BEFORE THE

FEDERAL ENERGY REGULATORY COMMISSION

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IN THE MATTER OF: :

CONSENT MARKETS, TARIFFS AND RATES - GAS :

CONSENT MARKETS, TARIFFS AND :

RATES - ELECTRIC :

CONSENT ENERGY PROJECTS - HYDRO :

CONSENT ENERGY PROJECTS - CERTIFICATES :

MARKETS, TARIFFS AND RATES - GAS :

MARKETS, TARIFFS AND RATES - ELECTRIC :

ENERGY PROJECTS - HYDRO :

ENERGY PROJECTS - CERTIFICATES :

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COMMISSION MEETING - 777TH REGULAR MEETING

Hearing Room 2 C

Federal Energy Regulatory

Commission

888 First Street, N.E.

Washington, D.C.

Wednesday, October 24, 2001

10:10 a.m.

APPEARANCES:

COMMISSIONERS PRESENT:

CHAIRMAN PAT WOOD, III, Presiding

COMMISSIONER LINDA KEY BREATHITT

COMMISSIONER NORA MEAD BROWNELL

COMMISSIONER WILLIAM L. MASSEY

SECRETARY DAVID P. BOERGERS

ALSO PRESENT:

JANE W. BEACH, Court Reporter

P R O C E E D I N G S

C O M M I T T E E M E E T I N G

(10:00 a.m.)

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

Let's start with the Pledge to the Flag, please.

(Pledge of Allegiance made.)

CHAIRMAN WOOD: Mr. Boergers?

SECRETARY BOERGERS: Good morning. On the consent agenda today are E-6, -11, -13, -14, -15, -18, -20, -21, -23, -24, -26, and -30; G-1, -2, -4 through -7, -9 through -15, -17, -18, and -21 through -24; H-1, -2, -3, -5, and -6; C-1 through -5 and -9 through -11.

Commissioner Brownell votes first.

COMMISSIONER BROWNELL: Aye.

COMMISSIONER MASSEY: Aye.

COMMISSIONER BREATHITT: Aye.

CHAIRMAN WOOD: Aye.

SECRETARY BOERGERS: The first item for discussion is E-5, Commissioner Brownell?

COMMISSIONER BROWNELL: Thank you. For those of you who participated in the wonderful event known as RTO week, it became clear to all of us that while there was much

consensus on many of the items, we needed to strengthen our relationship and our ability to communicate with the states as quickly as we can. And so with the memo to my colleagues whose support I am asking, I would like to ask the Staff to pursue structures that we might establish so that we could facilitate that communication.

We have in mind something along the lines that Commissioner Svanda recommended and others endorsed and that would be a regional panel who would have, as its, -- we would have as a mission to strengthen our relationships to enjoy the benefits of state input because I think we certainly learned a lot from their grassroots perspective to reduce the transaction costs wherever we can for those engaged in FERC issues for the smaller states, particularly; that's been an onerous burden.

To also increase the efficiency of our Staff. It is clear when we are inside that the Staff has gone overboard I think in many cases to be sure that we're getting that state input but because there's no central place and central way in which we can gather that, I think that's gone unrecognized. And I also think that we could be more efficient.

And I think it also gives us an opportunity to enhance our flexibility in problem-solving at a time when we're trying to change the way we do business and transform

ourselves and be more user friendly, as it were, I think we need to try new avenues. So I would not only like to ask the Staff to pursue a structure but also to recommend to us where this structure might report to and what kind of staffing we need.

It strikes me that at least for the foreseeable future, when we're doing so much that impacts the states and where the states' input is so valuable, that we might considered dedicated staff whose job it will be not only to collect information from the states, but to make sure that we are coordinating within the Agency so that we're responding to their needs, and also perhaps to create a one-stop-shop. I talked to several new state commissioners last week who frankly didn't know where to go within the Commission to get the kinds of information and support they needed, and so hopefully this would facilitate that.

The paper outlines some other thoughts on this issue, but I'd like to ask the support of my colleagues who had a lot of input into the development of this, to ask the Staff to move forward.

CHAIRMAN WOOD: I think it's important also to point out, Nora, and I agree with your recommendation, both globally and specifically, but the duties of the regional panel are not what I would consider a light load. I think in response to the desires last week, that we heard both in

the individual panels and the Thursday morning panel, that the states wanted to be in the loop as it were and involved here. The list of duties you laid out for these regional panels are very stout, and ones that will require I think a pretty full-time commitment, much along the lines that the similar bodies that the FCC do require Commissioners to spend a lot of time dedicated to these efforts.

Setting up RTOs, transmission ratemaking, and revenue requirement issues, demand side response mechanisms that we've talked about being both wholesale and retail oriented, market monitoring, mitigation, oversight, those efforts are, as we saw from out west, very important to be in concert with the states who are at the front line of these things.

And then the addition bullet, which I appreciate you adding on my behalf, was distributed generation issues. There's a lot of interest in distributed generation but in many instances, it does look more like a retail item than a wholesale item, and even though it is a power plant interconnection, it can have some fuzzy ground. So rather than quibble about whose jurisdiction it is, let's just get in there and solve the problem, so I appreciate the can-do attitude and the broad view of what these regional panels can do. I think the main thing that I would want to do in our discussions with the states in setting these up, is

emphasize that it's really intended to solve problems and to avoid them before they happen so that we don't really have the response that we had to our July 11th initiatives. That we really have done more sensitization ahead of time, gotten the best ideas from the state commissioners ahead of time, worked through them as a consultative body ahead of time, so that that really is fed into our effort and we can move forward in a more aggressive manner than would otherwise be if we didn't have this.

So thank you for taking the leadership on that and I think your suggestions about a location of a specific, discrete function within the Agency that is accessible has really become a state ombudsman is a great idea and I wholeheartedly support that.

COMMISSIONER BROWNELL: Thank you.

COMMISSIONER BREATHITT: Commissioner Brownell, I think this is a move in the right direction, as we heard from our session with state regulators last week, and it is certainly one that the four of us have always wanted to make sure that we have paid attention to state commission interests. I think that this is something that's doable, and if we can structure this in a way that's not so formal and expensive in terms of so many structured meetings that airplane flights become a question of whether or not state commissions can do this that that impedes what the goal is.

So I think this is a great idea and I'm looking forward to seeing Staff's recommendations and I think that the state commissioners will welcome this and just wondered if NARUC would have a role in helping set this up? Should we move forward with it?

Would we be seeking their input on sort of the form and structure and the what?

COMMISSIONER BROWNELL: I would certainly value their input and they I think have a lot of ideas that we discussed before I came here, so I'm certain that we'll look to them on a continued basis to resolve these issues. So I thank everybody here for their ideas. I'm getting more credit than I deserve because I think there was a lot of input and team effort here. So I'm excited, I think it's going to work. And I know that you're going to come up with brilliant suggestions.

COMMISSIONER MASSEY: I really appreciate Commissioner Brownell's leadership on this issue. I will state again today what I stated last week during RTO week, which is, it is my own perspective that we have had a lot of process on RTO formation and asking the input from all segments of the industry, state commissions and so forth, we first floated the idea of a formal grid regionalization policy in the NOPR that led to Order 888, as I recall. Betsy Moeller's back here in the audience and I think that's

where we did it, and asked for comment about whether we should go beyond mere functional unbundling and move toward large regional markets as a matter of formal policy. Now that was I think seven years ago, when we did that, and we've had lots of process, lots of comments.

When we began our discussions that led to Order Number 2000, the first thing we did was issue a notice under Section 202A of the Federal Power Act asking state commissions for their input into the process, and we had one or two rounds of hearings in various regions of the country on that. And we have had a lot of process, we've had a lot of input from state commissions.

If we need more, I think we ought to structure it in a way that gets us to and end game with respect to RTO formation. I think we should define the issues to be discussed and focused on very clearly and have a concrete end point and the buy-in, it seems to me, ought to be that we're all marching toward forming these institutions in the most reasonable cost-effective way we can, and in a way to bring robust wholesale competition to all regions of the country. And with that understanding, I support this initiative.

CHAIRMAN WOOD: All right, then. Why don't we direct Mr. Larcamp, and we'll make you the director in working with other staff to bring back at our next meeting a

proposal for the Commission to consider and for us to use that and go forward and work with the states on some maybe implementation details and get these up and going as soon as possible so that we can continue our efforts, as Bill pointed out, to get these RTOs up and going and whatever the appropriate configuration would be.

Okay, this is a posting really for the NOPR, and I guess last week we had five full days of discussions, and I wanted to just ask Shelton to give us a public update on what the next steps are.

MR. CANNON: Well, Staff certainly found last week's discussions to be very useful and gave us sort of a renewed interest and renewed momentum in terms of trying to get RTOs up and running. What we have been doing is having Staff prepare what they heard and trying to organize that. We're pretty close. We're going to try and get that posted our Web site later this week.

We recognize that this was a selected group of experts that we brought in and we recognize that there are other points of view out there, so we're very anxious to open up this docket and make sure that we get those other points of view incorporated. But we think that putting Staff's notes and what we heard on the Web will give some organization to that and some focus to those reply comments.

I can't give you a lot of details in terms of

exactly what's going to be happening, but one idea that intrigues me at least is maybe to have some smaller follow-on sessions at the Staff level to explore some of these topics and dig down and get into some of the details because I think we heard a fair amount of consensus at the 10,000 foot level, but I'm sure, as we dig down, there are still a lot of thorny issues that need to be worked through.

So we look forward to your comments. We will try to get those things up on the Web as soon as possible.

CHAIRMAN WOOD: Thanks, Shelton. Any more comments on the Rulemaking or E-5 this week?

(No response.)

CHAIRMAN WOOD: Okay, we'll move on to the next item. David?

SECRETARY BOERGERS: The next item, Mr. Chairman, is E-2, discussion of RTO developments in the Southeast, and I believe we have a presentation by Jonathan First.

MR. FIRST: Good morning, Mr. Chairman, Commissioners. My name is Jonathan First. I'm with the Office of General Counsel. With me is Sanjeev Jagtiani, Alice Fernandez, and Steve Rogers of OMTR.

In a July 12th Order, the Commission directed stakeholders in the Southeast United States to engage in a 45-day mediation to combine to form a single RTO for the region. Southern Companies, SPP, Entergy, and Grid South

and its sponsors were directed to participate. Other transmission owners, such as Grid Florida, TVA, Santee Cooper (ph.) and other public power entities were specifically invited to participate, as were state commissions and other stakeholders such as marketers, generators and end users.

Pursuant to the order, ALJ Bobbi McCartney convened a 45-day mediation on July 17th, and concluded the process on August 31st. About 200 entities participated from all industry sectors. The ALJ submitted her mediation report on September 10th. The report indicated that stakeholders in the Southeast have come a long way in reaching consensus on important issues.

The report also indicated that the independence and governance aspects of a combined southeast RTO posed the greatest challenge. This presentation will focus on the area of governance where full consensus was not reached. Rather, two competing models for a Southeast RTO emerged from their mediation process. The Grid Florida and Grid South RTO models coalesced into one model called the collaborative governance model, which is also joined by Entergy.

Southern Companies and seven public power entities sponsored the Independent System Administrator model which evolved from the C-Trans RTO model proposed

previously by the same parties.

The mediation report recommends that we adopt the collaborative governance model because it is more fully developed and it more fully satisfies the independence requirement of Order Number 2000. This will be discussed more fully later in the presentation.

The collaborative governance model draws from the Grid South and Grid Florida RTO proposals previously accepted by the Commission. For example, it adopts the Grid Florida process for a stakeholder selected, independent board of directors. The sponsors propose that a for-profit transco, with an independent board of directors, will act as the RTO. A stakeholder advisory committee would advise the board.

To accommodate public power participation, five functions -- market administration, operational authority over the transmission system, generation interconnection, security coordinator, and ATC calculation would be delegated to a non-profit, independent market administrator, IMA, for a minimum of five years. At the end of five years, the transco can initiate a process to assume control of the delegated functions.

Another feature of the model proposed by the sponsors is that transmission owners may divest their facilities or operational control of their facilities to

either the transco or a separate independent transmission company. ITCs would have a role in planning, operations, and rates.

The ISA model would consist of a for-profit, system administrator as operator of the RTO and allow for one or more transcos with both receiving input from a stakeholder advisory committee. The transmission owners would choose the system administrator from a slate selected by the stakeholders. The system administrator, while performing functions similar to an ISO, would be a for-profit, performance-based, incentive-driven third party operator that would operate but not own the transmission facility subject to the RTO's control.

The sponsors of this plan believe that an independent operator that does not own transmission facilities in the region served by the RTO would best meet the independence criteria of Order Number 2000. However, much of the mitigation report's concerns regarding the independence of the ISA model stems from the proposal to have a system administrator operate the RTO, learning that the profit-driven system administrator differs from any other ISO model proposed to date.

In particular, the ALJ expressed concern that the independent board that is contemplated in the ISA model is the shareholder board of the system administrator, not a

stakeholder selected board. The model can accommodate one or more transcos. Proposed transcos must satisfy the independence requirements of Order Number 2000. Any such transco would perform several functions for the facilities that it owns; rate design, system studies and planning, and generation interconnection studies. This transco more closely resembles the ITC concept proposed elsewhere.

Public comment on the mitigation report for the most part focused on the governance and independence of the two proposed RTO models. Support for the two models coalesced along industry sectors. Investor-owned utilities favor the collaborative governance model, except for Southern, which is the sponsor of the alternative model. These investor owned utilities support the transco format. They also favor the flexibility afforded by the model, noting that transmission owners may turn over functional control of their facilities to the RTO, divest, or form an ITC.

The IOUs indicate that the delegation of functions to the IMA should address any initial concerns about the RTO's independence. Generators and marketers generally support the collaborative governance model because the preferred transco model that structurally separates transmission owners from owners of generation and distribution.

Public power supports the independent system administrator proposal believing that it is more likely to produce an independent RTO. In contrast, they object that a transco on top will have the opportunity to favor the transmission that it owns over transmission that it simply operates. They also believe that the ISA model will better accommodate public power, noting that the plan calls for the tailoring of transmission operating agreements to meet public power needs.

Public power also supports the ISA because of its rate proposal for full recovery from day one of RTO operation. Public power criticizes the collaborative governance model's proposed IMA as too narrow and temporary in nature since it can be disbanded after five years.

The three industrial customers' filed comments have mixed opinion on which governance model was superior. All agree that the chosen model must be truly independent and have industrial customer representation on the stakeholder advisory committee. The few comments that were received from state commissions also indicate a mixed reaction. One state commission supports the collaborative governance model with some modification while another opposes it. Two other state commissions have initiated proceedings inquiring into the public benefits of RTOs.

In considering the pros and cons of the two

proposals, the considerations favoring the collaborative governance model include that a properly formed transco is acceptable under Order Number 2000. The inclusion of the independent market administrator has a significant concession to attract public power, and third, a viable transco on top may likely offer a greater chance of divestiture of transmission assets.

Other considerations favor the independent system administrator model. For example, because the system administrator would not own transmission or generation assets in the region, it should allay concerns of perceived or real bias toward some transmission assets over others. The ISA has shown considerable flexibility to meet the interest of public power, and also the model attempts to accommodate transcos for transmission owners interested in divesting their assets.

With regard to the cons or the downsides of each model, the collaborative governance model has the potential, or at least is perceived by some parties as having a built-in bias to favor the transmission assets owned by the transco as opposed to those assets owned by others but in the transco's control. The model presents real or perceived concerns that it presents barriers to public power entities.

With regard to the independent system administrator model, it appears that the proposed transco

concept has not been fully developed, and as proposed, may offer little incentive for divestiture, given the limited responsibility that would be delegated to a transco. Also, there may be potential or perceived control of the RTO by the ISA's transmission owners since they will select the system administrator.

One issue that arises from the context of the Southeast mediation process is whether the development of sub-regional RTOs, such as Grid South, should continue to be encouraged. Sub-regional RTOs can serve as helpful building blocks to establishing a regionwide Southeast RTO and working with a smaller number of parties may make it easier to build a consensus. Also, such development could keep the stakeholders working to resolve regional implementation issues while they are awaiting the Commission rulemaking on market design and structure.

On the other hand, stakeholders may be reluctant to forge ahead with resolving issues when their decisions may ultimately not comport with new Commission policy. Further, it would seem inefficient to encourage the development of sub-regional RTOs that may never operate. This in turn could lead to a significant strain in cost problem to the extent resources are spent planning, activating, and possibly operating a sub-regional entity that may ultimately be superceded by a different Southeast

RTO.

In conclusion, Staff believes that both proposals have positive features and both are viable models from which to work. Both proposals have the broad outline of a governance model that could appear to satisfy the independence requirements of Order Number 2000.

In choosing the RTO model for the Southeast Region, the following key questions should be considered: First, whether the transco on top or ISA on top would best satisfy the independence requirement of Order Number 2000. Does the transco on top have the real or perceived potential for bias when dealing with its own versus others transmission assets. Does the IMA proposal go far enough or should it have greater responsibility. And if more RTO functions are delegated to the IMA, will that lessen the motivation of transmission owners to divest their assets to the transco.

With regard to the ISA model, does the system administrator's for-profit aspect raise independence concerns, as well as the lack of stakeholder input into the RTO's board. Second, which proposal will have broader participation? As discussed earlier, already public comment is split along industry sectors. Most IOUs in the region support the transco model. Public power entities have uniformly supported the system administrator model as more

responsive to their needs.

However, if the collaborative governance model is chosen, and provides the benefits expected by an RTO, public power entities seeking to enjoy those benefits may ultimately join as well.

A key question should be decided when deciding the perfect model for the Southeast RTO. Thank you. This concludes my presentation.

CHAIRMAN WOOD: Thank you, Jonathan. I want to ask Judge McCartney and our mediator, former Chairman Herb Tate to come on up to the table and visit with us as well.

I want to say while they're walking up I had the pleasure to actually read this fine report and learn more about what is ahead of us the next for years, well, me. That's how long I'll be here, at least my term. That's not how long it's going to take to get RTOs in, don't worry.

(Laughter.)

CHAIRMAN WOOD: About really the details here, and I really appreciate the fine effort that went to not only the work you all did, Judge and Chairman Tate, but the way you explained it to me, because I'm your student, and I appreciate the effort you went through.

I was also impressed by the level of detail of the different appendices on rate issues. I know I've taken a pretty strong stand about how pricing ought to be done and they came back with something here that was different. And I have to admit, I kind of like what I read.

Kind of falling in behind the locational marginal pricing, financial congestion hedge model in Attachment 3 was very instructive, and the discussion about the planning

process. So those attachments were actually very helpful to read following onto all the discussions we had about those globally last week.

Herb's passing something around, and why don't I ask Judge McCartney. The mike is yours. I'm not going to pose you an opening question because you usually don't need them, so I won't give you one.

JUDGE McCARTNEY: Thank you very much. First I want to thank you for the opportunity to serve the Commission and to serve the parties in the Southeast RTO mediation. It was quite a challenge, quite an endeavor, but I think that it had real value added contribution to the work of the Commission on the RTOs.

You already know Herb Tate, the former Chairman of the New York State Commission. He was a vital part of our mediation team. He was with me throughout this arduous project and he was instrumental in facilitating our dialogue with the state commission. Likewise, I want to thank Laura Shepard and Jonathan Sims who were also part of our mediation team.

I want to tell you again, too, that I really appreciate the opportunity to tell you a little bit about what my mediation report is and what it's not. First, it is an imperfect document with a very short timeframe and a determined and deliberate effort to meet my deadline of

September 10th. Many of the niceties were foregone, one of which was a table of contents. This upset me greatly, because a table of contents for a 136-page report is important. It kind of gives you a blueprint to help you dissect what's in the document. So with the permission of the Secretary, I went ahead and got the table of contents together. I've got copies in the back for everyone here who would like a copy.

And, you know, just real quickly to show you what I mean about the table of contents giving you a little outline, you already know the parties. They've been generically referred to in reference to the docket numbers, all the parties with respect to the SPP Entergy docket, the Grid South and the C-Trans dockets were directed to come. The Grid Florida was invited to come as were state commissioners and public power. But what does that really mean? How did that translate?

It was very impressive. Virtually every IOU in the Southeast footprint as delineated in the July 12th orders came fully represented and fully engaged and stayed that way for the entire 45 days of the process. Likewise, we saw owner classification sectors with interests in the Southeast to the tune of over 200 market participants, from co-ops, munis, the federal sectors, for TVA, CEPA, Sam T. Cooper, IPP generators, power marketers, consumers,

including industrial consumers, and even state commissioners were actively involved in the process.

These stakeholders brought a synergistic relationship to the mediation process that I submit has not been provided in any other forum to date. The mediation process provided a structured, disciplined forum for these stakeholders to come together collectively for the first time to look at each other's platforms and each other's filings and to share notes for purposes of identifying common clusters, not having to reinvent the wheel, but identifying common clusters on very critical points that resolved themselves in the first week of the mediation through coalition and convergence of those points as they related to key characteristics and core functions under Order 2000.

I think that this was demonstrated by the results that came forward in the mediation report. I did my best to capture what was a very, very complicated process. It was a process that I have termed market-based mediation. What we did is come to the table not with the goal of creating more theory or just engaging in more dialogue. As Commissioner Massey has pointed out, there's been a lot of dialogue from at least the 1992 Energy Policy Act reaching through the March '96 NOPR for Order 888, evolving to Order 2000, even up to the present day under the national energy policy where

we hear the President of the United States telling us that the repair, maintenance and upgrade of our national transmission system is an issue of national concern and that the removal of discriminatory access to our transmission grid is considered absolutely imperative to the creation of a robust wholesale competition.

So the focus was there, the timing was there, and the parties came ready to really work at trying to effectuate the Commission's goals with respect to the Southeast.

Not this meant that we looked all of the multiple filings with respect to the Southeast RTO dockets as a benchmark. We did not go outside those filings. We didn't do, you know, an analysis of is PJM right for the South? Or is another RTO model that's currently in place right for the South? What we did was take the multiple filings to date that were of record and that already reflected a deliberate collaborative process effort by many of the stakeholders, and we used those as benchmarks.

What we found when we combined those previous filings for consideration were four basic models: The SPP Entergy model, the SeaTran model, the Grid Florida and the Grid South model. These models were the starting point for the analysis for the Southeast stakeholder mediation effort.

After the first week of this market-based

mediation where the planned sponsors were marketing their product to the 200-plus market participants in the room covering the key aspects of Order 2000 with respect to key characteristics and core functions and trying to persuade the greatest number of market participants how their platform or their model would best fit their business needs and courting, if you will, soliciting their support for the model.

The first week, of course, you were dealing with a stagnant situation where the market participants are reacting and responding to the documents that were filled with the models as developed in those filings. The market-based mediation through the utilization of such tools as separate breakout groups and preference polling provided an opportunity for iterative evolutions of the model in direct response to the input, issues and concerns of the market participants.

After the very first week of the mediation, Grid Florida, which had a very nicely developed for-profit transco model that had already received provisional approval, brought to the table many elements that were widely well received by the market participants, including elements with respect to their market monitoring and planning and several other key features: Market monitoring, operational authority, short-term reliability and key

aspects of planning.

The transco-for-profit platforms quickly determined that they had much more consensus among the platforms than they had even realized coming into the mediation, and as a result, Grid Florida and Grid South for purposes of the mediation -- I want to underscore that, you know -- formed a coalition with respect to presentation of a transco-for-profit model to the full group of market participants. This provided a very, very stable platform for a well developed, robust transco-for-profit model that was in accord with best practices and in accord with previous Commission rulings providing provisional approval for both of the models.

They continued to attempt to refine the models to address issues and concerns of the market participants. This is where the evolution of the independent market administrator component of the RTO presented itself. The idea there was that there were key aspects of Order 2000 that really should not be filtered through a for-profit entity. So recognition of that fact, specifically with respect to public power concerns, resulted in critical functionalities being carved out by contract if you will from the transco to the IMA.

Those critical functions included such things as OASIS, ATT, TTC, critical functions that went to the very

heart of the issues, and they're all set forth in the report, the very heart of the issues that were being expressed by public power as concerns.

I want to underscore that even between the two models that emerged, there were wide areas of general agreement. This is in my view an incredible value-added contribution of the mediation. Before we went into the mediation process, we had multiple filings from separate entities. They were all over the place, and they hadn't really even sat down to look at each other's platforms or models.

The wide areas of general agreement on critical functions included market monitoring, if you'll note at page 70 of the report. Operational authority. That's addressed at page 60 of the report. Short-term reliability issues. That's at page 62. And planning. That's at page 72 of the report.

And I can't underscore enough that this represented a real breakthrough where all then of the planned sponsors within the Southeast footprint were coming to consensus with regard to critical elements of a model to present to the Commission.

If you look at the table of contents, what you'll see is we took the four key characteristics and the eight core functions from Order 2000 and we broke them down into

pieces. And we had each of the plan sponsors do presentations to the full group of market participants for purposes of feedback. The market participants were broken down into owner classification sector summaries. You'll see that, page 3 on the outline.

So then you can see what you're doing when you're working your way through the 136-page report. You start off with descriptions of the two models that emerged. Then you see the breakdown in terms of the market participant responses, and you start with Characteristic 1, Independence and Governance, and then you see the eight sector summaries.

We added the state commissions as a special sector to promote and enhance their opportunity to be fully engaged in the mediation. Some decided to take advantage of that opportunity, others did not. So you can track then each of the four key characteristics and each of the eight functionalities.

The plan provides a detailed description of both the models. I think the Staff did a nice job of summarizing some of the key elements. What I want to impress upon you, however, is that it was the goal of the mediation team to maximize the Commission's options, not narrow the Commission's options. I want to underscore that my recommendation of the collaborative governance model is directly referenced to the fact that that model represents

the most, of the two models, represented the most fully developed model consistent with Order 2000 and prior Commission precedent.

That's not to say that I'm recommending that this be the model that the Commission ultimately adopt for the Southeast. I think the Commission has a very important responsibility and challenge to work through this very valuable information from all of the stakeholders to assess the way all of the information with respect to the key characteristics and the core functions that each of the groups of plan sponsors brought to the table, evaluate them in the context of all of the stakeholder sector responses, many of which were reiterated to the Commission during the RTO workshops last week which I also listened to, and to craft that platform that the Commission determines is more fully in compliance with the goals, policies and directives of Order 2000 as it may need to be manifested in the Southeast RTO.

So I want to underscore that this is to maximize the Commission's information and options, not to narrow it.

With regard to the independent system administrator model, I think it's absolutely critical that all of the parties, certainly the stakeholders left the mediation understanding that that ISA model is not an ISO model. We are not, you know, offering out of this mediation

a choice between a for-profit transco and a traditional ISO model. As underscored in the report, the ISA model differs in very material aspects from any ISO model that we've seen on the table to date, either currently functioning or in terms of filing. And there are serious concerns that I voiced in the report that I continue to have with respect to transmission owner selection of the independent system administrator and the fact that the ISA can be removed for cause, and that that process involves a lot of TO discretion.

So I'm really concerned that the Commission have an opportunity to fully explore whether that independence and governance model complies fully with Order 2000 criteria.

I'd like to note that one of the reasons that I determined it was in the best interests of the stakeholders and of the Commission to put the model forward for consideration, even though I had these concerns, is in large part in deference to the good faith demonstrated work effort of the plan sponsors and the public power entities that were supporting that plan. They had engaged in a very structured collaborative process before coming into the mediation that really showed that they were trying to get together to solve some of these very difficult issues.

Further, it was clear to me that there were a lot

of embedded issues with the ISA model that may have been impacting public power's perception with respect to participation in the collaborative governance model versus the independent system administrator model. Many of those did not have anything to do with the independence and governance structure. Rather, they dealt with issues embedded in the rate design. More specifically, as highlighted in the report, public power is very interested, very concerned with issues of full recovery on day one of the facilities that might be used by the transmission RTO.

Furthermore, they're very concerned about grandfathering of existing transmission agreements, ETAs. They're concerned about the test for which facilities will be included in the RTO and which will not.

If you look at the ISA model and you look more specifically at the rate design, which now the table of contents will help you to -- you can actually find it -- you will see that the ISA model made very significant concessions to those interests and concerns up front in the rate design.

The collaborative governance model is certainly--those plan sponsors are certainly continuing to grapple with and try to deal with those very thorny issues that really do need attention and perhaps even some help from the Commission to resolve, but they were reluctant to

go quite as far with respect to those kinds of concessions out of concern for cost shifting and negative impact on state commission concerns with respect to ratepayers feeling that there just wasn't enough information with respect to what impact those kinds of concessions would have on the operation of the RTO or on alternate costs with respect to those kinds of concessions.

So I wanted to simply bring to the Commission's attention in this public forum that this was a tremendous work effort by the stakeholders.

In my view, it was a true value-added contribution by permitting individual entities as well as groupings by sector summaries for evaluation and reaction to the filings as they were in existence as of the July 12th orders and with respect to opportunities to impact the plan's sponsors and the evolutions of the models.

Again, I recommend the collaborative governance model as contrasted to the two models that came forth from the mediation effort and as an example of a robust, well developed transco-for-profit model, not to in any way attempt to constrain the Commission's option to look at the individual pieces of both of the platforms for purposes of evaluation and consideration of a single Southeast RTO platform for our region.

Thank you.

CHAIRMAN WOOD: Chairman Tate, do you have anything to add?

MR. TATE: Chairman Wood and Commissioners Breathitt, Massey and Brownell, very little will I add to Judge McCartney's presentation.

First I would just like to note that I think that the Commission's position of taking into consideration the state commissioners' concerns is a very healthy one.

The part of the report that we submitted tried to outline very significantly state commission concerns, and it seems that the Commission now is going to go forward to take into serious consideration those things that the state commissioners have highlighted as concerns, which you will see has been appropriately put forward to the Commission in the latter portions of the report, particularly on pages 128 going forward to I think about pages 132.

The biggest concerns here were the cost benefit analysis issue that they raised. The second was the issuance of possibly a postage stamp rate through a larger RTO and concerns about cost-shifting on that. Third was the possibility of the states not having the jurisdiction from this type of an RTO structure or the concern about their jurisdiction for dealing with the transfer of assets into the transco model, and that impact on their findings in the Southeast as to whether or not retail competition was in the public interest in each one of those states.

I think those were the issues that were lined up that we had to deal with in the mediation report. I think Judge McCartney's done an excellent job in terms summarizing the concerns that not only the state commissions had but the two models had to present to this Commission in dealing with the transco issues and with the issues for the ISA and the IMA.

Again, I think she did make a point that there was going to be maximum flexibility afforded to the Commission in trying to come up with appropriate solution on this issue, and I think it's probably better that we, at this point, answer any questions that the Commission has at this point about the report. Certainly the Staff of FERC has outlined some critical issues going forward relating to the ISO and the transco model and the input that state

commissions are going to have going forward on this particular issue.

So rather than try to embellish what Judge McCartney has done, I think at this point it would be well worth us to answer and react to any questions that the Commission itself has.

COMMISSIONER MASSEY: I do have a question. The collaborative governance model, as put forth in the report, includes this independent market administrator function, the IMA function. As I understand it, as a way to separate out some of the functions that perhaps ought not to be performed by a for-profit entity? Is that it in a nutshell?

JUDGE McCARTNEY: That's correct, Commissioner. The thought was that the independent market administrator would perform functionalities that the public power entities had grave concerns being performed by a for-profit entity. Specifically, administration of all markets that would be administered by the Southeast Power Grid or the Southeast RTO, the exercise of operational authority over the transmission system, the administration of the OASIS and calculation of TTCs and ATCs, receiving and processing requests for transmission service and interconnection except for the performance of system impact and other studies, and the assumption of the security coordinator function.

It was the view of many of the public power

participants that these functionalities really should not be performed by a for-profit entity, and they were concerned about potential institutional bias in the performance of those functionalities.

The proponents of the collaborative governance model felt that they had already gotten provisional approval for the for-profit transco stakeholder selected independent board and that that, in conjunction with the market monitoring functionality, certainly addressed Order 2000 independence requirements, but in deference to those continued institutional bias types of concerns, the independent market administrator concept for a hybrid RTO was introduced and specifically those were the areas of functionalities that were of grave concern.

COMMISSIONER MASSEY: And so under the model, the independent marketing administrator and the for-profit transco together form the RTO?

JUDGE McCARTNEY: That's correct, Commissioner. If you'll look on page 10 of your mediation report, you'll see that the graph that was presented for the collaborative governance model underscores that fact. With that separation of functionalities, the transco, while remaining robust, would perhaps not be able to perform all of the RTO functionalities required under Order 2000. It is a hybrid model and would have to be considered in the totality of the

functionalities between the transco and the IMA.

COMMISSIONER MASSEY: Now I have a question about the ISA model, the so-called C-trans model. Tell me in what way -- it is characterized by the proponents as a for-profit ISO, is it not? I've heard it described that way.

Tell me how it differs from the traditional ISO governance and concept that we have approved say in the Northeast.

JUDGE McCARTNEY: Well, sir, I will refer you back to the mediation report for details, but I will attempt to summarize.

COMMISSIONER MASSEY: Okay.

JUDGE McCARTNEY: In my view, the independent system administrator model is nothing like the independent system operator models that we've seen to date. The idea here, and the selling point that was presented in the market-based mediation did garnish a lot of support. I'm not undermining that. Is the fact that the ISA would not own transmission generation or distribution facilities in the Southeast RTO footprint.

The fact that non-ownership fact standing alone garnished a lot of support for entities who would have been shopping for a traditional ISO model if one had been available for them coming out of the Southeast RTO footprint from the IOU-planned sponsors. No such opportunity having

availed itself and having to contrast between a for-profit transco, and an entity that would not own transmission generation or distribution facilities, you can see why public power would gravitate in that way.

My concern deals with the fact of the difference in the selection of the ISA and the accountability of the ISA. Unlike traditional models where you have either a stakeholder board, which frankly the great majority of the Southeast RTO market participants did not favor a stakeholder board, they did favor a stakeholder-selected independent board, which was considered very different where the stakeholder advisory committee would, through the help of a national recruiting firm with specific delineated guidelines of minimum qualifying criteria for potential board members, create a slate for selection for the board.

COMMISSIONER MASSEY: And the ISA proposal did not include that independent selection processes?

JUDGE McCARTNEY: Did not include any of that. In fact, the only board is the shareholder board of the limited liability company that one would contract with as the ISA. There would be no shareholder or stakeholder board other than the shareholder board of the LLC. Furthermore, with respect to the for-profit issue, I don't think that it should be ignored that the filings that are on record with the Commission that were the predicate for the dialogue that

initiated in the mediation clearly demonstrate a for-profit transco bent, C-trans, you know, transco.

It was in the name of the platform that was presented in the filing so when I tried to peel back that onion to see well is it a for-profit transco or is it an ISO, or is it a whole new type of hybrid or proposed model, I saw that the ISA really had characteristics that were wholly unique to it, and this caused me a little bit of concern in terms of the immediacy of the December 15, 2001 deadline, the fact that no component of these previous filings that had put forth the ISA concept had received any Commission approval, provisional or otherwise, and the details were markedly lacking in terms of how would this really operate, how would you go about contracting with an entity that does not have any, as one market participant referred to it, skin in the game, i.e., no assets in the Southeast RTO region, but may perhaps own transmission generation or distribution facilities outside the Southeast RTO footprint who would be coming into the Southeast with our assets from the Southeast and through a limited liability company selected by the TOs from a slate that would be provided by the stakeholder advisory committee and which could be added to by the TOs.

You know, how would that translate into true independence and decisional making authority with respect to

undue TO influence over that ISA? It's very, very different than an ISO.

CHAIRMAN WOOD: Judge, could you contrast that then with the IMA that's in the CGM model? I mean do they have a board, are they like -- I mean would they be, I hate to put proper nouns on it but are they kind of an Arthur Andersen or kind of a national grid? I mean what is the IMA intended to be?

JUDGE McCARTNEY: First of all, recognizing that the IMA is a product of a hybrid RTO, you've got a stakeholder-selected independent board that the transco and the IMA are accountable and responsible to. You've got a layer of independence and oversight that comports more closely with Order 2000 criteria.

But the discussion that ensued was with respect to the IMA being a corporate entity and the IMA having a corporate board, the IMA having contractual delegations of authorities for the performance of those critical functionalities that I delineated and are referenced in the report.

Did it go far enough? I don't know. That was the discussion as we had to bring it to closure on August 31st with the last iteration of the model. The dialogue centered around the breakout of the functionalities, how much functionality transfer would

render the transco nonviable and non-robust for purposes of attracting potential divestiture for purposes of an IPO.

CHAIRMAN WOOD: Were there additional duties beyond the five that, for example, the public power folks pushed to be in the IMA that other folks pushed back, or was that list of five a pretty easy to get to five?

JUDGE McCARTNEY: Well, easy to get to.

CHAIRMAN WOOD: Relatively.

JUDGE McCARTNEY: That represented a great concession from the transco for profit plan sponsors. I mean they felt very strongly that they had a good model, that they had really worked to achieve provisional Commission approval on the platforms, Grid Florida and Grid South coming in, and that any tampering with the model produced unintended adverse consequences.

Now with the introduction of the IMA, you got concerns about split of functionalities making the RTO too cumbersome for purposes of decisionmaking and multiple layers of bureaucracy and the who's on top dialogue.

The bottom line is, the plan sponsors for the for-profit transco felt that none of them needed to be in an IMA and that was strictly a compromise. The public power, really, in my view, in addition to the great majority of the state commissions, were looking for a traditional ISO model. And they gravitated to the ISA model because there wasn't a

traditional ISO model that was on the table.

So the ISA model did evolve to a hybrid by adding a transco and it was a good faith effort. I don't want to undermine it or belittle it but the addition of that transco really was more in the nature of an accommodation of an ITC, not the same kind of transco that you saw in the collaborative governance model. So public power wasn't satisfied with this five. The for-profit transco plan sponsors felt like they had already gone just about as far as they were comfortable in going. So now would be an optimum time to look to the Commission for some guidance.

CHAIRMAN WOOD: Well, I think it's, without stating too broadly, that this isn't the only region in the country where this is an issue.

JUDGE McCARTNEY: I'm sure of that.

CHAIRMAN WOOD: This was very instructive as we're looking at all of these at the same time to really work through the details about why the pushing and shoving was going one way or the other.

JUDGE McCARTNEY: I do think that if the Commission wishes to explore the ISA model more fully that greater attention to the issue of the selection of the ISA and the accountability issues of the ISA would need to be addressed.

I don't think it's an issue so much with respect

to the functionality of the ISA. The ISA simply has the functionalities that are outlined and required by Order 2000, the eight core functions. And basically what you see is a situation where very little likelihood of real divestiture, more likely formations of ITCs and the ITCs would in all probability be reflective of current planned sponsor footprints where the transmission assets would be retained in this ITC bubble that would be functioning at the direction and control of the ISA.

CHAIRMAN WOOD: And by ITC, you mean that it would be a transmission-only company that basically utility in the south spins off?

JUDGE McCARTNEY: The ITC, as that term was used in the mediation was an independent transmission company that in itself met the Order 2000 criteria. So the perception of the parties was that it would be given greater latitude and flexibility in terms of such things as local planning and perhaps suggestions and recommendations with respect to rate design, that the assets would be retained by the ITC, and then it would be under the direction and control of the RTO entity that was hosting the ITC.

The terminology of who's on top became very volatile and counterproductive so we tried to move away from that to talk about contractual accountabilities and authorities and how true decisionmaking would be implemented

on these critical functionalities in the RTO.

CHAIRMAN WOOD: Yes.

COMMISSIONER MASSEY: May I jump in?

CHAIRMAN WOOD: Sure. We're here all day.

COMMISSIONER MASSEY: You know, we have a proposal for us out west, RTO West, in which I think there's an ISO on top and transmission companies can function within that. Was that model discussed for the Southeast at all, or was it off the table because it wasn't proposed by any of the plan sponsors in the Southeast?

JUDGE McCARTNEY: It was off the table. It was never on the table. And I'm so glad you asked the question because it's really important for the Commission to know how the mediation was structured. I looked at the July 12th orders, and what I saw the Commission or I interpreted the Commission's task for me to do was to jumpstart a single Southeast RTO from those multiple filings with respect to the IOUs in the Southeast RTO footprint.

So given the fact that we were dealing with a continuum, with a very aggressive and structured history with all of these plan sponsors and a very tight deadline where we were genuinely trying to deliver a product that could produce a viable platform for purposes of December 15th, 2001, we worked with the products that were already in various levels of development from those plan

sponsors. This is why SPP was not on the table after the first week. SPP, regrettably, although having many, many critical functionalities that were well received by the market participants, and which had found their way into various aspects of both of the platforms, was unable to find a partner IOU from the Southeast RTO footprint. Absent that, having no viable mechanism for a supporting plan sponsor within the Southeast RTO footprint, that model was not a product, a viable product for purposes of presentation, debate and discussion with the market participants standing alone. SPP standing alone without partnering with at least one of the plan sponsor proponents was not going to be able to provide a viable platform for the entire Southeast.

MR. TATE: If I could add one other comment. All of the parties that participated, not just the IOUs, public power, the marketers, industrial users, pushed back on SPP because of the California experience and the fact that they had a stakeholder board. There's a big distinction between a stakeholder board for an ISO and a stakeholder selected board for an ISO.

There were a lot of people that talked about their acceptance or willingness to have stakeholder selected board for an ISO. There were a lot of people that talked about their acceptance or willingness to have stakeholder-

selected boards but not to have a stakeholder board in and of itself as an ISO concept. So that's a very big distinction. It sounds subtle but it was a huge distinction in terms of the acceptability of an SPP-type model in this experience, and a lot of it was cited after the California experience.c

JUDGE McCARTNEY: I'd like to add that really I don't know all of the dynamics that went into the failure to stabilize a partnership between SPP and any of the IOUs in the Southeast RTO footprint. I frankly thought the SPP model had a lot of really valuable elements to it and I made a serious and aggressive attempts to provide a stabilization of a partnering between SPP and either Entergy or the Grids groups, or the C-trans groups, and to no avail.

The Entergy relationship, with SPP, as you know from the filings, already had issues that were evolving and those issues were exacerbated by the intense scrutiny and involvement of the 200 plus market participants in the mediation. It wasn't my decision, it was a function of the feedback from the 200 plus market participants and the lack of a stabilization of a partnership with an IOU in the Southeast RTO footprint that resulted in SPP not moving forward in the same way that the collaborative governance model or the ISA model did through the mediation.

I hope that that does underscore the very narrow

focus and the reasons for the narrow focus that drove the evolution and development of the two models that came forward in the report. This is why I want to underscore that as the Commission moves forward to rulemaking, that they not be so constrained, that they have the opportunity to fully evaluate all of the current models, platforms, suggestions, ideas, feedback. I do think that the mediation report is valuable because it gives you, from the parties themselves that will be most directly impacted from a Southeast RTO, you know, what their views are with respect to key characteristics and core functions.

COMMISSIONER BREATHITT: Let me ask the staff or Dan or Shelton, didn't we not say though in a order around July the 12th that if SPP found a better home with the Midwest that it was free to explore that as well?

MS. FERNANDEZ: Yes, ma'am.

COMMISSIONER BREATHITT: Alice, what was that? Was in that order or a subsequent one?

MS. FERNANDEZ: I think it was in the Southeast order that the Commission said that SPP could participate in the Southeast mediation but also recognized that it might want to go to the Midwest, and I think they have had discussions with the Midwest.

COMMISSIONER BREATHITT: Pardon me?

COMMISSIONER MASSEY: I saw a press release last

week that the formally merged?

COMMISSIONER BREATHITT: Yes, we got press releases on that. Bill, were you --

COMMISSIONER BROWNELL: Go ahead.

COMMISSIONER BREATHITT: In terms of public power in the Southeastern region of the U.S., has the Staff in their analysis, how important do you feel it is for public power to participate in an RTO that actually becomes -- RTO or RTOs -- that actually become up and running in the Southeast?

Doesn't public power have a larger footprint in the Southeast than other parts of the U.S.

MS. FERNANDEZ: Yes. Without the participation of public power, there would be a number of very large holes in the Southeast if you're just looking at the IOUs, and it's more important there probably than in many other regions of the country.

MR. LARCAMP: But we faced that a little bit with Grid South with Sam T. Cooper (ph.). And ultimately after some negotiation there, Sam T. Cooper for legitimate state driven reasons decided that they were not interested in proceeding with Grid South. But certainly with the integrated transmission system in Georgia that has very heavy municipal involvement and TVA, for a regional solution you need to bring those facilities under regional control.

COMMISSIONER BREATHITT: How much was, if you can give me a short answer, how much was TVA a part of the discussions, either Sanjeve or Jonathan or any of you that wish to answer?

MR. TATE: Yes. Commissioner Breathitt, I did a lot of the ground work with Judge McCartney on the public power issues, and TVA did participate throughout the entire mediation process. They did not want to involve themselves in sector voting or in identification that way, but they had individual meetings with us, with a number of the plan participants. And in the end, they did issue a statement and comment supporting any one of the models that they would work with. They were not willing to join, but were going to work with whichever model came out of the Southeast.

What I'd like to, if you would indulge me just for a second, to spin off of your question about public power. Public power is critical in the Southeast. I don't think any viable regional transmission organization in that region will work without the participation of public power. Public power supported the ISA. However, in the final round of discussions and submitted responses, most of them indicated that they were more concerned not with that structure as they were with the commitment for full recovery on day one. And that they had indicated in a number of their comments that the ISO models of the traditional sense

were acceptable.

But the critical factor for their support was the fact of full recovery day one for their transmission facilities which was a commitment that was unequivocally made in the beginning by the ISA Group, C-Trans, and was not made by CGN. Then when there was a clarification later on, regarding exactly what the ramifications of that would be, impossible cost shifting, there were language that was put in which they all identified as having a concern.

So the reason why I go into that is that I want this Commission to understand that the ISO concept was a concept that they were familiar with, that they felt most comfortable with, but their support of ISA was, in a large part, predicated on the commitment to full recovery day one for any participation in the Southeast RTO.

JUDGE McCARTNEY: Commissioner, as you, yourself, have indicated, not just public power but the state commissions really need to be fully involved and fully engaged in the Southeast RTO.

As you well know, when you grapple the resolutions of these issues with every layer of movement in the RTO, you have layers of complications that impact market participants differently. If you add a for-profit component, it has residual penumbral impact on public power and on the state commissions' concerns. Both of those models raise those kinds of issues.

If you add a transmission-owning element to the RTO, it has penumbral impact on public power and state commission concerns. The tradeoff that you're looking at in balancing is how much value added contribution to the repair, maintenance and upgrade of the transmission facility are you going to get from a viable, robust transco? I'm just hoping that the mediation report provides you some information you may not have had in this forum before from the Southeast to help you with those decisions.

COMMISSIONER BREATHITT: No. It's definitely been a wonderful document to continue to have for me to go through and look at all the processes and the difficulties.

I think that the Southeast isn't unique in the concerns that it has for cost shifting state commissioner input. But I will say I think the Southeast is somewhat unique among the other regions of the country in that it truly does have low cost power and that has so many associated issues with it. That's the baggage that the

Southeast has.

And the Commission's going to have some tough decisions to make in the Southeast. It's perhaps been the section of the country that's gotten the most negative criticism for being Johnny-come-latelies, but it also has that very real issue that is present in that region of the country in that it's already low cost, so you don't have a lot of the reasons that are so readily apparent to go to totally restructured markets. You don't have industrial customers. We heard that California had a lot of its industrial sector clamoring for restructured markets and open access, and I don't think we've had the same apparent reasons in the Southeast, and it's just made our jobs more difficult. And I think that the cost benefit analysis that the state commissions are asking us to help them with in the Southeast is going to become important.

But your report and the work that the 200 participants provided for that 45 days I think has just been invaluable in helping the Southeast move forward to its next big hurdle.

COMMISSIONER BROWNELL: I just have two quick questions and a comment. It's unclear to me in the collaborative model who does transmission planning.

JUDGE McCARTNEY: The ultimate authority and responsibility for the transmission planning is going to

rest with the transco and the independent board of the transco, the stakeholder-selected independent board. The ITC component which was a compromise to that model to accommodate interests such as those presented by Energy permit limited local planning, and that was considered to be a very valuable benefit.

COMMISSIONER BROWNELL: And market monitoring is with the IMA?

JUDGE McCARTNEY: The market monitor is over the entire RTO. The market monitor is one of the most valuable contributions from the whole process, because Grid Florida did such a good job putting together a strong market monitoring functionality that it was adopted by the collaborative governance model and it was endorsed by the C-Trans independent system administrator plan sponsors. But it's over the entire RTO.

COMMISSIONER BROWNELL: Good. I would only add to the comments on the cost benefit study that we have to start considering other impacts that are not explicitly clear to us now, and that is the price that we're paying for transmission constraints and the lack of investment in transmission which I think is a really serous issue in the Southeast, certainly from what we heard last week.

JUDGE McCARTNEY: Yes, ma'am. And also the things that are not so apparent are the escalation of TLRs

throughout the transmission grid, the difficulty in getting access as reported by delayed plan studies, and the timeliness of getting real time information to be able to conduct viable, competitive business decisions. And with respect to the national energy policy issues, real issues about the condition of the transmission grid, you know, for purposes of repair, maintenance and upgrade.

COMMISSIONER BROWNELL: So it's conceivable that some of those low costs are masking other problems?

JUDGE MCCARTNEY: Yes, ma'am.

COMMISSIONER BREATHITT: I agree. I think there are a lot of intangibles that are harder to articulate and quantify but if we can do that, that would be helpful.

MR. TATE: If I might just add one tidbit. We did make, Judge McCartney and myself and the mediation team, some pretty strong overtures during the mediation process to have state commission formal involvement, whichever formal government structure was actually adopted, because we felt that bringing as has occurred, as you know, Commissioner, Brownell, up in the PJM region, we actually had an advisory council just for commissioners to work with the board of directors of the independent board of PJM.

And that always helped to develop education, information and an understanding of each other's concerns going forward on reliability as well as rate issues. And it

was something that we thought, and we actually put in the report, that was strong. That's why I was glad to hear today the Commission take this leadership role of directly including commissions more and more in this collaborative process in trying to solve these issues on cost-shifting and rate impact and reliability.

COMMISSIONER BROWNELL: Did all of the state commissions participate? It seemed to me you said only some did.

MR. TATE: They all participated in an informal way. One commission, Arkansas, participated I'd say in the most formal way, because they actually came into the process for sector voting and the like and went on the record.

All of our discussions with commissioners that came to see us did not come on behalf of their commissions individually, but they came to express, you know, what their state concerns were. The motions for rehearing that were filed in August I believe, August 13th, those took the formal positions of the various state commissions.

But we can say, and it was documented in our report, that a representative or a number of representatives from each state commission came to Washington or conference called with us during this process so that we were able to get their concerns.

COMMISSIONER BROWNELL: Thank you.

COMMISSIONER MASSEY: I have one more quick question. I thought Staff, in your presentation, I thought I heard you say that you thought the ISA model as presented in the Southeast did comply with Order 2000. Am I overstating that? Did I hear that incorrectly? If so, it seems -- have you concluded that it does comply?

MR. FIRST: I think that is a bit of an overstatement. I think we said that it has the broad outline of a plan that could comply with Order 2000.

COMMISSIONER MASSEY: How would it have to be changed to comply, let's say, with respect to the issue of independent governance?

MS. FERNANDEZ: Well, I think there may be sort of differing decisions. When you're saying sort of how much you may want to improve it, I mean, I think the judge mentioned several aspects of it that the Commission might want to deal with and that the Commission has a number of options when the orders come up, that it could look at ways of giving more independence to the ISA. It could even consider it an ISO-type model. So I don't know if we would say that there are specific things.

I would be careful about saying there are specific things that have to be changed to comply with Order 2000, because I think you would really be looking at, if you went with that type of a model, what changes would you need

to make to make the overall proposal reasonable.

COMMISSIONER MASSEY: Well, I know there's a lot of moving parts, and it would take us another three hours to describe all those. I guess I was focused more on the selection process and the concerns about independence there. Do you agree that that is a legitimate concern?

MS. FERNANDEZ: Yes. I think there are some areas of legitimate concern there that if the Commission were to look at that model, it probably wouldn't want to go through and make some changes.

COMMISSIONER MASSEY: Thank you.

CHAIRMAN WOOD: To whom is the independent board of directors of the CJM accountable? I know that it was selected by a stakeholder advisory committee. But do they have a fiduciary duty to the profitability of the transco from that day forward, or to the operations?

JUDGE McCARTNEY: Their accountability is back to the SAC, until such time as they go to IPO, and then it would be shareholder accountability.

CHAIRMAN WOOD: And the IPO timeline was after two years. Is that right?

JUDGE McCARTNEY: Five is what they were looking at.

CHAIRMAN WOOD: After five.

JUDGE McCARTNEY: There were all kinds of issues

like put-right periods and grandfathering ETAs and phase-in of recovery of facilities and those kinds of issues that they were trying to encompass in a reasonable timeline to a viable IPO.

CHAIRMAN WOOD: Okay. If the CJM had made the accommodations on rate design that public power was interested in in the ISA model, am I kind of reading between the lines here that that's the main difference? Is the accommodations that remain to --

MR. TATE: I made that statement more in line with their support for the ISA because of that commitment.

CHAIRMAN WOOD: Okay.

MR. TATE: If that issue had been a toss-up, there were still the issues of the comfortability of the public power entities with an ISO concept. And this now starts to get into the more obstreperous issues of what is their statutory mandate under their bonding and their tax exempt status? And turning over operational control as opposed to divesting their assets seemed to present another level of issues.

Now we didn't explore whether or not those issues are legalistically real. You know, are they really that much of a deal-stopper? But what I wanted to give the Commission a clear view of was that because the ISA did make the commitment originally for full recovery in the rate

design issue, they were significantly able to get support. But when that unequivocal support was changed because of language and ambiguities arose, there was concern from the public power entities about that issue going forward keeping their support.

So there's a two-part answer here. One, that's a huge issue for them in terms of the rate design. But their historical viewpoint was that an ISO concept they would be more comfortable with, and they thought it would be simpler for them to participate because they had their tax issues and they had a lot of issues that had to deal with their statutory mandate for establishment.

COMMISSIONER MASSEY: Just real briefly. Am I remembering what you said correctly that the states that participated also supported the traditional ISO-type concept?

JUDGE McCARTNEY: That's what I said, yes, sir. As contrasted to a transco for-profit model or the ISA model that was on the table. We continued to get feedback -- and you'll see those in the formal filings as well -- that they really prefer a nonprofit, nonownership RTO entity. And that having to have them focus on the products that were on the table for the Southeast RTO market was a challenging task.

MR. TATE: In that regard, it wasn't unanimous,

but there was more consensus from the state commissions that way. And it did revolve also around their concerns about the transfer of assets and divestiture.

CHAIRMAN WOOD: Clearly, we heard that last week. That puts a pretty big kibosh on the CJM model if the state says you're not able to transfer -- of course, I do think that on your little chart on page 10 you do allow for them to have standard transmission operating agreements with munis, co-ops, investor-owned's that don't unbundle and things like that. So I mean it seems to encompass that.

Why does that ability to have an operating agreement but not ownership -- why are the publics, why are they not okay with that? Because that can allow them to do, as I think some of the publics out in the West are doing are in the middle part of the country are doing, joining in the transcos in a way that preserves their -- works around the tax issues.

JUDGE McCARTNEY: It seemed to be much more of a philosophical issue than a pragmatic issue.

CHAIRMAN WOOD: That they're doing it with a for-profit entity as opposed to --

JUDGE McCARTNEY: Yes. I would recommend the comments filed by the Arkansas State Commission to you. I thought that they were very thoughtful and represented a lot of background and information because of the full

participation in the process. And you'll notice that they start off with the comment that they would really prefer to be dealing with a nonprofit, non-ownership ISO model, but that given the two models on the table, their preference was for the collaborative governance model, and they gave you the reasons why.

CHAIRMAN WOOD: Herb, based on your experience in the past and looking at that diagram on page 10, would the PJM analogy to that be a little box underneath the independent board of directors that would be a regulator advisory commission that feeds into that board?

MR. TATE: It's actually off to the side.

CHAIRMAN WOOD: But it's like the stakeholder advisory group?

MR. TATE: Yes. In other words, we were very active in the PJM area. Commissioner Brownell I guess I can mention was in Pennsylvania at that time. And the issues for a strong, regional transmission group was that they had a very good relationship with their states. Now here we have cost-shifting issues. Back then, we didn't have that problem because we went directly to ISO. But what we did have were huge issues on reliability, and then the transformation of that marketplace over a period of time, because we all had retail competition.

We made a very strong case, and the transmission

owners, PJM accepted it that the state commissions had to have their own advisory council to deal directly with their state issues, particularly because those commissions would be representing the governors of their various states on these very important issues.

So they were willing to give us a separate advisory council role directly to the board of directors, the independent board, separate and apart from any other group.

COMMISSIONER BROWNELL: I would just add that as that transformation was taking place, the involvement of the state commissions who pretty much worked in tandem was critically important to ensure issues like independence. That oversight and the gentle nudging that took place as that transformation began and worked its way through I think was important. So I think it's something we really ought to consider.

COMMISSIONER MASSEY: And it seems to me that -- I don't want overstate this -- but what I've heard about the way that the state commission involvement in PJM works is they are very active, as I understand it, in the PJM processes and generally speaking are very happy with it. They're so happy with it that they don't want something new.

(Laughter.)

COMMISSIONER MASSEY: I mean, it's not that they

don't want us to move forward with RTOs, they just like what they have so well that they're afraid that their role influence, that the benefits will diminish if it's moved to a single RTO for the Northeast. So that's a different perspective. And an interesting perspective I think. This is working so well, don't change it.

MR. TATE: Well, we did develop a great relationship, and I think, you know, having weathered the storms of the last few summers in terms of market and price volatility, reliability, people have gotten a certain confidence in that model. It's not that that cannot be transformed into the new models in another way. But, of course, you know, you're much more comfortable with the people that you know than the people that you don't know.

But all of this adaptable and flexible, and it was done in that context at that time. I'm pretty sure we can get past those problems and move on to the new day. Although I'm not here to speak on behalf of that model at all.

(Laughter.)

CHAIRMAN WOOD: Anybody else?

(No response.)

CHAIRMAN WOOD: The exit question is, when the Commission moves forward on this recommendation, knowing what you know now, since you've issued it on September 10th,

since RTO Week, since everything else that's up in the air right now, what would you do?

JUDGE McCARTNEY: Listening very carefully to all of the workshop presentations that I could from my desktop which, thank you again for that technology, meeting with the parties, working side-by-side with them for 45 arduous days, looking at Order 2000, looking at the emphasis on our transmission grid as underscored by the tragedy of September 11th and how that impacts the importance of the transmission grid and the national energy policy, I would at this point take all of the wonderful information that's been provided and I would carefully through the wonderful expertise of Staff sift through what you've got, because you've got a lot of really good stuff.

And try to break it down into essential elements. Not essential elements of functionalities. You've already got that. Order 2000 is a viable, cohesive document that's gone through APA Rulemaking Notice and Comment. But rather in terms of trying to decide what are the essential elements of the independence and governance scope and configuration characteristics of an RTO that would apply nationally first. And then add layers of complexity as you feel necessary and appropriate in response to Rulemaking Notice and Comment for a particular region.

By that I mean do you want to add a layer of for-

profit motive or incentive? If so, what would the character and the flavor of that be? Do you want to add a layer of sophistication that comes from ownership of assets? If so, what's the benefit or the tradeoff from that added layer of complication? Or do you want to stay with the essential elements of an RTO entity for the performance of the Order 2000 key characteristics and core functions?

It is my view that the Commission is on track and is well advised to proceed in the way that Commissioner Brownell has suggested and in the way that Commissioner Massey has underscored to something that is an evolution of and consistent with all the rich history, previous process and previous filings that we've already gotten to date, that we not move away from that.

The sooner that the Commission is able to establish a truly independence governance RTO model, the sooner you will have help in dealing with, from the state commissions and the market participants and the stakeholders, through that RTO entity, which will be of course an entity subject to FERC jurisdiction for purposes of continuing to work out and hammer out the more complicated and difficult issues of things like congestion management and planning and all of those other things.

MR. TATE: I'd just like to add that Judge McCartney has indicated that our report basically tried to

work with the parties and what they wanted to bring to the table. I think when we issued this report we recognize that you, the Commission, have a larger responsibility. That is looking at the nation as a whole, looking at various models that are working, and looking at various new models that are being created to correct old problems.

I would say that, and of course, having been a state commissioner, that you are in a very unique position to put forward an initial plan, okay, on what would work, where you have principals that would be able to structure the first stages of putting these larger RTOs together. I think the benefit of this process that we had in 45 days is that all of the parties, whether they are sticking to their original positions or not, but a lot have moved, they learned a tremendous amount about each other. We had a lot of compromise and a lot of identification of best practices.

Public power is a critical element in the Southeast. And the concessions that probably need to be made, the idea of this ISO. As you can see from Staff, there are some issues and some problems with the ISA in terms of just compliance with FERC Order 2000. The ISO is probably going to go a long way to bringing that entire consensus together in the Southeast. Does it mean that a transco model can't work within that structure? I do think that that is capable, and as Chairman Wood, I think you've

indicated, the West is actually trying to come up and propose that.

So I'm going to be much more -- or I'm sorry, Commissioner Massey, you may have mentioned that. I'm going to be a little bit more pointed that, you know, you have all of the tools in these reports, and you have your precedent from other areas of the country that will enable you to fashion I think an initial state. I think we're in an evolutionary process, and a process where all the market participants have to have confidence in what the overall structure is. And we were really in a mediation where we started with what the parties gave us and we had to work toward a full consensus-building process based on those limitations. But I do think that this Commission has a wealth of information and much more creativity to go beyond what we've done and what we've recommended.

And I've listened to your questions, I've looked at the documents, the documents of Staff. And clearly, the ISO model is being able to present a much more unbiased view for all market participants. And I think I would, you know, call that to the forefront.

How the functionalities are to go, I do believe that, you know, because we had 45 days to do this and those of us that worked in PJM, it took 18 months to really iron out a lot of these steps, there needs to be an ongoing

established formal process to getting to the characteristics and the functionalities so that all the parties can get into an agreement with this.

And that work with state commission involvement hopefully will be able to make your job a lot easier. But I do think that you can form basically the process for that. I do think that you can go well beyond what this mediation report has said.

Because even today, what we've learned from the subsequent hearings that you've called, from the comments that have come in afterwards, there is clearly a need for you to get close coordination, not within a region, but between regions. And you have to have the confidence in the structure that you're going to establish that those can work together.

So I'm going to be a little bit more pointed than Judge McCartney at my own risk at this point in time. But I do agree with her and say that she started out, you know, really having to handle this process under the constraints of what the mediation goals were, and that was to take what the parties were willing to put on the table.

CHAIRMAN WOOD: We thank you, as does America. And I want to thank our fine Staff for their work.

MR. TATE: Thank you.

SECRETARY BOERGERS: We would turn now to a

similar discussion of the RTO efforts in the Northeast. And there is a Staff presentation by Doug Matyas. And, Mr. Chairman, I'm going to get Mr. Garcia on the speaker phone so he can listen and participate in the discussion.

(Pause.)

Okay. We're ready to go with the Staff presentation. I'm going to put you on the speaker phone.

MR. MATYAS: Good morning, Mr. Chairman and Commissioners. My name is Douglas Matyas. I'm with the Office of Markets, Tariffs and Rates. With me today is Valerie Martin, Alice Fernandez and Steve Rodgers, also with the same office, and Kent Carter with the Office of General Counsel.

The mediation proceedings for forming a single Northeast RTO were conducted from July 24th through September 7th. The proceedings were widely attended by generators, load-serving entities, marketers, transmission owners, state commissions, et cetera.

On September 17th, Judge Young's mediation report to the Commission was issued on the proceedings. Attached to the mediation report is a business plan developed by the participants to implement a single Northeast RTO that specifies alternatives in areas of disagreement among the parties.

The business plan contains three governance

options and three market design options. You have been provided a copy of the Executive Summary of this business plan.

Since the Commission issued its July 12th RTO orders involving the ISOs in the Northeast, five significant orders relating to the refinements in existing ISO market designs have been issued. These orders addressed clarification that ISO New England may continue to work on software for standard market design; changes to ICAP programs for ISO New England; changes to ICAP programs for New York ISO; dismissal of a complaint requesting termination of PJM's ICAP requirement and big caps on energy; and also approval of a pilot program to reduce congestion between New York ISO and PJM through redispatch.

This concludes my presentation. We're available to answer any questions you may have.

CHAIRMAN WOOD: Let's invite Judge Young, the author of the mediation report. We also have former chairman Joe Garcia on the phone. Joe, can you hear us?

MR. GARCIA: Barely, I can barely hear it. I now it's Pat's voice but that's the best I can do.

CHAIRMAN WOOD: I won't be talking that much. Let's figure out the best way that he could listen in.

Judge, why don't we start with yours, and I'll let you jump right in and go beyond what the written report is and talk about the character of where we are today. And some of the issues that we need to talk about to get over the hump here.

JUDGE YOUNG: Well, Mr. Chairman and fellow Commissioners, my segue to your questions can be brief. The entire mediation exercise in the Northeast was structured to produce a viable blueprint for the development and implementation of a single RTO for the Northeastern United States as its primary deliverable. I purposely confined the mediation to the procedural task of formulating a business plan for a subsequent going forward process of RTO development and implementation, an essential element of which will be stakeholder resolution of numerous substantive issues in accordance with the milestones established in the

business plan.

The report that I provided on September 17th supplements and clarifies the plan where I believe such supplementation or clarification will assist the Commission in its evaluation of and in further orders concerning the business plan. Those areas specifically include the post-mediation process and governance, market design, technology assessment, stakeholder process. And I refer you to both the Executive Summary contained in the business plan, which is pages 3 through 13, and also my brief summary in the report for the essential elements of the business plan. And I would not presume to attempt to restate those elements here. The parties did excellent work laying those out in a very clear fashion for the Commission's consideration, and with the exception of the areas which I have highlighted in my report, I feel it is very clear and viable insofar as it goes. And I would turn it back to the Commissioners to direct any questions to me on which I could be of help with respect to the issues that I specifically highlighted in my report.

CHAIRMAN WOOD: Let's take the first one first; Governance and the Stakeholder Process. There were three options that came out of that. I wonder if there was ever any discussion about having a board that was actually independent and not kind of representational? You get seven

smart men or women that aren't on some other board today and aren't from some other region today. I just wondered if we want an independent board, maybe we ought to get it the same way we get the other independent boards rather than kind of fight over divide it by load, divide it equally, permanent, long-term, short-term.

JUDGE YOUNG: Well, during the course of the mediation it was the consensus that there was great value in retaining the expertise from the existing boards.

CHAIRMAN WOOD: I guess I'm reading from the comments that there was also great angst with that same problem and I'm wondering if the negatives outweigh the positives. Clearly, these people, the wise seven, could be picked from the ones you've already got on the boards but at what cost? That's the only question I have.

JUDGE YOUNG: I can't answer that.

CHAIRMAN WOOD: Joe, can you hear us?

MR. GARCIA: I can barely hear pat.

CHAIRMAN WOOD: Why not put that phone, how long is the cord? How long is the cord on the whole phone?

(Discussion off the record.)

MR. GARCIA: Mr. Chairman and Commissioners, I think one of the reasons that might not have been delved into as deep as it should of is that I think it was in the infinite wisdom, although my great doubt, that the Judge

kept us on process and that's why we produced a lot of the information that's there and that it's very usable. Although I was not an early believer of that steam, it came to pass that it was very favorable.

I think at some point, your question, Pat, was addressed. And it was addressed more in a legalistic fashion and perhaps one of the few benefits of having that many lawyers in the room was the fact that at some point, someone said, look, once this board is appointed, they will have a -- this interim board or a new board -- they will in essence have a fiduciary duty to respond to the needs of that board, and not necessarily another group.

And at several junctures during the presentation, some people, for example, the PJM group said you know, we have a, we have a -- and they said it much to their dismay, we have a lawyer from New York on the PJM board and that he had been very efficient and effective. I don't think they meant it in a negative way. What they tried to say is, look, you respond to the board you sit on. But I don't think it was flushed out much more than that.

COMMISSIONER MASSEY: So the argument is you can select the board members from the new board, you can select them from the existing boards because they have the expertise now and once they get on the new board, you make it very, very precise, and very, very concrete what their

fiduciary obligation is. It's to the broader region, it's not to their former more parochial interest.

Is that an accurate statement of it, whoever wants to respond?

JUDGE YOUNG: In my understanding that is an accurate statement of it, and I note in my report that it very well may be desirable for the Commission to consider, if not require, that the RTO board members be RTO dedicated board members, that is, have exclusive fiduciary duties to the RTO and not to their respective ISOs.

MR. GARCIA: I would agree with the Judge's assessment of that. I will say that there was some personality games that play there strategically. You know, well, if we get this guy off here, then he won't be on this one but he'll be on that one and things like that. But as a broad statement, I think the Judge is absolutely right.

CHAIRMAN WOOD: On the business plan issue, which is the second broad set of, or I guess Market Design I think is what it's labeled, there are a couple of options there Judge; 1M, 2M and 3M. You and I assume Joe came down with kind of a 1M/2M hybrid. I was trying to piece that together and --

JUDGE YOUNG: I can't legitimately include Chairman Garcia in my recommendation. But what I did come down with in my evaluation and my recommendation for the

Commission's consideration was that the up front best practices, evaluation, identification, implementation, and technology assessment, which is reflected in options 1M and 2M, are absolutely essential. And I had serious concerns with respect to the shortened time frame which option 3M reflects being able to accommodate those two essential elements.

Therefore, in light of those concerns, I focused on options 1M and 2M and encouraged the Commission to give the most serious consideration to option 1M between those two.

MR. GARCIA: Hello?

CHAIRMAN WOOD: Jump right in.

SECRETARY BOERGERS: Do you have a comment on the options 1M and 2M?

MR. GARCIA: Yes, yes, I do. Again, I'm very respectful of the way the Judge set them up, but I think one of the problems we have is that we're in search of the perfect and we're throwing out the good, and I'm a big believer and I think the Judge states it pretty much there, is that a lot of the technology is the same or very similar. They worked off the basic platform. And so I believe that some of PJM's initial assessment, and I think it's 3M, the plan we're talking about, and you'll correct me if I'm wrong, but we can get started on systems that work, and we

know that they're working to some degree or another in the three markets, in particular using much of what PJM has learned through this process and get started. And I'm a believer that although the time frame is quick, I do believe that this is something that has to do with pragmatism.

And not putting any of the reliability issues aside or any of the other very important issues that were put out, I still am a believer, and as the Judge pointed out and I think the majority of the room was a believer, that we can move on a much tighter time frame which will produce I think much better results as we work through it and we put market into play.

COMMISSIONER BREATHITT: Judge Young, did you want to respond?

JUDGE YOUNG: I just wanted to clarify one thing, and as the Commission can clearly see on pages 78 and 79 of the business plan, Chairman Garcia's absolutely correct that option 3M support was by far the most extensive and broad-based.

MR. GARCIA: And the Judge pointed out, I think several times, even though he came to a little bit different conclusion, and that conclusion, while I don't disagree with it, in other words, to put everything and to stick to the very tight concept of best practices, but I think best practice is an evolving reality to market participants, and

what works now may not be the very best three months from now, as we put the system together. Therefore, I think that an exhaustive analysis of a year may just be too much. I think looking at what we know we have in these three systems and whether the best issues in some of these systems, knowing that we're going to have disagreements, still lends a good framework to get started in this process.

COMMISSIONER BREATHITT: Judge Young, you talked about, on page 19 of your report, that you recommend that there be an independent, non-vendor expert or experts involved in assessing the technology from the outset. How broad are you using the word "technology"? Are you talking about the software programs that are used by New York, New England and PJM, or what do you mean by a technology assessment?

JUDGE YOUNG: The technology assessment to which I am referring is the technology assessment with a larger Northeast RTO.

COMMISSIONER BREATHITT: For implementing a single market, the technology that would be needed to implement that?

JUDGE YOUNG: Both IT technology and the applications technologies.

COMMISSIONER BREATHITT: And you think that having non-vendor experts be involved will get you past the

possessiveness that maybe one design is better than another or?

JUDGE YOUNG: My concern really wasn't with possessiveness. My concern was with workability. It's one thing to make claims with respect to your technological capability and your softwares capability; it's another one to implement it and actually have it work. And it is my understanding that there is such a huge financial incentive to make unrealistic claims that those claims very well may be made and once the vendor or person who is contracted to come through on those claims is tasked with doing so, they very well may not be able to live up to the claims.

And the idea of having the independent non-vendor experts is to evaluate the claims in the going forward process, as they're being made, to make sure that they are realistic and that they can do what is represented they can do.

COMMISSIONER BREATHITT: I'm not directing all of these questions just at you. Who, if any of the Staff want to answer, is that the biggest hurdle for forming a single Northeastern market, is melding three markets into one, and how you do that and what technology protocols are used?

MS. FERNANDEZ: Well that has been a consistent issue in the Northeast. And I mean I think there are sort of two issues that come up. New York and PJM both now

currently have LMP systems in place, but there are some differences between the two models.

Admittedly, New York has had a number of problems with its software in its first year of operation. A number of those are being fixed.

In New England, New England started out with the assumption that it was going to come up with a congestion plan fairly quickly, and it's taken a very long time to get into a fact. They ultimately decided this year that the best thing to do was largely to adopt the PJM market design basically for the energy markets. I think they were still considering doing some things differently for the ICAP markets, and that they wanted to start working on the software for that. And that was still going to take I think at least a year or so to actually get in place, so that the time it takes to get some of the improvements in the software has been a major issue in both New York and New England.

COMMISSIONER BREATHITT: What did the report say on still keeping three control areas, or did it address that?

JUDGE YOUNG: My report?

COMMISSIONER BREATHITT: Yes.

JUDGE YOUNG: My report did not address still keeping three control areas although what is I think

implicit in the business plan itself is that there will be an evolutionary process from the state, as we have it today, to the state of the completely integrated RTO at some point in the future, which covers all of the three, actually four control areas, including PJM West.

COMMISSIONER BREATHITT: PJM West. Anything more on that?

MS. FERNANDEZ: I know that some of the state commissions had expressed some concern about immediately moving to a much larger -- I think some of the other participants too -- and that even with an integrated market for a time, it might operate more as a hierarchial structure, where it would be coordinated but you might maintain the separate control areas.

CHAIRMAN WOOD: I really don't have a big problem with that. I mean I think there are advantages to having a single control area, but I remember reading pretty early on after the July reports, Chairman Helmer from New York came out and said, you know, we can work with this concept but here's kind of some things that are real important, and that was the first one on the list.

And after having talked with Staff about what those implications are, I think they make sense, and so -- when I heard sitting actually in Alice's -- in your seat last week, our new friend, Chairman Reilly from Maryland --

(Laughter.)

CHAIRMAN WOOD: It's okay to be a straight talker in this Commission. I like her. You know, they have a good thing and they don't want it to be diminished by where we're going. Which, to me, I guess it's kind of like you love your mom. I mean, of course you want it to be that way, but we haven't said that, so I'm willing to say for all four of us, we want it to be that people are better off as a result of what we do, not diminished to the lowest common denominator. So let's do that.

But transitioning in a manner that really allows the three to continue on their day-to-day business because they've got some extremely important business to do. I mean, all these markets, I think it's up to Vermont, are open for, or at least are beginning to be open for retail competition, and I certainly don't want anything we do to impede that. I'd rather take longer to get there with integrating markets that are at least up and supporting healthy energy markets across this region than zoom into something that detracts people from their day-to-day business.

So I don't know which business plan is any better than the other on that. I mean, two years, three years, certainly are pragmatic time lines for me just thinking out loud, but technology assessment is a big issue. I mean, I

have looked through that in ERCOT and I know that that is absolutely a show stopper and with all these parts of the country going the same place at the same time, there aren't a lot of vendors that do this and do this real well. So that one or two or three vendors are going to be overtaxed already on resources because everybody's doing this at the same time.

I think we've got to be realistic about a time frame here because of the computer issues that Linda asked them really straightforward, good questions about because that's the show stopper here.

So I don't know. I just wanted to say I think you can have what are very different from the first discussion, you have here, you know, compared to the rest of America, very mature markets that we want to make sure go from good to very good or from very good to excellent. And I think we can do that in a very different manner than we're talking about both in the Southeast and the one that's in between in the Midwest. I think they are all different evolutions of market and we can customize how we get there in a way that makes everything better off at the end of the day rather than deviates through the swamp.

COMMISSIONER BROWNELL: Pat, I'm glad that you recognized, because I think we've all recognized that there are very different stages of maturity in these markets, and

we may have to approach them differently. Certainly we've had some conversations about the West and how we get to the place we want to be acknowledging kind of the issues there, and I appreciate the need to be thoughtful and go cautiously and make sure this is value-added for everyone, but I also, from my personal experience, and I think from what we heard from some of the commissioners who have gone to retail choice, last week, is that some of the inconsistencies between and among the existing ISOs are in fact working against successful choice programs because, among other things, they're adding to transaction costs which market participants are expected to absorb and which are not adding value to choice programs.

So, yes, we need to be thoughtful and yes, we need to do the evaluation on IT programs, but I think there are things that can move forward more quickly than others. And I wouldn't want to use the need for evaluation and thoughtfulness to delay things that we know we can do in a relatively short period of time. Witness New England adopting some of the software, PJM. So caution, yes, but let's not slow the train down where we don't need to.

CHAIRMAN WOOD: Yes. I wonder if there are certain categories of items that can be -- regional wide transmission planning -- to me seems like the lowest of hanging fruit, and I know there are others. And integrating

the real time imbalance market with the single software program may not be the highest fruit on the tree but it's not low either.

And I just wonder, when I read through the business plan here, it became clear to me that there probably is a stratification of issues, some of which can start getting the parties working together in a more regional sense earlier than 24 or 36 months, and that's why option 2 had some attractiveness to it.

JUDGE YOUNG: The parties do recognize that and that is one reason that on page 19 of the report, that I do encourage the Commission to endorse enhancing option 1M in case you decide to go with that one, or whatever you decide to do, by assigning priority to the identification of market systems which may be implemented on an expedited basis to capture interim benefits, as well as identification resolution of critical path issues that might accelerate phased implementation of additional market systems to the same end.

So I don't view any of the market options one, two or three as excluding the accelerated identification and implementation of anything that can be done on that basis. And I don't think any of the participants in the mediation did either. They all recognized that these things could be done, in some cases on a more expedited basis, and that was an operating premise.

COMMISSIONER BROWNELL: I would add relative not to this discussion, but to in fact what we're looking towards in the West that many of the parties have brought up similar issues in terms of incompatibility. And while we do understand the differences in their evolutionary stage, whatever the outcome of our decision is in the West, we need to recognize that we don't want to have happen what happened in the Northeast, which is three systems essentially in the same market being built up, making investment, making decisions that have I think added a level of complexity to sorting it all out that we would not want to see replicated.

We do have lessons learned here, and I think we need to observe those. I think the West made a great step a couple of weeks ago when they consolidated some functions in the WSCC, and those are the kinds of things we're looking towards.

MR. GARCIA (by phone): Commissioner Brownell, if I might, that is precisely my thinking about moving this

quicker rather than slower. The more we think about getting it absolutely perfect, the more time and the more pressure is put on other systems to get started with what they're doing. And if the Commission could delineate a pathway and set timeframes that are tight on this, I think first of all it pushes you to existing working systems, not trying to figure out brand new ones to serve all problems. And I think that is my personal view and I think many of the market participants' views were similar to that, that it gets us going in a direction so that others can follow that lead and we can fix things as we go.

COMMISSIONER BROWNELL: Thank you.

CHAIRMAN WOOD: Judge and Chairman Garcia, thank you all for your efforts. And I'll ask you the same exit question going out. Based on what you know that you've seen that has happened since your report went out, any comments on it, do you have a recommendation for this Commission about how we should act upon your report?

JUDGE YOUNG: I'll let Chairman Garcia go first on that.

MR. GARCIA: Well, let me again state that I think what the important thing that this report does is it puts out the "what". That's done. It's all in there, and then some. If you go through it carefully, you'll realize that there are some very simple questions that can be easily

answered that are part of the sub-issues that must be dealt with, and then some very complex ones.

What's left is the "who", "when" and "how". And I believe that the Commission is in the perfect position to do that.

I would also say that there are issues here that are personality-based. And as soon as the Commission can make a decision and a determination, I think a lot of that goes away. I think you have three very competent ISO staffs who, like all people who create something, love it and hold it dear against all pretenders. And I think in this case, once the Commission gives some leadership or I mean gives some pathway or decision, I think people are going to tend to follow that.

I would also say that there are four basic issues, and I don't think that a lot of those issues that were brought up as points of divergence are as difficult as the more nitty gritty engineering issues that will come about. And that is the issue of parity on the boards. I honestly believe that once that is done, in other words, once we decide what we're going to do and I, like the judge, who pointed out, I think we should let parity probably -- if parity is a concept, it should be a concept that has some type of relation to the size of the markets and what's been done and what's been achieved. And to some degree, that

does weigh heavily in PJM's favor.

But that said, I think once you put a board in place that has an obligation to do the very best it can for this new system, I think by the very nature of that, it will force people to stop looking at individual systems and looking at moving forward on the market.

The other issue is best practices. I guess I spoke enough about that. And technology was also dealt with.

And finally, the other of the four issues that were a problem, reliability. And I believe here the Commission -- I think you spoke about four control areas. I think that's only a natural consequence of where we are and where we're going to be for a while. But, you know, everybody believes that their system is unique and that there are certain issues that are involved. As a commissioner from Florida, I still argue we're unique and we shouldn't be involved with anybody else. But the truth is that on a national perspective, those issues I think no one lights to go out anywhere, and I don't think anyone running any of these systems would ever allow that to happen. And I think if ISO staffs work together and the Commission gives them direction, I think reliability is a minor issue. It's important as a central issue, but it is a minor issue in terms of real functioning of these systems.

And finally, and maybe I harken back to something Chairman Wood said at one point, maybe we should let some people take us to court here, but that shouldn't stop us. I mean, what I believe is that sort of forcing everyone to work together and yet having the cloud over us of litigation will probably hamper the work and not be in the best interest when you add the legal timeframes to that.

Perhaps we should let people take us to court and this Commission should go ahead and make some preliminary decisions about taking three to one and setting some tight timeframes, some critical areas where we can decide, and that will enable us to continue the work while the challenges begin, the legal challenges begin, and not design a good system and have to wait as the courts decide and we spend a lot of money and we find that we may be right or wrong on certain jurisdictional issues.

So if we can get the process started and those who are unwilling to work with this process for whatever reason, we'll give them an opportunity to take their grievance elsewhere, but let the rest of the process continue and with some tight timeframes and some goals that can be achieved.

JUDGE YOUNG: In fairness to all the participants in the mediation, I believe it's appropriate to say that there was no one participating that was not genuinely

interested in seeing a Northeast regional RTO implemented in an optimal timeframe. But the term "optimal" implies that it be done deliberately and in consideration of all the elements which are necessary in order to make the RTO a workable entity. And there is where I believe you have the disparity in the timeframe implementation, particularly with respect to market design and the technology assessment.

Those participants who endorse a longer timeframe, and we're talking about approximately 12 months longer, simply feel that more up-front attention needs to be devoted to ensure that we don't get halfway down the line and find out that we've got an unworkable system that we need to scrap and go back to square one and do over again. And we do have some experience in that area. And that is a legitimate concern.

Insofar as recommendations for how I believe this Commission could move this process forward, I have a number of them. They are in my report, but I will clarify them. Strange though it may seem, the terms "PJM platform" and "best practices" were the subject of intense disagreement and debate throughout the mediation. If the Commission could give additional guidance with respect to what it means, the parameters of those terms, it would greatly enhance the process going forward.

Similarly, it would greatly facilitate the

process going forward if the Commission could give guidance with respect to the governance options. As the report indicates, I do not believe the parties on their own are going to be able to get beyond where they are without further Commission guidance. So if the Commission could give guidance in that area, what it believes is appropriate out of the three governance options or what aspects of the various governance options it endorses as a hybrid, it would be very helpful in the going forward process.

Similarly with respect to market design. What the considerations the Commission considers to be most important and why would be very helpful to the going forward process.

The one thing that we really haven't touched on is the stakeholder process. As my report indicates, and I think as the business plan reflects at -- I can't locate it right now -- there is a stakeholder process strawman incorporated into the business plan. It is the most ill-defined aspect of the business plan. And whatever guidance the Commission could give with respect to stakeholder process would be very helpful, not only to the various industry stakeholders but this is an area which the various state commissions had serious concerns regarding as well. And I think that would be very helpful, are as getting the RTO to a stage where it is in fact viable and can be

implemented in the optimal timeframe.

CHAIRMAN WOOD: Any other questions for Chairman Garcia or Judge Young?

(No response.)

CHAIRMAN WOOD: We thank you very much. America thanks you and we thank the wonderful Staff. We'll take this up shortly. Thank you, Joe. All right.

(Pause.)

We'll take a five-minute break.

(Recess.)

SECRETARY BOERGERS: Mr. Chairman and Commissioners, the next item for discussion is E-3, a discussion of the RTO developments in the Midwest, and Patrick Clarey has a presentation.

MR. CLAREY: Good afternoon. My name is Patrick Clarey and I'm from OMTR. I'd also like to introduce today from OMTR Mike McLaughlin, Tony Ingram, Joe Power and Raheem Mamrikel (phonetic). This afternoon we'd like to give a brief PowerPoint presentation on the recent developments in the Midwest.

Recently both Midwest ISO and the Alliance companies filed status reports. These status reports focus on two main areas. First, their individual efforts to become operational by December 15th. And second, their joint efforts to implement the Inter-RTO Cooperation or

Seams Agreement resulting from the Illinois power settlement.

Now the Seams Agreement is an attempt by both Midwest ISO and Alliance companies to eliminate seams within the Midwest ISO Alliance region. By way of background, the Illinois power settlement resolved among other issues requests by three utilities to leave the Midwest ISO and join the Alliance companies.

In addition, the Illinois power settlement had three main goals: First to maintain the financial viability of the Midwest ISO. Second, to preserve the Alliance business model. And third, to foster seamless markets between the regions.

To put this into context, we prepared a map showing the regions we're talking about. In the blue is the Alliance companies. In the green is the Midwest ISO. And as I said before, the Seams Agreement is an attempt to work out seams issues between the two regions.

In the following slides, we will describe first what the Seams Agreement requires of the parties, and second, how and to what extent the parties have implemented those requirements.

Seams Agreement addresses seven major areas:

First, in the area of ATC coordination, the agreement requires the parties to develop a standardized

process to calculate ATC within the region. Midwest ISO, Alliance companies and SPP will calculate ATC using similar, however not identical, models. Each, however, will exchange information on an hourly basis to be used by each entity for determining ATC.

The second area is security coordination. The Seams Agreement requires the implementation of mechanisms to share security information and to work toward an agreement for reliability redispatch. The parties have established a framework whereby existing infrastructures will be used to share such information.

The next seams area is one-stop shopping. And essentially, what one-stop shopping is, is the ability for customers to go on to one interface to make a transmission request using multiple systems. Now the Seams Agreement calls for the facilitation of this one-stop shopping. Midwest ISO, Alliance companies, Grid South, PJM, SPP and TBA have all agreed on a common approach to electronically coordinate schedules between the RTOs. However, detailed protocols still need to be developed and agreed upon. And initially, one-stop shopping will only be available for hourly and daily nonfirm service.

The next seam is congestion management. The Seams Agreement requires the development of an open and accessible electronic bulletin board system for the posting

of congestion information. Both Midwest ISO and Alliance have agreed for Day One operations to use Midwest ISO's existing bulletin board for the posting of this information. Midwest ISO continues to develop its Day One congestion management procedures and it's anticipated that these will be completed soon. Both parties, however, continue to discuss Day Two congestion management procedures.

The next seam area is the imbalance market. The Seams Agreement requires the parties to cooperate in developing their imbalance market to ensure compatibility for multiple RTO transactions. The Midwest ISO and Alliance did not develop a common energy imbalance market. However, they note that their individual proposals filed in their RTO dockets are compatible.

The next seams area is transmission planning. The Seams Agreement requires that Midwest ISO and Alliance companies coordinate regarding long-term transmission planning. And the parties have established a transmission planning committee.

Underneath this transmission planning committee, two subcommittees will be formed by early next year, an advisory subcommittee and a reliability subcommittee. Final procedures for these subcommittees will be developed by early December, and it's anticipated they will be functional in early 2002.

Now the last major seams area regards market monitoring. And the Seams Agreement requires Midwest ISO and Alliance companies to jointly monitor the markets. Midwest ISO and Alliance companies have expanded this to include SPP, and all three have recently chosen a single market monitor to perform this function. The final market monitoring plan is due to be filed soon.

That concludes the major areas in the Seams Agreement. However, I also want to touch upon another product of the Illinois Power settlement, and that's the super region rate. The Illinois Power settlement called for the elimination of multiple access charges within the region. Now each entity has recently filed their version of the super region rate in their individual pending RT dockets.

Now lastly, I'd like to talk a little bit about the individual efforts taken buy Midwest ISO and Alliance companies to become operational. First, for Midwest ISO, they indicate that to date, approximately $160 million has been spent to become operational. They have staff assembled that is capable of assuming operational control over the transmission facilities by December 15th. And their physical infrastructure is in place. Additionally, market trials of its integrated systems have been completed and tested.

Alliance companies, on the other hand, have indicated that they will not be operational by December 15th. However they state they can be operational within 90 to 120 days upon final approval for their proposed RTO. They have instituted various systems such as billing, ATC and loss calculations, and currently these systems are being tested.

Other systems are currently on hold pending Commission action on the National Grid petition to become the managing member of Alliance as well as Alliance companies' business plan. Once these issues are resolved, they indicate that staffing will be complete.

And in a nutshell, that's what the two status reports have indicated, and that concludes our presentation. Thank you.

CHAIRMAN WOOD: Comments?

COMMISSIONER BROWNELL: When I hear words like "similar but not identical" and "compatible systems", I get a little nervous. Tell me if you are comfortable that when we say "not identical but similar" and "compatible" that in fact we're not looking at problems down the line such as we have seen in and among ISOs for example in the Northeast? That's the first question.

And then the second question is, is the Staff satisfied that the details of this agreement are getting

handled as quickly as possible with, as Bill likes to remind us, an endgame in sight of truly a seamless market?

MR. POWER: With respect to your first question, anytime you have differences, I think you should have seams left. But I would point out, though, that the settlement agreement the Commission approved has the terms in it "compatible". It doesn't require "identical".

So in that regard, they are moving along consistent with what was approved. I have concerns with respect to different ATC calculations and how that will affect the seamless market, different congestion management programs that they have and how that will impact.

So we do have concerns there, to answer your question. I don't know how much problem that would cause going forward, but I would just point out they are not identical so there are seams. And to me that is at least some level of problem.

Your second question: Are we satisfied on the timing of their implementation of this agreement?

The agreement set out certain dates for when they had to hit certain targets with respect to the various seven or eight items here that we outline for you, and they are on schedule. They have met those guidelines. There are I think three left that they have to deal with, and those are being worked on. And they anticipate that we file timely. So they are doing what they said they would do and what we approved.

COMMISSIONER MASSEY: I have a question about the congestion management issue. Is the commitment in the Settlement Agreement to adopt, is the word "compatible"congestion management systems, between MISO and Alliance? Talk to me about that.

MR. POWER: Actually, the Seams Agreement talks about they agree to form a single bulletin board. The idea is that sort of goes to--so there was no discussion about the overall approach to be used.

Their approaches are, by the way, very similar in that they sort of have a two-phased approach with it. For Day One operations they will be accepting bids to provide congestion management for the region, and the dispatcher will go to those bids when congestion kicks in in order to keep the reliability up.

That is the reliability aspect of the congestion management programs for both. To the extent the system operator has to do that, then those costs would then be uplifted to customers.

The second aspect of their proposal is sort of a market or a commercial element. That is, to say you're a transmission customer and you're looking to do a deal and you go on OASIS and they tell you 'no ATC,' well they are establishing a bulletin board and that is what this Seams Agreement talks about: where customers can go and there will be generator bids there and shift factors that they can look at and determine whether or not if they were to buy congestion management from that generator it would relieve the constraint and they would be able to do their deal.

And then if it would, schedule that with the RTO

and their deal could go off where otherwise it wouldn't.

So in that regard their systems are very similar.

But your question with respect to did we require identical methodologies, we did not.

COMMISSIONER MASSEY: Or even compatible methodologies.

MR. POWER: The ERCA required bulletin board, as the slide says here: Development of an open and accessible electronic bulletin board for posting congestion management info. And they have done that.

COMMISSIONER MASSEY: Thank you.

And your map that is in your slide presentation, does it assume the merger of MISO and SPP?

MR. CLAREY: Yes, it does.

COMMISSIONER MASSEY: Okay. And where is that merger in process? What is the status of that?

MR. CLAREY: I believe in a press release I read, I believe they're scheduled to complete the merger by the first quarter of 2002.

MR. LARCAMP: Commissioner, we have MISO people sitting on the front aisle if you'd like a specific answer. Someone can come forward. We have got an empty seat.

COMMISSIONER MASSEY: They're the folks with the big smiles on their faces.

MR. LARCAMP: Just for equal time, Nick Brown was

here. I don't know if he is still around.

MR. TORGERSON: I am Jim Torgerson. I am the CEO of the Midwest ISO.

The time frame for our merger with SPP, the boards have agreed on basic terms what the new board will look like. The time frame now is to get definitive agreements, and our plan is to have those signed and approved by the board and the membership in December.

Then we have to make filings with the Commission, and hopefully we will have that done in the first quarter. That's really our time frame.

COMMISSIONER MASSEY: And you would be creating an independent board, not a stakeholder board?

MR. TORGERSON: It is an independent board. It will be made up of seven members of our existing--the Midwest ISO existing board. I'm on the board, but I will not be on the board of the new company, and it will take four independent members from the SPP board and form an eleven-person board. It will be totally independent.

COMMISSIONER MASSEY: Okay. And so this is the plan: both boards have directed you to move forward to implement this plan? Is that an overstatement? What final step has to be taken before this is a done deal?

I know it has to come to this Commission, but short of that?

MR. TORGERSON: The boards have approved the plan that I just outlined with the consolidation of the two boards into a new, independent board.

They have approved what will be the structure of the transaction, which would be an asset purchase agreement.

What we have to do is move this to definitive agreements that will be executed and then approved by the boards. And it requires--some of the matters will have to have a new membership agreement and new bylaws which will have to be approved by the members, and we are shooting for December for that.

COMMISSIONER MASSEY: I would ask staff: Based upon what we know so far, we're not prejudging of course, but does this sound like it has a good chance of meeting the requirements of Order 2000?

MR. INGRAM: I think it certainly enhances it, but I would be very careful about prejudging. I think we need to see the details, and we need to see comments from interested parties.

COMMISSIONER MASSEY: I mean it certainly helps a lot on scope. There's no question about that. This is a--how big is this entity in terms of load generation?

MR. TORGERSON: It is about 120,000 megawatts that cover 20 States and one Canadian Province.

COMMISSIONER BREATHITT: Are you--I thought I

read in the press release, too, that you are contemplating a whole new name?

MR. TORGERSON: Yes. We will come up with a new name.

MR. LARCAMP: And Staff is looking forward to that.

(Laughter.)

MR. TORGERSON: If Staff has ideas, we'd like to take them.

(Laughter.)

MR. LARCAMP: Staff has an idea, but I won't say it here.

(Laughter.)

CHAIRMAN WOOD: The Trans--the one through Nebraska with XCEL, Translink?

MR. TORGERSON: Translink, yes.

CHAIRMAN WOOD: What is the status of that? Is that--

MR. TORGERSON: Translink has--we have signed an MOU with Translink, and Translink has made their filing under Appendix I with the Midwest ISO with the Commission on, I believe they did it on September 30th?

MR. INGRAM: Yes. That application is pending with the Commission now.

CHAIRMAN WOOD: Okay.

COMMISSIONER MASSEY: Now we were talking about the relationship between MISO and Alliance and how there still might be some seams.

Will there be an seams in the relationship between MISO and SPP? Like are you adopting identical congestion management, and so forth?

MR. TORGERSON: There won't be any seams. As part of the transaction, I will be the CEO of the entire organization. Nick Brown will be the COO. We will make certain that there is one set of market design rules that will cover both areas.

It may take us a little time, because we currently have two tariffs, but we are going to try to consolidate the tariffs as quickly as we can also so we have one tariff.

Now we have to work out rate issues, revenue distribution, those are what are going to take some time, but as far as market rules our intent is to get that to one as quickly as possible.

COMMISSIONER MASSEY: So this would be part of the deal. Nobody is going to be coming in here arguing that we ought to adopt the lesser compatibility standard for MISO/SPP? It's going to be identical?

MR. TORGERSON: No, we're not looking for a lesser standard.

COMMISSIONER MASSEY: And you're going to operate a single seamless market for the region?

MR. TORGERSON: Yes.

COMMISSIONER MASSEY: Okay.

MR. TORGERSON: If you can view it, we are just going to be combining. There will be one entity and it will have the same rules, market design throughout the entire region.

CHAIRMAN WOOD: Playing the contrast and compare game with what we heard earlier this morning from the Southeast parties about the items that were lifted up to an independent board and those that were left with the for-profit entity in the CGM, I believe it was called, model.

I don't know if ya'll are familiar enough with that to answer this question. If you're not, then just say so. But what would be the items that are left to the for-profit Transco and Alliance in this current setup that are uplifted to an independent, not-for-profit entity in the Grid's proposal in the Southeast that Judge McCartney wrote about?

MR. POWER: So that I understand it, are you thinking as Alliance is currently configured but with some sort of umbrella organization over them?

CHAIRMAN WOOD: Yes, to compare those two what would be the duties that today reside in the for-profit

entity Transco--the Alliance, that in the Southeast model as was discussed in the mediation among the parties down there got lifted up to I guess the umbrella organization?

MR. POWER: I'm not sure I'm following you, but let me take a stab anyway and you can tell me where I'm going wrong.

Alliance currently would have National Grid doing everything. So if you're asking me what my view is as to what we would uplift to the umbrella organization, I would think administration of energy markets, congestion management, regional planning--I'm just shooting from the hip here--ATC calculation across the region, one-stop shopping. You can go down the list.

Actually, I think if I went down the list I would pretty much throw the majority of things up. I think certain administrative functions like billing and settlements under the tariff could be done by the sub-entity, the ITC or whatever you would refer to it as, because they don't have market implications. Clearly that would be acceptable.

Other functions, you know, I'd have to go down the list and look at them to really give you a complete answer.

COMMISSIONER MASSEY: Joe, if you take the IMA concept that Judge McCartney and others talked about for the

Southeast and the way the functions are sliced and diced there between the IMA and the for-profit Transco, and you compare that to the MISO Appendix I Tariff that divides--it was adopted back when Commonwealth Edison was considering being a part of MISO and it was a binary RTO proposal, as I recall, and MISO then came in with an Appendix I Tariff to allow Commonwealth and other for-profit institutions to function within the MISO institution, that as a part of that there had to be some slicing and dicing of functions between MISO and the for-profit institution.

Are you able to compare and contrast the slicing and dicing that was done in the Appendix I Tariff that we approved versus the slicing and dicing that is proposed between the for-profit Transco and the IMA in the Southeast?

MR. POWER: Well from what I heard this morning, and I haven't read the report but from listening in, they sounded very similar. In fact, when the Judge was describing that I was thinking MISO Appendix I.

It all comes down to what, as you go through the list of what functions, that early Order you talked about with Com Ed when they first filed the Appendix I and Com Ed had its proposal, there was a laundry list of items there that would be considered to be run by the umbrella versus the individual company.

And the Commission has not weighed in on where it would stack those, but I think what I heard the Judge talking about this morning, OASIS, ATC, planning, these things would clearly be elements that the umbrella organization would be responsible for, in my view.

COMMISSIONER MASSEY: Mr. Torgerson, or someone on your row, do you know the answer to this question beyond what Joe has laid out?

I know it's a different structure. You have the ISO on top with the for-profit Transco operating within it under the Appendix I Tariff, and that is not proposed for the Southeast. But I am talking about the slicing of functions between the for-profit entity and the not-for-profit entity.

MR. TORGERSON: I'm not totally familiar with the IMA, but my understanding would be--well, for what is under Appendix I would allow a Transco can do their own, for example, planning, but funnel it up to the overall, the RTO.

Security coordination would clearly be done by the Midwest ISO under Appendix I. ATC calculations are done by the Midwest ISO. I'm trying to think of what else.

Overall planning is done by the Midwest ISO. The functions that would be left to the Transco would be anything internal to them and--I don't want to get into the Translink case, but they want to do their own tariff, for

example.

There are other aspects where anything to do in their region or in their footprint, for example obviously the maintenance and so forth they're going to do on their own. Contrasting it, it seems from what I heard they seem fairly similar.

COMMISSIONER MASSEY: As I remember the Appendix I Tariff, congestion management is the same, is it not?

MR. TORGERSON: Congestion management under Appendix I, in my understanding, they have the ability to ask for a different--their own congestion management under Appendix I.

COMMISSIONER MASSEY: I see.

MR. POWER: But I would weigh in. The Commission did encourage--it recognized that in that Com Ed Order but encouraged them to have one for the region.

COMMISSIONER MASSEY: As a matter of fact, I think we lauded the Commonwealth proposal at the time, actually.

MR. CANNON: Commissioner, if I might suggest, maybe we could do something in terms of the side-by-side as the Commission tries to parse through this issue of which functions go where. I think we could sort of try to line up what happens under Appendix I with what is being proposed by Translink and what is being talked about in the Southeast

Mediation.

That could be sort of useful I think in trying to figure out where the Commission wants to go in terms of distributing these functions.

CHAIRMAN WOOD: And I perceive this issue to have been, as we just--I think Linda pointed out in the Southeast, important to public power and also important to state commissioners who are kind of interested in some objectivity here and concerned about if that is lost somehow in a profit-driven entity that is focused on transmission only.

I would be very interested to see if we could some to some agreement as to how that split ought to happen. That could certainly make that a lot faster.

COMMISSIONER MASSEY: I would say in my mind this is shaping up to be a very important issue, how you divide--if you are going to have a regional entity that allows both a not-for-profit entity, either an IMA or an ISO, whatever, to function with a for-profit entity, how do you divide those functions in a way that is consistent with Order 2000 and creation of robust markets.

CHAIRMAN WOOD: I think where the Commission to date has led, and actually this report under E-3 between MISO and Alliance as two parties in the same region have led to, is there is a for-profit aspect that Transcos bring to

the table that has a lot of benefits to it. But it also has some things that scare other people off.

And we are trying to build bigger groups that do not have holes in the swiss cheese, that do not scare people off, and are there things that we can do with that model to mitigate some of the concerns about it while keeping that a viable investment vehicle.

I certainly would like to focus on that because I think the stand-alone transmission entities, whether they are called Transcos or ITCs or whatever we're calling them, Gridcos, have the advantage of not being, if they are truly independent, of not having generation assets to worry about playing favorites with, or power cells operations that we worry about, you know, tainting the incentives.

And so I think as an ultimate goal, as I think the Staff paper pointed out on the Southern, Southeastern Model, that the divestiture into an entity, or just the creation of a stand-alone entity not divesting it into something greater but just leaving it as whatever size it is, either one of those has some benefits for us as we see that codes of conduct only can do so much.

And corporate separation and functional unbundling and all the kind of what I call halfway terms that regulators do and we unfortunately split the baby don't really get us the independence that we need.

So there is a lot to like about the Transco Model. I am concerned, though, that if we dump all these duties into a stand-alone entity that is profit-driven whose board of directors are accountable as they should be to the shareholders of the transmission entity, that we're interested in creating viable wholesale markets. And the goals that we have for these regions of the country may not necessarily be coincident with those of a business-driven entity, at least in their totality.

There is probably a whole lot of overlap, but the more I read, the more I learn, the more I think about it, particularly after last week, it is becoming clear to me that there are some aspects of wholesale market creation that we in our role need to really think long and hard about who does them.

I think the rush toward trying to get the Transco Model out there may have in fact not thought through all that, and I am sensing that a little bit from Bill's questioning, and I've got it as well, and I just need to be made comfortable that the split is correct and is one that we can live with for the long term. Because this is kind of the last chance for us to make our cut before these things get out into the real world.

Dan?

MR. LARCAMP: I just have one question.

To the extent that we are reconsidering what Transcos can and cannot do, should Staff in its thinking keep the safe harbor provisions as they are?

Or, if we look at different roles and responsibilities for Transco, should we have the flexibility of seeking--the Independent Transco Model that the Commission has been perceiving assumes that there will be a de minimis amount of participation with in effect vertically integrated utilities that own generation with respect to the safe harbor.

So what I am asking is: To the extent we are reconsidering independence, if you will, in the Transco Model vis-a-vis certain functions, should we also consider whether those determinations of the Commission should be reconsidered?

CHAIRMAN WOOD: I'm sorry, I'm not familiar with "safe harbor." What's that term?

MR. LARCAMP: Well it's basically that there can be 5 percent ownership in a Transco basically by an entity that--help me here, Cindy--that owns generation up to a maximum of 15 percent. And that is a safe harbor that would qualify under our precedent as an independent for-profit Transco.

So I guess what I am asking is: To the extent that we are re-examining the functions that a Transco can

provide, should we look at that with that as a given? Or is that something that we would reconsider as we go forward in terms of our further discussions on what the Transco can and cannot do?

CHAIRMAN WOOD: I would put that in the paper that Shelton is proposing, the side-by-side. I mean the discussion on pros and cons of that is certainly timely.

COMMISSIONER MASSEY: Doesn't the active ownership of safe harbor phase out over five years, or--pardon me?--is it five or seven years, something like that?

COMMISSIONER BREATHITT: Well I think we might be seeing a headline tomorrow that says something like "Deathknell Wrong For Stand-Alone Transmission Companies," but when I think about the vision for the Midwest, I had seen it playing out over the short term, or maybe the long term, that we could have at least one stand-alone transmission company evolve in the United States.

To date, we have not seen that. We have got the ATC, which is a part of the MISO, and we have Transconect, which is so far part of RTO West, and we have the--we've got other hybrid kinds of transmission companies that are forming along with different kinds of organizations, but we have not yet approved a stand-alone transmission company.

And in the Midwest, there is angst about going

that next step to form an independent, stand-alone transmission company. It may be that it is a time that has not yet quite come, but I just wanted to say that my vision for either the present or the near future is that we can figure out a way to promote that model in the United States because I think it is a business model that will, in its for-profit nature, if we can get independence right and we can get governance right, can promote a lot of efficiencies and help us with infrastructure construction.

But none of these regions are going to be easy for the Commission to make their next, and perhaps toughest calls on. And certainly we have seen the Midwest as a region evolve I think quite a lot in the last 15 months, particularly with the addition of SPP into the MISO.

So I am not at this point saying whether I think there should be one entity in the Midwest, because I still have this vision that somewhere at some time I hope we will see a stand-alone independent transmission company formed, and I had hoped that the Seams Agreements that the two entities entered into would get us there.

I am not prejudging anything yet. We've got a tough decision to make in the Midwest, as we do I think in the Southeast as well. But I think we have moved quite a lot in the Midwest and we have some tough decisions to make.

CHAIRMAN WOOD: I don't know if the headline would be quite as broad as that. I do have to say that there are probably some duties that, in the pure vision of a stand alone transco that is truly independent, that even in that world probably should be dealt with on a much more public and stakeholder-driven process than just the for-profit shareholder board. And I don't know if that has to be a long list.

I thought what Judge McCartney and Herb did was actually it says here the five functions that they lifted out to the IMA were market administration, operational authority over the transmission system, generation interconnection, security coordinator, and ATC calculation.

I would love to hear, at some stage, why those five things, if that's what it took to get the public power folks and I would assume, having been one myself, state commissioners, comfortable with, maybe not just cheering up and down comfortable, but comfortable enough with this IMA and how you actually split the duties enough to give people confidence in this market, that's not a tall task. I just think this all-or-nothing approach is not real helpful, and it seems to me that if there were some body, and that may be MISO, it may be PJM, I mean, I'm looking at the map, and Alliance can go either way. I think it's more important to me to really ascertain what should be independent of this

entity that is almost independent, but even if it's totally independent still, because it's a wholesale market function that we care about, as opposed to profit incentive thing that the Alliance Shareholder Board would care about. We just need to make that cut.

And if there are not items that ought to be separated out and Appendix I really was just a relic, then let me know. I will let you know, I suppose. But that's the question I'd like to just hone in on. And I think there is a very viable business plan under that that is good at attracting capital, that is good at building America back up again, which is what we want. But it's also a business plan that doesn't allow for thwarting of the broad competitive goals that everybody should participate in, and that's where I'm going. So I wonder about leaving some of these things in a single entity may not be the best thing for wholesale market competition.

So if we can get a pro-investment/pro-market competition split of these duties, then that's the outcome I would like to find if we can.

COMMISSIONER BREATHITT: If we can do that, I'm there too.

COMMISSIONER BROWNELL: But I'd like to do that quickly because what I don't want the headline to read is, we have foreclosed a business model. I don't think that we

can have these models, these plans exposed in the markets while we tinker. I think that we need to address these issues quickly. I agree with you that in fact there are issues of importance to ensure that independence. But we have capital that's already been invested, we have capital that we desperately need in that infrastructure. So I think with the four thousand things on our list, this has got to be in the top five.

COMMISSIONER MASSEY: Yes. The other relevant question is if we're slicing and dicing functions between a for-profit entity and some other entity that is more public spirited, to use your phraseology, what functions do investors need in order to have an attractive investment vehicle. That's another question I'd like to know the answer to.

And I think when we issued Order 2000, the implication was a for-profit entity could carry out all these functions, all the functions that were listed in Order Number 2000, and if we are -- but I must say, and I have expressed it at this table -- had some qualms about that throughout the process because it has seemed to me that some of these functions need a more public-spirited decisionmaking process. But I would like to know what kind of investment vehicle investors really need, what functions do they need in order for it to be appealing?

COMMISSIONER BREATHITT: Bill, and along that line, maybe we've put the wrong emphasis on the word "stand alone." Maybe you can have a transco -- I don't know, maybe it's how we're defining stand alone that's causing this robust discussion among us all. Maybe you can have stand alone but some functions of that be elsewhere.

So if the stand along transco folks can give that some thought, help us out for the future.

MR. LARCAMP: We can give you some initial thoughts pretty quickly, but Nora, you've given us a very challenging assignment and I think that one big thing, there's clearly a tie-in to our first assignment today with the regional councils here because I think there's a real significant linkage between the state commission view and the investment community that we need to be in tune with.

COMMISSIONER BROWNELL: I like to give you challenges because you're up to it.

CHAIRMAN WOOD: What I would like to do -- is there anything else you want to say on the Midwest?

Linda?

COMMISSIONER BREATHITT: I had just a question I don't need answered because I haven't really thought it through but it's just I read a filing that was made in one of the RT dockets with the Alliance and several state commissions were responding to the settlement filings.

When we're thinking about these regional councils and state commissions are real active parties to cases and we're asking them to help us out in these areas, maybe I just had a question about how you do that.

MS. MARLETTE: I think OGC is going to have to help Dan and be creative. There is a problem where a state commission is a party and the commission can put non-advisory staff on these councils because then of course they can work with the state people and provide reports and information to the commission, but they can't be advisors, or the commission, if it wants to have advisory staff on some sort of council, then everything has to be done, noticed, and publicly open. So we'll work on ways to achieve your goals.

CHAIRMAN WOOD: There was a good paradigm that I think we all lived with in relation to having to deal with state regulatory issues before the Federal Communications Commission that allowed the commissioners from the states to interact very frequently and very heavily with their federal counterparts. And it was just a special provision of their ex parte rules, so I would suggest that we find an appropriate way to mirror that over here because if we're going to be partners with them, we need to be able to talk to them, and that's been a big part of the problem up to now.

MS. MARLETTE: Right. When we recently revised our ex parte rules, we did look at what the FCC had and we did broaden our ability to talk to the states but still had the problem where they're a party, so we'll see how much further we can go.

COMMISSIONER MASSEY: And the problem, is it a -- the problem arises because of our rules or the problem arises because of a statute that we can't change?

MS. MARLETTE: I am not sure if we have gone as far as we can under our ex parte rules but we do have to comply with other legal requirements and we'll take a look at whether we could go further but it could end up requiring us to again amend the ex parte rules.

CHAIRMAN WOOD: Whatever it takes.

To kind of close out the RTO concepts for the day, we've got a number of balls in the air. Last week we had the RTO week and the discussion about a third NOPR on open access to complete the job. We talked a lot about standardization. We have asked some great people to come give their brains to us, and we've asked all the rest of the great people with brains to write them on paper so we can read them and understand what they're thinking about, so that effort is out there.

We've got the dockets we've got here today and a couple in the West as well. We've got an investigation or

an audit of the California ISO, which is one of our existing RTO-types. We've got the regional council issue that Nora has raised and brought up and I think we've agreed to move forward on. I'm missing something.

MR. LARCAMP: Interconnection.

CHAIRMAN WOOD: We've got a NOPR on generation interconnection which, as we've heard last week, is an issue. The cost side of it is an issue as well. Got some items on today's agenda. We've got the cost/benefit commitment that we made to the states and to the parties to update our cost/benefit analysis that we did several years ago, to really focus in on some of the concerns that were raised by that.

So I would like to ask Staff, in the context of what we brought up today, to pull together some thoughts and some options about how to move forward because I think Nora's point is absolutely something I subscribe to as a matter of religious principle that what we're about is giving people certainty. And the whole point of this policy debate and of these discussions and of doing it in the sunshine and inviting the smart brains to the Commission to come here against all odds to talk to us and the conversation is that we want to make the best decisions, and then make them, and then live with them and go forward.

And I realize the awkwardness that sometimes that

puts investors and parties and all that that are moving forward but I would a lot rather sit back and think about it for a second and make the right decision about which fork in the road to take than to just blare down one and find that the bridge is busted and have to go all the way back.

So I would suggest that with all urgency, we get some suggestions for discussion at our next open meeting on the 7th of November and that the four of us kind of put that on a pretty high burner for us to come in and try to give some certainty to where we want to go. I think we've learned a lot in the past couple months and it's time to start digesting and producing some work product that will frame, if not decide with explicit detail, but frame how we're going to get these things closed out in a pretty short order. I think that will be time well spent.

So I would like to ask all the staff and senior leadership to work together on this effort with you all's consent.

COMMISSIONER BROWNELL: For sure, hallelujah

CHAIRMAN WOOD: All right. Thank you all and thank you for the presentation on the Midwest folks, that was great.

Mr. Secretary?

SECRETARY BOERGERS: Thank you. The next item for discussion is on Western Infrastructure, and there are

several staff presentations by Ed Murrell, Saida Shaalan, Norma McOmber, and the West Infrastructure Team.

CHAIRMAN WOOD: I guess this preface while they are walking up, just to let the world no part of this country goes untended to, we're making our first visit to the West on November 2nd to do an infrastructure workshop with parties that are staying on after the Western Governors' Association meeting and I look forward to that.

Staff's going to do a preview of the big items out there and the discussion about what the Commission is putting out there as resource materials for all the participants at that meeting.

MR. MURRELL: Good afternoon. My name is Ed Murrell, and I'm one of a member of the team of people working on putting together the Seattle Conference. With me here are Saida Shaalan, who will talk briefly about the draft agenda.

Norma McOmber, who is going to describe some infrastructure materials that she has compiled and summarized, along with the help of some other staff.

And Bob Eason who is with the Energy Projects Office and has been helping us with the conference.

When we're done, we'll be happy to answer your questions and when that's concluded, then we'll leave and allow the next group to come up and do their presentation.

MS. SHAALAN: My name is Saida Shaalan, and Mr. Chairman, Commissioners, what I'm about to say is very brief and to the point. The agenda for the conference is -- the conference is on the adequacy of energy infrastructures in the Western states. It's to be held in seattle on November the 2nd, and essentially it's a fact finding mission. The agenda has been structured around three main questions, the first being, is the current energy infrastructure in the West adequate as things now stand.

The second question is, what are the infrastructure needs of the region. We're talking the Western states, purely.

And then the third question is an outgrowth of the first two. What factors are inhibiting adequate investment on energy infrastructure. As part of the fact-finding effort, there are a number of other questions that arise and that will probably feature prominently. One of them is, well, what is the outlook for population and the growth in energy demand in the West.

A second question is what are the near term infrastructure needs of the area in light of the growth in population and energy demand.

Another question is why isn't needed infrastructure being built, what is that not happening?

What are the barriers that we need to remove?

And the last question is, what can the states and the federal government do to encourage investment.

The intent, at the end of the day, is to come up with some constructive ideas of what needs to be done and who needs to do it to improve the outlook for energy infrastructure in the West.

And as the Chairman has said, get in there and solve the problems as a result of what we learn at this conference. And that is all I will say about the agenda.

Norma now will tell you what she has gleaned from her research and the studies that she has reviewed.

MS. McOMBER: Hi. My name is Norma McOmber. And what I did to help prepare the Commission for these upcoming infrastructure conferences is some research of what the thoughts are out there that have been put to paper on energy infrastructure. And I've put together a report that is part of the agenda now that is called "A Snapshot of the Nation and a Focus on the West." There are more than 50 items in there that come from regulators at the state level, that come from organizations that are coalitions of regulators, that are different individuals that have put down their thoughts. And so I want to acknowledge their work in presenting this material to you.

I also want to acknowledge Ed Murrell and Purvis Swaggert for helping summarize this material for you, and I

want to acknowledge that Jim Campbell helped find some of this material. Copies of these reports are available for you if you would like to take a look at them.

So with that, let me go ahead and tell you that the reasons for this research, as I said, and Saida has said, is to prepare for the infrastructure conferences. I also want to provide some excerpts and sketches to you that would basically help answer the questions that Saida said we need to answer.

And the last part that I would like to make sure that you're aware I'm trying to address with this presentation is to tell you the Western infrastructure story just very briefly. You're going to be getting a subsequent presentation from another group from the Markets and Tariffs Office that will tell you a whole lot more detail on the Western infrastructure story, but I wanted to kind of tell you, just in a snapshot, what some of the authors and some of the organizations that I tapped into told us were what's going on in the West.

(Slide.)

So with that, let me go ahead and share this slide with you. This is from the Western Governors' Association and it basically tells you what the fuels that are being used in the West are, and there's a matrix there on the right that explains what the components of the fuel

mix are. And what the Western governors are saying is basically that gas is the primary fuel that's being used in the West and it will be increasingly so.

(Slide.)

So with that, let me go to the next slide, and this is basically just as a courtesy to you to provide you in one place, albeit a crowded map, all the famous transmission constrained paths in the Western Interconnection System.

(Slide.)

The next slide is also from the Western Governors' Association and what this slide shows is that the size of the generation circles is representing some are installed capacity by generation type within each transmission constrained area in the Western grid. The key that you see on the left shows the type of fuel that is being used in each of these areas. The width of the blue line that you see connecting the circles shows the relative transfer capacity between the transmission constrained areas. And I just want to point out, as the chart says, that this is capacity as of January 2000.

(Slide.)

So with that let me go to the next slide, and this one shows, according to the Western governors, what they find the location of the loads in 1999, that's in blue,

and what they forecast to be the case in 2010, that's in red. And as you can see, the greatest current and forecasted peak loads are in Southern California, Northern California, Oregon, Washington, British Columbia, Arizona and Colorado.

(Slide.)

The next slide shows the export and import dynamic in 1999 in the West, and what the Western governors are showing with this is that the greatest importers in 1999 are the states that have the areas with the largest red circles were Southern California and Colorado. The largest exporter for the region is by far the production that is coming out of the Columbia River Dam Systems.

(Slide.)

So with that, let me focus just very briefly on the California story. As one particular author compiled these graphics, I want to acknowledge James Sweeney and his work in this area.

(Slide.)

The next slide basically shows the electricity imports that have been going into California, the quantities that have been going in, and what regions they're coming from, whether it's the Pacific Northwest, which is shown in this slide in blue, or the Pacific Southwest, which is shown in green.

(Slide.)

The next slide shows one of the reasons why California got into some trouble. Basically this shows that there were hardly any applications in California to site new generation between 1980 and 1998, and this graph also does go a little further and show what the status is of the applications and the projects that are currently on the books.

(Slide.)

The next slide illustrates very graphically another reason why the California experience went the way that it did, and this basically shows the average daily capacity that went off-line in California beginning at the end of last year.

(Slide.)

The next slide shows what the Californians basically did in response to these supply crunches, and it basically plots the reductions in their use in 2001 relative to what they were using in 2000.

(Slide.)

And the last slide that I wanted to share with you, before I go into the highlight very brief summaries of the research in general is showing basically the power plants that are scheduled to come on line, the capacity that they are going to be providing, and that will help alleviate

the supply problem.

So as I said, this report that I've prepared for you for your use, and it's on the Internet for others to look at if they so choose, is a snapshot of what is going on on a national basis as far as energy infrastructure is concerned. And I grouped the materials that I found by fuel area, electric, gas, oil, what we traditionally think of, and also price responsive demand because that was a very significant component.

Out of all the research, the greatest amount of information was on electricity energy infrastructure. So with that, let me tell you what the research showed were the greatest findings, the most consensus around, the highlights of that research.

The first highlight is that the Federal Trade Commission has found that additional benefits are indeed going to accrue to the electric consumers, both at the residential and at the wholesale level once the transition is complete. I think that was a very significant finding in that report.

The second finding from the research is that research approaches are critical for an effective transition and for the subsequent operations. So, again, this is being said to us from the outside by people that are thinking about these issues outside of this agency.

The third finding is that price-responsive demand is indeed very important and needs to be more widespread.

With regard to price responsive demand, I just wanted to point out that there are about a dozen utilities in 17 states across the country that are offering pilot programs that have time-of-day pricing for electricity.

And in the West where the conference is going to be held next week, Puget Sound Energy in fact has gotten an award for the innovation that they have exercised as a utility in providing their customers with this real time metering.

The snapshot also includes information for the Commission to use on utilities that have price-responsive demand programs that are in other parts of the country, the ones in the Midwest, the Northeast and the South.

I thought it was also important to bring up to you that one cite that I found said if instituted nationally, the time-of-day programs could save $10 to $15 billion a year and postpone the construction of 200

additional power plants. I thought that was a pretty significant cite. I'll be happy to follow through in more detail on that.

(Slide.)

MS. McOMBER: The next slide that I wanted to share with you had to do with the findings in gas, and I don't think it's any surprise for anybody here to hear that more cooperation and reviews would facilitate the construction of more pipeline. And one highlight that would be useful to the proceedings that are going to be happening in Washington State next week is that there is an organization in that state government called the Office of Trade and Economic Development that has a report citing concern about the adequacy of gas and whether it's going to be available to fuel the electricity demand in Washington State and in the region.

(Slide.)

MS. McOMBER: The next slide, I just want to tell you about what I found in hydro. And the report that I looked at basically said that centralized decisionmaking would help the process along.

CHAIRMAN WOOD: Was that authored by somebody in this building?

(Laughter.)

MS. McOMBER: Look at the report to find out.

(Slide.)

MS. McOMBER: The last, well, the next-to-the-last slide, excuse me, on oil pipelines similarly chimed in that the Association of Oil Pipelines notes that oil pipeline infrastructure would expand if there were more coordinated reviews and also if there was government guidance and leadership in land use practice with regard to encroachments on pipeline right-of-ways.

(Slide.)

MS. McOMBER: The last slide that I wanted to call to your attention dealt with what I found on oil and gas and also coal and rail, because coal is such an important component to electricity generation. Basically, the oil and gas recovery efforts are really enhanced by specific state and federal incentives that are designed to increase oil and gas supply in the country. And the coal and rail relationship seems to be a very healthy economic one with the deregulation of the rail industry with the Staggers Act in the last few years. That's been quite successful.

So that concludes my presentation. I hope you find the report useful.

CHAIRMAN WOOD: We already have. Thank you very much, Norma.

MS. McOMBER: You're very welcome.

CHAIRMAN WOOD: Good job.

Ms. McOMBER: Thank you.

CHAIRMAN WOOD: Who's next?

MR. MURRELL: That concludes our presentation. We're ready for any comments or questions.

CHAIRMAN WOOD: Comments or questions?

(No response.)

CHAIRMAN WOOD: Great. Thank you both. Thank you all.

COMMISSIONER MASSEY: Let me just say, I think these charts and the way you've laid this out, they're really useful. Because you can look at the chart and understand it instantly. Thank you.

CHAIRMAN WOOD: All right.

(Pause.)

MR. JOHNSON: Mr. Chairman, Commissioners, ladies and gentlemen. My name is Bradley Johnson and I've been chosen to lead off this presentation on the Western infrastructure assessment. But I'd first like to introduce my team members. Fellow presenters James Caruso, David Lengenfelder, and Cynthia Pointer has stepped out for a minute but she'll be right back.

Out in the audience we have Meesha Bond, Ken Kohut, Brian Harrington, Camilla Ng, Brian Craig, David Bailey, Lyle Hanagami and Thanh Luong. Team members not

present, Scott Miller and Bob Czarick.

A brief background about this presentation. In August our team started to collect and analyze data on the Western infrastructure, specifically for background information for the Western Infrastructure Conference. This presentation is a summary of a larger, more complete package of data that will be available this Friday.

This larger data package will be used for background information at the Western Infrastructure Conference, but can also be used as background information for policy formulation. This presentation is slightly different than the one that was distributed this last Friday but still consists of the original four parts: Demand, supply, markets and transmission.

First slide, please.

(Slide.)

MR. JOHNSON: On this first slide, what we see is each state's portion and a percentage of the total population consumption within the WSCC. As an example, for the state of Oregon, the blue number, or 5.6 percent, represents that 5.6 percent of the total population within the WSCC resides in the state of Oregon. Same with the red number which is your electric consumption. Eight point six percent is consumed in Oregon, and the same with gas.

One point that I would like to make with this

graph is that when electric or gas consumption appear low, the other commodity offsets and balances out the state's total consumption figure. An example of that is in California where you have 55 percent of the population. Forty percent of electric consumption appears to be a little bit on the low side but is offset by the high gas consumption of 58 percent. Inversely, Arizona is just the opposite, where you have about 8.4 percent population within the WSCC but a higher consumption rate relative to the population, and they have a lower gas consumption rate.

(Slide.)

MR. JOHNSON: This next slide shows population and consumption changes between the years 1990 to the year 2000 and also the electricity per capita use per kilowatt hour per capita. One thing I'd like to note here is within the WSCC, total consumption between 1990 and the year 2000 for electricity approximately grew 22 percent. The population grew approximately 20 percent, and gas consumption grew 40 percent.

One thing that becomes obvious when you start looking at this graph is that the Southwest starts to show a larger increase of electric consumption and with gas consumption. The reasons for this larger increase in consumption is because of the explosive population growth which has stimulated economic growth.

(Slide.)

MR. JOHNSON: This next slide shows gas consumption within the WSCC by sector from the year 1990 to the year 2000. It's broken down into four elements: Residential, industrial, commercial and electric utilities. While gas overall increased 40 percent, 15 percent was residential -- or residential grew approximately 15 percent, commercial 4 percent, and industrial grew a whopping 119 percent. But we must take note of that 119 percent. Most of that is due to the sale of the electric generation plants within the state of California.

Upon the sale and the repurchase of those plants by new companies, data changed. And instead of them being put into the electric utility sector, got switched over into the industrial sector. So that's why you start seeing with the maroon line in 1998, '99 and 2000 industrial sector starting to take off.

(Slide.)

MR. JOHNSON: The next slide shows the total capacity and peak load within the WSCC. Total capacity or your top line increases from 132,000 megawatts to 136,000 megawatts, or about 3 percent over that 10-year period between 1990 and the year 2000.

Peak load increases between 1990 and 2000 about 18 percent. Hydro capacity, at the bottom of this graph,

remains relatively flat.

Towards the right side of this graph, you'll see your projections. It is projected that by the year 2005 with the capacity that is supposed to be put on line, it will grow to 188,000 megawatts within the WSCC area. That 52,000-watt increase between the year 2000 and 2005 represents a 39 percent increase in total capacity.

With demand, we have gone ahead and fanned out a future forecast with a high/low.

What the low line represents with your future forecast for demand, or the dark blue line, represents a 10 percent bound, meaning that there is a 10 percent probability that demand will fall below that line.

Conversely, with the orange line, that is your 90 percent bound for demand, meaning that there's a 10 percent probability that demand will be above that line.

So what we're basically saying is that we are 80 percent sure that demand will land somewhere between the dark blue and the orange line as we start projecting demand out in the future years.

The light blue line that you see in the middle of that projection is the NERC estimation.

Projected hydro, which is on your bottom line, continues to remain flat.

CHAIRMAN WOOD: Let me ask a question. Does that

NERC projection peak load take into effect the intermittency of the hydro, or do we have to kind of do that as part of the brackets there?

MR. JOHNSON: Okay. With the information that is given by NERC, they do take that into consideration. That is part of their methodology.

CHAIRMAN WOOD: Okay. So the 114 for the year 2000 reflects an estimate of what will actually be available? I'm sorry, the 136. The 136 reflects an estimation of what would actually be available as capacity, or is that just nameplate added up?

MR. JOHNSON: Okay. That 136,000 for the year 2000 total capacity is total capacity. That's what it was for that year.

CHAIRMAN WOOD: That assumes --

MR. JOHNSON: That's your peak summer capacity.

CHAIRMAN WOOD: That assumes one hydro megawatt is one hydro megawatt, not factored for the fact that it didn't rain?

MR. JOHNSON: That's correct.

COMMISSIONER MASSEY: While we're on this chart, your 188,000 megawatts projected, are those just planned units? Are they sited units? How did you measure whether this unit is likely to be available and generating capacity by the year 2005?

MR. JOHNSON: Okay. This information came directly from the NERC database. So it was NERC information that was transmitted or given to us by EIA. They are saying that the NERC estimation is that it will be growing to 188 percent through their methodology, through what they're planning out in the WSCC.

COMMISSIONER MASSEY: I see. So it used the nERC planning methodology to come up with this number?

MR. JOHNSON: Yes.

CHAIRMAN WOOD: And this is the salient chart that we've got to figure out the right way to get the best data here, because projecting load and projecting what's really going to be there is something actually at my last job I got pretty good at, but just kind of depending on utilities or depending on kind of external people sometimes is not necessarily the soundest deal, because you don't know how soft that number is in '05 and you don't -- I mean, I couldn't have depended on 136 gigawatts last summer out there because of that hydro took a walk.

That's the problem with the current state of the data, and that's really what necessitated us going out there and getting smart at this. So I would want to think about what use we make of this chart next week. You all can kick that around.

MR. JOHNSON: Okay.

CHAIRMAN WOOD: All right. Sorry to interrupt.

(Slide.)

MR. JOHNSON: Okay. The next chart is basically the last chart with the reserve margin superimposed on top of it. Reserve margin in 1990 started at 26 percent but in '91 grew to 29 percent but gradually tapered off to 14 percent by the year 1998. And in the year 1999 and in the year 2000 hovered around 16 percent.

Using the total projected capacity increases from the last slide with the NERC demand, it shows that as time goes forward, reserve margin will hit approximately 23 percent by the year 2003 and 31 percent by the year 2005.

That sums up the demand portion of this presentation. Next will be supply and Jim Caruso.

CHAIRMAN WOOD: Can I ask a question?

MR. JOHNSON: Sure.

CHAIRMAN WOOD: Do you know if reserve margin is going up to 31 percent, that sounds pretty high if you're in a market-based system. Of course, the states don't have markets at retail. But is there any state policy out West that would drive a reserve margin of 31 percent?

MR. JOHNSON: Not that we know of. Not that I know of anyway.

CHAIRMAN WOOD: Again, I think this ties back to my concerns about the prior data being something that at

least a decisionmaker or investor would rely upon. And I think a real thorough analysis of what the demand is probably you could get rough consensus on that. But as to whether the capacity is going to be there and how much percentage of it being there on a day-to-day basis do you factor in. And you might take a hydro megawatt, multiply it by .7 for planning purposes to get a real, I don't know how you'd -- I'm sure somebody smart has thought about it. But that's kind of been my concern, particularly out there where there's such a dominance of an intermittent resource that we've got to factor. But the 31 surprised me too, Bill, for the same reason.

MR. JOHNSON: Another comment about the capacity figure. As time goes out -- total capacity figure in the projections -- what we're finding is that as time goes out, like two years, three years out, these projections have a tendency to get higher and higher. It becomes very difficult. So like a projection for future capacity is only good for about two years, maybe three years. When you start projecting out to 2005, it's just too much time out is kind of what we're seeing as far as the data goes. It becomes real screwy. It starts messing around.

COMMISSIONER MASSEY: Sure. Well, then are you saying that as a group you are not -- you doubt that the reserve margin for the Western interconnection will be 31

percent in the year 2005?

MR. CRAIG: Yes.

MR. JOHNSON: That would be high, yes.

MR. CRAIG: And even with the capacity numbers going all the way out, we felt very uncomfortable with them.

CHAIRMAN WOOD: I would put, then, for the use of next week, I would put in here what you guys, because you're the smart guys that we're going to rely on to make good decisions, and we're going to either sound the alarm bell or not sound the alarm bell based on that. But I know that 31 number is not right. And if you guys want to say there's a 40 percent likelihood that any plant that's permitted today won't be built, then discount that future gigawatts by the according amount. I mean, I think that's the kind of projection that's going to be real helpful for the governors out there and the other folks who have to live with this infrastructure or lack of it.

But you all's best guess about how many of these plants that get announced in the press release actually get turned on and energized on the grid, I've never seen that number be higher than 50 percent in my short experience. So it may be even lower out there.

COMMISSIONER BROWNELL: I think you also just might want to footnote your caution that the further out you go, the less reliable it is for the following reasons so

that people don't take away this -- we understand it now, but others will not.

MR. CARUSO: My topic is supply. And I'm going to start with the electric supply.

(Slide.)

MR. CARUSO: A lot of information on this chart. This chart depicts both total Western capacity and total Western generation output based on year 2000 data. Beginning with the top chart, which is demonstrated capacity, we have approximately 139,000 megawatts for year 2000.

This chart is further broken down by state. You see starting with the columns at the left, we begin with California, Washington, Arizona, Oregon and so forth. And it's further broken down each state by fuel type. So we see the light blue is our hydro capacity, the dark blue our natural gas, the pink color coal, and the orange nuclear.

Dropping down to the bottom graph, we see total net generation for the year 2000 at 650 terawatts. Another way of saying this would be 650 million megawatts.

(Slide.)

MR. CARUSO: Notice that -- I'm going to switch a little back and forth -- the top chart, two states, California and Washington, own more than 50 percent of the total Western capacity. And on the bottom chart you can see

that three states -- California, Washington and Arizona -- produced more than 50 percent of the total generation for the Western states. Another thing you might notice on these charts is that coal, which is the pink, and nuclear, which is the orange, have a greater share of total generation than they do their share of capacity, which is understandable in the fact that these are generally base load units that are run continuously, whereas the hydro is run according to water levels, which were below normal in the year 2000. And of course your natural gas is run when it's more -- your gas-fired units are run when it's more economical to do so or when it's necessary to do so.

Next chart.

(Slide.)

MR. CARUSO: Here's a couple of points that were not on that chart. It's interesting that 20 entities, most of these are holding companies, some of them large federal projects like Bonneville, own 73 percent of the total Western capacity, and 20 entities, almost the same 20 entities, produced 71 percent of the generation.

Another interesting fact I put on this page is that from 1996 through 2000, gas-fired generation increased a whopping 221 percent, as we saw in Norma's charts earlier. And during this time, hydro decreased some 17 percent, and other types of generation combined increased only about 20

percent. All this time, installed capacity changed very little.

Next slide.

(Slide.)

MR. CARUSO: Now this slide first off, you can see this is 1996 through 2000, you can see the dark blue being the natural gas generation, has increased quite a bit over that five-year period. But this chart is also very good to illustrate the interrelationship of hydro to natural gas and coal. So that you can see over the years as the hydro has decreased because of below normal or decreasing precipitation -- the last two years it was below normal -- that the natural gas increased to pick up the slack.

You can see there's hardly any change in the coal. Actually, there's a 19 percent increase over that five-year period, but nothing to compare with what natural gas is doing.

Next slide.

(Slide.)

MR. CARUSO: Now here's a subject we talked about earlier. This shows our current capacity at August of this year, and our projected capacity. There's about a 21 percent increase because we're projecting out to 2003. Brad's chart projected out to 2005.

Our current capacity is 141,000 megawatts. My

first chart showed 138, but we've included what's come on line, two or three thousand megawatts this past year -- this current year.

Our new capacity, 32,000 megawatts, is coming mostly from three states: California, Arizona and Washington. But that's not really surprising because you can see from the bars that they own the major part of the existing capacity.

Of that 32,000 that we're projecting, 24,000 megawatts is actually either under construction now or is in the advance development stage. The 8,000 remaining is in the early development stage, but I'd like to point out that this is only 50 percent of what was reported by the company. So we built in this degree of conservatism. I'm thinking with the recent economic downturn that we might need to go a little more conservative than this. We don't know for sure.

Next slide.

(Slide.)

MR. CARUSO: Well, we're going to move from electric supply into gas supply, and we have a few slides in that area. The first slide here is a map of the Western states. Those looking on the monitors probably can't make out much, but if you have a paper copy, you can see the tan areas, the broad tan areas are the gas supply basins, and the receipt and delivery points are illustrated by the blue

and red dots, and the storage facilities by the green triangles. The pipelines, of course, are the network of red lines.

The pipelines, there are approximately 20 major pipelines that serve the West. We believe that there is enough interstate gas capacity, and this is based on approved filings, recent approved filings and filings that -- or projects that we have on file. I might add that we think that this will continue based on how responsive the market has been to capacity needs through a well-functioning open season process.

Next slide.

(Slide.)

MR. CARUSO: Here we see storage for the Western states. We have three lines here. The light blue line is last year. The red line is this year to date, and the dark blue line is a five-year average. You can see last year we started out well above the five-year average but then trailed off in the last five months below the five-year average.

However, this year we quickly soared above the five-year average and we're continuing to rise, and we've surpassed last year's high level in storage.

(Slide.)

MR. CARUSO: Now this last slide here in my

section. This again is another map. It shows the supply basins. We've expanded the map a little bit to show more Eastern states East of the WSCC states because they're all a part of these basins, don't know state boundaries, and also parts of the Canadian basins.

We've included all of the Western states except Alaska, of course.

There are some 434,000 trillion cubic feet of reserves in just these Western basins. And throughout the United States, considering all the reserves -- and these are just proven and potential reserves. This isn't any fudge factor for growth or what have you that's a little bit questionable maybe. But with all of these reserves, the U.S. Geological Survey has said that we have enough reserves in this country to develop and produce economically enough gas to serve for the next 50 years.

And that concludes my section. We're going to move to Part 3, Markets, with my colleague, David Lengenfelder.

COMMISSIONER MASSEY: Can I ask you a question? Did you say that the proven reserves give us enough gas production capacity for the next 50 years?

MR. CARUSO: Proven and potential reserves.

COMMISSIONER MASSEY: Proven and potential. Can you define "potential"?

MR. CARUSO: I had a definition. Potential are --

MR. CRAIG: I think when they talk about potential where they have done some type of starting research saying that they could go down there and find these reserves. They located them, but there's no wells attached.

COMMISSIONER MASSEY: I see. So there's strong reason to believe the gas is there?

MR. CARUSO: It's very strong.

MR. CRAIG: Right. More than a strong reason.

MR. CARUSO: David?

MR. LENGENFELDER: Thank you, Jim. My name is Dave Lengenfelder and I'll be presenting the markets section.

(Slide.)

MR. LENGENFELDER: In this section I'll identify the primary wholesale electric and gas trading hubs in the Western United States, capture a snapshot of the spot market trading volumes, plot the monthly wholesale electric and gas price indexes for the Western hubs. And then finally I'll illustrate a recent downward shift in the 12-month forward electric futures index.

Next slide, please.

(Slide.)

MR. LENGENFELDER: This map depicts the locations

of the major wholesale electric and natural gas trading hubs in the Western United States. Note the electric hubs are in black with the natural gas hubs in pink. These trading hubs will be referenced throughout my presentation, and you may hear me refer to them by their affiliated acronym names. For example, I may refer to the California-Oregon Border as COB.

Next slide, please.

(Slide.)

MR. LENGENFELDER: This bar graph provides us a snapshot of the monthly electric trading volumes in the Western spot markets compared with PJM West as reported by Megawatt Daily. The red represents the total trading volume during March of 2001, and the blue represents the total trading volume during August of 2001 for each respective market.

Note the trading volume in PJM West is three to four times greater than that found in the Western hubs. Consequently Western spot markets are more susceptible to price volatility as a result of this limited liquidity.

Next slide, please.

(Slide.)

MR. LENGENFELDER: In my next two slides, I will show the average monthly electric and gas spot prices in the Western market beginning in January of 1998 through July

2001 as reported by power DAT and gas DAT. Here the electric spot markets show that prior to the summer of 2000, the Western hubs exhibited relatively stable electric prices with electricity trading at or below $50 per megawatt hour.

Beginning in the summer of 2000, we see electric prices start to break out of their historical trading patterns, and during the summer of 2000 average monthly electric prices rose significantly to $100 to $150 per megawatt hour range.

During the winter of 2000 and 2001, the Western electric prices reached unprecedented levels. We saw electricity trading in a $200 to $400 per megawatt hour price range, and during this period, we witnessed significant price variations between the various trading hubs in the Western market.

During the summer of 2001, prices began to return to normal, trending towards the $50 per megawatt hour range at all Western hubs.

Next slide, please.

(Slide.)

This graph shows the monthly gas index of the various trading hubs for the same time period as the previous slide. Here we see that the price volatility in the gas market echoed the price volatility in the previous slide as the electric markets.

Prior to the summer of 2000, gas was trading at or below three dollars per mmBtu and price uniformity existed between the various trading hubs in the western market.

During the summer of 2000, gas prices began to rise to the five dollar per mmBtu range, and then once again in the winter of 2000-2001, gas prices skyrocketed peaking out in January of 2001 at or above fifteen dollars per mmBtu. During this period, we once again witnessed significant price variations between the trading hubs.

Fortunately, once again during the summer of 2001, prices began to return to normal levels and by July of 2001, gas was trading at or below five dollars per mmBtu.

(Slide.)

The next two slides capture a snapshot of the 12-

month forward price curve, comparing COB with PJM. Here the 12-month futures index in March of 2001 at the COB reflected the volatility of the Western spot markets in the Spring of 2001. The COB 12-month futures index tracked seasonal patterns but exhibited greater volatility versus PJM. The 12-month futures index for COB was at $450 per megawatt hour for delivery in August of 2001 to $150 for delivery in March of 2002. During the Spring of 2001, the futures market was predicting another summer like that of 2000.

(Slide.)

By August of 2001, the COB 12-month futures index subsided to reasonable levels. What's interesting between this chart and the last chart is the vertical access. On the previous chart it goes up to $500 and on this chart fortunately it only goes up to $70. So there was a significant downward shift in the price curves. The 12-month futures index at COB was reported at $58 for delivery in December of 2001 to $36 for delivery in April 2002.

The COB 12-month futures index currently exhibits less volatility and begins to converge with the PJM market in the latter months of 2002.

In conclusion, the decline in prices in the Western markets are most attributable to a combination of factors; mild weather throughout the summer of 2001; plentiful generation with additional capacity coming on

line; increased projected reserve margins as highlighted in the previous slides, reduced demand and active conservation programs were starting to take hold in the Western markets.

Lower natural gas prices started to emerge, and lastly FERC composed electric wholesale price mitigation throughout the entire WSCC region to effect in early June of 2001.

I am happy to report that currently wholesale electric and natural gas prices in this region are exhibiting uniformity. Electricity is trading in the $25 per megawatt hour range and natural gas is trading in the $2.30 per mmBtu range.

Thank you, and this concludes my portion of the presentation. I will now turn it over to Cynthia Pointer --

COMMISSIONER BREATHITT: Can you repeat the two prices that you just mentioned that electric is trading at what?

MR. LEGENFELDER: In the $25 per megawatt hour range.

COMMISSIONER BREATHITT: All over?

MR. LEGENFELDER: In the Western --

COMMISSIONER BREATHITT: All over in the West.

And the gas is what?

MR. LEGENFELDER: In about the $2.30 per mmBtu range.

COMMISSIONER BREATHITT: Those are impressive numbers.

MR. LEGENFELDER: They are. Thank you.

MS. POINTER: My name is Cynthia Pointer, and I'll be giving a very general overview of transmission in WSCC and transmission projects of interest that have been identified by that area.

Can I have the first slide, please?

(Slide.)

The map illustrates 345 kV and higher lines of transmission in WSCC. The table provides a breakdown of the 1999 miles of transmission, their percentage of miles in WSCC and transmission assets for each of the WSCC NERC subregions.

The 1999 assets are representative of all the assets considered transmission within each of the NERC subregions which also includes transmission at the lower voltages, so not just the 345.

Although not shown on this map, the majority of transmission in both the California/Mexico, the pink area on the map that's shown only by California, and the Northwest Power area, the gold area, fall in the lower voltages of 115 kV, 161 and 231 kV voltage categories.

The Northwest power area in California/Mexico are also the two densest subregions in terms of miles of lines,

comprising over 70 percent of the total miles of transmission in WSCC.

Combined 1999 transmission assets for the Northwest power area and California/Mexico near 19 billion making up nearly 80 percent of the 24 billion for the WSCC area.

(Slide.)

The Western Interconnection Transmission System is closely planned between each of the transmission owners, WSCC and NERC. A biannual transmission plan issued July 7th, 2000 by the Northwest, Southwest and Regional Transmission Associations in cooperation WSCC identified the ten projects as shown on the map of significant interconnection interest. Note that seven of the ten projects are in the California/Mexico and Northwest Power areas.

Sponsors of projects of significant regional or subregional impact had to demonstrate that their projects met ten planning guidelines according to their coordinated planning process, two of which include transmission constraint mitigation and operational constraints created or removed by the project.

A third planning guideline weighs economic considerations concerning the evaluation of cost and benefits of the project and the reasonable alternatives.

(Slide.)

This table details the names of the projects from the previous slide and their completion dates. The project numbers correspond to the number on the map. The projects include installation of new facilities and/or lines of grades, reconstructing and bundling of lines. As you can see from the table, the majority of the projects are expected to be in service by 2004.

This concludes our presentation of the Western Infrastructure Assessment. Keep in mind that today's presentation represents only the highlights of a larger package, which will be made available on Friday, close of business October 26th.

Work on a similar infrastructure assessment of the east is in progress. We will have a more extensive presentation on transmission constraints when we present our electric transmission constraints study on I believe November 21st.

Thank you for your time, and we are available to answer any additional questions you may have.

CHAIRMAN WOOD: Ya'll, these were great presentations and really to lay a great factual predicate for I think a lot of work that we're going to be doing over the next couple of years out with people all across the country, and what's good for the West is good for the rest

of the country too, so we'll probably be seeing you folks again, or at least your colleagues, as we start to hit the different regions. But thank you for setting a real high bar for good quality work.

COMMISSIONER MASSEY: Can I ask one question, please? We often hear and there are I think statistics to back this up, that transmission investment for the nation as a whole has not kept pace with the expanding needs.

Now there are those who believe that very strongly. There are those who would debate that. But in any event, how would you assess the validity of that statement for the Western interconnection?

MS. POINTER: The project that they identified as being of significant interest took into consideration say ten planning guidelines, only two of which include transmission constraints and operational constraints.

So that relates to keeping up with the growing need for transmission.

With regards to say how that applies to the West and how well they have kept up with it, I think generally most transmission providers plan with not just those two things in mind.

For instance, some of the other criteria they used included if those projects could be done in parallel with other things. If the projects were broad in scope, which mean that they included other concerns that were of interest to adjacent areas.

So there are a lot of things that go into building transmission to make these projects reality, not just the need.

COMMISSIONER MASSEY: Yes. I guess I was thinking about the chart that showed the potential increase in generation going from 135,000 megawatts up to 188,000

megawatts, and there is some doubt among you that that will actually happen, but suppose it went from 135,000 to 160,000 megawatts, or 150,000 megawatts? Would the transmission be available to deliver that power at a reasonable price?

MS. POINTER: I would probably refrain from answering that question because I'm not certain.

COMMISSIONER MASSEY: Well here is someone chomping at the bit.

(Laughter.)

MR. LUONG: Hi. My name is Thanh Luong and I am a Team Leader of the Transmission. As you say that the transmission expansion, you know, for the last five or ten years is, no doubt about it, lacking compared to generation expansion. And you see a lot of projects going on, if you look at the data in the Midwest.

Like recently like Wisconsin PUC just approved something, and PUC in Minnesota already approved. I mean it takes a longer time to build a line, and the same thing with the Kanawha Met area in West Virginia. You know, the 765 kv line, you know, to build into the West Virginia area takes a longer time to build.

So even though we look at a table, that provides only ten projects, and you see that the days, you know, go further to 2004, 2005, I think the transmission is much harder than the generation. That's my point of view, and

based on the data that I see.

I know that somebody will disagree with that, but that's what I say.

MR. ROBINSON: Commissioner Massey, I think one of the things that you will hear, or we will hear when we are in Seattle next week, is that, as one example, there is about a $2 billion deficit in the BPA system of things that they know they want to do to upgrade that system, and that is just in that high kv infrastructure the BPA has under their control.

CHAIRMAN WOOD: Thank you all, again.

SECRETARY BOERGERS: The next items for discussion, there are several items being called together with E-25, which Commissioner Breathitt has asked for, and they include E-7, E-10, E-12, E-16, E-17, and E-25, and Jonathan First has a presentation on E-25.

MR. FIRST: Chairman, Commissioners, in E-25 the Commission would grant rehearing and require American Electric Power, the transmission provider, to pay interest on transmission credits for system upgrades to DPL, the generation interconnection customer.

The Commission has previously disallowed interest, finding that the transmission provider could not make use of the money because there is no significant time lag between payments made by a generator to a transmission

provider and the obligations of the transmission provider to reimburse equipment suppliers and firms that provide construction services.

On rehearing, the Commission finds that whether or not the transmission provider holds generation payments for any length of time should not be the determining factor as to whether interest should be paid.

Rather, the Order finds that failure to adjust credits to reflect interest would impose financing costs on generators which may unduly impede capacity additions, and that making the new generator bear the financing costs while all ratepayers bear the underlying construction costs for system upgrades on a rolled-in basis is inconsistent.

The Order emphasizes that today's ruling is an interim decision, and that the issue of interest payments on transmission credits will be revisited in the context of a generic proceeding on generation interconnection issues.

In addition, the same interim decision is applied in each of the Orders for the other items called in this group: E-7, E-10, E-12, E-16, and E-17.

Thank you.

COMMISSIONER BREATHITT: Thank you for that presentation.

I called--I'm not sure if I called these items or if you did, Chairman Wood, but I did ask for the

presentation. So thank you very much.

I wanted to talk about these because I am going to be dissenting on this DPL AEP case, and dissenting in part on the others that you called.

How do you want to proceed? Do we want to discuss them now?

CHAIRMAN WOOD: Yes.

COMMISSIONER BREATHITT: Okay. My reasoning for my dissent is as follows in the AEP DPL case:

On July the 26th of this year, the Commission issued an Order which denied a request by DPL Energy, Inc., that system upgrade payments should accrue interest.

In this Order, the Commission reverses its earlier policy on interest and grants rehearing on this issue.

As I just mentioned, I am dissenting on this policy change for several reasons:

First, I am not convinced that this Order adequately counters the reasons set forth in the July 26th Order for rejecting DPL's position on this issue.

And second, the Commission is poised to take up issues related to interconnection procedures shortly in an Advanced Notice of Proposed Rulemaking, which is the appropriate forum for resolution of this issue.

The July 26th Order denied DPL's request because

it failed to address the rationale set forth in an earlier Order in this issue, which was that the proponent for interest payments had not shown that the payments made by the generators are held by the transmission providers for any significant length of time.

In fact, the July 26th Order observes that DPL made its first monthly payment installment in October of 2000 and construction began in December of 2000.

Thus, the July 26th Order concluded that AEP had begun using the money soon rather than simply holding it. That Order, the July 26th one, also explained that the main factors involved in the request for an upgrade, which are the financed amount and the timing, are in the hands of the entity requesting interconnection which chooses the interconnection location and decides whether the generating facility will be used for either baseload or peaking purposes.

On rehearing, DPL argues that AEP will be receiving a windfall in the financing costs, but adds no specific data to support that assertion, even though--as I had previously said--the time frame was October to December. So I don't know if I would characterize that as a "windfall."

DPL asserts that the market dictates where a particular facility is needed. Further DPL maintains that

the primary factor dividing the cost of the system upgrades is neither the location nor the type of generating facility, but that it is the current condition of the utility's transmission system.

I would respectfully disagree with DPL that the location of the generating facility is not a primary factor driving the cost of system upgrades. And I am further not convinced that DPL has proffered compelling arguments that counter the rationale that the Commission has already used in its July 26th Order to reject its proposal on the interest issue.

Furthermore, as was discussed at our October 11th, 2001, meeting, the Commission has agreed to issue a proposed rulemaking on the standardization of generator interconnection agreements and procedures.

The full Commission was in agreement that this issue was ripe for quick action. There are clearly valid arguments to be made on both sides of the interest argument. In fact, the Commission Orders on this agenda where the issue is present state that this is an interim policy decision on interest accrual and that we will reconsider this issue in the Interconnection Rulemaking based on all relevant facts and circumstances.

I believe the more appropriate course of action would be to decide this matter in our rulemaking rather than

making this call now, albeit on an interim basis. I thought that is what we had decided to do.

There are cost issues involved and these will most likely get passed on to end-use customers. So I would prefer to do this in the context of our rulemaking.

Thank you.

CHAIRMAN WOOD: I guess just to respond, I do support the Order Granting Rehearing. I think, as I wrote separately at the time in July, that the Commission's decision at that point was incorrect and should be remedied and the Grant of Rehearing is the opportunity to do that.

I would have preferred to have done it now, but I think we did commit to doing it--or do it now on a permanent basis, but I think we did commit that it should be subject to notice and comment as to this particular issue, but the whole broad issues about how money gets divvied up.

But the core point that I have felt strongly about is that transmission owners should both construct and take the responsibility for getting transmission built. And that includes the financing of that as well. And generators should focus on what they do well, which is build generation plants, and not serve as a bank.

And I think it is so critical, as we have seen not just in the West but across the country, that we formulate policies that encourage investment in new

generation, which in turn makes markets more competitive.

And I am pleased that the Order in its second paragraph

points that out.

So I support the grant of rehearing and have an open mind about how this ought to be dealt with. I think quite frankly, some of the issues that we heard on the transmission planning panel last week might be dealt with in a different way than through kind of an obtuse financing angle.

But if people are locating in bad locations and forcing excess costs onto the system, then maybe that's a role that we want the transmission planning aspect of the RTO to say either no to or the local state commissioners if they don't want to approve a transmission line or a power plant location that doesn't benefit the system, they could say no to that. But I don't want the Commission by setting up policies here that put roadblocks in the way for new generation investment by requiring them to shoulder costs that should be borne by another market participant to be the excuse for that.

So that's my support for the order as it's written, or as it's proposed here.

COMMISSIONER MASSEY: My support is based fundamentally on two points. Number one, the policy now does require, that we've applied, does have an element of socialization in it. If the generator is going to be used as a bank as it is now under our current policy, my view now is that it should be paid interest. And so I'm willing to

vote for the order.

But point two is -- I wanted the explicit language in the order that said this is just on an interim basis. Because, frankly, I haven't made my mind up on this long term, this issue of socializing interconnection costs versus pricing the interconnection cost incrementally. And I was educated last week when a number of state commissioners raised this question. There are parts of the country where a lot of generation is being built for export, and the state commissions in those regions are concerned that the local consumers, their ratepayers, will have to pay the cost of those upgrades and they won't -- they may benefit a little bit, but they generally won't benefit a lot from all that generation being built for export to other regions.

Now I'm sure there are counterarguments to that. And all I'm saying is I have an open mind about what the policy ought to be long term. And I respect Commissioner Breathitt's point of view that we're kind of belly flopping on this right now on an interim basis.

But as long as our policy is what it is right now, even if it's just an interim policy, I am persuaded as a matter of logic that interest ought to be paid. But I want to underscore that my long-term view has not been formulated, and I have an open mind about how to price these

generation interconnection costs.

MR. LARCAMP: Mr. Chairman, I hate to do this, but in looking at the language, I just want to make doubly sure I understand that we've got this right.

CHAIRMAN WOOD: On the E-25?

MR. LARCAMP: On E-25. As I understand what the Commission is trying to accomplish here, it is that once the generator pays for the upgrade until the credits have been expended that they will receive interest on that amount which will be amortized over time through the credits?

CHAIRMAN WOOD: Right.

MR. LARCAMP: Is that correct? Then I would suggest that maybe there is some language that needs to be revised briefly about talking about payment of the interest.

CHAIRMAN WOOD: We'll pass the order until the next meeting.

MR. LARCAMP: Well, I think we could do this notational very quickly.

CHAIRMAN WOOD: Well, I've kind of got a policy against trying to do substantive things on notational. If you all want to do that notationally, I'd be happy to do that. But -- or wait til next time.

COMMISSIONER BREATHITT: I would rather wait til next time.

MR. LARCAMP: Okay.

COMMISSIONER BREATHITT: Are you finding something in the order we have before us that needs to be changed?

MR. LARCAMP: I just find an ambiguity in there that I'd like to make sure I'm clear about. If the Commission is clear, that's fine.

CHAIRMAN WOOD: Well, if you're not clear, the parties won't be either. We'll pass that item til the next. All four of them? Is it the same ambiguity in all four?

MR. BARDEE: Some of these items are statutory items that need to go before the next meeting. If we hold AEP until the next meeting, one option would be to treat the ones that are on deadline before then the way the cases have been treated until now, which would be to deny interest. The other option would be to do AEP notationally when the first case has to go out of here in the interim.

CHAIRMAN WOOD: What's your preference?

COMMISSIONER MASSEY: Well, we're discussing it here today, and so it seems to me everybody's going to know what the rationale for the vote is. I'd just as soon go ahead and vote as quickly as we can so that we don't get in a problem with these 60-day items.

COMMISSIONER BROWNELL: I agree with Bill.

CHAIRMAN WOOD: That's fine.

COMMISSIONER BREATHITT: Mr. Chairman, I

basically read my dissent and I needed to add another paragraph, so I just wanted to share that with you. I go on to say that I fully understand that policy decisions can be made in individual proceedings, and I have voted to do that many times in the past. However, the decision on interest payments here affects other proceedings on this agenda as we just pointed out.

The policy change will now be incorporated into orders in which the issue was not even raised, as well as in cases that are set for hearing. In addition, there are technical issues that must be resolved as a result of this policy change, and those are when interest should begin accruing and when payment of the interest should begin. And these orders were totally silent on that. And I think that creates some confusion.

The implications of this policy change, again, I will reiterate, I think should be decided in a rulemaking where the ramifications can be more fully explored, but I respectfully dissent and I'm glad that this is on an interim basis in case issues do arise that we don't know about now.

MS. MARLETTE: Commissioner, I'd also point out, these will all be subject to rehearing, even the AEP, which is rehearing will now be subject to further rehearing because we flipped on the issue. So all the parties will have an opportunity.

CHAIRMAN WOOD: All right. Then we will take all those items up notatoinally and vote as we indicated we'll vote. Thank you.

SECRETARY BOERGERS: We'll get those around as soon as we get some revised language.

CHAIRMAN WOOD: Sounds good.

SECRETARY BOERGERS: THe last items for today are Item C-6 and 8 which I understand Commissioner Breathitt would like to speak to.

COMMISSIONER BREATHITT: I did not call for a presentation on this. I wanted to have these two cases called separately because this is a continuation of issues that I raised in two previous cases.

And so I will be concurring today on these Kern River Orders. And I have written separately concerning Kern River's recent expansions in order to highlight what I consider to be an important issue, and that is:

How FERC should respond to applications for interstate pipeline expansions when intervenors allege there is insufficient take-away capacity to ensure that additional gas supplies reach the markets where they are needed?

And I am not going to recite my every concern with how the Commission has addressed the parties' allegations of congestion at Wheeler Ridge and the potential effects of increasing interstate capacity at that point.

In fact, I am pleased that over the past six months the Commission has come to acknowledge that our actions in certificating the Kern River expansions could exacerbate the problems of delivering natural gas to end users in Southern California.

More importantly, the Commission has recognized that the potential degradation of shippers' firm rights resulting from the certification of additional interstate capacity is an appropriate factor in the public benefits'

analysis that we use to determine whether a project is in the public convenience and necessity.

I am relieved that certain events are occurring in California that will mitigate congestion at Wheeler Ridge. More take-away capacity is on the horizon, and the California PUC is considering certain regulatory relief that will facilitate the transportation of natural gas from Wheeler Ridge to Southern California markets.

Nonetheless, I remain uneasy about the strain of policies the Commission has advanced in favor of certification of interstate capacity, despite the inefficiency of take-away capacity, and particularly the confidence with which the Commission has rejected the legitimate concerns of shippers on Kern's system.

I am issuing a concurring opinion today to urge that we not lose sight of the panoply of issues we must consider in issuing natural gas pipeline certificates.

In these times, there is great emphasis on expanding and improving our Nation's energy infrastructures which we have heard not only today in excellent presentations but last week during RTO Week. I most certainly share the sense of urgency of ensure adequate and reliable energy supplies.

However, there is more to the Commission's mandate under the Natural Gas Act than simply getting more

pipe in the ground.

We must ensure that the pipeline facilities we certificate have the desired effect of bringing additional supplies to the areas where they are needed, and we must also ensure that we take into account the potential for unused facilities, stranded costs, and unwarranted disruption of property rights, and the environment.

The Commission has come a long way this year in understanding the physical constraints and regulatory impediments to natural gas transportation in California, but there is still much to be done.

We will revisit issues concerning the adequacy of take-away capacity in Kern River's pending certificate application, CPO1-422-000, and I will continue to advocate a thoughtful and coordinated approach to fostering badly needed interstate and intrastate expansion in California.

Thank you.

CHAIRMAN WOOD: Thank you, Linda.

Are we ready to vote?

COMMISSIONER BROWNELL: Aye.

COMMISSIONER MASSEY: Aye.

CHAIRMAN WOOD: Aye

COMMISSIONER BREATHITT: Aye.

CHAIRMAN WOOD: That is on C-6 and C-8.

COMMISSIONER BROWNELL: Yes.

COMMISSIONER MASSEY: Yes.

SECRETARY BOERGERS: That was a concurrence by Commissioner Breathitt?

COMMISSIONER BREATHITT: Yes.

CHAIRMAN WOOD: And as a final announcement, all the Staff Power Point presentations will be available on the web page following our meeting today.

Meeting adjourned.

(Whereupon, at 3:02 p.m., the Commission meeting was adjourned.)