Katherine Gensler who is accompanied at the table by John Carlson, Robert Shelton, Mike Goldenberg, and Sandra Elliot.

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The draft order in Tennessee requires that the Pipeline's tariff contain objective criteria for establishing creditworthiness. Northern's tariff already

meets the standard in that a shipper with an investment grade credit rating is deemed creditworthy. The draft orders reject proposals that require non-creditworthy shippers to post security with five days notice of suspension or termination.

The orders find that the pipelines have not shown five days to be a sufficient period of time for shippers to obtain the requisite security. The orders permit the pipelines to refile, justifying a specific notice period as providing shippers with a reasonable opportunity to provide collateral. The orders also allow pipelines to adopt an alternative arrangement wherein a shipper that becomes non-creditworthy would be required to prepay for one month's service within those first five days, but have at least 30 days in which to provide the next three months security for service.

Further, the order suggests that NASBE consider this issue as part of their standards development process and recommend an appropriate notice period. The draft order accepts Northern's proposal to require a non-creditworthy shipper to provide security for any loaned gas the shipper contracts for.

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Northern to propose a more reasonable security requirement.

Finally, the draft orders reject proposals to take possession of gas left on a pipeline's system by a non-creditworthy shipper whose contract has been terminated. This confiscation mechanism has not been justified by the pipelines and may not adequately protect the rights of the shipper and other parties that may have an interest in the gas. This concludes my presentation.

CHAIRMAN WOOD: And it was good. Thank you.

I want to acknowledge Nora and her leadership on these orders, particularly your staff folks working on this to help us kind of draw some correlations between these two orders and one that we did not deal with that I believe we can get out notationally in the near future to deal with these issues. But I hope that parties on the outside can start to get a sense of the policy cuts that the Commission makes on creditworthiness concerns that are being raised in these first tariffs that we have referred the implementation of to NAESB. I know that people don't want to be making policy decisions of NAESB. In fact, that's correct, we make them here but these two cases today and I think the others to come will give us the opportunity to really flesh out a good policy on what we think the creditworthiness criteria and implications and implementation ought to be for all the gas pipelines, so I hope these are helpful decisions today

to the industry as they move forward in this era of little credit uncertainty and to know where we stand.

COMMISSIONER BROWNELL: I wanted to thank the staff actually I learned a lot during this process and particularly my staff in helping me kind of work through some of the issues. My overriding concern is that we don't do what we've seen happen I think in the last year, and that is the unnecessarily onerous in such a way as to cause a death spiral when one is not necessary. And I think equally important not to have such variations in rules so as to allow entities the potential for discrimination against certain shippers, and so I think we've really worked through some of these issues. I thank everybody and I know there's more work to be done but while this isn't the headline stuff, this is the underlying important work that we need to do to bring some stability and certainty to the marketplace and to the people in the marketplace, so thank you.

COMMISSIONER MASSEY: Let me ask a question to my colleagues and to staff. These issues strike me as fairly complex and yet they are I'm sure going to be common threads among the pipelines in terms of how to handle these questions, common issues. Is there a sense that we should be proceeding more generically on this, rather than on a case-by-case basis, and I would raise that.

We certainly have plenty of conferences that

we've already scheduled on generic policy, questions mostly with respect to electric policy, but I wonder about that.

Is proceeding on a case-by-case basis the best way to handle this issue that is common to the industry as a whole? And I raise that question, I'm open to ideas.

CHAIRMAN WOOD: And I've thought about it too. I know we started off, what was the first one, on the Tennessee case. Some of it took to NAESB and the rehearing of that case? Have we done the rehearing? That's when we said we are going to, we acknowledge that before but we're going to be addressing these on a case-by-case basis.

I guess my thought to that, Bill, would be we've got five to do. We've got the North Baha and then we've got two more, is that right? On the big ticket list we've got five total. Okay.

I would like to suggest maybe we get through the batch of those and then at that point if there is still some need to kind of pull it all together in a different type forum, these are clearly orders that could be reheard. I think at that point, once we make the cuts and lay them out there, if there needs to be some additional open processes, I would certainly be open to that and invite the interested party in maybe like Spring once we lay these on the table to come talk about how this all hangs together.

But if we do have five dockets, we've got five

months to deal with them or else they turn into a pumpkin and so we need to process but I'm open to that Bill if that's something that I guess parties tell us that we need to do come about March or April when we get through all of these, at least the first batch of them. And if there's not enough clarity at that point, then perhaps we should.

COMMISSIONER BROWNELL: Yes, Bill, I started as the person who would like to do everything by a generic proceeding so the rules are the same and people don't have to be confused about what works where. I think the exercise of going through these cases is at least helping me get a better understanding of some of the very highly nuance differences in the customer classes of each pipeline and maybe some different needs. And so I'm certainly open to it and actually started where you are but began to kind of see these differences and want to get into these cases to make sure that we fully explore how real those are and how meaningful those are and what kind of a difference that makes, but I would be certainly open to kind of bringing them all together at the end.

CHAIRMAN WOOD: I think that points is when you go through like on G-1, and I was reading these things, and you were kind of going through, okay, well that's the implication and you read about it in a kind of over policy document, it's one thing. And that was very well done too,

by the way, trying to integrate that as you all did. But to really see it specifically here, it does kind of start to whittle down the sharp edges of the sword. So I do appreciate having some real life experience as we do perhaps walk into a proceeding later on, if there are still some unsatisfied issues.

You all add anything, the folks in the front line here? Mike?

MR. GOLDENBERG: I was just going to mention that I believe NAESB is to report back to us in June of this year, and they are working on developing standards for some of the issues that are addressed in these orders, I believe, such as the kinds of documentation shippers need to provide to the pipelines and things like that. So it might be worthwhile to see what their report is like and then see what issues are left over if we want to proceed generically.

COMMISSIONER MASSEY: And I'm assuming that NAESB will not, it's not their business to make policy calls. That would be this Agency's responsibility and I'm assuming that we're not taking a cookie-cutter approach but the precedents that we're setting in these orders today will form the framework of our later orders in these cases.

Or are you saying are there such differences among the pipelines that these will not be relevant precedents?

MS. GENSLER: Well I think I can address that.

The issues that you saw both in the paper and being discussed here today are somewhat general across the pipelines. And they're trying to build in some flexibility so that there's one common idea of this is the highest standard one can set, or generally we should be treating shippers in this manner, but not specifying this is the only right way to do it.

It enables pipelines to make some calls as far as what's going to work best for their company, for their customers. And you'll see in future orders that there are other issues on the table outside of what's being discussed today into the broader policy spectrum.

MR. CARLSON: Commissioner, I think in part what we're trying to do is establish, at least in for a number of items, objective standards that we can apply generally so that they should be applied in the future proceedings in the same manner that you see today.

COMMISSIONER BROWNELL: I will support these orders.

CHAIRMAN WOOD: Is that your vote?

Yes. A conversational vote. I will support these orders as well. And I can't let you all stand alone, so I'll vote aye as well. Thank you all. Nice job and thank you for working things through at the end as well.

SECRETARY SALAS: In the final item this morning is A-3, 2003 Natural Gas Market Assessment with a presentation by Lisa Carter, accompanied by Tom Pinkeston, Kara Much and Ken Kohut.

MS. CARTER: Good afternoon, Mr. Chairman, Commissioners. Everybody else who's waiting to have lunch. I'm here today to present to you the Office of Market Oversight and Investigations recently completed, 2003 Natural Gas Market Assessment. There are some slides.

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In coordination with my presentation today, this assessment is being released to the public on the FERC Web site. Copies were available in the back of the room at the start of this meeting as well.

Before starting, I'd like to thank FERC Staff, the Commissioners and the Commissioners Staff for all of their comments as we moved this from a working draft we used in the fall to steer our analytical and investigative priorities to the final draft that it is today.

The purpose of this assessment is to provide the Commission with an early warning on market developments. Guide short-run oversight investigation priorities and communicate priorities to market participants. The healthy functioning of natural gas markets can have profound effects on the overall economy.

In 2001, customers spent \$142 billion on natural gas in the United States, which represents 1.4 percent of the gross domestic product. Of that, almost one quarter of the natural gas sold in 2001 was used by residential customers who have an average gas bill of \$844. OMOI has identified five pressing concerns for gas markets as of the winter 2002-2003.

Those issues are the deteriorating financial condition of market participants, the management of credit exposure, shaking confidence and price discovery methods, a continuing need for efficient investment in infrastructure, and the continuing potential for manipulation. I'm going to briefly address each of those in term.

First let me address the financial condition of market participants. OMOI finds that the energy sector is facing unprecedented financial challenges. This graphic shows the average 2002 change in stock prices for a group of 111 key energy market players. As you can see, stock prices fell across the board for every energy industry category except producers. Credit downgrades have also been common and many companies have exited the energy trading business and other lines of business.

Unfortunately, there's potential for further financial instability in 2003 due to the amount of energy company debts scheduled to be renegotiated over the next few

years.

Why is this important to the function of energy markets? Financial weakness can have a number of implications. For instance, a reduction in the number of energy traders can reduce the number of agency agreements also known as asset management contracts and shift risk closer to consumers.

Constrained finances could also defer necessary infrastructure maintenance and infrastructure build potentially affecting reliability.

What's being done to address this situation?

There are a number of actions that both the industry and FERC have taken and planned to take to address the situation. Industry has responded to this crisis by improving its finances through cost cutting and by developing best practices for energy trading and general business behavior. Industry is also increasing its use of exchanges where they don't need to worry about the creditworthiness of a particular partner for a bilateral transaction.

2002 was a record year for NYMEX gas futures and in a new exchange, the Intercontinental Exchange or ICE was launched this year. Finally the industry is encouraging new entrants including banks and brokerages. FERC will respond to this financial situation by monitoring natural gas

markets and natural gas market participant financial health in making policy is necessary.

The second challenge to gas markets addressed in the 2003 Natural Gas Assessment is the need for successful management of credit exposure. New methods of addressing credit management are being adopted and used in natural gas markets. Credit clearing is the newest tool. Credit clearing is a mechanism for settling mutual claims, the results of which is that the risk that a company might fail to fulfill its contract is pooled among many companies.

It's been estimated by the Committee of Chief Risk Officers that companies can save 75 to 90 percent of the collateral required to support transactions by using clearing.

While generally valuable as improvements over traditional methods, some of these new approaches are not well understood by energy market participants, and their misuse could have unintended consequences for markets. Clearinghouse limitations for non-members and limitations also exist that result from the need to adapt traditional clearing used in financial markets to energy markets. The industry needs to ensure that they use these mechanisms wisely and report on them in their financial statements.

FERC is planning to cosponsor a technical conference on these issues with the Commodity Futures

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Those issues are the deteriorating financial condition of market participants, the management of credit exposure, shaking confidence and price discovery methods, a continuing need for efficient investment in infrastructure, and the continuing potential for manipulation. I'm going to briefly address each of those in turn.

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markets and natural gas market participant financial health in making policy is necessary.

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FERC is planning to cosponsor a technical conference on these issues with the Commodity Futures

Trading commission in early 2003. FERC is also monitoring the use of these new methods from credit exposure and will showcase positive developments.

They are challenged in natural gas markets at this time has shaken confidence in price discovery methods. Confidence in natural gas price indices has weakened amid allegations and missions of false reporting. The quality of the methodology used by the trade press to create gas price indices has also been questioned.

A drawback of the methodology is that the traders who traditionally provide the price quotes have financial incentives to influence market behavior. Unfortunately no serious alternative to the trade press developed price index system exists to day.

What does this mean for markets? Price discovery via the price indices hopes customers determine the cost of meeting their needs, helps sellers determine the value of their investment and when working correctly officially allocates resources to the customers who most value them.

Difficulties with price discovery can affect parties' willingness to enter into new contracts. It can also lead to the unraveling of existing contracts as parties question the validity of the data upon which their contracts are based.

How are industry and FERC responding to this

situation? The industry has taken this issue quite seriously. They're currently developing best practices for price reporting that industry participants will hopefully follow.

I first include the Committee of Chief Risk Officers development of best practices for price reporting, the Coalition for Energy Market Integrity and Transparencies challenge for price reporting and publishing guidelines, and actions by some trade publications to look for ways to increase confidence in their data.

FERC has also taken this issue quite seriously. On January 15, 2003, FERC Staff reported concerns regarding price index formation to the Commission at its open meeting. Staff recommended that in the future, the Commission require the price indices meet certain minimum standards before natural gas pipelines are permitted use of indices and new tariffs or for other new regulatory purposes.

FERC is also analyzing natural gas price index issues in its fact-finding investigation of potential manipulation of electric and natural gas prices in Western markets.

Finally, the Office of Market Oversight in Investigations is planning a technical conference to address price index issues.

The fourth challenge to gas markets addressed in

the 2003 Natural Gas Market Assessment is a continuing need for efficient investment in infrastructure. Despite its current financial problems, the natural gas industry requires continued investment to maintain adequate supply, delivery facilities and operational flexibility and safety. The challenge to industry is to maintain adequate efficient levels of investment in today's competitive environment.

Prices this winter are higher than they have been in the recent past. However, market participants appear not to believe that the current high prices will last. NYMEX futures prices for delivery of natural gas over the next three years show prices generally lower each year for the same month.

The challenge then is for industry to continue to invest in natural gas exploration and production in this shifting price environment. Shifting supply and demand patterns also challenge the market's ability to provide sufficient transmission and delivery infrastructure. Areas of concern include the Rockies, the New York metropolitan area, other parts of the Northeast and parts of the Southeast. Recent price spikes of over \$20 in New York City reinforce our concern about that area.

What can we do to address the need for efficient investment in infrastructure? The first thing industry can do is to maintain its existing infrastructure. The

extensive facilities required to supply and deliver natural gas to customers makes it inherently vulnerable to disruptions. Failure of any part of the system, rigs, pipelines, compressions, storage, facilities can result in failure to deliver to certain customers for some period of time.

A second step industry should take is to improve the performance of price discovery mechanisms and forward markets for capacity. Both of these improvements can increase confidence and the price signals that provide markets with an indication of the value of investment in new infrastructure.

Finally industry needs to make use of risk management services. Tightening supply pipeline constraints and reduced operation flexibility can all increase short term price volatility to customers. Industry focus on stability is critical for customer confidence. FERC actions in this area will include continuing to monitor regional markets and capacity constraints, supporting development of forward markets and encouraging state regulators to make rules that allow timely price signals to reach retail customers.

The final challenge I'll address today is unfortunately the continuing potential for manipulation. Evidence indicates that price manipulation has occurred in

certain U.S. natural gas markets and may be continuing. Since OMOI's inception, it has increased the number of active natural gas related investigation steadily.

A reflection of manipulation taking place during the current period of stress on energy markets.

Manipulation is more likely when liquidity is low, price discovery is obscure and capacity is constrained.

Investigations are currently taking place in the following five categories of price manipulation.

Control of market prices through weak liquidity, withholding of capacity in violation of regulations, manipulation of illiquid physical market places to affect prices and associated financial market places.

Communication of market information from pipelines to the marketing affiliates in providing false data about price or volume information to index publishers.

Companies active in the natural gas marketplace must take responsibility to stop manipulation of markets, either by their employees or by others. Our experience has been that some companies have taken actions to clean house internally and others have reported suspicious behavior to the Commission and other governmental authorities.

Collective industry efforts have include those spearheaded by the CCRO, Committee of Chief Risk Officers, related to appropriate controls and by the Electric Power

Supply Association related to ethical behavior.

Commission activities in this area include the following: In early 2001, the Commission formed the Office of Market Oversight Investigation. Since mid-2002, the Commission has received energy market briefings at regular closed meetings which review price movements, financial conditions, market intelligence, system outages, potential market manipulations and more.

OMOI is developing a side of market metrics and thresholds designed so that when anomalies occur, OMOI investigates to determine if the deviations can be explain by market fundamentals, market structure, or by improper market behavior. OMOI operates the Commission's toll-free enforcement hotline which is available to people who wish to report problems.

Finally, the Commission is increasing its coordination with other regulatory bodies as they investigate issues in the energy marketplace.

I'd like to speak with OMOI Staff believes the natural gas marketplaces are manageable but industry participants and regulators must seek out and aggressively promote solutions to assure efficient, cost-effective, and valuable natural gas service to all U.S. customers.

To promote these solutions, FERC will monitor the markets to ensure first deteriorating company financial

health does not impair dependable deliver of natural gas.

Result in rating of affiliated unregulated assets reduce the liquidity of gas markets.

Second that new methods for managing credit exposure are used beneficially. Third that price index issues are resolved. Fourth that regional and national infrastructure exists to support market needs. And finally that any instances of manipulation are identified and addressed.

FERC will also continue to monitor the market for new issues which need to be studied and addressed. Thank you. We would be happy to take your questions.

CHAIRMAN WOOD: Thank you, Lisa, and the rest of you all on the team and all the folks I know that helped you in pulling this together. I think it's well written and well said, and quite frankly don't want to detract by adding one word because I think you said is exactly what our agenda is and should be about. So thank you for articulating it so well.

COMMISSIONER BROWNELL: Thanks as one who probably made everybody's lives miserable during the development of this report. I want to say thank you.

I think it's important -- I think you've done a terrific job of summarizing kind of where we are now, and as you should focus on the greatest areas of vulnerability.

But I think it suggests one thing and I want to focus on yet another.

The first is that markets evolve in this process of evolution, we need to be responding with kind of changes in the way we do business and making sure that we're on top of them. But in pointing out the vulnerabilities, I don't want to lose sight of the fact that we also have a marketplace that has worked very well for this country, and that we talk about, you know, having enjoyed the benefits, and I think we talk about \$6,000 per family of savings and so I don't want people to lose sight of that.

What we're doing here is our job, is saying what next, what must we do and the industry do to evolve to respond to new opportunities, changing business models and changing market conditions. And that's good and that's what we are here for, all of us. But we do have a marketplace that is in need of fine tuning, but unlike the electric marketplace which needs complete restructuring, we have restructured those when you were here and did a pretty good job. So I just want to keep sight of that.

CHAIRMAN WOOD: I agree. I'm looking at really the five baskets of issues and they're really none of them except probably the latter which is a traditional enforcement function in any mature industry.

The five baskets of issues are ones that quite

frankly just benefit from discussion, from participation, but don't require the government to get in and do what we did on the electric side which is kind of set up a framework. It's just bringing to people's attention that there are issues, as you point out, Lisa, and used the good word, was it manageable?

MS. CARTER: Manageable.

CHAIRMAN WOOD: Manageable. They're manageable by all of us. We are at a very different point than we are in the other industry that we're busy with today. It's a good point.

MS. CARTER: Thanks.

COMMISSIONER BROWNELL: Thanks, nice job all around.

CHAIRMAN WOOD: We will close this meeting and do our closed meeting at 2:00, I'd say 2:10.

(Whereupon, the Open Session of the above meeting was adjourned, to reconvene in Closed Session at 2:10 in the same place.)