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BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

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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

868TH COMMISSION MEETING
OPEN MEETING

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

Wednesday, September 15, 2004
10:10 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 SECRETARY MAGALIE R. SALAS

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19 ALSO PRESENT:

20 JANE W. BEACH, Reporter

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P R O C E E D I N G S

(10:10 a.m.)

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

Please join us in the Pledge to our Flag.

(Pledge of Allegiance recited.)

CHAIRMAN WOOD: It's my sad duty, but genuine pleasure to, on behalf of the full Commission, recognize the people who have either retired in the past few weeks, or are retiring in the coming couple of weeks.

In response to our Commission's bio package, which we were fortunate enough to receive approval to do this year, we have some stellar people that have contributed so much to the life of this Commission and to the benefit of our country, that I wanted to recognize here today, as well, as the people who will not be able to attend.

I would like at this time to mention the folks who aren't going to be able to attend, that have also retired from the Commission, and to them, we send our thanks:

From the Executive Director's Office, Marian Moore, Raymond Reed, Dwight Siddell, Olivia Wallace, Frances

1 Young; from the Office of General Counsel, Bob Christin;
2 from the Office of Administrative Litigation, Theresa Burns;
3 from the Office of Market Oversight and Investigation, Jim
4 Caruso; from the Office of Energy Projects, Patricia Johnson
5 and Michele Patchan; and from the Office of Markets,
6 Tariffs, and Rates, Shirley Arrington, Thomas Celantano,
7 and Joseph Hamilton.

8 Today, we do have here a number of folks who,
9 again, are leaving, and I want to recognize all of them, and
10 bring them up here one at a time and present them with a
11 token or our esteem.

12 First of all, is our Irish Pennsylvanian, former
13 head of the Office of External Affairs and has been for my
14 entire time here, my very first hire and a good friend,
15 Kevin Cadden, receiving an Exemplary Public Service Award.

16 (Applause and presentation.) Our long-time Chief
17 Accountant from the Office of the Executive Director, John
18 Delaware, has been with FERC for seven years, but has been
19 in the Federal Government for 26 years, and so it's hard to
20 let you walk out the door, too, but I guess we'll have to
21 let you do it.

22 (Applause and presentation.)

23 CHAIRMAN WOOD: From the Office of Energy
24 Projects, I think we call him the father of LNG, Bob
25 Arvedlund has been with the Commission for 22 years. His

1 total federal service is 35 years. There's Bob.

2 (Applause and presentation.)

3 CHAIRMAN WOOD: You know, LNG came and went and
4 came back, so I guess it was you that brought them back.
5 We're glad you did. Thank you, Bob.

6 From the Office of Market Oversight and
7 Investigation is an old friend of mine and an old Texan, as
8 well, Darrell Blakeway. Darrell's been with the Commission
9 for a quarter of a century, and that's his federal service.
10 We're going to miss you a lot, too, Darrell.

11 (Applause and presentation.)

12 CHAIRMAN WOOD: We have four folks from the
13 Office of Markets, Tariffs, and Rates, and I want to
14 recognize first, Bob Catlin. Bob has been with FERC for a
15 quarter century, as well, just like Darrell, and has a full
16 federal service of 25 years, so congratulations, Bob.

17 (Applause and presentation.)

18 CHAIRMAN WOOD: Also in OMTR, Yvonne Owens, who
19 has been in the Gas and Electric Rate Filing Division, is
20 leaving us after 29 years and 30 years of federal service.

21 (Applause and presentation.)

22 CHAIRMAN WOOD: Willie Oxendine, 32 years of FERC
23 service and 33 years of total federal service. We're going
24 to miss you, too. You're a fixture around here.

25 (Applause and presentation.)

1 CHAIRMAN WOOD: When I was a little pup here the
2 first time around back in '90 and '91, all of us who worked
3 for Commissioners at the time, knew that we could always
4 count on Alice Fernandez to tell it like it was on the gas
5 side, and how pleased I was to come back to the Commission
6 three years ago and see Alice in a position of leadership,
7 not only on gas issues, but on electricity.

8 She was the author and is the author of the
9 document that has reshaped this industry, our Proposed Rule
10 on Standard Market Design, and has, in addition to that,
11 done a lot of things, in addition to just being a good
12 friend. Alice, I will miss you a tremendous amount. I
13 guess it's like Alice in Wonderland. Please come back and
14 see us. You know where we live.

15 (Applause and presentation.)

16 CHAIRMAN WOOD: Let's see -- okay, we'll do
17 Kris's in a little bit. All right, from the Office of
18 General Counsel -- and this is our record. She doesn't show
19 it. There's not a wrinkle on her face, so she must have
20 started here when FERC had a childcare center.

21 (Laughter.)

22 CHAIRMAN WOOD: She is the smiling face of the
23 Office of General Counsel. Joan Elizabeth Ross is leaving
24 us, and I know Cindy weeps, as we all do. But, Joan, come
25 on up. You've been with us 36 years and have a total

1 service with the Federal Government of 37 years, and we want
2 to send you off with a big hug and a lot of thanks.

3 (Applause and presentation.)

4 CHAIRMAN WOOD: And our final awardee is to
5 Kristina Nygaard, Kris Nygaard, who's been with FERC for 30
6 years, probably also started in the childcare center with
7 that good Scandinavian blood that never shows your age, and
8 total federal service of 30 years, as well. We want to give
9 her an Exemplary Public Service Award and thank you very
10 much for all you've done for this good Commission.

11 (Applause and presentation.)

12 CHAIRMAN WOOD: All right, we'll weep a few tears
13 and know that that group of people and all those that are
14 behind them, did a lot to bring us to where we are and to
15 make this country a better place, so thank you all very
16 much.

17 (Applause.)

18 CHAIRMAN WOOD: It's been a good seven weeks
19 since we last met, and there has been a significant number
20 of weather events in the country that have taxed our energy
21 infrastructure, and I want to just say, on behalf of all of
22 us, to the hardworking men and women in the gas, electric,
23 hydro, and oil pipeline industries, that we appreciate the
24 hard work that has gone on to keep our nation's energy
25 customers equipped with reliable and affordable service.

1 In regard, certainly to those kinds of events,
2 particularly the one that we see approaching the Gulf Coast,
3 I just wanted to clarify for, particularly the electric and
4 gas utilities that are subject to our independent
5 functioning requirement of our standards of conduct for
6 transmission providers, which is Section 358.4 of our
7 Regulations, which requires that in emergency circumstances,
8 a transmission provider may take whatever steps are
9 necessary to keep the system in operation, including
10 overlooking the separation of functions requirement.

11 We have asked in the rule that was promulgated
12 that such deviations from the standards of conduct be
13 reported on the Internet or OASIS website within 24 hours.
14 I know this is going to be a busy 72 or even longer hours
15 for folks down on the Gulf Coast where a number of our
16 energy companies operate, so I want to just say that, first
17 of all, good luck, keep the lights and the gas as reliable
18 as you possibly can, and with regard to reporting of any of
19 these deviations here, next Monday close of business is fine
20 enough and we'll be very flexible on waivers.

21 We are very interested in reliability first; and
22 the observance of the standards of conduct, while very
23 important to this Commission, is something that we have
24 always emphasized is really second seat to system
25 reliability, and particularly in times like this.

1 So we'll monitor that situation closely, as we
2 have all the other events this Summer, and wish our very
3 best to the customers in that part of the country.

4 Okay --

5 COMMISSIONER BROWNELL: Could I just add
6 something? I think a lot has been said about what happens
7 when monopolies get to a competitive industry and how
8 relationships change and the structure changes.

9 But I think what's happened in Florida as they
10 have received an extraordinary amount of help from their
11 neighbors, and in fact some quite distant neighbors who are
12 down there working on the lines with people is an example of
13 how the industry does and can and will continue to work
14 together for the service to their customers.

15 And to the folks at FPL and all the people who
16 have been out there for about three or four weeks without
17 sleep that we've talked to, we wish them well, and we're
18 thinking about them.

19 CHAIRMAN WOOD: Amen. All right, Madam
20 Secretary.

21 SECRETARY SALAS: Good morning, Mr. Chairman and
22 good morning, Commissioners. The following items have been
23 struck from the agenda since the issuance of the Sunshine
24 Notice on September 8: A-4, E-4, E-10, E-29, E-35, E-68, E-
25 71, E-72, E-73, E-75; H-3, H-7; C-1 and C-7.

1 Your consent agenda for this morning is as
2 follows: Electric Items - E-1, 2, 5, 11, 12, 13, 15, 16, 17,
3 18, 19, 22, 24, 25, 26, 28, 30, 33, 37, 38, 39, 42, 43, 44,
4 45, 46, 47, 48, 49, 50, 52, 53, 55, 56, 57, 58, 59, 60, 61,
5 62, 63, 64, 65, 66, 67, 69, 70, 74, and 76.

6 Gas Items: G-1, 2, 3, 4, 5, 6, 9, and 10.

7 Hydro Items: H-2, 4, 5, and 6.

8 Certificates: C-3, 5, and 6.

9 As required by law, Commissioner Kelly is recused
10 from the following items on the consent agenda: E-1, E-59,
11 E-64, E-67, E-70; G-4; H-4; and C-5.

12 Specific votes for some other items on the
13 consent agenda are as follows: E-24, Commissioner Kelly
14 dissenting, in part, with a separate statement; E-30,
15 Commissioner Kelliher concurring, with a separate statement;
16 E-43, Commissioner Kelly dissenting, in part, with a
17 separate statement; E-47, Commissioner Kelly dissenting, in
18 part, with a separate statement; E-49, Commissioner Kelliher
19 dissenting, in part, with a separate statement; and
20 Commissioner Kelly votes first this morning.

21 COMMISSIONER KELLY: I vote aye on all cases,
22 except those from which I am recused, and the three cases in
23 which I dissent, in part, as noted by the Secretary.

24 COMMISSIONER KELLIHER: Aye, noting the separate
25 statements observed by the Secretary.

1 COMMISSIONER BROWNELL: Aye.

2 CHAIRMAN WOOD: Aye. In that group of consent
3 items, we approved on E-33, a Basket Order addressing the
4 request of 25 transmission providers for exceptions or
5 waivers to the Standards of Conduct, as we've done in prior
6 meetings we're proceeding with exceptions and waiver
7 requests seriatim.

8 I want to note that under Order 2004, the
9 transmission providers are required to be in compliance with
10 the requirements of Standards of Conduct by September 22nd,
11 this month. Beginning on that date, OMOI Staff will roll
12 out a program of compliance evaluations for transmission
13 providers.

14 About 25 Staff from OMOI will begin reviewing the
15 OASIS and Internet websites to determine if transmission
16 providers have complied with all of the posting
17 requirements. As part of this program, OMOI will also
18 initiate contact with each of the Chief Compliance Officers
19 of the transmission providers, and work with them to ensure
20 that the transmission providers are in compliance with the
21 Standards of Conduct.

22 The main contact person for these compliance
23 evaluations will be Demi Onnis, Bryan Craig, and Janice
24 Gerson Nichols.

25 SECRETARY SALAS: The first item for discussion

1 this morning is a joint presentation of E-3. This is the
2 Public Utilities with Grandfathered Agreements in the
3 Midwest ISO Region, and E-23, Midwest Independent
4 Transmission System Operator. This is a presentation by
5 Jennifer Shepard Amerkhail, Sarah McWane, and Stephen
6 Pointer, who are accompanied this morning by Elizabeth
7 Rylander and Jeff Hitchings.

8 MS. AMERKHAIL: Good morning, Mr. Chairman and
9 Commissioners. Today's Draft Orders in E-3 and E-23,
10 resolve the treatment of grandfathered agreements in the
11 Midwest ISO's energy markets and conclude a paper hearing on
12 the allocation of Schedule 16 and 17 charges.

13 These two Orders, along with the August 6th Order
14 on the Midwest ISO's energy markets tariff, mark a major
15 milestone in creating efficient energy markets in the
16 Midwest.

17 When the Midwest ISO originally proposed its
18 transmission and energy market tariff, it estimated that
19 approximately 300 grandfathered agreements represented up to
20 about 40,000 megawatts of transmission rights or roughly 40
21 percent of the peak load in the Midwest ISO's footprint.

22 At the time, the Midwest ISO acknowledged that it
23 had limited data on the transmission capacity usage for half
24 of the grandfathered agreements, and no data on the
25 remaining agreements.

1 The Midwest ISO argued that allowing the parties
2 to the grandfathered agreements to maintain their current
3 scheduling rights, would require a physical reservation or
4 carve-out of the transmission from the Midwest ISO's
5 proposed energy markets.

6 The Midwest ISO also argued that this carve-out
7 would impair the reliability of the operation of its markets
8 and would impose additional financial costs on parties to
9 non-grandfathered agreement transactions.

10 Therefore, the Midwest ISO proposed three options
11 for scheduling and settling the grandfathered agreement
12 transactions: They proposed to allow parties to the
13 grandfathered agreements to choose from among these three
14 options.

15 In response, the Commission initiated a three-
16 step process under Section 206 of the Federal Power Act, to
17 gather information on the grandfathered agreements and to
18 address the treatment of transmission service provided under
19 the grandfathered agreements in the Midwest ISO's energy
20 markets.

21 The Commission also offered the parties to the
22 grandfathered agreements, an opportunity to settle on the
23 treatment proposed by the Midwest ISO, and the parties to 52
24 contracts actually reached agreement.

25 In Step Two of the process, Presiding Judges

1 Cintron and Johnson determined specified facts for 52 of the
2 grandfathered agreements, and presented their findings of
3 fact to the Commission at the July 28th Commission meeting.
4

5 The issuance of the Draft Order in E-3, the third
6 step of our analysis, will provide the Midwest ISO with the
7 information it needs to continue its market development
8 efforts, namely, to begin allocating financial transmission
9 rights in October, to begin market trials soon thereafter,
10 and to start the energy markets on March 1st of 2005.

11 The issuance of the Draft Order in E-23 resolves
12 how to allocate Schedule 16 and 17 charges, the
13 administrative costs of operating the energy and FTR markets
14 to entities within the Midwest ISO footprint.

15 Now, Sarah McWane will summarize the findings in
16 E-3.

17 MS. McWANE: Good morning, Mr. Chairman and
18 Commissioners. In E-3, the Commission completes its initial
19 analysis of the Midwest ISO's proposed transmission and
20 energy markets tariff.

21 As a result of the Commission's fact-finding
22 investigation, we have analyzed the contract information and
23 have divided the grandfathered agreements into several
24 categories. There are differing consequences for the
25 treatment of each group of contracts in the Midwest ISO's

1 energy and FTR markets, based on the parties' election to
2 settle, findings by the Presiding Judges in the hearing held
3 in Step 2, or our determinations in this Order.

4 As Ms. Amerkhail described, the Midwest ISO
5 initially estimated that up to 40,000 megawatts of
6 transmission service, 40 percent of total Midwest ISO load,
7 is provided under the GFAs, however, the results of the
8 fact-finding investigation conducted in Steps 1 and 2,
9 indicate that only 25,000 megawatts of transmission service
10 or 23 percent of total Midwest ISO load, is provided under
11 229 GFAs that will remain in effect on March 1, 2005 and
12 when the Midwest ISO commences operation of its energy
13 markets.

14 Of this 25,000 megawatts of transmission service,
15 approximately 9700 megawatts or nine percent of total
16 Midwest ISO load, will participate in the Midwest ISO's
17 energy markets, because the parties voluntarily settled on
18 one of the Midwest ISO's three treatment options for GFAs,
19 or decided to voluntarily convert their service to TEMT
20 service. The Draft Order accepts these voluntary
21 settlements.

22 Approximately 5,000 megawatts or 4.5 percent of
23 total Midwest ISO load, is represented by GFAs subject to
24 the just and reasonable standard of review. Those GFAs will
25 also participate in the Midwest ISO's markets, pursuant to

1 the requirements of this Order.

2 This leaves only approximately 10,400 megawatts
3 or 9.6 percent of total Midwest ISO load. Those GFAs
4 represent transmission service provided under GFAs for which
5 the parties have explicitly provided that the Mobil-Sierra
6 public interest standard of a review applies, those GFAs
7 that are silent with respect to the standard of review and
8 those GFAs providing for transmission service by an entity
9 that is not a public utility.

10 The Order requires the Midwest ISO to carve these
11 GFAs out of the energy markets. We find that the Midwest
12 ISO will be able to reliably operate its energy and FTR
13 markets with this carve-out of GFAs, given the relatively
14 small amount of transmission service, which is less than ten
15 percent of total Midwest ISO load involved.

16 Moreover, we find that even with this carve-out,
17 the Midwest ISO's energy and FTR markets will be more
18 reliable and efficient, overall, than the market currently
19 in place in the region.

20 Certain GFAs that we do not have certain
21 information in the tariff record before us to determine
22 whether transmission service under them is provided over
23 Midwest ISO facilities, or whether these contracts should be
24 excluded from the proceeding and not be considered GFAs for
25 purposes of the energy markets, therefore, we will set them

1 for further hearing and Settlement Judge procedures for the
2 parties to address the threshold issue of whether the
3 service provided under these contracts will impact operation
4 of the energy markets.

5 Finally, this Order finds that the Midwest ISO's
6 proposed Options A and C for treatment of GFAs, as filed in
7 Section 38.8.3(a) or the TEMT, are just and reasonable, and
8 accepts the relevant tariff sheets. It limits the
9 availability of Option B to those parties that settled on it
10 prior to July 28th of 2004.

11 In conclusion, we expect that this Order will
12 provide parties to the GFAs and the Midwest ISO, with the
13 framework they need to begin the FTR allocation process on
14 schedule, thereby meeting a deadline critical to an on-time
15 start to the energy markets.

16 I would now like to turn the presentation over to
17 Stephen Pointer, who will be discussing the applicability of
18 Schedules 16 and 17 to transactions taking place under GFAs
19 and a discussion of E-23. Thank you.

20 MR. POINTER: Good morning, Mr. Chairman and
21 Commissioners. The Draft Order in E-23 addresses a paper
22 hearing that the Commission previously ordered to evaluate
23 the cost allocation of the charges for financial
24 transmission rights and energy market service as Schedule 16
25 and 17, respectively.

1 The Draft Order finds that Midwest ISO's
2 unbundling of the Schedule 16 and Schedule 17 charges from
3 the Midwest ISO cost adder in Schedule 10, is reasonable.

4 Specifically, the Draft Order in E-23 finds that
5 only those parties receiving a hedge against congestion
6 costs should pay the Schedule 16 charges.

7 For Schedule 17, the Draft Order finds that all
8 parties injecting and withdrawing energy from the
9 transmission system, benefit from the energy markets and
10 should thus be assessed the Schedule 17 charge.

11 In E-3, the Draft Order applies the findings in
12 E-23 to the grandfathered agreements. The Draft Order finds
13 that both Option A and Option B grandfathered agreements
14 benefit from a hedge against congestion, therefore, both
15 groups should be assessed the Schedule 16 charge.

16 Conversely, the Draft Order finds that since the
17 carved-out grandfathered agreements are not assessed
18 congestion and will not be allocated FTRs, they should be
19 exempt from the Schedule 16 charge.

20 With respect to Schedule 17, the Draft Order in
21 E-3 finds that transactions under grandfathered agreements,
22 including those that have been carved out, benefit from the
23 existence of energy markets, and should be assessed the
24 Schedule 17 charge. Thank you.

25 CHAIRMAN WOOD: Any questions, comments,

1 thoughts? Joseph?

2 COMMISSIONER KELLIHER: I support the Orders, and
3 I just wanted to make a few comments about E-3. And I'd
4 like to commend Chairman Wood for the deliberate approach
5 taken in this Order.

6 A few months ago in the Spring, it looked like we
7 had two start choices, either abrogate 300 contracts of
8 cripple MISO's energy and transmission markets, and they
9 were pretty unpleasant choices.

10 But there were legitimate questions about the
11 accuracy of MISO's estimates with respect to the number of
12 contracts and the transmission capacity associated with the
13 contracts, and there also were some signs that the parties
14 might be willing to settle.

15 So I just wanted to commend the Chairman for the
16 approach we took in the Procedural Order. The fact-finding
17 investigation showed that MISO's estimates were not
18 accurate, and the parties showed a remarkable capacity to
19 enter into settlements, so I think we avoided the two-star
20 choices we were presented with in the Spring, and it didn't
21 just happen; it happened because of the hard work of the
22 ALJs, the Commission Staff, and also the good faith of the
23 settling parties. So I just wanted to make those comments.

24 CHAIRMAN WOOD: Before -- you're very kind, but I
25 will have to give the credit to Sudeen. She wandered down

1 several weeks before our last Order, and just said there is
2 a third way here, and to go out and craft it. I'm looking
3 at the crafters over here and a few others in the audience,
4 but I am a big believer, as I think we've all are, when
5 parties get to agreement on their own, or get close to it,
6 it's a whole lot more lasting than when we have to kind of
7 force it to happen.

8 And I think that the Commission has learned that
9 time and time again, and this is a good example of it.

10 COMMISSIONER KELLY: Thank you, Pat. I'd like to
11 just add to Joe's commendation of the parties and the
12 Presiding Judges and the Commission Staff. They made all
13 this progress in a short three and a half months, and that's
14 quite remarkable, and it was a lot of work, and thank you
15 all for your efforts. We appreciate it.

16 CHAIRMAN WOOD: Do you want to add anything?

17 COMMISSIONER BROWNELL: Just a wonderful job.
18 It's hard to follow on that eloquence. It was Solomon-like
19 in the way in which the Staff and the Judges approached
20 this.

21 I think it's illustrative that, as my colleagues
22 have said, when parties really have an incentive to settle,
23 they can do so. I hope people look at this, which was
24 enormously complicated, and say, if we can do it here,
25 there's a whole lot of other places that we can get to some

1 settlement before we have to delay and litigate and add more
2 cost to the market.

3 CHAIRMAN WOOD: And I think, in that spirit,
4 through the power of our wonderful new tool, virtual agenda,
5 we can sure pull up a lot of the pleadings a lot easier than
6 we used to when they were all reams of paper.

7 And I recognize that there are a lot of, you
8 know, intense feelings from the parties in this docket,
9 because it is a huge docket. But it's time to move on.

10 The Commission has provided opportunities for
11 people to settle, and a wonderful amount of people took
12 advantage of that. We've implemented the terms of
13 contracts, as contracts were written in a different time and
14 place, and yet we've been able to work them into this
15 current model and live with the intents of the parties.

16 We have taken, as has MISO, very seriously, the
17 responsibility to ensure that customers receive service at
18 least equal to the quality of transmission service they're
19 getting today, if not better.

20 But it is time for the folks out in the large
21 Midwest ISO footprint to move on. It's time to rally around
22 to get the FTRs allocated, to get the training done, the
23 necessary training to get comfortable with the new systems,
24 and to enable MISO to focus exclusively on that effort of
25 getting the markets in place, and not fighting the brush

1 fires of this or that person trying to jockey for personal
2 or professional interest, but looking after the broader
3 public interest out there.

4 So I strongly encourage and will expect to see
5 people rallying around the flag and getting this important
6 market moving to a more reliable and more efficient and more
7 customer-benefitting level than we have seen so far.

8 It's a real positive movement, and I join in the
9 lauds for Judges, for our Staff, for the parties, for MISO,
10 for all you. This was a very significant Order that I know
11 sucked the life out of our hall these past two weeks, but
12 the Staff has been working really through what's
13 traditionally a quieter time here at FERC in August, and the
14 folks over here didn't get their lingering weeks on the
15 beach. I think they were lingering weeks behind a
16 wordprocessor, and reading pleadings, and running numbers
17 and doing spreadsheets, because this is a tremendous amount
18 of data here, particularly the attachment to the Order that
19 we vote out under E-3.

20 So, thank you for the time you all gave, and for
21 all the team behind you that cranked out the hard work here.

22

23 COMMISSIONER BROWNELL: Can I use the platform to
24 give a pitch on the training issue? Dan and I and Mike
25 McLaughlin and others were at MISO recently. We met with

1 the TOs and the coops and some of the smaller entities to
2 talk about the importance of training.

3 We saw some examples in other markets where some
4 of the entities didn't avail themselves of that training,
5 and I think that there is a tremendous amount of effort
6 being put into this by both MISO and the TOs, and we
7 encourage and will ask for reports on who is getting
8 trained, who is taking advantage of this, and we'll do
9 whatever we can to make sure that everyone who is playing in
10 the market, has the tools to play.

11 And I think that will be a critical component,
12 going forward, so maybe we can actually have a report at one
13 of the meetings as the modeling continues.

14 CHAIRMAN WOOD: I'd ask Mike McLaughlin if we
15 could just go ahead and get that lined up, just whatever
16 their training timetables are, some report thereafter, in
17 probably the November timeframe or so, just to get an
18 update? Either call it in or come here, whatever works
19 easier.

20 Don't pull them away from training to come here,
21 but if we have to do it on the phone, we can do that, too.

22 MR. McLAUGHLIN: Yes, sir, Mr. Chairman.

23 CHAIRMAN WOOD: Great, thanks, Nora, for your
24 personal leadership on that, being out at the MISO
25 membership meetings for the past several months on behalf of

1 all of us. We appreciate that, and I know they do, too.

2 COMMISSIONER BROWNELL: We love Carmel, Indiana,
3 and Indianapolis.

4 (Laughter.)

5 CHAIRMAN WOOD: Good retail, and with a little
6 time off, you can hit the malls.

7 All right, let's see what we have. Are we ready
8 to vote? Anything else?

9 (No response.)

10 COMMISSIONER KELLY: Aye.

11 COMMISSIONER KELLIHER: Aye.

12 COMMISSIONER BROWNELL: Aye.

13 CHAIRMAN WOOD: Aye.

14 SECRETARY SALAS: The next item for discussion
15 this morning is E-6. This is Financial Report and Cost
16 Accounting Oversight and Recovery Practices for Regional
17 Transmission Organizations and Independent System Operators.
18 It's a presentation by Julie Kuhns, accompanied by Lodie
19 White, Jim Guest, Mark Hegerle, Larry Greenfield, and Chris
20 Thomas, and Katherine Gensler.

21 COMMISSIONER BROWNELL: Fellow Commissioners, I
22 asked to call this today, because I think it is an important
23 issue on which we need to focus.

24 In the past six months or so, my friend, John
25 Delaware, has led a team to audit the RTOs. Rob Gramlich

1 and a team have been looking at the request of the Southwest
2 Commissions and a report to see if we could separate day one
3 and day two costs, and really begin to get a handle on the
4 costs.

5 Of course, there has been an ongoing process that
6 Allison started and Dan Larcamp's team is continuing to work
7 on, and that is IT costs, which are the largest drivers of
8 costs in, particularly, startups.

9 One of the things we discovered, much to our
10 dismay, is that we are not accounting consistently between
11 and among RTOs, and, in fact, as the world has changed, we
12 thought we needed to look at the broader Uniform System of
13 Accounts as it applies to all of the regulated entities, so
14 we can begin to do a compare-and-contrast, which is
15 impossible, candidly, to do today in any meaningful way,
16 although we're going to continue to give this our best shot.

17 But I think this NOI, we'll find, raises issues
18 that we need to answer. The RTOs themselves have begun to
19 work on this, and I think will provide leadership. But
20 that's kind of what this -- what led to this.

21 We had hoped to have some of these reports ready
22 to fly, but we'll have those ready in the next couple of
23 weeks, and you'll begin to see, firsthand, some of the
24 challenges that the teams faced.

25 CHAIRMAN WOOD: Great. Thanks, Nora.

1 MS. KUHNS: Good morning, Mr. Chairman and
2 Commissioners.

3 Before I begin my presentation, I would like to
4 acknowledge Mark Close as a member of this team. Mark is
5 currently in St. Louis, speaking to the NARUC staff
6 Subcommittee on Accounting and Finance, so he could not be
7 with us today.

8 E-6 is a Draft Notice of Inquiry which invites on
9 the Commission's accounting and financial reporting
10 requirements for oversight of RTO and ISO costs. The draft
11 encourages broad comments, but, more specifically, asks
12 whether the Commission needs to adopt changes to the Uniform
13 System of Accounts for public utilities, subject to the
14 Federal Power Act, to better account for and report RTO and
15 ISO cost information on whether RTOs and ISOs have
16 appropriate incentives to be cost efficient, and whether the
17 Commission's rate review methods for RTOs and ISOs are
18 sufficient.

19 To put this draft NOI in context, some brief
20 background information may be helpful. When the Commission
21 began unbundling and restructuring the electric industry,
22 new forms of businesses were created called RTOs and ISOs.

23 At that point, however, the Commission did not
24 mandate a specific business model, but, instead, followed an
25 open-architecture approach to these organizations. Since

1 that time, RTOs and ISOs have developed more defined
2 operations and the process is still evolving.

3 Over the past seven years, the Commission has
4 approved several RTOs and ISOs: The PJM Interconnection,
5 ISO New England, and Midwest Independent Transmission System
6 Operator] were first approved or conditionally approved as
7 ISOs and later as RTOs.

8 New York Independent System Operator and
9 California Independent System Operator were approved as
10 ISOs. The Commission has also conditionally approved
11 Southwest Power Pool, which currently operates a regional
12 transmission tariff as an RTO.

13 This draft NOI examines on a more formal basis,
14 the sufficiency of current accounting, reporting, and cost
15 review practices for these entities. Thank you.

16 CHAIRMAN WOOD: Thank you, Julie. This is
17 probably overdue. I mean, we've got now the study that
18 we've got over two-thirds of our nation's economy, GDP, in
19 these organized regional grids, and, of course, electricity
20 is such an important infrastructure of our whole country,
21 that the fact that two-thirds of it are under these
22 organizations, it is time to move from the, you know,
23 experimental phase to the full-bore phase of having proper
24 apples-to-apples, standardized approaches toward financial
25 reporting that we have had for many years with all of our

1 other utilities.

2 I understand from Nora, I think your meeting with
3 some of RTO folks recently, that they're there. They are
4 ready to embrace this, and I think it's really just getting
5 the information to where it's useful to everybody.

6 One that was useful to me in a earlier career was
7 just such information. We didn't have quite the same
8 expectations for ERCOT as we're laying out here for the FERC
9 jurisdictional RTOs and ISOs, but nonetheless -- and one of
10 the questions goes toward this end.

11 It was clear that when these costs were clearly
12 recorded, it became easier for regulators, both state and
13 wholesale regulators, to look at whether there was a
14 duplication of costs. And one of the things we had not
15 seen, really the benefits that we had not really seen here,
16 that we usually do see in utility-to-utility mergers, are
17 synergy savings of combining operations of multiple
18 divisions into a single entity.

19 Economies of scale and of scope are the kind of
20 things that utilities present to us as rationales to support
21 their merger applications and have done for many years, and
22 legitimately so. I think it's the same type of thing that
23 we should look for here, and that we are not capturing as
24 well, that when activities that are being performed across,
25 say, in the case of Texas, ten different control areas, were

1 consolidated into one, the savings run in the Day One ERCOT
2 model were dwarfed by the fivefold amount that were removed
3 from transmission providers' rates, because it was functions
4 that they no longer performed.

5 So, one of the questions here in (b)(5) asked, in
6 fact, you know, are we providing state regulators and
7 ourselves, the proper information to make sure that there's
8 not a double recovery for functions that are being
9 consolidated and being more efficiently performed under the
10 umbrella organizations?

11 So I hope that this will be a useful tool, not
12 only for us in our broad regulatory oversight and obligation
13 to the customers to make sure that RTOs and ISOs are being
14 run efficiently and being run well, it's useful information
15 for their boards, for the independent boards to look at, as
16 they look at other entities across the country, and they can
17 see if they're comparable, if they're higher or lower than
18 the other utilities, but also to the state regulators, who,
19 like us, are charged with a broader public interest charge.

20 And I think that this information, assuming that
21 we move forward with the proposed and final rule, would be
22 just the type of information that makes it helpful for state
23 regulators and for us to make sure we're getting the best
24 bang for the buck in our energy industry.

25 So, I'd like to see the comments come out on all

1 of these other issues, as well.

2 COMMISSIONER BROWNELL: I'm glad you brought up
3 the state regulators. Diane Munz, who is in the leadership
4 at NARUC and has been active in the Accounting Committee,
5 met with us, not anticipating that this is something we were
6 doing, and asked that we begin a process like this.

7 There is great frustration that they are not
8 seeing the efficiency and the energy gains, that they are
9 largely hidden. Sadly, I'm not sure we're ever going to be
10 able to reconstruct, particularly in the older RTOs, but I
11 hope that the comments get to this particular issue in a
12 very surgical way, because I think this is very important,
13 going forward, for all of us, for just those reasons.

14 COMMISSIONER KELLY: And I'd like to thank Nora
15 for her leadership on this issue. She's really been the
16 driving force behind it, and she's committed a lot of
17 personal time and extra time, and I appreciate it. Thanks,
18 Nora.

19 COMMISSIONER BROWNELL: The mere thought that I
20 would be involved in accounting matters, would frighten my
21 family.

22 (Laughter.)

23 COMMISSIONER BROWNELL: And my former banking
24 employers, too. Thank you.

25 (Laughter.)

1 CHAIRMAN WOOD: It is an item on our strategic
2 plan, on the costs and oversight, so thank you for
3 delivering on one of the things we promised the world we're
4 going to do this year.

5 COMMISSIONER BROWNELL: Thank the team. They did
6 the hard work. I was just the noise.

7 CHAIRMAN WOOD: All right. We call her a
8 catalyst around here.

9 (Laughter.)

10 CHAIRMAN WOOD: Thank you? Joe, anything?

11 COMMISSIONER KELLIHER: I just wanted to commend
12 Nora for her leadership on this, and say that I agree with
13 Pat, that this is something that probably is overdue, and
14 I'm glad we're going to take this step, and I support the
15 Order.

16 There's a lot of concern that RTOs aren't
17 adequately managing their costs, and I'm looking forward to
18 seeing the responses to the questions in the cost management
19 area. I support t the Order.

20 CHAIRMAN WOOD: Great.

21 COMMISSIONER KELLY: Aye.

22 COMMISSIONER KELLIHER: Aye.

23 COMMISSIONER BROWNELL: Aye.

24 CHAIRMAN WOOD: Aye. Thank y'all again.

25 SECRETARY SALAS: The next item for discussion is

1 C-2. This is Trunkline Gas Company. It's a presentation by
2 Buu Nguyen, who is accompanied by John Myler, John
3 Wisniewski, Steve Busch, Frank Sparber, and Pamela Seeley.

4 MR. NGUYEN: Good morning, Chairman Wood and
5 Commissioners. The Draft Order in Item C-2 grants Trunkline
6 LNG Company, LLC, amended Section 3 authorization to expand
7 its LNG terminal located in Calcasieu, Louisiana. The Draft
8 Order also issues a Certificate under Section 7 of the
9 Natural Gas Act, to Trunkline Gas Company, LLC, to construct
10 and operate a sendout line to accommodate the regasified LNG
11 from Trunkline LNG's terminal expansion.

12 Here, the Draft Order authorizes Trunkline LNG to
13 install unloading facilities, vaporizers, and second-stage
14 pumps to provide additional firm vaporization service and to
15 increase the sendout capability for its customer, BG LNG.

16 The sustained sendout capacity of the LNG
17 terminal will be increased from 1.2 to 1.8 billion cubic
18 feet per day, with 2.1 billion cubic feet per day peak
19 sendout capacity.

20 The modification will not change the nine billion
21 cubic feet authorized level of storage capacity of the
22 terminal. Trunkline LNG also requests authorization to
23 convert a previously approved lay berth to an unloading
24 facility.

25 This conversion will give Trunkline LNG two

1 unloading berths and will permit continuous unloading of
2 ships from either of the two docks, however, no simultaneous
3 unloading of LNG ships will occur.

4 BG LNG will use 100 percent of the terminal's
5 expanded capacity under a long-term contract that terminates
6 December 31, 2023. The combined total cost of Trunkline
7 LNG's expansion projects is approximately \$253 million.

8 The Draft Order also authorizes Trunkline Gas to
9 construct approximately 23 miles of 30-inch diameter
10 pipeline, looping its existing LNG lateral and related
11 facilities, in order to accommodate the increased sendout
12 capacity of Trunkline LNG's terminal.

13 Trunkline Gas entered into a firm transportation
14 service agreement with BG LNG to provide transportation
15 service up to 1.5 million decatherm per day of regasified
16 LNG. Because the revenue generated by the BG LNG contract
17 will exceed the projected costs of the LNG loop, the Draft
18 Order will permit Trunkline Gas to roll in the costs of its
19 proposed facilities when Trunkline Gas files its next
20 Section 4 rate case. The cost of the proposed LNG loop
21 project is estimated to be \$40 million.

22 Notices of the application were issued on
23 February 19th and March 16th, 2004. In response, no party
24 protested or argued that the adverse economic result will
25 occur as a result of either application. An EA was issued

1 on July 29, 2004.

2 Trunkline LNG and Trunkline Gas estimate that an
3 overall 27-month construction period is needed to complete
4 the projects previously authorized, as well as the
5 construction contemplated herein.

6 Since construction has already commenced on the
7 previously-authorized LNG expansion, Trunkline LNG and
8 Trunkline Gas intend to complete the projects to meet an in-
9 service date of January 1, 2006.

10 This concludes my presentation. And we are now
11 available to answer any questions you may have. Thank you.

12 CHAIRMAN WOOD: Thank you, Buu. I just wanted to
13 call this separately to call attention to not only the nice
14 work of the Staff in handling these issues, the technical
15 and environmental issues in such a short time, but also to
16 focus, as we have done so frequently, on the investment
17 that's taking place in the liquified natural gas arena in
18 our country.

19 This is kind of quiet. Everybody is focusing on
20 the loud and screaming applications that, you know, may or
21 may not get approved by this Commission, but there are ones
22 that go through where the companies work with the local
23 neighborhoods, they work with the environmental permitting
24 officials, state and local governments, and they get
25 expansions done.

1 The expansion here is significant. It's as much
2 as some brand new proposals that are being considered
3 elsewhere in the country. And while I think it's important
4 to have a nice dispersion of LNG across the country, it is
5 of primary importance to get the gas to our continent.

6 We have learned how to develop systems to move
7 around the continent quite well over the last 60 or so
8 years, so we can do that. That's not to say that we
9 couldn't use them on the West Coast and on the East Coast as
10 well, but as a Gulf Coaster, I'm glad to see them on the
11 Gulf Coast, too.

12 So, this is a good day for customers and for the
13 stability of this industry, to see that evolve in a short
14 year and a half, I suppose, when we'll have a substantial
15 expansion already in place there in Louisiana.

16 So, thanks for your hard work and your
17 presentation.

18 MR. NGUYEN: Thank you.

19 COMMISSIONER KELLY: Aye.

20 COMMISSIONER KELLIHER: Aye.

21 COMMISSIONER BROWNELL: Aye.

22 CHAIRMAN WOOD: Aye. Thanks.

23 SECRETARY SALAS: And the final item for
24 discussion this morning is A-3. This is a Staff Report on
25 Natural Gas Storage. It's a presentation by Berne Mosley,

1 who is accompanied by Tom Pinkston, John Carlson, and Tom
2 Bahumian.

3 MR. MOSLEY: Good morning, Chairman and
4 Commissioners. The purpose of today's presentation is to
5 give you a preview of a Staff Report on Underground Storage,
6 which will be publicly available within two weeks.

7 First, a little background: This effort began in
8 response to questions posed to Staff at the June 17th open
9 meeting. Over the Summer, a team comprising Staff from the
10 Offices of Energy Projects, Market Oversight and
11 Investigations, Markets, Tariffs, and Rates, and the General
12 Counsel, worked together to prepare a Staff report that is
13 not only responsive to your earlier questions, but also
14 presents some new regulatory and policy approaches that may
15 help to ensure that needed underground storage
16 infrastructure is, indeed, developed.

17 More specifically, the upcoming Staff report will
18 address four main aspects of the state of and issues
19 concerning the underground storage of natural gas, namely,
20 the history of storage development and its physical
21 characteristics, the need for new storage, the economics of
22 underground storage, and the effects of various rate designs
23 on future storage development.

24 Now, to the presentation: May we go to the
25 second slide, please?

1 (Slides.)

2 MR. MOSLEY: This slide shows a map of the U.S.,
3 superimposed with icons representing the three types of
4 commonly used storage facilities -- Salt caverns, depleted
5 reservoirs, and aquifers.

6 It's interesting to note the lack of storage
7 infrastructure in New England and the Southwest. This
8 uneven geographic distribution will be described in more
9 detail in the upcoming Staff Report.

10 (Slide.)

11 MR. MOSLEY: The next slide provides an overview
12 of some projects that have been recently authorized, are
13 currently pending at the Commission, or are on the horizon.
14 Again, there is little storage development activity in New
15 England or the Southwest.

16 However, from an overall perspective, we are
17 making some progress, and we are seeing continued
18 development of storage. For example, since 2002, we've
19 certificated 75 Bcf of new storage, 57 of which is already
20 in service, and we have projects totalling 54 Bcf still
21 pending at the Commission.

22 For 2005, we're expecting to certificate an
23 additional 116 Bcf, yet, according to certain forecasts, the
24 development must continue apace to meet the projected need
25 of 700 Bcf of storage by 2025.

1 So, what approaches can help keep us on target?
2 Later, we'll discuss policy changes that may encourage
3 development, but as far as physical approaches,
4 reclassification of base gas to working gas, is one
5 technique that has proven useful in developing new storage
6 deliverability.

7 Other new engineering approaches also show
8 promise. And while another form of gas storage, LNG, is
9 emerging to supplement our national needs, it can't
10 necessarily match all of the types of service available from
11 underground storage.

12 Staying on track to develop new storage, however,
13 can be challenging, particularly in areas of the country
14 where there are geological and other limitations. Now,
15 let's look at the economics of storage and how the valuation
16 of storage may impact its development.

17 (Slide.)

18 MR. MOSLEY: Prospective developers determine the
19 value of storage from a variety of financial considerations,
20 including the expected return on equity. From a regulatory
21 standpoint, the Commission has allowed returns on equity up
22 to 15 percent, although, as a whole, potential storage
23 developers, including non-regulated companies, typically
24 target equity returns exceeding 20 percent.

25 The physical operation of storage fields, such as

1 how many injection and withdrawal cycles can be achieved in
2 one season, also helps determine the value and helps predict
3 the potential returns on equity, yet multi-cycle fields,
4 such as salt dome caverns, can be more than twice as
5 expensive to develop as depleted reservoir fields.

6 Other physical factors such as the proximity to
7 existing pipeline infrastructure, also affect the
8 development costs, and hence the market valuation.

9 In addition, the intended use of the storage,
10 such as for reliability, imbalance management, or seasonal
11 arbitrage, impacts the costs-versus-value decision.

12 (Slide.)

13 MR. MOSLEY: So, let's look at valuation. We
14 have four typical approaches for valuation: Cost of
15 service, least-cost supply planning, intrinsic, also known
16 as seasonal arbitrage, and extrinsic, or option-based
17 valuation.

18 I should point out that these approaches are not
19 mutually exclusive, that all of them are currently in use,
20 and that many gas customers will avail themselves of more
21 than one of these.

22 The first approach involves consideration of the
23 availability of storage at rates developed by traditional
24 cost-of-service ratemaking. The least-cost supply planning
25 approach, which is typically used by local distribution

1 companies and other large gas customers, employs the concept
2 of first using the cheapest available supply option, then
3 the next cheapest, and so on and on, until the load is fully
4 served.

5 Intrinsic valuation involves assessing the
6 difference between a pair of forward prices. It is the
7 fundamental value of storage, and does not include
8 additional trading benefits. Extrinsic valuation considers
9 the trading benefits that increase with the number of
10 injection and withdrawal cycles within a year.

11 Essentially, gas in storage is a call option on a
12 time spread, with the value of the option being a function
13 of forward prices, volatility, strike price, and the timing
14 of the expiration.

15 Pricing options also influence storage investment
16 decisions. Historically, rates for storage were designed
17 using traditional cost-based ratemaking. However, over the
18 last few years, the Commission has developed non-
19 traditional approaches to cost-based rates, in order to give
20 more flexibility to project developers and to customers
21 alike.

22 In addition, the Commission has granted market-
23 based rate authority to storage applicants that satisfied
24 market power tests.

25 Earlier, I described various physical approaches

1 already being pursued, that may help ensure that the
2 development of storage stays on track to meet projected
3 future needs, but to the extent that the Commission believes
4 that additional storage development would be beneficial to
5 gas markets, it could reexamine its policies to determine
6 where the new approaches or non-traditional cost-based
7 rates, market-based rates, and certificate matters, may
8 encourage the development of new storage.

9 For example, consideration could be given to
10 cost-of-service adjustments, such as return on equity
11 premiums or accelerated depreciation, or a modification
12 could be made to the certificate requirement that calls for
13 a cost versus revenue study after three years.

14 With regard to market-based rates, a possible
15 approach may be to grant market-based rates for new
16 independent storage projects or possibly adjusting the
17 current market power test when it comes to storage.

18 Another approach could be to develop new optional
19 certificate procedures or otherwise grant appropriate
20 waivers.

21 Now, let's review the preliminary findings of the
22 upcoming Staff report: First, when we look at storage from
23 a broad perspective, it appears to be adequate, although in
24 light of some recent price spikes, more storage may be
25 appropriate.

1 Next, storage is a way of managing price
2 volatility, so, long-term investment in storage really comes
3 down to how much volatility customers are willing to accept.

4

5 And, finally, creative ratemaking approaches,
6 along with certificate and policy choices, may result in
7 more storage development. This concludes my presentation,
8 and I'm available for questions.

9 COMMISSIONER KELLY: Berne, why do developers
10 target 20 percent return on equity? What's the risk
11 involved?

12 MR. PINKSTON: The developers target 20 percent
13 returns on equity. That's not to say they always achieve
14 those types of returns.

15 There's a lot risk, especially with the higher
16 deliverability storage. There's geologic risk, operational
17 risk, timing risk, because of the leaching, to develop the
18 cavern, and then the disposal of the brine. Those types of
19 risks are probably justified -- that type of return is
20 justified, at least targeted for the risk.

21 COMMISSIONER KELLY: And for a developer, what's
22 the time range that they typically work with, in bringing a
23 project online?

24 MR. PINKSTON: It could be one, two, or more
25 years, depending on what the local permitting situation and

1 opposition may be.

2 COMMISSIONER KELLY: So --

3 MR. PINKSTON: Now, this is speaking more towards
4 the salt cavern storage.

5 COMMISSIONER KELLY: So the variability in
6 development really has to do with the regulatory process, as
7 opposed to the physical development?

8 MR. PINKSTON: It's regulatory in geologic, also,
9 especially if you're not working with the salt dome, as is
10 typical on the Gulf Coast, but looking at more layers of
11 salt. There's quite a bit of risk as to the size of the
12 cavern and the stability.

13 COMMISSIONER KELLY: Thank you. In the
14 Southwest, you pointed out that there is not much storage,
15 and you said, in part, it was geologic, and, in part, market
16 forces. Are you able to talk in any more detail at this
17 time about what those market forces are?

18 MR. CARLSON: Commissioner, historically, El Paso
19 has served most of the customers in the Southwest, and until
20 last September, it offered services on a full-requirements
21 basis.

22 Essentially there was no demand for separate
23 contracts for storage services. All of the requirements of
24 the full-requirements customers were met by El Paso.

25 In contrast, its California customers were

1 contract demand customers, PG&E and SoCal. And over the
2 years, they built considerable amounts of storage in their
3 service territories. In fact, I think that back in the
4 '70s, there used to be arrangements where El Paso would back
5 off from delivery to California to serve the East-of-
6 California requirements.

7 Since last September, you know, conditions have
8 changed on El Paso. We've converted the full-requirements
9 customers or the majority of them to contract demand
10 service, and since that time, actually, El Paso just filed a
11 settlement on Monday that would for the first time, start to
12 impose some -- if it's ultimately approved by the Commission
13 -- some balancing requirements on the system. Those are
14 some of the reasons why there hasn't been development thus
15 far.

16 COMMISSIONER KELLY: And is El Paso going to --
17 didn't they announce plans to expand their pipeline?

18 MR. CARLSON: They have had a couple of open
19 seasons. One, I think there's an open season to do an
20 expansion on the very far western end of the system, to give
21 it some additional capability to move gas from the northern
22 system to the southern system.

23 They have on the books and have actually
24 purchased, the rights to develop this Copper Eagle storage
25 facility that's on the chart, that showed the on-the-horizon

1 projects. I think they have a couple of other expansions,
2 as well, in the works.

3 COMMISSIONER KELLY: And are there any other
4 pending projects, storage projects in the Southwest yet?

5 MR. MOSLEY: Not that I'm aware of. Back to your
6 question about the types of projects that did nor did not
7 get developed, we're going to have a better description of,
8 I believe, four, in the Staff report that we're issuing,
9 which will tell what the project was, whether or not it was
10 authorized or not, and if it was authorized, why or when
11 it's gone into service, and it will go into the economic
12 factors and the environmental factors associated with the
13 individual projects.

14 COMMISSIONER KELLY: Thanks. And then one last
15 question: What's the technology that's allowing base gas to
16 be used as working gas?

17 MR. BAHUMIAN: Loss of existing storage fields in
18 the United States, depleted oil and old gas reservoirs. And
19 they have naturally capability of producing 50 percent
20 working and 50 percent as a cushion.

21 And from 1992 to 1994, by 636 going to affect
22 lots of companies that modified their cushion gas, working
23 gas to cushion gas ratio, they increased that. By doing
24 that, there's a technical reason behind it, and they are
25 able to provide higher deliverability rate and to be able to

1 recycle the gas with today's market, but also they have
2 reclassified some of their working gas to cushion gas.

3 That's a cushion right there, sitting there, 400
4 Bcf as the cushion gas, but actually is a working gas. If
5 we put additional facilities in there, we can reclassify it
6 as working gas and that would compensate a lot of short
7 volumes we have in storage.

8 COMMISSIONER KELLY: Thank you.

9 MR. HEDERMAN: Commissioner, if I could add to
10 that, putting on one of my old hats, technology like
11 horizontal drilling comes into play, because basically you
12 go in and do horizontal drilling into the old field that you
13 had produced in a conventional way. It increases the
14 ability for flow, and, therefore, you need less pressure, so
15 less pressure means less base gas, and so you convert it.

16 COMMISSIONER KELLY: Thank you.

17 CHAIRMAN WOOD: Joe?

18 COMMISSIONER KELLIHER: I just had a couple of
19 questions. Thank you for the presentation. I thought it
20 was very interesting.

21 The certificated projects that were approved and
22 put in service, how does that compare to the existing
23 capacity? What kind of capacity increase, on a percentage
24 basis, have we seen since 2002?

25 MR. MOSLEY: Compared to pipeline throughput,

1 normal?

2 COMMISSIONER KELLIHER: No, if you look at the
3 universe of gas storage capacity and then you look at the 75
4 or look at the 57, what percent increase does that
5 represent?

6 MR. BAHUMIAN: I can tell you a general answer to
7 that. Last ten years, really, if you look at total working
8 at total certificated capacity -- I should say, operating
9 capacity in the United States, it's 7.6 Tcf and it has not
10 been modified, so it likely goes up and down.

11 And also -- but the return of working gas has
12 been reduced. We have in the last 30 years, certificated 77
13 storage facilities in the United States, and we have
14 abandoned 44.

15 That shows -- those two graphs, if you compare,
16 if you could see it's staying at 7.6, but the proposed
17 figure is increasing continuously, and we have a chance --
18 and another way to say it, we have extra working gas
19 potential sitting there which could be utilized by
20 horizontal well drilling, table drilling, and location of
21 wells in a probable location. All these things increase the
22 working gas capability.

23 But that does not mean we do not -- we can't --
24 we should not build any more storage facilities. Storage
25 facilities should be built in the proper location to always

1 compare the pipeline transportation, plus storage to be
2 equal to the demand we have.

3 COMMISSIONER KELLIHER: But if the concern is
4 price volatility, certain storage facilities are better than
5 others, right.

6 MR. BAHUMIAN: Definitely. At last salt cavern,
7 for example, storage facility, they can recycle ten to 12
8 times a year. That's a capability they have that's to void
9 the space. And we design it that way, we design it to be
10 used over short period.

11 But that does not mean our old storage fields are
12 not that -- don't have that capability. There are lots of
13 storage fields in the United States that are extremely
14 large, but do have the same capability, but they can
15 maintain big swing, and also they can maintain a long run.

16 And the combination of all of these just makes
17 our storage, gas storage technology working sufficiently.

18 MR. MOSLEY: We can get you a percentage number
19 on that and follow up with that. In our staff report that
20 we're going to issue, we do have information on
21 certifications, recent certifications over the last few
22 years, and also compared to the number of fields, and just
23 the general picture or snapshot over the last few years, of
24 what we've done. And that information can be derived quite
25 easily.

1 COMMISSIONER KELLIHER: Okay.

2 MR. MOSLEY: We'll get that to you.

3 COMMISSIONER KELLIHER: I know that the State of
4 the Markets Report had some numbers on storage for 2001 and
5 2002 and they looked at -- I think that in one year, it was
6 a 1.2 percent increase, and in another year, it was 0.1, so
7 it was pretty flat, and I was just wondering.

8 We have approved a number of projects, but did
9 the numbers pick up last year?

10 MR. ROBINSON: We'll give you a report on what
11 we've certificated and what's gone into production.

12 COMMISSIONER KELLIHER: Of the projects we've
13 certificated, have they tended to be -- which of the three
14 categories? Of salt cavern, aquifer, and depleted
15 reservoirs, have most of them been depleted reservoirs?

16 MR. BAHUMIAN: No. I don't think we are going to
17 see a large storage capacity like 1970s, 70 or 100 Bcf
18 capacity. The trend is going toward smaller capacity of 10
19 or less, but provide high availability, short -- low gas
20 cushion gas requirement, and also new technologies are
21 coming in that are certificated in central New York,
22 utilizing completely horizontal drilling.

23 Instead of 50 wells, we put only eight wells, but
24 those are those horizontal wells that act as a salt cavern.
25 They can cycle four to five times. That reduces the cost of

1 cushion gas and more effectively and is safer than salt
2 caverns.

3 COMMISSIONER KELLIHER: But does that mean that
4 most of the capacity being added is storage in depleted
5 reservoirs?

6 MR. BAHUMIAN: Lately we are seeing lots of salt
7 caverns.

8 COMMISSIONER KELLIHER: Okay.

9 MR. BAHUMIAN: But by new technology of
10 horizontal drilling, I think it is a change that may start
11 competing with salt caverns, because there are -- they are
12 able to provide similar storage -- I mean, availability and
13 storage capabilities as salt caverns have.

14 MR. ROBINSON: Historically, depleted reservoirs
15 has been the primary source of storage, more recently, salt
16 caverns are starting to come up, and it's -- recently, we
17 had a mixture of those different types that the Commission
18 has been working with, depending mostly upon the area that
19 they're going into and whether you have salt cavern domes
20 available, or you have depleted reservoirs that are either
21 available for expansion of existing projects or new depleted
22 reservoirs, so it's been a combination of the two.

23 COMMISSIONER KELLIHER: Thanks.

24 CHAIRMAN WOOD: Well, is there much of a
25 performance difference between the ones you label as

1 aquifers and the ones that are depleted gas? I understand
2 that salt caverns have a different aspect to them, but are
3 aquifers and depleted gas similar?

4 MR. BAHUMIAN: It depends what kind of dry
5 mechanism they have. If it's 100 percent water dried
6 aquifers, usually they have high cushion gas deployment,
7 like up to 80 percent of the requirement.

8 CHAIRMAN WOOD: In an aquifer?

9 MR. BAHUMIAN: Aquifers. But the advantage of
10 that is that they are able to sustain a high availability
11 rate, but the depleted gas field, they may have a low water
12 dry and that lower water dry may see pressure decline and
13 availability declines in a period of 150 days to withdrawal.
14 That's the difference.

15 CHAIRMAN WOOD: Okay, thanks.

16 MR. BAHUMIAN: And cushion gas in a depleted gas
17 field is a lot less, 50 percent, average.

18 COMMISSIONER KELLY: Just by your choice of
19 words, that certain regions lack infrastructure, is it fair
20 to say that you would conclude that New England could use
21 more storage infrastructure, and if so, are there
22 alternatives available, given the geologic limitations in
23 New England? Are there alternatives available that make
24 economic sense at this time?

25 MR. PINKSTON: Any region at the end of the pipe

1 that's prone to price volatility, could benefit from
2 storage. The trick, as I think you're referring to, is the
3 cost/benefit ratio.

4 It's very hard to sometimes match the costs and
5 the benefits, especially with the more expensive salt dome
6 storage. Their are public policy interests in mitigating
7 volatility, might be greater than what the market is valuing
8 the volatility mitigation.

9 But the answer is yes, more storage would reduce
10 the risk for extreme price volatility.

11 COMMISSIONER KELLY: The fact that we don't see
12 pending applications even on the horizon in New England,
13 would you conclude that that's an appropriate situation, or
14 is it something that you think needs incentives or
15 intervention?

16 MR. PINKSTON: Thus far, users probably are
17 performing calculations, looking at a very high cost for a
18 very short period, versus year'round demand charges. And
19 likely bearing the very high costs for a short period is
20 still the optimal route.

21 Now, that's assuming that energy is available at
22 some price.

23 CHAIRMAN WOOD: It's challenging in New England.
24 It's a big rock.

25 MR. ROBINSON: It has storage. It's all above-

1 ground. It's all LNG storage, and, in fact, Connecticut --
2 it's all -- I don't think that we have any jurisdictional
3 LNG above-ground storage facilities in New England. Correct
4 me if I'm wrong on that, but I think it's about 40 of them
5 up there, and, in fact, Connecticut has just authorized an
6 additional above-ground LNG storage facility to be
7 constructed.

8 I think it's about 1.2 B that they're going to
9 put in there, so there is a recognition in New England that
10 there is a need for more storage. It just doesn't come to
11 this Commission because of the jurisdictional aspects of how
12 storage is handled in New England.

13 They also use storage in New England, underground
14 storage, but it's back in Pennsylvania and New York and they
15 bring it in on the existing pipe system.

16 COMMISSIONER KELLY: To the extent that we're
17 going to use this report as suggestions for maybe incentive
18 regulation or, in other words, that it's going to signal to
19 us that we should be doing something to incent storage, will
20 you include the availability of non-jurisdictional storage
21 in the information, so that we get a full picture of the
22 storage?

23 MR. MOSLEY: We have information on non-
24 jurisdictional that we'll be able to provide in the Staff
25 report.

1 And as a followup to what Mark was saying about
2 the above-ground LNG storage in New England, there is one
3 jurisdictional plant, the Distrigas plant, but what it does
4 is, it not only regasifies and sends out the gas, but it
5 also ships LNG in tanker trucks to the above-ground
6 facilities that Mark was talking about. So, that's
7 currently how they are meeting their storage needs.

8 As mentioned in the report, it's not an exact
9 match for the type of services that typical underground
10 storage can provide.

11 CHAIRMAN WOOD: How could I forget Everett?

12 (Laughter.)

13 COMMISSIONER KELLIHER: I'm just curious as to
14 what would kind of be a benchmark to the cost of above-
15 ground LNG storage be to underground gas storage. Is it,
16 you know, ten times as much, 20? No? I'm just curious.

17 I just have one last question. The NCP and INGAA
18 estimates on the gas storage that they believe we will need
19 by 2025 and 2020, what's the bases of those estimates? Is
20 it that if we don't have 700 Bcf of new storage, we won't be
21 able to meet peak demand, or is it that we will, but there
22 will be tremendous price volatility? Do they think there is
23 physical capacity to build 700 Bcf?

24 MR. BAHUMIAN: I'll try to respond to that. The
25 700 Bcf, when I saw the number, it looks like -- first of

1 all, I didn't know if it was working gas or --

2 If it's working gas, we do have existing storage
3 fields. And that would take care of that.

4 But if you're talking about 1.4 Tcf for
5 certificated capacity, I feel like it's not a good idea.

6 Storage fields have to be recycled. If you over-
7 build a storage field and you do not recycle it, you're
8 going to have capacity expansion and gas loss, cushion gas
9 increase, and all those things are going to affect the
10 storage.

11 And it is a balanced thing. If you go back and
12 look at the graphs, you could see that they are staying
13 constant, and companies are doing a lot of work bringing the
14 capabilities, balancing demand.

15 But that does not mean we are not going to build
16 storage fields in a variety of locations, as they need it.

17 MR. PINKSTON: Just to add to what Tom's saying
18 about the balance, I think some of the modeling in these
19 projections look at the cost differential between Summer and
20 Winter, and when that differential begins to exceed, on a
21 regular basis, the cost of new construction, they will
22 estimate that new storage is needed.

23 COMMISSIONER KELLIHER: Okay, thank you, thanks
24 very much. That was very interesting. I look forward to
25 the report.

1 CHAIRMAN WOOD: Just to let the world know what
2 goes on next, because we do like to take things all the way
3 to their natural conclusion, this report, as it comes out,
4 is intended to be out in advance of what I'm announcing
5 today would be our annual Fall State of the Gas Industry
6 Conference that we've held for the last two years on October
7 21, that we're looking at for this particular issue, as we
8 did two years ago with the LNG policies and gathering
9 policies.

10 Last year it focused on the NPC's report on their
11 projections and estimates. This year, we'd like to look at
12 this issue of storage. We may add other issues later, but
13 this is our kind of core issue that we'd like to look at
14 this year, and particularly these policy options to
15 encourage development. We like to just, quite frankly, have
16 an open forum and invite folks that are looking for
17 different approaches, as well as folks who have concerns
18 about different approaches, to bring those out, as we did
19 with LNG policy.

20 I should note that two years ago, on the LNG
21 policy, we heard quite a few things about coming away from
22 the open access requirement in the comments in response to
23 that, and I think in November of 02, we didn't hear much
24 deviation from that. In fact, there was pretty large
25 support that we go there, and we actually implemented it in

1 the following month in an Order with regard to the Cameron -
2 - it was called at that time, the Hackberry Policy.

3 So these informal policy forums actually have
4 borne some fruit, pretty quick fruit, in the past, and I
5 think it's a really good solid way to have the discussions
6 and dialogue we need to make -- explore whether policies
7 need to be changed in response to the marketplace. I think
8 our nimbleness on the LNG front has served us well, and I
9 hope that the similar creativity can come out on the
10 discussions relating to storage this year.

11 MR. MOSLEY: Absolutely. One of the plans is to
12 have the report out, three weeks in advance of the
13 conference, so roughly two weeks from today.

14 And what that will do is hopefully serve as a
15 great start for talking points and discussion to better
16 inform the participants as to what we've considered, but
17 will also open the floor up, as you mentioned, to other
18 approaches, new ideas, new concepts, new policy
19 modifications, potentially.

20 CHAIRMAN WOOD: I think the plan is to put your
21 presentation from today up on the Web, so I would just call
22 attention to page 10, which named three categories of policy
23 options to encourage development and invite people to be
24 thinking about that, as well as some of the other points you
25 raise in this presentation, as well as in the more detailed

1 report. Nice job.

2 MR. MOSLEY: Thank you.

3 CHAIRMAN WOOD: When you first got here, Joe, you
4 brought this up as something you were personally interested
5 in, so thanks for the prod to kind of elevate it up on the
6 Commission's agenda, as we did in the strategic plan, and
7 now we're doing here.

8 All right, folks, nice day, welcome back. We're
9 back to work, as if we ever left, and we'll see you in three
10 weeks. We'll start the close meeting at 12:45 in the posted
11 room.

12 (Whereupon, at 11:33 a.m., the open session was
13 concluded.)

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