BEFORE THE

FEDERAL ENERGY REGULATORY COMMISSION

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MARKET DESIGN WORKSHOP WITH : Docket Numbers

STATE COMMISSIONERS ON A SINGLE : RM01-12-000

TRANSMISSION TARIFF : EX01-3-000

- -x

Hyatt Regency

Regency Room

400 New Jersey Avenue NW

Washington, DC

Sunday, February 10, 2002

The above-entitled matter came on for workshop, pursuant to notice, at 10:10 a.m.

BEFORE COMMISSIONER:

NORA MEAD BROWNELL

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ON BEHALF OF THE FEDERAL ENERGY REGULATORY COMMISSION:

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PANELISTS:

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THE HONORABLE MARSHA SMITH, IDAHO

THE HONORABLE DAVID SVANDA, MICHIGAN

THE HONORABLE SANDY HOCHSTETTER, ARKANSAS

THE HONORABLE BRAULIO BAEZ, FLORIDA

P R O C E E D I N G S

THE HONORABLE BROWNELL: Thank you very much. Thanks for being here this morning. Kevin Kelly assures me God is giving extra brownie points for those of you solving these important issues and gives you a pass this morning from church.

I'm going to ask Bill Nugent, our distinguished leader and close friend and great thinker, and a good pathfinder if you find yourself in a foreign country lost, to open it up.

Bill?

THE HONORABLE NUGENT: Thank you, Commissioner Brownell. For the business at hand, my state colleagues, both here and on the platform and in the room, are delighted to welcome the members, you and your colleagues and staff here at the winter meetings. We very much appreciate your willingness to meet with us while we're here in Washington and to continue our search for the best way to develop wholesale power markets that work for the power customers that we're both dedicated to serve.

State commissions, regardless of their views on how wholesale markets ought to be organized, wholeheartedly welcome the Commission's effort to work with the state officials, both the Commissioners in this room, those who are not here, the governors, and the

legislators on these issues, and we're also delighted to remark that you've brought District of Columbia Commissioner Ed Meyers on board to manage the liaison activities. We've worked with Ed for as long as I've been in this business, which is 11 years now, and know him to be knowledgeable and very thoughtful and judicious in his recommendations. We think that's a very positive addition to this mix.

Just as I had the honor of kicking off the state commissioner panel in October during RTO week, as you know, I have the honor to lead this discussion. In October I noted that state commissioners' opinions varied widely on RTO scope, formation, operation, governance, and other issues based on geography, demographics, history, and economics. Similarly, a diverse range of opinion exists on transmission tariff issues.

For example, the Commission surely knows a number of states have asked the Supreme Court to decide whether FERC or the States have the legal authority to regulate transmission services provided to retail consumers on a bundled or unbundled basis. Accordingly, those states likely would oppose broadening the FERC jurisdiction to cover transmission services provided to retail customers. Other state commissions may be more receptive to a single tariff policy where FERC regulates

all transmission services, wholesale and retail, under a single nondiscriminatory tariff. This may, or may not, be the case in states that have implemented retail choice programs, which are already subject to your jurisdiction under the open access transmission tariff. But even these state commissions likely will want to ensure that they have a continuing role in deciding how the Commission implements its policy, either individually or regionally.

Moreover, yet another group of states that support the development of large, transparent, and seamless regional bulk power markets but are unwilling to pursue retail competition for the foreseeable future can be expected to ask precisely how a single-tariff policy at FERC would work in situations where a state chooses to rebundle retail services through a single service provider. A lot of people take a careful second look at what's going on here.

Clearly, these and other questions of real world workability must be resolved, particularly if the Supreme Court's impending decision affirms or expands your authority over retail transmission services. In its white paper, the FERC Staff has raised many of the right questions. I expect that the other issues will be raised this morning, and in comments as the Commission's market design Giga-NOPR proceeds.

It seems to me, as Maine's commissioner, that a nationwide single tariff is inadvisable until underlying state policies and retail structures in each of the regions are much more similar. In Maine the integrated systems are largely characterized by structured retail regimes. Now, clearly, the Southeast and the West are vastly different, different not only from the Northeast but also from each other. Imposing an identical single tariff structure in all three instances is likely to have differing results and not necessarily desirable.

The Maine commission supports the single Commission tariff and New England has almost achieved it, but only with great difficulty. There are certainly flaws that occur in a national system. It's okay to begin a transition. It's better before you get them all worked out, but it's important for market stability that the Commission not move too quickly or too precipitously. The imposition of a single tariff as proposed will affect different models in different ways, as I've already suggested.

The FERC Staff position paper's oft-repeated "all load is somebody's native load" is not quite correct in Maine and only somewhat correct in the rest of New England, for example, where retail choice has been adopted by all states but Vermont. We actively encourage

competitive providers in the New England region, and in adjacent areas, for that matter -- I'm thinking here of Atlantic Canada -- to serve loads in New England. Competitive providers will only do so if they perceive it to be in their economic interest, no surprise there. They're not required to serve the loads in Maine and therefore are only asked voluntarily and for a limited time to take on that load obligation under contract.

Maine has taken the concept further by removing the utilities from the business of energy services. As you know, we even bid out the opportunity to serve as a provider of last resorts. It seems to me that all loads should have the same rights, only if they're willing to pay for the consequences of their behavior. If they impose additional burdens on the system, perhaps they should pay for those consequences.

Now, the problem becomes one of determining what are new obligations and new burdens on the system. Is it a new customer on the system or is it growth in a particular service area, and these both may produce similar effects. The question is how do you accommodate that.

In a vertically integrated, fully bundled, single control area utility system, the costs of any transmission congestion that occurs within the system are

fully internalized within the vertically integrated structure. The utility has an incentive and presumably works to minimize these costs. When a competitive generator locates in such a service territory, intending to sell to customers elsewhere, outside of that service territory, the competitive generator may increase the level of congestion that occurs there. These costs should not be allowed to escape the calculus of the parties to the new transaction; that is, these externally imposed costs or these newly imposed costs should not be imposed on the customers in the vertically integrated utility, which has already fully calculated the cost burdens on its existing customers. It seems to me it's a mistake to believe that any load must be permitted to choose any generation facility.

Conditions on the transmission system, such as forced or scheduled transmission and generation outage, loads, and weather, can and do change the patterns of flows across the system. They change from moment to moment, hour to hour. Under these circumstances, the chosen generator may run either more or less than necessary to supply a designated load. Somebody booked to serve a 50-megawatt load which may be at a moment in time, 52 or 48 or whatever, the system is helping support that circumstance.

Generation mix and congestion vary over time. Load varies independently of contracted supply. As the position paper notes, there must be mechanisms within the tariff to reflect these changes.

Don't focus too much on price. The position paper assumes that the price of electricity is all that matters. Yet, I believe it's still legitimate and important to many state legislatures and commissions to adopt and seek to achieve other policies, such as generation portfolio diversity, seeking to hedge against over-dependence on any single fuel source.

Does it make sense to maintain the dual jurisdiction transmission model that currently exists? Yes. There are still many state jurisdictions in this country that want to maintain oversight of the total cost of providing electricity to their consumers. The dual tariff model appears to be the best way at this time to maintain that oversight while also allowing for some increase in wholesale market activity. The benefits to the model are that it allows states to continue such activities as integrated resource planning, or even try things like environmental dispatch, while, at the same time, internalizing any associated costs within the bundle of customers who are being served.

The continuing weakness, of course, is that

even within this system, there's a temptation to pass costs on to neighbors, and there are probably a number of existing contracts within the current system that are imposing their external costs on other systems.

Now, it's somewhat of an extreme likelihood, but suppose we had Maine buying electricity from Mississippi. Let's say we want to buy some. That's going to create parallel path flows, congestion. Should we pay the costs? Should they be socialized? Should the people of Mississippi pay? Should we all? How do you work that out? Where the proper burdens are for an arrangement like that. What are the options for managing the transition to a single tariff system? It takes time. Grandfather contracts from distant suppliers; when they're concluded, buy from the market. Identify benefits in excess of costs and, for a transitional period, negotiate a means of distributing the benefits so as to buy down higher-cost utilities' excess costs.

We have a situation in New England as we move toward a single New England-wide tariff where you have some people who have -- one utility is adjacent with a $35 per kilowatt-year transmission requirement and adjacent to one with a $16. Do you have a single uniform tariff for people in adjacent regions collecting dollars to pay for someone nearby whose costs are seemingly much higher? We

began that transition years ago in New England, right after the 1992 EPAct. Years of negotiation were required, and only now are we in the middle of a transition from a license plate to a postage stamp regional network rate.

An RTO in itself does not guarantee that the transition will occur as a matter of course. The revenue requirements of transmission providers can vary dramatically, as I've just said. It may be illegal to lump them together by a simple edict, and in our experience, in New England, it's hard to lump them together by negotiation.

Existing contracts must be allowed to continue but not to be extended indefinitely. Such contracts often impose external costs on others. Once a contract with a load generator ends, for example, the consumer should either be forced to pay for any congestion associated with that old contract upon renewal, or turned loose to rely on the market.

There's no such thing as firm transmission service to any single source in a diverse system. It seems to me more of a contract writer's fiction. Imbalances always occur and what's most important is to minimize their level to make sure the parties to the transaction bear both the cost and the benefits of any imbalances. This means that making sure that consumers in

vertically integrated bundled service utility environments pay their own congestion costs, and making sure that in other areas, locational pricing and financial congestion rights are made available for market participants to understand and accommodate hedging against the costs.

The latter parts of the comments were mine. So I thank you for your willingness to listen to me and my colleagues here on the panel, and ultimately others as they choose to speak later on, and look forward to the discussion and learning from others.

Thank you.

THE HONORABLE BROWNELL: Thank you, Bill. We're glad to be here, and we appreciate your approach to offering not only your thoughts, but solutions. I'd like to step back a moment to talk about why we're here and what we hope to accomplish, and just a little bit about how the process works. This discussion today is part of an extension of RTO week. We're now into RTO season. We found, in fact, that the discussions in RTO week really allowed us to focus in a way that we had not focused before on very specific issues and on very specific solutions.

We want to engage as many people as we can. We say the smart people don't reside at 888 First Street -- most, but not all -- and leverage both the experience from

the business experience and the state public policymakers' community and other resources to make sure that in a new way we're really working together toward those solutions.

So in the last week we had three days of hearings on a wide variety of topics, energy markets and operating reserves, market monitoring and transmission rights and financial rights and different topics where we were very focused and very specific and very disciplined in the discussion, and we came away with a number of ideas that will inform the development of the Giga-NOPR.

Consequently, we're here today and tomorrow to drill down on some issues that we think really affect all of us. This may be -- it may be the most difficult issue that we have to face in the transition to the new world that will bring benefit to all of our consumers, and I don't think any of us pretend to have a magic answer, but what we do ask of everyone is to really focus in not simply on the history and why we shouldn't change, but how we make these transitions and what ideas you have for facilitating that.

It's also part of an ongoing effort, as you know, to continue to work with the states. The regional panels, in our mind, were just the beginning. We hope to be creative, and we hope to be very committed to the outreach. Consequently, the new office headed by Ed

Meyers, which will be supported by regional representatives throughout the country, who largely come from state commissions so we get that state perspective, but I think there is no limit to the ways in which we can work together.

I said the other day that when we transform markets, we're transforming ourselves. We may not have the organizational institutions in place to do that that are codified in the brave new world, and maybe we're not ready for that. But it is time, I think, that we all look for opportunities to work together in different ways to fulfill that perhaps organizational vacuum.

So with that in mind, our goal is to get informed to open the debate, to get specific. The process works in this way. The panel members will open with beginning remarks, as Bill did, throw out some ideas, respond to the white paper that we developed, and I'll read a little bit from that. Then we're going to ask our fellow state commissioners who are not on the dais to share with us their thoughts. And then the FERC Staff, some of whom are up here and some of whom are in the audience, will ask questions, and then we'll throw out to all of the audience members to ask a question.

I'd like to introduce our staff, Ed Murrell, Kevin Kelly, Shelton Cannon, Alice Fernandez, Alison

Silverstein. We're joined with Dennis Bergeron from Maine, and we appreciate his participation.

If the other FERC Staff members in the audience would stand so if you want to grab them, they will be here throughout the week at any time so you know their faces. Why don't we go around and everyone give their name.

(Various individuals identified.)COMMISSIONER BROWNELL: Thank you. So be sure and bend their ear if you want to talk about FERC, and they're certainly looking for good ideas as well. I think this morning we'll start with Marsha, following with Bill, and we'll move over to Braulio and Sandy and Dave and then ask our colleagues in the front row for comments, if they want to add, and we'll throw it open for dialogue.

I know that the coffee break is going on now. If anybody's dying, you can sneak out very quietly, because we're not going to take a break until noon. There's too much to accomplish.

I think as we all know, one of the difficulties that we have in moving forward is there are fundamentally two sets of rules governing transformation of electric energy to state customers. Chuck pointed out to me that the court may decide this for us, but until and unless the court decides this for us, I think we need to move forward and come up with some answers for ourselves. We need to

really identify, get the diagnostics of what the results of the conflicting regulation are.

I think we understand that each public utility system was designed to serve and protect its own native load, and that's clearly an important first priority, but we are in a transition period. We are seeing new technologies, both information technologies, generating technologies, and transmission technologies that allow us to conduct our business in different ways.

So how do we respond to the public policy forum to make sure that we're leveraging all the new assets and gaining the efficiencies and the opportunities that we see in restructured markets? We've asked a series of questions. There are probably many more questions that could be asked, but we've asked the panelists to respond to those. If you have not seen our Staff white paper, it's one of many that lays out some of the issues as we see them, and I would encourage you, both in this white paper and the others that are up on our Web site, to give us your thoughts on the variety of issues that we discuss.

So with that, my esteemed colleague, Marsha Smith.

THE HONORABLE SMITH: Thank you, Commissioner Brownell. I'm very, very pleased to be here. It is kind of humbling to go after President Nugent. When Alison

called me and asked me to do this a few days ago, I got the message of what I'm supposed to do here today, and what I'm supposed to do, as I understood it, although she may not have said it in these exact words, was to create controversy and to stimulate discussion by throwing out fairly exclusive ideas.

I would say that President Nugent has said some of the things I intended to but in a much more eloquent and diplomatic manner. Of course, that won't stop me from making two points. My first one is that I have to disagree fundamentally with the premise of this paper which Bill mentioned, which is something like everybody is somebody's native load. Well, you know, I'd really love to hear Bill Steinmeyer sing that, and if he were here, we could ask him to do that, and it would be very enjoyable. But it doesn't apply actually to the situation, the issues that we're trying to resolve, and let me try and explain that, what I mean.

Merchant generators and marketers do not have native load. Now, they do have contracts, and I don't want to, you know, make those seem less important than they are, because they are very important. However, I maintain that they are not qualitatively the same as the governmentally imposed obligation to serve in a manner that -- in the particular groups of customers, to serve

particular groups of customers in a manner that provides reliable, safe, and cost-based energy service to customers.

So in states that have chosen not to do retail access, that's very clear, but I have noticed that even in states that have chosen to do retail access -- in the West we always look to our neighbor to the south, who shall remain nameless but is a large state that has an economy of 1/6 of -- whatever. Anyway, even in those states, it seemed to me that the scheme left someone on the hook for providing the energy when the customers flipped on the switch. If you disagree with that, I think you ought to talk to someone at Pacific Gas & Electric.

So that is my first fundamental point which I hope creates discussion among the FERC Staff members and among the Commissioners.

I did want to ask a question back because I didn't understand on page 2 of the paper, under the first paragraph in the options, what it meant when it said that the lowest-cost generators may no longer be proximate to the load they serve. Were they ever? I don't understand. So maybe I'm missing an important point here that could dramatically alter my position, but I don't think so.

THE HONORABLE BROWNELL: Do you want an answer to that question? I think the Staff would like to

respond.

THE HONORABLE SMITH: Sure.

MR. CANNON: I think the only point we're trying to put forth here is traditionally the way systems were planned, they were planned on a somewhat local basis. Traditionally, the way utilities plan their system, you've got distribution, transmission, generation, planned and peak load in a fairly small area. As we've seen competition start to flourish, we've seen those markets get larger and larger. So we're seeing, you know, generation coming in from much more remote areas. We're seeing lots of stresses put on the transmission system that I don't think were independent, and it's made us really sort of rethink how the transmission system's getting used.

So I do think that if you were to trend it out, that it's a lot more long-distance trades going on now than there were in the past.

THE HONORABLE SMITH: And that may very well be true in some areas of the country. I guess I just point out that in the Northwest, with our hydro system, there's always been a pool that has tried to do the most economic dispatch of all the generation in a region, and sometimes when you want to do that, it takes transmission, and because of the cycles and the changes in load, hourly,

need -- demand, I guess, would be the better word, and seasonal, you don't always know where the lowest-cost generation's going to come from. So to do that economic dispatch, you need transmission.

So you've got to be very careful when you're talking about changing how you're doing that so that you don't actually impair the ability to do dispatch of generation on that basis. I think we've seen the same thing. What we've seen is an increase in the transactions that people want to have occur over the system.

Okay. Second point, Commissioner Brownell said how to make the transition, and I have the answer: RTOs. It's an initiative that FERC, I hope, is still actively engaged in and involved in and interested in, and my point with regard to this is that -- I don't know how it is in other regions, but I assume it's the same as in the West. A large number of people are working very hard, long hours to labor over a number of really tough issues to try and put together these organizations that will operate the transmission grid in an independent way according to how FERC would like to see it.

And I've got to say, we agree with a number of things. For example, on page 3, when it talks about OASIS and available capacity, I don't think anyone disagrees that it needs to be calculated directly by an independent

entity. That's an important fundamental principle.

But our resources are stretched. We're in tight economic times, and states, I think the resources are stretched. I think the industry is. I think the competitors, the marketers and generators who want to participate in this are sometimes frustrated because they can't cover all the bases.

And my point is, that it's really kind of counterproductive to keep lobbying what I see as shells into that process with papers like this, which distracts the people from the work they're doing, which, in part, is to answer the question of how do you want to do your transmission tariff? How do you take a region where there's a nine times or greater difference in the prices of the transmission owning and operating utilities and put it into one tariff in a way that can accommodate the state and local concerns. And they're working on that, and they're going to come to you with a proposal, and it doesn't really help in the middle of all this to throw in a paper that distracts everybody and, quite frankly, maybe scares them to death and just slows things down.

So I guess work hard on what we're working hard on, which is the RTOs and getting these difficult questions worked through on a regional basis, which I really appreciate Commissioner Nugent's point about I

think that's the way you get the transition. I think you have to start with what works on a regional basis and grow it.

I will answer a couple of questions. On page 2 where it says can any preference be granted for the transmission of electric energy without unduly discriminating against someone else? The answer is yes. I just point out, this transmission was built, paid for to serve customers, and I think they're entitled to know that it's there when they need to use it.

So I think I've done what I'm supposed to. Is that good enough, Alison?

MS. SILVERSTEIN: Absolutely.

THE HONORABLE SMITH: So thank you for the opportunity to hopefully create a little controversy and raise issues.

THE HONORABLE BROWNELL: Thanks, Marsha. It's an interesting thought, perhaps that I think was implicit in your comments, that we're overconsulting. My how far we've come.

THE HONORABLE SMITH: Commissioner Brownell, I don't think you're overconsulting. What I think is happening is people are working hard on these issues, and they're working toward resolutions, and then all of a sudden they're distracted by something else that causes

them to have to run off -- it's like a new little fire they have to run off and put out, but I don't think you're overconsulting, and I do appreciate the fact that you are consulting.

THE HONORABLE BROWNELL: Commissioner Baez -- and I want to note, Commissioner Baez has a proceeding before him that limits him to some broad but well-informed remarks. So in the question and answer period, we need to respect that, and we do.

THE HONORABLE BAEZ: Thank you, Commissioner Brownell. I just wanted to say, since Commissioner Smith said that her purpose of being up here is to perhaps create controversy, given your comments and the realities that I'm facing at home right now, I guess my purpose is to create as little controversy as possible.

I want to thank you for inviting Florida up on the dais and to make some comments, and I would like to remind everyone that these comments are my own and they don't reflect -- perhaps they don't reflect those of the rest of my colleagues on the Florida Commission.

We do have open dockets on these and many other issues concerning RTO. I think, to my knowledge, we may be the only state, I think in the Southeast there may be one other state, if I'm not mistaken -- the representatives of North Carolina can correct me -- they

also did have some dockets on the matter, and we've decided to try and tackle some of these important issues ourselves for the time being, given our particular geographic limitations or benefits and try to address it that way, and therefore, the reason for our open dockets.

We're hoping they might culminate into some type of fortifying with the FERC -- in fact, we're confident that that will happen -- the single transmission pricing model being discussed as a necessary step to further wholesale competition. However, in going back to something President Nugent said, not all the states or regions are at the same point in moving towards retail choice on limited services or even toward a more robust competitive wholesale market, and I would just -- that plays into one point that I'd like to make, that you mentioned transition, Commissioner Brownell, and Commissioner Smith also took up on that.

I think there are many transitions going on, many similar transitions, all of them moving at different paces, and I think we need to keep that in mind. It seems to me that these developmental differences require caution, as I said, before we move to any type of "one size fits all" pricing model. That's a notion that certainly Florida has tried to put out there time and time again. Many areas of the country with generation

transmission distribution continue to be bundled retail services, and as has been mentioned, company utilities have that final obligation to serve. In some areas it's truly a partially unbundled transmission, but there are a few areas that have completely separate of the three, generation, transmission, and distribution.

So in most places, native load is still retail load with an obligation to serve by a state regulator, integrated utility. If we accept this premise, then we have to look to legal precedent and look at the real question that we're trying to answer, and that is, do native load customers have a superior call on transmission services for the reason that these systems have been supported and paid through rates by these retail customers? And for one, I hope to have a better sense of the answers to that question after all this panel discussion is over, and certainly I'm sure will continue.

I do, however, believe that there is a lot of areas where there's agreement or agreement can be reached. The first is the calculation of TTC, total transfer capacity, and available transfer capacity, which has to be done more accurately and without giving advantage to any particular market participant.

The second, and I want to stress this second one because I think in terms of my personal conversations

and conversations of other colleague commissioners on the Florida Commission, with Chairman Wood, in particular, he stressed this factor as being important, and I happen to agree with him, that the communication protocols to share the transmission information, they do need to be standardized on some level. I believe I've heard him say that, you know, none of this is a done deal and certain markets or structures are going to look different in different regions and so on. But the way we communicate, I think, has to be of a fair amount of importance, and I happen to agree with that.

Lastly, the costs of incremental transmission services, those interconnections, system operations, et cetera, should, to the extent possible, be assigned to those requesting such services, and I know, speaking for my region, that's something that we've -- that's a feeling that we've communicated, not just to FERC but to our national association as well, and I suspect we may have some conversation along those lines in the days to come at the meeting.

It's my feeling that we should proceed with caution and deliberation before we impose a totally new pricing model that may not be appropriate for all states and regions, given their different developmental stages. In many cases, transitions or phase-in periods would be

appropriate and might even be required to match that speed at which generation and transmission are unbundled.

And we also shouldn't forget that many of the transmission lines in the country were built first to improve reliability by connecting power plants to their load centers, but that their primary function was not to promote both power transfers between utility areas. I keep thinking I can strap a mattress on top of my car. It doesn't make my car a pick-up truck. We have to keep that in mind, and our challenge today is to keep both functions in mind, and explore these options and change our historical transmission allocation of pricing.

I want to thank you all for having me.

THE HONORABLE BROWNELL: Thank you. When I hear the pick-up truck description, I think you've been spending too much time with our chairman.

Now we're going to hear from Sandy Hochstetter from Arkansas.

THE HONORABLE HOCHSTETTER: Thank you, Commissioner Brownell. On behalf of the state of Arkansas, we appreciate the opportunity to be on the panel here this morning. The focus that I'd like to bring for my comments here today is to first define what our future objectives are in comparison with our current reality, and then identify some of the economic issues that are

creating the gap between the two.

First of all, let me share you with my own starting point. As chairman of the Arkansas Public Service Commission, I represent a state with relatively small population, quite rural, based on a 20 percent poverty level and challenged with one of the lowest educational and economic levels in the United States. Many in the South share the same circumstances.

I have to focus on the practical realities and consequences of any increase in costs to our state, rather than on economic theory or academic speculation. My responsibility, which I believe I share with other state regulators, is to insist on quantifiable cost/benefit analysis and ascertaining realistic cost consequences. Accordingly, my suggested approach on this topic and related issues is for us to do two things. First of all, develop realistically attainable goals, and secondly, ensure that we provide economic fairness to customers in the process.

Along those lines, I think it's reasonable to envision and develop a competitive wholesale electricity market that can provide efficient and reasonably priced electric energy to either reselling utilities or to end-use customers. Such a wholesale market can be used to provide incremental generation requirements on a

competitive RFP basis, even in states like ours that may decide not to deregulate existing generation assets. Wholesale competition can and should exist independently of retail competition. It has done so in most states in the natural gas industry for many years, and it can do so as well in electric markets.

With that said, the next step is obviously the transmission service needed to transmit that wholesale power to utility distribution systems. I think it is reasonable to envision an open and nondiscriminatory transmission system that serves both retail and wholesale loads on an equal access basis, just like we have in the natural gas industry. Separating generation from transmission, as in Orders 436 and 636 in the gas industry, will be necessary to achieve that goal.

However, this vision goes to physical access in a legally nondiscriminatory manner. It speaks to having one set of general terms and conditions for both retail and wholesale transmission service, but it does not necessarily require one price for all. If economic fairness is one of the public policy objectives that we want to achieve, economic fairness requires us to focus on current reality, which consists of some of the following facts.

First of all, as has been noted previously

today, the existing transmission systems were primarily designed and built to deliver specific generation output to location-specific customers. There was a matching principle used between generation and transmission, and costs were allocated to customers accordingly. The costs of these existing transmission systems have been paid for by existing customers over many years. The transmission systems were designed to handle utility system needs as opposed to regional needs.

Most of the country still operates in this fashion, with dedicated rate-based generation being delivered to specific customers over specific transmission assets. It's the minority of electric flows that take place either in a wholesale market or a retail competition market, and the reality of how these existing systems are used today will likely remain reality for the foreseeable future. It may well be a long time before the incremental generation requirements supplied by the wholesale market, in combination with a small percentage of retail competition transactions, eventually overtake and supplant the amount of rate-based generation flowing to customers over current transmission systems which are already being paid for.

So, with these economic realities in mind, how do we construct a different transmission regulation

regime? Do we want to make a modified transformation or perform radical surgery, because we are, after all, talking about a minority of electrons flowing in either wholesale or retail competition commerce. If we keep economic fairness as a public policy objective we want to achieve, then the answers may well lie in design and the associated cost of the new transmission configuration.

Here are some questions. If the transmission system must be designed to enable any generation, no matter where its location, to reach any customer, regardless of location, as opposed to economically matching generation with the load, how much is this going to cost? How much overcapacity and transmission service could we possibly have? What kind of cost shifting or increased costs would we have in each state due to averaging the RTO build-out costs across each state in the RTO? Can customers in these states absorb these cost increases? Will the new wholesale transmission capacity be built in incentive rates? How high and what's that going to cost?

Until we have the answers to these and other questions, I don't believe it's prudent to accept without question the notion that one transmission rate should apply for all transmission transactions within an RTO. What we may need to explore is the concept of one set of

transmission general terms and conditions that apply to all on a nondiscriminatory basis, but within that context, utilize a cost allocation and rate design matrix that recognizes the historic cost contributions that ratepayers have already made to existing transmission assets and that will likely continue to be used to deliver the same rate mix generation to supply the majority of their needs for the foreseeable future.

We need to create a tariff that will follow the economic principle of matching equity investment of cost with associated price and benefits. As the asset mix of a system changes over time, we can change the cost allocation and pricing design as well.

This is not a retail versus wholesale split proposal. It's actually an asset allocation split or a rate split based on the history of the users or the beneficiaries of the assets. It's a concept that encompasses gradualism as opposed to a flash cut to accommodate economic fairness. This is just a potential starting point for discussion and analysis, and I know it will require a lot more thought to reach the right answers, and I appreciate your hearing our thoughts today. Thank you.

THE HONORABLE BROWNELL: Thank you, very thoughtful. And last but not least, the distinguished

Dave Svanda.

THE HONORABLE SVANDA: Thank you very much, Commissioner, and let me echo the accolades of all the other speakers in terms of your staff being here today in helping us to kick off this NOPR meeting.

You have asked us to consider and give our views on whether all wholesale and retail transmission services should be under the same rates, terms, and conditions. I think that for regional, wholesale, and, for that matter, statewide retail electricity markets to flourish, the answer has to be largely yes. For those interested in markets, seamlessness means that the rules of the road should be similar, if not the same, for all participants. Although there may be instances where there are legitimate reasons for differences between wholesale and retail rates, terms, and conditions, market participants need consistency in order to function.

Our bifurcated regulatory system creates mutually beneficial opportunities for constructive change, but they can also magnify differences, creating market-stifling roadblocks. In light of this possibility, does it make sense to maintain the dual jurisdiction transmission model? I think, and I think others have already expressed this, that the answer is yes. We must, however, work together to eliminate barriers of market

development -- and we've already heard considerable agreement in this regard -- while preserving the positive aspects of the federal and state regulatory system.

In October of last year I had the privilege to address the entire Commission on behalf of the Midwest commissioners, and I, for one, am gratified that as a continuation you have moved into the season of RTO and that you continue to seek out our opinions and impressions and to better understand what it is we all bring to the table.

Also on behalf of that same group of colleagues from the Heartland, I guess I'd like to take the opportunity to thank the Commission -- and please pass along to your colleagues -- for your December 2001 orders, which provided some really welcomed clarity for the Midwest RTO/ISO confusion in the Midwest. The orders really provided a giant step toward solving the scope and configuration problems that threaten wholesale electric markets in our region.

Back to the particular point at hand here. Almost two years ago, Michigan's legislature enacted a customer choice and reliability act to, among other things, ensure that all retail customers in our state have a choice of electric suppliers. The statute required the Commission to establish rates, terms, and conditions of

service to allow customers the opportunity to select alternative electric suppliers by the beginning of this year, which we have done.

Michigan's plan is not to require customers to leave federal service but recognizes the need to unbundle distribution services so as not to tilt the playing field in favor of either the incumbent or alternative electric suppliers. Competitive fairness demands this.

For the most part, all end users must have transmission assets at the same rates, terms, and conditions afforded to bundled customers, all things being equal. We do recognize that all things are not always equal and that there needs to be accommodation. For example, in Michigan, at least one of our transmission owners filed an open access tariff with you that would grandfather lower rates to existing customers of its affiliate and increase the rates for new retail direct access customers up to 72 percent.

Supposedly, this arrangement protected native load. It also created an advantage for the incumbent, which is not acceptable for retail or the wholesale level if we are to see markets develop. Besides, as noted by the FERC Staff -- and I may be on a different page than some of the other speakers in this regard -- although it is someone's native load, and I believe that all load is

someone's native load.

Needless to say, when we see proposals that conflict with our state goals and, in fact, undermine those state goals, we need to let you know. In my opinion, it is our responsibility to point out those areas of conflict that prevent us from developing our own market as we see fit in our state, and hopefully, it's your responsibility to continue to listen and to react to the concerns that we raise.

As I noted earlier, in order to successfully implement our retail choice program, there may be rates, terms, and conditions that should not be the same at the wholesale and retail level. Energy imbalance charges come to mind where individual retail loads are less predictable than wholesale loads. There's a valid argument that the threshold for imbalance charges should be broader for retail than for wholesale.

Some have argued that these excessive imbalance charges triggered by too narrow a range will discourage customers from taking retail choice. We have to work that out. As we move forward, it's likely that we will discover other terms, conditions that should be able to accommodate the developing markets in each of our jurisdictions.

What is the best way to get your attention? We

need to know that. In the past, we could require the interstate transmission provider to request a waiver or tariff change at the FERC. This, however, takes considerable time, and time is not the ally of the competitor. It's not the ally of developing a competitive marketplace. So we need to address how to communicate those issues and get them resolved timely.

Michigan's legislature decided that our residents deserve benefits of competition and customer choice. They could have decided, as other legislatures have, to stick to traditional bundled utility service and avoid the great new world of retail competition. If they had, in my mind, the question of wholesale and retail rates, terms, and conditions for transmission would be a largely academic exercise. States implementing retail choice programs, however, need to be increasingly sensitive to federal transmission decisions that could impact our programs or, as I mentioned, undermine them.

The ability of the states to act locally and provide feedback to the FERC will be increasingly crucial, and Michigan, for one state, will be filling in that information void for you.

How do we make the dual jurisdictional model work? I believe state commissions are still the best monitor. Whether the state adopts the choice program or

not, state commissions are much closer to the customer and will continue to be the eyes and ears that you will need to assess the efficacy of your national and regional policy decisions. Furthermore, as we move to single transmission tariffs -- tariff approaches, states must be afforded some special deference by the FERC with or without an intervening RTO. This unique status is based on individual state statutory authority, which in Michigan requires us, the Commission, to ensure that all persons in our state are afforded safe, reliable electric power at a reasonable rate.

In regionally certifying an RTO, transition to a single transmission tariff approach should be the goal with significant guidance from state commissions. If an RTO moves forward with a proposal without state support, that proposal should be subjected to your most intense scrutiny.

Many of the concerns regarding native load and firm transmission service will be alleviated by well-functioning RTOs. RTOs should make no distinction as to whether the load served is a bundled service or is a direct retail access service. Firm transmission service should be provided to both under the same rate, terms, and conditions.

As I stated earlier, Michigan's customer choice

program allowed both direct access and bundled service. In most cases, a single tariff federal model would have little, if any, impact on our regulatory responsibility, as long as there is no unfair discrimination based on the type of load served. We must be vigilant at the state and the federal level to detect and disarm rates, terms, and conditions that tilt the table one way or another.

New transmission investment should be the responsibility of the RTO through its FERC-approved government process. States must be fully engaged in this process and accorded deference that recognizes our statutory responsibility. Subsequent prudence reviews of transmission investment is ultimately a FERC responsibility. However, I would suggest an enhanced process modeled on Section 271 of the Federal Telecommunications Act, which requires the FCC to consult with states prior to allowing a unilateral market. This approach might offer an opportunity for the affected state commission to perform initial prudence reviews and to advise the FERC of its findings in individual circumstances. Where a project is interstate in nature, a Section 209 joint board approach could also be considered.

We anticipate additional concerns may still require this more formal arrangement and continue to encourage you to consider the formation of joint boards.

Specifically, joint boards might be established related to interstate transmission siting as well as other specific retail competition issues.

The success of any model of cooperation coordination adopted depends in large part on the deference the ultimate decisionmaker gives to the advice forthcoming. Today, we've been pleased with the deference this Commission, the FERC, has shown to the Midwest states and hope it continues. As I said last October, we promise to work very hard with you and have to work today to ensure a highly reliable and vibrant, competitively neutral regional market. A single transmission tariff model will help us along this path. I think that will be a benefit to customers in states that embrace both retail customer choice as well as those that have not.

Thank you.

THE HONORABLE BROWNELL: Thank you, David. As always, lots of thoughts for us to go home and contemplate and respond to. One of the things that we had during the sessions regarding this is often we're not always clear about definitional issues. Indeed, several of the panelists last week said we need a glossary, which I assume somebody's home working on. Shelton pointed out that we may need to have a clarification here, and I'm going to ask him to do that. It may not be needed, but

just in the interest of good communication before we turn it over to the other commissioners, I'm going to ask him to do that for us.

MR. CANNON: I'm worried a little bit when we start talking about the single tariff, that people look at that and say oh, that means a single rate for everybody. I'm really drawn, I think, to the distinction that Chairman Hochstetter made of trying to marry up the past with the future. In terms of what we've been trying to propose in this white paper and, indeed, I think precedence sort of bears this out, we've been very concerned about cost shifting and to be sure that any movement to RTO does not result in, you know, one state being a huge winner and another state being a huge loser. And that's been particularly a concern in terms of the existing transmission which native load ratepayers have, indeed, paid for, and we've tried very hard to send signal after signal that we're willing to look at license plate-type proposals that sort of preserve the value, if you will, or the native load customers who have indeed paid for that system so we don't get into those kinds of cost shifting issues.

Looking forward, as we start moving into, you know, transmission expansions that may be undertaken to benefit the entire region, as we start looking at

congestion management and how that should be priced, those kinds of issues, I think, we do need to step back and make sure that we don't unintentionally wind up having one set of customers subsidize another, and I think there is a real need for consistency in terms of how we look at expansion decisions, how we look at pricing associated with expansion decisions, and in particular, in the shorter term, how we look at pricing associated with congestion management.

THE HONORABLE BROWNELL: Thanks, Shelton. Before we turn to our colleagues, I want to thank President Nugent for joining us this morning. He has, as I can personally testify, a president's agenda that is very full and has other commitments, but we thank you for participating and kicking us off.

THE HONORABLE NUGENT: Thanks for coming, Nora, and thanks to you and your colleagues for the openness you've shown to the state commissioners.

THE HONORABLE BROWNELL: Thank you. Do any of my colleagues from the state -- yes?

THE HONORABLE ARTHUR: Glenn Arthur from Connecticut. During the discussion this morning, several thoughts came through my mind, and I wondered if you had looked at them. The chairman from Arkansas brought up the point before, should their state pay for what looks like

will be necessary to get generation capabilities from the south up to the north. And being a high-cost state, I'm just wondering if a single transmission rate is not going to add up to such a point of add-on that will, in fact, not make rates any cheaper in New England. I.e., if some of that generation in the south -- and we're also looking at Nova Scotia, but if, in fact, it's built down there and we have to pay for those transmission costs, are we going to have cheaper electricity? And that applies to all states.

And just as the states with low generation costs currently are concerned about unbundling because -- we're looking at that now with New York. We're going to be paying more. New York's going to be paying less. That's a simple equation that we're looking at. So what are we gaining by doing it? PJM may be a better deal for us because there's some low-cost power in PJM. But if, in fact, we go together with New York, PJM's cost analysis tells us it's going to cost the Northeast state -- the six Northeast states money. We're not going to gain.

So my question is, should a single transmission tariff be more important than requiring new generation be located close to load? If you're going to legislate or mandate that we have a single transmission tariff, is that -- why not take the bull by the horns and say hey,

you can only build generation where there's load, instead of forcing everybody into a single transmission. And perhaps that will solve some of the transmission problem.

The second comment I had was just as in gas, where in Connecticut we pay three zones' worth of transmission rates, so gas is very costly to us when it comes from the south, perhaps that's something we ought to look at for generation. If you go more than 150 miles, 300 miles from where you sit, then the generator pays to get that electricity to wherever you want to send it. If he wants to send it across the country, then he pays so many rates so that we don't shift those costs.

Those are my two questions really, or two comments, or maybe input. Thank you. I appreciate you all being here.

THE HONORABLE BROWNELL: Thank you, Commissioner. I think Kevin Kelly just wants to make some observations, not point/counterpoint, just answer or inform some of the issues that you raised.

MR. KELLY: Yeah. You've raised a couple of really good issues, Commissioner Arthur. What we were trying to get at in the paper on the single tariff, at least the Staff contend it's not that important an issue but a different set of issues.

Let me try to make the distinction, following

up on what Shelton said. A tariff process is two parts: the terms and conditions of service, and then there's the price. And when we say single tariff, we mean single terms and conditions, single price. Let me explain that a little bit. By terms and conditions, we mean we're asking, for example, should a retail and wholesale customer face the same curtailment priority? Should they face the same liability provisions? Should they face the same provisions for raising complaints, et cetera.

As to the price, the question is, should two customers located in the same place, let's say in Hartford, should two customers in Hartford, one wholesale and one retail, pay the same price for transmission service?

Commissioner Svanda raised an interesting question about whether energy imbalance should be the same. I turn the question around a little bit and say should a 100-megawatt wholesale customer and 100-megawatt factory in Hartford face the same energy imbalance charge versus should a small customer, wholesale or retail, maybe 100-kilowatt retail versus -- barber shop versus 100-kilowatt wholesale, if there were such a thing, face the same energy imbalance service? Should there be no distinction between retail and wholesale customers who are located in the same place?

What we, I think, didn't necessarily mean by the single tariff proposal is the question of whether a customer in Hartford and a customer in Portland, Maine, should face the same transmission price. It might be the case that the license plate pricing being different would be the same. That's an important question but a separate question from what we were trying to address.

Similarly, there's the -- the license plate goes to the allocation of the past, already sunk transmission cost. There's a very important issue -- I had six conversations on this before we started the session this morning -- when new transmission is built, how is that cost allocated? Should it be allocated geographically, or should -- so that different users pay for the costs? The only question we're raising in the Staff paper, I believe -- or intended to raise is not that very important issue of how you allocate cost of new transmission and the cost of old transmission, but if you have two customers, one wholesale and one retail, located in the same city, whether they should face a different allocation or get the same allocation.

THE HONORABLE BROWNELL: Thank you. Any of my other fellow commissioners have a comment? Yes?

UNIDENTIFIED SPEAKER: Commissioner Brownell, and like the rest of my colleagues this morning -- I never

did like microphones. Is that better? Again, like most of our other colleagues, Ms. Brownell, we do appreciate your willingness to come listen to us this morning. I want to echo a couple of thoughts that I've heard from some of the panel members but maybe put a slightly different spin on it.

Like Marsha, I have some concerns about the presuppositions on which the Staff paper was based. There's been enough discussion of whether everybody is somebody's native load that I'm going to kick that one around a little more without reiterating a concern that we make sure what you mean by that. I wouldn't disagree with it if we meant everybody is an end user customer at some point. That's true. All end-user customers, however, are not similarly situated, and you need to be careful in making that distinction.

Secondly, the Staff paper lists a number of factors that they characterize as suggesting the appropriateness of this single transmission tariff. The existence of those factors in any particular state varies. I counted up last night and we may have 1-1/2 of those four, and I'm not sure that we only have one. So as you sit there and try to figure out how to accomplish what you're thinking about, please remember that if you try to compose uniform terms and conditions on a nonuniform

situation, you may get some results you don't like.

The third thing I would like to emphasize to you is when you use the term "discrimination," let us remember what that term means. That term does not necessarily mean, at least in North Carolina law, that everybody gets treated the same, period. It means that everybody that is similarly situated gets treated the same. And so please keep in mind that not everybody across the country is similarly situated.

North Carolina is a state in which we still predominantly have service from vertically integrated monopoly providers. As has been stated several times, our retail customers have historically and to date paid for our transmission system. Our retail customers have also been entitled to a certain quality of service. If what you do degrades the quality of service or raises the cost, putting it very bluntly, there's not much in it for our customers, and I hope you can understand why that made some of us concerned about a proposal to make everything uniform.

You asked the question can the existing system be made to work. The first thing I would say to you is, as a representative of one of the nine states that is involved in the court proceedings, we, of course, take the position that you don't have any jurisdiction over bundled

retail sales, and therefore, this discussion is purely academic. I think my general counsel would get mad at me if I didn't preserve my position before I went on.

Having said that, in engaging in this academic discussion, if you decide to proceed with this and if you, contrary to our position, have the authority to do it, I urge you to take into consideration some of the things that Commissioner Hochstetter has mentioned and others have mentioned.

It is unfair, in our opinion, to degrade service received by native load customers from vertically integrated utilities. They have paid rates for several generations for the existing transmission service. If they are suddenly put on par with a group of folks that haven't done that, we would contend that they've been unfairly treated.

Similarly, there's been a lot of discussion of service costs. If you, in fact, say that we're going to change the native load priority in terms of service quality, that has real ramifications to native load customers.

If you want -- one of the questions you asked is what can be done to make the existing system better. I'm reading your orders. I don't claim to have an encyclopedic knowledge of it, but I read in your orders

reference to things like anecdotal misuse of transmission and calculations and things like that. One thing you may want to consider before you decide that you want to abandon the existing model is to look at the issue of enforcement. You've already started doing that, but if, in fact, things are going on in the existing system that shouldn't be going on, the remedy may not be to just throw the baby out in the bath. The remedy may very well be to look at your enforcement efforts and try to improve.

So I offer those comments for what they're worth. I appreciate your willingness to listen to us today and look forward to hearing from everybody else.

THE HONORABLE BROWNELL: Chairman Showalter, thank you for joining us.

THE HONORABLE SHOWALTER: I'd like to get at this question by way of an analogy, which I hope is insightful. Most of our states have public universities that have been built with tax dollars, and the citizens of our individual states can go to those universities for a subsidized price or a lower price, and the tuition level for out-of-state students is higher.

Now, suppose we have some federal economists who came and looked at our universities and said you've got barriers here. The goal here should be everybody gets an equal education and high -- the market price should

prevail. So you've got a barrier, number 1, to outsiders who want to use your university, and by the way, it's not only out-of-state students who ought to be able to use this for the same price, but what about companies? Why should this state laboratory, state university laboratory be limited to use for in-state students or even out-of-state students? Why shouldn't the private company, who pays a higher price for that lab, be allowed to use it. After all, isn't this for the same end goal. I don't know, prescription drugs, other things that labs ultimately do.

Like universities, public utilities are public service companies providing essential services to the citizens of a particular state. It seems to me that what you are saying is that it is a barrier for a public service utility to charge different rates for its users as opposed to other users, whether they be retail or wholesale. The issue is, should the wholesale system serve the retail system, or should the retail system serve the wholesale system? I think most people would agree in the abstract it's the first: The wholesale system ought to serve the retail system, meaning the wholesale system ought to serve the ultimate retail customers.

If you're a person who already thinks you -- who thinks that what is going to serve the retail

customers is open markets all the way through, then there isn't a particular conflict, and many of you feel that way. But if you're a person, like me and our state, who feels it has not been demonstrated that, in our state anyway -- and I frankly don't think in other states it has not been demonstrated yet, that open retail markets are beneficiary to the retail customer, then it also follows that the system that those retail customers have built should not be subordinated to the wholesale system.

I think that's the fundamental issue, and it's very hard to -- it's easier to say well, can't we have wholesale competition but maybe retail regulation and let the states do what they want on the retail side. And there is an answer, a qualified yes to that, which is so long as the wholesale market is subordinated to the end-use customers and what those customers and their states feel is in their best interest, you could have a competitive wholesale market. It just might not be a pure one, and the transmission is an element of that. It won't be as competitive at the wholesale level as if you freed up the transmission that the retail customers had paid for.

But that isn't the goal. The goal is not to have a purely competitive wholesale market. The goal is to have the best services, reliable and affordable, at the

retail level, and until it's demonstrated, which it has not been, that a wholly pure competitive wholesale market actually would serve the retail customers better, including their yielding up their transmission, it shouldn't be allowed.

In the meantime, as with public universities, state of Oregon has -- Washington and Idaho have reciprocity agreements. If those states decide that it is in their mutual benefit, mutual interest to have an arrangement, they should do so. That is essentially the RTO exercise that's going on right now. If the states can get together and determine that an RTO is in their mutual interest, then I think it should go forward.

However, it shouldn't be mandated by FERC, and it shouldn't happen at all unless the benefits clearly outweigh the costs, including the risks that one takes when going to the transition of a new system.

THE HONORABLE BROWNELL: Thank you, Marilyn. I would add -- I know that Kevin Kelly wants to add something as well. I think it's important that we agree that the reason we're asking these questions and raising issues is not, in fact, to take any course of action that would degrade the system in any way for retail customers. So let's just all accept that as a given, if we can. We may disagree on how to get there, but in fact, we're

trying to enhance the system for everyone's benefit.

Kevin?

MR. KELLY: Commissioner Showalter, I hope this doesn't sound too much like point/counterpoint, but in terms of what we're trying to achieve, it is good, high-quality, low-cost retail service to retail customers. In today's world, we seem to be getting to where to get low-cost retail power, by and large you need to shop around and find the best deal, as well as locally, whether it's a state with retail access or a state without retail access, where their local utility would be shopping around from the neighboring utilities or utilities far away to get the best deal.

The ability to shop around means that they have to have good quality transmission access, so that you have a city who buys from several states away. They will probably only do so if they have the confidence that if they buy some power from several states away, they get firm transmission service, that that service is just as firm to the native load in Seattle as it is to the native load of the utilities along the way who provide firm service as well as transmission service. And it's getting to a kind of quality of service for all customers, regardless of whether they are being served by a utility that's calling them retail or being served transmission by

a utility that calls them a wholesale customer.

That's what we're trying to achieve is that kind of equality. We're putting on the table the question of whether that kind of equality, wholesale and retail, is ultimately good to customers by letting them shop around for the lowest cost power.

THE HONORABLE BROWNELL: I think we have Commissioner McDonald first and then Commissioner Anderson.

THE HONORABLE MC DONALD: Thank you, Commissioner. When you were speaking in Georgia back in last fall, the freshest remarks I heard in the RTO dilemma was the cost-of-service study that was going to be pursued. My question is, what is the status of the cost/benefit study, and will state commissions have an opportunity to review and even provide input into that before it's finalized?

And my second question, of course being an elected commissioner, and my responsibility, as my colleague of Michigan -- statutorily, we have a responsibility to our customers for the lowest cost and reliability that we have. If, as a state commissioner, that I'm required to approve an RTO for our regulated utilities in our state, which would mean that these consumers would not have priority to that system, how can

I truly justify that with the people that I represent as a public service commissioner in Georgia?

Those are my two questions. Thank you.

THE HONORABLE BROWNELL: I'm going to take the first stab and ask my friends to jump in here, because I've been a little distant from the cost/benefit study. We wanted to make sure it went on independent without any direction from the 11th floor at the FERC. For those of you who don't know, we began a cost/benefit study about two months ago, hired a consultant, asked a number of state commissioners from different regions to help with that process, with the goal of creating a greater degree of comfort, which I agree we probably should have done a year ago, that we understood fully the ramifications of both short-term and long-term costs and benefits.

And I think there have been some studies out there that have only looked at very short-term things, and I think as public policymakers, I think all of us are cognizant of some longer-term goals here. That is estimated, I believe, to be out mid-February. I think it's still on track, and while we have not discussed it with my colleagues, I think it probably would be our expectation that, of course, we want to get comments.

Let me say, though, in that regard, I would expect that and know that there are other studies out

there and that at some point we'll have dueling studies. It's going to happen. What I think we all need to do is make sure we understand the assumptions that went into these studies and what they were directed to do. In our case, the direction was with the input from Staff and state commissioners, look at the issues that are important, challenge yourself on the assumptions, but we did not dictate outcome. Whatever the outcome is, it is. So I would hope -- and I'm going to turn it over to Staff, who are a little closer to this than I am.

MR. CANNON: The only thing I would add is we have indeed tried to work very closely with state commissioners in terms of putting the study together, in terms of making sure they understand the assumptions that underlie the study. We had a group that actually visited the consultants' office, ICF, and sort of worked through and asked smart questions about are you studying this, are you studying that, so at least everybody understands what the study's purporting to do. It is trying to get a better handle on what this cost/benefit analysis means for a particular region, rather than just sort of looking across the entire nation and averaging a lot of numbers.

With that said, the intention will be to issue this and let, you know, everyone comment, but we had to cut it off in terms of state commissions having sort of

special access to the report once they start crunching the numbers, once they start actually turning out the model results. At that point we had to say okay, the consultant will do what they've been paid to do, and then once that report comes out, it will be issued so that state commissions, consumer advocates, and, you know, any market participant that's interested in commenting on the study and critiquing the study will be able to come back and tell us what they think about it.

THE HONORABLE BROWNELL: I'm going to ask Kevin to elaborate on your second question, but as I think we tried to say, it was not our goal -- and we certainly understand your responsibility as an elected or, indeed, appointed official. The goal is to provide low-cost, reliable service to the retail customer. Our goal is not to create two classes of citizens. That's not what this is all about.

Kevin, do you want to add to that?

MR. KELLY: Just to mention, if the question is if there is wholesale and retail equality, why would you want to improve, say, an RTO in Georgia that gave a priority that Georgia customers might have, and I guess the answer would be, to me, that if that gave Georgia citizens priority in the surrounding states when they were reporting low-cost power from them, you'd have to make

judgment there as well. That is, if they don't have priority in South Carolina and Alabama, et cetera, and got it through that trade-off, would that be worthwhile.

THE HONORABLE KELLY: I'm an elected commissioner, but unlike him, I'm term limit. So I have zero accountability.

THE HONORABLE BROWNELL: That's a very scary thought, and it's very liberating.

THE HONORABLE KELLY: I just have a couple points. One is about the term "native load customer." When I saw in the paper that the premise was that everybody is somebody's native load customer, I thought that's bull. In states like Montana, which are deregulated, there are industrial customers and some other aggregated commercial customers who have gone off the system, that are no longer native load customers for anybody. Nobody has the obligation to serve them.

But then you think well, maybe the term "native load" needs to be reconsidered. Maybe it needs to be unbundled just like we are unbundling the system. That is, we have native load supply customers, and some are and some aren't, but everybody probably is a native load transmission customer. Maybe that's what you meant, and maybe that distinction needs to be drawn a little more clearly.

If we're just talking about transmission rates, sure, everybody takes transmission unless they're self-generating. So that may help as you approach this problem.

The second point is by -- I guess to try to respond to the way Kevin has posed the question, should these two different customers in Hartford pay different transmission rates. The answer is maybe, and the reason is not, as some of my colleagues would say, that customer A has been on the system for generations and has paid for it and has some -- I infer some entitlement because of that. I don't think that's the case. I think those customers paid for what they got. They paid for the service, they got the service. That doesn't create any ownership on the system or any entitlement. Maybe this is a fine point, but the key distinction, I think, is the age-old principle of cost causation.

So the question that, Kevin, you have to look at is do those two different customers at Hartford impose different costs on the system? If a new load or a new generator comes on and new transmission has to be built to provide the service to that load or that generator, then it's not fair or right to impose the cost of that transmission on another customer who didn't impose that cost. So that's the distinction that I think should be

made, is who caused that cost and try to allocate those costs to the cost causers.

THE HONORABLE BROWNELL: Good distinctions. Thank you, as always. Commissioner Dworkin?

COMMISSIONER DWORKIN: Thank you. You've heard me talk on many of these things in nuts and bolts, and I don't want to get into detail right now, but I can't resist making one very abstract, I think fundamental point that is triggered by a comment I heard earlier.

With all due respect, I want to seriously disagree with it and express the fear about what I heard. The comment was to take as a given that the goal is benefit to retail customers, and I really want to focus on the difference between a given and a constraint, because I accept as a given that is your goal, out of both personal respect and a careful reading of what you've written. Yet, I'm deeply concerned about the attitude that because it's a given, we can set it to the side and move on. Instead, I feel that goal is a constraint against which we have to test what we might otherwise do, never to be abandoned, yet remembered again and again, and because it's a constraint, sometimes it means we don't do what you might otherwise want to do. That's the nature of a constraint as opposed to a given, and I really plead with you again and again to test what seems like a good idea in

theory, maybe even in limited practice, against the constraint of whether it may cause harm to end users. There is the risk that reality does not turn out the way we expect, that the anticipated billion dollar savings in California turned out to be the $23 billion loss, that the anticipation and the event between the being and the becoming turns out to be the demonstration of our very human limits. The concept that because we know our motives are pure and our goals are good that what we are doing will not cause harm is a terribly scary concept. I really can't be any more serious that these things are not givens, they are constraints, and again and again we have to ask ourselves whether they're limits on what we should do rather than motives for doing it.

THE HONORABLE BROWNELL: Thank you, and we thank you for reminding us of that as we move forward with what is an aggressive agenda. We do need to do that, what I call the look in the mirror test, along the way. Thank you. Commissioner, welcome.

THE HONORABLE ATKINS: Buddy Atkins, Commissioner from South Carolina. Again, I appreciate the opportunity to speak before the panel, Commissioner Brownell and the other panel members. Thank you for being here.

I'm one of those fortunate commissioners who

got to sit in and advise the consultant on the cost/benefit study, which, my understanding, will be coming out this Friday, the 15th. Commissioner Dworkin and former Commissioner Meyers, Commissioner Showalter, Schriber from Ohio and some other folks, we had a good opportunity to sit and have input on that, and I think we're very interested to see what the outcomes will be. I must say I was very impressed with the consultant and with some of the capabilities of the model and the things that were being done. I do believe, though, that at the end point and when the study comes out, there will be some additional questions and model runs that will be needed by some of the various regions and, in particular, the Southeast, and I think that's been kind of the knowledge base anyway, that we would have the ability to do some of those, to answer some of the questions that, perhaps, are more important to us than they would be to the broader agenda that FERC has.

I bring that up, because it's interesting that Bubba from Georgia was asking about the outcome of the model and what was going on, and there was an e-mail that wandered around on Thursday before I left South Carolina about this alleged cost/benefit study and who was on it, and I guess being the only Commissioner from the Southeast on it, there were a lot of questions of how I got on it

and why was I on it and how was it going to work and ying, yang and yang.

I think what we have here is a problem that's inherent to all of us. As state commissioners, we have so much on our plate. Last year, we in South Carolina gave approval to BellSouth for 271, which was probably close to 150,000 pages of testimony and exhibits. We have water cases pending before us. We have Merchant siting generations coming before us, all very controversial, all very time-consuming and complicated. There's not a single commissioner that has the time or the opportunity to dedicate, I believe, what is needed to interact effectively with FERC on this issue.

I want to support what Commissioner Svanda said in terms of the new model. Perhaps the coordination vis-a-vis 271 on state issues that are of importance, and then also the joint state and federal panel. Commissioner Brownell, I had the opportunity to watch you all yesterday on C-SPAN 2 at the Energy Daily conference, and I appreciated all the things that you had to say. There seems to be this movement towards integrating state commissions more and more into the process, and I must say I'm very pleased with having Ed Meyers there to lead that. I know he'll do a great job, but I think we need those joint panels now. I think as long as we put that off,

there's going to be this continuum of misinformation, and I have a hard enough time communicating with my fellow commissioners because we're all so busy, let alone all the commissioners in the Southeast. You can imagine commissioner Showalter trying to communicate with everybody in the West.

I think we just have to move forward with those panels, and I think they need to be regulatory in nature. I think we're going to have to bite the bullet here.

On page 4 of your white paper, item 3, talking about state commissions' obligations and then FERC's obligations. The only way you're going to marry these, whether you have a single tariff or a dual tariff or retail and wholesale, whatever it comes down to, I've heard all the panel members say that it's incumbent we foster this federal relationship, and I think that it just has to happen.

This is consistent with a letter that I wrote to Chairman Wood last year. I hope he will dig that out of the file and look at it again. It's also consistent with the DOE national transmission study in Atlanta when they came back last March. I appreciate very much the opportunity of having been on that advisory group for the model, because it makes me have a better feeling about what's going on in terms of some of the cost/benefit

studies, although it's not going to be the end-all. But the only way that I can know to move forward with that is to have greater interaction all the time with FERC in a more formalized process and to bring the states together. We're going to have an RTO. Let's talk about the siting issues. Let's talk about the planning issues. And the only way you can have a tariff, I believe, is to do that.

I appreciate it very much, and thank you. It's a difficult issue, as everybody knows, and I think we're getting close, and I certainly don't want to obstruct the process at all, but there's still some key questions that need to be answered, but it's going to require sitting in a very formalized process and not so much informal facilitation.

THE HONORABLE BROWNELL: Thank you very much, and thank you for the time that you've spent on the cost/benefit study and these other issues. A couple of observations. Before we designed the state regional panels, we had a pretty extensive internal discussion about the options that were available to us, the models that were out there, including the joint board contract, which I don't think any of us are opposed to, but we were concerned that that process did not lend itself to the flexibility that was probably needed as these issues evolved. So the doors are closed, but we kind of felt

that we wanted to try this other way in terms of state and regional panels, which we do not envision, by the way, as being once. We need to -- we've been waiting for Ed to come on board to help us amplify our resources so that we could get organized, but we see those on a fairly regular basis. But we're not limited to that model. Let me talk a little bit about the informal process. If we were transforming ourselves in a corporate world, we would use many different tools in order to get to that transformation. It isn't always possible, particularly as we move to markets which require answers faster, as we are both adjudicating different issues, that the traditional processes may not work.

And so just as we've had informal panels of experts during RTO season, we do need to have that room to use informal small groups of people to inform the decisions that then go out and get tested against a larger group in a more formal fashion. There is no magic of who participates in those. Often it's people who volunteer, people who have a particular set of skill sets. We do not all have the same skill sets, and that's the good news, but it also means that we'll be calling on different people for different kinds of things. So it isn't an exclusionary process. It's just a how can we work more effectively process.

As far as the 271 model, boy, I guess you guys had more fun than I did, because it wasn't fun, and I'm not sure it in the end worked all that effectively, but that's my own opinion, not those of any of my colleagues in Pennsylvania, I can assure you. So I think we need to -- that's a long way of saying I think we all need to push the envelope in terms of how we respond, the depth with which we respond, the resources that state commissions and indeed our own Commission is indeed a brutal one. We may need to kind of pick and choose those areas in which different states wish to get involved or designate people to get involved. It's an aggressive agenda that is taxing everyone, I can assure you. We have some cranky folks. We've got a lot of very tired folks. So I appreciate the input and don't mind institutionalizing anything, but I'm not sure institutionalizing actually gets you where you need to go in this transitional process.

Let me talk a little bit about siting. We've been working with the National Governors Association to look at different models. We are agnostic. We do not wish to have siting authority. Both Pat and I have said that. We will do whatever Congress tells us to do in that regard. One of the problems with the joint board model, as we looked at it, is that it does get you that legal

authority that you may or may not need, but I would encourage all of you to look at the NGA Web site to look at some of the options that they laid out in a white paper, and they were actually coming to some, I think, conclusions the other day after I left.

So they may actually have a series of recommendations. But they looked at joint protocols as they're doing in the West. They looked at joint boards. They looked at compacts, and then they were looking at variations on the theme, and I think there was some unanimity that they did actually have consensus on, they didn't want the FERC hands in it at all. So be it.

THE HONORABLE BURG: Jim Burg, South Dakota. The last comments you made go pretty near to where I want to go because of comments that Jim Kelly made. Coming from a state that we feel very fortunate has one provider, let alone competitive providers, and they're satisfied with that and oversight over that, and being a skeptic onto whether markets really will bring fair services to everybody, especially those people that don't show them an adequate profit.

Kevin mentioned that we want to get there, but one of the obstacles to getting there, to getting to competition is transmission, and that's a concern that I have had for a long time, that we've gotten the cart ahead

of the horse to a degree, trying to have deregulation and restructuring, even of the wholesale market and especially the retail market, before we know that we can get the power from point to point.

The fact that I feel the transmission issue needs to be satisfied before these others even have a chance of succeeding, and it's becoming a larger challenge than any of us have ever figured it would be, siting being only one of those. So I suppose that we get the answers to how we are going to transmit this wholesale power if it's available, and we definitely need that cost study to know if we're going to build all this transmission, are we really going to end up with a cheaper product. I thought that's what the goal was from the very beginning.

THE HONORABLE BROWNELL: It was the goal, it is the goal. I think a combination of factors are going to help inform this discussion, not only our study and what, I'm sure, are a lot of other studies out there bubbling up, but I think the DOE transmission constraint study is going to give us a better picture of what price we're paying for not moving forward and not doing what we need to do to get clarity to these issues, so we can get the investment and allow people to go forward with business decisions and allow the states and regions, as well as ourselves, to get a better understanding of what those

costs are going to be and what benefits they bring, both short-term and, as I said earlier, long-term.

We have 10 minutes left, and I want to give our staff a chance to ask a wrap-up question of the panelists and whoever else may comment. Normally, we have an opportunity for the rest of the audience to ask questions. Unfortunately, we're going to go over time, and I've known Ms. Shelton long enough that I would not survive the day if I delayed this past 12:00. We have now nine minutes, and I'm going to ask Kevin Kelly to ask a couple wrap-up questions. We will stay around if you want to talk and we will certainly be here for the next couple of days, and maybe the panelists can stay around if you have any more questions of them. Kevin?

MR. KELLY: Many of the comments went to transmission pricing issues, the license plate versus rolled-in issue for old transmission, and for new transmission, the rolled-in versus the charged cost. If you were to set both of those important issues aside and just ask the question should wholesale unbundled retail and unbundled retail customers all face the same terms and conditions of transmission service, and should all those customers, if they're at the same location, face the same transmission price? How would you come down on that?

THE HONORABLE BROWNELL: Marsha?

THE HONORABLE SMITH: I thought Commissioner Anderson's comments were particularly to the point on that issue, and I think the answer is maybe, maybe not, and you need to look at it carefully. But I don't think it would be some injustice if there were different rules for those different categories that had a rational basis.

THE HONORABLE BROWNELL: Commissioner Baez?

THE HONORABLE BAEZ: It's one of those things that I have to stay away from, but I think on principle we have to stick as closely as possible to whatever our similarly situated -- whatever our concept of similar situations are and maintain some level of fairness, some level of consideration of fairness in that situation. Beyond that, I'm not sure I'm comfortable saying any more.

THE HONORABLE BROWNELL: We appreciate that. Commissioner Hochstetter?

THE HONORABLE HOCHSTETTER: I think that was one of the distinctions I made in my comments, that access and nondiscriminatory provisions of service, I see as a different issue from price, and I think that price differentiation is most likely appropriate and necessary for all the various reasons that we discussed today, and I think, you know, we can hold that as a separate issue, separate and apart from the general terms and conditions.

THE HONORABLE SVANDA: And I think I answered

that in my prepared comments by saying yes, but then I also proceeded to give some qualifiers to that yes, and I think those qualifiers are consistent with a lot of the other comments that you're receiving.

THE HONORABLE BROWNELL: Thank you. Any other -- we've got two minutes in case any other Staff members have a question.

Thank you so much for giving up your Sunday morning. These are not easy issues, none of them are, but I have confidence with the collective commitment we'll get there. Enjoy. Thank you.

Don't forget, tomorrow 4:00 p.m., discussion with state commissioners on ensuring adequate capacity reserves; February 14th, Valentine's Day, demand site management.

(Whereupon, at 12:00 p.m., the workshop was concluded.)