

**ORIGINAL**  
STATE OF INDIANA

**INDIANA UTILITY REGULATORY COMMISSION**

**RECEIVED**

DEC 18 2001

INDIANA UTILITY REGULATORY COMMISSION  
ELECTRICITY DIVISION

**IN THE MATTER OF THE JOINT PETITION )  
OF INDIANA MICHIGAN POWER )  
COMPANY, D/B/A AMERICAN ELECTRIC )  
POWER, AND NORTHERN INDIANA )  
PUBLIC SERVICE COMPANY FOR )  
APPROVAL, TO THE EXTENT NECESSARY, )  
TO TRANSFER FUNCTIONAL CONTROL )  
OF TRANSMISSION FACILITIES LOCATED )  
IN INDIANA TO THE ALLIANCE REGIONAL )  
TRANSMISSION ORGANIZATION )  
PURSUANT TO IND. CODE 8-1-2-83. )**

**CAUSE No. 42032  
(Consolidated with  
CAUSE No. 42027)**

**APPROVED:**

**DEC 17 2001**

**BY THE COMMISSION:**

**David E. Ziegner, Commissioner  
David W. Hadley, Commissioner  
Scott R. Storms, Chief Administrative Law Judge**

**I. Procedural Background.** On June 29, 2001, the Indiana Michigan Power Company, d/b/a American Electric Power ("AEP" or "I&M") and Northern Indiana Public Service Company ("NIPSCO") (collectively referred to as the "Joint Petitioners" or Jt. Pct. Alliance") filed a joint petition requesting approval to transfer functional control of transmission facilities located within the State of Indiana to the Alliance Regional Transmission Organization ("Alliance RTO" or "ARTO").

By docket entry dated July 26, 2001, the Presiding Officers' determined that the proceeding filed by the Joint Petitioners shared common issues of fact and law with issues raised by a joint petition filed by Hoosier Energy Rural Electric Cooperative, Inc. ("Hoosier"), Indianapolis Power & Light Company ("IPL"), PSI Energy, Inc. ("PSI"), Vectren Energy Delivery of Indiana, Inc., also known as Southern Indiana Gas & Electric Company ("Vectren"), and Wabash Valley Power Association, Inc. ("WVPA") in Cause No. 42027 ("MISO Participants"). The Commission ordered that the two causes be consolidated in accordance with the provisions set forth in 170 IAC § 1-1.1-19. The Commission further indicated that, at a minimum, the following list of issues regarding the formation and functionality of Regional Transmission Operators ("RTOs") should be considered as part of the consolidated proceeding: (i) Congestion Management; (ii) Real-Time Balancing Markets; (iii) Security Coordination; (iv) Transmission Load Relief ("TLR"); (v) Control Areas; (vi) Rate Design; (vii) Market Monitoring; (viii) Regional Planning; and (ix) Interconnection Policy.

On August 2, 2001, the Presiding Officers issued a second docket entry providing more detailed guidance regarding the issues to be addressed in the consolidated proceeding in order to facilitate the Commission's review of market reliability in Indiana in the context of the relief requested.

On July 23, 2001, Citizen's Action Coalition of Indiana, Inc. ("Coalition") filed a petition seeking intervention in the proceeding. On August 13, 2001, Indiana Municipal Power Agency ("IMPA") filed a petition to intervene. On August 22, 2001, the Indiana Industrial Group ("IIG"), consisting of a group of customers served by some of the petitioning public utilities in the consolidated cause, filed a petition to intervene. On September 24, 2001, Enron Power Marketing, Inc. ("Enron") filed a petition seeking intervention in this proceeding. The Commission subsequently granted all of the requested interventions.

An Evidentiary Hearing in the consolidated proceeding was held on November 19-21, 2001, in Room TC10 of the Indiana Government Center South, Indianapolis, Indiana. At the Evidentiary Hearing, evidence in the consolidated proceeding was submitted by the Joint Petitioners in this Cause, the MISO Participants, the Indiana Office of Utility Consumer Counselor ("OUCC"), Intervenor IIG and Enron.

The following witnesses testified at the Evidentiary Hearing in the consolidated proceedings: Mr. James P. Torgerson, Chief Executive Officer of the MISO; Mr. John C. Procario, Vice President and Chief Operating Officer of the service company for PSI and its utility affiliates; Mr. Ronald R. Jackups, Vice President of Electric System Operations for the service company for PSI and its utility affiliates; Mr. William Doty, Senior Vice President of Energy Delivery for Vectren; Mr. Michael L. Holtsclaw, Team Leader, Transmission Operations for IPL; Mr. Ronald C. Snead, Manager of Bulk Transmission Planning for the service company for PSI and its utility affiliates; Mr. Douglas E. Hils, Manager of Control Area Operations for the service company for PSI and its utility affiliates; Mr. Michael J. Mooney, Manager of Corporate Planning for Hoosier; and Mr. Martin J. Blake, a consultant specializing in the areas of marketing, market research, rate and regulatory support, training and strategic planning for energy industry clients. J. Craig Baker, Senior Vice President - Regulation and Public Policy, American Electric Power Service Corporation and Frank A. Venhuizen, Director, Electric Transmission and Market Services, NIPSCO, testified in support of the joint petition filed by the Alliance RTO Transmission Owners. These witnesses also sponsored the responses to issues presented by the Commission in its Docket Entry dated August 2, 2001. Dr. Peter Boerger testified on behalf of the OUCC, James R. Dauphinais testified on behalf of Intervenor IIG, and Michael J. Roan offered testimony on behalf of Intervenor Enron. Members of the general public appeared at the Evidentiary Hearing.

Based upon the applicable law and evidence herein, the Commission now finds as follows:

A. **Notice.** Notice of the hearing in this Cause was duly given and published more than ten (10) days prior to the hearing in newspapers of general circulation as required by law.

B. **Jurisdiction.**

1. **Jurisdiction over the Joint Petitioners.** AEP and NIPSCO are each a "public utility" under IC § 8-1-2-1, and are subject to the Commission's jurisdiction in the manner in accordance with the Public Service Commission Act, as amended, and other laws of the State of Indiana.

2. **Jurisdiction over the Subject Matter.** Ind. Code. 8-1-2-83 provides, in relevant part:

No public utility, as defined in section 1 of this chapter, shall sell, assign, transfer, lease, or encumber its franchise, works, or system to any other person, partnership, limited liability company, or corporation, or contract for the operation of any part of its works or system by any other person, partnership, limited liability company, or corporation, without the approval of the commission after hearing.

Each Joint Petitioner seeks to transfer to the Alliance RTO, by contract, the responsibility for the functional control of part of its transmission facilities. These transmission facilities constitute a "part of [each utility's] works or system." Consequently, the Commission has subject matter jurisdiction over this cause.

C. **Joint Petitioners' Characteristics and Business.** I&M is a wholly owned subsidiary of American Electric Power Company, Inc. I&M is a corporation organized and existing under the laws of the State of Indiana with its principal executive offices located at One Summit Square, Fort Wayne, Indiana. I&M has the corporate power and authority to engage in, among other things, generating, transmitting, distributing, and selling electric energy within the state of Indiana and Michigan. I&M's Indiana service area consists of approximately 8,260 square miles and is located in northern and eastern Indiana and southwestern Michigan. AEP's electric system is a completely integrated and interconnected entity and is operated as a single utility. I&M's transmission system in Indiana consists of approximately 4,428 circuit miles of line, including 599 circuit miles of 765 kV line, 1,146 circuit miles of 345 kV line, 1,421 circuit miles of 138 kV line, 401 circuit miles of 69 kV line, and 591 circuit miles of 34.5 kV line.

NIPSCO is a public utility corporation organized and existing under the laws of the State of Indiana, having its principal office at 801 E. 86<sup>th</sup> Avenue, Merrillville, Indiana. NIPSCO is engaged in rendering electric utility service to the public in the State of Indiana and owns, operates, manages and controls plant and equipment within the State of Indiana used for the production, transmission, delivery and furnishing of electric utility service. NIPSCO currently supplies electric energy to approximately 430,000 customers in 21 counties in the northern part of Indiana. The territory in which NIPSCO provides electric service covers approximately 12,000 square miles and has a population of 2.2 million. NIPSCO owns and operates four coal-fired electric generating stations, two hydroelectric generating plants, and four gas-fired combustion turbines providing a total system net capability of 3,392 megawatts. NIPSCO's transmission system consists of approximately 3,066 circuit miles of line, including 354 circuit miles of 345 kV line, 759 miles of 138 kV line, 1,529 miles of 69 kV line, and 245 miles of 34.5 kV line.

D. **Nature of the Case.** The Joint Petitioners seek the Commission's approval of the transfer of functional control of operation of certain of their electric transmission facilities to the Alliance RTO. The facilities in question are all 138 kV and above network transmission facilities

for I&M; and all 69 KV and above system for NIPSCO (Tr Venhuizen p.6). The facilities are integral to the provision of adequate and reliable electric service to retail customers in Indiana.

**E. Legal Overview of Requested Relief.** The Joint Petitioners in this proceeding seek Commission approval to transfer control over certain transmission assets as provided under Ind. Code. § 8-1-2-83(a), which states, *inter alia*, that:

No public utility, as defined in section 1 of this chapter, shall sell, assign, transfer, lease, or encumber its franchise, works, or system to any other person, partnership, limited liability company, or corporation, or contract for the operation of any part of its works or system by any other person, partnership, limited liability company, or corporation, without the approval of the commission after hearing.

The provisions set forth in IC § 8-1-2-83, are intended to ensure that Commission approval is granted before a utility may be operated or controlled by any person other than the person that is licensed or permitted to do so. *Illinois-Indiana Cable TV v. Public Service Comm'n*, 427 N.E. 2d 1100, 1108 (Ind. App. 1981). In enacting the foregoing provision, the Legislature intended the Commission to regulate public utility transfers "in the interest of public welfare." See, *In re N.W. Ind. Tel. Co.*, 171 N.E. 65 (Ind.1930). Explaining the purpose of the transfer approval legislation, the court stated:

By [Section 95, predecessor to Ind. Code sec. 8-1-2-83], the Legislature undertook to supervise the sale of public utility property in the interest of the public by providing a means for the investigation of the proposed sale in advance of its consummation. Such investigation necessarily has to do with the effect in the future on public convenience and necessity....One of the reasons for this statute, and there may be many more, is to protect the public in the use of utility service with as little inconvenience as may be essentially necessary to furnish the same.

*In re N.W. Ind. Tel. Co.* 171 N.E. at 71.

Consistent with the foregoing analysis, the Commission has applied the public interest standard of review in numerous proceedings and determined that, "[I]n reaching a decision to approve a purchase or sale of utility property, the Commission's threshold inquiry must be whether or not that proposed purchase and sale is in the public interest." See, *In the Matter of the Joint Petition of Commonwealth Edison Company of Indiana, State Line Energy L.L.C and Commonwealth Edison Company*, Ind. Util. Reg. Comm'n, Cause No. 40575, (December 18, 1996), citing *Indiana ex rel Indianapolis Traction & Term Co. v. Lewis* 120 N.E. 129 (1918).

Also, in considering whether a transfer satisfies the public interest test of IC § 8-1-2-83, the Commission must look to other statutes. The combination of Commission decisions under IC § 8-1-2-83, and decisions under other statutes, yields a set of public interest factors with direct application to this cause.

Reliability: The Commission is charged with ensuring that a utility provide reliable service and facilities. See, IC § 8-1-2-4 (each utility "is required to furnish reasonably adequate service and facilities"); *Office of Util. Consumer Counselor v. PSI, Inc.*, 463 N.E. 2d 499, 503 (Ind. Ct. App. 1984)(finding that the Commission .."was established to insure that public utilities provide constant, reliable and efficient service to customers...."); *Indiana Michigan Power Company*, (Ind. Util. Reg. Comm'n, Cause No. 41982 ( July 27, 2001), (approving sale of a transmission facility in part because the transfer would "result in the improvement of transmission facilities and provide for customer load growth").

Financial Viability: See, *Commonwealth Edison of Indiana*, Ind. Util. Reg. Comm'n, Cause No. 40575, (December 18, 1996), (approving the transfer of certain assets and inventory because the transferee had significant experience in the business of operating coal-fired generating stations and had the necessary financial strength and experience to operate the project); *Investigation into the Operation of Arlington Utilities*, Ind. Util. Reg. Comm'n, Cause No. 41540 (March 29, 2001), (reviewing financial viability of transferee to consummate purchase of water utility's assets).

Impact on Competition: See, *Ameritech Communications Inc., and Williams Communications, Inc.*, Ind. Util. Reg. Comm'n, Cause No. 41678, (August 2, 2000), (In which the Petitioner's sought approval to transfer assets under IC § 8-1-2-83, and in which the Commission found that system enhancements resulting from asset transfer will lead to increased competition);

Impact on Efficiency and Rates: IC §§ 8-1-2-58 and 8-1-2-69, prohibit any rate or charge may be unreasonable or unjustly discriminatory or that any service is inadequate regulation, act, practice or service as shall be just and reasonable. See also, *Ameritech*, *Id.* at \*9 (finding that the transfer would allow for "system-wide consistency" in the method of providing services and will result in a better utilization of resources and streamlined operations which will benefit the public");

Access to Information: IC § 8-1-2-48 requires that the Commission have access to "all necessary information to enable the commission to perform its duties."

These public policy concerns -- reliability, financial viability, competition, efficiency and rates, and access to information -- all are implicated by the proposals in this case, and will be discussed in more detail below. As fully set forth in this Order, the Commission has reviewed the evidence presented in each Cause with respect to its effect on the public interest concerns in Indiana. While the review of each Cause is within the same general framework, the Commission hereby issues separate Orders for Cause Nos. 42027 and 42032.

**II. The Joint Petitioners' Evidence.** The Joint Petitioners submitted the testimony of two witnesses in this Cause. The testimony presented by the witnesses described, among other things: (i) the belief that the transfer of functional control of I&M's and NIPSCO's transmission facilities to the Alliance RTO would benefit consumers in Indiana by improving the reliability and economic efficiency of the electric transmission system, (ii) the Inter-RTO Cooperation Agreement ("IRCA") would provide enhanced reliability and economic benefits for Indiana customers, (iii) the formation of the Alliance RTO, (iv) recent developments relating to the ARTO, including the FERC-approved settlement agreement in *Illinois Power Company*, FERC Docket No. ER01-123-000 (the "Illinois Power Settlement Agreement") establishing the terms for a cooperative relationship between the Midwest ISO and the ARTO, including how "seams issues" will be dealt with by the two RTOs.

The witnesses provided the following explanation of ARTO:

The companies seeking to form the ARTO propose a for-profit company that will own and operate transmission facilities divested to it, and will exercise functional control over the transmission facilities of nondivesting transmission owners. Mr. Baker testified that under this "Transco" model, the entity controlling the transmission would itself be managed by an independent entity. (Transmission owners under a Transco format have the option of divesting their transmission facilities to the Transco, or having the Transco operate their facilities pursuant to a contractual arrangement.) (Jt. Pet. Alliance JCB, p. 4).

Mr. Baker testified that the Alliance business plan is the first proposed Transco model that provides for an experienced independent company to make a significant investment in the Transco and to become its managing member. Mr. Baker further testified that that the Alliance Companies have filed their contract with National Grid Group PLC, ("National Grid" or "NGC") with the FERC for approval. If approved by the FERC, the contract would allow NGC to serve as managing member of the ARTO for an initial seven-year period. (Jt. Pet. Alliance JCB-S, p. 5). Before the FERC can rule on this contract, it must decide if NGC is a market participant. (Under FERC Order 2000's ("FERC Order 200") requirement of independence, an RTO may not be managed by a market participant. (FERC Docket No. RT01-88-000) Mr. Baker testified that he is confident that NGC is not a market participant. Mr. Baker also testified that the Alliance Companies do not have an alternative managing member if NGC does not get approved (Tr. pp. C-207-C-208)

If NGC is approved, it has committed to contribute not less than \$1 billion to Alliance Transco to be used to: fund startup cost reimbursements and working capital requirements; make capital contributions to fund projected system-wide capital expenditures or additional working capital needs; and, make subsequent capital contributions in connection with contribution of transmission facilities to Alliance Transco. (Jt. Pet. Alliance JCB-S, p. 6). NGC will be reimbursed of compensation and benefits expenses incurred by it; receive an annual management fee of \$14 million adjusted annually; and a percentage of incentives earned under performance-based rates and other incentive based compensation. Certain of the incentive-based compensation may be netted

against the annual management fee. (Jt. Pet. Alliance JCB-S p. 6-7).

Further details on Joint Petitioners' submission are presented in context later in this order.

### **III. Effects of the Joint Petition on the Public Interest**

#### **A. Introduction and Overview**

The transmission facilities at issue in this case are integral to the provision of reliable, efficient electric service to retail customers in Indiana. Their importance to our state requires the Commission to consider carefully the implications of the proposed transfer, both short-term and long-term.

In Indiana, it has long been a fundamental principle that public utilities must furnish reasonably adequate service to customers at reasonable rates. IC § 8-1-2-4. Indiana utilities must be reliable and efficient. Providing reliable, efficient service means acquiring power supplies efficiently, either by building generating plants or acquiring generation resources in wholesale power markets. Thus the ability of utilities to carry out their responsibilities depends heavily on the efficiency and competitiveness of wholesale power markets.

Throughout the electric industry there is a growing recognition that transmission policy is central to the efficiency, reliability and competitiveness of wholesale power markets. Transmission access, pricing, operations, planning and construction all require attention. Particularly relevant to the present case is the growing recognition that power supply markets are regional markets. As power supply markets are regional, then transmission policy must also be regional.

Over the past five years, it has become increasingly apparent to the Commission that the institution necessary to assure regional transmission service is the regional transmission organization. Most prominently, the Federal Energy Regulatory Commission ("FERC"), beginning in late 1999, issued a series of orders that strongly encouraged electric public utilities subject to its jurisdiction to join an operational FERC approved RTO by December 15, 2001.

This Commission shares the central goal set forth in these orders: the evolution of efficient, effectively competitive regional power supply markets, and the development of transmission practices necessary to assure that evolution. We expect our utilities to act consistently with that goal.

Whether the transfer of Indiana transmission assets to an RTO serves the public interest depends heavily on the RTO's internal design and readiness to start operation. To ensure that reliable service will be provided to Indiana customers, the RTO must have developed an efficient and reliable infrastructure and operating practices. In order to ensure reasonable costs and effective generation competition in the markets serving the State, the RTO must have governance that is independent of any market participant, and must rely on a fully participative stakeholder advisory process. Moreover, the market rules should be well understood and provide sufficient transparency to assure

market participants, as well as the Commission, that access to the transmission highways will be "fair" in both fact and perception.

However, an adequate internal design, in and of itself, cannot address all issues that must be considered by an RTO. An RTO must have relations with neighboring RTOs that assure seamless markets. Even subtle differences in operational practices, definitions, communications equipment, hardware and software could cause severe problems with seams.

In the subsections that follow, the Commission will apply these principles to the proposals before it, focusing specifically on (1) reliability of service to Indiana customers, (2) financial viability of the RTO, (3) impact on competition and costs, (4) coordination with other RTOs and other transmission owners (the "seams" issue) and (5) responsiveness to the public's needs.

## **B. Reliability of Service to Indiana Customers**

### **1. The Relationship Between RTOs and Reliability**

Formation of a regional transmission organization can have a variety of reliability benefits, including:

- i. Improved coordination of multi-company operations, which will decrease transmission loading problems;
- ii. Ability to import economical power from a wider region;
- iii. A broader, more regional approach to security coordination and the calculation of available transmission capacity (ATC);
- iv. An improved ability to coordinate generator outages that might otherwise adversely affect the transmission system;
- v. Improved coordination of merchant plant operation; and
- vi. Increased options available to operators to respond to system loading problems.

(Jt. Pet. Alliance Ex. JCB, pp. 16-17.) and (MISO Ex. C, pp. 27-28.).

RTOs can and should enhance the reliability of our region's electric systems. Effective coordination of power supply on a regional basis should improve both short and long-term reliability. A specific indicator of improvement to short-term reliability, including system security, should be a reduction in the incidence of TLRs. TLRs are issued in different levels. The initial stages are merely notifications to transmission users that the system conditions are such that transmission constraints may occur. Final stages involve actual curtailment of transactions. The TLR procedure,



introduced by North American Electric Reliability Council ("NERC"), is a step-by-step procedure to maintain network security by avoiding or relieving transmission overloads. It is used to mitigate potential or actual violations of the operating limits on the transmission system. The TLRs are issued by a Security Coordinator who has the responsibility and authority to direct actions aimed at maintaining real-time security for a control area, group of control areas, NERC subregion, or NERC region. The TLR identifies the actual transactions causing Operating Security Limit violations, and then considers the actual paths over which transactions are flowing to determine which transactions to freeze or curtail.

The testimony in this Cause demonstrates that recent years have seen an increasing number of TLRs in this region. (Jt. Pet. Alliance JCB-1 pp. 15-17). While most TLRs are warnings and do not ultimately necessitate a curtailment of transactions, the mere issuance of TLRs has a deleterious affect on the power markets by limiting transactions that could have enhanced market efficiency. While reliability is the impetus for a Security Coordinator to curtail transactions, or even issuing warnings that there is a potential that transactions could be curtailed, there are obvious commercial implications associated with transactions that are curtailed as well as those transactions that are not consummated for fear of curtailment.

RTOs would increase reliability in the long term as well, by improved planning and better coordination of enhancements to the power supply system, thereby attracting new supply. An RTO can manage congestion on a price basis providing the requisite price signals to generators, customers and transmission investors that induce (a) enhancements to the transmission system; (b) construction of new generating facilities in locations most likely to relieve congestion on the grid; and (c) demand-side management in the form of interruptible load, direct load control, indirect load management.

Whether these benefits will accrue from a transfer of Indiana transmission assets to an RTO depends on whether the RTO (a) is capable of operating the to-be-transferred assets, and functionally able to assume control of them; and (b) is able and willing to coordinate its operations with neighboring RTOs and other transmission owners. Conversely, a transfer of transmission assets to an entity that is unprepared or unable to operate them, or unable or unwilling to coordinate with other RTOs or other transmission owners, will not be consistent with reliable service in Indiana. In this section, we address the internal RTO issues; in a later section we will address the matter of inter-RTO coordination.

## **2. ARTO's Internal Readiness**

Internal readiness depends on whether the operational infrastructure is in place, whether the RTO is ready to operate and has successfully completed market trials, and whether the RTO is in compliance with applicable regulations.

**a. Infrastructure**

Mr. Baker testified:

"The Alliance RTO is not planning to build a large infrastructure including a single, all-inclusive control center like other ISOs have done. Instead, the Alliance will rely on service providers, new technologies, development of robust communication systems, and adequate and redundant hardware/software between the ARTO, service providers and control areas. This will ensure reliable and efficient operation while fostering innovative ideas to reduce costs."

(Jt. Pet. Alliance JCB-R pp. 13-14).

Mr. Baker also sponsored the *Alliance Companies Report and Update on IRCA implementation*, dated October 9, 2001, ("Alliance Report") which has been filed with the FERC. He testified that the report indicated that:

The operational systems of Alliance Transco are based on computer systems with built-in multiple redundancies that allow for decentralized, distributed operations and which permit adaptation to changes required by the independent decision maker or necessitated by evolution in the marketplace. This philosophy was captured in the expression Alliance RTO: ready to operate with clicks not bricks.

(Jt. Pet Alliance JCB-R4 p. 24).

According to Mr. Baker, Siemens Power Transmission and Distribution Inc., ("Siemens") is hosting all of these applications, in addition to others necessary to the provision of regional transmission services, in a secured computer facility. (Jt. Pet Alliance JCB-R4, pp 25-26) The contracts with Siemens and other vendors are assignable to Alliance Transco at its option and can be concluded within three years, although there are options to extend the contracts for an additional period of two years. Siemens is also managing an Enterprise Integration Bus that is used to fully automate the exchange of transmission information with the transmission functions of the Alliance Companies. The Siemens facilities are based in Minneapolis, Minnesota. (Tr. pp. C-240-241).

Mr. Baker explained that the independent manager, National Grid, if approved by FERC, could reverse these actions already taken by the Alliance companies and build a different infrastructure. (Tr. pp. C-262-265).

**b. Market Trials**

Mr. Baker testified that BridgeCo was established to facilitate implementation of the infrastructure, and that BridgeCo has conducted market trials for the Alliance companies. System tests of customer registration, Open Access Same Time Information System ("OASIS"), tagging and

supporting applications began on July 9, 2001, and are now completed. On August 23, 2001, Phase 1 of the operation trials, which involve integration and testing of the Alliance RTO systems with the corresponding Alliance companies systems, were initiated. Phase 2 of the trials will involve market participants, followed by Phase 3, which will include additional market participant involvement. Mr. Baker testified that while BridgeCo may be slightly behind MISO in its operation trials, the infrastructure for Day 1 operation is being developed over a one (1) year period. (Jt. Pet. Alliance JCB-R, pp. 17-18).

The Commission notes that while Mr. Baker's testimony provided a general overview of the status of the Market Trials, the Joint Petitioners failed to present any specific details with respect to the conduct of the Market Trials, including whether any follow-up was necessary. It is important to know if concerns were raised by the Alliance companies that participated in the trials, BridgeCo employees, vendors, or other stakeholders in terms of the communications systems, computer systems, software, procedures, implementation ramifications. No evaluation, or objective framework, was offered with respect to any of the aspects of the tests. In the end, we don't know if, by an objective measure, the testing was successful. In addition, the Joint Petitioners only offered sketchy testimony with respect to the number, or role of any specific employees, and did not indicate whether any employees that are currently in place had taken part in the market trials in an effort to fully understand the system. (Tr. C-231). We found the Joint Petitioners' responses to the Presiding Officers data request of August 2, 2001 regarding market trials to be less than satisfactory.

#### **c. Conclusion on Internal Readiness**

Based on the evidence presented, the Commission finds that ARTO's operational readiness is clouded by fundamental uncertainties. In a system such as that described by Mr. Baker, where much of the activities are contracted out by the RTO to other organizations under short-term contracts, where there is no central physical infrastructure and no central personnel infrastructure in which training, career development and long-term institutional commitment can occur, such uncertainty about operations and personnel is not consistent with Indiana's short or long term interests. These unresolved issues lead to obvious uncertainties regarding the current nature, structure, and attendant costs of the entity that is to assume functional control over a substantial portion of the transmission system in Indiana. The uncertainty increases immeasurably upon Mr. Baker's statement that National Grid, if approved as managing member of the ARTO (or presumably any other future managing member), could reverse many features of the structure described by Mr. Baker in this proceeding. (Tr. pp. C-262-265).

This uncertainty involves not merely specifics about personnel, procedures and resources; it is uncertainty about leadership and vision. We cannot entrust critical transmission facilities -- facilities whose costs have been historically recovered from Indiana ratepayers, whose daily operation and adequacy are critical to provision of reliable service and whose long-term sufficiency is vital to the state's economic future -- to an unknown operational leadership, working in an environment consisting of short-term contracts, unknown staff development procedures, and non-existent career ladders. Once the Commission approves the transfer, our jurisdiction becomes shared with the FERC's. This jurisdictional sharing occurs when the functional control of the

transmission assets move from utilities providing bundled, state jurisdictional retail service to an RTO providing unbundled, FERC jurisdictional transmission service. Given this, we must know what will become of these assets.

The Joint Petitioners in this case have simply failed to inform us about the present let alone persuade us that their recommended future is in Indiana's interests. While Mr. Baker described efforts to overcome these hurdles, that evidence does not dispel the pervasive vagueness in his presentation. The Joint Petitioners' evidentiary efforts come uncomfortably close to a leap of faith, and that we cannot take, at least consistent with our statutory duties to protect the public interest.

The record contains Mr. Baker's statement in which he indicates that, assuming the FERC gave approval to National Grid as the Alliance RTO's independent manager, the system could become operational on March 6, 2001. (Tr. C-166-170). But for the Commission, the question is not whether readiness will occur in 3 months or 4 months or in some other time period. The question is whether this record supports a finding that the public interest will be protected by authorizing the transfer of control of infrastructural assets to a collection of organizations with no stated history of collaboration, connected by short-term commercial contracts not subject to this Commission's oversight, whose operational personnel are unidentified, whose career ladders and training protocols are unknown. Indeed, the very fact that an applicant would ask for approval under these circumstances creates for us concerns about credibility, because it implies a lack of recognition of the seriousness of our regulatory task.

We wish to be clear. The problem is not merely the paucity of supporting evidence, e.g., the absence of witnesses from Siemens or BridgeCo, the absence of specifics on how the systems will work and how they were tested, the absence of information on how National Grid might change most of what Mr. Baker described. The evidentiary gaps, by themselves, are sufficiently large to require a finding that the Joint Petitioners have not met their burden of proof. But to say no more would be to imply that Commission approval will be forthcoming as soon as the evidence comes in. We mean to say more: that dispersed infrastructure, managed by shifting entities with short-term contracts, all planned by decision makers who, it appears, underestimate seriously the magnitude of our regulatory responsibility, is not a model to which this Commission will entrust vital infrastructural assets.

#### **d. Regulatory Compliance**

Transmission services provided by the ARTO, and contracts related thereto, are subject to the FERC's jurisdiction under the Federal Power Act. The history of the ARTO's proposal at FERC, as recorded in FERC's public decisions, raises additional questions about this organization's consistency with Indiana's interests.

While the FERC has determined that certain portions of the Alliance RTO meet the FERC's standards under FERC Order No. 2000, certain other aspects of the Alliance RTO have not yet been approved by the FERC. As of the date of the hearing in this Cause, FERC had not ruled on the Alliance RTO's business plan, and BridgeCo is mostly performing startup activities. The Alliance companies created BridgeCo as a limited liability corporation to finance and perform certain

operational activities until a managing member was established. (Tr. pp. C170-C171).

**(i) FERC Treatment of Alliance Orders:** On December 20, 1999, the FERC issued an order conditionally authorizing the Alliance RTO transmission owners to transfer functional control of their transmission facilities to the Alliance. *Alliance Companies, et al.*, 89 FERC 61,298 (1999) ("*Alliance I*"). The FERC noted that the proposal could provide significant benefits to the industry and consumers if certain aspects of the proposal were modified or further developed. FERC was troubled by the geographic configuration, which in FERC's view appeared to have strategic implications. Specifically, the Alliance's boundaries would separate buyers and sellers that constitute the predominant east-west trading patterns, and thus allowing the Alliance transmission owners, who also owned and traded generation, to behave as a tollgate. (89 FERC at p.61, 928).

The FERC also found that the Alliance Companies did not meet the Commission's independence standard, because Alliance Companies ownership of up to 25 percent of "Alliance Publico's" stock at formation could allow the Alliance Companies to effectively control of Alliance Publico. Also, the FERC found that the proposal would not prevent control, and the appearance of control, of decision-making by any class of participants, a standard associated with the FERC's "independence" requirement. (89 FERC at 61, 918).

In response to the requirements of *Alliance I*, the Alliance RTO transmission owners made a compliance filing on February 17, 2000. On May 18, 2000 the FERC issued an order, *Alliance Companies, et al.*, 91 FERC para. 61,152 (2000) ("*Alliance II*"), which accepted the compliance filing but required some modifications. FERC directed that further filings be made and reiterated elements of the specific guidance previously offered in *Alliance I* relating to independence and governance, rate design, scope and configuration, congestion management and redispatch and coordination with neighboring control areas.

Specifically, the FERC in *Alliance II* found that the Alliance Companies had not revised their proposal for active ownership of Alliance Publico, as required by *Alliance I*. The FERC found that the Alliance Companies sought to justify their 25 percent ownership level largely on the arguments made in their original filing rather than justify their proposal based on guidance provided in Order No. 2000. Furthermore, the FERC directed the Alliance Companies to address the independent audit requirement with respect to Alliance Transco. (91 FERC at 61,580-81).

On September 15, 2000, the Alliance Companies filed another compliance filing to comply with the FERC's directives in *Alliance I* and *Alliance II*. The compliance filing contained a proposal to create a for-profit transmission company or Transco in compliance with FERC Order No. 2000. On January 24, 2001, the FERC ruled on these compliance filings. *Alliance Companies, et al.*, 94 FERC para. 61,070 (2001) ("*Alliance III*"). The FERC found that the Alliance Companies filing basically met the four characteristics and most of the functions discussed in Order No. 2000, but directed further modifications. In particular, the FERC stated:

"The processes that stakeholders can use to communicate and consult with an RTO should be developed in consultation with stakeholders. If RTOs are to be responsive

to the needs of the market, there must be a meaningful and efficient process for communication and consultation that serves not only the needs of the RTO, but also the needs of stakeholders. We believe that requiring Alliance to unilaterally propose these processes and having the Commission direct changes in processes based on comments of stakeholders is not the best way to develop workable processes for stakeholder communication and consultation. We believe a better way is for the Alliance Companies to develop an advisory process in consultation with stakeholders, and to describe that advisory process and identify the participants. Only if they cannot will the Commission step in."

(94 FERC at 61,304).

On January 16, 2001, the Alliance Companies submitted their FERC Order No. 2000 compliance filing in Docket No. RT01-88-000. In an order issued July 12, 2001, the FERC conditionally approved Alliance Companies RTO filing subject to the following conditions:

A. RTO Characteristic No. 1: Independence

The Alliance Companies' revised proposal presented two alternatives. Under the first alternative, an outside investor, not known or identified, would both own and control transmission facilities within Alliance. The FERC stated that if the outside investor was not a market participant, and if the outside investors and not market participants would actually control Alliance, the FERC's concerns about independence would likely be reduced. However, the Alliance Companies did not identify the strategic investor(s), so the FERC was unable to rule definitively. (Slip op. at p.12).

Under the second proposal, Alliance Companies would form the Publico Corporation themselves, and seek one or more strategic investors to provide capital investment. FERC found that if the strategic investor were not a market participant and actually controlled Alliance, its concerns about independence would likely be reduced. However, the Alliance Companies did not identify the outside investor. (Slip op. at 12).

The FERC also said:

"We are concerned that business decisions prior to implementation of an Alliance RTO are being made by Alliance Companies. Therefore, we direct Alliance Companies to decide which of the alternative business plans proposed they intend to implement within 45 days of this order. We further direct that from the date of this order an independent board be established to make all business decisions for the RTO. Until final RTO approval is granted, a stakeholder advisory committee should advise the independent board." (Slip op. at 13).

B. RTO Function No. 1: Tariff Administration

The FERC directed the Alliance Companies to file their actual rates 120 days prior to

commencement of operations and stated that this filing should address all outstanding tariff issues. (Slip op. at 19).

C. RTO Function No. 2: Congestion Management

The FERC stated that the Alliance Companies' long-term congestion management proposal was still a "work in progress," leaving FERC without enough information to rule on its appropriateness. (Slip op. at 21).

D. RTO Function No. 3: Parallel Path Flow

The FERC stated that the Alliance Companies had not responded to the Intervenor's concerns about the need to develop a way of compensating small transmission owners for the use of their system. (Slip op. at 24).

E. RTO Function No. 4: Ancillary Services

The FERC noted the Alliance Companies proposal was a "work in progress" and directed the companies to finalize the tariff filing 120 days prior to the Alliance transmission service date. FERC also directed the Alliance Companies to step up their efforts to insure that all stakeholders have adequate input in the development of the final proposal. (Slip op. at 27).

F. RTO Function No. 5: OASIS and Total Transmission Capability and Available Transmission capability

The FERC again directed the Alliance Companies to file the system of tests and checks to ensure the reasonableness of data they propose to use, consistent with the requirements of Order No. 2000 for verifying ATC/TTC-related data. (Slip op. at 28-29).

G. RTO Function No. 6: Market Monitoring

The FERC found that the Alliance Companies did not file their market-monitoring plan with the necessary detail. (Slip op. at 31).

H. RTO Function No. 7: Planning and Expansion

FERC found the Alliance Companies failed to support eliminating the Operational Planning Committee ("OPC") and revisions made to the Reliability Planning Committee ("RPC"). The FERC directed the Alliance Companies to refile the Planning Protocol without those changes or with detailed reasons for eliminating the OPC and how the RPC will ensure adequate representation for all stakeholders. (Slip op. at 33).

I. RTO Function No. 8: Interregional Coordination

The FERC deferred ruling on this issue until the final mechanisms have been agreed upon in the FERC approved settlement agreement in Illinois Power Company, FERC Docket No. ER01-123-000 establishing the terms for a cooperative relationship between the MISO and ARTO, including how a seam issues will be dealt with by the two RTOs. (Slip. op. at 35). The FERC ultimately approved the settlement in that case.

J. Other Issues: Customer Advisory Process

The FERC stated (slip op at 38):

Although we note that Alliance Companies have made significant progress as evidenced by the information on its website, we still have serious concerns over the effectiveness of the stakeholder processes. Stakeholders should have input into aspects of RTO formation necessary to ensure that the RTO develops practices that produce a seamless, well-functioning marketplace. While we do not wish to micro-manage the stakeholder process, Alliance must have a useful stakeholder process. Since the stakeholder processes are the key to resolving many of the issues that are still facing Alliance Companies, Alliance Companies must resolve this issue immediately. We agree with Intervenors that there are many significant issues outstanding which need to be resolved in a timely manner. While resolution of some of these issues is not required for Day One operations, they do involve significant market related matters that should not be decided without input from all affected stakeholders.

**(ii) ARTO Filings Related to National Grid:** On August 27, 2001, the Alliance Companies submitted a supplemental compliance filing which provides their initial business plan for the Alliance RTO. The Alliance Business Plan ("Alliance Business Plan") was filed in response to the directive contained in the FERC's July 12, 2001 order, which instructed them to specify within 45 days, the initial business structure for the Alliance RTO. The Alliance Business Plan compliance filing included a term sheet and letter of intent between the Alliance Companies and National Grid pursuant to which those entities would negotiate definitive agreements for National Grid to become the Managing Member of the Alliance Transmission Company. A direct or indirect subsidiary of National Grid would become the manager/operator of Alliance Transco. Under the proposal the managing member would direct the business and affairs of the Alliance Transco. NGC would serve as managing member for an initial term of seven years. Its term would thereafter be extended for successive two-year terms unless notice of termination is given by NGC or a majority of the holders of the voting units in Alliance Transco. (Jt. Pet. Alliance JCB-S, p. 5).

The August 27, 2001 compliance filing also included a proposal to establish an interim three-member board of trustees that would be authorized to make business decisions for the Alliance RTO until such time as the National Grid is approved by the FERC to become the managing member. (Jt. Pet. Alliance JCB-S, p. 9).

**(iii) ARTO Filings Related to Advisory Process:** On October 12, 2001, the



Alliance filed an Offer of Settlement with the FERC, entitled "Principles Of Agreement For The Formation Of The Stakeholder Advisory Committee." Jt. Pet. Alliance JCB-R3). This settlement was the direct result of the involvement of FERC's Dispute Resolution Service (DRS).

**e. Conclusion on Regulatory Uncertainties**

We cite the foregoing history not for purposes of adopting the specific findings made by the FERC, but to provide the basis for one of our concerns: the uncertainty to Indiana's transmission future caused by ARTO's regulatory relations. For ARTO's regulatory past is a controverted one, consisting of a significant number of failures to adhere to regulatory standards, requiring reminders, and a great deal of patience from its chief regulator. Its regulatory omissions tended to fall, in the FERC's stated view, on the side of too little responsiveness to the goals of seamless competition, independence, and stakeholder participation.

While this history of regulatory difficulty speaks clearly on its own, the concerns it creates for us grow larger in the context of this proceeding, in which Joint Petitioners' witnesses offered generalities when specifics were requested. This context provides a reasonable basis for concluding that the regulatory difficulties of the past will continue in the future. We readily acknowledge that there is not certainty that the future will resemble the past. Certainly an independent manager, if one arrives and is approved, may deal differently with these issues. But the Commission may make reasonable judgments based on reasonable predictions rooted in the record. In this situation, the new independent manager would be handpicked by the Alliance Companies; through a private process culminating in a contract whose renewal would be discretionary with the Companies. While there certainly will be a subsequent public process at the FERC to review the contract and any renewal thereto, it is reasonable to assume that the Alliance Companies would favor selection of an independent manager that the Alliance Companies viewed as responsive to their concerns. For that reason we cannot assume that regulatory uncertainties would automatically disappear on entrance of an independent manager. Indeed, the ARTO-NGC filing of August 27, 2001 has attracted protests. (Tr., pp. D-207-D-208). We cite the fact of these protests not because we necessarily agree with them; we recognize that many filings at FERC attract protests. But we are concerned that the level of controversy over the ARTO is not diminishing, after almost three years. As we discuss later in this order concerning the issue of ARTO responsiveness (*see*, Part F: Responsiveness to the Public's needs below), we have similar concerns in the area of the Stakeholder Advisory Committee.

We also recognize that FERC's RTO policy is itself a "work in progress," and that ARTO may seek to attribute its past regulatory difficulties to that source. We have carefully reviewed the FERC decisions with that possibility in mind, and respectfully conclude otherwise. We see in the FERC decisions a tendency in the Alliance Companies toward unresponsiveness to regulatory requirements, when they conflict with the ARTO members' business aims. The messages on independent governance and stakeholder participation were consistently clear from the FERC. It was not changes in FERC policies, but the ARTO companies' responses to those policies, that produced the repeated conditions and statements of concern from FERC. We wish not to have our state's transmission assets subjected to this type of time-consuming and uncertain regulatory relationship.

The Commission may, in its discretion, consider relevant history and make reasonable extrapolations about the past. We do so here, and find it does not serve Indiana to move its transmission assets to an organization that consistently experiences regulatory difficulty of the type and intensity that the ARTO has experienced.

As this order is issuing before FERC acts again on the pending Alliance and NGC requests for approval, we do not know how our federal regulatory colleagues ultimately will act. FERC could find that the ARTO has eliminated all the concerns that have arisen over the past two years. The issue before this Commission is not whether the FERC approves or disapproves the ARTO. Our statutes and case law place reliability at the center of our responsibilities. We will not compromise that responsibility. While we strongly support RTOs as a way to maintain and improve reliability, we have no compulsion to see any particular RTO succeed. There are other options, which we will explore in a separate investigation.

### **C. Financial Viability**

For the Development phase of the Alliance RTO, the Alliance companies created BridgeCo as a limited liability corporation to finance and perform certain operational activities until a managing member was established. (Tr. C-170, C-171). The initial funding for BridgeCo is from the Alliance companies. In the August 27, 2001, business plan filing, the Alliance Companies notified the FERC that NGC will make an investment in, and serve as the managing member of, the Alliance Transco. If NGC is approved as managing member, it must establish and maintain its independence and refrain from taking any action that would cause it to lose its status as a non-market participant.

As to the financial position of NGC, the proposed managing member, the record indicates that it has committed to contribute not less than \$1 billion to Alliance Transco to be used to: (i) fund start-up cost reimbursements and working capital requirements, (ii) make capital contributions to fund projected system-wide capital expenditures or additional working capital needs, and (iii) make subsequent capital contributions to be made in cash in connection with contribution of transmission facilities to Alliance Transco. In return for these investments, NGC will receive reimbursement of compensation and benefits expenses incurred by it, an annual management fee of \$14 million, adjusted annually and a percentage of incentives earned under performance-based rates and other incentive-based compensation. Certain of the incentive-based compensation may be netted against the annual management fee. (Jt. Pet. Alliance JCB-R p. 6).

### **D. Impact on Competition and Costs**

#### **1. In General**

The FERC recognized in Order No. 888, (FERC Stats. & Regs. para. 31,036 at 31,682) that unduly discriminatory and anticompetitive practices existed in the electric industry. In that order the FERC stated:

It is in the economic self-interest of transmission monopolists, particularly those with high-cost generation assets, to deny transmission or to offer transmission on a basis that is inferior to that which they provide themselves. The inherent characteristics of monopolists make it inevitable that they will act in their own self interest to the detriment of others by refusing transmission and/or providing inferior transmission to competitors in the bulk power markets to favor their own generation, and it is our duty to eradicate unduly discriminatory practices.

Vertically integrated utilities have the incentive and the ability to provide their generation or affiliated marketers with more favorable treatment of transmission requests or more favorable access to transmission information than is provided to market competitors. The result is that these market competitors are unfairly disadvantaged. Retail customers are hurt because the wholesale power market is less competitive and efficient than it would otherwise be.

In FERC Order 2000, the FERC recognized that the perceptions of undue discrimination can cause considerable harm and stated that:

[W]e continue to believe that perceptions of discrimination are significant impediments to competitive markets. Efficient and competitive markets will develop only if market participants have confidence that the system is administered fairly. Lack of market confidence resulting from the perception of discrimination is not mere rhetoric. It has real-world consequences for market participants and consumers. As stated by NERC, there is a reluctance on the part of market participants to share operational real-time and planning data with transmission providers because of the suspicion that they could be providing an advantage to their affiliated marketing groups, and this can, in turn, impair the reliability of the nations electric systems. Lack of market confidence may deter generation expansion, leading to higher consumer prices.

FERC Order No. 2000, December 20, 1999, (slip op. at 69).

The FERC recognizes that an RTO or an ISO needs to be independent in reality and perception if the potential benefits of establishing these organizations are to be realized. Even the perception of unfairness or discrimination can have an adverse impact on the reliability of the nations' electric system. As a result, FERC has stressed the importance of a decision making process and governance structure that is independent of control by any market participant or class of participants. (*Id.* at p. 194).

The record shows that the potential benefits of the transfer include many relating to enhancing generation competition and reducing transmission costs. These benefits can include: (i) the elimination of pancaked transmission rates for deliveries into Indiana from within the ARTO or within the MISO/ARTO Super Region; (ii) access to a very large, and therefore more competitive generation market; (iii) common business practices within an RTO; (iv) implementation of

improved, and then later more sophisticated, congestion management systems, which will reduce the use of TLR procedures; (v) an energy imbalance market to physically and financially stabilize the delivery of power into Indiana; and (vi) an Independent Market Monitoring function that will be exceptionally broad in scope in the interests of protecting electric customers from gaming or market abuse. (Jt. Pet. MISO Ex. C, pp. 27-28.) and (Jt. Pet Alliance Ex. JCB, pp.16-17).

Moreover, reductions in both generation and transmission costs will arise from: (i) improved coordination of transmission planning, resulting in reduced environmental impact and minimum cost solutions; (ii) a broader list of options to improve the Transmission System; (iii) improved coordination of interconnection studies among multiple companies; and (iv) a more regional evaluation of the impact of siting merchant generation in and around Indiana. (Jt. Pet. MISO Ex. C, pp. 27-28).

The question is whether the transfer of Indiana transmission assets to the ARTO can realize this potential. We analyze this question further in the subsections that follow. More detail follows, focusing specifically on the need for an independent board.

## **2. Independent Board**

A transfer of transmission asset control from an Indiana utility to an RTO cannot be consistent with the public interest unless the management of the RTO is independent of market participants. On this subject, as with the subject of reliability and readiness, the ARTO history gives us concern.

### **a. The Alliance Companies' Initial FERC Filings**

On December 20, 1999, in the *Alliance I* Order, the FERC found that the Alliance proposal did not meet Order No. 888's and FERC Order No. 2000's independence standard because the Alliance Companies could own as much as 25 percent of the Alliance Publico's stock at formation that could allow the Alliance Companies effective control of Alliance Publico. The FERC also found that the proposal would not prevent control, and the appearance of control, of decision-making by any class of participants. (89 FERC at p. 61, 918.)

On May 18, 2000, in the *Alliance II* Order, on review of the compliance filing required by *Alliance I* the FERC found that the Alliance Companies had not revised their proposal for active ownership of Alliance Publico. FERC noted that the Alliance Companies sought to justify their 25 percent ownership level largely on the arguments made in their original filing rather than justify their proposal based on guidance provided in Order No. 2000. (91 FERC at 61,580-81).

On September 15, 2000, the Alliance Companies made another compliance filing that contained a proposal to create a for-profit transmission company or Transco in compliance with Order No. 2000. In a January 16, 2001 compliance filing under FERC Order No. 2000, the Alliance Companies described two alternative approaches to achieving the independent governance required by FERC Order No. 2000. The first was the identification of an outside, non-market participant

investor that would both own and control transmission facilities within the Alliance and would serve as the managing member of the Alliance Transco. The second option was to find a financial-only investor to provide capital to a newly-created corporation that would serve as managing member of the Alliance Transco.

The FERC's July 12, 2001 Order found that either proposal would reduce the FERC's concerns about independence if the investor, in either case, was not a market participant and that the investor would actually control Alliance. However, the Alliance Companies failed to identify the investors so FERC was unable to rule definitively. Slip op. at 12.

The FERC also stated in its July 12, 2001, Order:

"We are concerned that business decisions prior to implementation of an Alliance RTO are being made by Alliance Companies. Therefore, we direct Alliance Companies to decide which of the alternative business plans proposed they intend to implement within 45 days of the date of this order. We further direct that from the date of this order an independent board shall be established to make all business decisions for the RTO. Until final RTO approval is granted, a stakeholder advisory committee should advise the independent board."

(94 FERC para. 61,363 at p. 62,325 (2001).

#### **b. The Alliance Companies' Current FERC Filings**

On August 27, 2001, the Alliance Companies submitted to the FERC a supplemental compliance filing describing their initial business plan for the Alliance RTO. The filing included a term sheet and letter of intent between the Alliance Companies and National Grid, pursuant to which those entities would negotiate definitive agreements for National Grid to become the Managing Member of the Alliance Transmission Company. A direct or indirect subsidiary of National Grid would become the manager/operator of Alliance Transco. Under the proposal the managing member would direct the business and affairs of the Alliance Transco. NGC would serve as managing member for an initial term of seven years. Its term would thereafter be extended for successive two-year terms unless notice of termination is given by NGC or a majority of the holders of the voting units in Alliance Transco. (Jt. Pet. Alliance JCB-S, p. 5)

The August 27, 2001 compliance filing also included a proposal to establish an interim three-member board of trustees that would be authorized to make business decisions for the Alliance RTO until such time as the National Grid is approved by the FERC to become the managing member. (Jt. Pet. Alliance JCB-S, p. 9)

#### **c. Concerns**

FERC has stated that "an RTO must be independent of any entity whose economic or commercial interests could be significantly affected by the RTO's actions or decisions. Without such

independence, it will be difficult for an RTO to act in a non-discriminatory manner." (FERC Order No. 2000, slip op. at 195).

Mr. Dauphinais noted that before National Grid can become the managing member, the company will have to demonstrate to the FERC it is a non-market participant. (IIG-1 at 22) Mr. Dauphinais explains why FERC approval of NGC as a non-market participant is "problematic". He explained that National Grid owns the former subsidiaries of the New England Electricity System. In addition, NGC is in the process of acquiring Niagara Mohawk Power Corporation in New York. (IIG Ex. 1, p22). Due to these existing and pending acquisitions, National Grid currently has ownership interests in the power merchant business. (Jt. Pet. Alliance JCB-S, p. 4). In addition, National Grid owns distribution facilities of the acquired entities and has a role as retail provider of last resort in certain states in New England and New York. (IIG Ex 1.p. 22). According to Mr. Dauphinais, there are some concerns that even if NGC divested itself of its power merchant business interests, it would still be a market participant due to its role as a retail provider of last resort. That is, NGC could favor transmission of power over the ARTO toward the Northeast to the benefit of its distribution interests at the expense of other transmission customers in the region. (IIG Ex 1, p 22).

Mr. Baker stated that NGC was in the process of divesting their interests in the production and marketing of electricity. He also stated that the process was not complete so NGC retained certain minor residual interests in the power merchant business with respect to the companies it has acquired or is acquiring in New England and New York. (Jt. Pet. Alliance JCB-S, p. 4).

On August 27, 2001, National Grid made a compliance filing in Docket No. EL01-80-000 detailing its plan to complete divestiture of, or to transfer to a non-affiliated third party, the economic interests that its affiliates retain in the power merchant business and to be independent of all such market interests. (Jt. Pet. Alliance JCB-S, p. 4).

As with other aspects of the ARTO approval process at FERC, uncertainties persist. Most prominent is whether FERC will (a) determine that NGC is not a market participant, (b) and approve the NGC-ARTO agreement, over the numerous protests, expeditiously. ARTO also has no backup plan should either of the preceding two conditions fail. These concerns, plus the absence of any direct evidence from NGC in this proceeding, create too much uncertainty. Under the NGC-ARTO scenario, the transfer whose approval is sought here, from I&M and NIPSCO to ARTO is really a transfer to NGC's functional control. There is no evidence in the record directly from NGC. The Commission cannot responsibly approve a transfer under these circumstances. There are too many unresolved issues to allow the Commission to protect the public interest.

Several years after the Alliance Companies began working on their organization, they remain unable to show compliance with the most fundamental of RTO requirements: independence. The Commission can reasonably assume that the Companies would have achieved independence if independence were their priority. This lack of commitment to a goal necessary to Indiana's electricity future precludes us from approving the relief requested by the Joint Petitioners.

**E. The Seams Issue: Coordination With Other RTOs and other Transmission Owners**

**1. Overview**

**a. Seams in General:** Whenever there is more than one RTO within an interconnected area, the issue of "seams" arises. While there is no official definition of this term, commenters have noted two types of seams issues: reliability practices across seams and market practices across seams. (See, FERC Order No. 2000 at text following note 349). Seams are eliminated when there are, for example, "coordinated operations and consistent methods of access, pricing, and congestion management...." (*Id.* at text preceding note 368). In addition to seams relating to operations, seams can develop in ways that are less obvious but no less important to the efficient and reliable functioning of the wholesale power markets. Differences between RTOs over governance structures, stakeholder involvement and incentive structures (such as incentives relating to the construction of transmission facilities) also can be impediments to trade.

Hils articulated that there is an inherent "co-dependence" between the MISO and the Alliance RTO. Differences in operations or rules between the two have the potential to create a dysfunctional market. (Hils at Tr. C-73) and (Jt. Pet. MISO Ex. E, p. 5). As more than one witness observed, even subtle differences in operational practices, definitions, communications equipment, hardware and software could cause severe seams problems. As MISO witness Snead said: "Especially when you go to...an overall single market design for a region, small – very small subtle differences between the market designs can cause events to occur that you don't anticipate." (Tr. C-110). With regard to subtle differences being critical, the experience of the Northeastern Independent System Operators' inability to resolve relatively minor seams problems was cited. (IGG Ex. 1. p. 14). The experience of the northeastern systems is particularly salient because they evolved from "tight" power pools where there was a history of considerable cooperation. In contrast, utilities in the Midwest were participants in "loose" power pools with very little coordination.

The FERC's concern with seams led it to include the following "minimum function" requirement in Order 2000: "The Regional Transmission Organization must ensure the integration of reliability practices within an interconnection and market interface practices among regions." (18 C.F.R. §. 35.34(k)(8)). This obligation, while not requiring identical practices between RTOs, does require "compatible" practices. In short, "RTOs must coordinate their practices with neighboring regions to ensure that market activity is not limited because of different regional practices." (FERC Order No. 2000, slip op. at p.510). In discussing the seams issue in this proceeding, the Commission recognizes that seams management does not require a perfect market with no inconveniences, for there are no perfect markets. However, the Commission recognizes that there should not be any artificial barriers to efficient trading created by the failure of coordination between MISO and Alliance RTOs.

**b. Seams in Our Region: The *Illinois Power* Case and the IRCA:** The boundary between MISO and Alliance splits large portions of the Midwest market. This fact received widespread recognition in late 2000, when three MISO members (Illinois Power Company,

Commonwealth Edison Company and Ameren Corporation) announced their intent to withdraw from the MISO in order to participate in the Alliance RTO, and made filings at FERC accordingly. This departure would mean that ARTO members would surround the Indiana members of the MISO on three sides, drawing a line at roughly the northern third, and isolating not only the Indiana members of MISO but also the MISO members in Ohio, Illinois, and Kentucky. The withdrawal thus would cut the MISO into two separate, unconnected segments, threatening MISO's viability in terms of its operational capability, its financial viability, its ability realize economic efficiencies and its ability to comply with the FERC Order No. 2000 requirements for geographic scope. (Jt. Pet. MISO Ex. C, pp. 14-15); and (Jt. Pet. MISO Ex. A, p. 4).

In response to these and other concerns raised by Intervenor in the three utilities' FERC cases, FERC consolidated the three cases in *Illinois Power, et al.* FERC Docket No. ER01-123-000 (the "Illinois Power Settlement Agreement"), and ordered a settlement conference. The resulting March 2, 2001 Illinois Power Settlement Agreement, ultimately approved by FERC, enabled the MISO, with its existing membership, infrastructure and staff, to remain viable. A copy of the Illinois Power Settlement Agreement was introduced into evidence in this proceeding as Jt. Pet. MISO Ex. C-1.

The Illinois Power Settlement Agreement included three significant features. First, the settlement resolved all terms and conditions necessary to permit the three Illinois companies to withdraw from the MISO, but required them to pay the MISO \$60 million -- a sum designed to fund the MISO's remaining startup costs. Second, the Agreement required the MISO and the ARTO to establish a single, nonpancaked rate methodology to apply to transactions from any source within the combined MISO/ARTO boundaries (MISO/ARTO Super Region) to any sink within the MISO/ARTO Super Region. Third, in response to concerns that the boundary between ARTO and MISO would contain "seams," the settlement includes an Inter-RTO Cooperation Agreement (IRCA). The IRCA commits the MISO and the ARTO (and, the Alliance companies, before the creation of the ARTO) to provide the basis for the development of a seamless market throughout the combined MISO-ARTO region, and to use the processes and timeframes contained in the IRCA to meet this objective in a timely fashion. (Jt. Pet. MISO Ex. C, p. 18.)

The IRCA provides that the MISO and the ARTO will develop procedures and protocols in several areas, including: (i) coordinated transmission planning; (ii) security coordination; (iii) congestion management; (iv) independent market monitoring; (v) accommodation of one-stop shopping; (vi) compatible real-time balancing markets; (vii) common generation interconnection agreement; (viii) compatible business practices; and (ix) dispute resolution procedures for resolving real-time operational disputes. (Jt. Pet. MISO Ex. C, p. 18.) The successful and timely implementation of the IRCA protocols and procedures in each of these areas is the key to assuring that the boundary between MISO and ARTO does not contain, or maintain, "seams" that impair efficient trading across the combined region. (Jt. Pet. MISO Ex. C, pp. 18-19.) In the subsections to follow, we address certain concerns raised about the IRCA process.



## **2. Deficiencies in the Operating Protocols**

Mr. Jackups testified that concerns remained among the MISO regarding the ability of the MISO and the ARTO to reach agreement on a sufficient level of detail on development and implementation of the IRCA-required protocols and procedures. Absent timely completion of these tasks, he stated, MISO startup still could occur, and reliability would not be compromised, but the desired level of seamlessness would not be achieved. (Tr. C-29)

Based on the concerns expressed by the MISO members, as well as his own analysis, Enron witness Michael Roan testified that the IRCA process has failed to resolve seams issues. He stated (Enron Ex. 1, p.8):

I make reference to the cooperative procedures and protocols as set out on the Alliance website...on October 5, 2001. A careful read of these protocols demonstrates that many of them are nothing more than agreements to develop systems or provide information at a later date. These documents contain little detail or substance. In the absence of further detail these documents will not achieve the intent of Settlement.

ARTO witness Craig Baker testified that the IRCA process was proceeding smoothly, and provided a report that he asserted supported his conclusion.(Jt. Pt. Alliance JCB-R, p.10) See, *Alliance Companies' Report and Update on IRCA Implementation: Building a Strong Foundation for a Seamless Market*, October 9, 2001, page 1. (Jt. Pt. Alliance JCB-R4).

## **3. Security Coordination**

FERC Order 2000 requires that each RTO provide its own Security Coordinator function on a regional basis. "Security Coordination" is intended to safeguard reliability by curtailing transactions in extreme instances during periods when the transmission system is at risk of overloading. Because electricity travels at speeds approaching the speed of light, instantaneous communications are essential to the ability of the Security Coordinators to handle real-time operations of the grid. While reliability is the impetus for a Security Coordinator to curtail transactions, or even issuing warnings that there is a potential that transactions could be curtailed, there are obvious commercial implications associated with transactions that are curtailed as well as those transactions that are not consummated for fear of curtailment. The ability to interrupt transactions vests considerable power in the hands of individual Security Coordinators. Because a Security Coordinator has the opportunity to favor transactions of its own RTO or member companies, it is essential that the use of the Security Coordination authorities be fairly administered and transparent to all of the market participants. Given the extraordinary complexity of the physical power flows involved in transactions, combined with the large commercial value of power transactions, errors, whether intentional or inadvertent, could go undetected. Remedies are time-consuming, expensive and uncertain.

The Alliance RTO proposes that its Security Coordinator will have three regional sites with the authority, responsibilities, and functionality to carry out Security Coordination in the Alliance

footprint. Mr. Baker testified that the three sites would be in constant communication with each other to provide seamless security coordination for the Alliance RTO. (Jt. Pet. Alliance JCB-1, pp. 13-14). The Alliance RTO Security Plan has been submitted to NERC for approval as a reliable mechanism for regional Security Coordination.

Mr. Hils testified that Security Coordinators must fully coordinate their activities to prevent adverse economic and reliability ramifications. Mr. Hils indicated that:

As consistent and effective coordination will be necessary between the Midwest ISO and the Alliance RTO, I am concerned that the expected security coordination scheme of multiple Security Coordinators within the Alliance RTO adds additional degrees of complexity to an already difficult task of coordination with the Midwest ISO. Absent one Security Coordinator for the Midwest region, it is my opinion that a single Security Coordinator for each RTO is the only other option that should be considered.

Mr. Hils went on to state that:

It is feasible and preferable to have a Security Coordinator over the Midwest region in daily operations and to assure proper coordination of any measures necessary to maintain the reliability of the interconnected system. More importantly, the Security Coordinator must have an effective means of managing congestion across the Midwest region without having to rely on implementation of TLR procedures. Having more than two Security Coordinators over the Midwest region forces a level of codependence under normal operations and complicates responses by the Security Coordinators in emergency conditions.

(Jt. Pet. MISO Ex. E, pp. 3-5).

In contrast to the detailed discussion of the potential short-term reliability concerns caused by multiple Security Coordinators presented in testimony by the MISO witnesses, Mr. Baker provided only vague assurances that the Alliance Security Coordinators will be able to coordinate with the MISO Security Coordinator on a real-time basis so that short-term reliability (primarily referring to System Security) will not be jeopardized by the Alliance RTO multiple Security Coordinator scheme. (Jt. Pet. Alliance JCB-1, pp. 13-15).

Notwithstanding the clear notice of the Presiding Officers' concern about security coordination, as set forth in their August 2, 2001 Docket Entry, Mr. Baker failed to provide a rationale for multiple Security Coordinators, and failed to indicate why a single Security Coordinator for the entire Midwest would not be preferable for managing congestion and maintaining reliability. Mr. Baker did not address the possibility that the use of multiple Security Coordinators would be duplicative and wasteful, and could be used by companies to the detriment of other market participants.

While the Alliance companies expressed confidence that ARTO can supply reliable Security Coordination for Indiana, the Commission is less sanguine. From the record before us it is unclear what the division of authority and responsibility is among the Alliance Security Coordinators. It is also not clear based on the testimony presented, how communication between the Alliance Security Coordinators and other RTOs will be accomplished in real time. The need for instantaneous communication and decision-making is crucial if the security of the transmission system is to be optimized. The Commission's longstanding support for RTO development has been, in large part, premised on the aspiration that RTOs will enhance reliability and reduce duplication and expense in the transmission of electricity. Therefore, the Commission is not content to maintain the status quo, or to the creation of a more cumbersome and duplicative process as part of this proceeding. Authorizing the transfer of responsibility for Indiana transmission assets to an organization with such a different view of Security Coordination from our own is not consistent with Indiana's interests.

#### **4. Congestion Management**

Congestion Management is a market-based mechanism to prevent reliability problems on the grid without having to resort to the use of TLRs or equivalent processes to curtail transactions. While TLRs can be a tool of last resort for RTOs, congestion management is a more efficient, robust means of relieving transmission concerns in advance of the real-time operations because it uses pricing mechanisms to accurately reflect the costs of the transmission congestion. Accurate pricing, in turn, will send appropriate price signals to the marketplace that discourage uneconomic transactions, encourage the construction of generation and transmission in locations that are limited by the transmission constraints, and encourage load control and consumer rate incentives to reduce usage during periods when the reliability of the power system is at issue. Ultimately, the success of any congestion management approach will be to enhance reliability and the economic value of transactions while minimizing the need for the RTO to physically curtail transactions.

The IRCA goal is a coordinated MISO-ARTO process. The IRCA looks at this from a short-term or "Day One" perspective, as well as a longer-term or "Day Two" perspective. With respect to Day One congestion management, under the IRCA both RTOs have agreed to utilize a joint bulletin board to post congestion management information, including generation shift factors and identification of facilities that are likely to be constrained. The IRCA calls for both RTOs to require all generators "to the extent necessary for inter-RTO congestion management purposes" to provide bids for emergency and market redispatch, to increase or reduce generation or loads on both sides of a constraint. In addition, the agreement contains other provisions that provide, at a high level, processes and procedures to be followed by the two RTOs. As of this time, the joint bulletin board has not yet been completed. (Jt. Pet. MISO Ex. D, p. 25.)

As with other seams issues, what may appear to be minor differences in the congestion management practices of the RTOs could result in a dysfunctional market. Mr. Hils testified:

"Even if...a common system is used independently by the Alliance and the Midwest ISO in making its decisions, that could still impact the reliability... You still need to be assured that the independent systems of the Midwest ISO and the Alliance would

use information in a way that wouldn't cause conflict.

(Hils TR C-78 line 12).

Mr. Snead's testimony supported Mr. Hils' statements:

While both RTOs appear to be using similar approaches (i.e., Locational Marginal Pricing, LMP, in real-time with flow-gate rights available for the forward market), there are significant differences in the details of the implementation of these congestion management approaches so as to create uncertainty as to how the approaches behave at the RTO seams. Because of the lack of a common approach will make congestion management more difficult in the region, this area of the IRCA needs to be worked on...

(Jt. Pet. MISO Ex. D, p.6).

Mr. Roan further substantiates the concern in his enumeration of congestion management, and other issues, that "have not been developed so as to conform with the Settlement agreement." (Enron Ex 1, pp. 8-9).

In addition to the foregoing issues, there are several component issues that also need to be addressed. The following is merely a partial list of issues that need to be addressed and, according to some witnesses, have not been addressed or, in some cases, satisfactorily resolved. (i). "redispatch (Jt. Pet. MISO Ex. D, p 5)," (ii). "imbalance" (Jt. Pet. MISO Ex. D. p.18)," (iii). "bulletin board" (Jt. Pet. MISO Ex. D, p. 5), (iv). "Day 2 real-time balancing markets" (Jackups TR C-129), (v). "the development of a day-ahead market," (vi). "whether in Day 2 parties have a physical right or a financial right to transact when the transmission system is constrained. To the extent that there are differences in any of the above-mentioned issues, the congestion management regime among the RTOs could be jeopardized.

With regard to redispatch, for instance, Mr. Snead stated:

The determination of costs, allocation and payments are vital for the successful implementation of redispatch, and without these important issues settled, redispatch between the RTOs is extremely unlikely, as generators will want these issues resolved before they bid. To my knowledge, these important issues have not been fully resolved.

(Jt. Pet. MISO Ex. D, p. 5)

In addition to differences in the approaches to the matters subject to the IRCA, there are definitional matters that seem certain to exacerbate seams issues. Mr. Snead stated (Jt. Pet. MISO Ex. D, p. 5): "As an example of one of the differences, the Midwest ISO will consider a transaction to be firm if an associated redispatch is available and approved by the Midwest ISO. The Alliance

RTO appears to regard such a transaction as less firm than other transactions.”

As the foregoing discussion shows, while the congestion management coordination procedures to be created under the IRCA may represent an improvement over current market practices, many congestion management issues between the two RTOs have not been resolved consistent with IRCA's requirement of seamless markets. As Mr. Hils testified:

There could be economic consequences if the real-time balancing market can see only pricing of one RTO or the other. I believe that the IRCA should address this seams issue. Likewise, there are reliability consequences if the market is forced to bid into separate RTOs for congestion, as it is possible that units heavily integrated within the Midwest ISO and Alliance RTO ‘footprint’ could receive conflicting dispatch instructions without coordinated congestion efforts by the RTOs. This again is another seams issue to be addressed.

(Jt. Pet. MISO Ex. D. p.18)

### **5. Available Transmission Capacity**

The MISO will use the data it collects to create power flow models every hour. It will use these models in turn to calculate ATC, which will be posted. Under the IRCA, the MISO will share its ATC calculations with the ARTO, and vice versa. (Jt. Pet. MISO Ex. D, pp. 26-27).

MISO and ARTO will create common databases to allow input of data for individual Control Areas to facilitate central calculation of the required ATC values. The ATC calculation procedures will provide the ability to identify and adjust for parallel path flows both within the region and neighboring regions. A draft document entitled Cooperative Procedures and Protocol on ATC determination has been prepared and will be the basis of the coordination. Provided that appropriate external conditions (e.g. outages, reservations, load levels) are included in the RTOs calculation process and internal conditions are appropriately modeled, ATC values should yield similar results. (Jt. Pet. Alliance JCB-1, pp. 17-18).

Yet there will be opportunities for incompatible results, due to limitations of data exchange or generation dispatch information. To the extent differences in calculation result in overloaded flowgates, relief measures could be required, such as shutting down particular transactions unnecessarily, resulting in a less efficient marketplace. (Jt. Pet. MISO Ex. E, p. 21; Jt. Pet. MISO Ex. D, pp. 20-21).

For example, the values used in the calculations are forecasts so that the transmission capacity that exists in real-time will differ from the previously posted ATC values. The ATC values are typically calculated assuming only a single incremental transmission outage may occur. If in real-time the transmission system would suffer an outage exceeding the worst single contingency outage, the previously posted ATC values would overstate the ATC values in real-time. Thus, subtle differences in forecast or interpretation of the data will result in different ATC values.

While the process should be an improvement over the coordination mechanism of today, there are still opportunities for incompatible results due to the limitations of data exchange or generation dispatch information. To the extent differences in calculation result in overloaded flowgates, relief measures could be required, such as shutting down particular transactions unnecessarily, resulting in a less efficient marketplace. (Jt. Pet. MISO Ex. D, pp. 21-22).

## **6. Ancillary Services**

The control areas within the ARTO and the MISO will continue to provide ancillary services to the customers within the control area's metered boundaries, unless the transmission customer chooses to self-provide applicable services.

The ancillary services are control area specific; as such, they do not require services from other RTOs or even other control areas within the same RTO. However, the Alliance RTO model anticipates that markets for ancillary services will develop and permit competition within the region (Jt. Pet. Alliance JCB-1, p. 37). To ensure reliable and efficient sources of generation resources for providing ancillary services, the Alliance RTO will require generators interconnected to its transmission system to execute an Interconnection Agreement. The interconnection agreements will require the generation owners to supply ancillary services as determined to be necessary by the Alliance RTO. The generation owners will continue to provide ancillary services until it is determined that sufficient third party ancillary services are available through a regional power exchange or other market means. The ARTO and MISO are committed to develop and implement appropriate mechanisms to coordinate super regional operations and to assure the compatibility of their operations. Therefore, Joint Petitioners believe the MISO and Alliance RTO configuration will not impair the viable market for ancillary services (Jt. Pet. Alliance JCB-1, p.38).

The MISO Joint Petitioners, however indicated a concern that a viable, practical market for ancillary services will be impaired unless the configuration, requirements and other seams issues between the MISO and the ARTO can be made completely transparent to the market. (Jt. Pet. MISO Ex. E, pp. 22-23).

Specifically, Mr. Hils indicated a concern that a viable, practical market for ancillary services will be impaired unless the configuration, requirements and other seams issues between the MISO and the ARTO can be made completely transparent to the market. Mr. Hils further indicated that there should be standardization so that the rules for self-provision of an ancillary service are consistent across RTOs. (Jt. Pet. MISO Ex. E, pp. 22-23).

## **7. Conclusion on IRCA and Seams**

The status of progress on the IRCA-required procedures and protocols is dealt with extensively in both the MISO and the ARTO Joint Petitioners' testimony. From that testimony, it appears that the IRCA process has produced some agreements. In other instances, the Agreements between the Alliance transmission owners and the MISO were merely agreements to agree. In other cases, there are fundamental disagreements on matters that could, if unresolved, scuttle any hopes of

Inter RTO cooperation. There are still other instances where less than satisfactory agreements have been reached. The testimony also reveals significant differences of opinion over other seams issues, as well as serious differences in perception as to the success of the IRCA effort.

The Commission recognizes that the process of achieving coordination between RTOs is complex and new. We do not expect seamlessness to occur without effort, and we do not expect inter-RTO coordination to occur without difficulty. But our recognition that coordination will be difficult, and will require effort, cannot blind us to certain facts, facts from which the Commission may draw reasonable inferences. In the context of the IRCA, those facts are:

- a. Alliance, up to the FERC's July 12, 2001 order banning business decisions, was controlled by a single class of market participants: vertically integrated transmission owners who also controlled generation.
- b. As evidenced from the long line of FERC decisions discussed elsewhere in this order, Alliance has shown reluctance, inability, or both, to implement the FERC's goals of independent governance and stakeholder participation.
- c. Maintaining seams would be consistent with FERC's early stated concern about the Alliance, that it would split markets and create a "tollgate," protecting from competition the generation of its members.
- d. The MISO has had processes, procedures, communications systems, hardware, and software in place far longer than the Alliance. The Alliance could adopt these same processes and systems and thereby eliminate a good deal of the seams problem. The ARTO witness did not explain why the Alliance could not or would not do so.
- e. There is a marked difference in how the two sets of Petitioners characterized the IRCA situation. The MISO witnesses provided a detailed analysis of each element of the IRCA problems. They testified candidly about the difficulties, about whether more progress was necessary, and about whether that progress was achievable. They expressed concern about the sufficiency of progress and warned specifically about the implications should progress not be achieved. They clearly set forth realistic expectations about what could and should be achieved, and demonstrated concern about the shortfalls from those expectations. In contrast, the ARTO witness provided far fewer details about IRCA implementation, expressed satisfaction with the progress and did not articulate concerns about the insufficiency of progress.

These facts are consistent with the concerns set forth by Witnesses Roan and Dauphinais.

We recognize that reasonable people can differ about an issue like IRCA success. But we were struck not only by the existence of a difference between the MISO witnesses and the ARTO

witness, but also by the magnitude of this difference. The specificity of the MISO witnesses, and their qualifications and knowledge of transmission, leads us to credit their interpretation over the ARTO witness' interpretation. It is squarely within our discretion to make this type of judgment. The judgment we make is that a significant reason why IRCA is not producing seamlessness is that the ARTO, the entity to which the Joint Petitioners seek to transfer responsibility for Indiana transmission assets, is not fully and unambiguously committed to the goal of seamlessness. We recognize that the ARTO witnesses testified otherwise, but it is our duty to assess the credibility of that testimony, and we find the facts set forth above more credible.

As set forth in the preceding legal analysis, the Commission must consider the public interest. The public interest requires effective competition in wholesale generation markets, with those markets defined as broadly as physical capabilities and commercial realities permit. It is not in the public interest, and Indiana's interest specifically, to allow Indiana's transmission assets to migrate to an organization that is not committed, fully and unambiguously, to elimination of seams. As explained above, we conclude that the ARTO is not committed, fully and unambiguously, to this goal, and that the IRCA problems are at least in part a result of this fact. The IRCA problems therefore constitute an independent reason, and a sufficient reason, for this Commission to deny the Application in this Cause.

As we discussed previously in this order, it is possible that a change in leadership at the Alliance would change this result. But there is nothing in the record concerning NGC or any other possible manager that changes the facts. That there may someday be a new manager who may behave independently and who may commit, fully and unambiguously, to IRCA (and the record does not necessarily even support these multiple possibilities) is not substantial evidence sufficient to overcome the facts presented in this matter.

#### **F. Responsiveness to the Public's Needs**

A less tangible but still important criterion is the transferee's record of responsiveness to the public in general and this Commission in particular. The importance of responsiveness to this Commission grows as our jurisdiction becomes shared with FERC's. This jurisdictional sharing occurs when the functional control of the transmission assets moves from utilities providing bundled, state-jurisdictional retail service to an RTO providing unbundled, FERC-jurisdictional transmission service.

On this topic, the Alliance effort again has a troubled past and an uncertain future. In response to concerns about Alliance's stakeholder process raised by state regulatory commissions, utilities, customer groups, market participants, and others in numerous filings to the FERC, in its July 12, 2001 Order had offered the services of its Dispute Resolution Service ("DRS") to try and resolve the disagreement over a stakeholder process. (FERC July 12, 2001 Order, pp. 35-37, Docket No RTO1-88-000). The FERC directed the Alliance Companies and parties to resolve differences and for the Alliance Companies to incorporate changes that emanated from this DRS process in its future compliance filings. (Slip op at p. 37)



On October 12, 2001, the Alliance filed an Offer of Settlement with the FERC, entitled "Principles Of Agreement For The Formation Of The Stakeholder Advisory Committee." (Jt. Pet. Alliance JCB-R3). This settlement was the direct result of the involvement of the FERC's DRS. This settlement outcome followed a long and difficult path. Mr. Dauphinais testified that the relationship between the Alliance companies and stakeholders has been "dismal" because the stakeholders have not been afforded an opportunity for meaningful input. Mr. Dauphinais testified:

"It has been my experience that the Alliance Companies view of meaningful stakeholder input involves making a presentation to stakeholders, taking questions and comments from those stakeholders, and politely indicating they would consider the suggestions being made. Under such arrangements, the Alliance Companies control the agenda and the outcome. This problem has been made worse by the Alliance Companies tendency to take credit for soliciting stakeholder input even when such input was ignored. Understandably, this has soured relations with stakeholders." (IIG Ex.1, p. 25).

Mr. Dauphinais continued by discussing a forum established by the Alliance companies, called the Market Development Advisory Group. On this subject, Mr. Dauphinais testified:

"This group was formed by the ARTO after stakeholders pressed the Alliance companies to provide a more meaningful form of input into market design decisions. Unfortunately, the Alliance companies set the agenda of the meetings and stakeholders were confined to the audience. In addition, stakeholders were not permitted to appoint their own liaison to the Alliance Companies Management Committee." (IIG Ex. 1, p. 25).

An RTO advisory process, regardless of how well designed, is only as effective as the RTO's willingness to be advised. To focus on the new process alone while ignoring the matter of willingness, would be error. The Commission cannot disregard the history of unresponsiveness, unilateral action and delay, which characterized the Alliance Companies' treatment of a stakeholder process. Such difficulty is avoidable, as evidenced by the MISO experience described in the order we issue today in Cause No.42027. Put simply, where it takes five Presidential appointees and federal dispute resolution experts merely to create an advisory process, the Commission can reasonably infer that willingness is lacking.

As in the context of independence, we acknowledge that the entry of an independent managing member might change the situation. But there is no evidence on this record to transform that possibility into a probability. Based on this record, the Commission concludes that the ARTO has not shown sufficient responsiveness to stakeholder concerns to make a transfer of transmission responsibility from Indiana utilities to the ARTO consistent with the public interest.

**IV. Commission Findings and Conclusions** Before allowing Indiana utilities to transfer functional control of transmission assets to an RTO, the Commission must find that the evidence demonstrates that such transfer will be to an entity that will provide reliable, adequate and efficient service to Indiana customers and those who serve them. The record here does not support such a

finding. It supports instead the findings we have made: that a transfer of transmission responsibility to the ARTO is not consistent with reliable, adequate and efficient service in Indiana, and is not consistent with the development of seamless generation markets so important to our state's economic future.

The Joint Petitioners may argue that any lack of operational readiness is not their fault, because the FERC's July 12, 2001 order precludes them from making business decisions until there is independent leadership, and that if they had more time they could resolve all problems. The Alliance Companies have worked on this matter for several years. There was ample time to produce an independent governance structure, as evidenced by the MISO's ability to do so, and with substantially less controversy. The Alliance Companies' inability now to make business decisions due to the lack of independence is reason to question their assertion of commitment to independence, not give them more time to support that assertion.

Forming an RTO does take time. But how much time should not be a determination of the transmission owner alone, because as FERC has found in Order No. 2000, the transmission owner, when it also owns generation, has incentives and goals that are not necessarily aligned with the public interest. The Commission must make judgments about how much time should go by before results should appear. It is this Commission's judgment that the Indiana utilities seeking permission to transfer transmission responsibility to ARTO have had enough time within which to convince us that their goals are consistent with Indiana's interests.

By rejecting the Joint ARTO Petitioners' Application, we do not mean to suggest that the status quo, in which NIPSCO and I&M are not members of any RTO, is satisfactory. As made plain in both this order and our Order on the MISO Joint Petitioners issued today in Cause No. 42027, the public interest requires seamless generation markets, and the transfer of operational control of transmission assets to a properly designed RTO is a prerequisite to seamlessness.

ARTO may argue that transferring operational control of NIPSCO's and I&M's transmission assets to some ARTO is better than doing nothing, because the coordination among the ARTO utilities will be greater than without the ARTO, and that the inter-RTO coordination enabled by the IRCA, even if not fully seamless coordination, is more than exists today. But one can assume the accuracy of these arguments and still find that such arguments focus only on immediate benefits rather than long-term needs. We find that the proposed transfer to the Alliance will impede achievement of seamlessness in the longer-term, for the many reasons set forth in the foregoing pages. Indiana's long-term interests will be served, however, if responsibility for its transmission assets is transferred to an organization that has a more credible commitment to the aforementioned goals.

Implicit in the foregoing explanation is our expectation that NIPSCO and I&M will not maintain the status quo, in which they have not transferred their transmission assets to any RTO. We expect that either voluntarily, as a result of an eventual FERC mandate or as a result of a mandate from this Commission, they will make such a transfer. To make certain that such a transfer does occur and occurs in a manner consistent with the public interest, we will be initiating a separate

investigation, to examine the alternative courses of action practically available to the Joint Petitioners.

**IT IS THEREFORE ORDERED BY THE INDIANA UTILITY REGULATORY COMMISSION, THAT:**

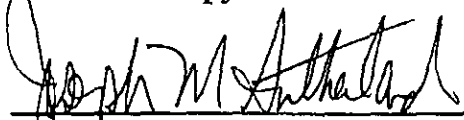
1. The Joint Petitioners transfer of functional control of operation of Indiana Michigan Power Company, d/b/a American Electric Power and Northern Indiana Public Service Company of transmission facilities located within the State of Indiana to the Alliance Regional Transmission Organization is hereby denied.

2. This Order is effective on and after its date of approval.

**MCCARTY, HADLEY, RIPLEY AND ZIEGNER CONCUR; SWANSON-HULL ABSENT:**  
**APPROVED:**

**DEC 17 2001**

I hereby certify that the above is a true  
and correct copy of the Order as approved.

  
\_\_\_\_\_  
Joseph M. Sutherland, Secretary to the Commission

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