

BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

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IN THE MATTER OF: :
CONSENT MARKETS, TARIFFS AND RATES - ELECTRIC :
CONSENT MARKETS, TARIFFS AND RATES - GAS :
CONSENT ENERGY PROJECTS - MISCELLANEOUS :
CONSENT ENERGY PROJECTS - CERTIFICATES :
DISCUSSION ITEMS :
STRUCK ITEMS :
- - - - -x

920TH COMMISSION MEETING
OPEN MEETING

Commission Meeting Room
Federal Energy Regulatory
Commission
888 First Street, N.E.
Washington, D.C.

Thursday, June 21, 2007
10:06 a.m.

1 APPEARANCES:

2 COMMISSIONERS PRESENT:

3 CHAIRMAN JOSEPH T. KELLIHER

4 COMMISSIONER SUEDEEN G. KELLY

5 COMMISSIONER MARC SPITZER

6 COMMISSIONER PHILIP MOELLER

7 COMMISSIONER JON WELLINGHOFF

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21 ALSO PRESENT:

22 JANE BEACH, Reporter

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

2 (10:06 a.m.)

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

8 And --

9 (Child interrupts.)

10 CHAIRMAN KELLIHER: I have some special guests to
11 help with the Pledge of Allegiance today. The kids are out
12 of school and we're trying to keep them off the streets.

13 (Laughter.)

14 CHAIRMAN KELLIHER: I thought they'd come to the
15 FERC meeting and help with the Pledge of Allegiance. And
16 Damien has a fascination with ties, and so I'm wearing my
17 flag tie to commemorate his participation.

18 He was just kissing the FERC flag back there.

19 (Laughter.)

20 CHAIRMAN KELLIHER: And he loves the eagle, so he
21 really likes our official seal.

22 But why don't we do the Pledge of Allegiance.

23 (Pledge of Allegiance recited.)

24 CHAIRMAN KELLIHER: I think Phil's kids can join
25 us, maybe in your second term. They could help us out.

1 COMMISSIONER MOELLER: Not this morning, I can
2 tell you that.

3 (Laughter.)

4 CHAIRMAN KELLIHER: This is actually a pretty big
5 meeting. Normally at the Commission's summer meetings, July
6 is the big meeting and June is a somewhat smaller meeting.

7 I think we've reversed things this year. I think
8 we have a big agenda at this meeting. We have some major
9 actions we're taking on competition in the wholesale power
10 markets.

11 And we also -- if you look at the rest of the
12 Orders, I think today, by my count, we're doing two final
13 rules, three proposed rules, and nine rehearing orders, so
14 it's actually a pretty substantial meeting.

15 Some of the things we're not talking about, are
16 important, but it's just the two major items, the ANOPR and
17 the market-based rate final rule that are so significant
18 that we're really going to dedicate our time to those
19 Orders.

20 But I encourage you to look at the other matters
21 we're disposing of today.

22 And before we really turn to other things, I
23 would like to make one announcement regarding financial
24 forms. I'm just pleased to announce that all natural gas
25 companies and public utilities with recently-due annual

1 financial forms, have filed on time or requested an
2 extension.

3 And just to put it in context, last February, the
4 Commission issued an Order on Show Cause for Compliance with
5 form-filing Requirements, and the Order directed delinquent
6 filers of FERC financial forms, to show cause within 30 days
7 of the date of the Order's issuance, why they were not in
8 compliance with the Commission's regulations.

9 And we issued the Show-Cause Order as a result of
10 a compliance review of the financial forms, undertaken by
11 the Office of Enforcement, beginning in April of 2006.

12 In this review, the Commission looked for
13 discrepancies between potential filers and actual filers,
14 and identified 140 public utility and natural gas companies
15 that had failed to file the required forms.

16 Staff contacted the companies, and at the
17 conclusion of the review, 14 companies had failed to meet
18 one or more of the Commission's filing requirements and were
19 listed as Respondents in the Show-Cause Order.

20 But today, we now see that we have received on-
21 time or requested extension of all companies that are
22 required to file these forms.

23 So think it appears that the February Show-Cause
24 Order sent the right message; companies received the
25 message, and they are now looking to comply fully with those

1 requirements, as well as others.

2 (Child laughs.)

3 CHAIRMAN KELLIHER: Damien thought that was
4 funny.

5 (Laughter.)

6 CHAIRMAN KELLIHER: And, with that, I'd just like
7 to again point to the large amount of business that we
8 disposed of in between open meetings, and since the May 17th
9 open meeting, the Commission has issued 105 Notational
10 Orders.

11 I really want to express my gratitude to my
12 colleagues and to their advisors, as well as the Commission
13 Staff and the Secretary's Office, for that very significant
14 production.

15 Any other comments from my colleagues, before we
16 turn to the consent agenda?

17 (No response.)

18 CHAIRMAN KELLIHER: No? Madam Secretary, let's
19 turn to the consent agenda.

20 SECRETARY BOSE: Good morning, Mr. Chairman, good
21 morning, Commissioners.

22 Since the issuance of the Sunshine Act Notice on
23 June 14th, 2007, E-9, E-23, E-25, and H-2, have been struck
24 from this morning's agenda.

25 Your consent agenda for this morning, is as

1 follows:

2 Electric Items are: E-2, E-4, E-5, E-6, E-7, E-
3 8, E-11, E-12, E-13, E-14, E-15, E-16, E-17, E-18, E-19, E-
4 21, and E-22.

5 The Miscellaneous Item is M-1.

6 Gas Items are: G-1 and G-2.

7 The Hydro Item is H-1.

8 The Certificate Items are: C-1, C-2, C-3, C-4,
9 and C-5.

10 As required by law, Commissioner Moeller is not
11 participating in Consent Item E-7; Commissioner Spitzer is
12 not participating in the following Consent Items: E-13, E-
13 14, and E-15.

14 As to E-1, Commissioner Moeller is dissenting, in
15 part, with a separate statement; as to E-2, Commissioner
16 Kelly is concurring, with a separate statement; as to E-3,
17 Commissioner Kelly is concurring, in part, and dissenting,
18 in part, with a separate statement.

19 Now we will take a vote on the Consent Agenda
20 Items, beginning with Commissioner Wellinghoff.

21 COMMISSIONER WELLINGHOFF: I vote aye.

22 SECRETARY BOSE: Commissioner Moeller?

23 COMMISSIONER MOELLER: I vote aye, except as
24 noted on the recusals.

25 SECRETARY BOSE: Commissioner Spitzer?

1 COMMISSIONER SPITZER: With the exception of the
2 recusal items, E-13, E-14, and E-15, I vote aye.

3 SECRETARY BOSE: Commissioner Kelly?

4 COMMISSIONER KELLY: I vote aye, noting my
5 concurrence.

6 SECRETARY BOSE: Chairman Kelliher?

7 CHAIRMAN KELLIHER: Aye. Why don't we turn to
8 the discussion agenda?

9 SECRETARY BOSE: The first item on the
10 discussion agenda for this morning, is E-3. That's
11 concerning the rulemaking on wholesale competition in
12 regions with organized electric markets.

13 There will be a presentation given by David
14 Kathan from the Office of Energy Markets and Reliability.
15 He's accompanied by Harry Singh and Chris Thomas from the
16 Office of Energy Markets and Reliability; Kathryn Kuhlen
17 from the Office of Enforcement; and Moon Athwal from the
18 Office of the General Counsel.

19 MR. KATHAN: Good morning, Chairman Kelliher and
20 Commissioners. My name is David Kathan and I am from the
21 Office of Energy Markets and Reliability. Joining me to day
22 are Harry Singh and Chris Thomas from the office of Energy
23 Markets and Reliability; Kathryn Kuhlen from the Office of
24 Enforcement; and Moon Athwal from the Office of the General
25 Counsel.

1 This Draft Advance Notice of Proposed
2 Rulemaking, or ANOPR, is intended to improve the operation
3 of wholesale electric power markets in the regional
4 transmission organization, RTO, and independent system
5 operator, ISO, regions.

6 Recent Commission conferences on the status of
7 wholesale competition, along with other Commission efforts
8 to reach out to members of the industry, have led to
9 proposals in this draft ANOPR.

10 The Draft Order addresses wholesale competition
11 in RTO and ISO regions. Its goal is to improve the
12 operation of the organized markets, without disturbing the
13 significant progress already achieved by RTOs and ISOs in
14 providing benefits to wholesale customers.

15 It is intended to complement other Commission
16 actions to address wholesale market challenges, both inside
17 and outside RTO and ISO regions.

18 It presents for comment, preliminary proposals
19 for achieving specific improvements to organized market
20 operation.

21 The Draft Order makes proposals in four areas:
22 Demand response; long-term power contracting; market
23 monitoring; and responsiveness of RTOs and ISOs to customers
24 and other stakeholders.

25 Demand response is necessary for any market to

1 operate efficiently. The Draft Order presents four
2 potential proposals to facilitate greater participation of
3 demand response in organized markets.

4 The first would require RTOs and ISOs to accept
5 bids by demand resources, to provide certain ancillary
6 services, if the demand resources meet the necessary
7 technical requirements and the bids are at or below the
8 market clearing price.

9 The second would modify RTO and ISO tariffs to
10 eliminate, during a system emergency, certain charges to a
11 power purchaser, for taking less energy in real time than it
12 purchased in the day-ahead market.

13 Third, it would require RTOs and ISOs to accept
14 demand-response bids from those who aggregate demand
15 responses of individual retail customers, unless not
16 permitted by state law.

17 Finally, it proposes several possible ways to
18 modify the bid- and price-cap provisions of market power
19 mitigation rules during an emergency, so as to allow more
20 effective demand response.

21 Regarding long-term power contracting in
22 organized market regions, the Draft Order asked for comment
23 on three preliminary proposals. It would require RTOs and
24 ISOs to help facilitate long-term contracting opportunities,
25 first, by allowing others to post long-term offers to sell

1 or buy power, on the ISO's or RTO's website.

2 Second, by helping develop standardized forward
3 products, and, third, by posting publicly-available
4 information on recent long-term contract terms and prices.

5 The Draft Order also asks for comment on whether
6 the Commission should modify its data requirements for the
7 Electricity Quarterly Report, to provide more information to
8 those wishing to enter into long-term power contracts.

9 With respect to market monitoring, the Draft
10 Order proposes strengthening the independence of market
11 monitoring units and expanding the dissemination of market
12 information to the states and to the public.

13 One proposal for strengthening independence, is
14 to require RTOs and ISOs to provide the market monitors with
15 adequate staff, resources, and market data.

16 Another is to have the market monitors report to
17 the RTO's or ISO's Board of Directors, rather than to
18 management.

19 A third is to remove the market monitor from
20 tariff administration.

21 A final proposal would require that the market
22 monitors refer to the Commission, any violations or adverse
23 market impacts caused by the RTOs and ISOs, as well as those
24 caused by market participants.

25 The proposals for expanding the dissemination of

1 market information include: Holding regular conference
2 calls among the market monitors, interested state
3 commissions, and the Commission Staff, to discuss current
4 items of interest; releasing offer and bid data that is
5 lagged and masks participants' identities; and entertaining
6 the submission of tailored requests for information from
7 state commissions, with appropriate safeguards for
8 confidentiality.

9 The Draft ANOPR also proposes that all
10 provisions related to market monitoring, including ethics
11 standards, be included in the RTO and ISO tariffs, and that
12 a pro forma tariff section be developed to standardize those
13 provisions.

14 Finally, the Draft Order makes a preliminary
15 proposal to require that all RTOs and ISOs, ensure that
16 their customers and other stakeholders, have some form of
17 direct access to the RTO or ISO Board of Directors.

18 This is so that they can express their views
19 about proposed actions before Board decisions are final.
20 The Draft Order states that there are at least alternative
21 ways to provide such access: A Board advisory committee and
22 a hybrid Board with some stakeholder members.

23 The Draft Order also seeks comment on other ways
24 for an RTO or ISO to be responsive through RTO/ISO
25 management, stakeholder processes, and budget processes.

1 The Draft seeks comments from interested parties
2 on these proposals and the questions posed. Comments are
3 due 45 days from publication in the Federal Register.

4 This completes my presentation, and we would be
5 happy to answer any questions.

6 CHAIRMAN KELLIHER: Thank you very much, David.
7 I'd just like to make some comments on this Order.

8 One of the principal focuses of the
9 Commission's electric regulatory program, currently, is
10 strengthening competition in wholesale power markets, and
11 this Order proposes a package of reforms designed to
12 strengthen competitive markets.

13 I think it's clear, in the wake of the Energy
14 Policy Act, that competition is national policy in wholesale
15 power markets.

16 There have been three major federal laws enacted
17 in the past 25 years, all of which have embraced competition
18 as national policy in wholesale power markets.

19 So, I really think that the central question
20 before the Commission today, is not whether competition is
21 the right policy, whether the Commission should promote
22 competition in wholesale power markets. I think that
23 question has been asked and answered three times by
24 Congress.

25 I think the question before us, is, what can the

1 Commission do to promote effective competition in the
2 wholesale power markets, really, how can we follow the will
3 of Congress?

4 I think it's important to draw, though, the
5 distinction between competition and deregulation. I think
6 that distinction is frequently blurred by people who are
7 debating the merits of competition policy or the soundness
8 of competition policy.

9 Deregulation is not and has never been the policy
10 of the Federal Energy Regulatory Commission or the Federal
11 Government. Deregulation, to me, is the absence of
12 regulation, and the Commission has never stopped regulating
13 wholesale power sales, so, we have continued to regulate
14 wholesale power sales throughout the past quarter century.

15 The nature of our regulation has changed, but
16 we've always regulated wholesale power sales, and we've also
17 never relied solely on competition to assure just and
18 reasonable rates in wholesale power markets. We rely on a
19 mix of competition and regulation, and that mix always has
20 to change over time.

21 The nature of the market, the wholesale market is
22 that it's a very dynamic market; it changes pretty
23 dramatically and sometimes pretty quickly.

24 So I think it's important for us to be
25 constantly considering changes to regulatory policy, and

1 considering changes in that mixture between reliance on
2 competition and reliance on regulation.

3 Now, our policy also has to reflect the
4 realities and recognize the realities of wholesale markets
5 themselves. We don't have a national wholesale power
6 market; we have regional wholesale power markets, and there
7 are some very significant differences between those regions.

8 Some of the differences are structural. We have
9 organized markets in the RTOs and ISOs, and we have
10 bilateral markets in the West and in the South.

11 I think those differences are likely to persist,
12 and I also see no reason for the Commission to try to impose
13 one preferred market structure on regions of the country.

14 So, if you accept that our duty -- I think our
15 fundamental duty, is to promote effective competition in
16 wholesale power markets, to assure just and reasonable rates
17 in wholesale power markets.

18 If we recognize the differences in the nature of
19 the wholesale market, the regional nature of the wholesale
20 market, and the different structures, we have to promote
21 competition in both the bilateral markets and the organized
22 markets.

23 Now, last year, last December, we began a high-
24 level review on the state of competitive wholesale power
25 markets. We looked at both the organized market structure

1 and the bilateral market structure.

2 I have to say that I'm impressed that we're
3 acting today. This process, we announced it in December; we
4 had our first technical conference in February; we had a
5 second technical conference on competition in May; we had a
6 market monitoring conference in April, and we had a demand-
7 response conference in April, so we had four very
8 significant technical conferences between February, late
9 February, and early May, and then here we are acting on an
10 ANOPR.

11 I just want to commend the Staff for all the hard
12 work that has gone into this ANOPR.

13 Now, the competition review is a major
14 initiative. It's certainly a top priority of mine, and I'm
15 very pleased that we're taking this action today.

16 Now, the package of reforms that we're looking at
17 today and that we're poised to approve, does concentrate on
18 the organized markets. I want be very clear that that's not
19 because we think that there are no competitive challenges in
20 the bilateral markets; there are.

21 The reason this order today is focusing on the
22 organized markets, is because we're already acting to
23 address the challenges that are facing the bilateral
24 markets.

25 If you look at the OATT reform rule that we

1 approved in February, I think that the clear -- the primary
2 goal of that Order, is to prevent undue discrimination and
3 preference in transmission service, but it also has a
4 secondary goal of promoting competition.

5 I think it will make a major difference in the
6 bilateral markets.

7 We also have the competitive solicitation process
8 that Commissioner Spitzer is leading, and that's intended to
9 improve generation entry and to assure market access, and
10 that will help in the bilateral markets.

11 And I think the market-based rate rule that we're
12 going to consider shortly, that also will have a major
13 effect on the bilateral markets, so we are acting to address
14 the challenges in both the organized and bilateral markets,
15 we're acting in different proceedings.

16 Now, today we're acting to address some of the
17 challenges that face the organized markets, and there are
18 some distinct challenges.

19 I think there are different strengths and
20 weaknesses in the bilateral and organized market structures.
21 Staff has reviewed the major changes that we're proposing,
22 but I think it's clear that we need more effective demand
23 response.

24 The lack of effective demand response results in
25 higher wholesale prices, higher peak prices, greater price

1 volatility, and, I think, higher average prices.

2 It also causes the need to build perhaps more
3 generation capacity than would otherwise be the case.

4 Now, competitive markets also require a strong
5 energy infrastructure, and long-term contracts are one tool
6 to develop a strong energy infrastructure. So we have some
7 suggestions to address both the need for effective demand
8 response, as well as the need for long-term contracting.

9 Now, there's also a need to clarify Commission
10 policies with respect to market monitoring units in the
11 organized markets.

12 Up to this point, the Commission has had a very
13 flexible approach towards market monitoring, perhaps too
14 flexible of an approach, but at this point, we've
15 accumulated enough experience to make decisions and properly
16 define the role of market monitoring units.

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1 I think it is important though to recognize that
2 it is the Commission's duty to police wholesale power
3 markets to prevent market manipulation and prevent the
4 exercise of market power. That is the Commission's duty.
5 It is our responsibility to prevent unjust and unreasonable
6 wholesale power prices.

7 Now in the wake of the Energy Policy Act, we now
8 have the enforcement authority to properly police wholesale
9 power markets, and we are exercising that authority. I do
10 think market monitors can play an important role as we
11 discharge our duties, though.

12 Now the Commission held a conference on April 5th
13 to examine the role and the structure of market monitoring
14 units, and there was a broad recognition of the need for
15 sufficient independence as well as the need for
16 accountability.

17 The ANOPR proposes some specific reforms to
18 assure adequate independence by market monitoring units and,
19 as staff indicated, we also propose greater information
20 sharing to state commissions.

21 Now another proposed reform relates to RTO
22 governance and accountability. I think it is important that
23 RTOs and ISOs have good governance. The Commission has
24 placed in the past great emphasis on the independence of RTO
25 and ISO boards, and I think there is no doubt that RTO

1 boards are now independent of market participants.

2 However, there are persistent questions about
3 whether members and stakeholders have sufficient access to
4 RTO boards, and there are questions about whether RTO boards
5 and management are sufficiently responsive to the concerns
6 of members and stakeholders.

7 Now in order to address these concerns, the ANOPR
8 proposes to require some form of direct access to RTO boards
9 by members and stakeholders. We do not prescribe the exact
10 form this access may take and recognize there is more than
11 one way to assure this access.

12 The ANOPR proposes two approaches that could
13 provide such access, one being a hybrid board, and the
14 second being a board advisory committee composed of member
15 representatives.

16 We seek comment on these approaches. We also
17 recognize that other approaches may be developed, as well.

18 Now while competition remains national policy,
19 we recognize that competitive markets face challenges. My
20 personal view is that competition is sound policy when
21 combined with effective regulation. We are acting to
22 establish the best possible mixture of reliance between
23 reliance on competition and regulation on behalf of the
24 consumers.

25 Now I just again want to commend the staff for

1 their hard work on this. If you look, a core mission of
2 the Commission since 1935 is to guard against market power
3 exercised, to guard the consumer from exploitation, and I
4 think the market-based rate program is a key aspect of that
5 mission. So I thank you for your work. I think you have
6 done good work over the past year. It has been a major
7 undertaking.

8 So again, my thanks.

9 Colleagues? Jon?

10 COMMISSIONER WELLINGHOFF: Thank you, Joe.

11 I want to say first of all that the technical
12 conferences we had on competition and wholesale markets and
13 demand response I found very valuable for me personally, and
14 I think ultimately were very valuable to the entire
15 Commission in helping us and the staff formulate this ANOPR.
16 And I want to thank the staff for organizing those
17 conferences for all the hard work they did.

18 I also want to thank all the participants, again,
19 because without those participants I don't think we would be
20 where we are here today.

21 Today with the Commission acting on the
22 information and advice on what work is needed in some areas
23 of RTO and ISO markets, including demand response and market
24 monitoring, among other issues, I think we recognize that
25 we're starting the process but I want to emphasize that it

1 is not the end of the process, either.

2 This is a continuing dynamic thing here. So this
3 is one part, and there may be many parts to come as well.
4 But, Joe, I want to thank you for your leadership in this
5 areas, and my colleagues for their expeditious action here.
6 Finally, I want to thank the team for all their work on this
7 ANOPR.

8 Also I want to emphasize and encourage all
9 interested parties to not stop here either, to continue to
10 provide us comment and provide us input on this ANOPR,
11 because without that we can't move forward.

12 I think you all know my feelings on demand
13 response, and I am very happy that this first effort here
14 does in large part emphasize demand response. The ANOPR
15 encourages the ISOs and RTOs to coordinate, to identify
16 common issues and best practice solutions for direct
17 participation of demand resources in their energy and
18 ancillary service markets.

19 In particular we encourage the RTOs and ISOs to
20 work within the ISO/RTO Council to consider best practices
21 that may be applicable to the members' regions.

22 I want to indicate that I recently had an
23 opportunity to participate in a meeting of the board of
24 directors of all the RTOs and ISOs at their annual IRC
25 conference and discuss with them the benefits of

1 incorporating demand response into organized wholesale
2 markets.

3 As I understand, afterwards the IRC met and
4 agreed to develop a collaborative effort to investigate
5 demand response practices that could be considered for
6 implementation by individual RTOs and ISOs.

7 It is further expected that that plan for
8 collaboration by the IRC will be finalized at the IRC
9 meeting in late July. So I am pleased that our ANOPR will
10 provide support and direction for that effort of the IRC.

11 With regard to market monitoring I previously
12 noted that MMUs have the duty to serve not only the
13 respective RTOs and ISOs, but also certainly this
14 Commission, stakeholders, and other governmental bodies. In
15 this ANOPR, we propose steps that would facilitate those
16 important relationships.

17 With regard to the responsiveness of RTOs and
18 ISOs, I would like to note that we are asking commenters to
19 discuss whether we need to take additional steps to ensure
20 that minority interests are adequately represented in those
21 stakeholder processes. I think that is very essential,
22 especially for nascent industries like demand response.

23 With that, I am happy to support the ANOPR.
24 Thank you.

25 PRESIDING JUDGE: Thank you. Colleagues? Phil?

1 COMMISSIONER MOELLER: Thank you, Mr. Chairman.

2 It is my understanding that we wouldn't even have
3 this before us today if a lot of the team hadn't worked deep
4 into the night, or morning, working on some edits. So thank
5 you very much for your hard work and dedication.

6 This is an amalgam of about four different areas
7 that are related but somewhat distinct, as well. Again I
8 want to thank Commissioner Wellinghoff's leadership on
9 demand response. It is an issue I have been following for a
10 long time, as well.

11 It is serious, and it is something that we are
12 going to need in the next few years to shoulder us through
13 this period where demand is increasing and yet our
14 infrastructure deployment is behind.

15 The long-term power contract issue is one we
16 heard a lot about, as well, and so I encourage every entity
17 out there that has feelings on how to encourage more of
18 these to let us know their thoughts.

19 This ANOPR is just one, as you've mentioned,
20 Mr. Chairman, of many actions that this Commission has taken
21 to try and improve competitive markets. It is not the first
22 time we will be dealing with this larger set of issues, and
23 it is certainly not the last.

24 What I would not want people to walk away from is
25 a perception that only competitive markets have problems.

1 As you alluded to, there are problems in bilateral markets
2 as well. And particularly on demand response it is a lot
3 easier to implement it. It's not impossible to implement
4 it in bilateral markets, but it is a lot easier because the
5 price signals are clearer. And that is something we need to
6 keep in mind again as we move forward through a period of
7 years where demand response is going to be more important
8 than ever.

9 As a few of you have heard over the last couple
10 of weeks, I have drawn analogies to the telecom industry. I
11 spent probably 10 years at the state level implementing
12 competition in that industry, and it was--it was difficult.
13 There were a lot of difficult decisions. There were cost
14 allocation issues, network access issues, and yet if you
15 think back on it 25 years ago you didn't have a choice as to
16 who your telecom provider was.

17 You didn't have a cell phone. You had one
18 choice, and that was it. And now 25 years later, through a
19 lot of hard work, tough decisions, a constant evolution of
20 policy, it is an industry that was unimaginable 25 years
21 ago.

22 And I feel the same way about competitive markets
23 in the power field, that we are relatively early in the
24 process. It is not going to necessarily be easy, but it is
25 the law of the land. It is what will benefit consumers, and

1 this is one step of many steps to make it work better.

2 Thank you, Mr. Chairman.

3 PRESIDING JUDGE: Thanks. I would just like to
4 pick up--I mean, I agree. This is not the first step we
5 have taken to promote competitive markets; it is the latest
6 in a series of steps, and it is not the last word.

7 Colleagues? Suedeem?

8 COMMISSIONER KELLY: Thank you, staff. This was
9 really a heroic effort. You accomplished so much in such a
10 short time, and I think that the product that we have today
11 is very responsive to the concerns that were expressed to us
12 during our technical conferences.

13 I just want to focus at this point on two aspects
14 of our ANOPR: demand response, and RTO competitiveness.

15 I think that demand response and moving on the
16 front of demand response is one of the most important things
17 that we do today. At our last open meeting, we heard from
18 Steve Harvey and our Office of Market Oversight about the
19 importance that demand response will have this summer in
20 particular, but overall.

21 And NERC in 2006 issued its report pointing out
22 that demand continues to grow. We expect over the next 20
23 years a 16 percent increase in demand. At the same time, we
24 only expect a 6 percent increase in capacity. Some regions
25 are already below, or almost below their regional capacity

1 needs.

2 And so it is not only appropriate but necessary
3 that we focus on demand response to ensure that we continue
4 to maintain the reliability in our system.

5 So I support the NOPR with one exception, and I
6 wanted to talk about that. We propose here to eliminate
7 price caps during times of emergency either through
8 establishing--either through the elimination of a bid cap,
9 or an offer cap, or a market cap, or by having a debanned
10 curve for operating reserves.

11 I know that this was suggested to us by Professor
12 Holgan when he participated in our technical conference, and
13 I want for the record to say that I think that scarcity
14 pricing is something that we should look into. And I think
15 that we should be asking questions.

16 But I have two problems with how we approach it
17 today. One is that we propose to do it. And the second is
18 that we propose to do it in the name of demand response. I
19 think that it may indeed be helpful to have scarcity
20 pricing, but I think it is helpful to focus on it as a
21 potential advancement in the markets not only for demand
22 response but for all resources, including generation supply
23 resources.

24 I think that the timing of this proposal is
25 significant and that the devil's in the details. By

1 proposing to eliminate the bid cap, we hope to stimulate
2 more demand response. I think that while in theory that
3 makes sense, I think that our own studies, FERC's own staff
4 studies of the state of demand response in the United States
5 and the studies of others' show us that there are more
6 important impediments to stimulating demand response than
7 bid caps, at least at this point.

8 First and foremost is whether we are paying the
9 providers of demand response the value of demand response.
10 And in fact in our NOPR I would have preferred to see us
11 propose to pay providers the value. But we don't do that.
12 We ask the question whether they should be made an
13 additional payment in order to reflect the value of demand
14 response.

15 I think before we talk about limiting bid caps,
16 we should first establish that in an organized bid-based
17 auction market we should first be paying--we should be
18 allowing for additional payments for demand response to
19 adequately reflect its value; and we should be exploring
20 what the existing demand response markets are doing in that
21 regard, find out what best practices are, and propose to pay
22 the value and ensure that all markets are paying the value.

23 Only when you first establish that demand
24 response is being paid its value can you then talk about
25 whether a bid cap on what should be paid should be lifted.

1 The second issue is that studies have shown--
2 including one recently done by the Brattle Group--that how
3 much demand response will occur in a marketplace depends on
4 two things.

5 First, how rapidly utilities and regulators move
6 to install new pricing designs that provide the correct
7 price signals to customers. And particularly what the
8 Brattle Group was focusing on is dynamic pricing.

9 And secondly, how well customers respond to the
10 price signals.

11 A prerequisite to the provision of dynamic
12 pricing is the installation of advanced metering
13 infrastructure. Now we know that California is in the
14 process of implementing advanced metering infrastructure,
15 but our own staff report tells us that the penetration of
16 advanced metering infrastructure is very slight in the rest
17 of these markets.

18 Again I think that while it may be a good idea
19 to consider eliminating a cap and having scarcity pricing in
20 the long run, in the short run if you're going to do that
21 you need to ensure that people can respond to it on the
22 demand side. And the studies are clear that we need dynamic
23 pricing and we need better technology.

24 So I would have preferred to see us propose
25 incentives for establishing this kind of technology,

1 ensuring that utilities that invest in it or provide it can
2 be paid appropriately. And only after we enable consumers
3 to respond to higher prices for demand response, and only
4 after we ensure that consumers will be paid the value of
5 demand response, should we look at raising the bid price in
6 an emergency.

7 What concerns me about raising a bid price in an
8 emergency situation is that we will have the unintended
9 consequence of raising the cost of electricity without
10 enabling our consumers to adequately respond on the demand
11 side.

12 So I just wanted to underscore that I think the
13 timing is important, and that this should not be a proposal,
14 it should be something we think about, something for the
15 long term, maybe a long-term objective, but to propose the
16 elimination of a bid cap today seems to me somewhat like
17 issuing a mandate today that coal-burning power plants can
18 no longer release CO2.

19 While you might argue that that is a good way to
20 spur carbon sequestration, the fact of the matter is that we
21 don't have carbon sequestration technology and it is going
22 to take a while to get it in place.

23 So my suggestion is that we not propose to
24 eliminate the bid caps yet, but that we rather ensure that
25 the technology is in place to enable the demand resource to

1 participate effectively and that the demand resource in
2 these markets is paid its value.

3 Secondly, on the RTO responsiveness point, I
4 agree with every suggestion that we make, and every proposal
5 that we make in our ANOPR with the exception of one. That
6 is the proposal to increase RTO/ISO responsiveness to
7 stakeholders by establishing a hybrid RTO/ISO board of
8 directors that would be composed of both independent members
9 and non-independent members of stakeholders.

10 Under this proposal, each member would have a
11 seat on the board and participate fully in board decisions
12 with an equal vote. I don't think that such a hybrid board
13 is advisable, and I don't think it would be effective.

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1 Let me just explain why Order 888 in 2000,
2 required that an ISO or an RTO be independent from market
3 participants, so that the Board can provide regional
4 transmission and energy market services on a
5 nondiscriminatory basis.

6 Order 888 sets forth the fundamental principles
7 that the ISO should be independent of any individual market
8 participant or any one class of participants, for example,
9 transmission owners or end users.

10 Similarly, Order 2000 emphasized that
11 independence is the bedrock principle on which ISOs and RTOs
12 must be built.

13 Order 2000 also stressed that an RTO, quote,
14 "needs to be independent, in both reality and perception."

15 I believe that establishing a hybrid board, would
16 jeopardize the fundamental principle of independence upon
17 which the ISOs and RTOs are based.

18 I do not believe that it is a good idea to have a
19 board that contains market participants on it. I also
20 believe that establishing decisionmaking by entities with
21 narrowly-focused interests, would not result in good
22 decisionmaking.

23 For example, I believe it would be difficult for
24 the independent members of the board, to interact with the
25 non-independent stakeholder members that would be

1 representing their particular interests.

2 In our NOPR, we say that expect stakeholder
3 members to vote independently. I think that's pretty naive.
4 The reason that a stakeholder member is elected to the
5 board, is to vote its interest.

6 I was at the California ISO in 2000 when it had a
7 full stakeholder board, and it did not function well. I
8 think that the argument that having a majority of
9 independents, but a few stakeholders, doesn't really save
10 the day for me on independence, and I believe it would
11 inject in decisionmaking by an independent board, an extreme
12 amount of difficulty.

13 How do you deal with the stakeholder participant
14 on the independent board, if you're the independent board
15 member? How do you trust their decisions? Do you ignore
16 them? Do you include them, when you know that they are
17 participating in it for their own interests?

18 I do understand that a concern has been raised by
19 minority stakeholders, that the stakeholder process does not
20 give them a big enough voice and they are concerned that
21 their voice never gets translated, or rarely gets translated
22 to the board.

23 I hear that concern, but I think that there are
24 other ways of ensuring that the voice of minorities gets
25 translated to the board, short of electing a minority

1 stakeholder to the board.

2 I think an advisory committee is a good idea. I
3 also think that another proposal that should be considered,
4 is whether a stakeholder should elect board members.

5 I know that in some ISOs and RTOs, stakeholders
6 do elect board members, which, it seems to me, addresses the
7 issue directly, and similarly to how corporate America does,
8 by having shareholders elect board members.

9 So, with those two exceptions, I support the
10 ANOPR and even with those two exceptions, I still think that
11 it is a wonderful job that advances the competitiveness of
12 organized RTO and ISO organizations, and I thank you for
13 your efforts, and I'm pleased to vote for it.

14 CHAIRMAN KELLIHER: Commissioner Spitzer?

15 COMMISSIONER SPITZER: Thank you, Mr. Chairman.
16 The interesting aspect of this proceeding, is that you have
17 at least four or five separate narrow issues that have a
18 very synergistic effect with the global policy issue of
19 competition.

20 And the way this evolved, as our team worked on
21 these issues with the staffs of my colleagues and the Staff,
22 it enabled us to formulate some global positions.

23 I do have some remarks that I will post, and I'd
24 like to deliver those here as well, as well as post them on
25 the Internet.

1 It was interesting that Commissioner Moeller
2 referred to the analogy of telecommunications. And in
3 speaking with one of my colleagues yesterday, I described a
4 proceeding involving total element long-run incremental
5 cost, that took about nine months of my life, determining
6 some very arcane -- I would even use the term, "accounting
7 concepts."

8 Economics, I guess, is the gray science. And
9 ultimately, the Court of Appeals reversed the FCC order and
10 it went for naught, this proceeding.

11 I think the process undertaken today, with
12 technical conferences, in a very transparent process that,
13 although proceeding quickly, has been deliberative and open,
14 yields, I think, better lawmaking. That's not to disparage
15 the telecommunications practice, but really to say that the
16 parties, I think, can have more faith and confidence in this
17 Commission's deliberations on this issue, and that state
18 commissioners, ratepayer groups, and the industry, can take
19 some confidence that ultimate proceedings will yield
20 reasoned decisionmaking that will not be transitory and that
21 will give us confidence going forward.

22 Since the late 1970s, it has been Congressional
23 policy and, therefore, the policy of this Commission, to
24 foster competition in wholesale electric markets.

25 I am a supporter of competition and I believe the

1 policies this Commission has adopted to implement Congress's
2 clear pro-competition directives, have benefitted consumers.

3 Yet, over the past year, this Commission has
4 heard from various segments of the industry, that
5 competition, particularly in the organized markets, is not
6 working.

7 For example, we have heard that prices in the
8 organized markets, have risen faster and higher than in non-
9 RTO/ISO markets.

10 We have also heard from buyers and sellers of
11 power, that they cannot enter into long-term contracts,
12 which are a useful means to hedge against the volatility of
13 the short-term markets.

14 We have also been told that the stakeholders
15 question whether the market monitors of the RTOs and ISOs,
16 are effective in ferreting out improper behavior.

17 Today's action demonstrates that the Commission
18 has listened to those concerns and that we are taking steps
19 to evaluate and to address them where we can in the
20 organized wholesale electric markets.

21 In today's ANOPR, the Commission makes certain
22 proposals and also poses a variety of questions designed to
23 enhance competition in organized markets.

24 For example, one of the key issues raised, is
25 long-term contracting. In sum, the ANOPR seeks information

1 as to what the Commission may do to encourage long-term
2 contracts.

3 I continue to believe that long-term contracts,
4 as well as enforceability of contractual provisions, are
5 critical to the stability of wholesale electric markets.

6 For example, it is difficult to encourage
7 entities to build much needed infrastructure, including
8 fostering renewable resources, if those parties are unable
9 to enter into enforceable long-term contracts.

10 Therefore, I look forward to hearing from all
11 segments of the industry as to what we can do to encourage
12 parties to enter into long-term contracts.

13 Another issue addressed, is demand response. The
14 ANOPR includes several proposals to ensure that demand
15 resources, including retail demand resources, are treated
16 comparably to traditional supply resources in the provision
17 of energy and certain ancillary resources in the organized
18 markets.

19 For example, the ANOPR recognizes the retail
20 customers and aggregators of retail load, may not
21 participate in the organized wholesale markets today as
22 demand resources, because certain rules or technical
23 requirements act as barriers to their participation.

24 Today's ANOPR seeks to remove these barriers, so
25 that retail consumers and aggregators of retail load in

1 organized markets, can offer demand response as an
2 alternative resource.

3 A major point in the ANOPR, is to require RTOs
4 and ISOs to develop certain mechanisms that will allow
5 retail demand resources to offer demand response service in
6 a manner comparable to the services offered by traditional
7 supply resources.

8 By ensuring that all resources are treated
9 comparably, supply is driven by market principles, rather
10 than by command-and-control directives.

11 I support demand response, because I believe that
12 a properly designed demand resource program, will help to
13 dampen down wholesale power prices, increase awareness of
14 energy usage, provide for more efficient operation of
15 markets, and enhance reliability.

16 Further, attention to the demand side, affords
17 Government and industry, the moral authority to enhance
18 energy supply through necessary exploration, production, and
19 infrastructure.

20 Therefore, I look forward to reviewing the
21 comments on the demand response proposals, including remarks
22 on the steps we need to take to ensure that all resources
23 receive comparable treatment in the organized markets.

24 Finally, the ANOPR raises certain issues with
25 regard to the independence of market monitors and the

1 responsiveness of RTO and ISO boards. I Have an open mind
2 on the significant issues that must be addressed to ensure
3 organized markets are true markets that are operated for the
4 ultimate benefit of consumers.

5 I will, therefore, be particular attentive to
6 comments on these issues.

7 Finally, I wish to reiterate my support for
8 competition in bilateral markets, although outside the scope
9 of this specific proceeding.

10 For the foregoing reasons, I support this Order.

11 CHAIRMAN KELLIHER: Thank you. Shall we vote?

12 COMMISSIONER WELLINGHOFF: I've got a comment.

13 CHAIRMAN KELLIHER: Sorry.

14 COMMISSIONER WELLINGHOFF: I just have one
15 comment and maybe a clarification. I just want to make it
16 clear that I do understand that, today, we are proposing
17 potentially raised bid caps.

18 However, I would never vote to implement the
19 raising of bid caps, unless and until I believe we had
20 adequate demand response in those markets.

21 I just want to make that clear.

22 CHAIRMAN KELLIHER: Sure. I mean, we are making
23 proposals and we're also seeking comments, so I think -- an
24 ANOPR is an unusual thing. The last ANOPR I can recall the
25 Commission issuing, was Bastille Day of 2000, when the

1 Commission issued an ANOPR on OASIS II, and that was the
2 last.

3 So it's been a while. And an ANOPR, I think, is
4 something that's appropriate when you're almost certain
5 there's a problem and you have some idea of the solution or
6 solutions, but you're also seeking comments, so it really
7 falls between a Notice of Inquiry and a NOPR.

8 I think we are making proposals and we're also
9 very openly seeking comment, and this is the very beginning
10 of a proceeding.

11 COMMISSIONER WELLINGHOFF: I just want to make it
12 clear that we're not implementing anything raising the bid
13 caps today.

14 CHAIRMAN KELLIHER: Exactly. It's an ANOPR, so,
15 yes.

16 Colleagues, shall we vote?

17 SECRETARY BOSE: The vote begins with
18 Commissioner Wellinghoff.

19 COMMISSIONER WELLINGHOFF: I vote aye.

20 SECRETARY BOSE: Commissioner Moeller?

21 COMMISSIONER MOELLER: Aye.

22 SECRETARY BOSE: Commissioner Spitzer?

23 COMMISSIONER SPITZER: Mr. Chairman, it's not
24 Bastille Day, so no heads will roll.

25 (Laughter.)

1 COMMISSIONER SPITZER: I vote aye.

2 SECRETARY BOSE: Commissioner Kelly?

3 COMMISSIONER KELLY: Aye, with the exception of
4 my dissent, in part, and my concurrence, in part.

5 SECRETARY BOSE: Chairman Kelliher?

6 CHAIRMAN KELLIHER: Aye. Thank you very much to
7 the Staff. I appreciate it. I know some of you were up
8 late, and I am grateful.

9 SECRETARY BOSE: The next items for discussion
10 this morning, are E-1 and E-20. They are concerning the
11 rulemaking on market-based rates, and an Order concerning
12 the Western System's Power Pool, respectively.

13 We will have a presentation by Elizabeth Arnold,
14 from the Office of General Counsel, and Deborah Dalton, from
15 the Office of Energy Markets and Reliability.

16 They are accompanied by Marek Smigielski, Melissa
17 Lozano, and Jerry Pederson from the Office of Energy
18 Markets and Reliability, and also Deborah Leahy and Melissa
19 Mitchell, from the Office of General Counsel, and Demetra
20 Anas, from the Office of Enforcement.

21 MS. DALTON: Good morning, Chairman and
22 Commissioners. I will provide an overview of the technical
23 issues addressed in E-1, and Elizabeth will follow with an
24 overview of the implementation process and legal issues of
25 E-1 and a summary of E-20.

1 E-1 is a Draft Final Rule which codifies for the
2 first time, the Commission's standards under which public
3 utilities may obtain and retain market-based rate authority
4 for sales of electric energy, capacity, and ancillary
5 services.

6 The Draft Final Rule reflects significant changes
7 in the Commission's market-based rate program, since its
8 beginnings in the 1980s, including a more rigorous review of
9 a seller's market power, and improved filing requirements.

10 The Draft Rule reforms the current four-pronged
11 analysis that currently examines generation market power,
12 transmission market power, other barriers to entry, and
13 affiliate abuse, into a more traditional horizontal and
14 vertical market power analysis.

15 The horizontal analysis considers generation
16 market power, and the vertical analysis considers
17 transmission market power and other barriers to entry.

18 The Draft Rule also codifies the Commission's
19 affiliate abuse restrictions, and makes compliance with
20 those restrictions, an express condition of market-based
21 rate authority.

22 With respect to horizontal market power, the
23 Draft Rule retains the indicative, uncommitted market power
24 screens that have been used by the Commission since 2004,
25 with certain modifications that reflect the Commission's

1 experience in applying these screens and the comments
2 received in this proceeding.

3 In particular, the Draft Rule adopts two
4 indicative market power screens, the uncommitted market
5 share screen with the 20-percent threshold, and the
6 uncommitted pivotal supplier screen, each of which will help
7 to determine whether sellers may have market power and
8 should be further examined.

9 Sellers that fail either screen, will be
10 rebuttably presumed to have market power, however, such
11 sellers will have full opportunity to present evidence
12 demonstrating that, despite a screen failure, they do not
13 have market power.

14 With regard to the default relevant geographic
15 market, the Draft Rule provides that the Commission will use
16 a seller's balancing authority area or the RTO or ISO
17 market, as applicable, as the default relevant geographic
18 market.

19 However, where the Commission has made a
20 specific finding that there is a submarket within an RTO,
21 that submarket becomes the default relevant geographic
22 market for sellers located within the submarket, for
23 purposes of the market-based rate analysis.

24 The Draft Rule modifies the native load proxy for
25 the market share screens, from the minimum peak day in the

1 season, to the average peak native load, averaged across all
2 days in the season.

3 In addition, sellers are given the option of
4 using seasonal capacity instead of nameplate capacity.

5 The Draft Rule eliminates Section 3527 of the
6 Commission's current Regulations, which was adopted in 1996,
7 and which provides that sellers do not have to demonstrate
8 lack of market power in generation for sales from capacity
9 for which construction commenced on or after July 9, 1996.

10 All sellers will now have to perform a
11 horizontal analysis for the grant of market-based rate
12 authority, regardless of when their generation was
13 constructed.

14 With regard to vertical market power, and, in
15 particular, transmission market power, the Commission
16 continues the current policy under which an open access
17 transmission tariff is deemed to mitigate a seller's
18 transmission market power.

19 However, in recognition of the fact that OATT
20 violations may nonetheless occur, the Rule states that a
21 finding of a nexus between the specific facts relating to
22 the OATT violation and the entity's market-based rate
23 authority, may subject the seller to revocation of its
24 market-based rate authority, or other remedies the
25 Commission may deem appropriate, such as disgorgement of

1 profits or civil penalties.

2 In addition, the Draft Rule creates a rebuttable
3 presumption that all affiliates of a transmission provider,
4 should lose their market-based rate authority in each market
5 in which their affiliated transmission provider loses its
6 authority as a result of an OATT violation.

7 With regard to affiliate abuse, the Draft Rule
8 contains specific affiliate restrictions and provides that
9 these restrictions must be satisfied on an ongoing basis, as
10 a condition of obtaining and retaining market-based rate
11 authority.

12 These restrictions are aimed at protecting the
13 captive customers of franchised utilities. They prohibit
14 power sales between a franchised public utility with captive
15 customers, and any market-regulated power sales affiliate,
16 with first receiving Commission authorization for the
17 transaction.

18 They also address separation of functions, the
19 sharing of market information, sales of non-power goods or
20 services, and power brokering.

21 With regard to rates for sellers found to have
22 market power or presumed to have market power, the Draft
23 Rule contains default cost-based rates that sellers may use,
24 depending on the length of the service provided.

25 Alternatively, sellers may propose other cost-

1 based methods of mitigation tailored to their particular
2 circumstances.

3 The Draft Rule concludes that the Western
4 System's Power Pool or WSPP Agreement rates, may be unjust,
5 unreasonable, or unduly discriminatory or preferential for
6 sellers that have market power or are presumed to have
7 market power.

8 Therefore, in a Draft Order being issued
9 concurrently with this Draft Final Rule, the Commission is
10 instituting a proceeding under Section 206 of the Federal
11 Power Act, to investigate whether, for sellers found to have
12 market power, or presumed to have market power in a
13 particular market, the rates under the WSPP Agreement, are
14 just and reasonable in such market.

15 Elizabeth will provide further details on this
16 companion Order.

17 The Draft Rule does not impose an across-the-
18 board, must-offer requirement for mitigated sellers, because
19 there is insufficient record evidence to support instituting
20 a generic must-offer requirement.

21 However, the Commission will consider whether
22 such mitigation is necessary, on a case-by-case basis.

23 The Draft Rule requires mitigation, only in the
24 market in which the seller has been found to possess or
25 chosen not to rebut the presumption of market power. A

1 seller may sell at market-based rates in other areas.

2 The Draft Rule allows mitigated sellers to make
3 market-based rate sales at the metered boundary between a
4 mitigated market and a market in which the seller has
5 market-base rate authority, subject to certain conditions,
6 including a record retention requirement and restrictions on
7 affiliate sales back into the mitigated market.

8 MS. ARNOLD: The Draft Rule adopts several
9 reforms to improve the administration of the market-based
10 rate program.

11 The Draft Rule establishes two categories of
12 sellers with market-based rate authorization: Category I
13 sellers, generally consist of wholesale power marketers or
14 producers that own or control 500 megawatts or less of
15 generating capacity, in aggregate, per region; own little or
16 no transmission; and that are not affiliated with the public
17 utility with the franchised service territory in the same
18 region as the seller's generation assets.

19 Category I sellers will not be required to file
20 regularly-scheduled, update market power analyses. The
21 Commission will monitor any market power concerns for these
22 sellers, through the change in status reporting requirements
23 and Electric Quarterly Reports.

24 Category II sellers consist of all other
25 sellers. Category II sellers, in addition to the change in

1 status reports and EQRs, will be required to file regularly-
2 scheduled updated market power analyses.

3 To ensure greater consistency in the data used to
4 evaluate Category II sellers, the Rule requires each
5 Category II seller to file updated market power analyses for
6 its relevant geographic markets, on a schedule that will
7 allow examination of the individual seller at the same time
8 that the Commission examines other sellers in the region.

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1 The Commission will continue to make findings on
2 an individual seller basis but will have before it a
3 complete picture of the uncommitted capacity and
4 simultaneous import capability into the regions under
5 review.

6 In addition, the draft rule adopts several
7 standard tariff provisions rather than a Market-Based Rate
8 tariff of general applicability. Two of these standard
9 tariff provisions must be included in each Market-Based Rate
10 seller's tariff.

11 Other standard provisions must be included in a
12 seller's Market-Based Rate Tariff to the extent that they
13 are applicable based on the services provided by the seller.

14 Sellers may also elect whether to transact under
15 a single Market-Based Rate Tariff for an entire corporate
16 family or under separate tariffs.

17 The draft rule addresses arguments regarding the
18 Commission's legal authority to adopt a Market-Based Rate
19 regime and about consistency of the Market-Based Rate
20 Program with filing requirements in the Federal Power Act.

21 The draft rule concludes that the Program
22 complies with the statutory and judicial standards for
23 acceptable Market-Based Rates.

24 The Federal Power Act leaves the timing and form
25 of filings to the Commission's discretion, and the rule

1 finds that the multiple layers of filing and reporting
2 requirements incorporated into the Market-Based Rate
3 Program, including change in status filings, quarterly
4 filings of transition-specific, transaction-specific data in
5 EQRs, and updated Market Power Analyses in conjunction with
6 market manipulation rules and enhanced market oversight and
7 enforcement provide adequate protection from excessive rates
8 and are in full compliance with the Federal Power Act.

9 Turning to E-20, as previously noted the draft
10 order in E-20 institutes a proceeding under 206 of the
11 Federal Power Act to investigate whether the WSPP Agreement
12 Rates for coordination energy sales is just and reasonable
13 for a public utility seller in a market in which such seller
14 has been found to have market power or is presumed to have
15 market power.

16 The draft order notes that when the WSPP
17 Agreement was initially accepted by the Commission in 1991,
18 there were 40 members. Now there are over 300 members.
19 Additionally, the WSPP Agreement is now used by entities not
20 only in the Western Interconnection, but throughout the
21 Continental United States.

22 Further, the demand charge component of the WSPP
23 Agreement's ceiling rate is based on the costs of only 18 of
24 the original WSPP Agreement members in 1991, utilizing 1989
25 data.

1 The investigation in E-20 is limited to the
2 justness and reasonableness of the WSPP Agreement cost-based
3 ceiling rates for coordination energy sales by public
4 utility sellers that are found to have or are presumed to
5 have market power.

6 And if the existing WSPP Agreement rates are
7 unjust and unreasonable for such sellers, how the Commission
8 should establish a just and reasonable rate.

9 If the WSPP Agreement ceiling rate ultimately is
10 found not to be just and reasonable, E-20 seeks comments on
11 whether the Commission should set a just and reasonable Up-
12 To Rate based on:

13 1) Individual sellers' costs;

14 2) The costs of a representative group of WSPP
15 sellers, including how such Agreement-wide rates should be
16 calculated; or

17 3) A different methodology.

18 E-20 provides all interested persons an
19 opportunity to address these issues through a paper hearing.
20 At this time I would like to invite all the other team
21 members who are present to stand.

22 (Team members stand.)

23 (Applause.)

24 MS. ARNOLD: This concludes the Staff's
25 presentation and we would be happy to answer any questions.

1 PRESIDING JUDGE: Thank you, very much. I really
2 want to commend the Staff for their work on this rulemaking.
3 This began in May of 2006. It began under the Unscien
4 regime, and it is really one of the more complicated areas
5 of FERC law.

6 The record is very substantial, but I think you
7 have done really fine work on this final rule. I think that
8 summary that you just presented was excellent.

9 Let me just make some comments, though, about
10 what we are doing today in terms of why we are doing it, and
11 what the effect of what we are doing should be.

12 We are really taking an important step to
13 strengthen our Market-Based Rate Program in order to prevent
14 the exercise of market power. I think the action we are
15 taking is very timely.

16 Last Monday, this Monday, the Supreme Court
17 decided not to review the Lockyer Decision, and I think that
18 was a very important action. The decision by the Supreme
19 Court not to look at Lockyer really means that it
20 effectively removes any remaining question about the legal
21 authority of the Commission to authorize Market-Based Rate
22 sales.

23 So I think it is clear that we have full legal
24 authority to promote competition and to authorize Market-
25 Based Rate sales.

1 The action we are taking today is not the first
2 action to strengthen the Market-Based Rate Program. We
3 have actually taken four major actions since 2001 to
4 strengthen the Market-Based Rate Program.

5 In 2001 we issued rules that strengthened the
6 reporting requirements that were very important to the Ninth
7 Circuit's reasoning in the Lockyer Decision.

8 In 2004 we changed the Generation Market Power
9 Test and raised the bar to demonstrate the absence of
10 Generation Market Power.

11 In 2004, I believe--it might have been 2005--we
12 issued the Change of Status Final Rule, again intending to
13 prevent the accumulation of market power after receipt of
14 Market-Based Rate Authorization.

15 Then beginning in 2005 we began to revoke Market-
16 Based Rates for companies that violated the conditions of
17 their authorization. Namely, the requirement to make
18 electronic quarterly reports; and to file triennial
19 analysis.

20 I think that action is important because it
21 really showed a view on behalf of the Commission that
22 Market-Based Rate Authorization is a privilege, it's not a
23 right, and if you violate the conditions of the privilege we
24 will revoke it.

25 So I think those four actions were very

1 significant steps that we took since 2001 to strengthen the
2 program. Last year we issued the proposed rule that has led
3 us to the action we are taking today.

4 Last December in the Ninth Circuit contract cases
5 the court was very critical of the Commission's Market-Based
6 Rate Program. But the program that they were criticizing
7 was the program as it existed in the year 2000 and 2001.
8 And if you look at the major changes that we have made that
9 I just reviewed since 2001, the program that the court
10 criticized in the Long-Term Contract Case really bears
11 little resemblance to the Program as it exists today.

12 We are again making another important change
13 today with the Final Rule.

14 As I indicated in my earlier comments on the
15 ANOPR, the Commission's policy has never been deregulation.
16 We have never stopped regulating wholesale power sales. In
17 fact, we do rely on competition but we have always relied as
18 well on regulation.

19 We have been strengthening our regulation of
20 wholesale power sales, and we have been steadily
21 strengthening this program. And I think we take a major
22 step today.

23 Now effective oversight is a very important
24 aspect of the Commission's regulation, and it is necessary
25 to prevent exploitation by noncompetitive electric power

1 companies. It is necessary for us to discharge our core
2 mission. I think we have taken--we have made very
3 significant changes to our oversight and enforcement program
4 over the past seven years.

5 If you look back to seven years ago, the
6 Commission did have an enforcement staff. It had a very
7 modest, a very small enforcement staff that was dedicated
8 largely towards hearing complaints about hydro license
9 violations, certificate violations, and certain affiliate
10 rules.

11 Now we have an Office of Enforcement that's large
12 and growing, and it is policing. It is looking completely
13 across both power and gas markets.

14 Seven years ago the Commission had virtually no
15 civil penalty authority. Now we have the authority to
16 impose penalties up to a million dollars per day per
17 violation. And seven years ago it did not violate Federal
18 electricity law to manipulate power markets; now there is an
19 express prohibition in the Energy Policy Act 2005. We have
20 issued implementing rules, and we are actively investigating
21 alleged manipulation.

22 So our enforcement and oversight program are
23 critical. If you compare the situation now to the situation
24 in 2000 and 2001, it really is night and day.

25 I just want to thank Congress for giving us the

1 tools that we needed, and we probably could have used back
2 in 2000, but I am glad we have them now and we are certainly
3 exercising them.

4 I think the purpose of this Rule is very clear.
5 It is to strengthen our Market-Based Rate Program. It is to
6 prevent the exercise of market power. And I accidentally
7 misdirected certain comments towards the last team, and I
8 want to repeat them towards you, just about the importance
9 of the Market-Based Rate Program. It is one of the more
10 complicated areas of FERC law. We have had a mission since
11 1935 to prevent the exercise of market power, to guard the
12 consumers from exploitation, and the Market-Based Rate
13 Program is a critical aspect of that duty, and I just want
14 to thank you for all your work on this. And I am glad we
15 are issuing this Final Rule today.

16 So thanks for your work. Colleagues? Jon?

17 COMMISSIONER WELLINGHOFF: Mr. Chairman, thank
18 you.

19 First I do want to thank Elizabeth and Debora and
20 all the members of your team. It is great work on this
21 Final Rule. I want to assure you that I did read every page
22 of it.

23 (Laughter.)

24 COMMISSIONER WELLINGHOFF: In fact, I think an
25 additional requirement we ought to put in the Rule is that

1 any applicant has to prove they've read the entire rule to
2 get Market-Based Rates.

3 (Laughter.)

4 COMMISSIONER WELLINGHOFF: But the Rule really is
5 the gate to getting the Market-Based Rate but, Mr. Chairman,
6 I think it is very appropriate what you said, that beyond
7 that gate we have all these other processes and procedures
8 in enforcement and oversight that are essential that were
9 not in place before now that now is in place, that once
10 Market-Based Rates are authorized it is not the Wild West.
11 It is not open season.

12 They then still are very much in continued
13 oversight, and I think with that I certainly support the
14 Rule. Thank you.

15 PRESIDING JUDGE: Thank you. Colleagues?

16 MR. CANON: Commissioner, I would have to
17 interject that I think forcing anybody to read the entire
18 Rule could be perceived as a barrier to entry.

19 (Laughter.)

20 PRESIDING JUDGE: Commissioner Spitzer?

21 COMMISSIONER SPITZER: Thank you, Mr. Chairman.

22 For many years this Commission has struggled with
23 the appropriate standard to evaluate whether a public
24 utility can exercise market power with regard to its
25 wholesale sales.

1 This Rule, in conjunction with other actions we
2 have taken in the past year will ensure that Market-Based
3 Rates charged by a public utility are just and reasonable,
4 and that the wholesale energy markets will remain
5 competitive.

6 We had to make some difficult decisions in the
7 Final Rule. However, given our ultimate duty of ensuring
8 that utilities charge just and reasonable rates, I believe
9 that the balances achieved in the Final Rule are the correct
10 ones.

11 I am particularly pleased that we are now
12 actually issuing this Rule. Industry has been operating
13 under an Interim Market Power Test and has been awaiting a
14 decision for several years.

15 Having read the Rule and the other related
16 papers, I understand and appreciate why we needed to take
17 the time that we did. However, I think we all agree that
18 the industry, including consumers, will benefit from our
19 action today because we are now providing regulatory
20 certainty as to how market power filings will be reviewed
21 and processed.

22 Although the Order does not make drastic changes
23 to the interim measures we have followed over the past few
24 years, we are providing more certainty with respect to our
25 requirements and that benefits industry, consumer, and

1 energy markets.

2 Finally, I would like to thank staff for their
3 hard work and persistence over the past few years. Each of
4 their contributions has made this Final Rule a better
5 product.

6 And finally, to my friends in the Wild West, I
7 would like to point out that with regard to Western Systems
8 Power Pool, this is an inquiry not a determination, and that
9 we would be derelict in our duty, having had this matter
10 brought to our attention, not to pursue it on behalf of
11 ratepayers throughout the country.

12 For these reasons, Mr. Chairman, I support the
13 Final Rule.

14 PRESIDING JUDGE: Colleagues? Commissioner
15 Kelly?

16 COMMISSIONER KELLY: I also support the Final
17 Rule. I thank you all for working on it. The Market-Based
18 Rate Rulemaking involves a lot of complex issues, and I feel
19 that we have struck an appropriate balance in this Rule and
20 a balance that we can all be proud of.

21 It is, as Commissioner Spitzer mentioned, it is
22 difficult to achieve the appropriate balance with some of
23 these issues, they're so complex, and positions can be very
24 extreme. I would like to elaborate on one thing that Debora
25 mentioned in her overview.

1 She explained that mitigation can be tailored to
2 the circumstances. I just wanted to touch on that because
3 a number of organizations argued in their comments that
4 cost-based mitigation is not enough if the mitigated seller
5 can just shift all of his or her sales to a neighboring
6 region where she or he has Market-Based Rate Authority.

7 These organizations wanted a rule that mitigated
8 sellers should be required to offer cost-based power in the
9 mitigated market, or else customers in that market might not
10 have access to sufficient supplies to serve their own needs.
11 We are, through this Rule, cognizant of that concern, and
12 that is not an outcome we want to have: insufficient
13 supplies serving needs.

14 The Rule essentially finds that these concerns
15 cannot be addressed generically, however, because they are
16 so dependent on specific circumstances such as the existence
17 of available transmission capacity to reach alternate
18 suppliers.

19 So, accordingly, the Rule declines to put such a
20 must-offer requirement in place on a generic basis, but it
21 notes that parties can, as Debora mentioned, make a case-by-
22 case showing of need for such specific mitigation, including
23 a must-offer requirement.

24 In my own preliminary thinking on the subject, I
25 suspect that such a case-by-case showing would have to

1 demonstrate that the mitigated seller is the only entity
2 physically able to meet all of the buyers' needs. If other
3 entities are physically able to meet those needs, then I'm
4 not sure that a must-offer requirement would be appropriate.

5 However, if only the mitigated seller could meet
6 the customers' needs, then applying a cost-based must-offer
7 requirement would appear to be appropriate, and in fact
8 basically equivalent to a return to the old regulatory
9 compact of guaranteed cost recovery plus just and reasonable
10 return in exchange for an obligation to serve where no one
11 else can provide the service.

12 But again I think that any such argument would be
13 highly dependent on the particular circumstances and thus
14 would require a case-by-case determination to achieve an
15 appropriate outcome.

16 Regarding E-20, I also would like to praise the
17 West for giving us the classic, the WSPP Agreement. I think
18 we all recognize the positive effects on liquidity and the
19 smooth operation of the bilateral market that that has
20 achieved not only in the West but elsewhere as its use has
21 spread across the country.

22 I think the fact remains, however, that the cost-
23 based ceilings in the WSPP Agreement are 18 years old, and
24 they are based on costs of only 18 companies that were
25 originally deemed 18 years ago to be representative of the

1 WSPP, and changes happen over 18 years.

2 There are now 300 members, instead of only 40
3 and, unlike the original members, many of the new members do
4 not even operate in the Western Interconnection.

5 So I think it is appropriate to update the rate.
6 My daughters tell me it is appropriate every five or ten
7 years to look at your hair style and decide whether it needs
8 an update. So I think it is probably a good idea here.
9 Maybe it doesn't need an update, but take a look.

10 Thank you.

11 PRESIDING JUDGE: Commissioner Moeller.

12 COMMISSIONER MOELLER: Thank you, Mr. Chairman.

13 I actually have a few questions for the team. I
14 guess first of all for both, for the team leaders, can you
15 give us an idea, or by your team members, what were some of
16 the other proposals that you contemplated as you deliberated
17 and put together the Final Rule?

18 MR. PEDERSON: Commissioner, there were several
19 proposals we looked at. Let me start with one that the
20 audience would probably be very pleased with, which is the
21 Standard Tariff.

22 We had looked at and had proposed in the NOPR to
23 standardize the tariffs for everyone, one-size-fits-all. We
24 were trying to get--we have a lot of tariffs out there even
25 within corporate families where they have several, and they

1 have different terms and conditions, and there was no
2 conformity on any of them, on many of them.

3 So we had proposed to do a standard tariff. The
4 E-1, I don't know that anyone came in and said that's a
5 great idea, and so we rethought about that concern and how
6 we could address it.

7 What E-1 does is, rather than impose a standard
8 tariff, it takes a different look at it and says that here's
9 two required provisions that you're going to have to have in
10 your Market-Based Rate Tariff. It also says that there are
11 other standard services, and the Commission has standard
12 language for those services. If you're providing those
13 services, here's the tariff language we want in your tariff.

14 But beyond that, it allows the seller to come in
15 with their own terms and conditions. And part of the
16 benefit we saw there was the transparency. If the sellers
17 want to put the terms and conditions on their tariff, that's
18 a good thing in terms of transparency.

19 I think the Order notes that the Commission won't
20 be reviewing those. And so that was something that--a
21 proposal that we had kicked around.

22 Also, another one, another proposal that came out
23 in the NOPR that we did not adopt was the Asset Managers.
24 We had said in the Affiliate Section that we were going to
25 treat asset managers as though they were affiliated with the

1 company they were working for.

2 There was a lot of confusion out there with that.
3 I think the intent was that you couldn't circumvent the
4 affiliate restrictions through an asset manager, and we got
5 a lot of push-back on that. We've had a lot of confusion
6 out there.

7 So we relooked at that problem, as well, and
8 said, well, we don't need to use that phrase. Some
9 commenters I think took it literally. We said, we don't
10 need to approach it that way. So we've dropped that and,
11 instead of that, you would want to adopt a no-conduit
12 provision which simply says you cannot use a third party to
13 get around the affiliate restrictions. So that was another
14 change.

15 Another change dealt with the OATT violations.
16 Originally in the NOPR what NOPR proposed was that if a
17 transmission provider violated its OATT in a significant way
18 and there was a nexis to the Market-Based Rate Authority,
19 that--and the Commission took the step of revoking the
20 Market-Based Rate Authority, that all affiliates in that
21 control area would likewise lose their Market-Based Rate
22 Authority.

23 E-1 takes a different look and a different
24 approach on that. What it says: In those circumstances
25 that the affiliates will have a rebuttable presumption, that

1 they should lose their Market-Based Rate Authority. And I
2 think the thinking there was to allow the affiliate to come
3 in and be able to make a demonstration before the Commission
4 that they weren't involved--they may have benefitted
5 indirectly, but they had no knowledge and they should not
6 have their Market-Based Rates revoked.

7 Another change that we made from the NOPR itself
8 was on the triennial reviews. The NOPR proposed a regional
9 approach. A "regional approach," we defined that in an
10 appendix of the NOPR. The original proposal was nine
11 regions, three per year.

12 There was a lot of concern in the industry that
13 they were going to be in here all the time making triennial
14 reviews. And what E-1 does is it shrinks those into six
15 regions, two a year. That is going to reduce the number of
16 times they come in here.

17 Those are the main changes. I think there was
18 another one where in the NOPR the Commission originally
19 proposed to allow known and measurable changes in the
20 Market-Based Rate analysis.

21 The E-1 looked at that proposal and decided not
22 to go with the known and measurable for the Market-Based
23 Rate Program because the whole function of the Market-Based
24 Rate Program is taking a snapshot in time, just looking at
25 what are the actual facts.

1 We will look at the actual facts. We will
2 evaluate the actual facts. And if they change, you have to
3 come in and let the Commission know.

4 So those are I think the main changes.

5 COMMISSIONER MOELLER: That's helpful. I hope
6 that that perspective gives some benefit to people who will
7 be reading all 670 pages.

8 A couple of more questions. And, Debra maybe
9 this is for you, maybe it is for Elizabeth, but there is
10 talk of a submarket within an RTO. Can you elaborate on
11 what a "submarket" might look like?

12 MR. PEDERSON: I'll do that one.

13 (Laughter.)

14 COMMISSIONER MOELLER: I'm sorry, Debra, I didn't
15 mean to put you on the spot.

16 MR. PEDERSON: I was focused on the geographic
17 regions, so maybe I should do that one.

18 I think a "submarket," there's a couple of
19 things. A submarket is just a market. A submarket, the way
20 we're using the term in E-1, has to do with we talk a little
21 bit about the RTOs, but also in bilateral markets where the
22 Commission has default geographic markets. If the
23 Commission--if there's a load pocket, for example, and the
24 Commission determines that there is a submarket, there's a
25 market within a market--for example, New York City would be

1 an example. I think probably PJM East would be an example
2 of where the Commission has found load pockets.

3 What E-1 says is--or a submarket. What E-1 says
4 is that we will now consider those as the default geographic
5 market. So if you think about the New York ISO, you have
6 the New York ISO that sellers can use the New York ISO as
7 the default footprint. However, if you are in New York
8 City, the Commission has found that to be a submarket. That
9 is going to be your market, default market, to look at.

10 The E-1 also states that the Commission will look
11 at--will consider additional submarkets as evidence is
12 presented, so it is not frozen in time. In addition, what
13 E-1 does is it provides guidelines as to what constitutes a
14 market.

15 The Order also makes clear that when we're
16 talking about what constitutes a "market," it applies not
17 only to expanding the default geographic markets, but it
18 equally applies to a submarket shrinking that market. And
19 primarily the guideline is, the first thing we look at would
20 be the frequently binding physical transmission
21 constraints. That's your first cut.

22 So if there's a frequently binding transmission
23 constraint, that kind of gives you an idea of where the line
24 from a market may or may not--may occur, and then of course
25 we would look at other factors.

1 COMMISSIONER MOELLER: But you could arguably
2 have a submarket within New York City, too.

3 MR. PEDERSON: Presumably, sure.

4 COMMISSIONER MOELLER: Thank you.

5 Seasonal capacity is an item that's discussed
6 related to--you've changed the averaging, or you're
7 proposing the averaging based on seasonal. My concern is
8 hydro and how that can impact.

9 As most people who know hydro know, flows differ
10 and seasons are important.

11 MR. PEDERSON: Well I think the Rule recognizes
12 that. Originally, going back to the April 14th Order when
13 we redid the market screens, we allowed only for Nameplate
14 Capacity. In E-1, E-1 comes out and says you can use
15 Nameplate or Seasonal capacity.

16 Now in terms of hydro, it recognizes hydro is a
17 little bit different. Hydro has the same options. They can
18 use Nameplate or Seasonal Capacity. But in lieu of those,
19 they can also come in and, with a five-year average of their
20 capacity for the last five years, and also in conjunction
21 over that they would have to do a sensitivity analysis of
22 the low and the high year.

23 So hydro has got a lot of flexibility there.
24 They can go to the Nameplate, the Seasonal, or do the five-
25 year approach in lieu of that.

1 COMMISSIONER MOELLER: Okay. Good explanation.
2 Finally, you'll see I made a comment about the
3 '96 Exemption. If anybody has any comments on that, I want
4 to make it clear that if were to have gone another way, that
5 universe of players is very small, and we could still do a
6 206 on anybody who had market power, if we had gone a
7 different direction.

8 MS. LEAHY: That's true. When the Commission
9 established that exemption back in 1996, it specifically
10 acknowledged that the entity, the seller, would still have
11 to come in on a -- you know, to obtain market-based rate
12 authority, and the Commission specifically said that it
13 would not ignore specific evidence, if an intervenor were to
14 bring it.

15 And the Commission expected at that point in
16 time, that in the course of the market-based rate
17 application, and intervenor could come in and produce
18 evidence that, well, notwithstanding that the seller had
19 only post-'96 generation, it still posed some market power
20 concerns and that would be addressed.

21 COMMISSIONER MOELLER: Okay, I've taken enough
22 time. Thank you, Mr. Chairman.

23 CHAIRMAN KELLIHER: Any other comments?
24 Colleagues?

25 (No response.)

1 CHAIRMAN KELLIHER: No? Let's vote.

2 SECRETARY BOSE: We will take a vote on both
3 items together, beginning with Commissioner Wellinghoff.

4 COMMISSIONER WELLINGHOFF: I vote aye on both
5 items.

6 SECRETARY BOSE: Commissioner Moeller?

7 COMMISSIONER MOELLER: I vote aye, noting my
8 partial dissent in E-1, please.

9 SECRETARY BOSE: Commissioner Spitzer?

10 COMMISSIONER SPITZER: I vote aye.

11 SECRETARY BOSE: Commissioner Kelly?

12 COMMISSIONER KELLY: Aye.

13 SECRETARY BOSE: Chairman Kelliher?

14 CHAIRMAN KELLIHER: Aye.

15 Thank you very much, thanks to my colleagues,
16 thank you to the staff for excellent work, a good day's
17 work. This meeting is adjourned.

18 (Whereupon, at 11:33 a.m., the meeting was
19 adjourned.)

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