1 BEFORE THE
2 FEDERAL ENERGY REGULATORY COMMISSION
3
4 -x
5 IN THE MATTER OF: :
6 CONSENT MARKETS, TARIFFS AND RATES - ELECTRIC :
7 CONSENT MARKETS, TARIFFS AND RATES - GAS :
8 CONSENT ENERGY PROJECTS - HYDRO :
9 CONSENT ENERGY PROJECTS - CERTIFICATES :
10 DISCUSSION ITEMS :
11 STRUCK ITEMS :
12 -x
13
14 898TH COMMISSION MEETING
15 OPEN MEETING
16
17 Commission Meeting Room
18 Federal Energy Regulatory
19 Commission
20 888 First Street, N.E.
21 Washington, D.C.
22
23 Thursday, November 17, 2005
24 10:05 a.m.
25

1 APPEARANCES:
2 COMMISSIONERS PRESENT:
3 CHAIRMAN JOSEPH T. KELLIHER
4 COMMISSIONER NORA MEAD BROWNELL
5 COMMISSIONER SUEDEEN G. KELLY
6 SECRETARY MAGALIE R. SALAS
7
8
9
10
11
12
13
14
15
16
17
18 ALSO PRESENT:
19 DAVID L. HOFFMAN, Reporter
20
21
22
23
24
25

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

2 (10:05 a.m.)

3 CHAIRMAN KELLIHER: Good morning. This open

4 meeting of the Federal Energy Regulatory Commission will

5 come to order to consider the matters which have been duly

6 posted in accordance with the Government in the Sunshine Act

7 for this time and place.

8 Please join us in the Pledge of Allegiance.

9 (Pledge of Allegiance recited.)

10 CHAIRMAN KELLIHER: As of today, this is the

11 first Commission meeting where we're offering free, live

12 webcasts of our open meetings and most D.C.-based technical

13 conferences. This service will be available, as I announced

14 at the last meeting, to the first 750 users.

15 I want to welcome all of you, any of you who are

16 watching this meeting via the webcast. We think this is a

17 great opportunity for citizens, Congress, state regulators,

18 and anyone else to observe our policymaking and

19 decisionmaking processes.

20 And if you'd like to watch energy regulation,

21 real-time, ferc.gov is the place to be. Now, where --

22 (Laughter.)

23 CHAIRMAN KELLIHER: It's possible, it's possible.

24 COMMISSIONER BROWNELL: Are we going to get a fan

25 club? Are we going to get this -- and make e-tainment or

1 whatever that thing is?

2 CHAIRMAN KELLIHER: We'll see. There might be

3 some junkies out there.

4 Now, we're going to archive these free webcasts

5 for three months for those of you who can't watch the

6 meetings live or want to watch the meetings again and again

7 and again.

8 (Laughter.)

9 CHAIRMAN KELLIHER: Now, the archived webcasts

10 will usually be available in 24 hours after the completion

11 of a meeting or earlier, and you can access our free

12 webcasts on our free website, ferc.gov. Tomorrow, for

13 example, we will be webcasting our technical conference on

14 reliability standards, which starts at 9:00 a.m.

15 I'd like to take the time to reintroduce a

16 familiar face who is sitting a different place at the table.

17 And that's Susan Court. Susan is the new Director of the

18 Office of Markets, Oversights, and Investigations, which is

19 the Commission office charged with assisting the

20 Commission's efforts to protect energy customers by

21 understanding energy markets and energy regulation,

22 identifying and fixing market problems, and enforcing

23 compliance with the Commission's rules and regulations.

24 I have to say that I am very pleased and honored

25 that Susan has agreed to take on this responsibility. The

1 depth and breadth of her experience, particularly in the
2 natural gas area, makes her particularly well suited for
3 this position as the Commission is facing record high
4 natural gas prices this Winter.
5 Now, Congress has given the Commission
6 significant new enforcement authority, and it will require
7 additional resources to discharge this responsibility.
8 Susan has a very strong track record of management
9 experience, and she's strengthened every office she has
10 worked for here at the Commission, and I have no doubt that
11 she will continue to do the same here.
12 I just want to express my complete confidence in
13 Susan. I'd also like to announce that, effective
14 immediately, Robert Solomon will be Acting Solicitor of the
15 Commission, replacing Dennis Lane. Bob, if you could stand
16 for a moment?
17 Dennis has returned to private practice, and Bob
18 has agreed to take on this post, and I'm delighted that Bob,
19 a 17-year Commission veteran, with prior experience in the
20 Solicitor's Office, and an assistant to two Commissioners,
21 and a Deputy Assistant Counsel, will assume this
22 responsibility. Thank you, Bob.
23 And now I think Commissioner Brownell has an
24 announcement.
25 COMMISSIONER BROWNELL: Thank you. I have been

1 remiss in not announcing the new team in my office. We have
2 Joyce Edmunds. Joyce, please stand.
3 Joyce has been with the Commission for 18 years.
4 She's worked in the Solicitor's Office, the Enforcement
5 Division, Markets, Tariffs, and Rates. She joined me about
6 four months ago, along with May Briscoe, who has cautioned
7 me that I have to keep this quick, because she's very shy.
8 (Laughter.)
9 COMMISSIONER BROWNELL: May worked for Judge
10 McCartney and Judge Benkin in the Office of Administrative
11 Law Judges. She's been with the Commission for five years,
12 and prior to that, was with the Department of the Navy.
13 They have been a wonderful addition. The team
14 loves them. You will love them. My children love them
15 because they know where I am and what I'm doing and how to
16 find me. I am enormously grateful for their commitment and
17 their enthusiasm and the great good will they have in
18 tolerating the rest of Team B, including myself.
19 (Laughter.)
20 CHAIRMAN KELLIHER: Commissioner Kelly?
21 COMMISSIONER KELLY: I'd also like to make an
22 announcement and introduce a new member of my staff. Many
23 of you know my advisor, Laura Valas. She gave birth to her
24 first child, William, last week. They are both happy and
25 healthy.

1 And Elizabeth Blau, Elizabeth, would you stand
2 up, please? Elizabeth Blau will be working for me for the
3 four months that Laura is off with maternity leave, and I
4 want to tell Elizabeth publicly, how much I appreciate her
5 willingness to take over this job for four months, and how
6 much I have appreciated her help in getting ready for this
7 open meeting. Thanks.
8 CHAIRMAN KELLIHER: I'd like to make a few
9 announcements before we get to voting items, and the
10 discussion items. First of all, one is on Hurricane Wilma.
11 As you know, the State of Florida was recently
12 hit by Hurricane Wilma on October 24th. Hurricane Wilma
13 passed through the greater Key West area and impacted
14 several cities in southern Florida, metropolitan areas,
15 including Palm Beach, Ft. Lauderdale, and Miami, causing
16 severe damage as a result of the intense winds of the
17 rapidly moving system.
18 Hurricane Wilma was the most devastating storm to
19 hit the Florida Power and Light System, causing a loss of
20 power to 3.2 million customers in South Florida. To help
21 the recovery efforts, on October 28th, the Commission issued
22 an Order waiving the standard of conduct recordkeeping
23 requirements for Florida Power and Light, through November
24 15th.
25 Eighteen days after the storm hit, Florida Power

1 and Light had restored service to every capable of accepting
2 power. I just want to praise Florida Power and Light for
3 its impressive recovery efforts.
4 I'd also like to announce a new publication that
5 the Commission has, a Guide to LNG: What all Citizens Should
6 Know. It's now available to the public by contacting the
7 Office of External Affairs, at 202-502-8004, and it's also
8 available in the back of the room for those of you who are
9 present physically -- not electronically. It's also
10 available on our website for those who are here
11 electronically.
12 The Guide's purpose is to provide facts, to
13 provide citizens with information regarding the future
14 demands for natural gas, the nature of liquified natural
15 gas, the Commission's role in the development of new LNG
16 terminals and opportunities for citizens to be involved in
17 the LNG terminal review process.
18 Demand for natural gas is certainly growing, and
19 the increased demand will be met, in part, through importing
20 natural gas, and acquiring LNG from overseas, will require
21 the construction of new LNG import terminals.
22 In recent years, the Commission has authorized
23 eight new LNG terminals, three of which are under
24 construction, and more than a dozen projects in various
25 stages in the Commission's process, and another ten

1 potential terminal sites that have been identified by
2 various sponsors.
3 Given the nationwide interest in LNG, we're
4 hopeful that this publication will be valuable to the public
5 in understanding this critical energy source and our efforts
6 to authorize safe and secure LNG projects.
7 I have another announcement on Joint Boards.
8 This week, we consider our work on Energy Policy Act
9 implementation. In accordance with our September 30th Order
10 and the Energy Policy Act of 2005, the Commission recently
11 held two initial Joint Board meetings in Palm Springs,
12 California, to address economic dispatch.
13 The meetings studied the issue of security-
14 constrained economic dispatch to the various market regions;
15 considered issues relative to what constitutes security-
16 constrained economic dispatch, and how such a mode of
17 operating affects or enhances reliability and affordability
18 of service. We discussed possible recommendations to the
19 Commission.
20 Our remaining two Joint Board meetings will be
21 held in Chicago, Illinois and in Boston, Massachusetts on
22 November 21st and 29th, respectively, both chaired by my
23 colleague, Commissioner Brownell.
24 The Joint Boards are a new thing for the
25 Commission. The Joint Board meetings held earlier in the

1 week, were the first the Commission has held in decades.
2 Since I joined the Commission, I frankly have
3 been looking for an opportunity to establish a Joint Board,
4 and Congress gave us one with the Joint Boards in the Energy
5 Policy Act.
6 I just want to clarify that the Commission has no
7 preconceptions on any recommendations that might be made by
8 the Economic Dispatch Joint Boards. We have no agenda,
9 other than doing the job that Congress gave us.
10 I want to be clear on how the Joint Boards are
11 supposed to operate under the Energy Policy Act. Under the
12 Energy Policy Act, the Joint Boards are charged with, quote,
13 "... considering issues relevant to economic dispatch and
14 making recommendations to the Commission. In turn, the
15 Commission is directed to report to Congress on the
16 recommendations of the Joint Boards, if any."
17 In short, the Commission is required to report to
18 Congress, but not required to make recommendations on
19 statutory or regulatory changes. Whether we do so, will
20 depend on the deliberations of the Joint Boards.
21 Tomorrow, as I mentioned earlier, the Commission
22 will hold a Reliability Technical Conference. It will be
23 the first of two technical conferences that will focus on
24 current and future procedures for establishment and approval
25 of electric reliability standards.

1 The discussions at the technical conferences will
2 focus on, one, the process that the electric reliability
3 organizations will use in proposing new mandatory
4 reliability standards; two, the role of regional entities in
5 that process; and, three, how existing reliability standards
6 can be improved over time.
7 At the technical conferences, we'll hear from a
8 variety of stakeholders, including NERC Regional Reliability
9 Councils, regional utilities, the Canadian Provinces, and
10 U.S. Government entities.
11 There will be three panels at tomorrow's
12 conferences. The first panel will discuss future
13 interactions with NERC Regional Councils, and with
14 anticipated future interactions with ERO and the regional
15 entities and the challenges anticipated.
16 The second panel will elicit comments from
17 Regional Councils regarding preparations being made to
18 implement the Energy Policy Act and their perspectives on
19 regional standards, variances, compliance, enforcement, and
20 delegation agreements.
21 And speakers from the final panel will provide
22 insights into how standards are developed, the challenges
23 faced, and lessons learned.
24 The second conference will be held on December
25 9th and will continue explore related issues and

1 stakeholders' views to assure successful implementation of
2 the Energy Policy Act. These conferences come at a
3 particularly important time.
4 On August 8, 2005, President Bush signed the
5 Energy Policy Act into law. That law gave the Commission
6 important new responsibilities to improve mandatory
7 reliability standards and to ensure that they are properly
8 enforced.
9 The Commission is committed to faithfully
10 executing these new responsibilities.
11 Now, in anticipation of the filing of the Version
12 0 Standards, once the Commission issues a Final Rule, the
13 Commission has been conducting a constructive review of
14 existing reliability standards.
15 We've also been examining the relationship of the
16 Version 0 Standards to existing regional standards. This
17 process has been very instructive.
18 We're holding these technical conferences to help
19 the Commission better understand existing reliability
20 standards and the relationship between North American and
21 regional standards.
22 As I said earlier, you can view the webcasts of
23 these conferences, free of charge, through our website.
24 Another upcoming meeting is the Office of Energy
25 Projects Hydro Workshop. On December 1st, the Commission

1 will be hosting its fifth Hydro Licensing Status Workshop.
2 This year's workshop will focus on 18 license
3 applications pending at the Commission for three years or
4 more. Our objective is to determine the best course of
5 action to remove obstacles to final Commission action.
6 We'll begin the workshop at 10:00 with projects
7 located in the East -- Maine, Vermont, New York, and
8 Wisconsin. Then, at 11:30, we'll begin discussion of
9 projects in the West -- California, Oregon, and Washington.
10 On November 23, 2005, copies of the slides for
11 each project on this year's workshop will be available on
12 our website, and, again, another advertisement,
13 www.ferc.gov.
14 I'd like to make a few comments on notationals.
15 I appreciate my colleagues' forbearance, but I'd like to
16 note the good work of the Commission in between these open
17 meetings.
18 Now, since the October open meeting, we've issued
19 79 notational Orders, including some very significant
20 Orders, and I'd just like to make some comments on three of
21 those notationals.
22 First of all, the Enron settlement: This week,
23 the Commission approved a comprehensive settlement between
24 Enron and the California Parties, Oregon and Washington
25 Attorneys General, and the Commission Staff.

1 This settlement marks a turning point in the
2 Commission's efforts to bring closure to the 2000-2001
3 Western energy crisis. I want to congratulate the parties
4 for reaching this comprehensive settlement with Enron, which
5 resulted from the Commission's strong enforcement actions to
6 date.
7 Now, with this settlement, the Commission has
8 accepted or facilitated $6 billion settlements related to
9 the 2000-2001 crisis. This is an impressive record, even
10 more so because the enforcement tools available to the
11 Commission were so weak before enactment of the Energy
12 Policy Act of 2005.
13 The Energy Policy Act gave the Commission
14 significant new enforcement authority, including significant
15 civil penalty authority, and we're moving to implement this
16 new authority, swiftly and thoughtfully.
17 Now, settlements are often in the best interests
18 of all parties. Negotiations continue with other parties
19 and are continuing in an attempt to reach agreements with
20 Enron and the Commission involving market manipulation and
21 overcharges during the 2000-2001 Western energy crisis.
22 Another significant notational approved since the
23 last meeting, was the LICAP Settlement Order. Last month,
24 the Commission issued an Order giving the New England
25 parties a further opportunity to pursue a settlement on an

1 alternative to the LICAP proposal.
2 At oral argument that the Commission held in
3 September, there was universal agreement that there is a
4 problem in New England. The status quo is failing and
5 generation resources are not being added at a level
6 necessary to maintain reliability and to assure just and
7 reasonable wholesale power rates.
8 There was also broad consensus that the
9 Commission needs to act. Now, oral argument gave parties an
10 opportunity to propose workable alternatives to LICAP.
11 After oral argument, a number of parties
12 submitted a joint motion requesting the appointment of a
13 Settlement Judge, and the Commission accepted this motion
14 and directed a Settlement Judge be appointed.
15 The Settlement Order gives the region a further
16 opportunity to develop a workable alternative to LICAP, and
17 I urge the parties to dedicate themselves to that end and to
18 reach a settlement.
19 Now, our action was consistent with the Energy
20 Policy Act, which encouraged the Commission to, quote,
21 "carefully consider alternative regional views," and we have
22 been doing so.
23 Now, the collapse of generation additions and the
24 threat that poses to electric system reliability and to just
25 and reasonable wholesale power prices in New England, cannot

1 be ignored.
2 I do not want to see the California crisis
3 visited upon New England. Ultimately, the Commission does
4 have a duty under the Federal Power Act, to assure just and
5 reasonable wholesale power prices in New England.
6 A third significant notation we've approved since
7 the last open meeting -- well, actually a pair -- related to
8 market-based rates.
9 There were two market-based rate basket Orders
10 the Commission approved. These Orders relate to timely
11 submission of triennial market power analysis, a condition
12 of market-based rate authorization.
13 Under the Commission's market power test, public
14 utilities authorized to charge market-based rates, are
15 required to submit market power analysis at the end of three
16 years.
17 If that analysis demonstrates an absence of
18 market power or the applicant mitigates market power, the
19 applicant can continue to charge market-based rates.
20 Otherwise, the Commission may initiate a Section
21 206 proceeding and revoke market-based rate authorization.
22 Now, some companies have been negligent in filing triennial
23 analyses.
24 This issue came to light in the Spring in the Con
25 Edison Order. Con Edison was 17 months late filing its

1 triennial analysis, and the analysis it filed, was patently
2 deficient.
3 The Commission invested a great deal of time and
4 energy repairing the deficiencies.
5 Now, upon further investigation, the Commission
6 Staff determined that ConEd was not the only offender, nor
7 was it the worst offender.
8 Over 200 companies were late filing their
9 triennial analysis, and some were more than a decade late.
10 Now, in May 2005, the Commission issued a basket Order,
11 identifying all the companies that were late in filing their
12 triennial analyses and initiating a Section 206
13 investigation.
14 These companies had every opportunity to preserve
15 their market-based rate authorization. All they had to do
16 was follow the rules and submit a triennial analysis that
17 was consistent with our rules.
18 The Three-Es technology basket Order revokes the
19 market-based rate authorization of about 100 companies. All
20 of these companies either refused to submit a triennial
21 analysis, or submitted an analysis that was patently
22 deficient.
23 Now, since the Commission has been clear in its
24 requirements and has given these companies every opportunity
25 to preserve their market-based rate authorization, we

1 revoked their authorizations, effective immediately.
2 The Commission further directed the companies, in
3 the Revocation Orders, to file a report within five days,
4 stating whether they made any sales under their market-based
5 rate tariffs, after the refund-effective date established in
6 the May Order.
7 The Commission may order disgorgement of profits
8 from any such sales.
9 Now, going forward, the Commission will routinely
10 initiate a Section 206 proceeding when triennial analysis is
11 not submitted in a timely manner. Now, the revocation
12 basket Orders are a reminder that authorization to charge
13 market-based rates is a privilege, not a right, and the
14 Commission will not tolerate abuse of the privilege, and
15 companies that violate conditions of market-based rate
16 authorization, can expect similar treatment.
17 Now, the Commission issued another based Order,
18 ALCAM, which accepted the updated market analyses of more
19 than 50 companies that complied with the May 2005 Order, and
20 terminated the Section 206 proceedings initiated with regard
21 to those entities.
22 Those companies retain market-based rate
23 authorization, and may continue to make market-based sales.
24 The second basket Order shows that the Commission
25 will be fair and reasonable in reviewing market-based rate

1 authorization requests, when the companies comply with our
2 rules.
3 Now, I'd like to thank my colleagues, and their
4 Staffs and the Commission Staff for working closely and
5 effectively with me and my staff on the notationals we've
6 issued since our last open meeting, as well as the Orders on
7 the agenda today.
8 And I'd just like to ask my colleagues if they
9 have any comments on the subjects I've been discussion.
10 COMMISSIONER BROWNELL: Just a few quick
11 comments. In fact, I want to thank the Staff for the
12 prodigious amount of work that they are doing, not only to
13 keep us on target for our EPACT deadlines, but to continue
14 with the enormous work.
15 You can tell by the volume of notationals, that
16 that life goes on. So I'm grateful to them.
17 On the Enron settlement, I'd just like to take
18 the opportunity to say for about the 200th time, to echo
19 your sentiments, that settlements are often in the best
20 interests of the parties. That is particularly true, I
21 think, in California, which continues to suffer from a lack
22 of investment in infrastructure, and we talked about that
23 earlier this year.
24 And one of the reasons is the fear of litigation,
25 and so I would encourage the parties in all of the

1 California issues, to begin to really focus on your future,
2 as I think, quite clearly, the citizens of California did in
3 the most recent election when they resoundingly defeated an
4 initiative that would put them backwards and deny them
5 choice for the continued period of time.
6 So I think we need to start listening to the
7 customers, and I think that California needs to focus on the
8 future, as the Commission is with their resource adequacy
9 decisions and other decisions.
10 But closure is important, and I think we need to
11 expedite that closure.
12 On the LICAP settlement talks, I really add to
13 your sentiments that I hope the parties can come to some
14 settlement.
15 We certainly are prepared to help them along in
16 any way possible, but we can't ignore the fact that it's
17 important that that region begin to get a better handle on
18 their infrastructure needs, the regional planning process
19 that has not happened, which has been a barrier to entry,
20 and, frankly, the fact that one state seems to be holding up
21 any approval of infrastructure, whether it's on their
22 territory or not -- and interesting concept, I think -- and
23 I think people need to look beyond the political activities
24 of one state, to the larger needs of the economic
25 development of the region, in general.

1 I had a wonderful visit in New England last week,
2 and the Governor of Rhode Island was there, and that's
3 exactly what he's thinking of.
4 So I hope that we can help move forward, not only
5 here, but in other issues.
6 Thank you. That's all I wanted to say.
7 COMMISSIONER KELLY: I only wanted to add
8 something with regard to the efforts to undertake a
9 settlement in the LICAP case.
10 I'd like to thank, in particular, the Chair of
11 the Massachusetts Department of Public Utilities, who has
12 really spearheaded this effort to get all of the states and
13 the RTO together to see if they could come to an agreement.
14 And it does appear that with perhaps the
15 exception of one state in New England, all agree that a
16 long-term locational capacity market is necessary. I'm glad
17 that our oral argument -- holding our oral argument, seemed
18 to give some incentives for the parties to sit down at the
19 same table with each other, and I am hopeful that they can
20 make some progress, at least, in resolving this issue for
21 New England.
22 CHAIRMAN KELLIHER: Thank you. Madam Secretary,
23 let's turn to the consent agenda.
24 SECRETARY SALAS: Sure. Good morning, Mr.
25 Chairman and good morning, Commissioners. The following

1 items have been struck from the agenda since the issuance of
2 the Sunshine Notice on November 10; they are: E-1, E-5, E-
3 12, E-25; G-2, and G-6.
4 Your consent agenda for this morning is as
5 follows: Electric Items - E-4, 6, 7, 8, 9, 10, 11, 13, 15,
6 16, 17, 18, 19, 21, 24, 26, and 27.
7 Gas Items: G-1, 3, and 4.
8 Hydro Items: H-1, 2, 3.
9 Certificates: C-2, 3, 4 and 5.
10 The specific votes for some of these items are:
11 On E-24, Commissioner Kelly, dissenting, in part, with a
12 separate statement; and on C-3, Commissioner Brownell,
13 dissenting, in part, also with a separate statement; and
14 Commissioner Brownell votes first this morning.
15 COMMISSIONER BROWNELL: Aye, noting my partial
16 dissent on C-3.
17 COMMISSIONER KELLY: Aye, with the exception of
18 my partial dissent in E-24.
19 CHAIRMAN KELLIHER: Aye.
20 SECRETARY SALAS: The first item for discussion
21 this morning is the one scheduled under A-1, and this will
22 be a Winter Energy Market Assessment for 2005-2006. It is
23 a presentation by Steve Harvey from the Office of Market
24 Oversight and Investigations, and Jeff Wright from our
25 Office of Energy Projects.

1 CHAIRMAN KELLIHER: Let me just explain why I
2 asked for this presentation. There's been a lot of movement
3 in gas prices recently, and I thought it would help us to
4 really get a briefing to explain what the causes of those
5 movements are, and whether some of them are transient, some
6 of the causes are transient or permanent in nature, and also
7 to really look at the import questions.
8 We've talked over the past month, of how the U.S.
9 has lost significant gas supply from the hurricanes, and we
10 can't make it up through imports, but I just wanted to
11 really hone in on that second point -- why can't we make up
12 the loss of supply through imports?
13 And with that, I look forward to your
14 presentation.
15 COMMISSIONER KELLY: Joe, before they begin, I'd
16 just to like to say how much I appreciate your leadership
17 and the Staff's leadership on this issue. I think that
18 there is continuing interest around the country in the
19 facts, and in knowing what the facts are regarding the
20 supply of natural gas and the prices.
21 You and I were in the West last -- earlier this
22 week, and we had many people ask us about the cost of gas
23 and the impending cost of gas, and why the cost of gas
24 remains high, and so I think that although this is very
25 helpful to us, that it does a service to the entire country,

1 for your office, Steve, to be presenting this information.
2 CHAIRMAN KELLIHER: Thanks. And this shows how
3 focused the Commission is on gas prices, and if you've
4 watched the Commission over the past month, you'd think that
5 it's 1985 and we're a gas agency again. You know, this is
6 really the third major presentation we've had on gas price
7 issues over the past month, and I think we'll probably keep
8 it up throughout the rest of the Winter, but I look forward
9 to the presentation.
10 (Slides.)
11 MR. HARVEY: Thank you. Good morning Mr.
12 Chairman and Commissioners. Jeff Wright of the Office of
13 Energy Projects, and I would like to present you with an
14 update on natural gas market issues, as we enter the Winter.
15 At your last meeting, Tom Pinkston presented
16 Staff's Winter assessment, which underscored the significant
17 challenges faced by U.S. natural gas markets for the coming
18 Winter.
19 While there have been some changes in the
20 situation, the most significant drivers remain largely the
21 same: Prices and availability of supply will be dependent
22 on weather, with any significant cold weather likely to
23 drive prices higher, possibly much higher over the short
24 term.
25 Also important is the industry's ability to

1 recover production lost in the Gulf Coast due to Hurricanes
2 Katrina and Rita during the late Summer. These conditions
3 have resulted in volatile markets, where price spikes are
4 likely.
5 Over the past three weeks, however, there has
6 been some good news regarding our ability to face challenges
7 this Winter. I'll review those recent developments in more
8 detail next, and then Jeff will discuss the limited ability
9 of increased imports this Winter to make up for Gulf
10 production losses.
11 Over the past three weeks, spot prices weakened
12 considerably, due to a variety of factors. First, we began
13 to see real progress in recovery in Gulf production. In
14 addition, weather in late October and early November, until
15 today here in Washington, has been extremely mild.
16 This fortuitous weather pattern has given an
17 extra boost to storage inventories, allowing for continued
18 injections, despite the Gulf reductions. Still, prices for
19 futures for delivery across the rest of the Winter, have
20 remained relatively strong, compared to spot physical
21 markets, signalling the expectation that prices will rise
22 over the next few months.
23 Yesterday, spot gas prices across the Northeast
24 U.S. surged by 25 percent, with the approach of the cold
25 front we're feeling today.

1 Spot prices at Henry Hub, Louisiana, shown in the
2 figure now on the screen, rose a little less, about 20
3 percent, but the effect of volatility is clear here, as
4 well.
5 This graph starts in May and shows the Henry Hub
6 spot price rising through the Summer, largely due to
7 increased electric generation demand.
8 The effects of Katrina and Rita are clearly
9 marked. The red line disappears briefly after Katrina and
10 longer after Rita, because Henry Hub was not physically
11 operating, so trading wasn't taking place there during that
12 period.
13 Approximately three weeks ago, spot prices peaked
14 again on a variety of factors, including a quick cold front.
15 Since then, with the exception of yesterday, spot
16 prices dropped at Henry from their high that was close to
17 $50 per Mmbtu, to about $9.
18 Yesterday's increase brought the price back to
19 about $11. When I came down this morning, that price was
20 trading up to about $12, as well, with the continued cold
21 weather.
22 While these prices can't be considered low in a
23 historical context, they are now closer to late Summer, pre-
24 hurricane prices, than post-hurricane prices.
25 Today's trading could be interesting as the

1 traders work out their expectations of the duration and
2 effect of this cold front, as well, as the significance of
3 today's storage report from the Energy Information
4 Administration.
5 This graph shows the effects of the hurricanes on
6 Gulf production, plotted over time. The red line shows how
7 much production was not available due to the hurricanes,
8 starting with Katrina.
9 The initial effect of Katrina was to reduce
10 deliveries by close to nine billion cubic feet, or Bcf of
11 natural gas per day.
12 That fell over a few weeks to less than four Bcf
13 per day, before increasing again with Rita, to about eight
14 Bcf a day.
15 Reductions after Rita, dropped to between five
16 and six Bcf per day, with some additional supply shut in as
17 preparation for Hurricane Wilma.
18 That level did not drop significantly until the
19 last two weeks when close to two Bcf per day of shut-in
20 production returned.
21 As of yesterday's report from the Minerals
22 Management Service, shut-in gas is now less than four Bcf
23 per day.
24 Four Bcf is a significant reduction in supply,
25 and, clearly, concerns in the natural gas spot and futures

1 market are driven by this statistic.
2 We'll continue to watch the recovery of these
3 supply sources through the Winter, and as the Chairman
4 pointed out a moment ago, these are fundamental, permanent,
5 in effect, benefits to the supply situation as we go into
6 this Winter.
7 Nevertheless, the effects of mild weather have
8 largely overcome the effects of reduced Gulf production for
9 the past few weeks, resulting lower prices. This graph
10 plots storage inventories for the past five years, at the
11 same time of the injection and withdrawal season, starting
12 on April 1st.
13 The red line is the storage inventory this year,
14 and you can see that inventories remain quite high,
15 currently higher than any of the past five years, with the
16 exception of last year.
17 I was informed just moments ago that the EIA,
18 that reports at 10:30 in the morning on Thursdays, reported
19 another injection from last week of 53 Bcf, another strong
20 injection for this time of year, which reflects, again, the
21 mild weather from last week, so we continue to build that
22 inventory going into the Winter.
23 At these high storage inventories, it is harder
24 to inject as much into storage, consequently, recent
25 injections indicate extremely weak demand right now,

1 momentarily, contrasted with the weak supply situation I
2 just described.
3 The past now four EIA reports of continued
4 injections, have effectively put the country in a stronger
5 position to manage cold weather for the rest of the Winter.
6 The storage, alone, may not be able to make up
7 for the continuing severe supply reductions in the Gulf.
8 The remaining options include increasing imports
9 and decreasing demand through emphasizing conservation
10 efforts.
11 At last month's meeting, you heard from a panel
12 of state officials about conservation efforts.
13 Now I'd like to turn the presentation over to
14 Jeff Wright to discuss the limitations on the ability for
15 increasing imports to satisfy demand needs this Winter.
16 (Slides.)
17 MR. WRIGHT: Thank you, Steve. Good morning.
18 Steve noted that the shut-in production in the Gulf of
19 Mexico, is slightly less than four Bcf per day, while a
20 seemingly small amount is not going to be easily
21 replaceable.
22 Average daily gas consumption in the United
23 States is approximately 60 billion cubic feet, and, on peak
24 days, will exceed 80 billion cubic feet.
25 Some expect these volumes to be replaced by

1 imported gas, either pipeline imports from Canada, or
2 increased LNG imports. This will probably not be the case.
3 Traditionally, Canadian gas has accounted for
4 nearly all of our imported amounts of gas, as much as 16
5 percent of our total gas supply. However, through August of
6 this year, we are actually seeing imports from Canada,
7 running behind the same time period in 2004.
8 Canadian gas production is actually flattening,
9 while at the same time, Canadian gas demand is growing,
10 resulting in less gas being available for importation and
11 subsequent consumption in the United States.
12 In addition, it does not appear that there will
13 be a significant increase in LNG imports during this Winter
14 to cover production shortfalls.
15 Currently, the aggregate capacity of the existing
16 LNG terminals in the lower 48, is not being fully utilized,
17 and LNG import levels are lagging behind 2004 levels.
18 There are indications that LNG shipments to the
19 U.S. will increase over the next several months. Further,
20 there is new terminal capacity being constructed, but this
21 will not be available until 2008, at the earliest.
22 Increased levels of LNG imports are being
23 thwarted by non-regulatory impediments. The prime
24 bottleneck to increased imports, is the amount of available
25 of worldwide liquefaction capacity.

1 As of 2004, there was at least twice as much
2 regasification capability as liquefaction. This tight level
3 of liquefaction, while expected to ease somewhat by 2010,
4 does not cure the present sellers market.
5 This leads into the next impediment, which is the
6 existence of supply contracts. Merely having a
7 regasification facility, does not guarantee that you will be
8 able to easily obtain gas supply.
9 Much of the LNG imported into the U.S. is
10 imported into the U.S. under short-term arrangements, as
11 opposed to the rest of the LNG-consuming world that utilizes
12 longer-term contracts with suppliers.
13 These existing arrangements and commitments and
14 the willingness of non-U.S. LNG customers to in some
15 instances outbid U.S. entities for excess LNG cargoes,
16 demonstrates again that the capacityholders in U.S. LNG
17 facilities, need to negotiate supply contracts with longer-
18 term commitments.
19 Also looming is the spector of increased
20 competition in the form of developing countries like Chin
21 and India, whose gas demand is expected to increase
22 exponentially in the coming decade.
23 This slide shows our recent levels of LNG
24 imports, vis a vis the sendout or redelivery capacity. This
25 enforces my earlier point that capacity has not been fully

1 utilized.
2 This year, a new offshore LNG terminal, Gulf
3 Gateway, began service, and Trunkline LNG's Lake Charles
4 facility recently increased its deliverability slightly.
5 Next year, the Lake Charles facility will put
6 more storage and deliverability capacity into service, and
7 Southern's Elba Island facility will do the same.
8 It must be pointed out that these are relatively
9 minor additions, and while an uptick in the amount of
10 imports is expected, it will not be near-term panacea for
11 lost production.
12 The earliest one can expect a major increase in
13 LNG capacity, is in 2008, when three new LNG terminals will
14 come online. By that time, it is expected that the new
15 facilities will have supply contracts in place that will
16 take greater advantage of their redelivery capability.
17 For it's part, the FERC has acted quickly and
18 decisively on the applications put before it. The Hackberry
19 decision in December 2002, which no longer required open
20 access to terminal capacity, essentially deregulated, in an
21 economic sense, LNG terminals.
22 This paved the way for project sponsors to seek
23 authorization for a large number of new LNG facilities.
24 Since the Hackberry decision, the Commission has
25 approved eight new terminals with the ability to deliver up

1 to 12 billion cubic feet per day of regasified LNG.
2 Currently, as I mentioned, three of these
3 facilities are under construction, with a total
4 deliverability of 5.6 Bcf per day.
5 There are also 12 applications pending for
6 another 16.7 Bcf per day of delivery capacity.
7 I would note that the Commission is processing
8 these applications, on average, in less than a year's time,
9 and with the mandatory prefiling process required by the
10 Energy Policy Act of 2005, these processing times should
11 continue to decrease.
12 In sum, the hurricane activity of the last few
13 months, has shut in Gulf production that may not be
14 recovered until next Spring. In the interim, we do not see
15 any significant increase in storage inventories, pipeline
16 imports or LNG imports, that will make up for the production
17 lost this Winter.
18 Further, while the future of LNG looks promising,
19 significant supply increases may not be realized until 2008,
20 at the earliest. Given this, the key to this Winter and
21 possibly the next couple of Winters, besides hoping for mild
22 weather, is for increased conservation on the part of gas
23 consumers, and demand-side management programs to ease gas
24 demand in the United States.
25 That concludes our presentation and we'll be

1 happy to answer any questions.
2 CHAIRMAN KELLIHER: Thank you very much for that
3 presentation. I think that was very helpful, particularly
4 on the import question -- well, on both the import and the
5 supply question.
6 On imports, there seems to be a perception that
7 because of the celebrated nature of some of the LNG terminal
8 proceedings, that the bottleneck in importing more LNG is
9 the terminal capacity, that we're limited in our terminal
10 capacity, and that's what's impeding imports.
11 Your presentation shows that's exactly untrue.
12 Current import capacity is much greater than the current
13 level of imports.
14 We've approved tripling the amount of import
15 capacity, but even that addition is not contracted out.
16 Anyway, I think facts are useful things. Sometimes they're
17 nettlesome, but it's good to get them out, and thank you for
18 that.
19 Steve, I have a question about your storage
20 inventory chart. I have a question about March. What do
21 people think about March? Where will the 2006 line be? Is
22 it predestined to be lower than the previous five years?
23 MR. HARVEY: I think the general expectation is
24 that with some amount of Gulf production not available, even
25 -- in effect, there are two questions in there.

1 One is, what do we think weather will do for the
2 course of the Winter, and if I kind of flip that question by
3 saying, let's assume it's sort of like average, the question
4 is, if you take out, hopefully, something less than four Bcf
5 a day through the course of the Winter, as things continue
6 to improve, how much less is not completely clear.
7 It will mean drawing on storage more
8 aggressively, and, given sort of typical circumstances, we
9 would expect, I think, a sort of lower end by the end of
10 March, but, again, dependent on conservation efforts,
11 dependent on sort of other demand efforts.
12 So, much of the demand in the Winter is weather-
13 dependent; it really is heating load, in effect. That
14 really becomes the toughest variable.
15 CHAIRMAN KELLIHER: Okay. And you made this
16 point, but the recovery of offshore production is no reason
17 to think that's transient; that could be considered
18 permanent, and the only question is, what is the rate of
19 future recovery?
20 MR. HARVEY: Right, right. And it's particularly
21 sensitive through this Winter, obviously. I mean, if you
22 look at, like, the futures markets, they are, as we call it,
23 backward-dated.
24 They seem to assume, over the course of enough
25 time, there will be a good production response, there will

1 be a result there, but through the Winter, it's sort of more
2 of a question, and, so, consequently, this Winter's expected
3 or this Winter's futures prices are trading much higher than
4 other future Winters' futures prices, because of the local
5 condition that we've got.
6 CHAIRMAN KELLIHER: Thank you. I want to thank
7 OMOI, because OMOI is giving the Commission, the question,
8 and, it's more important now than it was a few months ago,
9 at least from our point of view, and OMOI is now giving the
10 Commission a weekly report on the recovery of offshore
11 production, because it certainly is affecting price. Thank
12 you for your presentation. Questions?
13 COMMISSIONER BROWNELL: I have some questions.
14 Help me out with the long-term contract issue.
15 What are the barriers? Is it my friend who was
16 here a couple of weeks ago from Standard and Poor's, that
17 loves it when some people, part of the energy sector, signs
18 long-term contracts and penalizes people who actually sign
19 them? What's the problem?
20 That price competition from Europe, particularly
21 for that spot LNG, we've already seen the impact of that.
22 MR. HARVEY: There's probably two answers to
23 that, one, sort of the LNG-oriented, and one is sort of the
24 market-oriented one.
25 Let me start real quick on the market and I'll

1 have Jeff kind of handle the LNG implications.
2 I think there are challenges in terms of long-
3 term contracts around credit, in particular. This is an
4 industry that takes credit a great deal more seriously,
5 probably, than it did a couple of years ago.
6 So, establishing creditworthy relationships for
7 that period of time, you also have another effect, which
8 really is, I think, a focus on spot index-based pricing,
9 which, because it's such a clear benchmark, becomes
10 appealing for many companies to say this is how I buy
11 against an index.
12 As we're seeing particularly this Winter, that
13 index can be quite a ride in terms of volatility off of the
14 spot price.
15 There are a couple of motivations that are still
16 out there: One, the difficulty of doing long-term contracts
17 from a credit perspective of getting creditworthy
18 counterparties in place; then the other one really is for
19 buyers. What are they motivated to do?
20 I hope, based on the conversations from the panel
21 at your last meeting, that people are focusing more and more
22 on looking out farther term, which I think will handle
23 volatility a lot better and at least take some of the bumps
24 out.
25 MR. WRIGHT: I think that on the LNG side, what

1 you see today in the world, is a lot of the regasification
2 capacity -- I'll use Japan as an example, Spain as an
3 example -- are owned by utilities under must-serve
4 requirements.
5 For instance, Spain has had a severe draught this
6 Summer, loss of much of their hydro generation capacity, had
7 to replace it with gas-fired. They are under a mandate from
8 their government to go out and pay anything -- Henry Hub-
9 plus -- to get those cargoes, any extra spot cargoes to come
10 to Spain.
11 In addition, like I said, being utility-backed
12 regasification plants, they have entered into long-term
13 contracts. They have long-term relationships with that
14 small, but crucial amount of liquefaction that's out there,
15 so they lock up that liquefaction.
16 There's not a whole lot left, and in the U.S. so
17 far, we don't follow that model in terms of utility-owned
18 regasification. I guess Everett could be the closest to
19 that, in that they do serve a lot of utilities up there,
20 and, in essence, act like a utility in many respects.
21 But the other three lower 48 regasification
22 plants, tend to just find cargoes when they can, and the
23 capacityholders tend to look more short-term than long-term
24 at this point in time.
25 COMMISSIONER BROWNELL: Spain has how many LNG

1 plants? And they've got them throughout, and they're
2 building at least one more, I think.
3 MR. WRIGHT: At least one more large one, I know,
4 is due to come online in the not too distant future, but, at
5 present, I'd say there's probably four; in Japan, there's
6 26.
7 COMMISSIONER BROWNELL: And they have relied on
8 that for a long time.
9 MR. WRIGHT: Yes, Japan being the country that
10 controls about half the LNG trade in the world.
11 COMMISSIONER BROWNELL: Maybe New England wants
12 to visit them.
13 Tell me this: The assumptions of 2008, the three
14 that are under construction, are they actually under
15 construction and we're not going to see any -- well, we can
16 never predict that, but they're on track, so that it's
17 likely they will be done. There's not going to be any
18 surprising litigation that holds them up in the end?
19 MR. WRIGHT: No, they've cleared all of the
20 litigation. It's a question of commencing construction and
21 keeping on schedule, in that sense.
22 COMMISSIONER BROWNELL: Just one observation that
23 I would like to make: This business group that was New
24 England and Canadian businesses, we talked a lot about
25 demand response.

1 In fact, in some sense, that turns into demand
2 destruction, particularly for the manufacturing sector,
3 which is already affecting Rhode Island, for example.
4 I think it's nice to say we'll rely on
5 conservation and demand response. Certainly, if we had
6 empowered customers with more choices to make, we could do
7 that more effectively.
8 But at some point, you have to say, what does
9 that actually mean, and we need to think about the economic
10 effects of this, I think, in a clearer way, so I'm hoping
11 we're going to work with some of the major industries or
12 even with Governors in the states to track what it is
13 they're actually seeing in that sense. We certainly saw it
14 in the Northwest during the crisis there. Thanks.
15 MR. ROBINSON: Could I just add one point to the
16 comment Jeff made on the contracts and how they differ from
17 what's going on now, versus what's coming in 2008?
18 The projects going online in 2008, are having
19 dedicated supplies associated with them. For example, the
20 Golden Pass Project in Texas, the Train 6 in Qatar, is
21 dedicated 100 percent to that project.
22 What we're seeing now wit the three projects that
23 came online as gas, became more of a concern in the late
24 1990s and 2000, and they're out searching for cargoes. It
25 won't be the model that's in play with the projects that

1 come online in 2008.
2 They're only coming online when they have a
3 supply source dedicated to them. It will be more of a
4 baseload type of situation with those projects, the newer
5 ones coming online.
6 COMMISSIONER KELLY: I was going to add to that
7 discussion. Basically, we can look in the United States at
8 two kinds of markets for LNG.
9 One tends to be in the supply area, so LNG in the
10 Gulf. The LNG that comes into that area, is basically
11 looked upon as more exploration, development, and
12 production, so it's part of the supply of gas in the United
13 States.
14 Therefore, they can compete in the spot market
15 for LNG, and put it into the pipes to serve the market
16 areas, as there's room in the pipes, and there tends to be
17 room in the pipes.
18 They may not have the stability of supply, even
19 if they have that liquefaction train dedicated to it. It
20 may not end up, unless it's under long-term contract, coming
21 to the Gulf. It will be spottier, I suspect, but even so,
22 we'll see more LNG come in there.
23 But the other markets in the demand areas, or in
24 the market areas on the East Coast or on the West Coast, are
25 different. If we're going to rely on LNG as a stable source

1 of gas for those market areas, it looks like we're going to
2 have to be and state regulators are going to have to be
3 willing to accept long-term contracts.
4 Because of the nature of the investment and the
5 back end of the system, the liquefaction won't be built, the
6 tankers won't be built, the tankers won't be dedicated to
7 serving the United States, unless there are long-term
8 contracts in place to justify any market investment.
9 So I think that we are going to see a bit of
10 upheaval, in particularly state regulation at the gas level
11 as we try to accommodate different kinds of supply.
12 I also wanted to point out another advantage to
13 LNG, particularly LNG sited in the demand areas. Not only
14 does it supply the gas that we need, but it also provides
15 for storage.
16 Those are precisely the areas where we don't have
17 underground storage, so it serves two needs along the coast.
18 So, I'm pleased that we have a very good record of having
19 approved these LNG facilities, because I think it's clear
20 that the country is going to need them.
21 I had just one question for you, Steve, about gas
22 prices. Do you expect a lot of volatility in gas prices,
23 more so than in the past year?
24 MR. HARVEY: Yes, we've seen that by a number of
25 measures. The most clear today -- again, when I came down,

1 gas was trading at Henry Hub for the next day for $12. That
2 had been as low as about $9 a few days ago, and, about three
3 weeks, ago, as high as $15 for the next day.
4 Those are swings of a third and a quarter within
5 a fairly short period of time. That's showing up across the
6 board, really, in terms of prices right now. The conditions
7 are just such that we have to expect it to be extremely
8 volatile and very linked to weather.
9 COMMISSIONER KELLY: One question about supply:
10 Do we have any information that would lead us to believe
11 that some supply cannot be brought on for the Winter, some
12 of the shut-in supply?
13 Do we know that, or is it possible that all four
14 Bcf could be brought on, or is some of it so adversely
15 impacted that we know we're going to lose it?
16 MR. HARVEY: It's hard to know, obviously. I
17 think there is some damage, which is significant enough that
18 there will be some loss of supply through the course of this
19 Winter.
20 MR. WRIGHT: I think I read, anecdotally, some
21 reports that say maybe as much as two to three Bcf per day
22 will not be recovered during this Winter season.
23 COMMISSIONER KELLY: So then the bottom line is,
24 although the increase in production is very encouraging, it
25 shouldn't change the message that consumers this Winter have

1 to be concerned about conservation.
2 MR. HARVEY: I think that's exactly true. I kind
3 of wanted to go through a set of things.
4 We are in a storage position that is close to --
5 it's not quite as good as it was last year, in aggregate.
6 It's actually a little stronger in the Northeast and a
7 little stronger in the West.
8 The weakness is more in the production area.
9 That puts us in as good a position as we can be in, but it's
10 very difficult to make up for a two- or three-Bcf hole on
11 the supply side.
12 Again, with extreme weather, we are still likely
13 to face difficult conditions. We can hope for no extreme
14 weather; we all are doing that, in which case, you won't
15 have to hear from me again at any time during this Winter.
16 But with any stress on the system, it probably
17 will show up in price fairly quickly.
18 COMMISSIONER KELLY: And that's because, in a
19 time of extreme cold, the pipeline might not be packed with
20 supply from the Gulf and storage might have to be utilized
21 in a way that has been different in the past.
22 MR. HARVEY: Yes. Typically, those pipelines
23 running up from the Gulf, the long-line pipelines running up
24 into the Northeast, if, for example, the Northeast, the area
25 we're talking about, which is the most likely area at this

1 point, those tend to fill up in order to handle the overall
2 demand from the Gulf.
3 Depending on how much is still out, they may not
4 be able to completely do that. I should note quickly that
5 the situation is geographically very different.
6 The West is in a very different situation. We've
7 seen that in prices. We've had much lower prices in the
8 West over the last couple of weeks, than we've seen in the
9 East.
10 The Rockies' supply has come on aggressively, so,
11 really, a line sort of running between the Louisiana and
12 Texas Gulf Coast, really up to the East of Chicago, west of
13 that line, other than prices that I'm sure customers don't
14 like, because they've sort of pulled up the entire national
15 market, the supply situation and the price situation is much
16 more favorable than it really is along the East Coast, which
17 will be the focus of our concerns.
18 MR. WRIGHT: I just wanted to emphasize that pre-
19 hurricane supplies were tight and prices were rising.
20 While that two to four Bcf per day seems de
21 minimis, it's not, because we were tight, even before the
22 hurricanes put us in an even more precarious position.
23 With regard to the Rockies, I'd point out that
24 infrastructure-wise, while it's a very robust gas production
25 area, we really can't expect help, at least on the eastbound

1 volumes until 2008. We've had a couple of proposals for
2 long-line pipelines from the Rockies going east.
3 The predictions are that it will be 2008 before
4 they could come online, as well.
5 COMMISSIONER KELLY: Thank you.
6 COMMISSIONER BROWNELL: I would encourage people
7 who are interested, to look at the INGAA website. INGAA did
8 a wonderful report that does take a look at the country,
9 region-by-region, and runs various scenarios.
10 In some parts of the country, none of them are
11 particularly pretty. I don't know if you spend any time in
12 Massachusetts, Steve, but it's always cold in December in
13 Massachusetts.
14 (Laughter.)
15 CHAIRMAN KELLIHER: Thank you very much; we
16 appreciate it.
17 SECRETARY SALAS: The second item for discussion
18 is E-2, Regulations Providing Incentive-Based Rate
19 Treatments for the Transmission of Electric Energy in
20 Interstate Commerce by Public Utilities. It's a
21 presentation by Jeff Hitchings from the Office of Markets,
22 Tariffs, and Rates, accompanied by Andre Goodson, Sebastian
23 Tiger, Zeny Magos, Steve Pointer, Tina Ham, Deborah Ott, and
24 Paul Robb.
25 MR. HITCHINGS: Good morning, Mr. Chairman and

1 Commissioners. E-2 is a Draft Notice of a Proposed
2 Rulemaking that promotes greater transmission investment in
3 new transmission capacity with pricing reform.
4 The need for capital investment in energy
5 infrastructure is a national problem that requires a
6 national solution. Evidence of inadequate transmission
7 capacity includes declining transmission investment over the
8 past two decades and a significant decrease in transmission
9 capacity relative to demand and generating capacity in every
10 North American Electric Reliability Council Region.
11 Inadequate transmission infrastructure results in
12 transmission congestion and impedes competitive wholesale
13 markets and impairs the reliability of the electric grid.
14 To address the nationwide need for transmission
15 capacity, the Draft NOPR proposes price reforms applicable
16 to the entire electric grid, in both organized markets and
17 in other markets, and to both traditional vertically-
18 integrated utilities and transcos, which the NOPR defines as
19 stand-alone transmission companies approved by the
20 Commission.
21 This Draft NOPR is intended to meet the
22 requirements of Section 1241 of the Energy Policy Act of
23 2005, which adds a new section, 219, to the Federal Power
24 Act, that mandates that not later than one year after
25 enactment of Section 219, the Commission shall establish, by

1 rule, incentive-based rate treatments for the transmission
2 of electric energy in interstate commerce by public
3 utilities, for the purpose of benefitting consumers by
4 ensuring reliability and reducing the cost of delivered
5 power by reducing transmission congestion.
6 Today's Draft NOPR proposes a number of price
7 reforms, including: A rate of return on equity sufficient
8 to attract new investment; recovery in rate base of 100
9 percent of prudently-incurred transmission-related
10 construction work in progress; expensing of prudently-
11 incurred pre-commercial operation costs; hypothetical
12 capital structures; accelerated recovery of depreciation
13 expense; 100-percent recovery of prudently-incurred
14 development costs, where construction of facilities may be
15 abandoned due to circumstances beyond the control of the
16 utility; deferred cost recovery; adjusted book value for
17 assets sold to Transcos; and a higher rate of return on
18 equity for utilities that join transmission organizations
19 such as, but not necessarily limited to RTOs or ISOs.
20 In addition, the Draft NOPR provides cost
21 recovery of prudently-incurred costs necessary to comply
22 with mandatory reliability standards and prudently-incurred
23 costs related to infrastructure development in national-
24 interest transmission corridors.
25 The Draft NOPR also seeks comment, without

1 proposing rules, on performance-based ratemaking, the role
2 of public power, and advanced technology.
3 This concludes our presentation, and we're
4 pleased to answer questions.
5 CHAIRMAN KELLIHER: Thank you. I want to thank
6 you for the presentation and also the hard work of the team
7 to develop this Order. I am impressed and surprised that we
8 have a 3-0 vote on this one, I have to say, but happy at the
9 same time.
10 I just want to make a few comments. One of the
11 major goals of the Energy Policy Act of 2005, was
12 strengthening our energy infrastructure, and particularly
13 the transmission grid.
14 And it's clear, as you indicated in your
15 briefing, that the transmission grid has suffered from
16 under-investment for a significant period, and that last
17 year, for example, according to the OMOI State of the
18 Markets Report, the transmission system expanded by a grand
19 total of 0.6 percent in circuit miles in the last year,
20 2004, and that transmission congestion has been rising
21 steadily since 1998.
22 So I think it is clear that under-investment in
23 transmission is a national problem and it is something that
24 deserves a national solution. Transmission pricing reform
25 can be an important part of the solution, and there have

1 been a number of theories advanced to explain why that
2 under-investment has occurred.
3 One possible cause is the Commission's pricing
4 policies don't adequately attract investment. Congress
5 directed us to undertake a rulemaking to reform transmission
6 pricing.
7 And today we issued proposed rules that would
8 make certain reforms in transmission pricing, and the goal
9 of the proposed rule is clear: Secure greater investment in
10 the transmission grid.
11 Now, a stronger transmission grid will increase
12 electric system reliability and will promote competition by
13 encouraging the development of a transmission grid that can
14 support competitive markets.
15 Greater grid investment will also make it more
16 difficult to engage in undue discrimination and preference
17 in transmission service, because it's much more difficult to
18 detect undue discrimination when the transmission grid
19 itself is constrained.
20 The proposed rules do encourage investment in
21 transmission in all regions and by both vertically-
22 integrated utilities and by Transcos.
23 Just a word on transcos: Transcos are a proven
24 vehicle for transmission investment. The Commission's
25 analysis shows that the three transcos in the Midwest are

1 investing at five times the rate as their prior owners.
2 We want to reinforce that success. The proposed
3 rules would do just that.
4 The Commission has been working on transmission
5 pricing reform for nearly three years. I'm pleased that
6 we're taking this step today and bringing up this Order. I
7 do support the Order.
8 COMMISSIONER BROWNELL: I think you summarized it
9 quite nicely. Thank you for your hard work. It's been a
10 long three years.
11 I think Congress did a great job in many ways,
12 first recognizing the importance of infrastructure. I'm
13 particularly grateful for their recognition of the
14 importance of new technologies.
15 We are not only a fragile, sad, tired, grid, we
16 are a very old fashioned grid. Most importantly, I'm glad
17 Congress gave us a deadline.
18 (Laughter.)
19 COMMISSIONER BROWNELL: Because I think it might
20 have been another ten years.
21 I know that the team has kind of had it with all
22 of us on this, so I'm grateful.
23 I just want one clarification in the adder for
24 joining an independent transmission organization. That is
25 one that's defined by having operational control; is that

1 correct?
2 Do we not say that it's approved by the
3 Commission for the operation of transmission facilities as
4 an RTO or an ISO?
5 MR. HITCHINGS: That is the same as the RTO or an
6 ISO.
7 COMMISSIONER BROWNELL: I think that's an
8 important distinction, since we're seeing new models emerge.
9 There are two areas that I'm anxious to see comments on, in
10 addition to the new technology area.
11 One of the things in new technologies is, could
12 someone define wireless power transmission for me?
13 Christine did a lot of research for me, and she was not able
14 to get anyone who actually knew. It's a great thing, but
15 there's a lot of problems in siting.
16 I think we called for comments on whether we
17 should recognize levels of independence. I particularly
18 think that's important, because I think we've seen different
19 performance in truly independent transmission companies, and
20 I think that's a distinction we've also seen in other
21 countries.
22 I also have questions about performance-based
23 ratemaking. We've seen an enormous change in behaviors in,
24 for example, the UK, where there is very clear performance-
25 based goals with very positive effects in terms of reducing

1 congestion and down time and greater efficiencies, the kinds
2 of things we are really looking for. I think those are two
3 important areas.
4 One of the things that I think people forget in
5 rulemakings -- and I've heard some discussion of this
6 recently -- that when we move so fast, perhaps we don't give
7 enough guidance.
8 I think the point of a NOPR is so that the people
9 participating, can give us guidance, if there's something
10 we've neglected or if there are new ideas.
11 I would encourage people not to be limited,
12 necessarily, to the questions we ask, but certainly be
13 expansive in your responses. I think this, along with the
14 backstop siting, may help the logjam that has put us in such
15 a vulnerable position.
16 There is clearly a nexus between a strong
17 backbone transmission reliability, of security, and of
18 efficiency, and we need to start focusing on that from all
19 three aspects. Thanks for the patience, guys.
20 COMMISSIONER KELLY: I think one of the primary
21 reasons that we are able to agree on this transmission
22 policy is because it is a comprehensive policy. It's a big-
23 ten policy.
24 The focus is really on getting infrastructure
25 built. We recognize that there are different ways, but we

1 have addressed the needs in this policy statement, of all of
2 the players in this industry.
3 I think we've also addressed the issue of
4 regional planning, including in those areas that don't have
5 regional transmission organizations.
6 We've provided for incentives for regional
7 planning, in part, because we think that that's a better way
8 to get transmission built, if you have regional planning and
9 you involve all the stakeholders in the process.
10 So, I add to Nora and Joe's thanks to the Staff
11 for developing such a comprehensive policy.
12 I wanted to focus on three areas in the rule that
13 ask for comment, just to let you know that I think they are
14 important areas, and I hope that there will be a lot of
15 comment. Two of them have been mentioned by Nora.
16 As to transcos, in our policy statement, we've
17 broadly defined transcos, and I think that is a good thing.
18 We've probably defined them as stand-alone transmission
19 organizations, and we've seen differences in the industry
20 already, different types of transmission organizations --
21 some that are independent of investor-owned utilities, and
22 some that are not.
23 And we've seen good performance from both, so I
24 think it is a good policy to broadly define transcos.
25 But the other question comes in on return on

1 equity. Should a return on equity be pegged to the level of
2 independence? That's an important question for me, and I
3 hope that we get a lot of comment on that.
4 Also, as to the advanced technology section, I
5 think that it is quite possible that performance-based
6 ratemaking could play a role here, so we ask that question.
7 It seems as if we could benchmark the benefits
8 that advanced technology would give us and that with those
9 benchmarks, we could embark on a meaningful performance-
10 based ratemaking regime.
11 We haven't proposed any, but we've asked for your
12 comments. I'd be very interested in hearing about that.
13 Then, finally, we have a provision that would
14 require jurisdictional public utilities to provide
15 information annually on their current and projected
16 transmission investment activity. I liked your comment on
17 that.
18 I think that is a worthwhile request, and the
19 data will be very helpful for determining the effectiveness
20 of the proposed rules, and to provide the Commission and the
21 public with an accurate assessment of the state of the
22 industry.
23 With respect to transmission investment, that's
24 important, when we embark on a regime like this of providing
25 incentives, that we understand the effectiveness of the

1 incentives we provide.
2 Speaking of effectiveness, I think the big
3 question that remains is, will this new policy be effective
4 in getting transmission built? I think that it will have an
5 impact, however, I'd also like to point out that some of
6 these policies that we codify here, have been in place at
7 the Commission for awhile, particularly some of the ROE-
8 based and non-ROE-based incentives for non-transcos, yet we
9 have not seen significant investment in transmission.
10 The returns on equity have been adequate, 11
11 percent or so, which I think is a very good return on equity
12 for something with relatively little risk. However, we
13 haven't seen investment in transmission, which tells me that
14 some of the other reasons that we haven't had investment --
15 that there are other reasons that exist for not having had
16 investment, and I think that some of them probably have to
17 do with investor-owned utilities that have existing rate
18 caps and rate freezes and find it difficult to make an
19 additional investment where it cannot recover that
20 investment.
21 I think that we have seen, particularly in the
22 past, with the building of generation, that capital within
23 an investor-owned and integrated utility, competes for
24 generation and transmission, and we've also been told and
25 heard stories of utilities that own generation, that have

1 been unwilling to add more transmission, because it would
2 put their generation into unwanted competitive arenas.
3 So these areas cannot be handled, these problems
4 cannot be handled by FERC. They are problems that are at
5 the doorstep of the utilities themselves and of state
6 regulators.
7 We have seen utilities overcome those challenges
8 and state regulators respond with boldness. In Wisconsin
9 and Michigan, for example, we've seen the formation of
10 transcos.
11 We have seen utilities around the country,
12 particularly in the West, announce new transmission building
13 programs. Southern California Edison comes to mind,
14 recently, with its program to build more transmission in
15 California. God bless them, because we need more
16 transmission in California.
17 I think that we have done the best that we can in
18 the areas in which we have jurisdiction. I also look
19 forward to continuing our dialogue with the existing
20 transmission owners and with states, to see if the country
21 can't devise a more comprehensive approach to getting more
22 transmission built.
23 CHAIRMAN KELLIHER: Thank you. Shall we vote?
24 COMMISSIONER BROWNELL: Aye, and hallelujah.
25 COMMISSIONER KELLY: Aye.

1 CHAIRMAN KELLIHER: Aye. Thank you very much.
2 SECRETARY SALAS: Next for discussion, we will
3 take up three items jointly. These are E-22, Investigation
4 of Terms and Conditions of Public Utility Market-Based Rate
5 Authorizations; G-5, Amendments to Codes of Conduct for
6 Unbundled Sales Service and for Persons Holding Blanket
7 Marketing Certificates; and E-23, Informal Staff Advice on
8 Regulatory Requirements.
9 This is a joint presentation by Frank Karabestos
10 from the Office of General Counsel; Roger Morie from our
11 Office of Market Oversight and Investigations; Chris Wilson,
12 Ted Gerarden, and Mark Higgins.
13 MR. KARABESTOS: Good morning, Mr. Chairman and
14 Commissioners. I'm Frank Karabestos from the Office of
15 General Counsel, and with me today are Chris Wilson from the
16 Office of General Counsel and Roger Morie, Ted Gerarden, and
17 Mark Higgins of the office of Market Oversight and
18 Investigations.
19 In light of the Commission's proposed rulemaking
20 last month to implement Congress's new anti-manipulation
21 provisions, today we propose eliminating existing and
22 duplicative behavior rules.
23 Specifically Agenda Items E-22 and G-5 and E-23,
24 to be addressed by Roger Morie, are matters related to the
25 Commission's ongoing effort in connection with the

1 implementation of the Energy Policy Act of 2005 to provide
2 guidance and certainty to the industry on compliance
3 matters.
4 Last month, the Commission issued proposed rules
5 to implement the new prohibition on market manipulation in
6 the Federal Power Act and the Natural Gas Act.
7 In doing so, the Commission noted the overlap of
8 the new anti-manipulation rules, with the existing Market
9 Behavior Rules, and announced that it would consider
10 revision or repeal of the Market Behavior Rules in the near
11 future. Agenda Items E-22 and G-5 do so.
12 Item E-22 is an Order proposing repeal of the
13 Market Behavior Rules which are currently included in all
14 public utility sellers' market-based rate tariffs and
15 authorizations.
16 Item G-5 is a Notice of Proposed Rulemaking
17 proposing repeal of regulations similar to the Market
18 Behavior Rules applicable to pipelines that provide
19 unbundled natural gas sales service and holders of blanket
20 certificate authority that makes sale or resale of natural
21 gas in interstate commerce.
22 The central purpose of the Market Behavior Rules
23 and code of conduct regulations is to prohibit market
24 manipulation. In addition, the Market Behavior Rules and
25 codes of conduct both contain requirements on price index

1 reporting and record retention.
2 The Market Behavior Rules also require that
3 market-based rate sellers of electricity follow Commission-
4 approved rules in organized power markets, communicate
5 accurate and factual information, and not violate their
6 codes of conduct or the Commission's Standards of Conduct.
7 The Energy Policy Act of 2005 amended the Federal
8 Power Act and the Natural Gas Act by, among other things,
9 specifically prohibiting, quote, "Any manipulative or
10 deceptive device or contrivance," close quote, in connection
11 with the purchase or sale of natural gas, electric energy,
12 or transportation or transmission services subject to the
13 Commission's jurisdiction.
14 The rules proposed last month to implement this
15 authority, are broader, both in their scope and in the
16 entities covered, than the Market Behavior Rules and the
17 codes of conduct.
18 Accordingly, the Order and proposed rulemaking
19 before you today, propose to repeal the Market Behavior
20 Rules and codes of conduct, in light of the new anti-
21 manipulation regulations.
22 In addition, the Order and proposed rulemaking
23 propose that certain other requirements of the Market
24 Behavior Rules and codes of conduct be reflected in other
25 rules and regulations.

1 Thus, repeal of the Market Behavior Rules and
2 codes of conduct, will simplify and streamline the rules and
3 regulations that sellers must follow, and will not eliminate
4 beneficial rules governing market behavior.
5 It is also important to note that the Order and
6 proposed rulemaking propose to take these actions only after
7 all substantive requirements are reflected elsewhere in the
8 Commission's Rules and Regulations, so that there will be no
9 gap in the rules governing market participants' behavior.
10 Roger Morie will now address Agenda Item E-23.
11 MR. MORIE: Good morning. Agenda Item E-23 is an
12 interpretive order regarding the adoption by the Commission
13 of a no-action letter process.
14 The Commission here would clarify that Section
15 388.104(a) of the Commission's regulations can be used to
16 obtain written, informal Staff advice on whether Staff will
17 recommend that the Commission take no enforcement action
18 with respect to specific proposed transactions, practices,
19 matters, or situations that may raise issues under certain
20 of the Commission's statutes, rules, regulations, or Orders.
21 Initially, the topics for no-action letter advice
22 from Staff, would be limited to matters relating to the Part
23 358 Standards of Conduct for transmission providers, the
24 existing Market Behavior Rules for electric power and gas,
25 and when the final rule is effective, the new anti-

1 manipulation rules in Parts 47 and 159 of the Commission's
2 regulations.
3 As with the Policy Statement on Enforcement
4 issued last month, the Commission would fashion this program
5 by looking to the practices of the Securities and Exchange
6 Commission and the Commodities Futures Trading Commission,
7 both of which have successful no-action letter programs.
8 As is the case with these agencies, no-action
9 letter advice from the Commission Staff, would not be
10 binding on the Commission. While not binding, the draft
11 Order notes that a no-action letter would represent the
12 consensus view of Commission Staff, the same Staff that
13 would advise the Commission, if a matter were considered for
14 enforcement action.
15 Requests for no-action letters, initially, would
16 be submitted to the General Counsel on a non-public basis,
17 however, Staff experts from a number of Commission offices,
18 would be consulted, as appropriate, and, as noted, responses
19 to no-action request should be treated as a consensus view
20 of Commission Staff.
21 When the Staff responds to a no-action letter
22 request, the request and the Staff response would be
23 published in order to provide guidance to the industry.
24 Initially, there would be no fees associated with
25 no-action letters. Adoption of the no-action letter process

1 would be another step the Commission is taking to increase
2 certainty for entities subject to the Commission's Orders,
3 Rules and Regulations.
4 It would provide another avenue for market
5 participants to obtain informal and advance advice by Staff
6 on transactions or matters that otherwise could lead to
7 enforcement actions. Together with the Order and NOPR on
8 the Market Behavior Rules that the Commission is considering
9 today, the draft Order on the no-action letter process is
10 intended to continue to provide clarity and regulatory
11 certainty regarding the Commission's enforcement program.
12 I'll be happy to answer any questions.
13 CHAIRMAN KELLIHER: Thank you very much. Those
14 were two excellent presentations.
15 I think these Orders are very well drafted. I
16 really like them. I'm proud to vote for them.
17 Let me make a few comments on the package. First
18 of all, this is an enforcement package.
19 We had an enforcement package at our last meeting
20 and we have one today. Today, really,though this package is
21 oriented around regulatory certainty, providing greater
22 regulatory certainty to the regulated community.
23 Let me just explain a little bit about why and
24 how I think we accomplish that in these Orders: At our last
25 meeting, the Commission proposed rules to prevent

1 manipulation of wholesale power sales and jurisdictional gas
2 sales.
3 We plan to finalize those rules as soon as
4 practicable. As we move to finalize the anti-manipulation
5 rules, the electric and gas Market Behavior Rules remain in
6 place.
7 At our last meeting, we discussed the need to
8 consider changes in the Market Behavior Rules, in light of
9 the new anti-manipulation proposed rules.
10 We also talked about the significant differences
11 between the Market Behavior Rules and the new anti-
12 manipulation rules. On the electric side, there are
13 significant differences that are discussed in the Orders.
14 First of all, the universe of sellers that are
15 covered by the rules, varies between the Market Behavior
16 Rules and the new anti-manipulation rules.
17 Under the Market Behavior Rules, it's only public
18 utilities; under the new anti-manipulation rules, it's all
19 entities, including otherwise nonjurisdictional wholesale
20 power sellers.
21 There's also a difference in the scope of
22 transactions that are covered under the Market Behavior
23 Rules. Only market-based rate sales are covered. Under the
24 new anti-manipulation rules, all wholesale power sales are
25 covered, whether they are cost-based or market-based, and

1 also the intent standard is different.
2 It's clear that the Energy Policy Act didn't
3 reverse or repeal the Market Behavior Rules, but it's also
4 clear it didn't ratify them.
5 Congress knows how to ratify a regulatory policy
6 when it chooses to do so, and it didn't choose so here.
7 Instead, Congress specifically directed the Commission to
8 use a different regulatory model than the Market Behavior
9 Rules.
10 Now, it's plainly our discretion to reform or
11 repeal the Market Behavior Rules. I think it will really
12 end up being a merits call. I think the comments on the
13 proposed rules will be very important.
14 There are six Market Behavior Rules. If you look
15 at Market Behavior Rule 2, it's the heart of the Market
16 Behavior Rules that is clearly covered by the new anti-
17 manipulation rules.
18 Market Behavior Rule 3 bars false statements and
19 it also is covered by the new proposed anti-manipulation
20 rules that we issued last month.
21 The remaining four rules, most of the prohibited
22 behaviors are already barred by existing Commission rules
23 and the rest can be covered with changes in those rules.
24 I think there's value to regulatory certainty in
25 repealing the Market Behavior Rules, and when the anti-

1 manipulation rules are finalized, they would offer greater
2 regulatory certainty.
3 I think repealing Market Behavior Rules would not
4 come at a cost to customers. Having two sets of rules
5 barring the same behavior, does not offer more protection to
6 customers, and there would be no regulatory gap created.
7 So I look forward to the comments on E-22 and G-
8 5, but I think these Orders do offer greater regulatory
9 certainty to the regulated community.
10 On E-23, the no-action letter process, that also
11 provides a greater regulatory certainty by providing means
12 for the Commission to clarify any ambiguities in its rules.
13 Congress gave the Commission significant penalty
14 authority in the Energy Policy Act. This regulatory tool
15 will help the Commission discharge its historic duty to
16 prevent unjust and unreasonable rates and to prevent undue
17 discrimination and preference.
18 The Commission has been careful in the way it's
19 proposed to exercise this new penalty authority, as
20 reflected in the Enforcement Policy Statement that we
21 approved at the last meeting.
22 As Staff indicated, the Enforcement Policy
23 Statement is drawn from the experience of other agencies
24 such as the SEC, CFTC, and Justice Department.
25 The Commission's purpose is firm, but fair

1 enforcement of our rules and regulations, and I just want to
2 be clear that the Commission's goal is compliance.
3 We recognize that we have a duty to be clear in
4 what the rules are, that compliance should not be elusive,
5 it should not be subjective, it should be objective to the
6 greatest extent possible.
7 In a perfect world, the Commission is clear on
8 what the rules are and there's universal compliance. In a
9 less perfect world, the Commission is clear on what the
10 rules are, there's near universal compliance, and violations
11 are quickly identified and sanctioned.
12 I do recognize that in some instances, our rules
13 are not perfectly clear, that in such instances, we must
14 work with the industry and the regulated community to
15 resolve any ambiguities.
16 It's to that end that the Commission today
17 interprets its regulations to allow the regulated community
18 to obtain Staff no-action letters, effective immediately,
19 with respect to whether Staff will recommend that the
20 Commission take enforcement action with respect to certain
21 proposed transactions, practices, or situations that may
22 arise under the Commission's regulations relating to
23 Standards of Conduct, Market Behavior Rules, or the anti-
24 manipulation rules, when finalized.
25 As Staff indicated, this approach is modeled on

1 the no-action letter process used by the SEC and the CFTC.
2 The potential risks of failure to comply with the
3 Commission's requirements, increased significantly on August
4 8, 2005, with enactment of EPACT.
5 EPACT greatly expanded the Commission's civil
6 penalty authority. While we intend to exercise our expanded
7 enforcement authority diligently, we also intend to exercise
8 our new authority fairly, and our goal with the no-action
9 letter process, is to facilitate compliance and quickly
10 identify and sanction noncompliance, and greater clarity in
11 our rules is necessary to accomplish that goal.
12 So I support the package, and thanks for the
13 presentation. Colleagues?
14 COMMISSIONER BROWNELL: Thank you. As with many
15 of us who have lived and continue to some extent to live
16 through the imperfect world in which we found ourselves
17 during the California meltdown, the importance of rules that
18 ensure customer protection and assure compliance and that
19 are clear, I think, is critically important.
20 I think today's step, while we had made enormous
21 progress, represents a more mature response to our increased
22 enforcement responsibilities, and, indeed our
23 responsibilities of oversight and setting the parameters
24 under which markets can operate.
25 The challenges that we faced were to set those

1 clear rules. What we found ourselves doing -- and Sudeen
2 and I heard a lot about this at the meetings we held -- was
3 perhaps limiting market opportunities, making people fearful
4 of adding innovation to the market, drying up liquidity, all
5 of which, in fact, add value to customers.
6 I think both the rules and the no-action letter,
7 will help us move forward into that next stage. I'm
8 grateful to Cindy, who started this process with the OMOI
9 team after our Chicago meeting, and, for John Moot, it was
10 his trial by fire. I thank you for helping lead the effort
11 to put together this package.
12 I'm hoping that the industry, which was very
13 helpful in helping us refine our thoughts on this, will
14 respond to this in a way that's helpful, but, frankly, won't
15 lean on the no-action letter process in a way that's
16 inappropriate or suggest that people want us to do their
17 compliance work for them.
18 I think we are very open to responding to areas
19 where we are ambiguous, but for those who take advantage of
20 that process, I think maybe we will consider charging a fee.
21 I'd charge a fee today and Dan Larcamp would charge triple
22 the fee.
23 (Laughter.)
24 COMMISSIONER BROWNELL: I really hope we can work
25 this through, and certainly in the initial stages, perhaps

1 we'll have more requests, but we also have to focus on
2 getting the rules right.
3 If we get a ton of requests, it means perhaps
4 that the rules aren't right. That's something we need to
5 focus on, but I think this is a great step forward, and
6 really appreciate the efforts that people make.
7 It's hard to kind of look at your own processes
8 and say, maybe we could do better, but I'm a big believer in
9 continuous improvement, and I think that's what this
10 represents.
11 COMMISSIONER KELLY: I call this the Commission's
12 no-overlap and no-gap enforcement policy for preventing
13 electric and gas market manipulation.
14 I want to thank you all for doing such a good job
15 and bringing us this comprehensive policy. I'm very pleased
16 with the Orders.
17 I would like to focus on one of the questions
18 that we asked. That has to do with the scienter requirement
19 in the new anti-market-manipulation provisions passed by
20 Congress.
21 In the Federal Power Act, Congress used the
22 terms, "manipulative or deceptive device or contrivance,"
23 and directed that the Commission use the same meaning for
24 those terms as is used in Section 10(b) of the Securities
25 and Exchange Act.

1 Under the SEC Act, those terms have been
2 interpreted to require a showing of scienter, an intent that
3 is to deceive, manipulate, or defraud, or, in other words,
4 intentional or reckless conduct is proscribed.
5 This contrasts with our Market Behavior Rule 2,
6 which does not require a showing of scienter, because it
7 prohibits actions or transactions that foreseeably could
8 manipulate market prices, conditions, or rules.
9 And as Nora has alluded to, this foreseeability
10 requirement has caused a lot of controversy and uncertainty,
11 and particularly given our new enforcement authority, we
12 have been told that it chills investment and innovation in
13 the industry, and, clearly, that's not our intent.
14 So, what we propose in this rule is our
15 understanding that when Congress passed the anti-market
16 manipulation provision, it meant us to replace the Market
17 Behavior Rule 2, that does not have the scienter
18 requirement, with this rule.
19 But I would appreciate the public's response to
20 that interpretation.
21 Regarding E-23, I'm very pleased that we have
22 issued this. At the last open meeting, the Commission
23 pledged that it would create a no-action letter process, and
24 we have done that. I'd like to emphasize that our no-action
25 letter process will be completely Staff-driven, as it is at

1 the CFTC and the SEC, in that requests will be considered by
2 Staff experts in a number of our Offices here at the
3 Commission.
4 We are very fortunate to have such an
5 extraordinarily qualified Staff at the Commission, and I am
6 quite confident that this process will lead to very good
7 decisions and increased certainty for the regulated
8 community.
9 CHAIRMAN KELLIHER: Thank you. Before we vote, I
10 just wanted to credit my colleagues. We're doing this
11 today, really because Nora and Sudeen have, ever since they
12 came back from Chicago, been pushing for a no-action letter
13 process, and we're doing it for that reason, and also
14 because it's a good idea.
15 (Laughter.)
16 CHAIRMAN KELLIHER: Okay, shall we vote?
17 COMMISSIONER BROWNELL: Aye.
18 COMMISSIONER KELLY: Aye.
19 CHAIRMAN KELLIHER: Aye. Thank you very much.
20 SECRETARY SALAS: The final item for discussion
21 this morning is C-1, Expediting Infrastructure Construction
22 to Speed Hurricane Recovery. It is a presentation by
23 Jacqueline Holmes and Michael McGehee.
24 MS. HOLMES: Good morning, Mr. Chairman and
25 Commissioners. My name is Jacqueline Holmes from the Office

1 of General Counsel. Joining me at the table today is
2 Michael McGehee from the Office of Energy Projects.
3 C-1 is a draft Order in which the Commission is
4 acting to waive its regulations on a temporary basis to
5 raise the cost limitations for projects that natural gas
6 pipelines may construct without prior specific authorization
7 under their Part 157, Subpart F, blanket certificates.
8 As has been frequently noted, Hurricanes Katrina
9 and Rita crossed directly over major zones of natural gas
10 production, processing, and transportation in the Gulf Coast
11 region, causing significant damage to production platforms,
12 offshore pipelines, processing plants, and other facilities
13 in the area.
14 Loss of such infrastructure exacerbated an
15 already-tight natural gas market, and has the potential to
16 negatively affect both the price and supply of natural gas
17 during the upcoming Winter heating season.
18 The more natural gas that reaches the market, the
19 less price impact there will be for users of that gas.
20 The Commission's goal is to prevent -- is that
21 gas prevented by infrastructure damage from reaching the
22 market, not remain shut in, but, instead, be able to reach
23 the market through rerouting, reconstruction, or other
24 regulatory remedies.
25 The Commission has regulations and procedures in

1 place which allow the industry to take significant steps
2 toward recovery as soon as physically possible after the
3 storms had passed.
4 Under Section 2.55 of the Commission's
5 regulations, pipelines were able to replace physically
6 deteriorated facilities without coming to the Commission for
7 specific authorization, so long as the replacement
8 facilities are of substantially the same capacity and
9 located in the same right of way.
10 Under the emergency reconstruction provisions of
11 our regulations, pipelines are able to construct otherwise
12 eligible facilities under their blanket certificates, again,
13 without coming to the Commission for specific authorization,
14 to the extent the facilities are necessary to remedy certain
15 sudden losses of gas supply or capacity.
16 In addition, under Part 284, Subpart I of the
17 Commission's regulations, persons engaging in emergency
18 natural gas transactions, including the construction and
19 operation of necessary facilities, are exempt from the
20 certificate provisions of the Natural Gas Act, for a period
21 of up to 120 days.
22 Also, in September, the Commission waived the
23 120-day time limitation in the Discovery case, to allow gas
24 to be rerouted around a currently-non-functioning process
25 plant for up to a year.

1 The draft Order in C-1 represents another step by
2 the Commission to speed recovery from the hurricanes and
3 expedite the construction of infrastructure that may serve
4 to provide access to additional supplies of natural gas.
5 The Order increases by temporary waiver, the cost
6 of projects that can be constructed under the automatic
7 provisions of blanket certificates, from $8 million to $16
8 million, and under the prior notice provisions of the
9 blanket certificates, from $22 million to $50 million.
10 In addition, the Order expands the definition of
11 eligible facilities to include mainline facilities.
12 The increased dollar limits and expanded
13 eligibility definition will apply to any projects which
14 provide increased or alternative access to gas supply,
15 provided the facilities are constructed and placed into
16 service by October 31st, 2006.
17 We'll be glad to answer any questions you have
18 about the order.
19 CHAIRMAN KELLIHER: Thank you. Thanks for the
20 excellent summary; we appreciate that.
21 I just want to make a few comments. I mean, we
22 all know and we've talked about it for a number of meetings
23 now, that Hurricanes Katrina and Rita did a lot of damage to
24 our infrastructure.
25 We have 20 percent of our supply that comes from

1 the Gulf, and much of that has been shut in in recent weeks,
2 and that's contributing to high gas prices.
3 Our action today will speed recovery from the
4 hurricanes and help bring additional gas supplies to market,
5 just when consumers need it the most.
6 As Jacqueline just described, the Order
7 temporarily waives certain requirements to expedite the
8 construction of natural gas infrastructure and mitigates
9 supply disruptions. It increases cost caps; it expands the
10 definition of eligible facilities.
11 But these waivers are temporary, and anyone who
12 is trying to take advantage of them, has to have projects
13 constructed and placed in service by October of next year,
14 by Halloween of next year.
15 This action follows on the heels of other
16 Commission actions to authorize the most efficient use of
17 the gas infrastructure. We've approved a number of
18 emergency Orders authorizing more efficient use of our
19 existing infrastructure, and it really just shows that the
20 Commission is very focused on gas markets these days.
21 We are staying on top of prices, and we're also
22 doing what we can to help on infrastructure, so I think it's
23 a good Order and I look forward to voting for it.
24 Colleagues?
25 COMMISSIONER BROWNELL: I think it's a good

1 Order, too. You know, given the number of steps that we
2 have taken in response to the tragedies that we've seen from
3 these hurricanes, it would be interesting to track, for
4 example, under this Order, what actually gets built, so that
5 we're building a record for future Commissions to look at
6 tools that are available to them for responding in an
7 emergency.
8 Regulations are notorious for being too little,
9 too late to the game. I think we've tried not to do that,
10 but I'd love to know the impact here. I think that would be
11 helpful, both to us and to future Commissions.
12 CHAIRMAN KELLIHER: We can do that on a going-
13 forward basis. We'd be able to identify the facilities that
14 are built as a result of the waivers.
15 We also do know that some of the increase in
16 offshore production and some of the decrease in shut-ins, is
17 the result of our emergency Orders. Our emergency Orders
18 have allowed for increased gas to flow to market.
19 We can't take credit for all of it, but we can
20 take credit for some of that.
21 COMMISSIONER BROWNELL: And Mark has an
22 assignment. Thank you.
23 MR. ROBINSON: One of Susan's duties is to make
24 sure I know when I have an assignment.
25 (Laughter.)

1 COMMISSIONER KELLY: I think our presentation
2 earlier today, showed us that there continue to be concerns
3 about the hurricane-damaged production processing and
4 pipeline infrastructure in the Gulf, and the concern that
5 already-constricted, tight supplies, will be further
6 constricted.
7 I wanted to note, for example, that the New
8 England RTO has stated recently that it expects the New
9 England region to set a new record for wintertime peak
10 demand for electricity, even with normal weather conditions
11 this winter, and the gas is an important part of New
12 England's electricity supply.
13 So, I am pleased to vote for this temporary
14 waiver that could expedite pipeline construction to provide
15 access to additional supplies of gas this winter.
16 I think it's also important to emphasize that
17 with this waiver, the projects constructed will,
18 nevertheless, remain subject to the Commission's existing
19 environmental regulations and compliance provisions.
20 CHAIRMAN KELLIHER: Great. Shall we vote?
21 COMMISSIONER BROWNELL: Aye.
22 COMMISSIONER KELLY: Aye.
23 CHAIRMAN KELLIHER: Aye.
24 An other business?
25 (No response.)

1 COMMISSIONER BROWNELL: I think we ought to make
2 autographed copies of this available to certain policy
3 leaders in other parts of the world, and to anybody else who
4 wants one.
5 CHAIRMAN KELLIHER: Thank you. With that, this
6 meeting is adjourned.
7 (Whereupon, at 11:45 a.m., the open session was
8 concluded.)
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25