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UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Technical Conference

Conference on Competition in Wholesale Power Markets
AD07-7-000

Commission Hearing Room
Federal Energy Regulatory
Commission
888 First Street NE
Washington, DC

Tuesday, May 8, 2007

The Commission met, pursuant to notice, at 9 a.m.

- JOSEPH T. KELIHER, Chairman
- SUEDEEN G. KELLY, Commissioner
- PHILIP D. MOELLER, Commissioner
- MARC SPITZER, Commissioner
- JON WELLINGHOFF, Commissioner (via videoteleconference)

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

2 CHAIRMAN KELIHER: Good morning.

3 Don Wellinghoff is in Portland, and that means
4 it's 6:10 Portland. And if he's going to be there at 6:10,
5 we should probably be pretty punctual.6 Welcome to the second Technical Conference on
7 Enhancing Competition in Wholesale Power Markets. Today
8 we're going to concentrate discussion on the organized
9 market, rather than bilateral wholesale markets. We will
10 review in greater detail some of the challenges that were
11 identified at the February conference, namely the need for
12 more effective demand response, promotion of long term
13 contracts, and assuring accountability by regional
14 transmission organizations and independent system operators.15 Competition in wholesale power markets is
16 national policy, recently affirmed by the Energy Policy Act
17 of 2005. Our job at the Commission, at least in my view, is
18 to use our regulatory powers to promote effective
19 competition in both bilateral and organized wholesale power
20 markets. The Commission for many years has relied on both
21 regulation and competition to assure just and reasonable
22 power prices. The power industry is a dynamic industry, and
23 we are reacting to change by adjusting the mix between our
24 reliance on competition and regulation. We are searching
25 for the best possible mixture of the two.

1 Now the Commission has taken action to improve
2 the competitiveness of wholesale power markets in recent
3 months. Order 890 will improve access to the grid and
4 improve transmission planning. We've also established a
5 federal-state working group on competitive procurement,
6 chaired on our side by our colleague, Commissioner Marc
7 Spitzer. These steps should improve competition in the
8 bilateral wholesale power markets.

9 Now in my view as regulators we have a duty to
10 constantly consider regulatory reform. That's what we're
11 doing here today, considering possible reforms to FERC
12 policy that could improve competition in the organized power
13 markets.

14 I think this is an important conference. It can
15 help shape reforms that FERC may take to improve demand
16 response, promote long term contracts, and assure
17 accountability by RTOs and ISOs.

18 And as I have indicated before, I fully expect at
19 the end of this process the Commission will propose a number
20 of significant policy reforms. And for purposes of full
21 disclosure, I just want to inform the panelists that I will
22 listen most closely to those of you who propose concrete
23 solutions to the challenges we're examining, rather than
24 merely recite problems. And I look forward to hearing the
25 views of the panelists today, as well as my colleagues.

1 And I will recognize my colleagues; and let me
2 point out Jon Wellinghoff is joining us remotely from
3 Portland, I believe. Right, Jon?

4 COMMISSIONER WELLINGHOFF: That's correct,
5 Mr. Chairman. Thank you.

6 CHAIRMAN KELIHER: You get high marks for being
7 an early riser today.

8 Colleagues?

9 COMMISSIONER KELLY: I don't want to take too
10 much of our time. I know that we have a great panel here,
11 and I want them to have the opportunity to talk to us. I do
12 think that it's fitting that we have focused in on the three
13 issues that we're going to be talking about today; demand
14 side, long term contracting, and RTO and ISO responsiveness.

15 I just wanted to mention that as I went through
16 the panelists, I saw that this morning we have ISO New
17 England and we have MISO represented. But when it comes to
18 the panel at the end of the day on RTOs, I think in the
19 efforts to try and get everybody to the table, MISO and New
20 England RTO are not there.

21 So I just wanted to tell you two that when it
22 comes time for my questions, I might ask you a few questions
23 about generally, more generally about RTO and ISO
24 responsiveness, because I know that your RTOs have been very
25 responsive and I'd like you to have the opportunity to put

1 that on the record.

2 Thanks.

3 CHAIRMAN KELIHER: Commissioner Moeller?

4 COMMISSIONER MOELLER: Thank you, Mr. Chairman.

5 I want to thank the panelists on this panel and the other
6 two for making the significant effort to be here. We know
7 that it takes a lot. And I'm hoping today that, I may even
8 cede some of my time so that we have a little bit more
9 discussion amongst analysts; so I'll telegraph that ahead of
10 time, that I might encourage some of you to, if you have
11 thoughts, either concurring or challenging another
12 panelist's point, I may encourage that.

13 We have, arguably, three technical conferences
14 today. Three separate -- related, but separate important
15 subjects, and at least on the first my feelings have always
16 been if we get the market signals right and the pricing
17 signals right, we look at demand response not just showing
18 up, but showing up in new and creative ways that will
19 benefit consumers.

20 So I'll be eager to again hear from all the
21 panelists today, and thank you to the staff for putting a
22 significant effort in this long day.

23 CHAIRMAN KELIHER: Thank you.

24 Mr. Spitzer.

25 COMMISSIONER SPITZER: Thank you, Mr. Chairman.

1 I'd like to congratulate the Chairman and the staff; the
2 issues before us are certainly those at the forefront. The
3 challenge is, as Commissioner Moeller pointed out, is to get
4 some interaction among and between the panelists, and
5 further challenges; the three issues interrelate. Clearly
6 the third item, the responsiveness of the RTO - ISO is part
7 and parcel of issues 1 and 2, the long term contracts and
8 demand side response.

9 I'm interested in the interrelationship of the
10 three issues, and as my colleagues have said, the degree to
11 which proposals are made upon which we need to take action
12 to move forward, we'd be very appreciative. Thank you.

13 CHAIRMAN KELIHER: Thank you.

14 Let me recognize Commissioner Wellinghoff, in
15 Portland.

16 COMMISSIONER WELLINGHOFF: Thank you, Mr.
17 Chairman. I don't have a lengthy statement either; although
18 I would indicate that, as you said, Joe, I would be very
19 interested in concrete solutions and very interested in this
20 first panel with respect to demand response as well as all
21 the other panels; but I'm very interested in hearing what
22 those individuals have to say with respect to specific
23 solutions. Thank you.

24 CHAIRMAN KELIHER: At this point, why don't we
25 turn to the first panel.

1 Panel 1: THE HON. ROBERT LIEBERMAN, Commissioner, Illinois
2 Commerce Commission; GORDON van WELIE, President and CEO,
3 ISO New England; RICHARD DOYING, Vice President of Market
4 Operations, Midwest Independent Transmission System
5 Operator, Inc.; WILLIAM HOGAN, Raymond Plank Professor of
6 Global Energy Policy, Harvard University; DAVID MEADE,
7 Manager, Structured Power, Praxair, Inc., and Chairman
8 Technical Committee, ELCON; DAN SHARPLIN, Chairman and CEO,
9 Site Controls; JOHN ROSSI, Vice President of Business
10 Development, Enterprise Group, Comverge, Inc.

11

12 CHAIRMAN KELIHER: And let me apologize to our
13 first panelist. I understand you've changed your title
14 since you came East. I hope that doesn't hurt your
15 reputation back in Illinois.

16 MR. LIEBERMAN: I have to say to my boss, "I
17 didn't do that."

18 (Laughter)

19 Frankly, given what's happening in Illinois, I
20 don't want this job.

21 (Laughter)

22 CHAIRMAN KELIHER: Well, if it will help, we'll
23 ask you really tough questions.

24 MR. LIEBERMAN: Make me look bad.

25 CHAIRMAN KELIHER: Why don't we start with our

1 colleague, the Hon. Robert Lieberman, Commissioner, with the
2 Illinois Commerce Commission. Welcome.

3 CMNR LIEBERMAN: Good morning. Thank you very
4 much for inviting me today. I have to be clear that I'm
5 speaking only for myself today; I am neither speaking for
6 the Illinois Commission itself or for the Organization of
7 MISO States, of which I also a member.

8 I come to this after being a regulator for only
9 two years, and I want to say that before that, I ran the
10 Center for Neighborhood Technology, a not-for-profit in
11 Chicago, where we did community based demand response and
12 energy efficiency programs. So I have some sort of
13 practical experience.

14 One of the things that we did was we ran the
15 first real-time pricing for residential customers pilot in
16 the United States, which was markedly successful. And in
17 fact, so successful that the State of Illinois, or the
18 General Assembly recently passed a law saying that utilities
19 in Illinois had to offer residential real-time pricing to
20 all residential customers.

21 So I come at the whole question sort of from that
22 perspective. I think it's real useful that you've done the
23 -- that you're holding these conferences. I want to suggest
24 three things; I'm going to summarize my summary in order to
25 get to the questions quickly.

1 When I first got this job as regulator, I would
2 ask -- when I was sitting on that side of the bench, I
3 would say to the witnesses: Are the wholesale markets
4 competitive? And I would get answers like, "Well, they're
5 workably competitive, or They produce outcomes that are kind
6 of like the outcomes you would get in a competitive market."
7 It sounded a lot to me like what regulators used to say in
8 the old says about cost of service regulation. You know, we
9 replicate what would happen in a competitive market.

10 I think the problem really is that my question
11 was naive, because it has struck me, as I've sort of thought
12 about in it in the last two years, that we really need to
13 define this not as wholesale or retail, as if they were
14 somehow two separate pieces; we need to define it as supply
15 and demand. And when we think of it as supply and demand,
16 then the answer to the question: Are the wholesale markets
17 competitive? I think becomes -- well, unless customers
18 respond to prices, the benefits of that structure is somehow
19 lost. And without a price response to demand side, it's
20 not clear to me how we get to the benefits of a competitive
21 market that I think we're halfway into. The dilemma, of
22 course, is the next gap. I think that the problem is that
23 for the most part, customers don't see price elasticity.

24 And I'll take it a step further; words matter in
25 this role, and to the extent that we say things like the

1 wholesale markets are workably competitive, it really takes
2 the pressure off of my colleagues and myself to think about
3 how you link wholesale to retail, think about how supply and
4 demand is actually going to work.

5 And I think this is the crux of the problem. It
6 really reflects the complexity of the governance system that
7 we have in the United States for electricity markets. You
8 guys are responsible for the wholesale, the supply side, in
9 a sense; and my colleagues and I at the state levels are
10 responsible for the demand side. And while wholesale
11 competition, whatever that means, might be the policy of the
12 United States, if we don't somehow get the demand side to
13 engage, it's going to be difficult.

14 And I say that because today, if you look around
15 at state policymakers --

16 TIMEKEEPER: You have one minute.

17 CMNR LIEBERMAN: Oh, man.

18 (Laughter)

19 CHAIRMAN KELIHER: But also, we -- state
20 colleagues get courtesy. More courtesy than the other --

21 CMNR LIEBERMAN: I actually --

22 (Laughter)

23 I have a productive thing that you could do, I
24 think; but I've got to get to it; I'm sort of running up to
25 it here.

1 It's the governance problem we all recognize; how
2 we get around that, I don't know. I think one of the
3 problems is that one of the enormous successes of the
4 organized wholesale markets over the past decade has been,
5 and I think this is underutilized and underappreciated; is
6 the fact that I can now tell what the value of electricity
7 is at any given hour.

8 Now the problem is, and I can tell you from my
9 experience sort of before this job and with this job, that I
10 would say 99 percent of the customers think that the price
11 of electricity is -- first of all, if they think about the
12 price of electricity, they have no idea what it is. And
13 second, if you push them they say 'it's whatever I pay the
14 utility.' They have no idea that it varies, number one; and
15 number two, they have absolutely no idea that most hours out
16 of the day, it's far lower than the bundled retail price.
17 This is not well known.

18 And part of, I had the opportunity to testify at
19 Chairman Boucher's hearing a couple days ago with
20 Commissioner Wellinghoff and -- one of the impediments that
21 I mentioned to commissions investing in new technology was
22 that there's no demand. It's not like there are people
23 rising up saying "We want new meters." Or, "We want access
24 to market prices." I mean, "Bring it on." That doesn't
25 happen.

1 And part of the problem is that for all of the
2 transparency of these markets, for all of the transparency
3 of the wholesale market, people don't know that that exists,
4 they don't know what the opportunities are. And I would
5 say, half facetiously and half not, that I think one of the
6 best things that FERC or the RTOs or DOE or somebody could
7 do would be to buy time on the Weather Channel so that
8 everytime I checked my weather for Chicago, I saw the hourly
9 price.

10 Because sooner or later people are going to start
11 to say "Wait, that's not the same price that I'm paying.
12 Why can't I have that price? That's a lot cheaper." And I
13 think that there is an enormous education process that has
14 to occur. It hasn't happened. The problem is, in the
15 current market structure, broadly defined, it's in nobody's
16 particular interest to tell customers about those prices.
17 And I think that that's one of the remarkable successes. It
18 is underreported in an enormous way; and I think the first
19 and perhaps easiest step we could take to sort of get people
20 saying, "What's going on out there?" Is to make those
21 prices really transparent in a sort of push-demand way, in
22 contrast to the current sort of tacit --. Go to the web and
23 you can see it.

24 Thank you. I'm willing to take any questions.
25 Well, most any questions.

1 CHAIRMAN KELIHER: Thank you, Commissioner.

2 Before I proceed, I should have pointed out at
3 the beginning for people watching on the Internet the
4 structure of the day, the first panel focuses on demand
5 side, the second panel focuses on long term contracts, and
6 in the third we focus on accountability by responsiveness by
7 RTOs and ISOs.

8 And with that editorial comment, or
9 administrative comment, I now turn to Gordon van Welie,
10 President and CEO of ISO New England.

11 MR. VAN WELIE: Thank you. Good morning,
12 Commissioner. Thank you for inviting me to speak today on
13 the topic of demand response. I think New England is a
14 success story when it comes to developing demand response;
15 however, success didn't come overnight and it wasn't without
16 significant effort and significant cost.

17 Our experience demonstrates the value of
18 initiating and evolving demand response programs, but
19 ultimately we believe the objective is to fully integrate
20 these resources into the market, since this will ensure that
21 they compete on an equal footing with supply and will
22 improve overall market efficiency.

23 Since the ISO began operations, our demand
24 response capability has grown from approximately 100
25 megawatts to almost 1000 megawatts. And I think the key

1 drivers behind this growth are worth mentioning: the
2 establishment of a Demand Response department in 2002, the
3 implementation wholesale markets based on locational pricing
4 in 2003, a gap Request for Proposals to protect reliability
5 in Southwest Connecticut, and shortly thereafter, a winter
6 supplemental program after the January 2004 cold snap; and
7 then finally, the Forward Capacity Market transition
8 payments. All of these elements have helped build the
9 demand response programs.

10 This is an impressive expansion in a relatively
11 short period, and it illuminates the elements for success in
12 growing the demand side resource base. The first element is
13 the establishment of a robust wholesale electricity market
14 that sends locational price signals; and as you'll hear from
15 Professor Hogan, properly prices electricity under scarcity
16 conditions.

17 The second element is an unwavering commitment to
18 the integration of demand resources into the markets by the
19 FERC, the ISO, the state regulators and the industry
20 participants. And this includes the establishment of a
21 dedicated staff within the ISO.

22 The third element is that demand response
23 resources, like power plants, must be compensated for the
24 value that they provide to the market; and this leads back
25 to the first point. Like traditional supply resources,

1 demand response requires investors to recover their costs
2 and earn a return. Unlike traditional supply resources,
3 however, the value provided by demand response is for the
4 most part established by programs today and not by the
5 market. The challenge is to transition from programs to
6 direct participation in the markets so that the price and
7 the amount will be determined by the intersection of supply
8 and demand.

9 The New England region has little choice but to
10 fully exploit its demand response and energy efficiency
11 potential. Siting has become increasingly difficult; the
12 Regional Greenhouse Gas Initiative will limit carbon
13 emissions beginning in 2009; continuing concerns exist about
14 the heavy reliance on gas, natural gas for power generation,
15 and New England's peak demand grows significantly faster
16 than its overall consumption.

17 By the time of the FCM Settlement Agreement last
18 year, the region was ripe to take a major step forward to
19 further develop the demand side of the market.

20 Beyond appropriate compensation, the FCM market
21 design provides greater certainty for demand side resources
22 through its three year forward-looking planning process and
23 the five year commitment period.

24 Our early 'show of interest' for the first
25 auction has been robust with over 2400 megawatts of demand

1 resources, including energy efficiency, responding to the
2 upcoming FCM market. Yet disconnects between wholesale and
3 retail markets remain, and untapped potential from
4 naturally-occurring demand response persists. While load-
5 serving entities participate in the wholesale energy market
6 by bidding in the maximum price that they are willing to pay
7 for energy, the products purchased on behalf of the vast
8 majority of retail customers do not encourage such
9 participation, as Bob has just mentioned.

10 Short-term fixed price contracts serve most
11 residential and commercial customers. Injection of some
12 form of dynamic pricing into these contracts so that the
13 actual cost to produce electricity at different times of the
14 day or year will reach retail customers we believe is
15 necessary to realize this potential.

16 It sounds logical and easy, but barriers to
17 participation exist, including the need for more advanced
18 metering and billing systems, aligning the incentives for
19 distribution utilities, and the need for customer education
20 on these benefits.

21 Given the region's energy goals and pressures,
22 combined with the experience that has been developed through
23 demand-response programs and the evolution of our markets,
24 we are confident that the region is poised to further
25 increase the level of direct customer participation in the

1 markets.

2 We have prepared detailed answers to all your
3 questions, and we will submit those to you in writing, and I
4 look forward to answering any questions that you might have.
5 Thank you.

6 CHAIRMAN KELIHER: Thank you.

7 I now recognize Richard Doying, Vice President of
8 Market Operations, Midwest ISO. Welcome.

9 MR. DOYING: Thank you. To start, I want to say
10 we agree completely with Chairman Lieberman, that so far the
11 organized markets have solved half of the equation of
12 markets; and that is, you've got supply there and
13 represented well, we're missing demand. And we believe that
14 demand elasticity is in fact essential to well-functioning
15 markets.

16 And you get that when markets allow vigorous
17 participation by both buyers and sellers. Today it's
18 primarily the sellers that are there; demand has an
19 intermediary represented to them, and we'll have to deal
20 with the barriers that exist in that intermediary
21 relationship.

22 You also need low barriers to entry for
23 participation in the wholesale market, and again we have
24 that on the supply side; much less so on the demand side.
25 And finally, prices have to be transparent and accurate; and

1 accurate is a key -- and I'll focus on that as I get a
2 little further into my comments.

3 Currently the organized markets provide full
4 flexibility for Day-Ahead participation. That is, demand
5 can make a bid into the market, price-quantity pair, and
6 indicate how much they're willing to consume at different
7 price points. In real time they have much more limited
8 ability to participate. They have the ability to respond to
9 prices, so when prices are high and they think that they
10 might want to reduce their consumption, they're able to do
11 so. That exposes them to financial risks that are different
12 than the risks that are faced by generators who are also
13 participating in that real-time market.

14 Our current market does include several
15 mechanisms that allow demand to participate, and to
16 participate as flexibly as possible. We have well-defined
17 pricing nodes for settlement of demand, so as a demand who
18 is eligible to participate at the wholesale level, you can
19 indicate the discrete meter points at which you are
20 withdrawing energy, and we will give you a price; and we
21 talked about price signals being important; that reflects
22 the value at that exact location of consumption, not on a
23 broader, regional basis but at the meter point, for example,
24 associated with an industrial-commercial complex.

25 Second, demand response can count towards

1 satisfaction of capacity obligations -- and that's uniform
2 across the region, even though we have multiple reliability
3 organizations and standards.

4 Demand response may also serve as an emergency
5 resource and contributed, in fact, 3,000 megawatts during
6 the 2007 winter peak; so there's a considerable amount
7 that's out there today that can respond, again in a reactive
8 manner.

9 We're also moving towards full incorporation of
10 demand response into the regional transmission planning
11 process. Again, very important as we evaluate capacity
12 needs in the future that we adequately capture the benefit
13 that is out there for existing and potential demand programs
14 that may be developed.

15 We're also evaluating barriers that may inhibit
16 economic demand response; and that's something that we're
17 working very closely with the OMS states on. Chairman
18 Lieberman chairs an Organization of MISO States working
19 group that is evaluating those issues that is a corollary to
20 our Demand Response Task Force Stakeholder group, and we're
21 coordinating with them to identify such barriers.

22 And lastly, we're evaluating new mechanisms for
23 price responsive demand to fully participate in the real-
24 time. And fully participate in real-time has two elements;
25 one, able to receive that price signal, so they are

1 dispatchable in some manner; and two, eligible to set price.
2 And again, that's very important, because currently the
3 inability to set price in real time by most forms of demand
4 response actually has price moving in the wrong direction
5 when you've got true scarcity on the system.

6 Even with all of the market implementation
7 mechanisms in place to facilitate demand response, there are
8 significant barriers that exist to full, active demand
9 participation. The retail-wholesale regulatory structures
10 definitely influence the amount of demand that we see
11 participating in our market. The link between the wholesale
12 market platform with wholesale prices that are set based on
13 the intersection of supply and demand --this has been
14 discussed by the last two panelists -- and retail
15 ratemaking, which often has an average price calculated over
16 a long time period, mutes the signal that the end users
17 typically see.

18 Ultimately, end users are best situated to
19 identify their willingness to pay for the energy that
20 they're consuming at any given point in time.

21 Ratemaking treatment may also provide
22 disincentives to those who hold demand response today;
23 typically traditional utilities in our region, to fully
24 participate with that demand to the market. They don't see
25 the direct benefit of the value of demand response that they

1 have.

2 And lastly, market clearing prices, when the
3 value of demand is the highest, often do not reflect true
4 scarcity. We have some mechanisms under our tariff that
5 attempt to address that scarcity pricing, that we must
6 provide operator reserves to conserve energy. The new
7 ancillary service markets co-optimize energy and reserves
8 and loss scarcity of which is actually reflected in prices,
9 and that would be very helpful.

10 In terms of concrete steps that can be taken to
11 improve the situation, we will be making a filing very
12 shortly to remove some of the disincentives that I talked
13 about for demand participation in the real time market,
14 particularly penalties that they may face when they respond
15 to emergency conditions. We're also working with
16 stakeholders to develop alternative treatments to assure
17 that we fairly compensate demand response when it shows up
18 in the market.

19 And last, the additional market mechanisms, and
20 this is really territory that's not been well-charted in any
21 of the existing markets to allow demand response to
22 participate in real time, flexibly, setting price, unable to
23 respond to dispatch signals.

24 That concludes my remarks. Thank you.

25 CHAIRMAN KELIHER: Thank you very much.

1 I'd like to now recognize Dr. William Hogan, the
2 Raymond Plank Professor of Global Energy Policy, Harvard
3 University.

4 Welcome.

5 DR. HOGAN: Thank you, Mr. Chairman. It's a
6 privilege to be here, and I emphasize that I speak only on
7 behalf of myself and not anyone else.

8 I submitted written comments, which are available
9 to you; but let me try to summarize those briefly in the
10 time I have available. I've been asked to address the
11 demand side response question, but I tried to also in my
12 comments deal with some larger issues that are related to
13 that.

14 As I mentioned before, in previous of these
15 technical conferences, I think there's a major challenge for
16 the Commission in dealing with this problem I characterize
17 as the difference between little 'r' regulation and big 'R'
18 regulation; little 'r' being working to get the rules and
19 the market design right so that you have the incentive so
20 that people can do exactly what the previous panel is to
21 talk about and have supply and demand really interact with
22 each other; and big 'R' regulation, by that I mean mandates
23 at other kinds of programs where you decide on the outcomes
24 and you say "This is what we're going to do, and we're going
25 to make people pay for it."

1 Now sometimes that's necessary, and if it's
2 necessary then it should be done in a way that doesn't do
3 too much damage to the market, but the emphasis should be on
4 the little 'r' as we have discussed previously.

5 In order to do the little 'r' regulation you have
6 to have a framework, and we've talked about that before, and
7 I won't go back into it. But as a long name, bid-based-
8 security-constrained-economic-dispatch-with-locational-
9 prices-and-financial-transmission-rights. That's one word.

10 (Laughter)

11 And the framework we have talked about provides a
12 way to evaluate different alternatives and see what extent
13 they're going to meet the objectives.

14 And then we have a problem, and as the Chair
15 emphasized, we need concrete actions if we're going to deal
16 with the problem; and I want to emphasize an example of that
17 today to illustrate the more general point; and the problem
18 is found in demand side investment and also contracting and
19 infrastructure investment; and there are many different
20 elements of those problems, but a common feature is one you
21 heard about, which is this inadequate scarcity pricing; and
22 what is sometimes known as the missing money problem in the
23 energy markets. And that's a very large number, as it turns
24 out, unfortunately.

25 So it's a big issue and it leads to concerns that

1 people are not getting the right signals for demand side
2 participation by a lot, and leads to concerns that we need
3 to create resource adequacy programs and capacity mandates
4 and many other programs that are time-consuming and
5 expensive to put in place in order to change the outcome.

6 But what I would argue is that the little 'r'
7 solution to this problem is to focus on the scarcity pricing
8 and fix the market design to the best that we can in order
9 to make that work better.

10 And as I argue in the paper that I provided and
11 had described elsewhere, there is a very important step that
12 could be taken that is under the control, basically, of this
13 Commission. And that has to do with prices are actually
14 determined in these organized markets, and the focus is on
15 the operating reserve demand curve.

16 By this I mean something quite different and
17 distinct from the demand curves for installed capacity that
18 have been discussed so much as part of these resource
19 adequacy programs. I'm talking about representing something
20 that's the load of the next 30 minutes, not the next 30
21 years, or 30 months or whatever; but next 30 minutes in
22 operating conditions.

23 Now if you look at what has evolved from the
24 theoretical market designs into practical implementation,
25 there's a combination of practices and conceptual mistakes

1 in the implementation of the pricing methods, some of which
2 you've already heard about, which create these perverse
3 results that Richard mentioned, where during an emergency we
4 take action and prices go down. Well, wait a minute,
5 something's wrong, and why does that happen?

6 And I tried to explain why that happens, and then
7 to explain why there's a solution; which is to implement
8 operating reserve demand curves. And the paper goes through
9 some examples about how to do that, and in fact talks about,
10 a practical experience we're doing it, that's already been
11 placed in the New York system. So this is not a pie in the
12 sky idea; it is something that New England and MISO are
13 moving towards, but timidly, I would characterize it.

14 And the numbers turn out to be quite large. the
15 amount of money that's being ignored, and by not having the
16 operating reserve demand curve represented is the same order
17 of magnitude as the cost of generation, and prices are
18 probably there that are going to be required at the maximum
19 levels; or probably an order of magnitude larger than the
20 numbers of people here are talking about. And I go through
21 in the paper and explain why that's important and what to do
22 about it.

23 And what do about it is to get your priorities in
24 order. What I often hear in these conversations is "Well, we
25 can do the scarcity pricing after we fix everything else."

1 If we fix everything else using big 'R' regulations, I think
2 you're not going to need scarcity pricing because you're not
3 going to have a market. The priority should be to get the
4 market design fixed as fast as possible, and this is a
5 concrete step that FERC endorse and embrace and make the
6 ISOs and the RTOs put in place. And I strongly recommend
7 that.

8 CHAIRMAN KELIHER: Thank you, Dr. Hogan.

9 Right now I recognize David Meade, Manager of
10 Structured Power for Praxair, and Chairman of the Technical
11 Committee at ELCON.

12 MR. MEADE: Thank you, Mr. Chair, Commissioners.

13 Praxair is a large industrial gases producer.
14 Our manufacturing processes are very electricity-intensive,
15 and we're also a member of ELCON, which is a national group
16 of large electricity users.

17 The first thing I'd like to say is that ELCON is
18 not yet comfortable with the lifting of all price caps and
19 uninhibited scarcity pricing until the other elements of a
20 competitive market are in place. I wanted to mention that
21 before it slipped my mind.

22 (Laughter)

23 ELCON members represent hundreds of facilities
24 nationally; over \$10 billion of electricity spend. When it
25 comes the integration of demand response into markets, we've

1 had a wide diversity of experiences, and much opportunity
2 for improvements and for the lifting of barriers. I've
3 organized our thoughts on barriers into three areas:
4 Access, compensation, and uncertainties on access, demand
5 response. You'd have all the opportunities of generation to
6 provide energy capacity and auxiliary services.

7 In some places they can provide some of the
8 services but not all of them. In other areas, demand
9 response is hindered by other stakeholders, other market
10 participants, by the notion that a customer dropping load
11 should be compensated to the same degree as an unregulated
12 generator just results in excess compensation to a regulated
13 customer. So there's a lot of resistance from generators,
14 from utilities, even from regulators in different states.

15 Going to move on to the compensation. Barrier,
16 demand response should be encouraged and fairly compensated
17 for the significant reliability and economic -- (P/A system
18 malfunction.)

19 Cutting off the industrials already?

20 (Laughter)

21 Should be compensated for the significant
22 reliability and economic benefits that it brings.
23 Guaranteed minimum prices and event durations can be helpful
24 in motivating demand response, as those are constituted in
25 certain emergency procedures. There should not be

1 generation offsets for a demand response participation; a
2 customer choosing to un-consume energy should be compensated
3 to the same degree as a generator providing energy.

4 I'm going to move on to the uncertainties
5 barrier. Regulatory uncertainties are a disincentive to a
6 demand response participation. Industry restructuring has
7 been going on for over a decade. Nothing is settled, and
8 demand response is still a work in process. Corporate
9 energy managers have trouble fully buying into speculative
10 programs that may not be around with the next budget cycle.

11 There's also an uncertainty in some places with
12 regard to RTO demand participation being prohibited by state
13 rules. This is something that certain customers have had
14 to wrestle with.

15 Another uncertainty is the ability of local
16 utilities to have a say in whether the demand response of a
17 customer is allowable in the first place; and then if they
18 are trying to participate, if the demand response activity
19 was legitimate.

20 And you can try and address those in dispute
21 resolution procedures; but that can go on for months and
22 introduce more uncertainty, and a barrier.

23 There's been talk about half a market; it's been
24 mentioned already, and I concur; without demand response
25 you've got half a market and half a market is not a real

1 market. What should FERC do to promote demand response?

2 Direct the development of a full complement of
3 North American business standards and practices that would
4 facilitate the integration of demand response. This would
5 set standards for the products and services that could be
6 offered, that demand response could be provided, and how the
7 CBL determination would be, how settlements would go; you
8 would like these things to be as automatic as possible, you
9 want it to be simple for users to participate.

10 Secondly, integrate demand response into market
11 clearing price mechanisms. Incorporate business demand
12 response standards and practices directly into the RTO
13 market tariffs; this would assure permanency.

14 Require technology neutrality and eliminate any
15 bias toward generation and transmission to problems that
16 could be solved with demand response, too.

17 Direct NERC to eliminate any generation or any
18 biases toward generation or other solutions other than
19 demand response, be they intended or unintended, that may
20 exist in NERC standards. We want to eliminate the bias in
21 existing standards and in new standards moving forward. I
22 also encourage technology neutrality there.

23 Do not burden demand response with unnecessary
24 regulatory and administrative burdens. Remember that while
25 demand response can be very helpful to the competitive Day 2

1 markets, they also can be very valuable to regulated Day 1
2 markets also.

3 And finally, keep in mind that demand response is
4 one of several market issues that all need to be addressed
5 in tandem; ELCON identified seven issues for competition;
6 these were mentioned at the first conference on competition.
7 Demand response is one of those.

8 Thank you.

9 CHAIRMAN KELIHER: Thank you, Mr. Meade.

10 I'd like to now recognize Mr. Dan Sharplin, the
11 Chairman and CEO of Site Controls.

12 MR. SHARPLIN: Thank you. Thanks again for
13 having me.

14 By way of introduction, I'll just explain a
15 little bit about who we are and what we do, and then give
16 our perspective on these issues before us today.

17 Site Controls is a company that's now almost four
18 years old. We set out to aggregate the loads from the
19 midsize commercial buildings, focusing first on chain
20 stores. And so over the last three years we've aggregated
21 something approximating 2,000 sites across the country onto
22 our network; and today we're delivering automated near-
23 generation quality demand response.

24 The characteristics are it's automated, it's near
25 real-time, has a five minute response time, and it's

1 validated in real time.

2 We're focused on this hard-to-reach small
3 building market, and that accounts for about 25 percent of
4 the ISO fee. New technologies are creating material network
5 load opportunities with minimal customer inconvenience.

6 Now the reasons we focused in those markets. The
7 commercial segment; it's the largest and fastest-growing
8 market segment. The consumption occurs at coincident peak
9 periods. Commercial buildings are largely unmonitored and
10 uncontrolled, especially below 50,000 square feet.

11 And lastly, and I think this is the most
12 important one, is that the business rules and the nature of
13 these buildings allow us to grab large percentages of load
14 at very low consequence. So a little more content around
15 that.

16 Our average load is around 100 kilowatts, we're
17 able to dispatch between 20 and 60 percent of that. 20
18 percent without anyone noticing for three hours, 60 percent
19 in a deep dive situation for four hours, without putting the
20 customer out of business.

21 So that's who we are. I still remember
22 Commissioner Moeller's frustrations in our last session --
23 this was a few weeks ago around the grid watch time about
24 demand response that's been here for a long time, and we've
25 heard a lot of this before; what's different today? And

1 just my perspective, as an outsider coming in, coming more
2 from the technology side of the business, what we see is we
3 believe we see a tipping point that's occurring with the
4 convergence of several technologies, market and social
5 forces coming together.

6 When that happens, we think we're going to see
7 the rapid acceleration, not just in the home market, in the
8 large industrial market, but in all buildings. Some of the
9 things that are happening today that are work in progress,
10 that I think we need to keep our eyes on; one is increasing
11 transparency for all participants in the transaction.

12 One of the interesting things as I visit with
13 people on the supply side of the business, they really
14 understand this stuff until it gets to the meter. And they
15 don't understand that on the other side of that meter,
16 there's a customer with a similar set of conditions that
17 he's trying to making business judgments.

18 The other one is automated and predefined
19 response games. I can tell you that flashing a light or an
20 orb or anything else inside of a Michael's store at 2 in the
21 afternoon is not going to elicit any meaningful response you
22 can rely on. However, working with those customers over
23 time to predefine the schemes that will kick in at various
24 price levels, they'll sign up for that today and they'll let
25 us automate that. They're doing it.

1 Low or no cost two-way comps. We believe there's
2 not a lot of work to be done there; that's happening, it's
3 called the Internet. It's in all these buildings, it's in
4 most of the homes. We need to find a way to break down the
5 artificial barriers that keep us from accessing that.

6 Lastly to scale, this just takes a little time.
7 We're growing at about 100 percent a year; companies like
8 Comverge are growing at similar rates, Internoc, other ones,
9 as the intermediaries have come into this marketplace to
10 begin to make this market. The growth rate is accelerating,
11 the interest level is very, very high amongst our customers.

12 But market rules, especially with respect to size
13 of loads and metering get in the way. Barriers to entry,
14 especially our cost of market participation at the ISO level
15 get in the way. And finally, the lack of qualitative parity
16 between supply and demand response. Frankly, we think that
17 there's a lot of that that's justified; sometimes demand
18 response is per visual, it doesn't have to be, and the
19 technologies that are being deployed today and the business
20 models that are being deployed today are making it less so.

21 And I know I'm about to run out of time, but I
22 wanted to make one point quickly on the economics; and that
23 is, our view of the primary value for demand response is not
24 so much in grid reliability, not so much in scarcity, but in
25 the optionality that's created from the wide scale

1 deployment in the financial markets. And we think we'll see
2 that in the coming four or five years. Thank you very
3 much.

4 CHAIRMAN KELIHER: Thank you.

5 I now recognize John Rossi, Vice President of
6 Business Development, Enterprise Group, Comverge, Inc.

7 MR. ROSSI: Thank you, Mr. Chairman.

8 Comverge is a leading supplier of demand response
9 systems, and it's in that, from that perspective that I'm
10 going to respond today. The first part of my prepared
11 remarks were to set the stage that there are no markets
12 today currently adequate for Comverge to invest directly in
13 demand response hardware or systems. I think that point has
14 been well made, so I'll move to some other issues.

15 I'd like to point out that in states that procure
16 full services during an energy auction, it would be very
17 prudent for them to procure super peak from demand response
18 under long term contract prior to that auction, so that the
19 energy supplies won't price this super peak into their bids.

20 For demand response, long term contracts
21 translate to lower fixed prices which may not be true for
22 generation due to the fuel volatility.

23 Let me talk a little bit about the economics that
24 we deal with when we do a pay for performance contracts.
25 Our largest sector is the residential sector, where we

1 install and operate intelligent switches or thermostats that
2 respond to price signals, remote control signals, or both.

3 For direct load control, the devices are marketed
4 to end customers, and they participate on a voluntary basis.
5 In these contracts, we're paid for megawatts. Therefore, we
6 assume the risks of recruitment and retention of customers,
7 installation and maintenance of the program, and operation
8 of all the technology.

9 In addition, we have the capability of providing
10 state-of-the-art monitoring and verification that will allow
11 a real time estimate of the available megawatts, and verify
12 that shed when an event occurs. These programs entail a
13 small payment to customers for the participation; or in lieu
14 of payment, they can choose a programmable thermostat for
15 their control device. The added benefit of this thermostat
16 is that it's remotely programmable over the web.

17 We also operate in price-responsive areas where
18 the customer incentive is saving money by controlling load
19 during high priced periods. The equipment and the
20 infrastructure in this kind of program may be slightly
21 higher than the direct control program, but this cost can be
22 offset by the load shifting and conservation that occurs
23 with an automated system. We have extensive experience in
24 this price responsive arena through the nationally-
25 recognized Gulf Power - Critical Peak Pricing program; and

1 also Bob Lieberman's program in Illinois.

2 From this experience, I'd like to make a few
3 observations about some promising developments that we see
4 for demand response across the country. The first is the
5 Reliability Pricing Model market in eastern PJM. It seems
6 to offer prices in the area of \$72 per kilowatt-year, but
7 currently does not provide certainty beyond a one year
8 period.

9 These prices are potentially sufficient to
10 support our investment in demand response if the contract
11 were extended to say 10 or 15 years. The same level is not
12 sufficient to support a combustion turbine, which would
13 require around \$85 a kilowatt-year.

14 Another development that's of interest to us is
15 the Forward Capacity Market in New England. It has some
16 promising characteristics. It's potentially a multi-year
17 arrangement, and if the Forward Capacity Market clears at
18 the cost of new entry of \$7.50 a kilowatt-month, which would
19 translate for us to \$60 a kilowatt-year, and a five year
20 commitment, that may be sufficient for us to directly
21 provide the system to the market.

22 The real time market in Illinois is also very
23 promising; it offers cost savings and control to the end
24 customer, but it doesn't provide sufficient incentive for us
25 to invest in demand response. In fact, Comverge is using an

1 existing Con Ed load control program to cycle the air
2 conditioners when triggered by a market price selected by
3 the customer.

4 If this market price principle were applied to an
5 area where we have generation or transmission constraints,
6 and these constraints were reflected in the market price,
7 again investment by us might be practical.

8 The Ancillary Services concept is another
9 mechanism that could support development in demand response.
10 Our 90 megawatt program in Utah has been tested and accepted
11 by the WECC as a non-spinning reserve asset. Also, we've
12 been chosen for two 5 megawatt demand reserves pilot
13 programs in New England from a portion of our 60 megawatt
14 access. This pilot will demonstrate demand response
15 capability over a range of conditions this summer.

16 In conclusion, Converge believes that demand
17 response should be a vital part of the energy market of the
18 future. There are multiple mechanisms for enabling
19 participation, and if the true cost and values of demand
20 response are recognized in the market, private investment
21 will deliver this resource at no risk to customers.

22 CHAIRMAN KELIHER: Thank you, Mr. Rossi. And I
23 want to thank all the panelists.

24 I think we should probably turn to Commissioner
25 Wellinghoff first; he's the first chair of the federal-state

1 working group on demand response, and we can see him on the
2 TV, so if you can address yourself to him, but make sure you
3 lean forward to the mic; that would be helpful.

4 And I think why don't we go with 15-minute rounds
5 of questions, so let's start with Jon.

6 COMMISSIONER WELLINGHOFF: Thank you, Mr.
7 Chairman, I appreciate it. Can you all hear me okay?

8 CHAIRMAN KELIHER: Yes.

9 COMMISSIONER WELLINGHOFF: First question I have
10 is for Dr. Hogan. Good morning, Dr. Hogan.

11 DR. HOGAN: Good morning.

12 COMMISSIONER WELLINGHOFF: In your paper that you
13 submitted to the Commission under your concept of operating
14 reserve demand curve. Would demand resources and energy
15 efficiency be able to provide operating reserves under that
16 concept?

17 DR. HOGAN: Yes; you'd have to address all of
18 these questions that have already been raised about the
19 quality, and comparable quality and automation; but
20 certainly that's an important part of it. And the critical
21 feature is not so much allowing them to participate but
22 rather identifying what the value is of participating, and
23 that's the thing that's missing, because we don't have it
24 characterized in the operating reserve demand curve.

25 COMMISSIONER WELLINGHOFF: Well, and that's my

1 follow up. Would that then, if they participated, if demand
2 resources participated, would that change the construction
3 of the operating reserve demand curve?

4 DR. HOGAN: Well, the way I would think of it and
5 the way I would recommend implementing it, the answer would
6 be no; there would be an operating reserve demand curve.
7 And if you provided operating reserves and you were passed
8 all of the characteristics that the system operators require
9 for operating reserves, and you would be compensated for
10 your operating reserves, and if you consumed, and the energy
11 price in the market will be determined simultaneously in the
12 same way that Richard Doying described; so both operating
13 reserve and energy prices would be high during scarce
14 conditions; and demand would be charged for that, for the
15 demand that actually occurred; and the generators would be
16 paid that, correspondingly.

17 So the way to think about it would be to change
18 the amount of operating reserves you actually had.

19 COMMISSIONER WELLINGHOFF: Okay, thank you.

20 Following up in another area, Dr. Hogan, with
21 respect to scarcity. You're talking about implementing
22 scarcity pricing in wholesale markets, is that correct?

23 DR. HOGAN: That's correct.

24 COMMISSIONER WELLINGHOFF: Do you think it's wise
25 to implement scarcity pricing in wholesale markets until

1 retail customers have the ability to respond to prices?

2 DR. HOGAN: Well, the short answer is Yes; but
3 obviously it would be better, the better the design of the
4 retail markets, the better the wholesale markets work; the
5 more demand response we have in the system the better it
6 works; but that doesn't mean it's not a good idea to do it,
7 the scarcity pricing in anticipation of those responses, and
8 frankly, I think it catalyzed the kind of activities
9 everybody here is talking about.

10 We waited a long time, Commissioner, to get
11 demand response, and I think this would be a big help in
12 providing the stimulus.

13 COMMISSIONER WELLINGHOFF: Well, it certainly
14 could, but I guess what I'm worried about is potential for
15 delayed rate shocks to retail customers who don't have
16 immediate view of the scarcity prices in the wholesale
17 markets. Could that be a concern here?

18 DR. HOGAN: It certainly should not be dismissed
19 out of hand, but there is an important feature of this that
20 I would emphasize; is that in the organized markets, because
21 of the missing money problem that everybody is concerned
22 about, we've designed all these resource adequacy programs
23 and capacity programs and charges in various other ways, and
24 these costs are going to be passed through to customers.
25 And when they're calculated, they're netting out the energy

1 and scarcity payments in the well-designed programs.

2 So to a certain extent of what happens with the
3 operating reserve demand curves is it changes the timing,
4 and where you collect the funds, and it provides high prices
5 exactly when you need them most as opposed to averaging them
6 out over the year.

7 So it's not clear that the total cost to
8 customers go up; it may actually go down, if it works as
9 anticipated in these resource adequacy programs.

10 COMMISSIONER WELLINGHOFF: Thank you.

11 Bob Lieberman. Bob, I sensed that you were
12 asking us for some help with respect to moving some of your
13 colleagues in the states towards putting in place retail
14 pricing that customers could respond to.

15 Would you consider it to be helpful if FERC
16 determined that wholesale markets will not be truly
17 competitive until states allow consumers to respond to
18 prices?

19 CMNR LIEBERMAN: Good morning, and thank you for
20 getting up this early.

21 I would never say publicly that I'm asking for
22 help.

23 (Laughter)

24 I'm not sure I would frame it quite that way.

25 But I do think that there's been a confusion, and certainly

1 in the restructured states, there has been a distinction
2 made between wholesale and retail. And I don't think that
3 it's been clear that we need, that it's really supply and
4 demand. And I think it would be helpful if that confusion
5 was cleared up in terms of the debates that are going on at
6 the state policy levels.

7 COMMISSIONER WELLINGHOFF: Thank you, Bob.

8 My next question would be for the two demand
9 response providers on the panel. You've indicated some of
10 the barriers that -- actually, I guess there's three if we
11 consider the gentleman from Praxair as well -- but for all
12 demand response providers on the panel, you have articulated
13 some of the barriers regarding demand response. I just want
14 to know, if you feel that the market is providing you access
15 in the regions where you are currently doing business and
16 whether you feel that you're being compensated comparable to
17 generators for providing comparable services?

18 MR. ROSSI: I would answer that by saying that
19 we're not being compensated by the market, but we're being
20 compensated by intervening long term contracts generally
21 with a utility or an ISO. So we don't actually see the
22 market.

23 COMMISSIONER WELLINGHOFF: Okay. So you don't
24 work in the wholesale markets such as Mr. Sharplin does?

25 MR. ROSSI: No. We're in the retail market.

1 COMMISSIONER WELLINGHOFF: Mr. Sharplin, any
2 comment?

3 MR. SHARPLIN: In the areas where we're dealing
4 with organized markets, because of the transactional
5 friction and the market rules, we're moving to partner with
6 much larger players in those markets that had the
7 infrastructure in place in order to deal with the ISO
8 markets.

9 With respect to, do we think that -- that demand
10 response resources are compensated in parity with
11 generation, you know, I think the real question is which
12 generation? If you say, is it compensated like a new
13 natural gas peaker, the answer is no. And I think frankly
14 it's not even close in a lot of markets today, when we see
15 the way that the pricing schemes are set up.

16 That said, I think it's important for us to be
17 honest about whether demand response really is the same
18 product as a generation resource; it's getting close, it's
19 getting real close, and it has a lot of value. But I'm not
20 here saying that even our system, which I think is the
21 closest to it, I don't think ours can be a perfect
22 substitute for generation. That said, it has a lot of value
23 in the marketplace.

24 COMMISSIONER WELLINGHOFF: Mr. Sharplin, I have
25 another question for you. I want to follow up on your list

1 of some of the barriers, and one of the ones that you listed
2 was cost of participation at the RTO level. Could you
3 elaborate on that a little bit, what costs you incur, and
4 are there ways that you see that those costs could be
5 reduced for you?

6 MR. SHARPLIN: Sure. One of the primary ones,
7 and we spoke about this during grid week, are the metering
8 requirements. And a lot of our challenge is due to just
9 having meters that are acceptable to the RTO or ISO
10 deployed. We've gone so far as to deploy a meter downstream
11 on every building that we install in, and it costs about a
12 extra thousand dollars for us to do that.

13 The other cost had to do with market rules where
14 a lot of times our customers are excluded. If you're
15 talking about a dispatchable load below 100 kilowatts,
16 that's excluded from a lot of markets. Lastly, when we look
17 at the cost of playing in the market, with respect to
18 settlement and the working capital that one would tie up
19 there, those costs are material also. We think we're decent
20 negotiators with a fair amount of scale, so we'll be able to
21 sort that out with the intermediaries, hopefully. But those
22 are some of the costs that we deal with.

23 COMMISSIONER WELLINGHOFF: Thank you.

24 Mr. Chairman, I don't think I have any further
25 questions. Thank you.

1 CHAIRMAN KELIHER: Thank you, Jon.

2 Commissioner Spitzer?

3 COMMISSIONER SPITZER: Thank you, Mr. Chairman.

4 Mr. Meade, you talked about bias in the existing
5 to standards and referred to NAESB, and about the need for
6 technology neutrality. It seems to me we have a challenge
7 with regard to engineering standards, and I'll say that I
8 was the first lawyer in our family; we had a number of
9 engineers who were on occasion disparaging --

10 (Laughter)

11 -- maybe with good reason. But engineering is a
12 conservative profession, I would say.

13 To what degree is this challenge with bias a
14 consequence of a reasonable conservatism on the part of the
15 engineering community with regard to the commitment to
16 reliability? And if so, in your background, can you
17 identify a solution?

18 MR. MEADE: And my comments in that area are
19 partly based on the feedback from industrials as they try to
20 participate in certain demand response activities in certain
21 places with certain utilities basically being denied that
22 ability, with the reasoning that the NERC standards do not
23 allow for that.

24 As to why the standards may have this effect, I
25 really could only speculate. It may not even have been the

1 conscious intent to exclude demand response; I mean, perhaps
2 it just wasn't anticipated at the time these standards were
3 being put together, and the result is a product that turns
4 out to be biased against demand response and favoring other
5 solutions.

6 I'd like to think that the problem could be
7 remedied and that it's not an issue of needing to deny
8 demand response, the ability, out of any kind of
9 conservative concern; which implies that demand response is
10 not going to be able to deliver it as well, to which we
11 would fundamentally -- don't disagree with that.

12 COMMISSIONER SPITZER: No, I disagree as well;
13 and as I've been engaged in these proceedings, here and
14 elsewhere, and tried to eliminate the systemic structural
15 undervaluing of demand response as reliability being a
16 pretext, and try to drill down to the actual engineering
17 protocols; which is difficult for me, not being trained in
18 that area.

19 And it seemed to me I encountered a conservatism
20 -- maybe appropriate, so, that resulted in these engineering
21 protocols not giving demand response full value. I was
22 wondering if you had any experience in, or Mr. Sharplin or
23 Mr. Rossi on the other hand, in actually being able to
24 assuage these concerns.

25 MR. MEADE: Well, I'm going to follow up with our

1 technical experts in electrical engineering at ELCON to see
2 if there's any legitimate concern in that area.

3 MR. SHARPLIN: I like that answer. I'm going to
4 hand this off to our man Hickman, and we'll send in a note.

5 MR. ROSSI: Well, I'll hazard an opinion.

6 I think that in many instances, the tendency is
7 to try and treat demand exactly the same as generation, and
8 hence to put in the same time response requirements and
9 accuracy requirements and so forth, on demand. And in some
10 cases it's perfectly appropriate, and easily doable. In
11 others it's onerous and unnecessary, because you can get an
12 adequate level of certainty in the demand reductions by the
13 metering that my colleague puts on a commercial building; or
14 by the sampling that we do on a residential program. It may
15 not be exactly equivalent, but it certainly is adequate.

16 COMMISSIONER SPITZER: I had one response that
17 was somewhat illuminating, which was that traditional
18 generation solutions was viewed as input. And as long as
19 the reliability community, whether it be NERC, NAESB,
20 whatever, were focused on inputs, demand response would be
21 challenged. However, if the scope of the analytical
22 reasoning was broadened to include outlooks, that's where --

23

24 MR. MEADE: Yes.

25 MR. SHARPLIN: I think it's important for -- I

1 think there's a consensus that there are gaps between demand
2 response and generation with respect to quality. There are
3 also gaps the other direction, that as we look out and the
4 technologies are being employed today, and they are being
5 developed and are getting up to scale today, is there's a
6 lot of ways where demand response is superior to generation
7 as a resource.

8 Those include, obviously, mobility; the ability
9 to target demand response around particular areas of
10 congestion or in response to outages and those types of
11 things, especially if you've got a distributed model where
12 you're not dealing with large points but a bunch of
13 aggregated smaller points.

14 Zero emissions. I think that's an enormous
15 benefit, especially as we're looking towards a carbon-
16 constrained economy. The idea that you can geographically
17 disburse this in such a fashion so it doesn't have a lot of
18 the negative effects on the grid from either large load
19 sources or large demand sources that turn on and off.

20 So I want to make sure that I'm clear on those
21 things; that while we talk about, it's not generation; it's
22 not as good in some ways to the grid operator, it's better
23 in some other ways. And that's the thing that's missed in a
24 lot of these conversations.

25 MR. ROSSI: I guess the other advantage would be

1 that it's an incremental resource, so it starts and builds
2 gradually rather than either being not there or there, as
3 with generation.

4 COMMISSIONER SPITZER: It seems, at first, there
5 are several positives. Yet you've got this conundrum.

6 Mr. Meade, you also brought up the issue of
7 certainty; and we hear a lot about regulatory certainty,
8 what not. In the uncertainty that the entities that you're
9 familiar with, the industrial class are challenged by, to
10 what degree is the certainty policy or economic in nature?
11 Obviously, regulatory bodies, Congress can deal with policy;
12 much more problematic dealing with economic issues.

13 MR. MEADE: Well, I think it's a combination of
14 factors. You know, where demand response resources may be
15 denied effective access to RTO opportunities, like what's
16 going on in the state. I think that some of the bias
17 against that kind of participation is coming from entities
18 that have economic interest in trying to prevent that
19 participation or make it difficult, so they'll rely on the
20 policy implications of the regulatory tariffs and policy in
21 the state, and try and use those. Basically, you know, it's
22 prohibited by the regulations in the state or state law.

23 COMMISSIONER SPITZER: You mean referring to
24 state retail?

25 MR. MEADE: Yes. So basically, I think it's a

1 combination of factors that are causing that kind of
2 problem; and where utilities have a say as to whether demand
3 response is -- should be allowed in the first place, where a
4 customer is trying to do that, or whether a demand response
5 event or performance was legitimate; and in some cases the
6 utility will say "Oh, well, you know, you were going to be
7 down anyway." And may not have any real basis for making
8 that kind of claim.

9 Once again, like having economic motivation to do
10 that, but the RTO policies are like allowing them, you know,
11 to. So I think it's a combination of economic and policy;
12 and so maybe there is room for addressing the policy part of
13 it, as you suggested.

14 COMMISSIONER SPITZER: Just to point out, and
15 this issue is more salient and obvious in the long term
16 contract panel, but to the degree to which there's
17 volatility and lack of predictability in commodity prices
18 globally, that's a problem in delineating value in demand
19 response. You can't price the product, because of the
20 commodity, and that's an economy issue.

21 MR. MEADE: Economic uncertainty; you've got good
22 markets. You can deal with that with forward contracts,
23 with operational-type strategies, with contingency planning.

24 There seems to be a big difference between economic
25 uncertainty and policy uncertainties, in our view. One is

1 observed in your comments in Congress and this morning a
2 silver lining, which is the communication. I have to tell
3 you, though -- I used to bring my charts with me. To retail
4 meetings, to the Kiwanis Club and the Lions Club, and
5 explain the value, the environmental value and the economic
6 value of demand response; and I would have some positive
7 response.

8 From the tech community I hear, "Price is
9 indifferent to us. Do you understand the value of one hour
10 offline in our chip manufacturing process?"

11 And I would also hear from other folks, "We're
12 busy people, and this is not on my agenda of issues to deal
13 with. So Commissioner, it's all very nice, but go away."

14 Again, the optimist in me would like to think
15 communication is the answer, but how would you -- being on
16 the front line yourself, evaluate my optimism?

17 CMNR LIEBERMAN: It's hard to know. I mean, we
18 haven't done it.

19 COMMISSIONER SPITZER: It hasn't been given a
20 fair chance.

21 CMNR LIEBERMAN: It hasn't been given a fair
22 chance. I mean, I think, in my personal experience, the way
23 we sold the real-time pricing project for residential
24 customers in Illinois was to look at the price shapes in the
25 wholesale market and the hourly issues they had, the day-

1 ahead price shifts, show them to legislators.

2 And say, "If you look at the average of the
3 bundle because the hourlies, people would have come out
4 ahead if they did nothing. And they saved significantly
5 more money if they reduce their demand." And what we found
6 that people were -- A, people had no idea that was the case;
7 they had no idea that 98 percent of the time in Northern
8 Illinois market or the Southern Illinois market that the
9 prices were significantly low, and the average of the
10 hourlies were always below, even with our 20 percent rate
11 cut --not a good idea, acknowledged-- ten year rate freeze
12 not a good idea.

13 But even at that rate freeze, the prices were
14 significantly below that; and I think the expectation is a
15 lot of that, because the cost of insurance is going to be --
16 I mean, the cost of insuring the same price for 8760 is
17 going to be higher than the average of the hourlies. And
18 the question is, how high is it and is it worth people
19 taking on in some way the self-insurance, and is it possible
20 to do?

21 I think that if people understood that dynamic
22 they would say "Well, there are lower prices out there, and
23 why don't I have access to them?" "There are lower prices
24 out there, why can't I engage with one of the technology
25 vendors to help me manage that?"

1 I just think we haven't explained that. It's
2 really in nobody's interest in the current market structure
3 to do that; and if we were to do it, I think you would get
4 significant -- given my experience, that you would get
5 significant advantages.

6 COMMISSIONER SPITZER: It's a challenging
7 environment to deal with those explanations, as well as
8 dealing with the cost.

9 CMNR LIEBERMAN: Agree.

10 COMMISSIONER SPITZER: Mr. Chairman, thank you.

11 CHAIRMAN KELIHER: Commissioner Moeller?

12 COMMISSIONER MOELLER: Thank you, Mr. Chairman.
13 I'm just stick with Commissioner Lieberman.

14 Thanks for being here. I wonder if you had a
15 chance to read Professor Hogan's paper?

16 CMNR LIEBERMAN: Unfortunately, I did not. I
17 wish I had. In my life, if there were no last minute,
18 nothing would get done.

19 (Laughter)

20 I intend to read it, but I --

21 COMMISSIONER MOELLER: Well, I'll be curious,
22 your reaction.

23 CMNR LIEBERMAN: I'll be happy to provide it.

24 I will say that in terms of scarcity pricing, let
25 me just address the point we were making earlier.

1 Without the demand response, I think in the midst
2 of this rate shock thing that's going on in Illinois right
3 now, I can't say I'm real sympathetic. On the other hand,
4 we don't really see those. So if a tree falls in the forest
5 and no one sees it, does it make any noise?

6 And I think that the dilemma that we have is, as
7 long as we -- on the retail side, have these long term fixed
8 price contracts with a significant, what I call an insurance
9 premium, to cover the variability, prices can be high for a
10 little while and we would never see it, and I'm not sure how
11 we would respond.

12 The dilemma is, we want customers to respond. I
13 mean, that's the point of scarcity pricing. And so the
14 breakdown, really, in the model is that -- and this really
15 goes to Commissioner Wellinghoff's question: It's always,
16 'it would be extraordinarily helpful for FERC to say, "You
17 want really competitive markets, we've got to have demand
18 side response. Without that, it's not competitive." I
19 should have been much stronger in my response there.

20 But you have a spontaneity problem, and until
21 there's some sense of 'we're willing to be exposed to that
22 because we believe the tools to manage it are worthwhile'
23 it's hard to think how that's going to happen. I guess that
24 part of my education is that those issues haven't been
25 raised; how the technology would benefit customers. I just

1 don't think people understand it, and until that happens
2 we're going to have this conversation over and over again.

3 COMMISSIONER MOELLER: Well, I enjoyed your point
4 about the fact that, simply stated but elegantly, that there
5 is a differing value to electricity throughout the day; and
6 as you said, consumers rarely appreciate it or are even
7 cognizant of it.

8 Curious your reaction to Mr. Rossi's suggestion
9 of an auction for super peak.

10 CMNR LIEBERMAN: I have to be careful here
11 because we have a docket --

12 COMMISSIONER MOELLER: I understand. And I don't
13 want to put you in a --

14 CMNR LIEBERMAN: In a conceptual way, obviously
15 if we could reduce the volatility of our demand, then the
16 suppliers would have less risk, and that insurance premium
17 would be lower. And we had talked often in Illinois, if we
18 had a million households with a site plan, air conditioner,
19 and we said to the suppliers, "At \$200, we're turning these
20 guys on." It essentially brings us 500 megawatts of peak.
21 It's equivalent to a peak, or caps the risk.

22 We're not there yet. Personally, I think it's a
23 great idea, but we're not there yet.

24 COMMISSIONER MOELLER: Professor Hogan, thanks
25 for the paper. I hope we can promote it; and I don't know

1 if it's for sale or what, but I found it fascinating,
2 interesting, and because we were all limited on time, I
3 thought you might want to elaborate a little bit more on
4 some of your thoughts in the paper.

5 DR. HOGAN: Well, I think the principle thought
6 to emphasize is that in every conversation about this that I
7 have ever seen until recently, when I got involved in this,
8 everyone agreed in principle that scarcity pricing was
9 inadequate; but since it was politically infeasible to do
10 anything about it, they didn't look at what it would
11 actually mean to do it.

12 And I was involved in conversations, including in
13 particular with Monsour and his group at the Cal ISO where
14 we suspended this belief for a moment and we said "Okay,
15 let's think this through, what would it look like?" And the
16 result is a series of papers that are referenced in the
17 notes that I sent you.

18 And it turned out that it was a little different
19 than we anticipated; and the numbers were actually quite
20 large. I was actually quite surprised at how large they
21 turned out to be when you thought it through. When I said
22 timid, I didn't mean that the MISO -- the people were timid
23 personally; but what I was referring to was, "We're going to
24 get up so that we've got reserve prices of a thousand
25 dollars and things are really dire."

1 But under those circumstances, the analysis that
2 we went through said you should be thinking more like
3 \$10,000. And if you look at the implicit prices that are
4 embedded in the Forward Capacity Market in New England,
5 \$200,000 or more per megawatt is embedded in those inputs
6 hidden in a way that you can't actually see it.

7 So I think there's a huge disconnect between what
8 we're actually doing in the marketplace and other kinds of
9 programs that are being developed and that we're putting in
10 place, and that are actually reinforcing the problem in some
11 sense; because they move it away from the marketplace as
12 opposed to putting the cost back in.

13 So I think it's critically important to do, as I
14 have said for long time, to fix the market design at every
15 opportunity, and do that first, and do the other things that
16 you can't do any other way second.

17 And then I went through in the paper a list of
18 issues that come up: Is it practical to implement? Yes.
19 New York ISO has already done it. Does it make the market
20 power problem worse? No, it actually helps. And that's a
21 very important feature because it provides a clear way to
22 distinguish between economic withholding, where people in
23 Texas and Australia they say "Well, we'll let you bid a big
24 number so that we can get the prices up."

25 And you say "So we're going to authorize the

1 exercise of market power in the interest of getting better
2 scarcity pricing." And then you have "Why would we want to
3 do that?" But if you have the operating reserve demand
4 curve, you don't have to do that, so you keep the caps that
5 you've got, and you can distinguish between withholding and
6 true scarcity, and it simplifies that problem a lot.

7 I already mentioned the issue about increasing
8 cost. I think it will catalyze demand, and it addresses a
9 lot of other problems; it makes everything else with these
10 resource adequacy infrastructure investments easier.
11 Doesn't eliminate everything else, and it's clearly under
12 FERC's control. This is something that by emphasizing that
13 priority and then approving the plans that come through, you
14 can ask the system operators themselves about this, but I
15 think you would find a favorable response, if that was
16 something that they could do and put in place, because it
17 helps them a lot.

18 If you think back to the question about the
19 conservative engineers -- let me say a good word for
20 engineers -- I think the standards are conservative and they
21 are appropriately conservative; because they were developed
22 in a context where we weren't giving people the right
23 economic signals, and they had a very strong economic signal
24 to do things which were bad, and would hamper reliability.

25 One of the most important things that happened

1 when we put LNP in place in dispatching energy, was we
2 aligned a lot of these signals for people in the actual
3 dispatch; and there's been plenty of evidence and testimony
4 from system operators that this made running the system a
5 lot easier, because people had their incentives aligned.
6 And I think the same thing would happen here in terms of the
7 operating reserves and everything else.

8 So if we don't price it, I want the engineers to
9 be overly conservative, thank you very much. And I don't
10 particularly want to change what they do; at least in the
11 first instance. What I want to do, and this is another part
12 discussed in the paper, is to price what they did; so when
13 they take actions to reduce voltage or interrupt customers
14 or any of the other things that actually get done because
15 they're running out of operating reserves, we don't tell
16 them "don't do that"; they know their business better than
17 we do. What we says is "When you do that, we're going to
18 incorporate it into the prices so that the signal gets
19 through to the marketplace"; and the mechanism for doing
20 that is through this operating reserve demand curve.

21 COMMISSIONER MOELLER: Well, that leads well into
22 my next question which is, the reaction to your paper by
23 Richard and Gordon. If you've had a chance to read it,
24 otherwise respond to the Professor's testimony.

25 MR. VAN WELIE: I scanned it on my Blackberry.

1 So if you know about a Blackberry and a long paper, they
2 don't go well together. But I saw the elements of it. I've
3 got a few comments.

4 I initially agree with what Professor Hogan said.
5 I think there is something that's with -- from the
6 discussion, though, I think the full capacity market has
7 been touted as innovative, and more often what we are
8 referring to are these five categories to divide resources
9 that are able to fit into the auction on an equal footing
10 with supply.

11 But I think there's another innovative element
12 that's worth considering in the context of this last
13 discussion, which is the issue around scarcity pricing.
14 What the full capacity market does is it provides -- it's
15 been designed to provide a natural hedge for load up to the
16 point of the capacity requirement. Now, let me just get a
17 little technical for a moment.

18 The capacity requirement is a probabilistic
19 calculation that looks on average, it's probabilistic on
20 average; how much capacity do you need, given the
21 distribution of availabilities and so forth in the
22 generation side; and it comes up with a number.

23 Well, I can tell you the number is approximately
24 75, it's about a 75 percent load profile. So if we look at
25 the ISO when you're doing market capacity analysis, we look

1 at what's 50-50 and we look at what's 90-10. 90-10 is
2 typically, has a 10 percent probability of occurring, and it
3 equates roughly to a heat wave, or 95 degrees across New
4 England for about three days.

5 So actually what New England is doing when it
6 buys capacity, it's buying less than what it's going to need
7 on that very hot day. So if you have to deal with, from a
8 systems operation point of view, you have to deal with that.
9 So I'll make the linkage in a moment.

10 Full capacity markets, what it does is it
11 essentially hedges load up to the historic capacity
12 requirement, at a price of roughly \$200 to \$250. By
13 essentially subtracting any energy market revenues on any
14 capacity market revenues against energy market revenues.
15 So it deals with the market power issue by removing
16 incentive for generators to play with prices.

17 But I think there's another interesting
18 opportunity. I think at the moment you've got a good cap of
19 a thousand dollars. Given the fact that we now have a
20 safety net, we can walk a tightrope with a safety net; you
21 can actually start increasing the energy, the bid caps over
22 time, to actually start creating those very high pricing, in
23 this case the conditions, and I think a couple of things
24 will happen.

25 First of all, when we're in that heat wave

1 situation, we are going to be needing more than one report.
2 And so what you may be doing is sending a very strong
3 signal for a limited amount of resources, which I think will
4 apply equally to supply and demand. But I think it starts
5 getting at the scarcity price issues that Professor Hogan
6 mentioned.

7 And I think you're also attracting demand
8 resources that haven't taken on a capacity obligation as
9 well. So I think there's a possibility there over time to
10 involve the strike price, where it's at the moment, and the
11 price caps that are in the market. The other thing you've
12 also got, is we recognize within our market design the
13 reliability issues, a number of different things:

14 There are different qualities and performance to
15 demand side resources. So for example we have an auction
16 for essentially purchasing operating reserves for a reserve
17 market. And guess what? It's clearing at around \$14 per
18 kilowatt-month. And you can math over a year, that's
19 whatever it is; \$1670 a kilowatt-year, which is a good
20 amount of money, and it's possible and probably better than
21 what you would need for a combined, for a gas-fired peak
22 load.

23 So the point I'm making here is that for those
24 resources we need within 30 minutes, within 10 minutes, and
25 we hang a premium price on them. And I think the issue,

1 when we talk about demand resources and the need for
2 protecting reliability, I think what the New York standards
3 are trying to get at is to make sure that we maintain
4 security of the system. They're not really dictating what
5 resources you have to use; but they can expect the operator
6 to maintain the security of the system.

7 I think it comes down to two things again: One
8 is, are the markets providing enough value through the
9 various market signals that are out there to pay for the
10 investment in the resources, and certain resources will
11 require more investment. And then the second thing is, will
12 the system operators be able to rely on those resources at
13 the right time. You've got to engineer that, too, to make
14 that so.

15 COMMISSIONER MOELLER: Okay. Richard?

16 MR. DOYING: I did have a chance to review
17 Professor Hogan's paper. It was very consistent with
18 discussions that we had in the past, and our internal
19 position on where the markets need to go.

20 It's funny that we, and unfortunately we've got
21 this term, scarcity pricing, I think it raises fear in many
22 people. It sounds like something that must be bad, it's
23 volatile, it's expensive. We find ourselves asking this
24 question: Is scarcity pricing a good idea?

25 It's really a more fundamental question that

1 we're asking, and that is: Are the markets sending the
2 prices? And the answer is clearly No. In most hours they
3 in fact do, and as Bill said, to the benefit of rival
4 operations, that dispatch signal during the majority of
5 hours, is exactly the right price signal sent, the right
6 incentive for generators to respond and for demand to
7 respond to the extent that they are interested in doing so
8 and available?

9 The problem with the current market designs is
10 that when supply is tight, when supply is scarce, prices
11 aren't in fact accurate; they don't reflect the value of
12 incremental generation or decremental demand, reductions of
13 demand. And that's why you call it scarcity pricing,
14 because it's addressing that known flaw in the current
15 market designs; and that is inaccurate price signals at the
16 margin.

17 And the good news is, we know what accurate
18 means; it has a definition. It means that it reflects the
19 value of energy being consumed or produced in the short
20 term, and in the long term it provides appropriate
21 incentives for efficient additions for both generation and
22 transmission and demand response resources.

23 That's good because we know what we're trying to
24 get to; and scarcity pricing through operating reserving
25 pricing is one mechanism to get us there. Another important

1 mechanism is providing more opportunities for demand
2 response to get into the market on very flexible times, so
3 they have the same ability to contribute to that short-term
4 supply balance as generation does, and they also receive the
5 same financial incentive to develop more of the resource and
6 bring it to the market.

7 So I think we agree with the paper; we don't
8 necessarily agree with the price level that you have to get
9 to in order to achieve appropriate price signals, as a
10 \$10,000. It should be tied to the value of loss mode or
11 some similar concept. I think that's something that we will
12 evolve towards over time, as all of us gain experience with
13 how these markets operate, up in that rarefied part of the
14 supply curve.

15 COMMISSIONER MOELLER: And moving forward,
16 working with the group that Commissioner Lieberman is
17 chairing; timing on those, timing on getting the
18 recommendations on real-time participation, lack of
19 penalties, the other item on fair compensation; we're going
20 to hear something from you this fall?

21 MR. DOYING: Actually, something as soon as next
22 week. It's several steps. Actually some of it you've
23 already heard about, so I won't detail the ancillary service
24 market incorporates some of the co-optimization of reserves
25 that's before the Commission.

1 In terms of removing some of the disincentive or
2 penalties for demand response in real time, that will be
3 filed, hopefully for approval and implementation by this
4 summer. Fair compensation for demand response that shows
5 up, we're working that through our demand response task
6 force; they had a vote on that just yesterday that said,
7 "There are a lot of questions here. Let's take our time and
8 make sure that we answer all the questions fully." And so
9 that will be unlikely to be filed prior to this summer, so
10 that may well be a summer or fall filing.

11 In terms of additional mechanisms that will be
12 developed, our plan was to have some of those ready for
13 filing later this year; and in part that will depend on the
14 speed with which our stakeholder process and the parallel
15 organization operates.

16 COMMISSIONER MOELLER: We'll look forward to the
17 time, Mr. Doying.

18 CHAIRMAN KELIHER: Thank you.

19 Commissioner Kelly?

20 COMMISSIONER KELLY: Thank you, Joe.

21 I thank you for the testimony that you gave and
22 the colloquy that's gone on so far today. That has given me
23 three take-aways, that I'll take away from this panel, and
24 I'd like to share them with you and get your comments.

25 First, it seems to me that it's not a question

1 right now of whether we are going to integrate demand
2 response into our organized markets. The question is, how
3 are we going to and when are we going to? I say that
4 there's not a question about whether, because I hear from
5 Bob and from Gordon that the consumers are demanding, and
6 it's something that they want; there is a demand, if you
7 will, for demand response.

8 And I hear from David and Dan and Jon that the
9 producers of demand response are ready to sell it. And as
10 Dan mentioned, the technologies are the tipping point, and
11 not only do they want to do it, but the technology has
12 evolved to the point where a lot of demand response can be
13 aggregated and can be sold, if you will, close to a utility-
14 grade commodity.

15 And I also hear from John that even on a
16 residential level, the technologies have advanced to the
17 point where we're ready to enable consumers to be able to
18 respond at the residential level.

19 So it seems to me that then the question for FERC
20 is, when do we start on this effort? And how do we do it?
21 And of course -- and that leads me to point two.

22 It seems that we should do it now. I haven't
23 heard any objections to that. If you have any objections to
24 that, I'd like to know. If you think there's any reason
25 that FERC should delay in an initiative to move our

1 organized markets into more demand response. And how do we
2 do it?

3 One thing that I think was overlooked in our
4 first panel was that, if we have here ISO New England, and
5 I've looked at the demand response market summary that our
6 staff has put together; and ISO New England has done it, at
7 least at a first cut, and more than a first cut. When you
8 look at the market elements that are potentially part of
9 demand response, ISO New England has demand response
10 participating in every one of those market elements;
11 emergency situation demand response program; real-time
12 demand response bids; day-ahead demand response bidding into
13 the market, capacity market demand response participation,
14 demand response and long term transmission planning, and bid
15 price floor cap for demand response.

16 Also, in the ancillary services markets, ISO New
17 England has demand response participating in the non-
18 spinning market and the long term supplemental market. I
19 also know that you have a docket before us to more fully
20 integrate demand response into capacity market, and I know
21 from having visited your Board and the New England States
22 meeting not too long ago, they also have an initiative going
23 on at the same time to better implement demand response into
24 the Forward Capacity Market, recognizing that initially the
25 Forward Capacity Market is looking at an annual product and

1 that demand response doesn't necessarily fit that mold too
2 easily. So what can you do to broaden your market?

3 So it seems to me that we have at least a model
4 of how to do it, and it's a starting point. So that also
5 leads me to conclude that there's no reason not to start
6 now, because we have a model that we can implement in other
7 organized markets and perhaps improve.

8 And as an aside, I wanted to talk about RTO
9 accountability. There is, in our last panel as I mentioned,
10 we were talking about, let's see: Enhancing the
11 responsiveness of RTOs and ISOs. And what I've observed
12 with ISO New England and their participation in the demand
13 response market is that they approached their job of running
14 a market very broadly; and they went to their customers and
15 said "What do you want from us?" And the customers said "We
16 want lower prices."

17 And instead of just saying "Well, we're going to
18 make sure our market runs efficiently to ensure that the
19 lowest costs are out there and get translated to you," they
20 actually said "Our job is to get you lower prices." And you
21 said to them, "Your high prices are significantly because
22 you buy a lot of electricity on peak, and we're going to
23 work to lower the peak and lower your price." And the way
24 to do that is to put demand side in the market, and you've
25 seen quite a bit of success.

1 So I wanted to just make that statement about,
2 and congratulate you on your broader vision of looking at
3 how RTOs can serve the customers.

4 Then the third point, it seems that what FERC's
5 jurisdiction is being the middleman. You have the people
6 who demand demand response, and yet the people who produce
7 demand response -- and we're in charge of the marketplace.
8 And that's our biggest job and our primary job. So it seems
9 to me that that's the next thing we do, is we look at how
10 these markets are organized and what the rules are; and it
11 also seems from this colloquy that the best way for us to
12 determine what rules are appropriate is to do in the future
13 exactly what we're doing today; and that is, getting the
14 producers here who can tell us what kind of rules you need
15 in order to get your product into the market.

16 And it's been very helpful to hear you speak so
17 broadly about the nature of your product and how it gets
18 deployed, and what you need in the market in order for it to
19 get deployed. Including talking about the technical details
20 of the product and the commercial arrangements that you need
21 to have in place in order to be able to bring your product
22 to market; and I think it's important that our market rules
23 reflect those realities and accommodate them if not
24 incentivize them.

25 So my next question is, how do we do that?

1 What's the best way? What's the best forum going forward to
2 continue this discussion and to get your expertise on the
3 record? Is it more technical conferences like this? Is it
4 a rulemaking? It is an RTO stakeholder process? Although I
5 understand that that can present a lot of cost. And not
6 that there shouldn't ultimately be some sort of stakeholder
7 process, but what's the next step for moving this forward?

8 So those are my broad questions; and rather than
9 direct them to anybody in particular, if any of you have a
10 comment or a response to some of those questions.

11 Bob?

12 CMNR LIEBERMAN: Yes, let me just say a couple
13 things. I think you may be just a tad more optimistic than
14 I am. I think, while there is potentially significant
15 demand, if people knew what the value was and understood
16 that it was easy to do, I think the first step is more price
17 transparency. I hate to keep harking on that, but I do
18 think that without a demand revealed, in a sense, that
19 hasn't yet quite revealed itself, I think it is going to be
20 more difficult to get retail and wholesale aligned; and I
21 think that's part of the critical variable here, and I
22 appreciate Commissioner Spitzer's concern about that, but it
23 seems to me that unless you tell what the price is -- I
24 can't guarantee that telling people what the prices are will
25 produce the appropriate response, but I can guarantee that

1 if you don't tell them what the prices are, you won't get
2 the appropriate response. That's my first point.

3 Second point is that, let me make a pitch here
4 for hourly pricing, because I think that hourly pricing
5 reflects an opportunity to get the same set of benefits with
6 less than 2.2 billion lines of code somewhere in a software
7 package.

8 Much of what we're talking about is how do we
9 sell demand response into a market; and that assumes that
10 you've got a particular rate structure at the retail side,
11 which is basically flat, where somebody's providing the
12 hedge, and you have to be compensated through the
13 marketplace.

14 In hourly pricing, where you're not taking the
15 hedge, effectively, the technology providers could be
16 engaged to provide the insurance, all the technology would
17 be the insurance against the high prices, and you would be
18 left simply consuming the low prices, and with all due
19 respect, you guys would have to figure out how to forecast a
20 price system and build it into your market. But it would
21 make the whole thing much simpler.

22 So when we talk about demand response, demand
23 response I think reflects a particular sense of how the
24 retail side is hedged; and the world gets very different, it
25 seems to me, in terms of how you get to do this, if you

1 think about more of a -- where there's less of a hedge for
2 people and more exposed to those prices.

3 COMMISSIONER KELLY: Well, I agree with you that
4 price transparency is important; and I think that what would
5 be helpful for us to discuss, but maybe this is not the time
6 right here given our time limitations, is the differences
7 between the retail market and the wholesale market. Because
8 we do need to have them working together, and you have
9 primary responsibility for the retail market and its
10 regulation and its rules, and we do for the wholesale
11 market.

12 And my sense is that the price transparency at
13 the wholesale market, which is our jurisdiction, is not as
14 troublesome as it is at the retail market. In other words,
15 I think ours is an easier nut to crack than yours, given
16 where we are on the transparency curve.

17 CMNR LIEBERMAN: I agree, and I think that if
18 there were a way to make it more, transparent beyond the
19 sort of aficionados in the stakeholder groups -- no more
20 stakeholder groups. Help me, no stakeholder groups.

21 (Laughter)

22 COMMISSIONER KELLY: It has its advantages and
23 disadvantages.

24 CMNR LIEBERMAN: I would be happy to have that
25 conversation.

1 COMMISSIONER KELLY: Gordon?

2 MR. VAN WELIE: Thank you for the very nice
3 comments, Commissioner Kelly. I would say in terms of what
4 to do next, I think you've said it yourself; you have
5 jurisdiction of the wholesale markets. You can move forward
6 with ensuring that function -- you're not saying that each
7 ISO has to implement exactly what we've done, because there
8 are other good ideas out there.

9 Functionally, the elements that you mentioned all
10 ought to be incorporated in all the wholesale markets
11 throughout the country, so that's something you have direct
12 jurisdiction over.

13 I think the collaborative that you've got going
14 with NAESB is a very important step, because you've put your
15 finger on it once again, the other element of this is how do
16 we integrate what's happening at the retail and wholesale
17 markets; and there are real problems out there; people are
18 nervous about showing that price volatility.

19 Now one thing that we've been doing recently that
20 may be instructive is that we've been pursuing what we call
21 the scenario analysis initiative, we've been doing that for
22 the last eight months. And when this arose was the concerns
23 expressed by policymaker, by customers in New England to
24 rising electricity prices.

25 And so one of the things we need to do is show

1 people where we are coming from. And we've projected
2 forward that by 2020 we'll need another 8,000 megawatts of
3 resources, to continue to grow at the rate it has been over
4 the past several years.

5 And so then the question becomes one of "Well,
6 how do you actually meet that demand in 2020? What's the
7 resource like you want to use?" And then you start asking
8 yourself the question, what are the economic reliability and
9 the environmental indications of the resource choices?

10 And we're coming to the end of this first phase
11 of this, and we'll be publishing it soon; but the results
12 are very interesting. When you look at, we've done
13 production cost runs, we've done analysis on what the
14 various emissions are of these different resource types,
15 very interesting. I think what that starts doing is it
16 starts getting policymakers aware of what the implications
17 of these resource choices are, so that they can get
18 comfortable that energy efficiency and DR, et cetera, is a
19 highly valuable resource, more than just from a price
20 perspective, so that they can take the next step in saying,
21 this gets the pricing to the customers, because it's good
22 for everyone.

23 COMMISSIONER KELLY: So it sounds to me like what
24 you're saying, and I am familiar with the scenario analysis,
25 because I met with the states in New England who are using

1 it; and they found it exceedingly helpful.

2 But I think what you're saying is that the
3 scenario analysis approach is a real -- it serves two
4 purposes. One, it will help to educate retail consumers
5 about the value of demand response, which in turn will
6 increase their acceptance of it in the marketplace; and two,
7 the knowledge that you get from being able to play those
8 games and run those scenarios is, helps you with the
9 development of the market itself.

10 MR. VAN WELIE: Well, I think the retail
11 consumers for the most part probably are not paying a lot of
12 attention to this; they've got -- they don't worry about
13 some arcane, wholesale market.

14 So I think the issue is, how do you get the state
15 regulators to get comfortable with changing the rate advice,
16 and how do they see this now as a policy imperative, because
17 they're the ones acting on behalf of those customers,
18 because the ultimate goal is to try and have electricity
19 prices as low as they can be, to have efficient markets, and
20 to the extent that it makes sense, to hedge against some of
21 the volatility that's out there.

22 So it's targeted really at policy makers and
23 industry participants with the hope that the region will
24 converge around a few choices, which we then can embrace and
25 say, "Let's take on the job of educating the customers as to

1 why this is necessary."

2 I think if you're going to get there first,
3 you've got to capture the first crowd or you're never going
4 to get through the next one.

5 COMMISSIONER KELLY: Good point.

6 Have you seen that, Bob? Have you seen the
7 scenario analysis yet?

8 CMNR LIEBERMAN: No, but I'm kind of familiar
9 with it; MISO did a series of runs for us in terms of what,
10 if we had a fixed demand, a fixed growth demand, what
11 resource, the adequacy issues would be over the next few
12 years and what the savings would be. And they're
13 significant. I mean, a very small reduction in the rate of
14 growth in demand produces -- it's a static analysis, it's
15 not a dynamic analysis, but it produces billions and
16 billions of savings present value. Literally a reduction
17 in their forecast for quarter percent growth, when you roll
18 it back, produces dramatic savings.

19 The question is sort of how you operationalize
20 that, and how you get those. Sort of, whether it's
21 efficiency or price response, and it's how do you build that
22 in, then.

23 COMMISSIONER KELLY: Thanks.

24 David?

25 MR. MEADE: Part of the challenge is that

1 customer entries have is as important as energy management
2 and procurement are to our businesses; it's not our core
3 businesses. We don't have unlimited resources and time for
4 participating in every NERC or NAESB or stakeholder
5 proceeding that may be going on. I mean, we can't even come
6 close to covering that.

7 So to answer your original question, to the
8 extent that good policies, good standards, good practices
9 could be done, instituted by a rulemaking and what not, in a
10 way that makes it more practical for customer interest to
11 get satisfactory solution; we'd be all for that, and if that
12 means borrowing upon aspects of the ISO New England program
13 and the best aspects of the other areas, and refining those;
14 but we're trying to keep this manageable from a customer
15 participate standpoint, too.

16 COMMISSIONER KELLY: Thank you.

17 Richard?

18 MR. DOYING: Thank you, Commissioner.

19 To amplify a little bit what Gordon said, I think
20 we do need to pay a lot of attention to that regulatory
21 alignment between the wholesale side and the MISO side, and
22 I really see that as one of the fundamental impediments to
23 getting more demand to the market.

24 We can think of lots of ways for demand to
25 participate, but there is very little demand that's able to

1 participate. Most of the demand response programs are out
2 there today with the regulated utilities, we are developing
3 a very different regulatory environment, and they're not
4 readily adaptable to the new markets that have evolved.
5 They are not dispatchable, able to respond to a price signal
6 for the most part, have limitations on how often they can be
7 called; there are lots of reasons why they don't offer the
8 flexibility that's necessary in order to extract the value
9 of them for the benefit of the folks that worry about demand
10 response.

11 It's not clear what the right answer is, and I
12 don't think it's only a change at the state level to change
13 the way the ratemaking works there. In some cases, it may
14 be modifying the existing program so that they can
15 participate more flexibly in the market, and that could be a
16 relatively easy fix, it can be pursued in the short term.
17 But longer term it is the end use consumer that's best able
18 to evaluate consumption decisions.

19 And that price transparency, the incidence and
20 the cost has to be expressed at that level if the market's
21 really going to work.

22 COMMISSIONER KELLY: I was actually surprised to
23 hear Dan say that in some states the individual consumer is
24 -- I think this is what you said -- prohibited from selling
25 in to the demand market.

1 Is that correct? Did I hear that correctly?

2 MR. SHARPLIN: The market mechanisms don't exist;
3 and it's not uncommon in some parts of the country for there
4 to be a 200 kilowatt or 100 kilowatt threshold that's
5 dispatchable. So for us that means, in the extreme example,
6 that would be a 200 kilowatt store. That excludes 30
7 percent of the coincident peak.

8 COMMISSIONER KELLY: So when you go to aggregate
9 load, what you're telling me is that load is not legally
10 available to be aggregated?

11 MR. SHARPLIN: In some cases no, and in some
12 cases yes. In some cases, whether you -- what we see is the
13 IOUs, especially in California, are emerging with a
14 disaggregation model that works very well for us, and that's
15 our view of the world is to be aggregated for a whole bunch
16 of reasons and not just because it's easier to monetize in
17 the markets.

18 In New England ISO specifically they have a
19 program where they've gone out and are trying to capture
20 these smaller loads and bring those into the market. I
21 think they call it Five program today. But certainly it's
22 working there.

23 But generally speaking, at the ISO level, our
24 loads for the most part, you know, don't qualify, meter by
25 meter, or in an aggregated fashion.

1 COMMISSIONER KELLY: Okay. Sorry, sure.

2 CHAIRMAN KELIHER: Okay, Bill, do you have a
3 short --answer?

4 DR. HOGAN: In response to Commissioner Kelly's
5 question about not only what to do, but what to do first, I
6 emphasize that if you don't get the scarcity pricing right,
7 then the design of the programs that you would want for
8 demand side response would be dramatically different, as
9 illustrated by the fact that historically you won't have a
10 different mechanism because of demand side programs which
11 are not appropriate for the new market.

12 So I think it's absolutely critical to get the
13 scarcity pricing right first, so that everybody know about
14 it, and they're thinking that through when they're designing
15 these programs.

16 COMMISSIONER KELLY: Thank you.

17 CHAIRMAN KELIHER: Thank you. And Phil, did you
18 have a question?

19 COMMISSIONER MOELLER: Very quickly to Dan, we
20 don't have time to talk about what you do; but metering can
21 be a barrier to entry, what are the key things we should be
22 following in terms of that issue? Is it open architecture,
23 is it security, what is it?

24 MR. SHARPLIN: I think it's more open
25 architecture; and there's a move -- our infrastructure needs

1 to know what's happening at the moment. There's two ways
2 for us to do that. One is for our device to punch through
3 the firewall, go out to a service where an AMI feed is in
4 place and pull that back down; the other one is to read the
5 meter directly.

6 And we're more than happy to put in our meter,
7 you know, which is certified to 1 1/2 percent or so of the
8 utility meter, and we can demonstrate that. A lot of times
9 that gets us disqualified; just the fact that we're not
10 using the utility meter.

11 What we see happening, and it's happening today,
12 is that you see a lot of meters going out with a Zigby under
13 glass module and those types of things, that will make it
14 much easier for a device inside the building to pick up that
15 feed. And we're actually investing in some of those meters
16 in a demonstration project. We're paying for them in the
17 City of Austin to do a large scale demonstration that
18 includes homes and offices and retailers, and that sort of
19 stuff, they've integrated.

20 COMMISSIONER MOELLER: Thank you, Mr. Chairman.

21 CHAIRMAN KELIHER: Thank you.

22 I just want to pick up on something Commissioner
23 Lieberman said. I thought your supply and demand
24 distinction was actually, was interesting and useful. But
25 we are still governed by the legal jurisdiction, the retail-

1 wholesale jurisdiction. I realize that may not respect the
2 way the marketplace is operating, but that's the hand that
3 we're dealt.

4 So I'm curious, a number of the panelists have
5 talked about how disconnects between federal and state
6 policy and even demand response -- I can't say I still
7 really have a fair understanding of what exactly the
8 disconnects are, at least given the orientation of these
9 conferences, I'm in list-making or list-taking mode, and I'm
10 curious if you could identify what are the three biggest
11 disconnects between federal and state policy that impede
12 demand response?

13 And one I assume is scarcity pricing. It's come
14 up from a number of the panelists, others have identified
15 lack of real time pricing, which they point out is something
16 not all the residential consumers are clamoring for in any
17 event, and lack of penetration of advanced metering.

18 But those panelists that want to answer the
19 questions, tell me what are the three biggest disconnects
20 that we have to address to get closer, to get better demand
21 response? I won't even say close to perfect demand
22 response, because I don't think we're really quite
23 approaching perfect demand response.

24 But is it scarcity pricing? Is it real-time
25 metering, is it real-time pricing? I just don't know what

1 the right list is of what are the major disconnects.
2 Because I also think that if there are disconnects between
3 federal and state policy, we're not going to accomplish
4 much. You can end up with a perfect provision in an RTO
5 tariff that is a beauty, but if it's inconsistent with state
6 laws in that region, it's a beautiful nullity; so we don't
7 want that to be the end result.

8 CMNR LIEBERMAN: I guess two quick responses.
9 One is, not to be flippant, but we really ought to come up -
10 - I agree with Richard, we've got to come up with something
11 other than scarcity pricing. It's not a real easy thing to
12 market; just scares the bejesus out of my colleagues and
13 myself.

14 But second, I think -- the more I think about
15 Commissioner Wellinghoff's question this morning, the more I
16 think it's critically important. I think as long as there's
17 this disconnect between wholesale and retail, and as long as
18 retail is workably competitive or produces outcomes which
19 are reminiscent of the competitive markets, or whatever, I
20 think that the sense of urgency on the part of state
21 commissions to align retail to wholesale isn't there.
22 That's been my experience at the Illinois Commission, and
23 it's been my conversations with other commissioners as well.

24 It's a byproduct. This is like, "Bob's
25 interested. Just let him go to the conference." And I

1 think until it becomes kind of a core value of how do we do
2 this? And how do we learn how to do it and how do we
3 develop the tools to do it, both on the retail side and on
4 the wholesale side? And I think we have to say, to make
5 these things work you get real customer benefits, extensive
6 customer benefits to reduce the capacity requirements over
7 time to save people money, you need to be doing this stuff."

8 I know that's not, hectoring is not your
9 function. But I think that it goes back to the fact that
10 they were misdefined, I think, at the beginning and it
11 hasn't been built in; it's a core job at the state
12 regulatory level, and I think that making that clear would
13 be very helpful. I can't promise anything, but it would
14 certainly be helpful. Thank you.

15 CHAIRMAN KELIHER: Mr. Doying?

16 MR. DOYING: You asked specifically for the
17 disconnects; I see two of them. Successful wholesale
18 markets presuppose that capabilities and economic value will
19 be brought to the market is the value is expressed in the
20 market. If there's a price, you have something you can sell
21 at that price and make a profit, you're going to be there.

22 That is not the case for most of the demand
23 capability that is out there today. If the end user is not
24 eligible to participate at the wholesale level, they're not
25 going to be there. If the intermediaries that represent

1 them today do not see the benefit in terms of a financial
2 benefit from bringing that capability to the market, which
3 is often the case due to ratemaking treatment, they're not
4 going to show up, either.

5 It doesn't do you any good to save a lot of money
6 as a regulated entity with demand response if that money
7 always passes straight through to the ratepayers. Some of
8 it has to be shared with the company in order for the
9 incentive to be there for them to show up with that demand
10 response.

11 So I think there are some very clear disconnects
12 that misalign the incentives of the parties that are able to
13 bring the demand response, or in some cases preclude their
14 participation; and those are the two areas that we really
15 need to resolve in order to make progress on this issue.

16 Scarcity pricing will be helpful; you've got to
17 have the right prices to provide the right incentives, but
18 if people can't show up or don't have the incentive to show
19 up, you still won't get the level of demand response you're
20 looking for.

21 CHAIRMAN KELIHER: Thank you.

22 Any comments? Mr. Meade.

23 MR. MEADE: Yes. To the extent that you can
24 effect state policies and as you said, the RTO tariff can be
25 perfect in that regard, maybe we can make an effort to make

1 the tariffs as demand response friendly as possible, with
2 the understanding that a state policy might be able to
3 negate the customer's ability to participate in this great
4 federal tariff, but just making sure that it fits that
5 criteria and perhaps makes it obvious where a state policy
6 is denying the customers in their state to effectively
7 participate in a federal program.

8 The other comment I wanted to make had to do with
9 the, where and RTO policy is allowing a state utility to
10 inappropriately deny demand response resource to participate
11 or to basically second guess that participation, and they
12 would like to clean that up, too, if that's within federal
13 jurisdiction.

14 CHAIRMAN KELIHER: Not quite sure I followed that
15 one. Are you suggesting a key word? The industrials a few
16 years ago proposed a, had a very grand proposal in PJM that
17 would have entailed preempting every inconsistent state
18 retail tariff; and the PJM industrials ended up withdrawing
19 that.

20 But you're not proposing that kind of path, are
21 you?

22 (Laughter)

23 MR. MEADE: I do not think so.

24 CHAIRMAN KELIHER: The other path is by regular
25 state colleagues, and I think the word collaboration is in

1 the title of Jon's working group; and you know,
2 collaboration had has a bit of a bad name since 1940, but
3 it's still not worked very well -- I think that's the path
4 that we have to go down with our state colleagues. It's not
5 going to be the fastest path.

6 MR. MEADE: We're frustrated, and work needs to
7 be done to improve that.

8 CHAIRMAN KELIHER: I want to ask Dr. Hogan: Do
9 you believe energy-only markets will provide actually more
10 effective -- will we see more effective demand response in
11 an organized market than as an energy-only market that has
12 either no caps or higher caps? That's a question mark.

13 DR. HOGAN: Well, I think if you force me to
14 choose between having adequate scarcity pricing and an
15 energy-only market, and inadequate scarcity pricing and the
16 best Forward Capacity Market you could imagine, I would
17 choose the former.

18 But that's not the choice that you're compelled
19 to make, and Gordon van Welie explained in several ways why
20 these actually can be complimentary. But I think without a
21 doubt, as I said several times, that the most important part
22 is the scarcity pricing; all the other things are fixes to
23 get around the problems that haven't been solved when you do
24 that, if there are any remaining.

25 I think the honest answer is about whether or not

1 you can get away with just an energy-only market is, we
2 don't know. And the reason we don't know is because we
3 haven't sent the right price signals. I suspect that a lot
4 of people who have been in many other room like this, have
5 been saying is correct; is that there's an enormous,
6 untapped potential out there in the demand side response.

7 And when they see the prices and they see the
8 money that they're leaving on the table, a lot of these
9 barriers to entry will become a lot easier to overcome,
10 because they'll see that it's there, and they'll respond in
11 ways; so the highest prices that we talked about, the
12 \$10,000 number, won't actually occur very often or hardly
13 ever, because there will be so much response on the demand
14 side that it will be essentially having the capability to
15 maintain the reserves, and you'll have enough, and you'll
16 price them much more evenly over the year; but in those
17 moments when things get really tough, which is what Gordon
18 was worried about, then you'll have the right pricing just
19 when you need it, and it will be enormously helpful.

20 Whether or not that's going to turn out to be
21 enough by itself I think is an open question, and if you
22 haven't put in a Forward Capacity Market yet and you're
23 busy, then I would say do the scarcity pricing first, and
24 then look at Forward Capacity Market second.

25 If you have a Forward Capacity Market in place

1 and you've already gone through all of that agony, then I
2 would say 'Well, don't disband it because it's already there
3 to net out the scarcity pricing story, just put the scarcity
4 pricing in now, because they're not incompatible with each
5 other.' So in either case, I'd get to the same operational
6 decision about what you actually do now.

7 CHAIRMAN KELIHER: Let's be clear, scarcity
8 pricing is little 'r' and --

9 DR. HOGAN: It's trying to --

10 CHAIRMAN KELIHER: -- the capacity market is Big
11 'R' or little 'r'?

12 DR. HOGAN: Well, since it's a mandate, that you
13 have to do it, and you have to do it in a way that forces
14 people to pay for it who don't want to pay for it, and so on
15 --

16 CHAIRMAN KELIHER: Okay.

17 (Laughter)

18 One last question. I think we have to entertain
19 any really first class staff questions. So you can prepare
20 those.

21 I have just one last question. Really, to get to
22 perfect or near-perfect demand response, what kind of
23 penetration do we need? Does every residential, commercial,
24 industrial consumer have real-time prices and an advanced
25 meter, or is it really more industrial, commercial and

1 willing residential consumers? I just don't really know
2 what kind of penetration we need to do to see perfect or
3 near-perfect demand response.

4 MR. VAN WELIE: My sense, if you look at the top
5 hours in New England, it's about 60 hours in a year. So you
6 really get good penetration with our system, 5 to 10
7 percent, 60 hours a year. I think that would be great.

8 And we're on track, you've gone down the physical
9 path. That will take some effort to get further.

10 CMNR LIEBERMAN: I guess it depends what you're
11 trying to do. To the extent that this, what we're really
12 talking about is customer's choices. You want it as
13 widespread as possible. I think our analysis in Illinois
14 showed that 10 to 15 percent of residential customers on a
15 real-time price with an elasticity that we've seen in the
16 pilot projects would provide a significant reduction in the
17 risk of the load that the supply would --.

18 So my sense is that somewhere in that 15 to 20
19 percent range of load -- but I do think it has to be across-
20 the-board. I think if you just focus on -- if you just
21 focused on industrial, that's not clear that it helps in
22 terms of residential pricing. The real issue here is
23 changing the load shapes at this phase. I think that's the
24 key point; how much do we need to change those load shapes.

25 CHAIRMAN KELIHER: Thank you.

1 Mr. Doying?

2 MR. DOYING: I think I would largely agree with
3 that, that it's one very small; but second, but more is
4 always better. Why do we pursue markets? Because there are
5 economic efficiencies that we can gain by doing so, and the
6 further you drill down the more of those efficiencies you
7 can get out. But I would agree that based on the demand
8 curve that we see in our region and the equivalent demand
9 response that we get with virtual activity today, it is a
10 very small number. The interim benefits would be in that 5
11 to 10 percent range as well.

12 CHAIRMAN KELIHER: Mr. Sharplin?

13 MR. SHARPLIN: Yes. I think that David's team,
14 when they did your blue book last year on DR, I think they
15 showed something like 3 to 5 percent made a huge difference;
16 and I think that was based on the New England study
17 primarily, and some other studies.

18 You know, the economic models that we have seen
19 indicate that in some cases, in some extreme conditions,
20 when the market is upside down, 10 percent of the load is 50
21 percent of the price, for the whole year. And some folks
22 challenge that, but it's some number like that.

23 So if you're talking about 5 or 10 percent
24 penetration, you're talking about enormous numbers. I think
25 that generally speaking you want to, you know, the market

1 should go where the money is; and I think that to the extent
2 we can credit transparent market, that allow demand response
3 products to come to the market efficiently, you're going to
4 have the proper penalties associated. And if you go hammer
5 off a large steel mill on the end of a long feeder, that's
6 not -- in some cases that's the perfect solution, but
7 generally for the grid operator, that's not the great
8 solution. If you trigger 20,000 homes, that might be a much
9 better solution in that instance. And I think those things
10 will sort themselves out, so that transparency and breaking
11 down the market rules so that participation can happen. We
12 believe it's happened real quickly.

13 CHAIRMAN KELIHER: Thank you.

14 Staff, questions?

15 MR. O'NEIL: I'd like to clarify something,
16 because Bill, earlier in his testimony, sort of said this;
17 but then I think we forgot. I don't think it's an issue of
18 implementing scarcity pricing; I think all the ISOs in one
19 form or another have scarcity pricing in at least three;
20 ERCOT, Australia, and I believe PJM. The encouragement is
21 for the generators to create the scarcity price by bidding
22 very high -- I'm not sure whether we would call that
23 encouragement or not, but that's the way it ends up.

24 But then the issue that comes back is, is that an
25 exercise in market power? And so my feeling is, are we

1 characterizing this debate right? Is getting the scarcity
2 pricing correct or improving the scarcity pricing that we do
3 today versus implementing scarcity pricing?

4 I think we have it in all of our markets, and the
5 real question is getting it right; and I was just wondering
6 how you'd feel about that.

7 MR. VAN WELIE: Well, as you well know, that was
8 a huge debate when we were dealing with the whole capacity
9 market construct. And so the whole issue that centered
10 around that was what drove us to the construct that we have.

11 So that's why I said the construct where beyond a
12 certain point you net out the energy revenues against the
13 capacity market payments, is a safety net. And I think you
14 can work from that point, once you've got the markets in
15 place and you've gotten everybody comfortable there working,
16 I think you can then further evolve it.

17 But to that next step, I don't think we will be
18 able to just sort of let everything go.

19 MR. DOYING: I think it's also fair to say that
20 although all the markets have attempted to do something to
21 address pricing during tight supply situations, that none of
22 them work well empirically; I mean, we can see that through
23 analysis of what the prices are and what we expect prices to
24 be when we run out supply; and second, some of them are
25 probably more likely than others to be successful if we keep

1 pushing them, asking generators to bid up until the price is
2 sufficiently high is probably not the best approach, and the
3 one -- it has attributes of a past bid market, and there are
4 some very negative attributes with that if we ask generators
5 to chase the price up.

6 Second, we run into market power problems, which
7 I will likely prohibit people from being able to move prices
8 up as high as they would need to be, accurately reflect the
9 fundamentals.

10 CHAIRMAN KELIHER: Any other questions?

11 Well, with that, why don't we take a break, and I
12 want to thank these panelists.

13 (Whereupon, at 11:20 a.m., the conference
14 recessed for lunch, to reconvene at 12:30 p.m., this same
15 day.)

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1 through the exchanges. There would be what would be termed
2 a physical settle, which could be called into the contracts;
3 and then there's the long term PPA, which is physically
4 backed by a resource -- a long term, maybe 30 year sale.
5 And as I discussed through these things, those are the three
6 types I see, and I think each of them needs to be touched
7 on.

8 First, if you look at the first question, more or
9 less, do forward markets support bilateral contracting in
10 some markets different than others. I actually submitted
11 some testimony that looks at the Nymex and the ICE, which
12 are one of the financial settled contract. And my Figure 1
13 actually showed that some of the volumes in NYMEX futures
14 contracts were higher for Western Hub, but you had some
15 volumes for some of the other organized market areas.

16 What's striking there is you don't see contracts
17 in nonmarket areas, at least financially settled. Then if
18 you look at my Figure 2, this looks at the -- not the
19 volume, but really the length of the contract; how far out
20 is there a volume, if you will; and it looks like about 12
21 to 18 months on the NYMEX you can get some amount of volume
22 on the NYMEX.

23 Then if you switch over and look at ICE, I didn't
24 have access to the forward stuff, but my Figure 3 actually
25 shows, you see a pattern of the physically settled contracts

1 actually diminishing, the financially settled contracts
2 increasing; and that can occur in the areas we have
3 organized markets. And areas where you don't have organized
4 markets, but a little bit of activity, but you really don't
5 see a lot of volume growth.

6 Now when you talk about the next question, which
7 we moved to, for the significant impediments of long term
8 contracting. I think the first impediment and the biggest
9 one I see is perception of risk. In other words, you look
10 forward in time, I think in this time of our industry; the
11 amount of uncertainty looking forward is bigger than it's
12 ever been. Given carbon legislation, entry of
13 environmental, you have regulatory uncertainty at various
14 stages.

15 The point, though, is that affects all types of
16 contracts. It affects the financially settled, the
17 physically settled is sort of gone in organized markets, but
18 the long term PPAs also have to face that risk. So it's a
19 universal issue, and I think that what you see, the
20 phenomenon you see in the financially settled is you don't
21 have volume beyond about 18 months. And a lot of that is,
22 again, the uncertainty looking forward; you can't agree on a
23 price. I mean, the seller may see the environmental risk
24 one way, demand customer may give it another, and there's a
25 gap.

1 And that same gap has to exist in the 30-year
2 type right also, both in the organized market areas and not.
3 And there may be different ways to off-weigh that risk;
4 through the market, you have to face the market in an area
5 where you may have a few closet customers, some way to
6 spread the risk to other customers, you may be able to write
7 a contract for a certain set of customers; but the risk
8 still remains, and has to be dealt with.

9 So I don't think it's a problem in a market area
10 as much as it is a universal problem.

11 I think if you go down to the perception of
12 inadequate opportunities, again gets back to this difference
13 in expectations. Fundamentally, again, buyers and sellers
14 have an incentive to trade forward; the sellers of course
15 want to lock in revenue, the buyers want to control cost.

16 But the issue is, coming together at a reasonable
17 price; and I think again this perception of the uncertainty
18 moving forward and the inability to hedge it, you can hedge
19 fuel uncertainty; but environmental and changes in the state
20 of affairs is not necessarily something that's easily
21 hedged.

22 As far as, I turn to what can the Commission do?
23 Well, one thing, you already have done a lot, at least in
24 our area, putting in long term transmission rights, helping
25 us get that done. It was a debate last year, putting in the

1 forward capacity construct.

2 I think there are some other issues related to
3 some of the state auctions that tend to only look forward
4 about a year or so, the load obligation, nobody knows who
5 has the load, having an incentive to work with your state
6 counterparts to look at maybe more standardized forward
7 option designs in those areas.

8 And I see the time is diminishing, so I look
9 forward to your questions; and thank you.

10 CHAIRMAN KELIHER: Thank you very much.

11 I now recognize Leslie Biddle, Managing Director
12 of Goldman Sachs.

13 MS. BIDDLE: Mr. Chairman, Commissioners, thank
14 you for inviting us to participate on the panel today. As a
15 financial institution, we've been involved in power markets
16 for many years, and we recognize that well-designed markets
17 are essential to achieving the full benefits of competition
18 for consumers, and we appreciate the Commission's ongoing
19 efforts to analyze and improve the design of performance
20 markets.

21 My background is somewhat diverse, and I touched
22 on this issue in many ways in the last 18 years. I come
23 from a finance background, have spent a number of years
24 developing power plants here with AES Corporation and then
25 at Goldman Sachs for the last five years, where I've been

1 responsible for power sales and in particular on developing
2 projects that help facilitate new investment in the power
3 sector through transactions as a pure cash flow, and by
4 supporting project finance.

5 My experience in structuring bilateral contracts,
6 since the market has evolved, I'd like to offer some
7 observations on what steps may be taken to improve the
8 opportunities for long term bilateral contracting. Bloodied
9 again by offering a somewhat contrarian point of view on the
10 issue of long term contracts.

11 While the folks on these panels are improving the
12 opportunities for long term contracting, there are many
13 different flavors of long term contracts, as Andrew just
14 stated. And in some instances, particularly with respect
15 to new generation development, the need for long term
16 contracts can be an indication of -- structure and
17 performance in the underlying markets.

18 Many utilities rely on competitive solicitations
19 to acquire new generation resources, with winning bidders
20 being awarded long term contracts of ten years or more.
21 These contracts are often structured as resource-specific
22 agreements, and as such tend not to be fundable or readily
23 tradeable.

24 While this approach to new generation development
25 relies on competitive solicitations, and therefore provides

1 benefits to consumers by shifting certain costs in operating
2 generators, it still places significant market risks on
3 utility ratepayers.

4 Ideally, competitive markets would support the
5 development of new generation resources without the need for
6 long term utility backed contracts. The existence of long
7 term forward markets in energy and relate products such as
8 capacity and renewable energy credits, will allow merchant
9 developers and intermediaries to create financing structures
10 that do not rely on a captive customer base.

11 The fundamental requirements for robust liquid
12 forward markets and standard tradeable products, and gold
13 design stock markets that ensure market participants of an
14 efficient and effective means of settling forward
15 transactions.

16 To the extent generation development can be
17 supported by robust, liquid forward markets, consumers will
18 benefit by shifting investment and operating risk from
19 generators and intermediaries.

20 The framework has proved most conducive and to
21 delve into these kinds of products, and most support the
22 bilateral contracting of forward markets that are well
23 organized, encompass a large geographic area, has a diverse
24 mix of resources that provide opportunities for trading and
25 resource optimization, and have stable liquid hubs.

1 In PJM West, for example, market participants
2 have traded out as far as 2016. Even in the context of
3 more developed markets, we have observed that there have
4 been fewer parties on the buy side as you get further out on
5 the curve. In some cases this may be due to state
6 regulatory policies that do not encourage long term
7 contracts beyond three years. Many of the slice of load
8 auctions that Andrew mentioned that make up the Eastern
9 market involve a term for up to three years.

10 In addition, long term contracting can be
11 difficult on some retail providers, and markets with retail
12 competition. Contracts between consumers and retail
13 providers typically do not extend beyond a few years.
14 Credit issue, load migration risk also make it difficult for
15 smaller retail providers to connect to a long term power
16 purchase contract.

17 The agenda for today's panel raises the question
18 as to whether potential buyers and sellers may have
19 different expectations with regard to contracting. We
20 believe that the developers in the power industry would make
21 the investment decision to build new generation if they have
22 a reasonable expectation that the prices they receive for
23 sold power capacity and related services will provide
24 appropriate return on investment. And this would occur
25 when the average price for energy and related products over

1 time reflects the long term marginal cost of the real
2 generation.

3 Our view is that the market prices over time need
4 to reflect those long term marginal costs if we're to write
5 economically efficient signals for both consumption and for
6 production.

7 To the extent that these prices are
8 systematically below long term marginal cost, the market
9 will encourage excess consumption and underinvestment in new
10 infrastructure. Similarly, if prices are systematically
11 above long term marginal costs, consumption that would
12 otherwise be economically efficient, will be discouraged,
13 and overinvestment would be encouraged.

14 The conclusions for this, as we have recently
15 taken a number of important steps to remove barriers to long
16 term contracting, such as Order 681 and Order 890.

17 Further actions that you could take or conserve,
18 are by providing regulatory stability, by getting to the end
19 state in terms of market design as soon as possible. The
20 overhang, the questions that Andrew had mentioned, are
21 important impediments to the current volume of the markets.

22 Further, recognizing FERC's need to cooperate
23 with the states, we need to move beyond the rate freeze and
24 referral programs that are common in deregulation-transition
25 period.

1 And thirdly, to address the unresolved issues
2 regarding contract certainty. We believe that a critical
3 factor encouraging development of future contracts is to be
4 providing market participants with certainties the contract
5 terms will be respected as agreed to by all parties.

6 Thank you for the opportunity.

7 CHAIRMAN KELIHER: Thank you.

8 I'd like to now recognize Duane Dahlquist, the
9 General Manager of Blue Ridge Power Agency.

10 MR. DAHLQUIST: Good afternoon.

11 Blue Ridge is a joint action agency consisting of
12 11 members that serve 350,000 Virginians across the
13 Commonwealth. I submitted my prepared remarks, and will
14 just summarize here.

15 For Blue Ridge, a long term is a bilateral
16 contract of one year or more. In the case of our members,
17 it would be a requirements-type load following contract with
18 a financially sound supplier that serves reliably.

19 Since 1995, Blue Ridge's members have had three
20 solicitations for alternative power supplies, seeking lower
21 wholesale power costs. In 1995, we had 18 bids for full
22 requirements load following contracts ranging from \$27 to
23 \$37 a megawatt hour, for power only, net of transmission and
24 ancillaries.

25 In the last solicitation, we received eight bids,

1 ranging from \$55 to \$65. If you do the math on contract
2 prices, that's over an 100 percent increase. When the
3 results of the 2005 solicitation were in, our members
4 decided that continued reliance on PJM's bilateral market
5 was only going to yield ever fewer offers at ever higher
6 prices. The associated risks were simply too high for not-
7 for-profit distribution entities that are concerned about
8 meeting their obligation to their customers to provide
9 reliable service at affordable and stable prices.

10 They concluded the contracting for long term
11 requirements type, load following supply in PJM using
12 periodic RFPs is simply not viable. As a result, some of
13 the Ridge members are evaluating signing or have already
14 signed 20 year formula-based requirements-type contracts
15 with their traditional, investor-owned utility on terms less
16 favorable than would have been available to them in a pre-
17 1992 EPAct, pre-PJM 2 market environment.

18 Others have signed shorter term, 24 to 30 month
19 contracts and are working a larger joint action agency to
20 build a portfolio asset of power supply resources that
21 includes generation ownership. Until those power supply
22 resources are in service, they must rely on short- and long
23 term contracts, one to six years, and market purchases to
24 supply their needs, and will continue to have substantial
25 exposure to the vagaries of the PJM markets.

1 One of our members, Bristol, took yet a different
2 direction. For years, Bristol had been a TVA captive
3 customer, and after a long struggle it obtained
4 congressional authority in EAct 1992, to stop for lower
5 cost power. It did so, and from 1998 through 2004, Bristol
6 contracted with a non-TVA supplier for indeed lower rates.

7 But after the 2005 solicitation, Bristol decided
8 to leave PJM entirely, and signed a 20 year requirements
9 contract with TVA, giving up the PJM interconnection that it
10 fought so long to get.

11 Our members at least have been able to pursue
12 other power supply strategies to reduce their dependence on
13 markets. Our experience with markets is not unique.
14 Municipal systems in other RTOs are having similar
15 experience, and I can only conclude that for many, other
16 power supply options have not been as available, leaving them
17 at the mercy of the bilateral markets.

18 So what is going on? We're seeing fewer bidders
19 with higher prices that seem to reflect clearing prices in
20 the PJM-run spot markets, which in turn are often set by
21 natural gas fired generation instead of being reflected with
22 bidders' production costs.

23 FERC has made the same observation in its 2006
24 State of the Markets Report. The logic is simple: Why
25 should a generator commit its resources to a long term

1 contract when it can receive high profits in the spot
2 market?

3 PJM Day-2 spot markets allow some generators to
4 receive prices for above their home cost to generate. This
5 is due to the use of the single clearing price mechanism.

6 Natural gas units were 27 1/2 percent of PJM's
7 installed capacity at the end of 2005. The natural gas
8 generated 5.9 percent of the total energy. Over 90 percent
9 of the energy was produced from coal and nuclear units.

10 The promise of one access was that competition
11 would give power suppliers incentive to lower their costs,
12 and that those lower costs would flow through to customers
13 in the form of lower prices. Instead what has happened is
14 that sellers with lower cost structures are free to raise
15 their bids to the levels of higher cost sellers. The
16 competition among suppliers of requirements-type power that
17 existed at the beginning of open access has significantly
18 diminished over time.

19 What can FERC do? This Commission must better
20 understand how prices are set in bilateral markets, and the
21 complicated interactions and interrelationships between RTO
22 spot markets and bilateral markets. The Commission should
23 investigate bilateral contracting processes in RTO regions,
24 assembling a comprehensive picture of who is selling and who
25 is buying, what prices are being offered, what prices are

1 being paid, and what kinds of contract terms are being
2 offered.

3 The Commission also needs to distinguish between
4 different types of bilateral power supply products. The
5 market for bilateral requirements-type power that follows
6 the load of the utility may be much different than the
7 market for set blocks of power, with a different universe of
8 suppliers and different terms.

9 Only after the Commission itself has a full
10 picture of what is actually going on in RTO regions will it
11 be possible to develop policies that will foster long term
12 bilateral contracting, ensure just and reasonable rates in
13 those markets, and therefore provide the long-promised
14 benefits to consumers of wholesale competition. Thank you.

15 CHAIRMAN KELIHER: Thank you very much.

16 I'd like to now recognize Mr. Daniel Allegretti,
17 Vice President and Director of Wholesale Energy Policy with
18 Constellation Energy.

19 MR. ALLEGRETTI: Thank you very much, Chairman
20 Keliher, Commissioners. I'm delighted to be here with you
21 today.

22 The organized markets, as you well know, consist
23 both of the highly visible spot markets, the real time and
24 day ahead, as well as the over-the-counter or bilateral
25 markets that Andy described. And buyers and sellers in the

1 organized regional markets all have the option of
2 transacting, every day, in either the daily markets or in
3 the forward markets for contracts of various terms.

4 To forego an opportunity to transact in the daily
5 market and instead reach agreement on terms and price in a
6 forward contract necessarily entails an assessment of the
7 probable outcomes in the daily markets, looking at the
8 future.

9 And therefore it's no surprise, again as Andy
10 noted in his written comments, that the regions with well-
11 designed and well-run spot markets in fact have the most
12 robust bilateral forward markets.

13 As you think about then how to promote bilateral
14 contracting, forward contracting, the most important
15 features that I think you should focus on are actually
16 aspects of the organized spot markets, keying off of this
17 interplay between the two markets, and facilitating
18 perceptions on the part of buyers and sellers about the
19 alternative outcome.

20 And there are four areas that you can focus on.
21 The first is price formation, where daily prices accurately
22 reflect actual supply and demand conditions, buyers and
23 sellers will feel more confident taking a future position.
24 Where spot prices are distorted through the imposition of
25 out-of-market compensation to generators in the use of

1 uplifts, or aggressive mitigation measures and price caps
2 are deemed necessary, then long term contracting will be
3 more difficult.

4 Improving price formation by encouraging RTOs to
5 adopt market mechanisms and designs that rely upon commodity
6 prices, that minimize the use of out-of-market compensation
7 mechanisms such as uplifts or RMR contracts will go a long
8 way. So will providing consistent guidance on the
9 appropriate measure and mechanisms for addressing market
10 power, and avoiding the need for ongoing or continuous
11 market intervention and price capping.

12 The second area that you can focus on is price
13 integrity. This goes both to the concept of price finality
14 in the daily markets, as well as the protection of contract
15 integrity in the bilateral markets. Assuring just and
16 reasonable rates through proper market design is the goal
17 here. After-the-fact determinations and modifications to
18 prices will impeded the development of the bilateral market
19 by creating uncertainty of outcome for both the buyers and
20 the sellers.

21 In this area you can improve price integrity by
22 providing continued affirmation of the Commission's
23 adherence to the file rate doctrine, as was done in the
24 Commission's recent dismissal of the care complaints,
25 sending a clear message to the market as to how the

1 Commission will view and respect market-based rates in light
2 of recent judicial precedents, will help to restore
3 confidence in the integrity and enforceability of such
4 agreements and reduce uncertainty for market participants.

5 The third area to look at is liquidity. Buyers
6 and sellers have greater confidence in their expectations
7 where there's real depth in the daily markets. As Leslie
8 indicated, trading hubs, larger scale and scope RTOs, ease
9 in transparency of transactions across seams, and a high
10 degree of operational competence will all serve to promote
11 more bilateral contracting as well as trading in the daily
12 markets.

13 Promoting greater liquidity by encouraging RTOs
14 to facilitate trading transactions across their seams and
15 between markets, and to bring their operational practices
16 and information systems up to the highest possible standards
17 will also help to promote bilateral contracting.

18 Finally, the Commission can help to promote long
19 term contracting opportunities by lending stability to the
20 organized markets. Regulatory uncertainty, as was noted, is
21 another important cost of long term agreements. Now
22 allowing the perfect to be the enemy of the good, and
23 bringing some stability to market design, especially as
24 regards to the definition of the underlying products;
25 energy, capacity, ancillaries, will also go a long way

1 toward promoting the kind of certainty about the future that
2 will allow parties to contract forward bilaterally.

3 I would close by saying that I think it is not so
4 much a question therefore of impediments to bilateral or
5 forward or long term contracting, but rather a question of
6 the perception of what the alternative is in the shorter-
7 term markets. Understanding whether parties can better
8 address risk and uncertainty by transacting a forward
9 market, or whether the fundamental costs associated with
10 those types of contracts in fact make the shorter-term
11 markets more attractive, is the real issue.

12 Improving short-term markets will fundamentally
13 improve long term markets. Thank you.

14 CHAIRMAN KELIHER: Thank you very much.

15 I now recognize Mr. Walter Brockway, Operations
16 Manager, Alcoa.

17 MR. BROCKWAY: Good afternoon, and thank you for
18 the opportunity to participate in this technical conference.
19 I'm Walt Brockway, Manager of Regulatory Affairs - Energy,
20 for Alcoa. Alcoa is a member of ELCON; however, the
21 following remarks are on behalf of Alcoa.

22 As the nation's largest manufacturer of aluminum
23 and aluminum products, Alcoa is one of the largest consumers
24 of electricity on the North American continent. The bulk of
25 that consumption, more than 2800 megawatts in the U.S.

1 alone, occurs at aluminum smelters. We consume at a very
2 high load factor, 24 hours a day, 7 days a week. Steady
3 state loads like these form part of the base load of the
4 electric power system, because they do not contribute to the
5 variability of system demand.

6 We currently have operations in New York ISO,
7 MISO, and ERCOT -- smelting operations; downstream
8 operations we have in every market. Aluminum smelting is
9 both electricity and capital intensive, because electricity
10 is on the order of 40 percent of our product cost, it is a
11 raw material.

12 When we determine where to locate our
13 manufacturing facility to smelt aluminum, a key factor is
14 our ability to secure a long term electricity supply at a
15 relatively low price. In our case, long term is 20 years or
16 more.

17 Most of the facilities we have in North America
18 are self-supplied by generation we own outright, or in
19 partnership with a supplier supplemented by a long term
20 electric supply contract with the local electric utility.

21 However, if we cannot secure certainty of supply
22 and pricing, we cannot economically operate smelters and
23 complete in the global market, and it is a global market.
24 The latest example of this is our smelting facility in
25 Frederick, Maryland, where unfortunately we were completely

1 dependent upon outside electricity suppliers. The facility
2 was well run, technically up to date, having excellent
3 access to the North American market -- still our largest
4 market -- as well as being located near a port for import of
5 ore and export of materials, of finished products. Yet, our
6 inability to negotiate a longer-term economically acceptable
7 electricity contract led to a curtailment of operations at
8 the end of 2005.

9 The plant now lies idle while we continue to
10 pursue viable options for electricity.

11 World aluminum markets have been relatively
12 strong in the last few years, so we really did not want to
13 shut that facility down. But in the end, we had no choice.
14 We found no supplier willing to discuss supplying us with
15 anything other than electricity priced to reflect peak load
16 generation, as well as placing on us all the risk of
17 transmission congestion.

18 Because we are a nonvariable base load customer,
19 we had expected that a competitive market would have at
20 least brought us contract offers reflecting the cost of new
21 base load supply, but we received no such offers. The
22 contracts that were offered were short-term, three years or
23 less, and completely based upon marginal pricing reflecting
24 the most inefficient peaking units. Had we accepted any of
25 them, the price for electricity at that facility would have

1 doubled.

2 The purpose of a long term contract is to provide
3 security to both buyers and sellers. The seller gets the
4 security of a long term revenue stream with which to finance
5 the capital cost of base load generation; the buyer receives
6 the security of locking in those capital costs for the term
7 of the contract. Long term bilateral contracts can be used
8 to finance long term investments, eliminating the risk of
9 recovering capital cost by means of spot markets or
10 regulatory proxies.

11 Long term forward markets are generally absent
12 from FERC-approved organized markets. Bilateral contracts
13 exist in these markets but are little more than a pass-
14 through mechanism of purchases in the spot market at peak
15 market prices; generally the gas-fired combustion turbines.

16 The buyer receives generation price to reflect
17 the least efficient producers of power as well as bearing
18 the full risk of spot market price volatility. What a buyer
19 does not receive is a recognition from the supplier as to
20 the nature of the load. These markets make the mistake of
21 treating all customer loads as being equal in terms of the
22 cost of serving them, which they are not.

23 Long term forward market and long term bilateral
24 contracts would make the spot market smaller, as we
25 originally envisioned it would be. We had understood the

1 goal to be to create a market based on long term bilateral
2 contracts with a relatively small spot balancing market.
3 The opposite has happened.

4 Generators ignore the forward market because they
5 expect to get higher prices in the spot market, and there is
6 nothing in the market structure that compels them or gives
7 them the incentive to recognize differences in load
8 characteristics. Moreover, the Commission's policies have
9 yet to create a situation in which additional transmission
10 investment is occurring that will relieve the increasing
11 congestion.

12 Manufacturing loads such as aluminum smelters
13 have different characteristics than other type loads; their
14 large size and high load factor provide a certainty that
15 permit base load generating units to run on a continuous
16 basis at their more efficient operating levels.

17 Yet we found this no longer make a difference to
18 suppliers functioning in organized markets where high
19 marginal prices are paid for all generation. Marginal
20 prices based on natural gas is unnecessarily lucrative for
21 existing coal and nuclear base load facilities, rendering
22 present average cost long term contracts obsolete, and that
23 is not producing construction of new base load generation.

24 We would like the opportunity to enter into long
25 term bilateral contracts that allow us to compete globally.

1 We can provide assurance that loads will be present at a
2 constant level, and in return seek reasonably priced
3 certainty. At the same time our loads provide benefits to
4 the bulk power system in the form of significant flexibility
5 to curtail load when reliability needs arise.

6 Initiatives that FERC should continue to pursue
7 include:

8 Address inadequate transmission infrastructure.

9 Continue to encourage price responsive load.

10 This will overall tend to moderate spot prices.

11 Assure that capacity payments are structured in a
12 way that encourages the development of base load capacity
13 and encourages long term bilateral contracts that fairly
14 reflect base load characteristics.

15 We are committed to continuing operation in the
16 U.S. market and are working hard to be more efficient in how
17 we purchase and use electricity here.

18 Thank you, and I look forward to your questions.

19 CHAIRMAN KELIHER: Thanks very much.

20 I'd like to now recognize Mr. Pedro Pizarro,
21 Senior Vice President-Power Procurement, Southern California
22 Edison.

23 MR. PIZARRO: Good afternoon, Chairman Keliher
24 and Commissioners and Staff. SCE appreciates the
25 Commission's commitment to competitive wholesale power

1 markets, and the opportunity to speak here today.

2 We are a major purchaser in the wholesale market.
3 Two-thirds of the electricity that we deliver to our
4 customers comes from market sources, with around \$7 billion
5 a year in power and gas transactions, and with nearly 17
6 percent of our energy coming from renewables, all of this
7 under the oversight of the California Public Utilities
8 Commission.

9 You asked us if there are barriers to long term
10 contracts. Well, for context, around 92 percent of our
11 energy in 2007 will come from long term commitments, both
12 ownership and contracts, with terms of five years or more.
13 However, we face real concerns with further long term
14 contracts.

15 I'll start with the three most significant
16 issues, which may be outside this Commission's jurisdiction,
17 and I will then cover some areas where you can help.

18 The first issue affecting long term contracts is
19 retail, not wholesale. California was one of the first
20 states in the nation to allow retail choice. We saw direct
21 access levels swing quickly with changing rules, going from
22 near zero to about 15 percent, back down to 1 percent, back
23 up to about 15 percent over a short period of time.

24 California suspended direct access in 2001;
25 however, state policy makers have stated their intention to

1 reopen retail competition under rules yet to be developed.
2 This puts us in a tenuous situation. Currently, SCE and
3 other utilities are the only entities doing any significant
4 long term contracting; and SCE cannot be the default
5 provider, signing long term contracts to create a reliable
6 system for all customers, not just our own customers, while
7 also being at risk of having customers depart to providers
8 who have not made or have no obligation to make any long
9 term commitments, leaving our remaining customers with
10 stranded contracts and higher rates.

11 Second issue: The financial industry views long
12 term power contracts as fixed obligations equivalent to
13 debt. The longer the contract, the higher the debt
14 equivalents that credit rating agencies impute on our
15 balance sheet when assessing our credit quality. In
16 addition, our counter-parties often require us to post cash
17 or letters of credit.

18 These items burden our balance sheet, they create
19 higher financing costs for our customers, and they reduce
20 our capacity to finance transmission and other
21 infrastructure investments. It's part of doing business,
22 but it's one that needs to be acknowledged.

23 Third, California is in the early stages of
24 implementing AD32, the greenhouse gas legislation. The
25 California Air Resources Board is currently doing a lot of

1 work in developing rules that will impact ultimately how we
2 procure long term contracts or make other long term
3 commitments. We simply do not know today what all those
4 impacts will be, and so that's a large uncertainty.

5 There are, however, areas where this Commission
6 can support long term contracts. First, we commend your
7 willingness to tackle the impediments to integrated resource
8 planning that are created by the current standards of
9 conduct. We need to get the right generation in the right
10 places in our resource selection and grid planning
11 processes.

12 The existing SOCs severely inhibit individuals
13 evaluating long term bids from accessing transmission
14 information that's essential to that process. The
15 Commission's NOPR attempts to alleviate that issue, but as
16 discussed in SCE's comments, the Commission should return to
17 a functional approach for determining access to information.
18 And there the employee is precluded from receiving nonpublic
19 transmission information to those in shorter term trading
20 activities.

21 Such an approach focuses on the individual's job
22 description as opposed to the organization within which she
23 or he works, and will help us as we think about the right
24 long term commitments to make.

25 Second, SCE is looking forward to the

1 Commission's decision in the market-based rate authority
2 NOPR proceeding. We appreciate your efforts to codify in
3 one place the test for market power. In this we urge you to
4 find the liquidated damages and call option contracts,
5 should no be in the calculation of an entity's capacity, and
6 that an entity's ownership of sites for future generation
7 should not be considered a market power test.

8 Third, I welcome some of the comments made
9 earlier about the ideas of the competitive market; can
10 deliver new generation with a long term contract in the
11 future, but that's not happening today. And California
12 needs new generation now, requiring long term contracts in
13 today's market.

14 California adopted a transitional mechanism by
15 which SCE can make long term commitments for new generation
16 needed across our entire distribution system, and pass on
17 the benefits and cost to all customers, regardless of their
18 retail service provider.

19 We launch an RFO, have already signed three 10-
20 year contracts for around 200 megawatts of new generation,
21 with more being considered. This is only a transitional
22 solution; however, because our balance sheet cannot handle
23 unlimited purchases on behalf of others, and because other
24 load-serving entities rightfully are not especially fond of
25 us purchasing in their behalf.

1 The long term solution is a capacity market. If
2 designed well, it can support existing generation and
3 construction of new generation in the right locations as
4 needed to meet load growth and reliability. It can fairly
5 allocate the benefits and costs associated with that
6 capacity, and it can mitigate market power in the presence
7 of a mandated resource adequacy and capacity requirement.

8 So we need the Commission to support development
9 of such a capacity market, as it gets worked up in
10 California.

11 Finally, we appreciate your efforts to support
12 new transmission infrastructure, including transmission
13 investment incentives, the Commission's backstop siting
14 authority, and the support for transmission facilities
15 reaching locationally-constrained generation resources, such
16 as those in the Tehachapi area in California.

17 Your efforts will help utilities secure
18 additional resources to meet customer's needs and the
19 state's policy objectives. One more action you can take is
20 to ensure that long term transmission rights can be
21 established when generation and transmission infrastructure
22 investment decisions are made, rather than waiting until the
23 facilities are built.

24 So with that, I thank you again for the chance to
25 speak, and welcome any questions.

1 CHAIRMAN KELIHER: Okay, thank you, Mr. Pizarro.
2 I'd like to recognize Commissioner Spitzer for
3 questions.

4 COMMISSIONER SPITZER: Thank you, Mr. Chairman.

5 It's interesting, this panel raised issues that
6 not only relate to long-term contracts but impinge on
7 competitive wholesale markets. The three areas of consensus
8 that I detected were, One, plainly a precondition to long-
9 term contracts is the law of the contracts, and I heard that
10 from some of the witnesses, that the contracts have to be
11 enforced and certainly the reasonable expectations of the
12 parties seem to be honored by the tribunals that are
13 enforcing the contracts.

14 Second, that there can be some retail -- retail
15 imperfections have tough consequences, and we can do Monday
16 morning quarterbacking on rate freezes and the like, but
17 that -- we need to learn from those experiences, and then I
18 think everyone mentioned this concept of regulatory
19 certainty. And the policy needs to incorporate some attempt
20 to delineate risk; and I think Mr. Ott spent most of the
21 time talking about some of the risk issues that -- he
22 described the problem as universal, and I would agree.

23 In this panel, though, we had a tension between
24 an academic view and a practical view, and it was a tension
25 that existed in the prior panel where there was a discussion

1 of price signals. And I did reflect on, at lunch, in the
2 last retail case I dealt with price signals, and one of the
3 witnesses spoke, and some of the consumer advocates followed
4 and said "The price signals you want are not real happy to
5 me and my people."

6 And that's one of the areas where we have this
7 conflict, and in the area of long term contracts, you have
8 the potential for a conflict if the academic view is the
9 long term contracts either are unnecessary or harmful,
10 because there's a great constituency -- I agree with Mr.
11 Dahlquist -- for the long-term contracts, particularly where
12 you have governmental entities providing the service.
13 There's a very clear fiduciary duty where you have elected
14 boards, city councils, distribution cooperatives who are
15 responsible for the rates, very directly, and are held
16 accountable in elections.

17 And I don't want this to be the case where we
18 have irreconcilable divergence between academic theory and
19 practicality. Here's my historical analogy for the day.

20 There was a division within the Democratic Party
21 in the State of New York --

22 CHAIRMAN KELIHER: Past tense?

23 COMMISSIONER SPITZER: Past tense. There were
24 the regular Democrats -- I think this had to do with the
25 nomination of Louis Katz -- and there were the more rabid

1 members, who were called the 'barn burners.' And the barn
2 burners arose from a -- I don't know if it's hypocrophal or
3 not -- story of a Dutch farmer in Upstate New York who was
4 disturbed by the presence of rats in his barn, and he
5 undertook every method possible to eliminate the rats from
6 his barn.

7 Finally, he burned down the barn to get rid of
8 the rats. And some of the folks who think, who are
9 concerned about price signals, for this panel, the people
10 who I think correctly won long-term contracts, view the
11 academic theory -- with due respect to Ms. Biddle -- that
12 doesn't put a great value on those long-term contracts, as
13 burning down the barn to get rid of the rats.

14 And we don't want to burn down the barn to get
15 rid of the rats. So in light of that view, what -- I do
16 understand the academic theory; maybe we'll start with Ms.
17 Biddle. How do we harmonize this, where I think Mr.
18 Dahlquist can say notwithstanding -- there will be a
19 premium, a risk premium his elected board's willing to pay.
20 How do we accommodate that, what I think is a reasonable
21 expectation?

22 MS. BIDDLE: There's nothing that limits his
23 ability to go out and enter into long-term contracts.
24 There's no rules against it, there's no market impediment.
25 If he can go out and reach an agreement, and there's lots of

1 solicitations out on the street. Obviously SoCalEd has
2 entered into long term agreements. If you can match up on
3 price and risk allocation, then you can do it.

4 COMMISSIONER SPITZER: If you construct a market
5 where everyone's driven to spot, and you heard the testimony
6 from Mr. Brockway and Mr. Dahlquist -- if I'm a generator
7 and I can sell on the spot market, why would I even
8 consider? Why would I even listen to --

9 MS. BIDDLE: Well, if you -- this gets to the
10 other side of it, which is, there's a lot of uncertainty in
11 spot market, right? It's a volatile commodity. And so, I
12 followed the direction that some of the paths were going to
13 go, was that in fact the spot market and its volatility was
14 dampening the ability of developers to put steel in the
15 ground and actually put on new generation. And I actually
16 thought that that was going to be more of a theme of this
17 panel.

18 Power plant developers want a surety of price.
19 They want to be able to get that, they want to be able to
20 operate their plant, and they want a return on capital. If
21 there's a marketability, if Blue Ridge or Alcoa will go out
22 and enter into a long-term contract for 20 years with a
23 plant developer. But the problem is that those entities
24 haven't been able to agree on price. And yet there's no
25 market construct that stops them.

1 COMMISSIONER SPITZER: What I hear from the
2 developers is they are looking for the long-term contracts.

3 MS. BIDDLE: Exact. So why do these folks not
4 have a long-term contract? Why does Alcoa -- it's because
5 they weren't able to agree on price.

6 COMMISSIONER SPITZER: Do the buyers and sellers
7 have such different views of the risk?

8 MS. BIDDLE: Yes. I think there has been a move
9 in the overall marketplace. I think there's a difference in
10 expectations. I think that there's a big part of the
11 market, it hasn't kept up with the permitting issues, the
12 regulatory concerns. Right now, one of the big issues for
13 new coal plant development, the base load development that
14 my colleagues here are talking about is, who is going to
15 take the carbon risk? I want a carbon pass-through. Or,
16 what happens with increased environmental regulation?

17 And those real costs and the impact of those is
18 what's leading to this price differential. So it's not that
19 folks can't do it; and developers, let me tell you, a 20
20 year contract at a price with the risk allocation that they
21 would like, you would have them lining up. Because don't
22 forget, they can't get those contracts at a price they like,
23 so what are they doing? They're coming to us, and they're
24 asking us to intermediate, because we are recognizing the
25 market, we are hedging out the risk for as long a term as we

1 can, and new coal plants are getting built, but they're not
2 getting built without PPAs, they're getting built based on
3 the market fundamentals.

4 So I don't think it's academic --

5 COMMISSIONER SPITZER: By market fundamentals,
6 you mean the status quo of the existing structure?

7 MS. BIDDLE: Yes. The two power plants, two
8 greenfield power plants that are being built are Plum Point
9 and Longview, and neither of those were built with 20 year
10 PPAs from industrials, or the authorities. They could have
11 been, if they were able to reach price.

12 And that way that those contracts are actually
13 being established in the market right now is that they're
14 going in and stepping in for almost like a bridge contract,
15 where it's five to seven years, and something that could be
16 unwound if they were able to get a long term contract in
17 place. Every developer wants a 20-year contract; the
18 problem is that they haven't been able to agree on price.

19 COMMISSIONER SPITZER: Mr. Ott, you wanted to --?

20 MR. OTT: Yes. I want to expand on it.

21 If you look at Duane's testimony, he was -- his
22 reference point in this sort of example, basic more than
23 anything of the perception differential. His barometer, you
24 know, 3 percent inflation over a period of time and says, "I
25 had a price here and if I look at 3 percent growth over

1 here" the guy on the other side of the table who he's
2 talking to is saying "Wait a minute, my fuel cost, even coal
3 costs have nearly doubled. I'm looking forward in time and
4 it's substantial, unknown, and what's going to happen as far
5 as my cost for environmental compliance?"

6 So he's across the table saying "Look, my real
7 costs, my costs of fuel alone have doubled. So the fact
8 that his contract price has doubled doesn't, from '95 to
9 2005, doesn't look strange to me." In fact, you see that in
10 the fundamentals.

11 MS. BIDDLE: EBC contracts have gone up 40
12 percent in the last 18 to 24 months. So just even
13 developing -- say if you look at the inputs; aluminum,
14 rolled steel, labor -- all of those have -- if you look at
15 the curves, they're just like this. (Gesturing)

16 So that is not being incorporated into the
17 analysis on long-term contracts. Not on the market side.

18 COMMISSIONER SPITZER: Mr. Dahlquist, do you want
19 a rebuttal?

20 MR. DAHLQUIST: I really would like an
21 opportunity to.

22 COMMISSIONER SPITZER: Please.

23 MR. DAHLQUIST: First of all, let me explain
24 where I'm coming from. You're talking about entities that
25 have to follow a load. We've got a load, isolated within a

1 utility. When we go out and try to get long-term contracts,
2 what I was trying to explain in my testimony is -- well, you
3 can't get more than three years. We've got to have somebody
4 follow our load.

5 Sure, we'd be happy to sign up with a contract
6 for a coal plant; in fact, we're helping build one with
7 another joint action agency. So we're doing that. But the
8 point is that we're buying power in a market that reflects
9 building a gas unit. It doesn't reflect the existing fleet.

10 And my issue is with cost, Mr. Ott, not the fact
11 that the cost is going up to build a new plant; I wouldn't
12 dispute that. My problem is with the market and how it was
13 supposed to bring us lower cost, and it was supposed to
14 benefit the consumer.

15 And what we found in our part, and that's why I
16 was saying this is kind of a different market, this
17 requirements-type full, load-following type of thing. If
18 we're just talking about an individual power plant, I don't
19 disagree with you that -- if we could agree on price and we
20 were interested in a piece of that plant, we would put our
21 money where our mouth is.

22 But we've got a whole load to serve, and they're
23 more than just Blue Ridge folks; there are hundreds of them
24 across the country, that you talked about the co-ops and
25 municipals who are sitting out there, and they're going to

1 fall off the end of a contract. A contract for a piece of
2 the unit only gives you the ability to start building
3 towards something you own and control, and that's where
4 we're going for most of our members.

5 But in the interim, and in these last few years
6 what we've seen is a market that reflects spot prices, and
7 people kind of indicate that the spot market does this --
8 the short-term market ought to discipline the long term
9 market. Well it doesn't, not in our view.

10 COMMISSIONER SPITZER: Well, I think to fill the
11 federal policy, we need to have market structures that are
12 conducive, that are competitive and at the same time
13 conducive to long-term contracts. I don't want to burn down
14 the barn.

15 Move to Mr. Pizarro's point, which I think is
16 important, which is symmetrical treatment by rating agencies
17 with regard to PPAs. I'm told by these folks that they
18 either, by attribution, permit the company to -- the revenue
19 stream, if you're going to attribute the debt so you have
20 symmetrical treatment on the balance sheet. Or in the
21 alternative, to just taking a discount feature for the debt
22 assumed, and negate the income.

23 So I'm told that the different rating agencies
24 take different treatment, but at the end of the day we have
25 to stay symmetrical.

1 MR. PIZARRO: But at the end of the day there is
2 a real impact from this; so the brief example from Southern
3 California Edison's perspective, as the debt equivalence has
4 been increased by the rating agencies on our books, we have
5 had to go out and layer in more equity on the balance sheet
6 to offset the imputed debt.

7 So there's a real cost here. Now this is --

8 COMMISSIONER SPITZER: But isn't the income
9 offsetting it?

10 MR. PIZARRO: Well, this is all ultimately being
11 passed through to our customers, and so it is increasing the
12 financing costs that our customers bear. It is having an
13 actual impact on our balance sheet; and therefore in the
14 revenue requirement that we have to recover from our
15 customers.

16 COMMISSIONER SPITZER: I don't want to get into
17 any confidential discussions you've had with the agencies,
18 but I understood the more prevailing theory now was to
19 discount that debt.

20 MR. PIZARRO: Actually, the trend has been in the
21 opposite direction. The way the debt equivalence works is
22 that they take a look at the fixed component of the
23 contract, the fixed payments, and they discount that stream
24 back; but they take that MPV and they used to take 10
25 percent of that MPV and treat it as debt. S&P moved it I

1 believe to 20 percent and the California Public Utilities --
2 or sorry, 30 percent is what S&P uses, as we understand it.

3 So the trend, overall move to take a larger
4 proportion of the discounted stream --

5 COMMISSIONER SPITZER: Was that in response to a
6 problem?

7 MR. PIZARRO: Well, that's in response to their
8 perception of the inherent risk that we are taking for cost
9 recovery of those costs ultimately.

10 Our point of view with the rating agencies, by
11 the way, has been that at least in California where we have
12 a fairly solid regulatory framework, the Commission has been
13 very responsive since the energy crisis. We don't think
14 that a 30 percent factor is adequately taking a look at the
15 risk environment; I think that's too high, it's assigning
16 too much debt equivalence. And we're in discussions with
17 the rating agencies constantly around this. But the trend
18 has been up, increasing as opposed to decreasing.

19 COMMISSIONER SPITZER: Thank you.

20 CHAIRMAN KELIHER: Thank you.

21 Colleagues? I'm happy to go, unless one of you
22 want to go first.

23 I thought that was a very interesting discussion,
24 and I want to follow up on it a little bit. Basically, let
25 me try to restate what at least some of you said; that

1 you're talking at high levels of risk. But some level of
2 risk is probably necessary for there to be an interest in a
3 long-term contract to begin with, right? If there's a
4 complete absence of risk, why would someone enter into a
5 contract.

6 But you're saying there's relatively higher risk
7 now for a number of reasons than would normally be the case;
8 so that creates more frenzied interest in a long-term
9 contract, but more risk to whose allocation to disagree on.
10 So to me that's helpful to know.

11 It's also probably true that over time, the
12 relative interest to a buyer or seller of a long-term
13 contract is going to wax or wane; in New England a few years
14 ago, there probably was a lot of interest by generators in
15 long-term contracts, a lesser interest by utilities. That
16 may be different now than used to be the case. So depending
17 on whether it's a relative surplus or lack of surplus,
18 there's going to be a changing interest in long-term
19 contracts.

20 But in terms of long-term contracts, do you think
21 they're relatively more important in the bilateral markets
22 than the organized markets? As a general proposition do you
23 think that's true? Andrew?

24 No?

25 MR. OTT: No. I actually think, again - for the

1 financially settled contracts there's an index; the spot
2 price would actually be able to be used by index. I mean,
3 most generators, as was alluded to, if you gave a generator
4 a 20 year guarantee that here's the revenue, and it was on
5 good terms -- meaning that they could manage risk going
6 forward -- they would gladly, at least according to the ones
7 that have talked to me -- gladly sell the discount against -
8 - you know, hunt for an expectation of spot, because the
9 spot could go down.

10 I mean, the point is you can walk in at a
11 certain, your return on investment, and for a period of time
12 you'd be glad to do that.

13 So I think whether that's in an organized market,
14 okay, or an area where you don't have one where it's more
15 bilaterally based; either one, there's a desire, if you
16 will, to lock in long term revenue.

17 CHAIRMAN KELIHER: Mr. Allegretti, do you think,
18 is a long-term contract, whatever value it has for new entry
19 by generators, is it equal and bilateral market roughly,
20 compared to an organized market?

21 MR. ALLEGRETTI: It's interesting, it goes to the
22 perception of what is the alternative to the organized
23 market? And again, as I indicated, I think buyers and
24 sellers in those markets, when they're deciding whether to
25 enter into long-term contracts really have to have a

1 perception about what the future is in that spot market.

2 And in regions that don't have that kind of an
3 organized market, that purely have a bilateral market, then
4 it really just comes down to: Okay, we're looking at
5 forward bilateral contracts, but again what is the term?
6 Are we looking at one year deals, three year deals, five
7 year deals? And again it's going to come down to what are
8 the things that make the future uncertain? Because
9 uncertainty is risk, and risk is monetized by both parties,
10 it's reflected in the price.

11 Which goes back to what Leslie was saying: It's
12 not an impediment to contracting, it's a divergency in views
13 on what the appropriate price is in the forward market.

14 Some of those uncertainties that I outlined in my
15 remarks, at least in the organized markets you have some
16 control over; you can help to try and lend some certainty,
17 some clarity that will help those perceptions to converge
18 and help parties to contract.

19 But there are plenty of things that you can't
20 control: Regional greenhouse gas initiatives, legislative
21 uncertainty about the future of retail choice. There are
22 things that are simply beyond the Commission's jurisdiction
23 or control; they're going to create uncertainties and
24 divergent views about the future, and that's going to lead
25 parties to desire shorter term contracting because of the

1 implications of those risks and uncertainties on the longer-
2 term deals.

3 CHAIRMAN KELIHER: You're saying that the risks
4 don't present an impediment to contracting, but they present
5 an impediment to reaching an agreement.

6 MR. ALLEGRETTI: There are costs fundamentally
7 embedded in those longer term contracts. Credit is a good
8 example. If we're going to contract for 20 years, we're
9 going to want bilateral credit support going out 20 years.
10 That gets expensive. That's, you know, letters of credit,
11 balance sheet guarantees -- I don't think that's an
12 impediment, it's just a cost. It's a transaction cost
13 associated with that alternative transaction that is avoided
14 by staying in a shorter-term market.

15 And so the question is, are the benefits of the
16 certainty of price associated with the long-term contract
17 enough to overcome that credit cost that's inherent in the
18 transaction? These uncertainties are just costs; they get
19 monetized in the parties' perceptions of the price, and it
20 becomes then a cost-benefit equation.

21 I think what you're seeing is people behaving
22 rationally in the marketplace, choosing the terms that are
23 appropriate to the costs they see in the longer term versus
24 shorter term transactions relative to the benefits. But I
25 don't see those as impediments; they're just the rational

1 workings of perceptions in the market.

2 CHAIRMAN KELIHER: From your point of view, and
3 looking at our point of view I want to see continued entry
4 into regions, if there is a need for entry, a need for new
5 generation. How do you do a long-term contract compared to
6 forward capacity markets? Is a forward capacity market a
7 perfect substitute, the next best thing; how do you deal
8 with the two?

9 MR. ALLEGRETTI: You know, I think if Gordon van
10 Welie were still here, he'd tell you about the tremendous
11 response that he's seen in the response to the first
12 capacity auction. I think there's been a strong response in
13 PJM; Andy could probably tell you.

14 I think certainly the capacity markets create
15 more opportunity for generation; they help to reduce some of
16 the uncertainty about the spot energy price, in terms of the
17 total compensation the generator will receive in the
18 organized market; and then they can -- easier to make
19 investment decisions.

20 The bilateral contract doesn't eliminate a cost
21 or a risk; it just shifts it. It moves it as between the
22 buyer and the seller.

23 And I think to Leslie's point, the more stable
24 and predictable the organized markets are, the easier it is
25 not only to make contracting decisions, but investment

1 decisions as well. And so more stability and predictability
2 in the organized market prices will lead to making it easier
3 for merchants to invest in generation without feeling the
4 need to shift that risk through a bilateral contract onto
5 the buyer.

6 CHAIRMAN KELIHER: Does the existence of forward
7 pass markets further complicate long-term contracts in those
8 same organized markets? Or does it create more of an
9 incentive to enter into a long-term contract, or mitigate
10 the risk exposure to the forward capacity market?

11 Ms. Biddle.

12 MS. BIDDLE: I don't think so. I think the
13 generators are making a decision about their view of the
14 forward capacity market and their ability to tap into that,
15 obtain those dollars, and generate a return on existing
16 generation or new build, versus the alternative of entering
17 into long term agreements.

18 So I don't; I think they're complementary. I
19 don't think it's pulled away from the ability to do long-
20 term contracts.

21 MR. OTT: I think the forward market lowers some
22 of those risk premiums. The way I view it, at least, it
23 facilitates the forward by bringing the bid asked spread a
24 little closer. Because the expectation, then, of the load
25 and the generator or the buyer or the seller converge a

1 little better because there's more certainty around what the
2 forward capacity is doing.

3 So I think what it does is more of an enabler as
4 opposed to a straggler or a substitute.

5 CHAIRMAN KELIHER: Yes, Mr. Dahlquist?

6 MR. DAHLQUIST: Mr. Chairman, we find that as
7 another added cost. I guess one of the things that we view
8 is, why should we go forward and continue to pay -- and I
9 see this as an impediment -- the spot market prices for a
10 product that isn't really costing that price. In other
11 words, you would think in a competitive market it would work
12 towards the real cost of production for a given supplier.

13 And since that's not there, we're going to pursue
14 building our own generation. And that's not necessarily the
15 best choice, if we had all our choices, but we don't because
16 we can't continue to fall off of short-term contracts, which
17 are the only kind of contracts we can get. We have to move
18 forward with that.

19 So it's an impediment for us to do a long-term
20 contract in the market because we don't know what the future
21 holds. The prices keep going up; and those prices again
22 continue to rise. And we're not talking about, again an
23 individual plant in our situation; we're talking about a
24 retirements-type contract.

25 CHAIRMAN KELIHER: Ms. Biddle, did you want to

1 add something?

2 MS. BIDDLE: I was just going to make a comment
3 about the risks embedded in the requirements-type contract
4 as well, which also gets to the uncertainty point.

5 So in the federal requirements contracts, the
6 regulatory overlay and also what is happening at the ISOs is
7 creating concern about going out tenor in that market as
8 well. And from our perspective, we would participate in
9 full requirements auctions. We would have a difficult time
10 going out beyond the three to five year period as was
11 stated, and the reasons though are all of the things we're
12 talking about in a long-term contract, which is we're
13 uncertain about some of the ancillary service charges;
14 uncertain about the overall regulatory environment, and the
15 risk allocation embedded in those, in the contracts.

16 So it is the same point, maybe a little different
17 format, whether it's a full requirements contract or a long
18 term contract.

19 CHAIRMAN KELIHER: Yes, Pedro?

20 MR. PIZARRO: Just to tag onto that, because I
21 think Ms. Biddle raises an important point; and it really
22 goes to: What is the use for the long-term contracts? I
23 really think there are two uses today. One of the uses is
24 really a financial hedging device. So whether you're a
25 customer or whoever, participant, you're looking at the math

1 between the short term and a long term arrangement, and
2 figuring out, can you strike the right balance or not or do
3 you end up with a mixture of risks and value?

4 The second bill is, in today's environment, in
5 most regions, certainly in California, we're not seeing any
6 generation, any new entry coming on line, absent a long-term
7 contract. Now hopefully that will change in the future, as
8 organized markets gain more civility and are recognized as
9 being stable by not only participants but the banks behind
10 them with the financing.

11 But in this environment, where we need the long
12 term contracts to build a new generation, then it really
13 becomes more of a question of how do we make sure that we
14 have sufficient long-term contracts with the rights for
15 responsibility on the system, in order to support
16 reliability on the system.

17 And it really think it parses it out so, it's
18 interesting to hear, as you're looking at serving a full
19 requirements kind of load. You can't take more than a three
20 or four year risk because of all these different variables;
21 that's actually what we're seeing, for example, in
22 California and other regions, as policymakers are looking on
23 the future, counting up the generators, not seeing enough,
24 realizing that we can't wait for organized markets to step
25 in; we should work in that direction but right now the long-

1 term contracts are needed. And so they're a necessity, not
2 a choice, in the sense of new entry.

3 #COMMISSIONER KELLY: I'm sorry, I have a comment
4 on everything. #

5 (Laughter)

6 Which is, California is becoming a little, also #
7 which is, everyone knows that utilities are a bid for long-
8 term contracts, and they also know that utilities are
9 fighting not to have a liquid mark LD products and tradeable
10 barret and tradeable products in the term.

11 So your ability to step in to a market maker or
12 go to a firm, for example, like Goldman, who in many markets
13 PJM will make a ten year price. It's much more complicated
14 in California to make a ten year price, for two reasons.
15 One, because the future of the liquid trading products is
16 uncertain; but secondly, even I saw to our client base,
17 "Utilities are a better bid." The utilities are pricing,
18 because of now they've created this engine, which is 'I have
19 to go out and procure' they're actually hoovering up all of
20 the new generation.

21 So it's becoming a little bit of a self-
22 fulfilling prophecy.

23 MR. PIZARRO: I'm sorry, just --

24 (Laughter)

25 CHAIRMAN KELIHER: Do you want to address the

1 overpaying?

2 MR. PIZARRO: Yes. We really love overpaying. I
3 think that's 7 billion, 8 billion a year.

4 No, I think on the contrary, we have been looking
5 to the market. We have actually been very active with folks
6 like Goldman in trying to develop some of these liquid
7 products.

8 I stuck with issues of a California policymaker;
9 and we did resist going on the path of the long-term
10 contracts as long as possible, hoping that the market would
11 step in, and it didn't, and unfortunately we were well
12 within the window of time; we had a mismatch between the
13 amount of time to build a generating plant and the time of
14 need; and we basically ran out of time, and California had
15 to flinch.

16 And I think that's similar how PJM has, the RPM
17 proposal has a backstop contracting mechanism; there's
18 basically a fail-safe built in there in case that the
19 capacity market alone does not deliver new generation, that
20 long-term contracting ability that PJM has is a fail-safe,
21 and that's what California had to pull the cord on last
22 year.

23 CHAIRMAN KELIHER: Thank you.

24 Ms. Biddle, you're the contrarian on the panel,
25 right?

1 MS. BIDDLE: I guess so. A little bit.

2 CHAIRMAN KELIHER: But you're basically arguing
3 that long-term contracts aren't as necessary as some might
4 think. But isn't it actually necessary for certain
5 generators? That might be true in an absolute sense;
6 generation might be built without long-term contracts. But
7 don't certain generators need that? Don't the renewable
8 generators, the wind developers, need long-term contracts?

9 MS. BIDDLE: Yes, and I'm not anti-long-term
10 contracts, actually.

11 CHAIRMAN KELIHER: No.

12 MS. BIDDLE: And in fact I have a different
13 opinion, too, in pure bilateral markets. Because where
14 there's no disability, no ability to allow for risk in any
15 format long term, I don't know how you as a generator-
16 developer would do anything but enter into a long-term
17 contract. If you were in the Soco market or Entergy market
18 where you have -- or SVP, where you have limited ability to
19 see into the future.

20 So I think in certain cases long-term contracts
21 are necessities for new builds; and I think when there's
22 public policy or mandates, for example renewables, I think
23 that long-term contracting is the best way.

24 CHAIRMAN KELIHER: Well, you're arguing there's
25 nothing broken with respect to long-term contracting.

1 MS. BIDDLE: You can -- everyone would love to
2 contract. So my point on the long-term contracts is that we
3 don't need to encourage them. If people met on price, then
4 the market would be very happy to bring them alongside of
5 everything that we're doing in the RTOs and the competitive
6 markets.

7 CHAIRMAN KELIHER: Sorry. Mr. Allegretti?

8 MR. ALLEGRETTI: I'll weigh in on this. I tend
9 to agree with Leslie. I think that every merchant generator
10 and his banker will tell you they need a long-term contract,
11 but I think that the need for a long-term contract tied to a
12 buyer for the regulated rate base is vastly overstated.

13 I tend to agree with you, Chairman Keliher, that
14 there probably are some technologies, some resources, that
15 if they're going to get built probably do need that kind of
16 support. Probably the best example would be nuclear.

17 I think wind is probably a poor example, and I'll
18 tell you why. Recently, Constellation New Energy contracted
19 with a wind developer in New England, a ten year offtake
20 agreement. Good as gold, take it to your bank, get yourself
21 a loan. That project is not going forward because of siting
22 issues, which I think are the largest impediment to new
23 generation development and not financing issues.

24 We're seeing a lot of new sources of capital;
25 we've seen hedge funds, private equity firms come in and buy

1 up existing plants that had no long-term contracts
2 associated with them. We see companies like FPL financing
3 new wind turbines across the country on balance sheet
4 financing. I think we've seen a lot of creative financing
5 and I think that there are a lot of sources of capital.

6 So while there may be some cases, I do think that
7 the overall case "that's dire and nothing's getting built,
8 and we have to return to some type of integrated resource
9 planning" is vastly overstated.

10 CHAIRMAN KELIHER: But is it necessary for not
11 just new entry but new entrants into the generation
12 business. One aspect of U.S. business with other countries
13 is just the disaggregation of generation market power. We
14 like that, we want to see that continue.

15 MR. ALLEGRETTI: Again, I'm back to the wind
16 turbines in New England. Start-up developer, first project,
17 long-term contract with Constellation. I don't see the
18 capital impediment.

19 CHAIRMAN KELIHER: Okay. Just a comment a number
20 of you made is contract certainty, and I think that's
21 something the Commission recognizes; I think all of us
22 recognize we need is contract certainty. It's not absolute,
23 and I usually say 'certain' not 'sanctity' despite the
24 difference.

25 (Laughter)

1 I think we all recognize the need for contract
2 certainty, but it's not absolute. The Commission has always
3 had the ability to modify contracts. I don't think we're
4 going to foreswear that.

5 With that being said, my time is out. So why
6 don't I recognize one of my colleagues, Commissioner Kelly?

7 COMMISSIONER KELLY: The risk issue of what's of
8 interest to me, and I appreciate your giving us insight to
9 the status of long-term contracts right now.

10 And as I understood your testimony, Andy, you
11 said that the primary risk area -- I think what I'm saying
12 is un-hedgeable risk -- is environmental?

13 MR. OTT: Yes. I mean that's obviously, "I own
14 nothing, I sell nothing, I'm just sort of there."

15 (Laughter)

16 COMMISSIONER KELLY: That's okay.

17 MR. OTT: Exactly.

18 What I hear the most angst created by is the, the
19 carbon legislation and additional restrictions on
20 generators' ability to perform. In the restart auction,
21 there were certain generators who really -- you know, had
22 pending environmental issues related to even -- so as far as
23 the future thing, that seems to be the largest
24 unquantifiable, unhedgeable, the regulatory uncertainty is
25 always the big one, especially retail; you try to decide

1 what is going to happen. But it seems, and those two near
2 the top.

3 Fuels. Again, fuels can be added. They're much
4 more developed markets than the ones I am involved with.

5 COMMISSIONER KELLY: Leslie, would you agree?

6 MS. BIDDLE: Absolutely. And I'll stick it
7 through to the financing markets, as well, that they'll
8 build the capital.

9 The carbon and environmental legislation overhang
10 is -- that we've had record levels of interest in debt and
11 equity. And in the power sector, there is a little bit of a
12 pause or a breath being taken right now in capital funding
13 until these issues get worked out.

14 And it's carbon, but it's also just the overlie
15 of the carbon regulation; and then as far as the --

16 COMMISSIONER KELLY: The uncertainty of it.

17 MS. BIDDLE: Uncertainty, exactly.

18 COMMISSIONER KELLY: Which is a portfolio
19 standard, or whether there will be changes to the Clean Air
20 Act, or --?

21 MS. BIDDLE: So you can go as far --ok, incumbent
22 generation, incumbent coal generation. Is it worth a lot?
23 Because it has an existing footprint and we're not going to
24 close down our existing coal, or is it worth very little?
25 Because the allocation mechanism, it's going to be an

1 auction, not an allocation; the prices that the incumbent
2 coal generators are going to have to pay is pretty
3 significant.

4 COMMISSIONER KELLY: For the CECs?

5 MS. BIDDLE: Yes. For whatever, the CERS or the
6 BERS or the, whatever the carbon offsets --

7 COMMISSIONER KELLY: Okay, well, that's what I
8 tried to get at. It's mostly carbon policy.

9 MS. BIDDLE: So that is, that's carbon policy,
10 but as it goes to the RECs, there's one school of thought
11 out there that as you address the carbon issue head on, what
12 does that mean to the RECs market? Are RECs less valuable?
13 You know, if we're somehow addressing --

14 COMMISSIONER KELLY: Well, of course that all
15 depends on what the legislation does.

16 MS. BIDDLE: That's it. So --

17 COMMISSIONER KELLY: Even if there isn't much of
18 a REC market right now.

19 MS. BIDDLE: There's not a RECs market
20 nationally, but we -- like Constellation had actually
21 stepped in, and with wind generation did go -- did not go to
22 a utility, but came to us and we bought 15 years of variable
23 wind power and RECs. We've done that in Texas and in
24 Illinois; and the question is, what's a REC worth? 15 years
25 from now. And there's this school of thought that a REC

1 actually might have much less value depending on the way
2 that we take carbon policy, and whether or not it's --.

3 So that's a pretty big swing; RECs are usually
4 valuable, they're worth however -- you know, \$43 a megawatt
5 hour.

6 COMMISSIONER KELLY: So is the response from the
7 financier to not offer financing long term because it's such
8 a great uncertainty, or is the response to offer it with a
9 big premium?

10 MS. BIDDLE: It's premium right now. First of
11 all, there are still market intermediaries, who are sucking
12 in and making -- you know, you can get a pay-down on your
13 debt in the 10 or 15 years while your contract is in place
14 or there's more visibility, then you size your debt levels
15 to those. And if not, their kind of sensitivity to the back
16 end and saying 'What if RECs? Which we now think are worth
17 \$30 a megawatt hour, are worth \$10 a megawatt hour.' And
18 you establish your debt levels on that.

19 You know, there are three pretty big questions
20 that are flowing through, again incumbent generators -- new
21 bills, when you look old, and there's almost nothing that's
22 not being -- and this is gas and coal.

23 COMMISSIONER KELLY: Daniel, do you agree that
24 that's the greatest area --

25 MR. ALLEGRETTI: I think environmental policy is

1 huge. Not only that the cap and trade and renewable
2 portfolio programs, but siting as well. Because when we
3 look out ten, fifteen years, we start to say "What's the
4 generation mix in the region going to look at so we can form
5 a view on where clearing prices are going to be so we can
6 assess the alternative.

7 Thinking about, well, are you ever going to be
8 able to build base load coal nuclear in this region, or not?
9 What kind of barriers to entry, what is the national mood on
10 climate change going to be? How is that going to accept
11 siting policy. I think all of that comes down to the state
12 level, and a lot of uncertainty there. So I don't know that
13 there's a lot the Commission can do about it.

14 But that's certainly a factor that I think makes
15 it difficult both for buyers and sellers to assess whether a
16 contract for a term of 10, 15 years makes sense for either
17 of them.

18 MS. BIDDLE: So having a National Environmental
19 card policy would be helpful, at least in a risk area,
20 almost no matter what it is.

21 COMMISSIONER KELLY: I want to ask about long
22 term forward requirements contracts. And if Duane goes out
23 to bid for a long term full requirements contract, who here
24 would respond to it?

25 Leslie and Dick. How do you think about that,

1 and how is that different from a request to finance a plant,
2 a new coal plant or a new gas-fired plant; that's Eastern.

3 MR. DAHLQUIST: Well, in a long term sale from a
4 supplier to a load, there's always going to be uncertainty
5 of demand on the load side of the deal; they just don't know
6 exactly how much electricity they're going to need.

7 But the contract can either leave that risk with
8 the load, in which case it's for a fixed quantity; or it can
9 place that risk with the seller. So their perceptions about
10 that risk, they're going to form their willingness to
11 contract.

12 Where we are entering into direct retail
13 contractual relationships with a customer, and we've got a
14 contract in place with that retail customer, I think it's a
15 lot easier for us to take a requirements position going out
16 five, ten years; and we're doing a fair number of those
17 deals.

18 Where it gets harder is when we're selling to a
19 distribution company that has a load made up of customers
20 who have choice; so leave that incumbent utility or come
21 back at any time. Those are harder to price further out,
22 because it's harder to assess what the attrition away from
23 or into that aggregated load is going to be.

24 So I think on those deals, I'm sort of with
25 Leslie, we're probably in the three to five years max range;

1 but in terms of retail contracts with individual retail
2 customers, we're willing to go out significantly further
3 than that.

4 With entities whose customers don't have retail
5 choice, we're probably somewhere in between; and there it
6 becomes more of an assessment of economic growth, and what
7 are the prospects for the region, and for that particular
8 area.

9 COMMISSIONER KELLY: Leslie, would you add
10 anything to that?

11 MS. BIDDLE: I think that -- Well, looking at it,
12 and I agree with everything Dan said -- was that in the
13 longer tenor, and you have a fixed price contract to a load-
14 turning entity -- you get away from some of the fundamentals
15 in demand response, and it's added efficiencies that you
16 would have if you didn't know that.

17 And so what we've seen is the peakiness of load -
18 - part of this is a dirt bike and home builds and size of
19 footprints and what have you -- but the peak demand of these
20 loads has gotten much peakier, which is a very hard time to
21 step into the market and the cure.

22 So the cost -- and once we enter into those long
23 term contracts if it's ten years from now, they know that
24 they have a fixed price, no one's saying "Hey, turn off your
25 air conditioning" or do some type of demand response. And

1 so it's been kind of feeding on itself.

2 So that has become -- I mean, toxic risk is a
3 pretty strong word, but it's a pretty complicated risk to
4 actually mitigate.

5 COMMISSIONER KELLY: So -- yes?

6 MR. ALLEGRETTI: I was going to comment that, I
7 think they've both described it correctly. What we've found
8 in the most recent contracts, negotiations with the
9 finalists, that the risk issue is shifting to the
10 distribution company, you essentially have a month-by-month
11 prediction of your peak, and if you go 10 percent above it
12 or 10 percent below it you get a premium for it.

13 But I guess I get back to the point that we seem
14 to not be talking about whether the price that's there
15 reflects a just and reasonable price. And I understand that
16 the risk -- there's a risk assessment by both parties, and
17 in fact if you go out for all requirements in the contracts,
18 there's a good chance they're not going to let you do the
19 SM. Or if you do, you're going to pay for it. Because
20 that's going to be inside that band, and if you drive that,
21 then you pay for it. So that's a disincentive for that.

22 I just want to keep reemphasizing that we feel
23 like the price itself needs to be looked at to see if it's
24 correct in the market, because there's no reason for a
25 supplier looking at a long term contract, to look over here

1 to a short-term or spot market transaction that he can do,
2 he's going to want to make the equivalent profits in this
3 long-term contract, in our view.

4 COMMISSIONER KELLY: Doesn't the short-term
5 market give you the long running cost?

6 MR. ALLEGRETTI: Excuse me?

7 COMMISSIONER KELLY: Doesn't looking at the
8 short-term spot market give you an idea of what the long run
9 incremental cost will be? I mean, isn't it reasonable to
10 price it based on that?

11 MR. ALLEGRETTI: I don't believe so.

12 That's, to me, ignoring all the assets that the
13 given supplier has. That's why -- we talked about the
14 differentiation between --

15 COMMISSIONER KELLY: But doesn't that depend on
16 whether you're going to build new, or sell old? I mean, if
17 you're going to build new, don't you have to --

18 MR. ALLEGRETTI: Oh, no. If you were buying from
19 a supplier, that the only thing they had was the new
20 generator they were building, certainly. But that's not the
21 folks that are buying; they've got fleets.

22 So, you know, it doesn't calculate too well.

23 COMMISSIONER KELLY: Duane?

24 MR. DAHLQUIST: He said focus supply and full
25 requirements have fleets, and Leslie and I kind of looked at

1 each other. We're one of the largest suppliers, for
2 example, in New England in a NEPOL control area where we
3 don't own a single megawatt of generation, and nor does I
4 believe Goldman, so.

5 Which means you're back on the markets for prices
6 that we don't know reflect the generation.

7 MR. ALLEGRETTI: Well, it comes back to our
8 perception. You indicated, Duane, that you were going to
9 build a generator because your perception of the market is
10 that price is too high in the organized market, and relative
11 to the cost of construction and the risk associated with
12 that facility, it's your expectation that it will be; and
13 it's therefore an economic equation for you to enter the
14 market with your own generation, and cut your costs.

15 To me that's a market working. That's sending a
16 price signal, and everybody's got their own perceptions
17 about whether or not entry makes sense in light of that
18 price. And I think, what I heard you say was that you
19 concluded that it probably does for you.

20 MR. DAHLQUIST: Yes, it does for us. Over the
21 long term.

22 And my point is that there are others in our
23 situation that don't have that option, necessarily. I mean,
24 they may not have the ability to go out and get economies of
25 scale with some other entity like them, and build a plant or

1 whatever. I'm speaking to a market that we've been in, that
2 we're going to be in until we get control of our risk.

3 So I'm sort of bringing the story to the
4 Commission, that we feel that there's a problem out there,
5 and that we think that the price in the spot market draws
6 away from a market segment that's there that vows that the
7 '92 Act is going to bring a situation where there was
8 competitive wholesale cost to buy the available floor
9 requirements, load following; we can go to the market and
10 get it.

11 And what I'm here to tell you is, we haven't been
12 able to get it; it's a volatile market, we think we're
13 paying prices that are excessive, and we will be paying
14 prices that we think are excessive for some of years now
15 until we can hopefully put in place assets which these folks
16 are talking about. And yes, it was in an assessment on our
17 part.

18 But there is a market out there that we think is
19 not being served properly.

20 COMMISSIONER KELLY: Thank you.

21 COMMISSIONER MOELLER: To follow up a little bit
22 with Duane; one thing is certain, I think in our case, we
23 can bring -- 98 percent of load factor, to say we're going
24 to be there with a large amount of load, we will be there.

25 Demand response frees up an interesting study, in

1 that if we get a guaranteed fixed price contract forever,
2 which we don't think we're going to get, we would be dis-
3 incentivized; could be responsive as a load. And I think
4 there are ways to build contracts that certainly would be
5 incentivized to respond as a load.

6 As far as building, self-supply, we've done that.
7 We look at that continually. Our preference is not to spend
8 our capital dollars building a power plant. Our preference
9 is to have someone else do that in partnership with us at a
10 price that we can afford to continue to manufacture; and we
11 look at that. We work with different vendors; what can we do
12 to work together to build a supply that suits our needs and
13 suits the needs of the market. Price is the question; we do
14 end up with a price that's just not making it for us at this
15 point.

16 MR. PIZARRO: I just want to underscore a point
17 that Dan made which I thought was a good one. He said that
18 in markets where you're looking at full requirements
19 contracts, and there's an uncertainty about retail access,
20 you're looking at a three to five year window, and I heard
21 it from Leslie, also.

22 I want to validate that, because that's also the
23 window that we're applying to ourselves as we look to supply
24 our load in California. As we look at new contracts, we
25 look at five years max; and that seems to be a time scale

1 where it would take that long to implement the whole
2 proceeding, and flip the switch on a different retail access
3 model.

4 But again, this goes back to the question of
5 reliability; that at some point you do need to support the
6 reliability for the whole system; you're no longer talking
7 about an economic hedging decision, and that's a decision
8 that needs to be made on a system-wide level, which is what
9 we've been advocating a capacity market, and kind of back
10 stop it at the lights. Or in the alternative, we've gone
11 through this transitional approach that I described earlier.

12 But it's just really interesting that we're using
13 the same time horizon in the face of that retail
14 uncertainty.

15 COMMISSIONER KELLY: Mr. Dahlquist?

16 MR. DAHLQUIST: Again, just to address the point,
17 the fact that you have a spot market doesn't disincent,
18 necessarily, people from moving forward and saying it is
19 something where, if I can agree on a contract price from a
20 supply side, and it meets my needs, certainly they have the
21 incentive to do that. They have a lot more transparency;
22 there's a lot more information about what's going on, but
23 the spot market -- back in 1999 when the spot prices were
24 high, I had loads come to me and say, "Nobody will write
25 forward contracts with me for a reasonable price."

1 In the down years, from '01 to '03, it was the
2 other side. The loads were fine, the suppliers were coming.
3 No one would write a long-term contracts, because there were
4 different expectations in the future. And it's like, the
5 fact remains the transparency doesn't inhibit; it just
6 creates an ability for people to create their own
7 expectation.

8 So this concept that somehow having a transparent
9 spot market disincentivizes rational forward contracting is not
10 absolutely not true. It may create more informed
11 stakeholders, but certainly disincentives, I believe the
12 term is.

13 COMMISSIONER KELLY: Well, as I understand, you
14 were saying it was a disincentive because you were saying
15 because it exists, somebody with a cheaper embedded cost can
16 sell there.

17 MR. DAHLQUIST: Right. The nuclear and coal
18 plants that I mentioned earlier, certainly the market -- may
19 be transparent.

20 CHAIRMAN KELIHER: Is your mic on, Mr. Dahlquist?

21 MR. DAHLQUIST: I'm sorry. The price is, there's
22 transparency but price, it's going to cause the supplier to
23 think, evaluate, "Should I even serve this load at anything
24 close to my cost of production?" And I know if we're
25 talking about the marginal market, generation has to be

1 built and it has to be covered, and we are investing in that
2 sort of thing ourselves.

3 But being transparent and the prices that are
4 there, transparent or not, whether they're just and
5 reasonable or not I think is something that needs to be
6 looked at.

7 COMMISSIONER KELLY: Thank you.

8 CHAIRMAN KELIHER: Before I recognize
9 Commissioner Moeller, I want to point out that we will have
10 time left after Phil's questions so Staff can use the last
11 15 minutes.

12 Commissioner Moeller.

13 COMMISSIONER MOELLER: Thank you, Mr. Chairman.

14 A little bit of discussion on this panel reminds
15 me of what we've gone through with transmission policy in
16 this country; arguably between 1990 and 2005 there was a
17 vast underinvestment in transmission because people weren't
18 sure where that industry sector was going. Was Congress
19 going to break up the vertically integrated utility? What
20 was the right pricing? Where were markets going? And it
21 seems analogous to where we're going with generation.

22 It doesn't surprise me that long-term contracts
23 are difficult to get because of the uncertainty of where
24 we're going as a nation with air policy generally. Whether
25 it's existing regulations or a new carbon trading scheme;

1 and I guess Mr. Brockway, I'd like to turn it to you. I
2 come from the State of Washington, so I'm pretty familiar
3 with the aluminum industry.

4 But why would anyone give you a 29-year contract
5 at a fixed price with all that uncertainty out there? And
6 you alluded to it before; self-generation seems to be
7 potentially the best option, unless that's too risky for
8 you, going out 20 years.

9 MR. BROCKWAY: The self-generation question is,
10 that's not where we prefer to put our capitol; we prefer to
11 put out capitol in building and plants; that's our business.
12 Certainly in areas where we recognize there is risk, we
13 recognize the same environmental risk in our process,
14 particularly since 40 percent of our process is electricity.

15 So we know there's risk out there, we know
16 there's a risk premium -- in fact, we understand over time
17 that the price to purchase electricity for our product has
18 gone up. So we recognize the risk. And I don't believe
19 that a fixed price contract is a fixed price contract;
20 there's always some type of formula, inflater in there,
21 there's something in there.

22 So perhaps there's a -- this is thinking out
23 loud, dangerous thing to do -- perhaps there's a way to
24 formulate in there a way to mitigate the risk. Of course
25 another way to mitigate the risk is the type of product that

1 we buy. If it's nuclear, there's no carbon risk. That's a
2 fix that could work. We can get our head around, do we want
3 to be nuclear?

4 Carbon sequestration is a big question, so what
5 do we know about that? But certainly I think we believe
6 there is a risk, there's a premium for that risk, and do we
7 need to figure out a way to work with a supplier to cover
8 that risk.

9 COMMISSIONER MOELLER: And one could say, you do
10 present a good 24/7, 365 load. But there's also a risk to a
11 supplier on that, because you lose power for an hour and
12 your pot lines freeze up, and so again there's a premium, I
13 think, to you needing power quality that is probably going
14 to cost.

15 MR. BROCKWAY: We don't typically look at it that
16 way.

17 (Laughter)

18 I think our history would say, disregarding
19 Tennessee a month ago, would say that our pot lines don't go
20 off and freeze up and the load goes away. Certainly that
21 can happen. We look at it more as the load is there all
22 the time, 24/7, the constant load; it's not swinging, and
23 that is a base load benefit to the system.

24 COMMISSIONER MOELLER: Duane, going back to your
25 earlier comments, it did kind of strike me that what we're

1 in now is a situation where, maybe unlike 20 years ago,
2 we're truly in a worldwide market for the price of natural
3 gas; and that's really setting the price of new entry,
4 because we as a society for one thing decided that it's a
5 lot easier to site a gas plant than it is to site anything
6 else.

7 So given that, I was kind of surprised at how low
8 those numbers were, coming in again for the premium of
9 certainty going out, I guess in your case ten years. And
10 your response was a market response to build your certainty
11 in that place.

12 MR. DAHLQUIST: The contracts that we've been
13 able to get have been more in the three year range. There
14 were some of our members that did sign on with investor-
15 owned utilities for 20 year requirements contracts for
16 formula-based rates. And of course that's essentially,
17 instead of -- one group of our members took the path of --
18 and one group of our members took the path of letting in an
19 IOU. You know, manages the risk.

20 And so we bring to the table in regard to the
21 question that you were just discussing, you know, load -- we
22 bring good credit; so there's some of that risk mitigation,
23 where our load is going to be there, we're not going
24 anywhere.

25 So it would seem like if a supplier were to

1 recognize that, and the suppliers that end up on our short
2 list -- if we could recognize in the price what it costs
3 them to produce, then I'd say that would be a fair deal.

4 Because the gas unit isn't -- for instance, I
5 think while driving a statistic, correct me if I'm wrong,
6 Jenny -- but the vast majority of energy in our market is
7 produced by coal and nuclear. So that's where I get the rub
8 in my head.

9 COMMISSIONER MOELLER: Sure. But again you look
10 at the age of the fleet in PJM East, it's something that the
11 average plant is 55 years old or something like that. I
12 mean, it's old, and there's a lot of uncertainty going
13 forward as to clean air regulation rules.

14 And there's a cost to that, is what I'm saying.
15 There's a big cost to the uncertainty as to where we're
16 going as a nation with policy on air. And I think you're
17 paying for it.

18 MR. DAHLQUIST: Yes.

19 COMMISSIONER MOELLER: Andy, can I turn to you?
20 Based on your experience, what's the right mix of contracts
21 and spot market?

22 MR. OTT: Well, again, there's obviously varying
23 degrees of contracts, but most of our market seems to be
24 coming in to our real-time Day-ahead markets relatively
25 protected; meaning that we're -- depending on how you run

1 the numbers, we've seen -- 15 percent of the load has seen
2 actual PJM price for down 6 percent.

3 So I think what you're seeing is, most people are
4 coming in with some kind of forward position, whether
5 they're long term, short-term is probably -- I would say
6 there some entities that want, again, 30 years deals tied to
7 a specific physical resource. They seem to be, again, the
8 public power folks seem to favor those types of contracts,
9 although I'm sure if they got to a place financially
10 settled, they would do the ones that do the best, from their
11 perspective, fine.

12 I think it's really a diversity of contract
13 lengths seem to be what people want; I don't think anybody
14 wants to lock into one contract term, with some exceptions.

15 So I think that to go back to the answer, though,
16 I think is probably less than 10 percent of the loads
17 actually seen. And I think that's probably the right
18 answer, and it guess the fundamentals of the market where it
19 creates an index that people can use to determine if the
20 deals are good.

21 COMMISSIONER MOELLER: Pedro, do you have any
22 thoughts on that correct mix?

23 MR. PIZARRO: I don't know if there's a number
24 mix, you know, a specific target. You think that a feature
25 of well working, well-implemented organized markets should

1 be a robust bilateral market around them; and so in our
2 case, for example, California did fall under the capacity
3 market implementation. I would fully expect us to continue
4 to see bilateral contracts, again now focusing on hedging
5 the financial risk and weighing the balance of terms and
6 conditions and risk allocation.

7 So I think it's a hazard to say 'Well, the mix
8 should be X or Y or Z.' It's really going to depend on
9 market conditions, what's changing out there, people's
10 perceptions of that.

11 One other comment I make, just since you raised
12 the issue of what's the risk out there on environmental, and
13 I second what everybody has said. We focused so far on
14 carbon and air in this discussion, but I would add water to
15 that, because I think it's going to be an increasing risk;
16 and in fact we're seeing that in California. There's
17 contemplated restrictions, and once they're cooling, they
18 could idle over 20 megawatts of the State's fleet.

19 We're hoping that's not the case, but I suspect
20 the water issues will rise to the forefront along with
21 carbon.

22 COMMISSIONER MOELLER: A true Westerner speaks of
23 water.

24 (Laughter)

25 MR. PIZARRO: Yes.

1 COMMISSIONER MOELLER: Somewhat related is a
2 question I posed to a couple of Californians recently:
3 What's your perspective on meeting the aggressive targets
4 the State of California has set for you on renewable
5 portfolio standards?

6 MR. PIZARRO: The good news is we're farther
7 ahead than anybody else, we're going to do at least 17
8 percent. The real unvarnished truth is that although I'm
9 confident we'll be there in terms of contracts I hand, I
10 don't think at this point there's any chance of being at 20
11 percent on a delivered electron basis by 2010. And we've
12 been saying this for a year or two now, and the main reason
13 for that is transmission, because getting transmission
14 permitted and built and paid for in that time period will be
15 very challenging.

16 Again, this Commission did a very important thing
17 with the support it provided particularly with the location
18 constraint facility framework that you've advanced; and
19 you'll see us use that for Tehachapi, and we're looking for
20 the next Tehachapi as well.

21 So I think renewables really start with
22 transmission, at least in California where the renewables
23 are going to be distant from the load centers. We'll spend
24 \$1.7 billion on Tehachapi, we spent more for other areas,
25 but that will take time in terms of layering on the

1 renewables.

2 A related comment that we're making that connects
3 back to carbon is, why renewables? And we support 20
4 percent; there are now calls in California for going beyond
5 that, to 33 percent. And our main message to policymakers
6 is: We think the problem you're trying to solve is
7 greenhouses gases; controlling bills, global warming, and so
8 we should be taking a look at the full portfolio of
9 potential tools out there and measuring renewables relative
10 to other GHG abatement tools.

11 So we're not supportive of just rushing to 33
12 percent renewables until we fully understand the cost, the
13 system reliability impact, et cetera, and importantly their
14 cost position relative to other offsets around the globe.

15 COMMISSIONER MOELLER: Thank you.

16 I guess in my remaining minutes, I'll close a
17 couple of thoughts for anyone to respond to; which is, I
18 think we as a Commission see ourselves as trying to
19 encourage long-term contracts if entities want to enter
20 them. And has that been misguided at all?

21 And the second part of that is, the certainty
22 that the Chairman related to contracts, thoughts on whether
23 it's sufficient, or your feelings on how important it is.

24 Andy?

25 MR. OTT: Certainly the encouragement or at least

1 not discouragement of long-term contracts, I think the
2 enabling features; in fact, we've already made a commitment
3 within our market and in others, setting certainty around
4 transmission planning, setting certainty around long term
5 transmission rates, we're in the 30-year type deals to get
6 the locational risk out of there.

7 And then recently the RPM -- you already have
8 done that, and I think that was a good thing to do to
9 enable, if you will. What you shouldn't do is pre-describe
10 whatever, some type of standard contract term; or for
11 instance, don't get anywhere near a certain percentage of
12 contracting. Because again, what we've learned in these
13 markets is giving participants flexibility in choice and
14 allowing them to make their own portfolio is essentially the
15 most efficient way, and certainly legislating that is not
16 the right answer.

17 So I believe from that perspective you've done
18 the right thing; and I think to encourage them any further
19 that you can is mostly just, for instance, working with
20 state colleagues on trying to deal with their retail issues
21 creates a tremendous amount of uncertainty. Probably that's
22 the biggest uncertainty.

23 COMMISSIONER MOELLER: Ms. Biddle?

24 MS. BIDDLE: I think Andy hit them all.

25 MR. DAHLQUIST: I do think that there is a

1 bilateral market out there that isn't all requirements, it's
2 different type of load that the stock market doesn't serve.

3 And I guess one other observation I'd have is the
4 issue of paying the incremental gas prices you discussed a
5 couple minutes ago, and does that bill generation. Or are
6 we just paying to have the concept of generation
7 construction? And if we're paying an increment that's not
8 doing anything, then again I say let's look at the price and
9 see if it reflects.

10 MR. ALLEGRETTI: I just talked to the thoughts in
11 my opening remarks. I think that well-designed, well-run
12 spot markets will actually foster more robust bilateral
13 markets and suggestions that I offered this afternoon, the
14 ones that certainly occur to me.

15 MR. BROCKWAY: Long-term contracts should be
16 encouraged, I agree with that; a robust, bilateral market is
17 a good thing like that. And I'll agree with Duane on, let's
18 not make payments that aren't building anything.

19 MR. PIZARRO: I'll just close with saying that
20 contracts are important; ultimately we need to connect it to
21 the purposes of, on the one hand, financial hedging which is
22 important, but let's not forget at the end of the day we all
23 have the responsibility to maintain a reliable system for
24 customers. And to the extent that long-term contracts and
25 financial responsibility by everybody in the system is

1 important, whether that's done through capacity markets or
2 through other tools, that's what will keep the lights on at
3 the end of the day.

4 COMMISSIONER MOELLER: Thank you, Mr. Chairman.

5 CHAIRMAN KELIHER: Thank you.

6 Why don't we turn to staff and use the rest of
7 the time; 12 minutes.

8 MR. O'NEIL: Duane, I have a question for you and
9 I have a general question for the group.

10 You said you're missing a choice and you don't
11 have options. And I'm wondering, what choice are you
12 missing and what options don't you have? And I heard, I
13 tried to figure out, listening to the discussion about the
14 end users arguing that the prices are too high, and try to
15 ask yourself the question why.

16 And one of them is because they can't come to
17 agreement, it's just different expectations. And another
18 one is that there is a shortage of existing sites to
19 actually build plants on, and consequently there's a
20 premium, if you control the site. And I notice Daniel
21 actually mentioned that issue to a certain extent, in that
22 wind issue in not being able to get siting.

23 So I was wondering, is there a problem in siting
24 new generation? And what choices are you missing.

25 MR. DAHLQUIST: The choices we're missing, I

1 think, are interrelated to the price. But in a sense, when
2 I'm trying to explain the choice we don't have is -- again,
3 we're full requirements customers, and that's what I'm
4 trying to represent here, is how full requirements
5 customers, load following full requirements customers;
6 meaning we can't go out and just buy a block, that doesn't
7 do it.

8 The spot market or the PJM market encourages, it
9 seems to us, suppliers to price the kind of product we need
10 at the short-term market price. And so the option that we
11 feel we need, and I don't know how you do it, I can't tell
12 you how to do it because I'm not sure what that answer is;
13 is that there is a market out there for bilateral contracts
14 for forward requirements, load following. And that means
15 that there's no way for us in the short term -- and by short
16 term I mean within six to ten years -- for a utility like
17 our members to go out and find a full requirements load
18 following supply that's reasonably priced. And they're
19 going to fall off the end of that contract and into the
20 volatility of the market.

21 And so there are options out there, and the
22 lights are going to stay on. And what we decided to do to
23 mitigate our risk is to start to build our own portfolio and
24 own our own generation; actually build it. Not pay a high
25 price to have it built, and then everybody keep saying it's

1 going to be built; but nobody's building it.

2 MR. O'NEIL: But as a matter of fact that's what
3 you'd expect somebody to do, if they thought that prices
4 were higher than they needed to be, and that is to go out
5 and build. So you're doing sort of what we expect people to
6 do.

7 MR. DAHLQUIST: Right, I am, but -- I don't think
8 you understand or appreciate that we had an opportunity the
9 others don't necessarily have; and I'm not just sitting here
10 speaking for Blue Ridge, I hope you understand that; I'm
11 speaking for all municipal loads that are sitting within
12 transmission systems, and they depend on contracts that
13 supply their every need. They don't necessarily have the
14 opportunity like we have had to work with another larger
15 agency similar to ourselves, and be able to pool our 90
16 communities and do something.

17 MR. O'NEIL: So is pooling your problem? I mean
18 not yours, but generally?

19 MR. DAHLQUIST: Economies of scale are the issue.
20 You know, it's not economical for a 20 megawatt load in the
21 middle of Utah -- to go out and build it; it's not cost-
22 effective. So they would go ahead and pay whatever price
23 they had to, or sell the system if they could sell it, if
24 anybody would buy it; it's unlikely they would. Why take on
25 a distribution system when you can sell generation on the

1 spot market?

2 MR. O'NEIL: But is there a lack of people
3 willing to offer, or is there this gap?

4 MR. DAHLQUIST: It's not the lack of people's
5 willingness to offer; it's the issue of not having a
6 contract that reflects a decent price in terms of the
7 generation cost at that time. That means we're paying --
8 we're paying the bill generation, we're paying the spot
9 price. Spot market price to incent generation of gas
10 prices. But the new generation isn't being built, so it's
11 not doing that job, right?

12 MR. O'NEIL: Well, and that gets my second
13 question: Is entry a problem?

14 MR. ALLEGRETTI: New England's my back yard, and
15 I talk to a lot of regulators, lawmakers, and I hear the
16 common complaint: Gas is on the margin, we need more base
17 load power, we need coal in the mix. And I look them and
18 say "Well, you know, every coal plant that's ever been
19 proposed in New England since 1990 was shot down on site."
20 Why would somebody try to build a coal plant here?

21 I think that there needs to be a clear
22 integration at the state level between energy policy and
23 environmental policy. And I think in most states they're
24 dealt with in separate silos, and that can create a problem
25 in terms of how you enter the market in those regions. And

1 I think a better understanding of the interplay between the
2 two is something that your state colleagues really ought to
3 look at.

4 MR. O'NEIL: I just want to clarify something
5 with Duane.

6 When you mentioned that you had decided to build
7 your own plant, was that based on PJM's spot prices, or was
8 it based on these full departments price quotes that you
9 got? Because one of the things I hear is that the price is
10 not to the liking of the buyer, but yet when I read the PJM
11 state of the markets report, I find that since 1999 it's
12 really not high enough to get new entry for a coal plant.

13 So how did you decide it was good enough for you?

14 MR. DAHLQUIST: The reason we decided to build
15 was to control our risk. I mean, we kept getting fewer
16 bidders and higher prices, and we didn't have any idea what
17 would happen in the future. The longest contract we could
18 get would be three years; We're going to fall off that
19 every three years, and in effect, the last contract was one
20 year because we were trying to figure out when's the market
21 going to be good to do the next one?

22 And so that's the issue. The way we decided to
23 control it was again to start investing in our own assets.

24 MS. BIDDLE: I think the point is correct, which
25 is the market price -- we obviously just had RPM cleared,

1 and that's in certain markets, adding an additional \$5.66 a
2 kVW-month. But for a new combined cycle, the market signals
3 in PJM have not been sufficient to actually justify a new
4 build.

5 MR. OTT: If you actually look at the spot price,
6 it's only really again, obviously gas sets price on the
7 margin sometimes, but really -- depending on where you are,
8 up to 30 percent of the price is set by gas, and in PJM the
9 price trends to be not only set by coal; obviously you would
10 expect in a market that size that much based on coal.

11 But I think the key there is the, if you actually
12 look at fuel-adjusted prices over time, they've actually
13 been shrinking. And again, the point is, the cost of new
14 entry is immense, and then you add on to that the perception
15 of Okay, if I were going to sink money into coal, what's the
16 environmental risk going forward, too? That part of the
17 equation makes it tough.

18 MS. BIDDLE: And also, I think the spot market,
19 if you think about the way the developer actually thinks
20 about it, they look at the term market as opposed to the
21 forward market. And so yes, there's been a pretty steep
22 affordation in that market, so the dollars just haven't been
23 there to entice someone to build.

24 MR. O'NEIL: Duane, without divulging a
25 confidence, what was your estimation of the environmental

1 risk when you decided to build a coal plant?

2 MR. DAHLQUIST: I don't have a dollar figure for
3 that, but our assumption is that if we were going to buy
4 coal capacity anywhere in the market, all suppliers would
5 face that same cost.

6 MR. O'NEIL: But you didn't actually quantify
7 what the potential CO2 --

8 MR. DAHLQUIST: That's right.

9 CHAIRMAN KELIHER: Other questions? Kevin.

10 MR. KELLY: Maybe a quick one.

11 When you leave the world of cost-based rates and
12 go to a world of market-based rates, if a buyer is buying
13 from a supplier with a mix of generation, most of which is
14 existing old, not necessarily new, is a long run marginal
15 cost to replace the power a just and reasonable rate, to use
16 your phrase, for a market-based rate? Or would you expect
17 to buy a slice of system as you think historically as a
18 requirements customer.

19 MR. DAHLQUIST: I think I may have made this
20 statement earlier; it would seem to us that the competitive
21 market price ought to move toward that melded fleet price if
22 you're buying it from a utility that indeed has iron in the
23 ground and is not selling from a purchaser, making from
24 something else.

25 So I guess yes, in a sense yes, we would expect

1 to see some form of that. If the utility has to go out and
2 construct, then, additional generation, of course that would
3 be mixed into that, wouldn't it. So all it seems like we're
4 doing is paying a premium to look forward and hopefully have
5 something to build. That's not happening with those
6 dollars. That's the way we see it.

7 MR. KELLY: Other views?

8 MR. ALLEGRETTI: I'll take one. I think if Bill
9 Hogan were here, he'd remind us to look for the missing
10 money.

11 When you talk about a single tiering price
12 market, you're talking about a market that is designed to
13 clear at a marginal cost price, albeit the highest marginal
14 cost. Your capacity markets actually clear at the lowest
15 cost of new entry; and so if you put the two together,
16 you've still got a missing revenue requirement that needs to
17 be made up with infer-marginal energy rents.

18 So I would reach the conclusion that yes, you do
19 in fact have just and reasonable rate in that marketplace.

20 MR. KELLY: A really quick question for Andy.

21 In terms of trying to bring together the
22 expectations of the buyers and sellers, which there seems to
23 be a, barely a mismatch according to everybody here, and
24 putting aside the carbon issues and renewable portfolio
25 issues, is there anything more that PJM could be doing in

1 terms of adding transparency or trying to match up buyers
2 and sellers who, in terms of some sort of longer term
3 product, that they're not doing now?

4 MR. OTT: One of the things we're doing I think
5 is trying to get educated and gather information. So we
6 have a couple over the next, nine to ten months, whatever it
7 is, what we were calling symposiums. We have one that
8 Commissioner Wellinghoff was nice enough to speak at, coming
9 up on demand response this week; and then we have a couple
10 on long-term contracting wholesale a week later. So just to
11 gather info and get again, the suppliers and buyers together
12 and say 'what's going on?' So that's part of what we can
13 do, and we are doing.

14 But I've also talked to others who -- sometimes I
15 find fascinating, where our folks that say "You know, I'd
16 almost like you to post a bulletin board about people who,"
17 on your web site, because I had trouble finding -- you know,
18 I'm willing to settle power, but I can't find somebody who -
19 - I don't even know who to talk to. And I understand it to
20 be the smaller players.

21 So I think we are looking at other ways we can
22 facilitate this information, at a very start. And then as
23 part of our strategic report, we're looking at is there more
24 that we need to do, say more fundamental. But I think as
25 far as an information exchange, if you will, almost like a

1 way for us to facilitate networking, which seems like in a
2 market this sophisticated you wouldn't need to do that; but
3 I heard that from at least two participants.

4 But I think probably what we will do is gather
5 the information through these symposia, and formulate plans
6 through the stakeholders.

7 CHAIRMAN KELIHER: Anything else? No?

8 Well, why don't we take a break now, and resume
9 at 2:40.

10 (Recess.)

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1 Panel 3: Enhancing the Responsiveness of RTOs and ISOs:
2 HON. MARK CHRISTIE, President, Organization of PJM States,
3 Inc.; YAKOUT MANSOUR, President and CEO, California
4 Independent System Operator Corporation; Audrey Zibelman,
5 Executive Vice President and COO, PJM Interconnection, Inc.;
6 MARC S. GERKEN, CEO, AMP-Ohio; LLOYD B. WEBB, Procurement
7 Manager, Eastman Chemical Co.; JOSE DELGADO, President and
8 CEO, American Transmission Company

9
10 CHAIRMAN KELIHER: Now we have the third panel,
11 and the focus of this panel of course is: Enhancing the
12 Responsiveness of RTOs and ISOs. We have a diverse panel
13 here, and why don't we start with our colleague, Judge Mark
14 Christie, President of the Organization of PJM states,
15 Commissioner with the Virginia State Corporation Commission.

16 Welcome.

17 JUDGE CHRISTIE: Thank you, Mr. Chairman. And I
18 know that history is appreciated at this Commission, so I
19 just have to note that Virginia is celebrating its founding
20 400 years ago this month, and therefore derivatively, the
21 United States of America.

22 Per my discussion with Mr. Moot, your General
23 Counsel --

24 CHAIRMAN KELIHER: It had some other flags,
25 though, in the meantime.

1 (Laughter)

2 JUDGE CHRISTIE: We're talking a chain of events.

3 Per my discussion with Mr. Moot, your General
4 Counsel, I've been assured that these comments will not
5 violate any ex parte rules here at FERC, and I'll be careful
6 not to discuss OPSI's opinion, under Section 206 and 207
7 against PJM on the market monitoring issue.

8 Given these circumstances, these comments will of
9 necessity be general. They also focus on PJM. We do not
10 propose any specific legal or regulatory changes at this
11 time, nor any changes to the PJM governing structure other
12 than those that we've already proposed in the manner in
13 which we cannot discuss today.

14 OPSI is comprised of the 13 states and the
15 District of Columbia which are in the PJM footprint. OPSI
16 commissions are governmental bodies created under our state
17 constitutions and statutory laws, and we are not members of
18 PJM. We are not another stakeholder group within the PJM
19 membership; just as FERC is not just another PJM
20 stakeholder, either.

21 Each of our state commissions has legal duties
22 that we must carry out under our applicable state laws, just
23 as FERC has its own legal duties to perform. We are
24 accountable to our citizens and to our elected legislators
25 and our elected governors.

1 What happens within the PJM RTO affects tens of
2 millions of people; consumers, employers and employees,
3 businesses and institutions within our states. The PJM RTO
4 has a huge impact on the economies of our states, so our
5 interest in accountability for the PJM RTO is not just
6 academic or theoretical. And I would just repeat the point
7 I made five weeks ago when I was here on the earlier
8 technical conference; those who are passionately supportive
9 of wholesale markets should understand that the credibility
10 of the wholesale markets is the key to their sustainability.
11 Otherwise, the barn burners that Mr. Spitzer talked about
12 will be out in force. So restoring accountability and
13 integrity and transparency to these markets is absolutely
14 essential if they're going to survive.

15 We realize that each RTO is organized and
16 governed a little differently; PJM is obviously very
17 different from ERCOT or the California ISO. Some OPSI
18 members are also in the MISO footprint, and members of the
19 Organization of MISO States.

20 Most industries that are regulated in America are
21 clearly under either state or federal, or explicitly
22 concurrent, jurisdiction. Jurisdiction for the electricity
23 industry, however, is less clearly bifurcated. While
24 wholesale power markets are under federal jurisdiction and
25 retail electricity service is under state jurisdiction, our

1 perception is that PJM seems to exist in an overlapping gray
2 area between state and federal oversight.

3 As state officials, we have apparently little
4 legal or regulatory authority over how PJM designs or
5 operates its markets, and apparently little if any authority
6 over how PJM is governed or managed. Yet how PJM operates
7 impacts tens of millions of our citizens, and whether our
8 states economies are healthy and can create jobs.

9 Accountability for PJM is therefore critically
10 important to our states. If states arguably have been
11 preempted by federal statute or FERC case decisions from any
12 significant legal authority to provide effective oversight
13 over PJM, how much authority does FERC itself have to
14 provide the needed oversight? How much oversight authority
15 should FERC have? How can FERC and the states together
16 effectively ensure that PJM is accountable for the effects
17 of its actions on tens of millions of our citizens? How
18 should FERC and the states exercise the oversight authority
19 they may each have in the future?

20 These are some questions that OPSI simply raises
21 today. We offer no answers to these questions or make
22 specific proposals at this time, but we hope this conference
23 is the beginning of a continued exploration of these and
24 other salient questions.

25 Thank you very much.

1 CHAIRMAN KELIHER: Thank you very much.

2 I'd like to now recognize Yakout Mansour, the
3 President and CEO of California Independent System Operator
4 Corporation.

5 MR. MANSOUR: Thank you, Mr. Chairman and good
6 afternoon, Commissioners. With a Judge on my right and a
7 lawyer on my left, I feel out of place. Can I switch seats
8 --?

9 (Laughter)

10 Let me try to address the key points raised in
11 the Commission's docket for this conference. Primarily
12 governance, stakeholder process, management accountability,
13 and results.

14 First the governance. And by way of background,
15 I haven't had the fortune -- or some may say the misfortune
16 -- I served as a senior executive under just about every one
17 of the known models for operations over the last ten years,
18 from a senior executive on the
19 vertically integrated structure, the firewalled environment,
20 to a Gridco that had both responsibilities for asset
21 management and operation, and now the ISO.

22 The ISO itself institutionally had the experience
23 of both ends of the book of governance. In the beginning it
24 was, it sounded more like 25 stakeholder board, that was 100
25 percent of the stakeholders, and now with a small 5 member

1 independent board.

2 So between myself and my institution, I think we
3 covered the whole landscape. If I can be of any help, I'll
4 try to.

5 Our corporate governance structure right now,
6 established by the California Public Utilities Code,
7 includes an independent Board of Governors of five members.
8 The members are nominated through a stakeholder process that
9 was approved by the Commission, appointed by the state
10 governor, and confirmed by the state senate. Members of the
11 Board serve staggered three year terms, and may be
12 reappointed to additional terms, but only after going
13 through a rigorous stakeholder process to be on the
14 nomination list.

15 The process provides a robust governance
16 structure that is open, transparent, independent and based
17 on significant stakeholder input. The nomination list
18 actually starts with an independent search firm that
19 prepared a list consisting of four nominations or four
20 recommendations per vacancy. So for every vacancy there are
21 four.

22 The number goes then to the stakeholder
23 committee, which is 30 people representing all six classes.
24 They vote on the nomination, and they make a rank
25 recommendation to the governor of the state to appoint from.

1 The governor makes that appointment, and then the nominees
2 go to the state senate for confirmation.

3 At this point, let me answer the question you
4 raised in this regard, as to whether stakeholder directors
5 should be considered on the ISO Boards, and my
6 recommendation to you is not. Independence of the ISO is
7 fundamental to restructuring and independence of the
8 governance is fundamental to the success of the mission.

9 Secondly, the stakeholder process. Again, this
10 is suitable -- I'm going to talk about suitable for
11 California, and may or may not apply to others. But all
12 meetings of the ISO Board of Governors are conducted in
13 accordance with the corporations' Open Meeting Policy that
14 provides for public participation in meetings consistent
15 with the general policies of California's Bagley-Keene Open
16 Meetings Act, and gives the public the greatest possible
17 access.

18 We're not talking about just public attending
19 meeting and witness; they actually are in a debate, and the
20 Board invites the public to comment on anything and
21 everything management may recommend to the Board.

22 In that process, the Board beforehand through
23 briefings and at the meetings to witnessing the discussions
24 and the debate, of the stakeholder with management and also
25 more importantly amongst themselves, they make those

1 decisions.

2 Again by way of background, when I took the job
3 at the ISO, I discovered that the 16 months before I came to
4 the ISO job, there was a stakeholder process going for 16
5 months to actually put together the process. And actually,
6 with all the issues that were in place, we didn't even start
7 to work yet, we were just talking about how we would do the
8 process to do the process.

9 So we started that, and we believe still that the
10 model of governance and the way the meetings are conducted,
11 I'm not necessarily necessitating having a formal voting
12 process or any structure other than stakeholders have access
13 to the Board.

14 Third, management accountability. In that
15 respect, you ask the question, "Well, should compensation of
16 executives be tied to performance?" I would say yes, and it
17 already is; and not just executives, but the entire company,
18 individuals.

19 To address this point, let me first summarize our
20 process for developing the multi-year business plan. It
21 starts with a lot of input from the stakeholders as to what
22 is important, and stakeholders by definition some have that
23 much stake, and some have that big stake. But at the
24 executive level and at the level of the stakeholder group.

25 We take lots of input from policymakers, from

1 utilities, from municipalities, from generators, from
2 marketers and from bankers. And really, our job is to try
3 to align our activities and our plan with policymaking,
4 public policies, regulatory policies and market needs. We
5 did not invent something on our own; we align it with all of
6 those.

7 Keep in mind how diverse they are in appearance.
8 When we go in that process, we find that 80 percent of them
9 are pretty much alike, and that's the good news. So
10 whatever plan we put in place, that is really the business
11 plan that we're accountable for; not just for our Board but
12 for the Board, for the policymakers, for regulators, and for
13 the market.

14 As for the budget, now at the basis for all our
15 performance metrics, compensation is based on the
16 performance of that plan; and that plan is very specific.
17 So this is something like demand response, it's something
18 about innovation and transmission -- it's all in that plan.
19 And it is the delivery from those products that align with
20 those policies and those needs, that determine how we
21 perform.

22 As for the budget, the annual budget is capped at
23 the level established through a stakeholder settlement
24 process, to review the priorities, assumptions and
25 activities that drive the resource allocation and hence, the

1 budget.

2 Now the last one, if I take the last minute or
3 so, is the results. After all, a business plan is about
4 managing the business, leading the people, and delivering
5 results. The delivery of the results as they compare to
6 expectation is what characterize institutional success. And
7 despite all of the things that we're saying are missing or
8 are to be improved, let me go through quickly a snapshot of
9 what we have achieved today.

10 Our operating budget is reduced by 18 percent in
11 spite of more responsibilities and products delivered.

12 The reliability cost is down by 60 percent
13 compared to 2004.

14 Investments are being made. We talked about
15 investment, is there investment? And yes, there is
16 bilateral and yes there is long term, as others mentioned
17 previously.

18 So far, about 16,000 megawatt of new generation
19 has been built in the state since 2000. By the end of 2009,
20 the total new capacity added will reach 20,000 megawatts.
21 That is almost as much as the entire BPA capacity, and twice
22 British Columbia.

23 The wholesale energy cost, normalized for fuel
24 cost, is the lowest since 1998.

25 And what about reliability? The forced outage

1 rate of generating plans has been going down year after year
2 since year 2000. The peak load of summer 2006 was 4,000
3 megawatt higher than forecast, and five years before its
4 time. Yet the grid held well.

5 Now in summary, competition is working, and the
6 system is not broken in spite of the remaining work --
7 that's a lot -- but that lot of work is not just our work to
8 do, but many others including yourself. Thank you very
9 much.

10 CHAIRMAN KELIHER: Thank you, Mr. Mansour.

11 I'd like to recognize Audrey Zibelman, Executive
12 Vice-President and Chief Operating Officer at PJM
13 Interconnection.

14 MS. ZIBELMAN: Thank you.

15 Yakout, I've been called a lot of good things
16 recently, but not a lawyer.

17 (Laughter)

18 Commission, I'd like to -- we provided some
19 comments, and I'd like to focus on two different things.
20 One is in terms of how RTOs are governed, and the issue here
21 is how do we govern ourselves relative to other corporate
22 organizations in terms of accountability.

23 One of the things we laid out in our testimony
24 that we looked at, and I think in talking about it to the
25 other RTOs, fairly consistent, is we looked at the Sarbanes-

1 Oxley requirements, we looked at the New York Stock Exchange
2 listings, and we've looked at the National Association of
3 Corporate Directors to see what you should do in terms of
4 setting up governance and accountability for an organization
5 for people invested, and we're generally in conformance.

6 These involved such things as financial
7 responsibility, fiscal recording, accountability, fraud
8 prevention, fraud detection, making sure that you have goals
9 that are in line with the corporate initiatives, assuring
10 that you have your compliance with your regulatory
11 requirements, and assuring that there's a good relationship
12 between Board and Management so that the Board is well aware
13 of what's happening in Management.

14 And in our prefiled testimony, we talk about the
15 various elements that are looked at by these various
16 agencies to see if in fact what is best practices for
17 governance, and how we rank against them. I won't go
18 through them in detail.

19 Actually, the results speak for themselves. From
20 PJM's perspective, we dropped our rates by 46 percent since
21 2003. We were at a high of 48 cents in terms of a bundled
22 rate in 2003. This year we're looking at something on the
23 order of 28 cents. This is after the refund that we do
24 under our stated rate, and next year we anticipate dropping
25 it again.

1 During this period we added economic planning,
2 long term FTRs, RPMs; so services are increasing but costs
3 are going down, just because of focus on cost reduction.
4 And the recognition that we have from our members about
5 their concern about maintaining RTO costs.

6 In addition, our membership has grown from
7 roughly about 300 to 500, so we have a broad-based
8 membership representing -- all sectors of the industry that
9 appear in front of you, and a number of sectors that
10 probably don't appear in any regulatory proceedings but
11 trade actively in the markets.

12 We also have substantial auditing requirements in
13 addition to the traditional NERC audits and traditional
14 internal audits, we have a SAS70 audit that we complete
15 which manages all of our control systems.

16 So all of these things are designed because it's
17 very important, as Commissioner Christie said, people are
18 depending on the accuracy of our numbers and so it's very
19 important that we have an auditing process and control
20 systems so that our rates are accurate, our bills are
21 accurate, and our settlement processes are accurate, since
22 our members rely on us for their own statements of fiscal
23 understanding.

24 And then in terms of the governing section and
25 our employees, we also have a goal setting process, it's an

1 annual goal setting process that is geared to looking at
2 stretching goals and what we need to do to meet our
3 reliability operations, market operations, FERC goals, et
4 cetera, and that we have payment at risk starting at the
5 highest level; we have more than 60 percent of our pay at
6 risk, and then tiering down, but that all of our employees
7 are set with the same goals, and every year those goals are
8 audited for performance by the Board to make sure that if
9 there is a payout under the goals, that is auditable and
10 clear.

11 So that's sort of everything that one would
12 expect a well-run organization to do, and I believe that we
13 and all the other RTOs are looking at Sarbanes-Oxley and
14 these requirements, and even though we're not sort of
15 trading companies, we're trying to model that perspective.

16 The other piece of this is, you know, I'm pleased
17 to say that PJM is a double A rated utility, and that we've
18 had clean audits every year since we've been in operation.
19 So I think in terms of that that the Commission should feel
20 confident, our members can feel confident that the
21 organizations are being run well.

22 The next question is, is that in terms of how are
23 we going to deal with the issues of the stakeholder
24 involvemenet and stakeholder participation; and that's
25 really to me the nub of it, because of the fact -- we're

1 unlike shareholder companies, where in fact the shareholders
2 are really interested in one thing is the return on their
3 investment, we have shareholders our stakeholders do
4 represent the broad perspective of the entire market. And
5 what we find is that the most difficult issues are the
6 issues around market in terms of free operations.

7 That's not really where the debates are in terms
8 of reliability and what you need to do in reliability; it's
9 really market design, market development, market rules. And
10 with that, what PJM has been focused on thinking about, and
11 where the stakeholders have been focused on, is how do they
12 make more accessibility to the Board? How do they know that
13 the Board is being sponsored to the stakeholder meetings?

14 We don't think that hybrid boards make sense. In
15 our own case, all our Board members have to have certain
16 requirements; they have to be representative of all sectors
17 of the industry, but they have to be independent. So what
18 we try to do, say we try to achieve what you want to do from
19 that hybrid board is make sure your people understand the
20 industry, but are not fiscally -- are fiscally independent
21 of the individual members.

22 And we also have the nomination process so that
23 actually up to a third of our Board can be renominated every
24 year, and that almost four-fifths of the Board is to be
25 renominated every two years. So the stakeholders can vote

1 poor members our if they don't feel like they're doing their
2 job.

3 The issue that we've been working with with our
4 members, and we continue to make progress on this, is that
5 when you have 500 members, how do the members get the access
6 they want to the Board? And things that we're looking at is
7 that, things like more written communications, more Board
8 activity at individual meetings, and last week we suggested
9 to our members based on some suggestions they made, that we
10 would establish a liaison committee that would be able to
11 work more directly with the Board.

12 Again, when you have that many members, it's very
13 difficult in a meeting setting to have the level of dialogue
14 that the members want to have.

15 So in our perspective, Commission, is that I
16 would agree with Yakout, having a stakeholder board would
17 actually probably compromise independence. That is really
18 the struggle, because you want the Board to be accountable
19 but you don't want the tyranny of a majority or as I would
20 say, the tyranny of the loud, for the people who are always
21 there. You want the Board to be able to be informed. We
22 want the Board to be in a position to let the members know
23 that they're informed, and then for the Board to make a
24 decision like anybody wants to make, on the best information
25 that is representative of their objective, which is of

1 course to maintain reliability and create robust,
2 competitive markets; not necessarily to achieve a certain
3 outcome for a particular member segment.

4 So with that, that's sort of where we are, and I
5 look forward to your questions.

6 CHAIRMAN KELIHER: Thank you.

7 I now recognize Marc Gerken, the CEO of AMP-Ohio.

8 MR. GERKEN: Good afternoon, Mr. Chairman and
9 members of the Commission.

10 AMP-Ohio is a nonprofit corporation that was
11 organized in 1971, which is comprised of 120 municipal
12 electric systems in Ohio, Pennsylvania, West Virginia,
13 Virginia and Michigan. Those 120 members comprise about 35
14 megawatts of peak load. AMP-Ohio owns, operates generating
15 facilities, provides wholesale generation and transmission
16 services, as well as coordinates and develops power supply
17 strategies as well as transmission interconnection.

18 AMP-Ohio wants to thank you for holding this
19 series of conferences to examine the current state of the
20 competition in wholesale markets. We appreciate the
21 opportunity to testify before you today.

22 Currently, AMP-Ohio purchases approximately 85
23 percent of its needs on that market. And as Andy Ott said,
24 that the majority of the people are between a little less
25 than 10 percent of that spot market we, after 2005 being at

1 10 percent, are now at 2 percent, just to give you an idea
2 of that market.

3 Accordingly, AMP-Ohio remains very concerned
4 about market structure as well as the market procedures, and
5 process for both MISO and PJM, who we deal with.

6 To sum up this concern, I ask you to recall an
7 analogy made by Chairman Wood during his tenure at the
8 Commission. Specifically, Chairman Wood said that 'public
9 power is the canary in the mind.' When it comes to
10 organized markets, in short, public power entities will be
11 the first to judge whether these organized markets are
12 working. Well, the canary is on life support, I have to
13 tell you.

14 And if you are familiar with APPA's Emory
15 efforts, I think you can read that well into that life
16 support system.

17 Let's consider the first question asked of this
18 panel: Are RTOs and ISOs designed to address adequately the
19 interest of their customers?

20 One needs to step back, however, and reassess two
21 other fundamental questions before answering that question.
22 First one was to identify the real customers of these
23 regional entities. I maintain the true customers of RTOs
24 and ISOs are load serving entities represented by a variety
25 of stakeholders.

1 Let me be perfectly clear that the customers of
2 the RTOs and ISOs are not the asset owners -- meaning the
3 transmission owners or the generation owners -- nor are they
4 the management of the RTOs or the ISOs.

5 Second, one must reaffirm what the true goal of
6 enabling wholesale competition is. To put it another way,
7 what is the RTO's real job? I would submit that the
8 establishment of regional markets is a means to the end and
9 not the end itself. Elaborate and complex structures that
10 don't ultimately provide real benefits to customers are not
11 what LSCs need. To truly serve customers, market structures
12 must ensure that ultimate customers pay just and reasonable
13 rates for reliable service.

14 In short, the goal of enabling competition is to
15 achieve just and reasonable rates for the true customers of
16 RTOs and ISOs. I do not believe that the current organized
17 markets have adequately served the interests of the
18 customers.

19 New initiatives are continually promoted by MISO
20 and PJM despite almost unanimous opposition to stakeholders
21 other than the TOs and TOs.

22 What action should the Commission take within its
23 jurisdiction to address these issues?

24 First of all, I would encourage the Commission to
25 take action on three broad areas. First, FERC needs to

1 address further RTO, ISO administrative costs through the
2 implementation of measures previously supported by AMP-Ohio
3 through TAPS in Docket No. ER04-12. Specifically, FERC
4 should establish benchmark RTO and ISO costs, conduct
5 biennial cost/benefit analysis by states, require a
6 cost/benefit assessment of major new initiatives, and
7 require stakeholder review of the RTO budget process prior
8 to its adoption.

9 Second, the governance of the RTOs - ISOs must be
10 changed. Specifically, FERC should modify RTO governance to
11 require hybrid boards that include a balanced stakeholder
12 minority, without current RTO-ISO management representation,
13 either.

14 In addition, FERC should work together to
15 establish a more robust Board election. Multiple
16 candidates for open board positions, individual candidates
17 subject to an up and down vote, no slate voting, elimination
18 of the self-perpetuating board model.

19 In addition, all stakeholders should receive more
20 tools for direct communication with this hybrid board.

21 Third, FERC should go slow on the major RTO-ISO
22 initiatives. For example, MISO's ASM as well as PJM's
23 GridSmart should not be allowed to proceed until the
24 majority of available potential benefits from ISO Day 2
25 markets have been captured by customers, not asset owners.

1 If the potential benefits from these last major
2 initiatives are not realized, FERC must be prepared to step
3 back, even perhaps to limits on the use of the uniform
4 clearing price, LMP, and the Day-2 market itself. I would
5 also encourage the Commission to consider whatever
6 recommendations are produced from EMRI's Phase II efforts
7 that will clarify a lot of recommendations from your
8 previous work.

9 I thank you very much and look forward to your
10 questions.

11 CHAIRMAN KELIHER: Thank you very much.

12 I now recognize Mr. Lloyd Webb, Procurement
13 Manager of Eastman Chemical Company.

14 MR. WEBB: Good afternoon. First I'd like to
15 thank the Chairman and Commissioners for the opportunity to
16 speak today.

17 My name is Lloyd Webb, I'm Procurement Manager
18 for Eastman Chemical Company, which is headquartered in
19 Kingsport, Tennessee. Eastman is a Fortune 500 company with
20 2006 sales of \$7.5 billion and approximately 11,000
21 employees. We manufacture and market more than 1200
22 chemical, fiber and plastic products worldwide. We have
23 facilities in PJM, SPP, ERCOT, and SERC. I'm also appearing
24 here today as ELCON's Chairman.

25 In the mid-1990s, ISOs and later RTOs were

1 established with widespread support in regions of the
2 country with high electricity rates. ISOs or RTOs were
3 promoted as a platform for competition that would bring
4 consumers lower rates, choice, and product innovation.

5 An important measure of success for a competitive
6 market is the degree to which it is self-regulating, This
7 means that the need for regulatory intervention is greatly
8 minimized. Not altogether eliminated, just minimized.
9 Markets that require frequent regulatory intervention are
10 considered market failures.

11 An unusual feature of ISOs and RTOs was the
12 addition of a quasi-regulatory, quasi-advisory stakeholder
13 process to the governing structure. In every ISO or RTO
14 that was established and approved by FERC, the determination
15 of a balanced stakeholder process ws a long, drawn out
16 battle of competing interests. These battles continue today
17 at great cost to consumers.

18 There are a few examples of markets that allow an
19 ad hoc stakeholder process to literally dictate the manner
20 in which business is conducted. While certain financial
21 securities markets were created as self-regulating
22 organizations, there has been no congressional authorization
23 that gives the ISO or RTO stakeholder processes the same
24 market oversight rights.

25 No existing FERC-approved ISO or RTO stakeholder

1 process consists of balanced representation between supply
2 side and demand side interests. All stakeholder processes
3 are skewed in favor of supply-side interests. While the
4 interests of supply-side participants are diverse on many
5 supply-related issues, it is not so diverse on issues of
6 importance to demand-side interests, and we often see
7 supply-side interests quickly converted to unanimity on
8 these issues. Thus, supply-side interests can often stop
9 any initiative with strong demand side support, but demand
10 side interests cannot stop any initiative with strong
11 supply-side support.

12 While it is true that ISOs and RTOs were
13 established as more-or-less nonprofit entities to ensure
14 independence from any market participants, it is clear that
15 ISO or RTO management may be increasingly aligned with the
16 commercial interest of some market participants. In order
17 to protect their interest, generators and ISO/RTO management
18 increasingly share the same need to talk up the benefits of
19 the markets, as consumers consistently question the presence
20 of these benefits.

21 There is often a high cost to consumers of not
22 participating in the stakeholder process. Yet, when all
23 stakeholders are at the table, they may never agree on any
24 important matter; and when they do agree on something, the
25 ISO/RTO Board may override them. Thus, our participation

1 tends to be for defensive purposes only.

2 It is not clear what the role of the ISO/RTO
3 stakeholder process should be. Is its role advisory or was
4 the intent a subtle delegation of FERC's regulatory
5 functions? An exclusively advisory role would make
6 stakeholder groups develop a consensus view on any issue
7 with minority views made public as well. The actual
8 decision making would reside at the ISO/RTO Board, but an
9 exclusively regulatory role can always be preempted by the
10 ISO/RTO Board. There may be no difference, except in the
11 expectations of the stakeholders themselves, and these
12 expectations, impact the quality and quantity of
13 participation.

14 While the RTO stakeholder process in most
15 instances would work satisfactorily on incremental changes
16 or enhancement to RTO rules, it tends to break down on more
17 critical threshold issues.

18 A couple of examples. The Midwest ISO
19 Stakeholders' Advisory Committee overwhelmingly rejected the
20 proposed Ancillary Services Market by a vote of 19 1/2
21 against 3 1/2 abstentions. MISO overruled, and the proposal
22 went through.

23 PJM recently had an experience with the RPM,
24 Reliability Pricing Model, which did not receive the super-
25 majority required; but as we all know, that proposal was

1 pushed through by management and went into a costly
2 settlement process; and they eventually have to be resolved
3 by a federal court.

4 In relation to the questions asked by the
5 Commission following our recommendations, first: Clarify
6 the role and rules of the stakeholder process, require
7 stakeholder balance between the two sides of the market, and
8 establish a super-majority vote requirement.

9 Secondly, to promote greater accountability, FERC
10 should consider adding stakeholder representatives including
11 consumers to each ISO and RTO board. Supply side and
12 demand side representation on the board must be balanced.

13 Thirdly, FERC should consider the scope of each
14 ISO or RTO's authorities, and whether the vertically
15 integrated industry is functionally being reassembled at
16 each ISO or RTO. The ISOs and RTOs are increasingly
17 replicating the wholesale functions of the vertically
18 integrated utility. They also must not evolve into a third
19 layer of regulation.

20 Next, stakeholders must have adequate access to
21 ISO/RTO management and their boards. Lack of access by
22 stakeholders leads to decision making in a vacuum. We
23 applaud PJM's recent efforts to improve this level of
24 access.

25 Finally, use the settlement process as a last

1 resort and not as a default decision-making process.
2 Consumer interests do not have the resources to be effective
3 in the settlement process and are overwhelmed by supply side
4 assaults.

5 In conclusion, we recommend a FERC dedicated
6 conference to the series, including additional examination
7 of the stakeholder process and how it operates.

8 Thank you for this opportunity.

9 CHAIRMAN KELIHER: Thank you, Mr. Webb.

10 I now recognize Jose Delgado, the President and
11 Chief Executive Officer of American Transmission Company.

12 MR. DELGADO: Thank you Mr. Chairman. Thank you
13 to all of you, and I'm going to be very focused in my
14 comments. There's a paper outside that is also intentionally
15 short.

16 American Transmission Company is a transmission-
17 only company within MISO. And I'm going to talk about the
18 need to revisit the governance of MISO. Now, I am very well
19 acquainted with MISO, and it is my impression that my
20 comments might be applicable to all this, but I cannot
21 guarantee you that.

22 It is not surprising the original council, the
23 councils, that the ISOs do have different backgrounds and
24 have different problems. You know, the Upper Midwest never
25 had joint operation of units, like they had in PJM and other

1 parts of New England and New York.

2 As a consequence, I think you will find that the
3 Midwest ISO began behind in the sense of comfort with joint
4 operation. And this I think is at the root of what I'm
5 trying to address. I think this is a very serious issue
6 that has to do with the governance, and the ability of this
7 organization to function; and I will try to be very plain
8 and simple.

9 As I say, I was one of about 20 or 30 executives
10 who worked for about three years, trying to form the Midwest
11 ISO. When it came to the point of filing it, only five of
12 us were willing to go ahead, and we did. And since then we
13 have been working very hard to make it happen. I am a fan
14 of the Midwest ISO, and I was and I continue to be a great
15 supporter. My intention is to make sure that it is
16 effective.

17 When we put it together, we had a very clear idea
18 of having a very narrow focus in our organization that can
19 operate the system. And the main reason was that since the
20 opening of the network for open access, that were being
21 affected by phantom flows, we used to call them. These are
22 the loop flows; nobody knew where they came from or where
23 they went. It's like a biblical wind.

24 And the problem is that it was creating some
25 havoc with the ability to operate. I have said that none of

1 us was big enough to know who was doing what to whom; and we
2 needed somebody to help us.

3 Well, we put together the ISO with that very much
4 in mind, and we intended for it to be a very serious
5 operator, because this was with that. I'm very happy to
6 tell you right now that in my assessment the ISO, after what
7 I would call a sputtering start-up, MISO is now an excellent
8 operator. I would say the help that MISO provides to the
9 system operations is everything we expected, and I expect it
10 will continue to improve.

11 Sometime in the middle of start-up, FERC request
12 that MISO begin to operate. And MISO in fact has had Day 1
13 and Day 2.

14 I will not comment on the effectiveness of the
15 market because our company does not buy or sell. But
16 regarding reliability, I will tell you that regardless what
17 happens in the economics of the market, your joint dispatch
18 of generation is a fantastic input to the reliability of the
19 system. As a consequence, I would say it has had a
20 tremendous beneficial impact on the operation of the system.

21 It is very apparent to us that there has been a
22 bit of a 'scope cree' in the scope of MISO, and this is
23 serious, because the fact that is that along with it comes a
24 start-up cost, and the credibility of this organization.

25 The concerns regarding scope and cost is what is

1 threatening the viability of the organization, because state
2 regulators are questioning whether MISO is worth the money
3 that we're spending on it. This is something that begun,
4 I'd say from the beginning; and it is becoming more and more
5 of a crescendo.

6 And it is something that in fact will have an
7 impact on the ability of MISO to continue to grow, to
8 operate, or to stay together. I am convinced that we're
9 talking about both focus and accountability, and I would
10 like to basically address a way of addressing it; basic,
11 basic governance.

12 As I put it here, I am proposing that there ought
13 to be a hybrid board of MISO. And in fact, there will be
14 three individuals who are heads of, or CEOs of load serving
15 entities that were part of the Board. When we formed the
16 MISO Board, we put ten people who were independent, one of
17 them happened to be the president, and the fact is that they
18 are extremely capable and have done tremendous work to make
19 it happen. On the other hand, there is a touch of reality
20 which is missing here, and I would say this is in fact what
21 is at the point of great critically here.

22 Let me put it this way: It is the load serving
23 entities that bear the bulk of the cost of MISO, or 95
24 percent of the cost of MISO goes to them. For example, our
25 company bears a very minute cost, because we do not have, we

1 don't have any obligation for load. And remember that that
2 is recovered through this Commission.

3 The state commissions have to approve what those
4 utilities are doing. Those utilities that bear the bulk of
5 the cost are facing the reality that they must either
6 convince the Commission that it is worthwhile, or not being
7 allowed to recover.

8 To give you an example, there was utilities that
9 serve load, of not being allowed to recover from rates, the
10 cost of starting up MISO. Accumulated cost right now, which
11 have been accruing, it's in the tens of millions of dollars;
12 which for those utilities is a very significant issue.

13 The commission has said that there is no reason
14 why they shouldn't recover except they would like to show
15 that it's worth it; and the utilities right now are working
16 very hard to be able to show the benefit of MISO, and the
17 fact that it's worth the money.

18 The fact is that MISO cannot justify its own
19 cost; it has no standing at the commissions. The fact is
20 the utilities have to do it. And if there comes a point
21 that the state commission will not allow a utility to
22 recover the cost, they would have not only the right but the
23 obligation to leave MISO.

24 We all know that already the utilities, at the
25 behest of the commission, left MISO. What happens when

1 entities like that leave MISO? The costs go up and the
2 benefits go down because the benefits of MISO, depend on how
3 many people are in it.

4 As a consequence, what we have here is
5 potentially what I have called "the race to the door."
6 Which would be the
7 organization that is having some very significant benefit to
8 the operation of the network; and I would have to say that
9 it's trying to bring to the occasion an open market that in
10 fact would be, should be very, very effective.

11 By having those individuals, in fact I believe
12 that we will be putting into an independent board a touch of
13 reality by people who have a very unique accountability. So
14 you may ask: Why only those individuals or CEOs who bring,
15 who are accountable for load.

16 I would say first of all because of our unique
17 relationship, they, their companies are accountable for the
18 bulk of the cost of MISO; number two, they themselves have
19 the obligation to justify it. There's direct accountability
20 to the state commission. MISO cannot do it. And three,
21 because they do have the authority to leave MISO.

22 In fact, these are the people who have the
23 ability to say "This is not worth it. We're getting out."
24 And at some point, it may have the obligation to do so.

25 By having them out front, do we jeopardize the

1 independents; and the answer to that is no, for about three
2 very good reasons. The first one is that the majority of
3 the directors have been independent, and the majority rules,
4 and that takes care of it.

5 The second one is that I believe that the
6 governance of MISO is and should be quite often as a
7 consequence, it prevents manipulation of anybody who might
8 want to do it; the quality of the Board is very high.

9 The third is that if MISO is as focused as it
10 ought to be, and I haven't had a chance to expand on focus
11 because I think it's terribly important; and I'll give you
12 an example of an organization of great importance and much
13 success, which is INPO. Which in fact will not take on
14 anything but a very narrow target of a very important goal.

15 I would say go the market and, help has the same
16 characteristics as you might put in there. If in fact it's
17 so narrow that in fact the controversies would be very, very
18 few.

19 I can speak from experience about the value of
20 hybrid board. The company has a hybrid board. We act
21 independent, nobody can say we're not from the experience of
22 many years; nobody has been able to say otherwise, but we
23 have the benefit of people and fact who bear significant
24 accountability for the cost of what we do.

25 In summary, I think that having the Board in fact

1 will increase the credibility of MISO, will increase the
2 accountable of MISO, will help MISO to focus specifically on
3 the things that are worth doing, and in the few things that
4 it does.

5 I believe that MISO will need help from this
6 Commission, and the other state commissions to really remain
7 focused, because MISO looks like an Christmas tree;
8 everybody can hang something on it when they go by. It's a
9 convenient organization for them to do things. I would say
10 that the failure of MISO will be totally guaranteed if we
11 can in fact try to make MISO something it has no authority
12 or availability to do, such as being a super-regulator.

13 Put that aside, that's not the point. I would
14 like to think that this Commission will be seeing something
15 from the MISO members. I would like to think that it is
16 possible for this Commission to encourage that. And I am
17 not so sure that it applies to the other ISOs, so I am going
18 to say at this point, I apply directly to MISO, I'm
19 convinced of that.

20 CHAIRMAN KELIHER: Thank you.

21 Why don't we go with 15-minute rounds. I want to
22 thank all the panelists for their comments. I'll start on
23 this one, then turn to my colleagues, and then if there's
24 time left, have Staff ask some excellent questions.

25 But it's an interesting subject. This is

1 something that I've had an interest in since fall of '04,
2 when ATA issued its white paper, and I thought that was a
3 very important work, and I think it raised some serious
4 questions.

5 And as Mr. Gerken said, when a public power is
6 asking questions are they benefiting from the organized
7 markets, that's a pretty serious matter. But to me again,
8 really look at RTO and MISO governance and accountability,
9 let's start off with well, what is the RTO, what is its
10 nature, what's it do? And that's an interesting question,
11 because it really is unique in the electricity business;
12 it's not unique in the outside electricity business.

13 But at least a Day 2 RTO, it's sort of half
14 nonprofit utility and half commodity exchange. So it's
15 really half New York Power Authority and half New York Stock
16 Exchange, and that's kind of an interesting combination,
17 really. How do you get an institution like that to operate
18 efficiently?

19 Unlike the New York Stock Exchange, though, an
20 RTO is not a self-regulating organization. I just want to
21 reiterate that; whenever that comes up, I want to mention
22 that. They are a FERC-regulated public utility.

23 Now if you get white papers, it's a big meeting,
24 it's an important work, and I did ask the question: By
25 insisting on complete independence by RTO Boards do we end

1 up with isolated RTO Boards? It seemed like APPA was
2 raising the question that RTO institutions may actually,
3 their focus may be to serve the market rather than serve the
4 members, serve the customers, and that that focus was
5 misplaced; and there was also concern that if in the, by
6 insisting on complete independence, which is something the
7 Commission did, do we end up -- I'm trying to state it in a
8 way, crudely, and not trying to offend anyone; but today's
9 concern was do we end up with a Disney board? Do we end up
10 with a board that's independent of market participants but
11 dependent on management.

12 And the hard thing is, well, if that's the evil,
13 that's what we're trying to work against, we don't want the
14 Disney board; and as RTO and ISO boards, how do we prevent
15 that? I think it's hard to write a rule that would self-
16 execute and prevent -- you know corporate America, could you
17 ever write a rule to prevent the Disney board ever from
18 being reestablished as a public corporation? Probably not.
19 You prevent it by voting off people who in practice could be
20 too close to management.

21 Now, different governance models can work.
22 That's probably another thing a number of you -- I don't
23 think there -- is there one perfect governance model for all
24 RTOs and ISOs. I think the reality is probably true if
25 there's different governance models.

1 I think we want RTOs and ISOs that have a focus,
2 that they're serving the members, they're serving the
3 customers, they're not serving an abstraction, open market.
4 That market enhancement does what the members want, the
5 customers want, and those are things that they should
6 pursue.

7 Now, a nonprofit utility, there is accountability
8 in a nonprofit utility. It's because the board of a utility
9 is elected officials, and they will react when prices get
10 too high. So there is accountability in the nonprofit
11 structure.

12 How do you get cost accountability? How do you
13 really get true attention to cost from an entity that's
14 nonprofit? It can be done, but I don't think it's easy. I
15 think some of the RTOs, they've taken a good step, they've
16 had state rate filings that they've submitted to the
17 commission, and I think that's a good thing. They're
18 basically saying "we can predict, we can control our
19 administrative costs, and are willing to prove that."
20 But there's other costs that they have much less control
21 over. Those costs get passed through.

22 So I'm obviously starting with a statement, and I
23 actually do have some questions. Before I get to questions,
24 I want to point out there are limits on what the Commission
25 do. There are legal limits on our ability to address

1 governance issues. We lost the CalISO decision, and it was
2 actually a pretty bad loss, the court's language was pretty
3 strong. So I think there are limits on our ability to
4 address the governance issue. I think we should probably
5 recognize those limits, but I think given the nature of the
6 customer concerns, we have to act, with a view that there's
7 not probably one perfect solution in mind.

8 I do have some questions. I am still not
9 convinced that the hybrid board doesn't have merit. If you
10 look at those other institutions, the commodity exchanges,
11 one-half of the RTO brain, if you will, They have tried
12 different models. You have the New York Stock Exchange of
13 course had a completely stakeholder board until some recent
14 events, and they dropped it for a completely independent
15 board. In part that was based on a lack of confidence by
16 New York Stock Exchange-listed companies in the management.

17 Now NYMEX still has a stakeholder board, I
18 believe; I'm not 100 percent sure. Are they --

19 MS. ZIBELMAN: I think now they're public. They
20 don't have an independent board.

21 CHAIRMAN KELIHER: NYMEX has an independent
22 board, because they went --

23 MS. ZIBELMAN: Public.

24 CHAIRMAN KELIHER: Okay. And then the SEC had a
25 proposal for NASD to be a hybrid board, with -- the

1 stakeholders have a minority role.

2 I guess I still don't see why a hybrid board
3 doesn't have some virtue. When the APPA report came out, it
4 raised the question: How does FERC make sure that RTO costs
5 are reasonable? Part of it is the traditional cost of
6 service tools don't fit RTOs very well.

7 If FERC had to, it could figure out what should
8 be on every line of a gas pipeline's budget. It would take
9 us a while, but we could probably figure it out; what's the
10 perfect rate for a typical, for a given gas pipe line. Your
11 costs are much harder for us to -- it's much harder for us
12 to say what should PJM's software cost be five years from
13 now, or last year or this year? The nature of the cost made
14 it difficult to use the traditional cost of service tools.

15 I think the typical ratemaking tools don't quite
16 fit, so we have to really look at more like more governance
17 approaches to assure accountability.

18 Stated rate is one; hybrid board, I still, I'm
19 not convinced why that doesn't have some virtue. I agree
20 that a large Board is unwieldy; I mean, the 25-member
21 CalISO board you could probably conclude one reason for the
22 failure, that the board at the time was -- without saying
23 anything about the Board members who sat there at the time,
24 it was just the sheer size. 25 is large for a board. I
25 think it's probably difficult for an organization that large

1 to make pretty crisp decisions.

2 So you could see a hybrid board, not necessarily
3 larger than the current ISO and RTO boards. I'm not quite
4 sure why that doesn't work. It can work in other contexts.

5 And Audrey, can you convince me?

6 MS. ZIBELMAN: I don't know if I can convince
7 you, but I can tell you my observations.

8 CHAIRMAN KELIHER: It's 'a reasonable man.'

9 MS. ZIBELMAN: The things that I would say, one
10 reason you want a hybrid board is you want a board that
11 really understands the issues of the constituents, which is
12 exactly I think what Jose is saying. People really
13 understand it because they understand it now.

14 CHAIRMAN KELIHER: I'm concerned about cost. The
15 perception is that management without stakeholders sitting
16 on the board, management could serve the market at any
17 price.

18 MS. ZIBELMAN: We do have a substitute for that;
19 one substitute we have, as you know we did file the stated
20 rate. But it's not as if we just have the stated rate, we
21 filed it with FERC, and then we do -- it's sort of a
22 ceiling, and we just work towards the ceiling. We actually
23 have, in addition to that, a finance committee that's made
24 up of stakeholders and board members, that on an annual
25 basis review our budget, and on a quarterly basis actually

1 review our quarterly reports. And actually when we have
2 capital plans, like you're saying software, actually review
3 it and can comment to the board in terms of approval.

4 So the one substitute, if you're not going to
5 have a hybrid board, is to have absolute transparency of
6 what you're spending money on, why you're spending money,
7 how you're doing compared to budget, where are you
8 forecasting, where are you going; so that the finance
9 committee, and it's made up of each -- two people from each
10 of our stakeholder groups -- is actually fairly
11 sophisticated, and as time has gone on, they really
12 understand this.

13 So for example, we have this second control
14 center we're building. Every time the finance committee
15 meets they go in depth; compare the budget, what's
16 happening, where it's going. So actually from my
17 experience, being in an IOU, our members have a lot more
18 information about what's happening in the RTO budget, what's
19 driving costs and what we're trying to do to maintain it;
20 then either our regulators or actually our customers.

21 So I think that issue can be taken care of by
22 having well thought-out processes and transparency; because
23 again, we're 500 people, and we don't have a lot of assets.
24 So reviewing our budgets is not going to get to read the
25 generator budgets and all sorts of things; they're pretty

1 standard. Software, hardware, and people.

2 The other question though is in terms of how do
3 our members then get confidence that the Board, when they're
4 making decisions, are making them with the interests of the
5 members at hand, and are doing so in such a way, with an eye
6 towards not saying "I want to protect these large utilities
7 because they're large utilities. I want to make sure that
8 it's working." And what we're really looking at in creating
9 markets, of course, is the type of thing that we keep
10 talking about, is getting investment in, getting prices to a
11 competitive level, really driving margins down, and making
12 the electricity dollar have that much more value to our
13 customers. That's really where we're headed.

14 So that's why what I think rather than hide the
15 horse, the better alternative is you get informed Board
16 members who know the industry, so they come in it with a
17 certain amount of knowledge of what is, and then the job,
18 really if they stay through the process, is to keep these
19 Board members absolutely current on what the stakeholders'
20 current needs are.

21 And the best way to do that is there what we're
22 trying to do, is making our processes more robust in terms
23 of when a state working group is looking at a particular
24 issue, having both majority and minority positions well
25 stated, and having a process of people who don't have a lot

1 of money to go to stakeholder meetings know that there's a
2 beginning and end, and this is what this group is going to
3 focus on. And then making sure that there's a lot more
4 access to the Board, both formal and informal.

5 Because what we found is, as we've gotten bigger
6 and the issues have become more divisive, it's more
7 important. Just like anyone will tell you, communicating
8 with your customer becomes increasingly important as the
9 issues get harder.

10 So what we've learned in going through the year
11 and hearing from our stakeholders is that we need to get
12 much more aggressive in making sure that the Board is in the
13 presence of stakeholders, have an opportunity to
14 communicate. And we're trying to encourage our stakeholders
15 to put a lot of things in writing, because the Board reads
16 these things. And as you know, these issues are fairly
17 complex, and a casual phone conversation is no substitute
18 for someone actually writing the position out in writing.

19 So to answer your question, I think the goal of a
20 hybrid board would be to sensitize the Board members. We
21 can provide the fiscal responsibility by doing the stated
22 rate, which is just like a regular utility rate; and then
23 you need to have a robust enough process that the Board can
24 stay absolutely current. And the Board can represent that
25 by making sure there's ways that they can allow the members

1 to see inside as why they made the decisions they did. That
2 would I think instill the confidence.

3 They are listening. They may not agree, but at
4 least they've understood and they've listened and they made
5 a decision based on the best information, based on their
6 judgment of what you really need to do to achieve our
7 objectives.

8 CHAIRMAN KELIHER: Yakout?

9 MR. MANSOUR: As I said in my note, Mr. Chairman,
10 first of all the budget of the ISO, the cap on the budget is
11 reached through a second, and actually, by the way, that
12 goes for - time.

13 The stakeholders review the priorities, they
14 review the activities, review the costs, and they put a cap.

15 If you go below that cap, we let you go fight with FERC,
16 and that's basically uncontested.

17 And so far for the last three years, first the
18 cap year after year has been reduced by actually - for
19 management, and secondly, it will be consistent even though
20 the cap.

21 So that's a check and balance on the budget.
22 Now, is the budget too high? We are talking about the
23 figures that Audrey quoted or figures I quoted. We are
24 talking about less than one percent of the bill.

25 Now, you tell me about anything, whether the

1 dispatcher of middle cap taxi, or airline or whatever,
2 dispatch and control of that sophistication at a charge of
3 less than one percent.

4 So in terms of, you know, it is the escalating
5 cost of RTOs, I saw some of the actual reports that came
6 out; it was -- I mean, it's not a joke, but if I calculate
7 how tall my son is going to be when he reaches 10 years old
8 using the same theory, he's going to probably be 24 feet or
9 so.

10 It's basically -- RTOs, the number of RTOs
11 increase, the responsibility of RTOs are increasing, there's
12 the expectations are increasing, the ISO is increasing, and
13 the cost is increasing in total. But when you put things in
14 perspective, how much is that in reference to the bills?
15 It's a pretty small amount compared to --.

16 Before we did our reduction and we showed that we
17 are following really best practices in any organization, not
18 just ISOs, ISO cost was a bargain. Every meeting I had with
19 stakeholders, the majority of, or at least most of what I'm
20 hearing is, don't nickel and dime now on cost, and
21 compromise delivery. Because delivery of the stuff that's
22 ahead of us, whatever, integration of removal or mission or
23 all of a sudden it's against, facing us, this is, 'Don't
24 nickel and dime on cost to achieve this. This is much more
25 important than making that line numbers."

1 So in terms of the cost, I said I see that the
2 checks and balances are there. Now the governance -- and
3 that's the other question which is the governance -- say why
4 not a hybrid?

5 Well, anytime I said hybrid, anytime I actually
6 said I'd like to have a committee of some sort of
7 stakeholders. Everyone tells me it's a great idea, as long
8 as I'm there.

9 (Laughter)

10 You're not going to have three people
11 representing all 25,000 of them. You're not going to have
12 that. And you're going to have the same problem. In fact,
13 you're going to have even more conflict, because now there
14 are people there who are a minority who represent commercial
15 interests. The rest is not comfortable with that.

16 So what do you do? You get like the original
17 board of ISO, so you have to have everyone in. So you get
18 25, 27. Now that you have that majority, by gosh, you can't
19 leave the sheep to the whatever. Now what you did is okay,
20 and let us have now a sideboard, appointed by the governor;
21 so this way, make sure that this is well protected.

22 And then let us also have a market monitor; but
23 since the market monitor is also part of management, and
24 management -- doesn't matter, management of what, as
25 management -- let us have a market surveillance committee

1 that is independent for market monitoring, goes inside to
2 monitor the market monitors who are monitoring that.

3 (Laughter)

4 And then -- and I can go on and on. And now
5 here's the fallacy in the whole thing: We created the so-
6 called market and every problem we face, we solve it by more
7 rules and more layers. Which is by definition taking away
8 market from being a market further and further, and then
9 when it fails, we have no market, which we never even meant
10 it to start with.

11 (Laughter)

12 And that's the issue you have to think about.
13 What are we after, and what's the use of putting in, and are
14 we really solving the problem? Or are we creating more
15 problems.

16 CHAIRMAN KELIHER: My time has expired --

17 (Laughter)

18 Anyone want to ask, or should we go to staff? Or
19 should I continue.

20 Commissioner Kelly.

21 COMMISSIONER KELLY: So Yakout, now your members
22 elect the Board members?

23 MR. MANSOUR: Yes.

24 COMMISSIONER KELLY: So how does that work?

25 MR. MANSOUR: Well, here's how it works.

1 COMMISSIONER KELLY: Does each group have their
2 own member?

3 MR. MANSOUR: Yes, every sector has five members,
4 that are in the group, and six sectors, there are 30. And
5 what we do is, they have an independent search firm that
6 goes and finds candidates, very independent from everyone.

7 When I say independent, the last one, the last
8 process, we had two vacant seats and they had to find at
9 least eight. So the nomination actually was nine; and
10 actually that was short-listed from a list of 15.

11 So we got the nine, and then it goes to -- other
12 than the incumbent, I did not have any names of the other
13 eight. It is that independent; I did not know them at all,
14 personally or even by name.

15 Then the committee, the committee of stakeholders
16 --

17 COMMISSIONER KELLY: Can I ask a question? Who
18 supervises that process?

19 MR. MANSOUR: The search firm.

20 COMMISSIONER KELLY: Who supervises the search
21 firm?

22 MR. MANSOUR: Those people, they -- the committee
23 first off, Like I still have the, to give them the actual --
24 this is a provision by the Board. And then the
25 facilitation of the committee is by a member called the

1 committee of the stakeholders, so they cannot supervise the
2 whole thing on behalf of the committee.

3 This is the kind of interaction.

4 But the search firm worked with the entire
5 committee. It presented the names, it is the 30 people
6 actually interview -- they do reference checks, and they
7 interview in person. And then the vote, and then the total
8 vote and rank all the members, and then they go to the
9 governor and say 'we recommend to you'.

10 And so far the governor has been very responsive
11 in his appointment, and then after that it goes to the state
12 senate who basically grill the candidates, as you know well,
13 and then you know whoever, when you pass there -- you have
14 checks and balances about four or five times as to what your
15 qualifications are, do you have standard issues, do you
16 stand for what we stand for, and so on.

17 COMMISSIONER KELLY: It seems to me that Mark's
18 testimony just summarized the kind -- what we're looking
19 for. That the focus of the Board should be that the
20 customers of the LSEs have the TOs and the GOs.

21 Now do you find -- who does your Board feel
22 they're accountable to? Do they feel they're accountable to
23 the LSEs? Who do they feel their customers are? Or to the
24 governor or to the senate, or to the people who elected --
25 who do they feel accountable to after that process?

1 MR. MANSOUR: Well, what is the mission of ISO?
2 The mission of ISO is basically work, operate the grid
3 reliably and decide on that we'll ultimately produce value
4 to consumers,

5 So by the fact that they are elected by the
6 stakeholders, they do have commitment to align with the
7 stakeholders' needs. The fact that they are appointed by
8 the governor and conferred by the senate, they have a
9 commitment to act in line with public policies and the
10 administration and the legislature level.

11 COMMISSIONER KELLY: Of course it's helpful that
12 you only have one state.

13 MR. MANSOUR: That's true.

14 MS. ZIBELMAN: I think that the ultimate goal is
15 to represent the consumers, but the question doesn't say
16 what the consumer -- what consumers may perceive may be the
17 best thing -- may not be changed depending on the situation.

18 I think, for example, our issue in terms of the
19 reliability pricing model, the objective was to create a
20 reliable grid. So that was the goal. It's whether, as you
21 know, people always agree that your outcome is the public
22 interest. There are differing views on what the public
23 wants, and that's the process of decision making.

24 COMMISSIONER KELLY: Mark, how do you feel about
25 the hybrid board puzzle, for example?

1 MR. GERKEN: I'm a very big supporter of the
2 hybrid board. I'm going through something with my own
3 board. I mean, this world is changing so fast and I have
4 public power entities on that board, and I want to move to
5 ex-officios that are better on the risk side, the financial
6 side, and the strategic planning side; because our people
7 that go back home and run the systems don't see that every
8 day.

9 I would tell you that I don't want to see the
10 RTOs and ISOs go away; I think economic dispatch has been a
11 tremendous asset. But I do believe that even in the last
12 four weeks, that if there was some representation from the
13 LSEs, a lot of things would change.

14 I, for one, I'd like to see PJM increase their
15 planning in the way they review interconnection studies.
16 I've got a thousand megawatt coal plant that I've been
17 delayed from an interconnection study for nine months. I
18 thought we wanted to get iron in the ground.

19 If I was an ex officio board or I had somebody, a
20 voice -- I'd say I'd look at their budget and say "I want
21 you to staff up, because you can't meet any of your cues."
22 That's not coming out. I think that they need to understand
23 us better. We're not just public power, it's a whole
24 different sector.

25 So I believe that the hybrid gets you closer to

1 that than independents. At one time we all thought
2 independence was the way to go -- don't get me wrong, but I
3 think there's nothing wrong with making changes when the
4 markets move.

5 COMMISSIONER KELLY: Why is independence not
6 working for you?

7 MR. GERKEN: Well, we look at this -- RPM is a
8 prime example. I mean, here we are, the stakeholder says we
9 don't like it, okay? What happened. It just got shoved
10 down our throats anyway. And then we get into, as he
11 indicated, lengthy lawsuits. That didn't do anybody any
12 good. Who do you think paid for those costs, from PJM or
13 MISO? We do, as a stakeholder.

14 We're just struggling to see any benefits out of
15 these markets, other than economic dispatch.

16 COMMISSIONER KELLY: And maybe that's the real
17 question. What do you want out of them? I mean, Yakout
18 said the market that gets value to the customers. I
19 shouldn't be speaking for Gordon, I should let him speak for
20 himself, but at least part of their mission was to lower the
21 cost to the customers. What do the customers want? Don't
22 customers want capacity in the long run? Isn't that part of
23 the RPM.

24 Isn't it that it's difficult to decide what the
25 customers want?

1 MR. GERKEN: Absolutely, but who knows it better
2 than the load serving entities. You can't ask the customer;
3 that's a pretty sophisticated market there. If it's a large
4 industrial customer, that may be different; but if you're
5 asking a residential customer, they don't know. They really
6 don't know.

7 So I think the load serving entity represents
8 that end user better than anybody.

9 MR. MANSOUR: I agree, but the thing is, first
10 even an ISO, do you think we can load our board with a
11 proposal that has everything done, cost implications, to
12 customers affected before we have a good consensus among the
13 load serving entities and the utilities commission in the
14 state?

15 MR. GERKEN: I think there's something, I
16 listened to the panel earlier, and one of the things that
17 you people don't do is run generation and have to worry
18 about load following; and you can talk it, but the issue is
19 you talk about, there's no new entries in the markets.
20 There's a lot of reasons why there's not new entries in the
21 market, and there are certain things that we need to talk
22 about and had a lot stronger voice, and talked to that
23 board, whether it's an ex officio matter or not, if your
24 Board is independent and it has some load serving entities
25 talking to them to help make decisions instead of just your

1 staff, I think there's a big issue.

2 I've listened to this board ahead of here, and
3 they don't talk about investor-owned being triple rated,
4 triple B rated, below investment grade -- that's part of the
5 problem, not getting into the entry into the new markets.

6 The other issue is you've got an LMP that sends
7 them a pricing signal so that their coal and nuclear get
8 uplifted, 30 percent of the time. That's a signal that
9 says, "If I can't borrow money cheaply and I can get
10 uplifted more hours of the day, that's my motto." So
11 there's a lot of reasons.

12 Now I'm not saying it's PJM's fault. What I'm
13 saying is, there's ways that we have to look at this and say
14 'what are we doing?'

15 COMMISSIONER KELLY: That was one of your other
16 suggestions, that would be more opportunity for
17 communication between the load serving entities and the
18 boards.

19 MR. GERKEN: I'll give you an example.

20 COMMISSIONER KELLY: That seems to make sense to
21 me.

22 MR. GERKEN: We haven't seen Phil Harris, all we
23 see is the PR rep from MISO or PJM, and the last time the
24 representative from PJM -- I purposely asked her to find out
25 where my transmission interconnection was in the queue. And

1 I haven't heard boo for a month and a half.

2 So when I get MISO, and I'm dealing with credit
3 issues, the guy tells me he's a real estate lawyer, that's
4 dealing with my creditworthiness. They don't understand us.

5 MS. ZIBELMAN: Marc, I'll get you an answer.

6 (Laughter)

7 COMMISSIONER KELLY: I'm glad this panel has had
8 at least one successful --

9 (Laughter)

10 MS. ZIBELMAN: But I actually agree with Marc. I
11 think that the challenges we have right in front of us is
12 that the issues facing the industry are very complex, and
13 the best solution -- I think the independence issues and the
14 challenges of hybrid board can be very difficult.

15 I don't think there can be any substitute,
16 though, in having a situation where you make sure that the
17 members who really do have the issues at stake have a clear
18 path of communication to the Board, that they can really
19 explain to the Board what's going on, how is this affecting
20 their business, so that the Board understands it. And
21 despite everything management might do, and we've had this
22 issue in PJM as to whether management filters or doesn't
23 filter, I don't think Marc is ever going to be satisfied
24 about my ability to explain to the Board his issues.

25 And so the only way to do this is if we have

1 these direct paths of communication so the Board isn't --
2 processes that you use to make sure that you're informed of
3 people's decisions. I think that's really going to be the
4 issue that we need to resolve, and it has to be the
5 complexity of these large markets of very diverse issues;
6 but that's what we're working on to try to resolve.

7 MR. GERKEN: And I would agree with that, and I
8 realize that I don't sit on these boards and know what they
9 have to deal with either. So I do realize that; I just feel
10 like a tweak to these boards may make a little sense; and
11 communication is a wonderful thing.

12 MR. WEBB: Commissioner, again at Audrey's
13 committee and helping people with interconnections, I think
14 I'd better jump in now, too.

15 (Laughter)

16 I just wanted to support what Marc said, and I
17 wanted to make sure that the Commission understands I think
18 a key concern of the demand side; and that is that we just
19 don't feel we have a voice at the table at levels where
20 important decisions are being made. And we feel we need to
21 have a voice there, and we think the only way we can get
22 that voice is through a hybrid board.

23 We're not asking for any more than that, we have
24 no grand expectations that we'll come in there and we'll
25 change the budgeting process and other things in the ISOs or

1 RTOs, but we just need a voice and we don't have the voice
2 there. As I said in my earlier comments, it is so heavily
3 skewed to the supply side at all levels; and when you get to
4 the upper levels, there's just no presence of the demand
5 side.

6 And I also have to object to some of the comments
7 that the demand side isn't sophisticated enough to
8 participate in the board. I know that I have many
9 colleagues that I work within the power industry who are
10 also industrials who are as knowledgeable if not more
11 knowledgeable than many of the existing Board members.

12 COMMISSIONER KELLY: Thank you, Lloyd.

13 MS. ZIBELMAN: Just to respond to Lloyd, just
14 quickly.

15 We had this issue actually debated last week, and
16 the industrial representative at PJM said that she did not,
17 that the PJM industrials did not want hybrid boards.

18 So I guess the only point I raising it is not to
19 say that whether ELCON represents or doesn't represent, but
20 there are a diversity of opinions. I think where folks are
21 fairly uniform is they want the ability to communicate to
22 the board, and to make sure that the Board understand their
23 concerns. And the issue there is really the director
24 access, I think.

25 COMMISSIONER KELLY: Having been at the

1 California ISO when there was a hybrid stakeholder board,
2 that model is very frightening. So maybe just one would be
3 okay, but that one certainly -- that of course didn't work.
4 And I appreciated your explanation about how these things
5 grow in order to achieve the objective of everybody being
6 represented.

7 I don't have too much time left, but I'm glad you
8 mentioned the word demand side, because there was one
9 question -- remember I ran out of time on the demand side
10 panel? -- There was one question --

11 (Laughter)

12 There was one demand side question I wanted to
13 ask, and so I'm going to ask what I didn't get a chance to
14 ask.

15 Can demand side be packaged with intermittent
16 renewables? And can the ISO do that through to the market
17 structure.

18 MR. MANSOUR: Y E S. That's the whole thing.

19 In fact, I was listening to the demand side
20 discussion this morning, and it was more or less primarily
21 focused on scarcity pricing and tying on the shortage, or
22 the mode is high --. Our vision and our plan is that demand
23 response is 365 days a year in the future, and the prime
24 writer is exactly this increment.

25 Now we talked about difficulties as to how to get

1 that signal to the consumer; there are a lot of ways to make
2 it less complex.

3 If you tell the consumer just monitor the prices
4 hour by hour a day ahead, they're not going to do that.
5 There is automation that is needed, and those things can
6 actually be done; like the consumers can subscribe to some
7 product. Let us say, 'do you want to subscribe to green L?'

8 COMMISSIONER KELLY: Well, for example, I am a
9 hundred percent wind power tariff.

10 MR. MANSOUR: Right.

11 So this way we can put you in the program --
12 where your usage is up and down with the ability of
13 greenpower. And that can be automated. There's a lot of
14 things in life that are not different, okay?

15 That would reduce the cost dramatically of the
16 price of green power if you take into account what has to
17 back green power in terms of regulation, of reserves and all
18 that stuff.

19 As I said, it's just something that we need to
20 think about; and for us we're thinking emission control, the
21 renewables, conservation and transmission. Every one of
22 these need a change in policy. In fact, all of us need a
23 change, and this business cannot be as usual. The law has
24 to be different, and of course the law is changing.
25 Regulation has to be different.

1 Planning is going to have to be different, and
2 operations drastically different. All four have to be very
3 different. But we really have to think of all of those as
4 one big vision. Not in pieces. We need a roadmap that
5 combines all of this.

6 COMMISSIONER KELLY: Thank you.

7 CHAIRMAN KELIHER: Mr. Moeller.

8 COMMISSIONER MOELLER: Thank you, Mr. Chairman.

9 I remember an article from the Journal, probably
10 a year and a half ago, which was outlining the fact there
11 was a crisis in Sino-American relations diplomatically
12 because there was no word in the Chinese vocabulary that was
13 equivalent to 'stakeholder'.

14 (Laughter)

15 And so speeches were made and analyzed, and they
16 couldn't figure out what we were talking about.

17 (Simultaneous discussion)

18 COMMISSIONER MOELLER: It seems like we've heard
19 a number of issues come up repeatedly. We've got the
20 concern over costs, and that can kind of be in one basket.
21 And little less concern there, because there are start-up
22 costs which are by nature start-up costs, and hopefully are
23 under control in certain markets and demonstrated, improved
24 in others.

25 The one thing that I think has come through

1 repeatedly, and Commissioner Keliher mentioned it, is it's
2 my feeling that the basis of all good relationships is open
3 and frequent communication. And it sounds like there's a
4 lot of opportunity here to approve that, regardless of the
5 stakeholders involved; whether they are load serving
6 entities or state commissions or a variety of other
7 entities.

8 Let me throw out the concept of, we're not just
9 really the hybrid board, but I'll call it a hybrid-hybrid
10 board. Which is you want people who can relate to the
11 issues going on in your market, but you want them to have a
12 conflicted personal interest in that market. So the concept
13 being you get someone from another market who knows the
14 industry, and can relate to the problems of various players;
15 but who does not have a direct role in your market, to
16 either benefit or to the detriment of decisions that are
17 made by the Board.

18 So as a kind of far-out concept, I will throw it
19 out there for your reaction.

20 MS. ZIBELMAN: It's not that far out.

21 COMMISSIONER SPITZER:

22 call upon the people that wouldn't necessarily volunteer,
23 and the ones who would volunteer are not the ones that sit
24 on the Board.

25 I guess my view is that it's a people issue and

1 if you're able to solve a people issue, the structural
2 issues take care of themselves.

3 Any responses?

4 MS. ZIBELMAN: I don't think any of us want to
5 raise our hands.

6 (Laughter)

7 MR. DELGADO: In the case of the C corporations
8 you were talking about, above all you're saying your purpose
9 is there's a fairly narrow purpose to what you're doing, and
10 is an objective to get it done.

11 From my perspective, the source of authority of
12 an ISO is whatever this Commission gives it, and whatever we
13 did to contract with them. That is a source of authority
14 that is for a very specific purpose.

15 When you're talking about the consumer, the Joe
16 that's going to end up paying for this, he has a
17 representative which is not even at the table. Happens to
18 be the state regulator, but by law, has authority to
19 represent the consumer. And they haven't decided where
20 these things are value are not, whether it is a value or
21 not, whether the consumer should pay for it or not.

22 Now the utilities are voluntarily joining this
23 thing and committed themselves to it, and when they do it of
24 course they come under the jurisdiction of ISO.

25 So the issue here is -- I don't think it's

1 straightforward; it's complicated. But the fact is that we
2 have to see the limitations of what the ISO can do. And
3 frankly, ultimately who is the ultimate customer of what the
4 ISO is doing and what is the mechanism by which the
5 authority of the ISO is exercised? Whose authority are they
6 exercising?

7 I would say that the ISO has to exercise whatever
8 FERC gives it, and also that the members of ISO have to
9 justify their participation, and that is the representative
10 of the consumer. That happens to the state commission.

11 So that is in fact what I am trying to address.

12 COMMISSIONER SPITZER: Commissioner, you've got
13 people with sharp pencils in your accounting department.
14 Regardless of how the board is constituted, if you have
15 faith and confidence in the board and in the management, us
16 there a real question that those are going to going to
17 affect cost?

18 JUDGE CHRISTIE: I was going to make two
19 comments, Mr. Spitzer.

20 First, having been someone in private practice
21 who did represent a lot of 501(c)(3)s, you're right,
22 whatever manager wanted was to pick a board that would do
23 what they wanted to do.

24 On the bigger issue about accountability, I'd
25 just like to say the fundamental question, whether hybrid

1 board or organizational chart you want to come up with, the
2 fundamental question in accountability is, if you're a party
3 who thinks that accountability is not running to you, where
4 do you go for a remedy? If a party thinks they've been
5 aggrieved by an action of the Virginia Corporation
6 Commission, they can appeal to the Supreme Court of
7 Virginia. If a party thinks that FERC has aggrieved them in
8 some way, they can appeal to the D.C. Circuit and hopefully
9 the Supreme Court.

10 As Chairman Keliher, your many good questions you
11 asked at the beginning of this Q&A, whether does one go for
12 a remedy if you are a party that's been aggrieved and had
13 your accountability violated, or your accountability has
14 been violated vis-a-vis you, in terms of the RTO?

15 It is in a gray area, jurisdictionally. Whether
16 the party's a consumer, ratepayer or producer, or any other
17 party who happens to be a member of PJM or any other RTO,
18 where do you go for your remedy if you think that
19 accountability has been violated with regard to you?

20 You can't go to a state commission because
21 arguably we have no remedies to offer. Chairman Keliher, as
22 you mentioned, there's a question -- and I don't want to get
23 in to another proceeding here about what your authority
24 might be, but you mentioned the CalISO versus FERC case. If
25 there's no remedy for any party to go seek, then there's no

1 accountability. And that's a fundamental issue that I think
2 needs to be addressed.

3 And if FERC doesn't have a remedy to offer, then
4 maybe FERC needs to recommend legislation so that it does
5 have a remedy. Because if there's no remedy, a legally
6 enforceable remedy, and I apologize for thinking like a
7 lawyer here -- if there's no legally enforceable remedy
8 there is no accountability. And saying we'll just go to the
9 stakeholder process and take it up with them. That's just
10 frivolous; that's not a legally enforceable remedy.

11 There has to be a legally enforceable remedy for
12 parties who think that accountability has been violated, or
13 there is no accountability.

14 CHAIRMAN KELIHER: If there's no accountability,
15 isn't the remedy to vote out the Board?

16 JUDGE CHRISTIE: Well, that assumes -- and again,
17 I wouldn't qualify as an expert witness on PJM's voting
18 procedures. But to say to just vote out the board, that's
19 not really a legally enforceable remedy. And there's been a
20 debate for 30 years in corporate law, whether stockholders
21 really do have power to vote out a board, even in a stock
22 corporation.

23 CHAIRMAN KELIHER: Just to stay with the Disney
24 matter -- it worked -- and there was a very clear sign with
25 voting.

1 JUDGE CHRISTIE: And again we're getting into
2 corporate law here, but I think you can probably cite a
3 hundred examples of stock corporations where the board was
4 not replaced by democratic vote; and for a long time it was
5 thought in corporate law that if you were a stockholder,
6 your real remedy was just sell the stock. If you don't like
7 it, sell the stock. Of course if you bought the stock at
8 100 and you're holding it at \$5 a share, that's not much of
9 a remedy.

10 COMMISSIONER SPITZER: You don't even want to get
11 into Sarbanes-Oxley.

12 JUDGE CHRISTIE: I won't.

13 MS. ZIBELMAN: You brought something up, I think
14 it's an important point that we need to talk about, too.
15 Actually, in fact, there is a voting process; in fact in
16 MISO they did vote out board members last year.

17 So I think there is a true accountability. But
18 the other issue you have is the attraction of people, and it
19 is the quality of people; so one of the things that I think
20 all boards struggle with these days is getting good people,
21 and I know we shared this with the IRC Council, our boards,
22 the RTO boards, in terms of volume of information they read
23 and the amount of meetings they have to attend, when you add
24 in not just one board member, but stakeholder meetings,
25 there's a huge volume of information.

1 So one of the things that we also need to balance
2 is if you're going to have CEOs of major corporations,
3 they're not free enough to attend two and three day meetings
4 every month, if they're running their own companies. And so
5 one of the things we need to balance in the stakeholder
6 process is make sure there's information; but if you're
7 asking for busy executives because you want them because of
8 their business acumen to attend meetings, you need to think
9 about, that it's not just board meetings, you add in
10 stakeholder meetings, you add in liaison meetings, you add
11 in regulatory meetings, it becomes a huge commitment and
12 something that I've heard from some of the RTOs is they're
13 looking for board member searches, is it's getting
14 increasingly difficult to find people who are able to make
15 that level of commitment that are current in the industry.

16 So as we think through these things, I think we
17 have to add that notion as well.

18 COMMISSIONER SPITZER: And a membership where
19 there's a public interest, like the charitable entity, is a
20 different animal than publicly traded firms.

21 Where it's very common to have other publicly
22 traded executives who aren't reading every --

23 MS. ZIBELMAN: Right, but --

24 COMMISSIONER SPITZER: It's a different
25 undertaking.

1 MS. ZIBELMAN: But in the RTO boards, they have a
2 huge volume of information they have to read. It's much
3 more different than just reading the national records.

4 MR. MANSOUR: Commissioner Spitzer, I think you
5 put your hand on the right points in terms of, this is about
6 communication and personalities rather than structure. --

7 CHAIRMAN KELIHER: Thank you very much.

8 Staff, any questions that need to be asked?

9 (Laughter)

10 CHAIRMAN KELIHER: It's all in how you phrase the
11 question.

12 I want to thank the panelists. This was a very
13 good panel, a really nice mix, and you all got along.

14 (Whereupon, at 4:36 p.m., the technical
15 conference concluded.)

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