

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25

BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

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

862ND COMMISSION MEETING
OPEN MEETING

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

Thursday, June 17, 2004
10:15 a.m.

1 APPEARANCES:

2 COMMISSIONERS PRESENT:

3 CHAIRMAN PAT WOOD, III, Presiding

4 COMMISSIONER NORA MEAD BROWNELL

5 COMMISSIONER JOSEPH T. KELLIHER

6 COMMISSIONER SUEDEEN G. KELLY

7

8

9

10

11

12

13

14

15

16

17

18

19 ALSO PRESENT:

20 DAVID L. HOFFMAN, Reporter

21

22

23

24

25

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

2 (10:15 a.m.)

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

8 Let's start, as we always do, although, I should
9 add, with less of an encumbrance than we've had in the past,
10 with the Pledge to our Flag.

11 (Pledge of Allegiance recited.)

12 CHAIRMAN WOOD: Before we start today, I wanted
13 to talk about something that isn't so happy, our first
14 opportunity to talk about further revelations that have come
15 out of the purported conversations with Enron traders during
16 the California Energy crisis.

17 These tapes that have come to light in the
18 proceeding here in recent weeks -- I just wanted to kind of
19 reiterate what I said two years ago when we found the memos
20 from the Legal Department that discussed the same type of
21 behavior that gave rise to Death Star, Ricochet and the
22 others.

23 The Gelinas Report found last Spring, the
24 following point that I was reminded of as I heard the
25 transcript of these tapes, that Enron's corporate culture

1 fostered disregard for the American energy customer.

2 The success of the Company's trading strategies,
3 while temporary, demonstrates the need for explicit
4 prohibitions on harmful and fraudulent market behavior and
5 for aggressive market monitoring and enforcement.

6 I think what these recent tapes indicate is that,
7 unfortunately, that corporate culture seeped down to people
8 in the front lines and permeated the work environment that
9 they lived in. I think it as a sad chapter in energy
10 history.

11 I would like to make sure that we ensure that
12 this evidence that has come to light, is appropriately in
13 the proceedings here at the Commission, so I'd like to ask
14 the General Counsel and other Staff to make recommendations
15 on the steps that we need to take to ensure that this
16 evidence -- and any other that may be out there -- is
17 included in the Enron proceedings that are pending here at
18 the Commission.

19 Suedeen will make another observation that.

20 COMMISSIONER KELLY: Thank you, Pat. I agree
21 with that. I think it's our duty to look into those tapes.
22 I think it's very important.

23 They show, in such a graphic way, the cold-
24 blooded greed that exists. They show how cruel the traders
25 were to the people of the West.

1 I was in the West then and was in California, and
2 it was cruel, and people did suffer, and the callousness of
3 the employees to the suffering is apparent. It's an
4 outrage.

5 The culture that you mentioned is also shocking.
6 It's shocking that the corruption had seeped all the way
7 down, that behavior like that was allowed to occur. It was
8 permitted; it was, perhaps worse, even encouraged, and maybe
9 even worse, it was rewarded.

10 I believe that it is imperative upon us to do
11 everything in our power to get to the bottom of what
12 happened, and to determine what we can do by way of
13 punishment in our cases.

14 I would like just like to remark for the record
15 that having been here at the Commission six months and
16 seeing a case like this, we were talking about corruption.
17 I am more and more distressed that our statutory enforcement
18 authority is so little.

19 There is in our statute, no ability to levy a
20 penalty for this kind of behavior. I know from having
21 talked to these Commissioners, that there is a will here to
22 impose penalties when we see unconscionable behavior, but
23 there is no way.

24 And so I would like to ask Congress to do
25 everything in its power to amend our statute to give us more

1 enforcement authority. Thank you.

2 CHAIRMAN WOOD: Thank you, Suedeen.

3 COMMISSIONER KELLIHER: These tapes prove what we
4 already knew, that Enron was a corrupt organization. I want
5 to commend the Chairman for initiating a Staff review.

6 The Commission has taken enforcement action
7 against Enron in the past. The Commission, to my
8 understanding, has conducted more than a dozen
9 investigations of Enron in the past few years, so this would
10 not be the first time the Commission has taken a hard look
11 at Enron, but as Commissioner Kelly pointed out, the
12 Commission only has the tools that Congress and the Courts
13 have given it.

14 In this case, Congress has not seen fit to give
15 the Commission adequate enforcement authority. We have no
16 ability to impose a civil penalty for most violations of the
17 Federal Power Act, and our criminal penalty authority is
18 limited to a daily amount of \$500. That was set in 1935,
19 and is obviously inadequate.

20 It might have been adequate in 1935, but not 70
21 years later. I think it's clear that we need to have
22 stronger criminal penalties and civil penalty authority, and
23 only Congress can do that.

24 Some in Congress recognize the need. Chairman
25 Barton, five years go, before the Enron market manipulation

1 came to light and before the California crisis, proposed
2 giving the Commission tougher enforcement authority.

3 President Bush proposed that three years ago.
4 Three years later, we're still waiting for Congress to act.

5 And I think Congress has a responsibility to give
6 the Commission the enforcement authority it needs to protect
7 the public. Congress has not done that yet.

8 I do hold out hope that Congress will act on
9 energy legislation and remain hopeful. The session has not
10 ended. There is support, not just in the House, but in the
11 Senate.

12 Senator Feinstein and Chairman Domenici support
13 tougher enforcement authority for the Commission. I do
14 think, though, that if the Congress does give the Commission
15 the enforcement authority it needs and the Commission fails
16 to act, it's fair to criticize the Commission, but until and
17 unless we have that authority, we have to soldier on with
18 grossly inadequate enforcement authority and do the best we
19 can under current law.

20 COMMISSIONER BROWNELL: I agree with my
21 colleagues, and I think that hearing and seeing more
22 corruption in such a systemic and pervasive way, is cause
23 for all of us to pause and wonder how completely and totally
24 this could have happened.

25 I think that we have taken a number of steps

1 since the earliest revelations. I wish, frankly, that we
2 had been better prepared in terms of our own analytical
3 skills to find this sooner, but I think the codes of
4 conduct, the affiliate rules, the financial disclosure
5 rules, the ongoing market power proceedings, the settlement
6 and the ALJ decision that I think is specific to some of the
7 information on the tapes, all of those are important.

8 I hope we will not only look at this information
9 in terms of existing dockets, but to make sure that the
10 steps that we have taken and the rules that we have
11 introduced into the marketplace are addressing these things,
12 and that if there is any new news, that we incorporate that
13 into a new rulemaking proceeding or make sure that we're
14 covered under the massive changes that I think we've made in
15 the last six months.

16 Hopefully, we have learned many lessons, but we
17 will continue to be informed by the horror of this kind of
18 disaster. Thank you.

19 CHAIRMAN WOOD: Thank you. On another matter, I
20 had the pleasure of representing us at the NERC Board of
21 Trustees meeting, which is the independent board that
22 oversees the North American Electric Reliability Council, in
23 Quebec on Tuesday of this week.

24 One item that came out of that -- and there were
25 several, but one item I wanted to bring up to your attention

1 was an action they took regarding public disclosure of
2 violations of NERC standards, based on the December 1
3 Reliability Conference that we had, when, Joe, you and
4 Suedeen got here.

5 We acted in mid-December to direct Staff to bring
6 up an Order that would recall all FERC jurisdictional
7 entities to disclose when they had violated a NERC standard.
8 There was a hue and cry at the time that we did that, that,
9 oh, you shouldn't do that because the standards aren't clear
10 or there is disclosure fatigue or that it was going to be
11 not understood by the public what this means.

12 So we got a lot of that. The NERC Board
13 indicated, through Chairman Drin to me, that they would
14 actually like a chance to take this on, so we've held off
15 issuing an Order. I'm please to report that the Board took
16 the task force report that actually went substantially in
17 that direction, but, importantly, it said that the public
18 disclosure would be for significant violations, and then
19 defined "significant," in a manner that would basically put
20 everything up to the Board to determine if it's significant
21 or not.

22 The Board actually receiving that task force
23 report, eliminated the significant-non-significant
24 distinction and just said, in fact, we're going to disclose
25 everything, putting in the appropriate due process for an

1 entity that was going to have their name posted on the NERC
2 website, to have that reviewed.

3 But I was very pleased, delighted, quite frankly,
4 that the independent board was doing an independent thing.
5 I look for that, certainly in the RTOs and ISOs that we keep
6 up with, that they're going to look at what's good for the
7 public interest, not just what is good for the individual
8 private interests that sit around the table.

9 I suggested that when they ask for public comment
10 at the end of the meeting, which they do -- but I would
11 recommend to you all that in light of the action this week,
12 that not issue that Order and report down. So that is my
13 recommendation based on that.

14 I think things are moving in the right direction
15 there. They intend to be very involved. We've got good
16 representation through Kevin Kelly. He's been involved in a
17 lot of the day-to-day work with NERC, as well as our
18 forthcoming reliability team.

19 But I'd put a lot of personal interest in this,
20 until, quite frankly, the boat gets into the harbor. We've
21 got some work yet to do, but it's going in the right
22 direction.

23 COMMISSIONER BROWNELL: A question: Is the
24 independent board looking at the independence of their
25 regional reliability committees? Are they considering a

1 different structure in light of the development of RTOs, for
2 example, in the Northeast? Are they discussing the
3 independence in terms of their funding, and can we help?

4 CHAIRMAN WOOD: Great questions. In fact, one of
5 the recommendations of the backup task force report was that
6 an independent study be done of -- I don't want to use the
7 wrong words here -- of the structure of NERC that would, in
8 fact, get at that issue.

9 This was a big debate at the stakeholders meeting
10 on Monday afternoon, which I had the pleasure of sitting
11 through as well. The existing Regional Reliability Councils
12 were charged with looking at what are they going to be in
13 the new world.

14 There was a concern raised by one of the customer
15 representatives from the industrial community -- and that's
16 rather self-interested that it should be about the
17 stakeholder's meeting.

18 At that point, the Board said, at this stage,
19 coming back in August, they would have the Regional
20 Reliability Councils, which are the ECAR, SERC, NPCC, come
21 back to the full Board with a discussion of the exact issues
22 you raised. What is their footprint; certainly, I think, a
23 lot of the questions are raised by the PJM-MISO move to an
24 integrated market that covers four full reliability councils
25 -- MAPP, MAIN, ECAR, and MAAC. And they all have slightly

1 different reliability and resource adequacy criteria, plus
2 the oversight, particularly the boundary line through Ohio
3 and Indiana being particularly unusual, but that's a
4 problem.

5 It's probably primarily there, but it also could
6 be in the South as well. So, they charged this group with
7 looking at the role, the structure, and the actual map as to
8 how many do they need, and do they need them?

9 I think there's an open question about what role
10 they would play when NERC goes forward. Under the statute,
11 though, there is an envisioning that regional reliability
12 councils or something like them and could exist as a
13 delegated authority from NERC, from the top, as opposed to,
14 now, it's just kind of a ground-up approach.

15 The task force was not asked to look over that,
16 but the independence, which I don't think will be fully
17 addressed by this task force, but what is the role and what
18 does the map look like, particularly in the eastern
19 interconnect where there are more than one.

20 I don't think this is an issue for WEC. WEC and
21 ERCOT were excluded from that discussion. They were
22 included in the broader discussion about what will these
23 actually do under the new NERC.

24 The customer rep was concerned that it was
25 basically going to be those people only making the report

1 back to the task force. The Board said -- will report back
2 to the Board, I'm sorry. The Board said we want NERC staff
3 in there. We want to get the report, and then we'll decide
4 where to go from there, but that will be the be-all, end-
5 all.

6 So the customer groups said that was all right
7 with them, so I'll report back to you all on that when that
8 comes out. That's an important piece.

9 NERC, today, does not have the resources to do
10 all of this directly. They have to count the regions, and
11 that's a lot of power entrusted to entities that don't meet
12 at least our standard of independence.

13 So, great question, with about an hour and a
14 half's worth of discussion at the meeting. I hope I did
15 good service to it in three minutes.

16 A happy moment: As it is in every summer, I
17 would like to take a moment to recognize and introduce our
18 intern class. We have a good class that I've not all met
19 yet. We're doing an ice cream social with them later this
20 week, but I'd like to ask the summer interns to stand up,
21 please. There they are.

22 Our class represents 30 universities from 12
23 different states, including one that I'm very fond of. The
24 program provide career experience in the world of energy,
25 the issues and challenges that face the industry, and folks,

1 just stay tuned. This meeting has just about everyone you
2 can imagine -- and an appreciation of the rewards of public
3 service.

4 I'm proud of you all, and I've seen everybody's
5 resume before you came here, so I look forward to getting to
6 know you one-on-one, but we're proud of your
7 accomplishments. Always, all of us in the leadership and
8 Staff of the Commission, always look forward to the Summer
9 Intern Program, because you all bring vitality and
10 experience and energy to this Commission.

11 A few of you actually stay on and make a career
12 out of it, so we like that, too. We want to thank you for
13 your academic achievements to date, and for your interest in
14 doing a little public service here this summer. We hope it
15 will be a typically Washington Summer that is warm but not
16 too hot. Today is not a good start.

17 (Laughter.)

18 CHAIRMAN WOOD: Enjoy your stay with us in
19 Washington. We appreciate your being here.

20 (Applause.)

21 COMMISSIONER BROWNELL: I think we need to get
22 their evening schedule. I found out how much fun everybody
23 had, so, remember, we would be available for that, too.

24 (Laughter.)

25 COMMISSIONER BROWNELL: They saw more of

1 Washington than I have.

2 CHAIRMAN WOOD: They know all the good watering
3 holes, too, I have discovered.

4 Madam Secretary?

5 SECRETARY SALAS: Good morning, Mr. Chairman,
6 good morning, Commissioners. The following items have been
7 struck from the agenda since the issuance of the Sunshine
8 Notice on June 10th; they are: E-4, E-8, E-29, E-36; G-3;
9 C-1, and C-2.

10 CHAIRMAN WOOD: Let me add one thing about one of
11 those. C-1 was Freeport Liquified Natural Gas's
12 application. As you all know, we had done a safety report
13 that was put out for public comment about a month ago on the
14 ABS Study. That's what we called it.

15 We have received comments on that study and
16 Staff has analyzed the comments and is using the suggested
17 improvements or recommendations to the analytical framework
18 that was set out in the ABS report, to apply those to the
19 Freeport application facts.

20 And so that is what is going on now, and it's my
21 expectation that that work is almost done, and we will see a
22 proposed Order, hopefully by the end of the week, and
23 hopefully we can get that out in the coming week and move
24 forward on that.

25 So, I want to thank the parties for their

1 feedback on that study, and look forward to seeing how that
2 can be a useful tool for us, as well as for the Coast Guard
3 and the local community.

4 SECRETARY SALAS: The consent agenda for this
5 morning is as follows; Electric Items: E-10, E-11, 19, 20,
6 28, 30, 32, 34, 35, 37, 39, and 41.

7 Miscellaneous Items: M-1.

8 Gas Items: G-1, 2, 4, 6, 7, and 10.

9 Hydro Items: H-1, 2, 3, 4, 5, 6, 7, 8, 9, and
10 10.

11 Certificates: C-4 and C-5.

12 As required by law, Commissioner Kelly is recused
13 from the following cases on the consent agenda: E-34, E-41,
14 G-4, H-2, H-3, H-4, H-5, and H-6.

15 With respect to G-6, Chairman Wood will be
16 concurring, with a separate statement; and with respect to
17 H-1, Commissioner Kelliher will be dissenting, with a
18 separate statement. Commissioner Kelly votes first this
19 morning.

20 COMMISSIONER KELLY: With the exception of those
21 cases that you read, Magalie, that I am recused from, I vote
22 aye.

23 COMMISSIONER BROWNELL: Aye.

24 COMMISSIONER KELLIHER: Aye, with a dissent, in
25 part, on H-1.

1 CHAIRMAN WOOD: Aye, with a concurrence, as
2 noted.

3 SECRETARY SALAS: The first item on the
4 discussion agenda for this morning is A-3. This is the 2004
5 Summer Energy Market Assessment. This is a presentation by
6 the Staff of the Office of Market Oversight and
7 Investigations, specifically Lisa Carter-Moerner; Kara
8 Mucha; Ted Gerarden; Steve Michals; Alan Haymes, Dean Wight,
9 and Ken Kohut.

10 MS. MOERNER: Good morning, Mr. Chairman,
11 Commissioners. OMOI is pleased to present our Summer 2004
12 energy market assessment. I'm going to start with an
13 overview of the assessment, and then the Staff gathered
14 here, who are a small representation of all of the Staff who
15 worked on the report, are going to present the report to
16 you.

17 (Slide.)

18 MS. MOERNER: As far as an overview goes, I'd
19 like to make four points: Firstly, that this summer may be
20 difficult for energy consumers. Fuel prices are high at the
21 moment -- oil prices, coal prices, gas prices -- and, partly
22 as a result of that, electricity prices are forecasted to be
23 high for the summer.

24 Fortunately, the Commission has taken a number of
25 actions from 2000 and 2001, which we hope will help prevent

1 a recurrence of some of the misbehavior that occurred in the
2 past in high-price environments. To that end, OMOI has
3 identified nine items that we plan to monitor, particularly
4 closely this summer, as a result of the high-price fuel
5 environment.

6 And we'll go over those toward the end of the
7 presentation. Kara?

8 MS. MUCHA: Next slide.

9 (Slide.)

10 MS. MUCHA: As Lisa noted in the first four
11 points of the overview, the forecasts for energy prices are
12 higher for this summer. This slide shows the PJM West,
13 historic and futures prices.

14 Last summer, at the start of June, prices were
15 around the \$40 range, and hit a little over \$52 in August of
16 last year. We started this June a little bit higher at
17 about \$42.

18 The projections in the Peak line show that we're
19 looking at the mid-70s for this August. That's from the
20 futures markets, so the market is expecting high prices.
21 Next slide.

22 (Slide.)

23 MS. MUCHA: This shows that the prices for
24 electric fuel sources are also under upward price pressure,
25 and the futures market for these commodities indicates

1 continued higher prices. The chart that's on the top left
2 shows natural gas prices.

3 Last summer, 2003, prices were also above \$6, but
4 then fell down, partially due to the cooler weather last
5 summer. Now, the prices right now for natural gas are above
6 the \$6 level, and are expected to stay above \$6 for the
7 balance of this year, based upon multiple factors such as
8 concerns about warmer weather, compared to last summer,
9 hurricane season, and the prices of alternative fuels.

10 The bottom graph on the left show coal prices.
11 In the six-year period we looked at, we're at the highest
12 price levels from this period 1998 through 2004.

13 Then, finally, the other fuel sources, the graph
14 on the right, the crude oil and fuel oil show that prices
15 have been in an upturn since 2003, and the futures
16 expectations have steady prices for the balance of this
17 summer.

18 (Slide.)

19 MR. GERARDEN: Turning to the next slide on
20 Commission actions that have been taken in the last year or
21 two to improve open and competitive markets, one, of course,
22 has been the now 15-month-long effort on improving price
23 transparency and price discovery to all market participants.
24 There will be a conference next Friday on this subject.

25 The information we have received from the surveys

1 conducted by the Commission, indicate that company processes
2 are improving in terms of the steps taken to assure that
3 accurate information is provided to index publishers, and
4 also that index publishers have taken a number of steps to
5 improve quality assurance and also the amount of information
6 that is provided to the market.

7 The Commission adopted the behavior rules last
8 November and has recently denied rehearings on those. They
9 are in place as of December. They provide new rules and
10 enforcement tools for the Commission in the wholesale energy
11 markets.

12 The Commission adopted the new standards of
13 conduct, and those are not effective until September, but
14 companies are taking steps now to put the processes in place
15 to meet the requirements of those standards of conduct. So,
16 significant efforts have been made in the Commission's
17 oversight and structure of the markets.

18 We are hopeful that will improve the competitive
19 picture that all the market participants seek.

20 (Slide.)

21 MR. MICHALS: In California, we're watching the
22 supply and demand picture for the summer. During the peak
23 of the summer, supplies appear tight relative to demand.

24 The economy is rebounding in California. Load
25 growth is anticipated to be up, and the California ISO has

1 forecast the reserve margin that does not have a lot of
2 excess above the basic minimum operating reserves.

3 Their summer assessment and forecast about is
4 about 1660 megawatts surplus, relative to a demand forecast
5 of 44,400 megawatts. That's under the most likely
6 conditions.

7 The graphic shows adverse conditions, which is
8 the sum of various constituent or component parts of demand
9 being estimated downward. The supplies are not evenly
10 distributed in the state, relative to demand, particularly
11 with Southern California's situation, where we are most
12 concerned about the congestion that occurs on a regular
13 basis on the transmission systems as imports are relied
14 upon, from Arizona, largely, and Nevada.

15 There's congestion on several key transmission
16 lines, plus there is derating of the California-to-Oregon
17 intertie to the Pacific DC intertie, and the hydro supplies
18 in the West are low. In the Northwest, Staff estimates
19 about 75 to 80 percent of normal exports to California from
20 the Northwest this summer.

21 Some action items that Cal ISO is taking for the
22 risks are: Limiting scheduled outages, monitoring loads and
23 resources, conducting summer preparedness training for
24 operators, and working with state agencies on raising the
25 awareness for conservation programs.

1 We're monitoring the situation closely this
2 summer.

3 (Slide.)

4 MR. HAYMES: One of the primary items of interest
5 for the upcoming summer that OMOI will be monitoring, is the
6 integration of ComEd into the PJM system. Almost seven
7 weeks into that integration, the process is running
8 smoothly.

9 The integration opens up opportunities for the
10 immediate and long-term future by opening larger areas to
11 single dispatch and widening the PJM spot market. The
12 challenges of integration, particularly without AEP in the
13 configuration, will continue into the summer, as ComEd and
14 PJM personnel adapt to new procedures.

15 Operations have worked well under low load and
16 medium-load conditions that we've seen so far. Hollowed
17 conditions during the summer may be the next test. OMOI
18 will be closely monitoring several aspects of integration as
19 we move through the summer.

20 (Slide.)

21 MR. WIGHT: As in the past, New York City and
22 Long Island are areas of concern with constrained load
23 pockets. We'll be keeping an eye on them this year.

24 The capacity situation in New York is a little
25 better than it has been for the past few years, so that's

1 good news, but it's offset somewhat by the possibility of
2 stronger than expected load growth, given the economic
3 growth that's been seen in the City in the first quarter.

4 There is an outage or derating of a transformer
5 in PJM that could affect imports into New York City from
6 PJM. As always, reliable operations in the metropolitan
7 area concern not just the NYISO, but also the PJM and ISO
8 New England Control Areas.

9 These operators have been doing this for many
10 years and they are pretty good at it, but after the
11 blackout, they have dusted off their protocols and tested
12 them to make sure that they are up to date.

13 We also have some policy issues we're aware of,
14 of line replacement on Long Island, or between Long Island
15 and Connecticut. The current unavailability of the Cross
16 Sound Cable on the market side uncertainties concerning the
17 possibility that scarcity pricing, which you approved for
18 New York last year but which did not get triggered last
19 year, could go into effect this year, if load gets high.

20 New York City also has refined its mitigation
21 system. I'm happy to report that in May, that has reduced
22 the amount of bid mitigation that's occurring in New York
23 City, so that's good news. Again, the Cross Sound Cable
24 being unavailable for imports and exports, lends some
25 uncertainty to the market.

1 (Slide.)

2 MR. KOHUT: On the gas side, we think there are a
3 number of factors that could cause prices to be more
4 volatile this coming summer, than last summer. There are
5 concerns regarding what appears to be a very uninspiring
6 U.S. production capacity number.

7 There are disagreements out there as to where the
8 production stands. From EIA -- the numbers are not final.
9 Right now, there's a very large lag on production numbers.
10 EIA right now is indicating 2003 production increased
11 slightly by 0.6 percent.

12 There are many other market analysts out there
13 that disagree with EIA, that are indicating production
14 declines of anywhere between two and six percent. Canadian
15 production for 2003 appears like it may be flat, and combine
16 that with increased domestic demand in Canada, there are
17 less imports into the United States now.

18 For next year, the early numbers from some market
19 analysts are indicating that 2004 production will fall about
20 three percent.

21 Moving on to weather, last summer's cumulative
22 cooling-degree days were below the five-year average and the
23 30-year norm across the United States. In addition to that,
24 cooling-degree days were slightly below normal from the
25 period of April through July in the core urban centers of

1 the Eastern U.S. where most of the cooling demand is
2 located.

3 It becomes clear that even a reversion to a
4 normal summer is going to increase demand for gas.

5 If the weather forecasters are correct, in that
6 hot weather for the Eastern U.S. does occur, this will
7 further compound and increase the demand for natural gas for
8 electric generation and increase price volatility.

9 On the storage side, anticipated winter demand or
10 increased winter demand due to a rebounding economy will
11 probably put some more pressure on storage refill to get
12 storage stocks up to an acceptable level by October 31st, as
13 last year.

14 We expect that this will be a high priority with
15 little regard to price. The difference between last year
16 and this year is, last year, we started the refill season at
17 very low levels in working gas storage. The worry was to
18 get storage levels up to an acceptable level.

19 This year we started out over 300 Bcf above last
20 year's levels, very comfortable levels, and would maintain
21 anywhere between 300 to 365 Bcf. So far, through the
22 season, we only really need to get to around 33,070 Bcf. We
23 will need about nine Bcf a day injected into storage.

24 If you compare that to last year, we averaged
25 11.3 Bcf a day last year with just very robust storage

1 refill last year.

2 In conclusion, as far as gas is concerned, we
3 think that there will be competition between storage and
4 electrical demand over the short term that could increase
5 gas prices and increase volatility.

6 (Slide.)

7 MS. MOERNER: I'm going to wrap up the
8 presentation by talking about a couple of regions that we
9 haven't talked about to this point, and then go over OMOI's
10 monitoring priorities for the summer.

11 In the Northwest, we expect below-normal hydro
12 conditions, and that will, of course, be a concern for
13 electricity production in the Northwest. In the Southwest,
14 there are some load pockets that we will be paying
15 particularly close attention to -- Las Vegas, Yuma, Phoenix,
16 and Tucson.

17 In the Southeast, there is a great deal of
18 stranded merchant generation, and, finally, in ISO New
19 England, Hydro Quebec firm contracts are expiring. There's
20 continued congestion in Southwest Connecticut and in the
21 NEMA/Boston area, and there is a possibility that scarcity
22 pricing may be activated in ISO New England.

23 (Slide.)

24 MS. MOERNER: Given all of this, and given the
25 high-priced fuel environment, gas volatility and some

1 regional concerns, OMOI is going to be quite busy this
2 summer.

3 Our top nine monitoring priorities are here on
4 this page: Electricity prices and trading activity; of
5 course, gas storage injections, and reporting the situation
6 with gas, hydroelectric generation in the West; California;
7 electric fuel prices; and trading activity.

8 As I mentioned previously, fuel and crude oil,
9 natural gas, coal, progress in ComEd's integration into
10 PJM's, New York City and Long Island markets, other local
11 markets, and, finally, some things that we can't talk about
12 publicly, that we'll be paying attention to.

13 That concludes our presentation. We'd be happy
14 to take questions, if you have any. Thank you for allowing
15 us to make this presentation to you.

16 CHAIRMAN WOOD: Thank you, Lisa and team. I
17 appreciate the nice graphic presentation o some pretty
18 complicated ideas and the conciseness of it. I think it's
19 helpful, again, as it was last summer and before for us,
20 internally as well as externally, to know what our market
21 oversight shop is particularly focused on, so that we can be
22 particularly attentive to that, but also be open to the fact
23 as has already happen, you've got that missing tenth item on
24 the list that inevitably comes our way, so we look forward
25 to focusing on all of these things in the traditional

1 handling format.

2 But I'm pleased we've got these focused on and
3 we'll be looking at them specifically.

4 COMMISSIONER BROWNELL: Let's hope that last item
5 doesn't come our way. Let's hope that nobody is that dumb,
6 to take advantage of a dysfunctional situation this summer.

7 COMMISSIONER KELLY: Steve, are we able to
8 monitor the supply situation in the unorganized markets very
9 effectively? In particular, I had questions about the West,
10 outside of California, how that works.

11 MR. MICHALS: Certainly not as efficiently as
12 with the organized ISO and RTO markets, where their primary
13 service is information service to the public, so it is more
14 challenging in the non-ISO regions.

15 There are particular issue with data sources and
16 the efficiency by which we get the data, but largely we are
17 able to monitor them from a broad level, not to the same
18 level of detail as in the organized ISO markets.

19 COMMISSIONER KELLY: What is the supply situation
20 in the West, outside of California? Is it as constrained as
21 California?

22 MR. MICHALS: Certainly the primary load sink, if
23 you will, is in California. That's the largest market out
24 West, so much of the surplus energy, when it is available,
25 is marketed to California. And there is still a surplus in

1 the Northwest and in the Southwest that they will sell to
2 California.

3 COMMISSIONER KELLY: Thanks. Ken, I had a
4 question about Slide 9. Would the Alaska pipeline alleviate
5 natural gas tightness significantly? Is it anticipated to
6 significantly alleviate it? Would it also put a damper on
7 price volatility?

8 MR. KOHUT: Yes, it would. There is enough gas
9 up there that it would make a significant contribution to
10 supply, but it's so far off in the distance that nobody is
11 thinking about it right now.

12 COMMISSIONER KELLY: How about the state of
13 storage? I know that you said storage is in better shape
14 this year than last year, but the storage facilities, do we
15 have adequate storage facilities in the U.S. at this time?

16 MR. KOHUT: You're putting me on the spot.

17 (Laughter.)

18 MR. KOHUT: Let me say that I have run some
19 numbers, just looking at rolling averages of injections and
20 withdrawals over the past ten years. It indicates that
21 there is more going into storage than coming out of storage
22 than in the past, which would indicate to me that there is a
23 need for more storage facilities.

24 There is a difference of opinion as to what is
25 actually working gas storage, either 3500 Bcf or 32 or 3300

1 Bcf. We are moving in and out of storage, greater
2 quantities than we had in the past, which would indicate to
3 me that there is a need for it.

4 MR. ROBINSON: Commissioner, could I add one
5 thing to that? Storage facilities in the U.S. aren't evenly
6 distributed. Some regions of the country are pretty well
7 set with enough storage, and have the ability to bring in
8 new storage.

9 Other parts of the country, especially in the
10 Southwest, have a lesser capability to actually add storage
11 and they are in need of storage in those areas. The
12 Northeast is similarly situated, in that they don't have the
13 underground storage capability that you have in other
14 places.

15 They are limited to above-ground storage, and
16 it's getting harder and harder to place above-ground storage
17 for natural gas in that area.

18 COMMISSIONER KELLY: Is that one of the reasons,
19 Mark, that we're seeing LNG applications in the Northeast?

20 MR. ROBINSON: That's a supply issue in the
21 Northeast. The storage issue in the Northeast is actually
22 LNG facilities, as well, for the above-ground storage of
23 natural gas there.

24 They just don't have the geology for below-ground
25 storage in that area, so you have a double problem in the

1 Northeast: One is siting new storage facilities above
2 ground, and, two, bringing in supplies, as in LNG along the
3 coast.

4 COMMISSIONER KELLY: I was wondering that because
5 there is difficulty siting storage, if that doesn't put more
6 pressure on the need to have more supplies like LNG.

7 MR. ROBINSON: It does, and it has to be a stable
8 supply, and it has to be a supply that can come in and feed
9 at the right time, but there is a need for additional
10 storage in the Northeast as well. This is going to be a
11 siting question, as to where you put those tanks.

12 COMMISSIONER KELLY: Thank you. I just have one
13 final question for Alan. I understand that the Illinois
14 Commerce Commission is monitoring price increases that have
15 occurred in Commonwealth Edison's area since its integration
16 into PJM.

17 Has OMOI observed that?

18 MR. HAYMES: We have seen some upward pressure on
19 prices, some price increases during that period. The price
20 increases are attributable to a number of things through
21 that area. We also see basically the same pattern in other
22 areas, so it's not something isolated in just the ComEd
23 area.

24 So there are not dramatic price increases that
25 would cause alarm, that are consistent with the integration

1 period, but we are looking at prices carefully as we move
2 forward through that.

3 COMMISSIONER KELLY: Thank you. If you look at
4 the map of the PJM control area, you can see that ComEd is
5 separated significantly from the existing PJM, and, of
6 course, one of the issues before the Commission is the
7 integration of AEP into PJM.

8 Does OMOI have an opinion on whether the impact
9 that that will have on prices?

10 MR. HAYMES: It will certainly improve the
11 situation in terms of the efficiency of the dispatch and
12 transmission through that entire area where there are upward
13 pressures. In a lot of these areas, I think it will relieve
14 some of that pressure and allow more efficient dispatching
15 and better prices.

16 COMMISSIONER KELLY: Thank you.

17 COMMISSIONER KELLIHER: I just wanted to follow
18 up on Sudeen's comments or questions about gas storage.
19 Expansion has been flat the past two years. Do we expect
20 that to continue, based on the applications that are coming
21 in the door?

22 MR. ROBINSON: We've had a few storage facilities
23 come in, but they are in the usual and typical areas, the
24 Pennsylvania area, down around the Gulf and those places
25 where you have support storage. That's a good thing, but

1 the storage in areas where we don't see applications, are
2 the areas that don't have the current storage now.

3 You can't just do it with more pipes and more
4 pipe and more supplies to follow that cyclic load of gas
5 consumption. There is a need for storage facilities to be
6 developed in the Southwest, and we don't see applications
7 there.

8 Also, probably, again, there is more above-ground
9 storage in the Northeast.

10 COMMISSIONER KELLY: You said that in the
11 Northeast, one of the issues is geology. Is that an issue
12 in the Southwest?

13 MR. ROBINSON: There are fewer sites in the
14 Southwest, but there are some sites in the Southwest that
15 are available.

16 COMMISSIONER KELLIHER: I just have one other
17 question on PJM integration. The fifth bullet on Slide 7
18 discusses unanticipated challenges such as confusion over
19 the 500-megawatt pathway. Could you elaborate on that?

20 MR. HAYMES: Yes. The two areas are connected by
21 transmission reservations. When this was initially set up,
22 as a solution to the fact that ComEd would be coming in
23 while there is a gap between the two areas, the number, 500,
24 was set as a reasonable number for that.

25 And it was determined by a series of accidents,

1 almost, in the last few weeks before the integration, that
2 they didn't have firm service in place for the entire path
3 that was contemplated or would have been put into filings
4 with the Commission to set this up.

5 So, when they announced that, that was one leg of
6 the path that was only 300 megawatts. This caused some
7 confusion and so forth, and a small reduction in the ability
8 to dynamically schedule between the two areas, reduces the
9 efficiency to a small degree.

10 COMMISSIONER KELLIHER: I'm sorry to interrupt,
11 but the confusion you're referring to is the confusion that
12 preceded the Commission's integration order, or confusion
13 that has followed the integration Order.

14 MR. HAYMES: The confusion as to what, exactly,
15 was in place before the integration took place, and so it
16 was assumed in the filings that it was 500 megawatts, and we
17 found, just weeks before, that it was not. That's the
18 confusion.

19 MR. LARCAMP: Commissioner, the last reports, as
20 I recall, all except one month -- I believe August --
21 they're up to the 500 megawatts. They had gone out and
22 acquired additional transmission capacity to basically bring
23 it back up to the 500.

24 According to the public reports, ComEd is still
25 out there shaking the bushes to try and find, for the

1 remaining month, the capacity they expected.

2 COMMISSIONER KELLIHER: So the pathway is
3 operating as well as we had hoped?

4 MR. HAYMES: Yes, it's 500 a day and it's
5 operating as contemplated. As Dan said, only August is
6 missing and the period between integrating and October 1st.

7 COMMISSIONER KELLIHER: Thank you.

8 CHAIRMAN WOOD: Good job, team. Thank you all.

9 SECRETARY SALAS: The next item on the discussion
10 agenda is strategic plan for the Federal Energy Regulatory
11 Commission. The Chairman will lead a discussion of this
12 item. That's A-4.

13 CHAIRMAN WOOD: Beginning in the Fall of 01, the
14 Commission began to collectively put together a strategic
15 plan with the promise that we would revise it periodically.

16 Today represents the fourth revision of that, a
17 significant revision we've had of the document along the
18 way, and it reflects the input of our two newest members.
19 I'm pleased to that, and I just wanted to remind folks that
20 the purpose of this document is multiple:

21 One is to let our Staff know what the leadership
22 team here wants to have happen across the Agency in the
23 coming year, and that's represented by the detailed layout
24 of the priority bullets under each item.

25 The document itself has the three major goals of

1 the Commission, the infrastructure goal, the fostering
2 competitive energy markets goal, and the market oversight
3 and potential customers goal.

4 In addition to our good government goals of
5 management initiatives that support everything that we do
6 here, all being represented in this document, there are
7 eight separate objectives underneath those three goals that,
8 in fact, are the eight baskets through which we allocate our
9 resources through the budgeting process and through the
10 business plan over the coming year.

11 As Tom and I and the Senior Staff put together
12 the 2005 operating budget to start October 1, our input --
13 actually, this is the first time we've done it early enough
14 to be actually very helpful in the process -- the input from
15 all of us collectively to this will dictate how our budget
16 is structured for the coming year.

17 Certainly things happen along the way, but I will
18 say that it was a slight bit of a surprise over the past
19 three years that this has worked out to be pretty much how
20 we stuck to the plan. There are a lot of items here. We do
21 a lot of work here. We think it is important for people to
22 know, internally and externally, that there's a lot of
23 significant activity that goes on here to ensure that we
24 have dependable, affordable energy through sustained
25 competitive markets, which is the vision of the Agency.

1 One of the main things that is in here -- and I
2 would like to invite all my colleagues to add anything --
3 there are significant changes along the way of both tone and
4 in the way things are presented, and I think it's important
5 for people to look at, but one of the main things that we
6 did here that I was interested in doing today, was to
7 incorporate the establishment of the Commission's
8 Reliability Division under Objective 1.4, and to, in fact,
9 rename Objective 1.4 to encompass not only the security and
10 safety of the energy infrastructure, which has been an
11 important goal up till now, primarily executed through OEP
12 and, again, primarily in that, represented through our many
13 staff and regional offices across the country that look at
14 hydroelectric facility safety projects.

15 But now to incorporate that different, but
16 related concept of reliability, reliability is not just an
17 electric issue, but certainly our appropriation from
18 Congress that was given for this fiscal year, represents a
19 significant nudge by Congress that we should get into this
20 area, so, in the coming week, we'll be making some public
21 announcements about Staff that I'm excited about, and
22 continue our approach that has been underway for some time
23 now to fill Staff positions with high-priority professional
24 engineers and others that would contribute to enhancing our
25 ability to do this job, I think, as Congress and the people

1 expect.

2 That is, from my perspective, one of the main
3 things I wanted to see reflected in our business plan, and I
4 appreciate your consideration of that, and would welcome any
5 other comments, because there were a lot of other
6 suggestions over the past week that we've worked on in this.

7 COMMISSIONER KELLIHER: I just want to say I
8 enjoy working with my colleagues, as well, on the plan. I
9 think it did make some important changes. It emphasized the
10 Commission's enforcement role, which is appropriate in the
11 wake of the market behavior rules that were issued recently.

12 It also emphasized the Commission's safety and
13 security responsibilities over LNG facilities and other
14 facilities, particularly hydro. And I do want to commend
15 the Chairman, as I have in the past, for making dam safety -
16 - with no "N" --

17 (Laughter.)

18 COMMISSIONER KELLIHER: -- dam safety as a high
19 priority of the Commission. I think that's due to the
20 Chairman's emphasis, and I want to commend the Staff for
21 committing resources to it, so I support this plan, and I've
22 enjoyed working on it.

23 COMMISSIONER KELLY: Thank you, Joe. I'd like to
24 just highlight a few changes that were made, that I thought
25 were important, and reflect what the Agency has been doing

1 and was going to do along the lines of the dam safety. That
2 is the LNG safety.

3 I see our Agency becoming the premier agency,
4 frankly, in the world, on LNG safety issues. I'm proud of
5 the work that the Staff has done, that you have reorganized
6 and created.

7 Well, we have enough LNG work now to demand more
8 specialization. We have terrific experts, and I'm glad to
9 see that that is being highlighted.

10 Also, I'm pleased to note that we have in here
11 for the first time that we are going to work at our existing
12 regulations to see whether they need to be reformed in any
13 way to accommodate renewable energy, particularly after the
14 State of the Market Report, and looking at the developments
15 in the states with renewable energy.

16 It's important that we have our regulations in
17 place in a way that accommodates increased use of renewable
18 energy, as well as efficiency, so I'm pleased that our
19 strategic plan reflects that.

20 Then, finally, I'd like to add that the emphasis
21 on reliability is very important and consistent with the
22 policy statement we issued after the blackout, that all of
23 our initiatives were going to be evaluated from now on,
24 looking at reliability and the impact on reliability. Thank
25 you.

1 COMMISSIONER BROWNELL: I think this is terrific,
2 and it really is fun, I think, to have more eyes and
3 thoughts on this. I think that one of the huge changes
4 we've made is the addition of the reliability team.

5 I think it would be great, if, Dan, you could
6 have the team come and play a presentation for us when
7 they're organized.

8 I'd like to talk a little bit about how we're
9 going to look at cost recovery, for example, and how we're
10 going to define legitimate costs. I think there's some
11 question in the eyes of the industry as to what we mean by
12 that, and I think, frankly, that we could provide some
13 guidance, perhaps, in helping the states who have to deal
14 with this issue, too, because I think it was really unfair
15 to expect companies to do the right thing, without the
16 assurance of cost recovery.

17 I think we owe them that, but I think this is an
18 addition that will add value, both in terms of market
19 development, infrastructure development, and really help us
20 get a bigger picture of what the future looks like.

21 I'd like to see if we could schedule that
22 whenever the new folks can give the Committee an hour.

23 CHAIRMAN WOOD: We'll do that. Good.

24 COMMISSIONER KELLIHER: I want to follow on to
25 something that Commissioner Kelly said. We did place the

1 greatest importance on the safety of LNG import facilities,
2 which is appropriate, since we have exclusive jurisdiction.

3 (Laughter.)

4 CHAIRMAN WOOD: I want to ask the Senior Staff,
5 obviously, I know we send this out electronically to the
6 Staff, but to encourage the frequent consultation on this
7 document, this is certainly an external tool so that people
8 on the outside know what we are doing, but this is one of
9 the measures of what we're about and what we're going to
10 doing in the coming year, so make sure that everybody, from
11 U.S. Tire to you guys and gals, know what's in here.

12 If anybody has questions about it, please let me
13 know. I'll be more than happy to flesh them out, if I come
14 to visit your management teams or your Staff meetings, to
15 walk through the business of the strategic plan.

16 I'll call for a vote on it. I would entertain a
17 motion to approve the strategic plan, as revised.

18 COMMISSIONER KELLY: So moved.

19 CHAIRMAN WOOD: Vote.

20 COMMISSIONER KELLY: Aye.

21 COMMISSIONER BROWNELL: Aye.

22 COMMISSIONER KELLIHER: Aye.

23 CHAIRMAN WOOD: Aye. All right, let's proceed.

24 SECRETARY SALAS: Next on the discussion agenda,
25 we'll be taking two items jointly. These are E-3 and E-42,

1 both for the New PJM Companies. This is a presentation by
2 Grace Goodman, Christopher Daignault, Catherine Waldbauer,
3 accompanied by Alice Fernandez.

4 MS. GOODMAN: Good morning, Mr. Chairman and
5 Commissioners. I'm Grace Goodman. With me at the table are
6 Alice Fernandez, Cathy Waldbauer, and Chris Daignault.

7 We also want to thank Mike Goldenberg, Lynn
8 Lichtenstein, Andrea Goodson, Jan Bargan, and Nicole Staduco
9 for their contributions.

10 Today, the Commission is issuing two Orders that
11 will enable AEP to fulfill its voluntary commitment to join
12 PJM and to transfer control of its transmission facilities
13 to PJM.

14 E-42 is an Order approving settlement among PJM,
15 AEP, and the Kentucky Commission, which allows AEP's
16 subsidiary, Kentucky Power Company, to transfer operational
17 control of its facilities to PJM. Underlying the settlement
18 is another stipulation in which the parties to the Kentucky
19 proceeding agreed to resolve their differences concerning
20 AEP's integration into PJM.

21 E-42 addresses several issues regarding the
22 Kentucky stipulation. The stipulation does not change the
23 authority of this Commission or of the Kentucky Commission.
24 In addition, the stipulation does not exempt AEP from
25 meeting the obligations of being a PJM member and signatory

1 to the relevant PJM agreements.

2 Further, the stipulation is premised on PJM's
3 market being voluntary. That means that AEP can elect to,
4 one, participate in PJM's spot energy market to meet
5 Kentucky Power's native load energy requirements; two,
6 contract bilaterally with other entities to supply energy,
7 or; three, schedule its own generation to meet those
8 requirements.

9 Finally, the stipulation specifies procedures to
10 be used during curtailment situations.

11 The Commission finds that these procedures are
12 not discriminatory. Based on these findings, the Order
13 approves the settlement without condition or modification.

14 I'll now turn the presentation over to Catherine
15 Waldbauer.

16 MS. WALDBAUER: In E-3, the Commission today
17 affirms an initial decision by an Administrative Law Judge
18 as to whether, under Section 2.05(a) of the Public Utility
19 Regulatory Policies Act, or PURPA.

20 The Commission may authorize AEP to integrate its
21 facilities into PJM, over the objections of the Commonwealth
22 of Virginia. PURPA Section 2.05 provides that the
23 Commission may exempt electric utilities from any provision
24 of state law or from any state rule or regulation which
25 prohibits or prevents the voluntary coordination of electric

1 utilities, if the Commission determines that such voluntary
2 coordination is designed to achieve economic utilization of
3 facilities and resources in the any area.

4 Section 2.05(a) also provides exceptions to the
5 Commission's authority to exempt utilities from state law.
6 In his initial decision, the ALJ determined that AEP's
7 integration into PJM was designed to obtain economic
8 utilization of resources and facilities in the Midwest and
9 Mid-Atlantic areas.

10 He cited to the extensive, quantifiable and non-
11 quantifiable benefits that would accrue to customers from
12 that integration, and found that the benefits of integration
13 would significantly outweigh the costs. The Commission
14 today affirms this ruling.

15 The ALJ further determined that the laws and
16 regulations of Virginia are preventing AEP from integrating
17 into PJM by October 1, 2004. The Commission also affirms
18 that finding.

19 Now, I'll turn it over to Chris.

20 MR. DAIGNAULT: Finally, under PURPA Section
21 2.05, the Commission may not exempt a utility from state law
22 or regulation, if it finds that the relevant provision of
23 state law, rule, or regulation is designed to protect public
24 health, safety, or welfare or the environment, or to
25 conserve energy, or is designed to mitigate the effects of

1 emergencies resulting from fuel shortages.

2 The ALJ concluded that if this exception is
3 interpreted as broadly as Virginia claims it should be, the
4 exception would swallow the general rule of PURPA Section
5 2.05, thus, the ALJ found that the exceptions to PURPA
6 Section 2.05(a) do not apply here.

7 The Commission affirms that ruling, thus, the
8 Commission exercises its authority under PURPA Section
9 2.05(a) to enable AEP to integrate into PJM and to provide
10 AEP, PJM, and their customers, certainty that the
11 integration will proceed by October 1, 2004.

12 However, to the extent that the Virginia
13 Commission is able to complete its proceedings prior to the
14 date of integration and reaches agreement as to reasonable
15 conditions that do not prevent or prohibit integration,
16 Virginia may not be foreclosed from imposing such
17 provisions. Thank you. We will be happy to take any
18 questions.

19 CHAIRMAN WOOD: I don't necessarily have any
20 questions, but I do want to make some observations. I think
21 this is a very significant chapter in the RTO development
22 story that has gone on here for some five years.

23 In our SMD discussions back in 02, we said that
24 states that wish to preserve the traditional regulatory
25 paradigm with vertically-integrated utilities, should have

1 no problem doing so while their utilities join an RTO, even
2 those RTOs with advanced market features such as PJM, and
3 the Kentucky settlement with PJM and with AEP that was
4 blessed by the state commission there proves that to be
5 true, as we also saw with Ameren and the State of Missouri.

6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25

1 On the other hand there was no such recognition
2 in my state of residence, Virginia. And I think we properly
3 affirmed the judge's finding that we have the authority to
4 override state laws that block a utility's voluntary
5 participation in an RTO. It's important for regional
6 reliability clearly and for efficiency to eliminate the
7 holes in the RTOs, especially when one state regulates
8 retail electric service in a small corner of the utility
9 that is really the transmission backbone of the center part
10 of the country.

11 There's a very delicate and deliberate time line
12 here which necessitates our action today to integrate in
13 October of this year. I don't think there is an ability to
14 wait. It has been five years since AEP has made a
15 commitment to join RTO and three years since it volunteered
16 to join PJM, a little less than three years. So it is time
17 to move forward. I think these two orders collectively lay
18 that out in a very thoughtful, meaningful manner.

19 COMMISSIONER KELLY: I'd like to talk a little
20 bit about some of the facts in this case. I think that the
21 fact that AEP is a larger utility that stands between
22 Commonwealth, Edison, and PJM and PJM is an important fact
23 here, OMOI in the last presentation confirmed that having
24 AEP become integrated into PJM will have a very positive
25 impact on prices as well as reliability. I think that's

1 compelling. The other thing is that AEP serves customers in
2 five states in addition to Virginia, Pennsylvania, Ohio,
3 Michigan, Indiana, and Kentucky. They all support AEP's
4 integration. So what we are looking at here is not only
5 facilitating the voluntary integration that AEP wants, but
6 also facilitating the integration that five sister states of
7 Virginia want. I think that's compelling.

8 Finally, I'd like to clarify that by this order
9 we are not exercising our authority under PURPA Section
10 205(a), we are determining that we have the authority. The
11 State of Virginia is going to consider later this month --
12 actually I'm not quite clear if it's later this month.
13 Unfortunately, not until July the State of Virginia is going
14 to consider whether or not it wants to bless the
15 integration. So indeed, it's quite possible that Virginia
16 will end up deciding like Kentucky did, when it turns its
17 attention to the matter, that it would be a positive
18 development for Virginia.

19 I just want to clarify that we aren't ordering
20 it, we're just saying that we have the ability to order it,
21 if need be.

22 Thank you.

23 COMMISSIONER KELLIHER: I wanted to commend the
24 Kentucky parties for settling. I expressed some regret that
25 the Virginia parties were not able to enter into a

1 settlement. As Commissioner Kelly pointed out, what the
2 Commission is presented with and faced with is a dispute
3 among the states. We have six states. They are addressing
4 the basic question of whether a multi-state utility should
5 be able to voluntarily join an RTO. Five of the states
6 believe they should, one believes otherwise.

7 The Commission has to resolve the dispute. It's
8 become a dispute, the kind of dispute the federal government
9 is commonly called upon to referee. I think the order
10 properly interprets Section 205. And that the Commission's
11 order is consistent with 205. I do think it's in the public
12 interest, and I support the orders.

13 COMMISSIONER BROWNELL: Hard to add to those
14 descriptions. But I would make one addition. That is that
15 this has gone on for five years and I think we didn't
16 undertake this decision lightly. The judge has, I think,
17 laid out a very clear and coherent fact pattern that indeed
18 supports. This is not only good for the states that want
19 it, it has clear benefits for Virginia and I feel confident
20 that their proceeding will identify those in a way that many
21 of the parties have.

22 I would also suggest that this is the result of a
23 merger commitment and I think that one of the things that
24 we've learned through this process is that we need to take
25 more seriously and hold people more accountable in a more

1 timely manner to fulfilling merger commitments. They should
2 not be held lightly. But I think it's something that should
3 be considered.

4 And I'm pleased to support this order and I
5 really think the work of the staff who I think worked very
6 hard with the parties to make sure that the information was
7 there for a settlement, Kentucky did a great job and the
8 judge, I think, is to be commended for really writing an
9 order that I think makes this clear for everyone to
10 understand. I am pleased to support it as well.

11 CHAIRMAN WOOD: Let's vote.

12 COMMISSIONER KELLY: Aye.

13 COMMISSIONER BROWNELL: Aye.

14 COMMISSIONER KELLIHER: Aye.

15 CHAIRMAN WOOD: Aye.

16 Thank you all again.

17 SECRETARY SALAS: The next item on the discussion
18 agenda is also a joint presentation. This time we had E-38,
19 Northeast Utilities Service Company and E-43, Long Island
20 Power Authority.

21 We have a presentation by Nicole Stoduto
22 accompanied by Hadas Kozlowski, Alice Fernandez, Elisabeth
23 Blaugh, Vinny Musco, and Gene Grace.

24 MS. STODUTO: Good morning, Mr. Chairman,
25 Commissioners. The draft orders address, pursuant to

1 Section 210 of the Federal Power Act, two interconnections
2 between Long Island and Connecticut. Dependable operation
3 of these interconnections would enhance reliability in New
4 York State and New England. Stated in the simplest terms,
5 Connecticut parties support action to ensure the operation
6 of the 1385 cables. The New York parties support operations
7 of the Cross Sound cable, but each side opposes the other's
8 preference.

9 Specifically the draft order in E-38 addresses an
10 application made by Northeast Utilities for an order
11 directing the Long Island Power Authority to replace the
12 1385 cables which connect North Port, New York to Norwalk,
13 Connecticut and provide a term transfer capability of 300
14 megawatts.

15 The 1385 cables are susceptible to damage due to
16 environmental concerns and are currently operating only
17 under special consent orders. The draft order in E-43
18 addresses an application made by the Long Island Power
19 Authority for an order directing energization and operation
20 of the Cross Sound cable, a 330-megawatt facility that
21 connects New Haven, Connecticut and Shoreham, New York.

22 Due to concerns involving its placement to the
23 cross-sound cable has operated only sporadically since its
24 construction in 2002.

25 The draft orders take a consistent approach

1 seeking in both cases to fulfill the public interest on such
2 issues as ensuring economic and reliable service for
3 electric customers while protecting the environment,
4 determining the proper allocation of costs and resolving how
5 a federal and state law interact in these circumstances.

6 Thank you.

7 CHAIRMAN WOOD: Thank you, Nicole.

8 I will do something a little unusual here after a
9 presentation and ask, I think, with the juxtaposition here
10 of what looks like so potentially a win/win for two states
11 and the utilities involved in them that we might do a
12 Commission-imposed time-out for about a week to encourage
13 before we vote these orders to see if there's really
14 potential to be grabbed here.

15 I'm aware in the air that there are parties
16 talking. I don't know how serious those are, but I would
17 think that before we would issue this order I would like the
18 opportunity to invite just informally through this
19 announcement and not through any sort of formal order to
20 invite parties to let us know if there is a settlement
21 potential here. I'd just hate to let it go.

22 I'd like to think that with these interstate
23 disputes we can maybe have something there. I would just
24 like to ask your forbearance at this time, Joe, Nora, and
25 Suedeen from voting and ask that if we don't hear anything

1 by this time next week that we put these out notationally
2 and leave them at that time.

3 COMMISSIONER BROWNELL: Certainly we always want
4 a settlement. We would encourage the parties to do so. I
5 think we ought to stick to the timeline. One week, and one
6 week is it. No excuses.

7 This has been, I think, a rather unconstructive
8 public debate without much focus on the benefits for both
9 states, not one over the other. I hope the parties can
10 focus on that, come to the table and get a resolution.
11 Because I think the customers deserve it. This is not a
12 healthy approach to solving problems.

13 CHAIRMAN WOOD: We will table action on that. If
14 we don't hear anything by close of business Thursday, I will
15 have my hardback in the Secretary's office at 5:00 on
16 Thursday to issue this, if that's fine with you all. Great.
17 Thank you, staff.

18 We appreciate the hard, hard work. We will see
19 whatever sees the light of day.

20 SECRETARY SALAS: The next for discussion is E-
21 2. This is California Independent System Operator
22 Corporation, a presentation by J. B. Shipley accompanied by
23 Jamie Simler, Derek Bandera, David Mead, Susan Pollonais,
24 and Susan Taylor.

25 As required by law Commissioner Kelly is recused

1 from this case.

2 MS. SHIPLEY: Good morning, Chairman,
3 Commissioners. My name is J. B. Shipley. Sitting with me
4 at the table are Jamie Simler, David Mead, Derek Bandera,
5 Susan Pollonais, and Susan Taylor. Also contributing to
6 this order were a number of people from across the
7 Commission, including Carlos Clay, Amos Dimitri, Matthew
8 Deal, Catherine Gensler, Harry Sing, and others.

9 Since the January 2000 Commission order, the
10 California ISO has been working on a redesign effort to
11 correct fundamental design flaws in California's energy
12 market, the California ISO's confidential market, the design
13 proposal which contains a security constraint integrated
14 forward market and locational pricing to manage congestion
15 would address these problems.

16 The draft order before you addresses the seven
17 elements of the California ISO's market redesign proposal
18 representing both reliability tools and market efficiency
19 improvements and directs a tariff filing within 180 days.

20 The seven issues addressed are the flexible offer
21 obligation, the residual unit commitment process, the
22 simplified hour-ahead market, ancillary services, marginal
23 losses, constrained output generators and virtual bidding.
24 With this order these issues should be substantially
25 resolved.

1 Leading up to this order staff, the CAL ISO and
2 market participants participated in a number of technical
3 conferences that assisted in the understanding and
4 resolution of these issues. However, going forward there
5 remained significant unresolved issues. Chief among them is
6 resource adequacy.

7 The California Public Utilities Commission has
8 stated that it will issue a decision on resource adequacy
9 this summer. The draft order defers ruling on the remaining
10 market redesign issues including market power mitigation
11 pending the CPUC's decision as the end of the summer.

12 Among the other unresolved issues are allocation
13 of congestion revenue rights, issues involving existing
14 transmission contracts, and the seller's choice contract
15 concerns.

16 To facilitate that timely resolution of these
17 issues, the order establishes additional procedures. The
18 order directs the submission of additional information on
19 existing transmission contracts and recognizes that there
20 will be transitional issues associated with incorporating
21 existing contracts including sellers' choice contracts into
22 the redesign.

23 Finally, the order directs staff to convene a
24 technical conference on congestion revenue rights in some
25 reforms that the California ISO is proposing to its current

1 operations are necessary for the reliable and efficient
2 operation of the grid.

3 It is critical that these reforms be supported by
4 adequate infrastructure including resource adequacy and
5 there be a comprehensive approach to reliability,
6 operations, and pricing. This order furthers these goals.

7 That concludes my presentation.

8 CHAIRMAN WOOD: Thank you, J.B. I have to say, I
9 always look forward to the little message from the
10 California newsletters when you all go out there because
11 you're kind of like Madonna, you're just kind of known by
12 your first names only.

13 [Laughter.]

14 CHAIRMAN WOOD: Derek said, J.B. said. Susan, I
15 guess they have a little trouble with that one.

16 I appreciate your personal leadership on the
17 California issues. It has not just been the drafting of one
18 order that has led to this. It is an ongoing commitment by
19 some really sharp minds on our staff and I'm looking at some
20 of them right here today that have assisted in this slow and
21 painful recovery from maladies that were identified a good
22 year before Nora and I came on this Commission by our
23 predecessors.

24 I avoid the use of the word "frustration" here
25 because I do think that there is a slow, but noticeable turn

1 in the tide in California toward wanting to do something.
2 And I'm not saying just at the political level, although
3 that certainly has been evident. But I think through the
4 stakeholder process the absolute just shell shock of getting
5 out 2001 -- the further that's away, the more rational
6 people can be.

7 This order comes at the right time. When we had
8 our October white paper conference down at the CPUC's
9 chambers in San Francisco, that really set the groundwork
10 for this order to come as well as for the ones that J.B.
11 pointed out would be coming later after the California
12 Commission addresses some of the resource adequacy issues
13 more thoroughly.

14 I do think it's timely and the cuts are good. I
15 would say consistent with the cuts we made elsewhere in the
16 country with the exception of where it doesn't work in the
17 absence of a resource adequacy requirement. I do think that
18 it is important both for minimization of the costs of ISO
19 software as well as rational, time-tested approaches that
20 are working elsewhere that we do borrow as heavily as
21 possible from the markets that are working into these
22 markets that are developing.

23 I recognize that some of the cuts that we've made
24 here are not consistent with some of the ones we've made in
25 other ISO/RTO markets. They are consistent with them such

1 as the flexible, must-offer obligation, the recapping of the
2 residual unit commitment bids and others. That will be once
3 we get to a more complete resource adequacy approach in the
4 California market as we do in these other markets that are
5 not infrastructure starved. That these policy calls made
6 here today as transitions to that world will in fact be over
7 taken and replaced by hopefully something that is
8 consistent.

9 There was one issue, and this is granular, as a
10 lot of things in this important order are, but there's an
11 issue about being able to self-provide RUC. I wonder if you
12 all could flesh that out a little bit. There's an
13 indication that some of the parties did not actually like
14 this and I wonder why that was.

15 MR. BANDERA: The RUC, the residual unit
16 commitment, is a process by which the ISO determines that
17 there hasn't been enough supply and demand that has cleared
18 in the day-ahead market. So, some parties preferred the
19 opportunity to not have to offer that capacity through the
20 market and rather self-supply that capacity into the market
21 in the same sense that a supplier or customer can self-
22 schedule energy, we've allowed them to self-commit that
23 capacity into the day-ahead market essentially. The
24 opponents preferred that all capacity in the residual unit
25 commitment go through the market and have a bid associated

1 with it rather than necessarily allowing someone to simply
2 self-schedule it. That was the main point.

3 CHAIRMAN WOOD: To what end do they make that
4 argument?

5 MR. BANDERA: In some sense, the opponents of
6 allowing the self-supply see it as a circumvention of
7 participation in the market in a sense. They feel that
8 forcing them through the market is a better mechanism than
9 allowing the self-supply.

10 CHAIRMAN WOOD: Can you self-supply ancillary
11 services out there?

12 MR. BANDERA: Yes.

13 CHAIRMAN WOOD: How does RUC distinguish from
14 ancillary services?

15 MR. BANDERA: They're very similar in my opinion.

16 CHAIRMAN WOOD: In the eastern markets, however,
17 the equivalent of RUC is in fact required to be provided
18 through the market or is this just not taken up?

19 MR. BANDERA: Actually, in the eastern markets
20 they have the resource adequacy requirement upon suppliers.
21 And in the east when they determine that there hasn't been
22 sufficient commitments of units in the day-ahead market,
23 they will simply tell them to start up and be available, in
24 that sense. That is one of the transitional issues that you
25 mentioned before in California. At this point there's not

1 this resource adequacy obligation on generators, and so the
2 value of that capacity that they're committing to the
3 California market needs to be made clear in the east.

4 There's the implicit commitment of that capacity
5 through the resource adequacy requirement.

6 CHAIRMAN WOOD: That's helpful. Thanks.

7 This is off line from this project because I
8 think this is an order we can really get on out. But I
9 would like to see what it is, can you just for the four of
10 us, do a little paper that says, here's what's going on with
11 the discussions on the resource adequacy requirement?
12 Versus, here is the resource adequacy requirement that will
13 actually draw these things together.

14 I would assume that would be one we've already
15 got working in an existing market somewhere.

16 Is California kind of pushing toward the resource
17 adequacy model that we've already seen being time tested, or
18 are we kind of dreaming up something new out there? And I
19 just wonder if we could get that so that when we engage with
20 the PUC commissioners out there, we can kind of emphasize
21 what we're about as things that have already been working
22 somewhere else and try to introduce that concept if they
23 want to go in that direction.

24 I just don't know, I don't have a sense from the
25 discussions because they're all very high level. Are they

1 putting something that works in one of these other markets
2 or are they doing something that's just very different?
3 That seems to me to be a pretty important piece that we have
4 not addressed here. And until we address that, this is not
5 going to be the complete book.

6 COMMISSIONER BROWNELL: I was just at a couple of
7 conferences out there with, I think, lots of stakeholder
8 representation, including the Commission. I think every
9 everyone has come to the conclusion that the resource
10 adequacy issue is the singular issue until and unless we
11 resolve that we cannot put the pieces together. So this
12 would be timely, and I think our encouragement and maybe
13 work with them to get this done. It's a struggle, but I
14 think as you wisely point out, whatever else we do just
15 doesn't have any impact in terms of this.

16 CHAIRMAN WOOD: Again, one of the benefits of
17 this approach is, let's get down from the heights. Let's
18 talk about the specifics. Let's build the bricks. We can't
19 just look at the plans, we've got to start building the
20 house, and doing these kind of steps with these orders --
21 which I know have been extremely difficult to do because
22 they are the kind of nuts and bolts, quite frankly, that I
23 came to this job to do, and I'm thrilled to see it finally
24 happening.

25 This is what we need to be doing everywhere there

1 are developing markets. We've done a lot of it with MISO.
2 We've still got more to do with MISO, SBP is actually
3 getting some of the basic, critical important things based
4 on experience about what works is very critical to getting
5 the California market back on track. I'm actually excited
6 about this order and keep the heat out and get the job done.

7 This is how you fix California plus the other
8 stuff you cite which is good for the infrastructure too.

9 COMMISSIONER BROWNELL: Can I just point out,
10 speaking of the granular details, I think regarding the
11 seller's choice contracts we have created a structured
12 environment to facilitate the resolution of a very narrow
13 set of issues' delivery points. I hope that the parties
14 take advantage of that. I am concerned there is an
15 expectation that this is an opportunity rather than too
16 narrowly focus on that issued, it's got to go to a whole
17 bunch of issues.

18 I think we need to be clear that we expect all
19 parties on both sides of this contract to focus on that
20 discrete issue and to do so in a constructive way. I keep
21 using the word "constructive" but a lot of the conversations
22 don't end up in resolution because people are not focused on
23 the issues and they're not contributing solutions, they are
24 busy talking about why this won't work for them. The
25 answers we're looking for is what works for them, but what

1 works for the larger market reforms which we're trying to
2 get to. And this is an impediment that I think could be
3 fixed. I think the hub concept that has been suggested has
4 worked elsewhere. The west is different, but we might just
5 want to take a look at some tried and true experiences. And
6 I hope people will also take a good open look at that.

7 Thanks for suggesting that. That was a good
8 answer.

9 CHAIRMAN WOOD: I think the way that was written,
10 the way that this particular discussion got sold was to
11 avoid the shopping mall approach. There's a potential issue
12 here that might need addressing, it might not, but hubbing
13 has worked in New England and perhaps elsewhere. Let's just
14 get that resolved and move on to kind of plow through these
15 other things.

16 COMMISSIONER BROWNELL: I think it's written that
17 way. I just want to make sure that people read it that way.

18 CHAIRMAN WOOD: The 29th of June can't come soon
19 enough. Let's vote.

20 COMMISSIONER BROWNELL: Aye.

21 COMMISSIONER KELLIHER: Aye.

22 CHAIRMAN WOOD: Aye.

23 SECRETARY SALAS: That final item on the
24 discussion agenda for this morning is C-3. This is AES
25 Ocean Express and Florida Gas Transmission Company. A

1 presentation by Sandra Delude accompanied by Carolyn Van Der
2 Jagt and Ed Murrell.

3 As required by law Commissioner Kelly is recused
4 from this case.

5 MS. DELUDE: Good morning, Mr. Chairman,
6 Commissioners. C-3 is a draft order that addresses a
7 complaint filed by AES Ocean Express LLC, against Florida
8 Gas Transmission Company alleging that Florida Gas has
9 insisted on unreasonable and onerous conditions in a
10 proposed interconnection agreement. The complaint raises
11 both operational issues related solely to Ocean Express's
12 Interconnection Agreement and systemwide issues related to
13 gas quality and interchangeability requirements and
14 procedures for changing them in the future.

15 In January of this year the Commission issued
16 Ocean Express a certificate to, among other things,
17 construct and operate a natural gas pipeline to transport
18 regasified LNG from the exclusive economic zone of the
19 United States and the Commonwealth of the Bahamas to an
20 interconnection point with Florida Gas in Florida Gas's
21 market area.

22 Florida Gas states that three other suppliers
23 have also requested interconnections to deliver regasified
24 LNG directly into its market area. The draft order requires
25 Florida Gas to make a filing to revise its tariff within 30

1 days to incorporate gas quality and interchangeability
2 provisions to address the introduction of regasified LNG
3 into its system. The order finds this action is necessary
4 in order to ensure the greatest degree of certainty and
5 transparency for Ocean Express, other LNG developers and
6 Florida Gas' shippers, and to ensure comparable treatment
7 among the several pipeline projects competing to deliver
8 regasified LNG directly into Florida Gas' market area.

9 The draft order also sets two operational issues
10 for settlement judge procedures. Namely whether Florida Gas
11 should have the ability to control flows at the
12 interconnection in order to maintain rates of flow up to 6
13 percent per hour and whether Ocean Express would be required
14 to install heaters at the interconnection point to avoid
15 liquid hydrocarbon fallout.

16 That completes my presentation.

17 CHAIRMAN WOOD: Thanks, Sandy.

18 How does this process that we set up in this
19 order link up with the broader discussions we're having on
20 interoperability and gas quality --

21 MS. DELUDE: I'll defer to Ed. I think he's been
22 more involved in that process.

23 MR. MURRELL: Unfortunately as a matter of timing
24 we are presented here with a case where we have a pipeline
25 that has a need to have interchangeability standards in

1 place and doesn't. The Natural Gas Council's ongoing
2 efforts to arrive at a consensus standard for the industry
3 have been making progress, but they're not there yet. We
4 may not see a resolution from the industry on any kind of
5 generic standards for several more months. Meanwhile, Ocean
6 Express is trying to move forward with its project and get
7 to the point where it can arrange financing moving that
8 project into operation. Unless we are able to resolve some
9 of these issues now, we have a little bit of an impasse
10 between developing LNG on the one hand and some kind of
11 standardization for these interchangeability standards on
12 the other hand. The process that we envision here would put
13 some standards in place in the tariff now. But we recognize
14 that in the future once generic standards have been arrived
15 at by the industry, there may be a need to make some further
16 changes.

17 CHAIRMAN WOOD: I think this will certainly spur
18 the industry broader discussions into a lot higher gear.
19 And I hope it does because these applicants that are so
20 needed in our country, whichever ones, ultimately get the
21 confidence of the market need to have the regulatory
22 decisions done on all fronts. So this is just one. But
23 it's an important one that was identified by the NPC and
24 EURGO at least last fall as one of the kind of top, punch-
25 list items that we need to deal with, it's here. And I just

1 wanted to call this item separately to let the world know
2 that this is now a docket and location where some
3 significant decisions will be made. But they need to be
4 made because an applicant has to have the answers. So we
5 will do it thoughtfully and expeditiously. Good process.
6 Thanks for being creative about how to set this up.

7 Let's vote.

8 COMMISSIONER BROWNELL: Aye.

9 COMMISSIONER KELLIHER: Aye.

10 CHAIRMAN WOOD: Aye.

11 And that is the wrap. Meeting adjourned.

12 [Whereupon, at 12:00 p.m., the Commission meeting
13 was adjourned.]

14

15

16

17

18

19

20

21

22

23

24

25