

UNITED STATES OF AMERICA
NUCLEAR REGULATORY COMMISSION

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BRIEFING ON ELECTRIC UTILITY RESTRUCTURING

- - -

PUBLIC MEETING

Room 1F16
11555 Rockville Pike
Rockville, Maryland

Thursday, April 24, 1997

The Commission met, pursuant to notice, at 9:00 a.m., Shirley A. Jackson, Chairman, presiding.

BEFORE:

- SHIRLEY A. JACKSON, Chairman
- GRETA J. DICUS, Commissioner
- KENNETH C. ROGERS, Commissioner
- NILS J. DIAZ, Commissioner
- EDWARD McGAFFIGAN, JR., Commissioner

STAFF AND PRESENTERS SEATED AT THE COMMISSION TABLE:

- JOHN C. HOYLE, Secretary
- KARYN D. CYR, General Counsel
- LEONARD JOSEPH CALLAN, EDO
- DAVID MATTHEWS, Chief, Generic Issues and Environmental Projects Branch, NRR
- ROBERT WOOD, Senior Financial Analyst, NRR
- MARYLEE SLOSSON, Deputy Director, Division of Reactor Program Management, NRR
- SUSAN TOMASKY, General Counsel, FERC
- BRUCE B. ELLSWORTH, Commissioner, New Hampshire Public Utilities Commission, President, NARUC
- ROBERT W. GEE, Commissioner, Texas Public Utilities Commission, Chair, NARUC Commission on Electricity
- EMMIT GEORGE, JR., Commissioner, Iowa Utilities Board, Chair, NARUC, Subcommittee on Nuclear Issues, Waste Disposal
- E. LINN DRAPER, JR., Chairman, President and Chief Executive Officer, American Electric Power Service Corporation
- JOE COLVIN, President and Chief Executive Officer, NEI
- PHIL HARRIS, President, PJM Interconnection Association

STAFF AND PRESENTERS SEATED AT THE COMMISSION TABLE:

[continued]

- JAMES ASSELSTINE, Managing Director, Lehman Brothers

CHAIRMAN JACKSON: Good morning, ladies and gentlemen.

The historic change to a competitive market for the electric power industry is having far-reaching consequences and presents many challenges for the nuclear power industry. As restructuring proceeds and the business environment changes, our licensees and the NRC must ensure that economic pressures do not erode nuclear safety and must assure the adequacy of decommissioning funding.

To ensure that the NRC is taking the right actions at the right time in the appropriate manner, it is important that we gain an understanding of the changes and emerging issues that are occurring as a result of these momentous changes. To address the significant issues and concerns, the NRC has brought together economic regulators and representatives of the nuclear industry as well as our own staff to present their roles and perspectives on the future of the electric power industry with the transition to a competitive market.

Yesterday, we focused in a Commission meeting, public meeting, on transmission reliability and security. Today, we will focus on other issues associated with electric utility restructuring and economic deregulation.

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The restructuring of existing utilities raises a number of complex issues. We are seeing proposed legislation at the federal and state levels and many new financial arrangements.

The NRC needs to keep itself abreast of developments and be able to respond to legislative proposals and financial changes which include mergers and acquisitions, antitrust issues, stranded cost recovery and the introduction of independent system operators.

I would like to welcome the NRC staff and the members of the two panels that will be speaking today on these issues.

On the first panel, after the staff speaks, will be Susan Tomasky, General Counsel for the Federal Energy Regulatory Commission; Commissioner Robert Gee, Chair of the NARUC Committee on Electricity; Commissioner Bruce Ellsworth, President of NARUC; and, commissioner Emmitt George, Chair of the NARUC Subcommittee on Nuclear Issues and Waste Disposal.

I am also pleased and will welcome them again at the time, to welcome the members of the second panel, Mr. Joe Colvin, President and CEO of the Nuclear Energy Institute; Dr. E. Linn Draper, Chairman, President and Chief Executive Officer of Electric Power Service Corporation; Mr. Phil Harris, President of PJM Interconnection

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Association; and Mr. James Asselstine, former Commissioner, now Managing Director of Lehman Brothers.

If the Commissioners have no opening comments, Mr. Callan, please proceed.

MR. CALLAN: Good morning, Chairman and Commissioners.

Chairman, as you just noted, we are the first of several panels to brief the Commission on the status of economic deregulation and restructuring of the electric utility industry. As you know, the NRC staff has, at the Commission's direction, undertaken several initiatives to address the NRC's concerns about the potential health and safety impacts of economic deregulation of its power reactor

licensees. Our briefing will update you on the status of our initiatives and will highlight several issues currently of concern to the NRC and other participants in the deregulation process.

This is our first briefing to the full Commission since July 30, 1996.

With me this morning are Marylee Slosson, the Deputy Director of the Division of Reactor Program Management in the office of NRR, David Matthews, a branch chief, who works for Marylee Slosson, and Robert Wood.

I will now turn the briefing over to David Matthews.

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David.

MR. MATTHEWS: Thank you, Joe, and good morning.

I am only going to spend a couple of minutes by way of brief summary and an outline of the staff's intended remarks.

If I could have the first slide, please?

As Mr. Callan indicated, we briefed the full Commission in July of last year with regard to a seven point action plan that the staff had undertaken starting in February of 1996. Today, we did not intend to go by rote through the individual items of that action plan because we view that that progress is generally well known. We have briefed the status of that action plan in many fora over the last few months. We did, however, want to focus on what we view to be the accomplishments that have been afforded through those efforts within the last year or 18 months.

I want to comment at this time, as an outgrowth of our last briefing in July, the Commission raised an issue to the staff for us to consider in connection with this general area of restructuring and that was the issue of non-owning operators who -- proposals had been offered associated with the operation of plants by people who had not previously been listed on the license and weren't licensees.

The staff has, at the Commission direction, undertaken a separate review of that issue and a paper

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presenting some policy considerations is in preparation and is due to the Commission here in the next month or two.

CHAIRMAN JACKSON: You will not be speaking specifically to that today?

MR. MATTHEWS: Right, although we will indicate that that is one of the "emerging issues," because of the unique arrangements that are materializing. It is not one that we are prepared to speak to in detail at this time.

With that, I want to indicate that Bob Wood will carry us through the presentation and he will focus on the accomplishments of the last 12 or 18 months. He will also briefly review what is the continuing NRC's involvement and review in restructuring activities that are taking place in the recent past, as we speak today and in the near future. He will also mention what we see to be some emerging issues that the NRC certainly has to keep an eye on and then particularize it to a few issues that we think the NRC has to be actively involved in addressing in the near future and then he will provide a summary and conclusions.

MR. WOOD: Thanks, Dave.

Slide number 2.

Chairman Jackson, Commissioners, I am happy to be here.

CHAIRMAN JACKSON: We are happy to have you.

mentioned, back last February with seven elements. Most of those elements are on here. I will try to be very brief in summarizing them. As you all remember, we issued an advanced notice of proposed rulemaking in April on decommissioning funding assurance and that now is coming close to final internal completion and will be coming up to the Commission as a proposed rule.

CHAIRMAN JACKSON: When do you anticipate that?

MR. WOOD: It will probably go to the EDO's office within a day or two.

CHAIRMAN JACKSON: So, in May?

MR. WOOD: Sometime in May.

CHAIRMAN JACKSON: Okay.

MR. WOOD: The administrative letters that we issued to all of our power reactor licensees last June reminded them of their obligation to inform us of any activities that might be considered direct or indirect transfer of control of the license under our 50.80 reviews and we have gotten a few responses back on that from time to time since then.

We issued a draft policy statement on September 23. We extended the comment period once because of interest expressed by the public. The final policy statement is now under staff review and is moving along internally and will be up to the Commission sometime later in June, I believe.

The draft standard review plans that were issued in concert or prepared in concert with a draft policy statement were published or notice of availability was published in the Federal Register on December 27. As you may remember, the standard review plans concern both the financial qualifications, review process and the decommissioning funding assurance review process as it stands now and there is a separate standard review plan on the antitrust review process. We got six comments back on that and will be revising the standard review plans based on those comments.

We have ongoing staff level liaison function that I think is going along very well with FERC and with the state PUCs through the NARUC committee framework. And, finally, we have work going on with the Financial Accounting Standards Board endorsing right at this point what they call an exposure draft which is a draft proposal which would give us information on the status of decommissioning funds.

Finally, we have an ongoing evaluation of our 50.80 process and our general financial qualifications framework and I will get into that a little bit more.

CHAIRMAN JACKSON: When do you expect your review of the FASB exposure draft?

MR. WOOD: Well, we have a guide which has been prepared which endorses the exposure draft. We are at the

mercy, of course, of FASB's schedule. My understanding is that FASB will probably either be issuing another exposure draft because of issues raised for non-nuclear facilities that also have long lives and have costs associated with their ultimate disposal. So they may do that in the second quarter of this year, which we are in now, of course. I understand that at the earliest, the final FASB guide or regulation wouldn't be coming out until December of this year.

CHAIRMAN JACKSON: This relates to reporting

requirements?

MR. WOOD: This relates to reporting requirements and the status of decommissioning and how people or companies would deal with the ultimate liability to get rid of that obligation.

Slide 3, please.

We believe that we have fairly well summarized the current process that we use by issuing the standard review plans. We will, of course, be changing the standard review plans as we change the regulations that underlie them. As I mentioned earlier, we have been reviewing all restructuring proposals under our 50.80 transfer of license requirements. So far, we haven't seen any divestitures of assets. Most of the things we have seen so far have been mergers or formations of holding companies.

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We do expect to see future issues where divestiture is raised. We also expect to see future issues where proposed purchases by foreign entities may occur.

Basically, our review is basically straightforward. As you know, we have a dichotomy in our regulations for power reactor licensees between those that are defined as electric utilities in our regulations in the definition section and then nonelectric utilities. And electric utilities have, because of their historic access to ratepayers through regulated rates, have a little bit lower threshold to meet than nonelectric utilities. We do ascertain in our reviews that a licensee would remain an electric utility and if they don't they would have to comply with the more rigorous standards that pertain to the electric utilities.

For holding companies, what we are concerned about is as holding companies are formed over our existing licensees that there may be transfers of assets away from our licensees to a parent or affiliated company. So we have been getting commitments from licensees that they will inform us if there are any significant transfers of assets so that we will at least know about it and take appropriate action if we need to.

CHAIRMAN JACKSON: Let me ask you two questions. One, in terms of obtaining the commitments to inform the NRC

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when significant assets are moved, are those commitments made a part of the license or the license transfer?

MR. WOOD: We do have, in recent -- in the last year or so made them as license conditions. Prior to that, there was less consistency on that approach and we had obtained letters. One thing in this broader review of our financial qualifications framework, I think we are certainly looking at the feasibility of whether to make that a requirement in the regulations rather than doing it through the license condition process.

CHAIRMAN JACKSON: If you were to do that, would that require a separate rulemaking or you would be doing this in the rulemaking coming forward in May?

MR. WOOD: It won't be part of the rulemaking coming forward in May. It would be a separate rulemaking. This rulemaking would look at more of the general qualifications process. The rulemaking that is coming forward in May is looking specifically at decommissioning funding assurance and the impacts of deregulation on that.

CHAIRMAN JACKSON: As a general practice today, you are making these commitments license conditions going

forward?

MR. WOOD: Right.

CHAIRMAN JACKSON: And the second question has to do with consideration of foreign ownership issues. How well prepared are we in terms of reviewing those?

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MR. WOOD: I think we have to do some more work on what the standards are. I think at this point part of the problem is, you know, clearly any entity that owns over 50 percent of a licensee and is foreign would raise -- would probably be in contravention of the Atomic Energy Act. Just as clearly, if there is a de minimis amount, under say 5 percent, it would be highly unlikely where they could exercise any form of control.

But you have a gray area in between that you would have to evaluate. In most cases, foreign companies aren't going to exercise control with 10 or 20 percent of voting stock but not always. So we would have to look at each particular situation, I think.

CHAIRMAN JACKSON: I guess I am really asking two questions. One is, how well prepared are we in terms of being able to look at what may be less than obvious situations? That's number one.

Number two, how well prepared are we to move quickly relative to those reviews?

MR. WOOD: You know, I think we could make a review and I don't think it would be on the critical path; it would be on the general review that we would look at and it would take, like most reviews do now, in the order of three to six months and it would be another element we would look at.

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At the same time, I think we want to look at resolving, if we can, some sort of benchmarks or milestones below which we wouldn't have to look at at all or above which we would clearly have to look at.

CHAIRMAN JACKSON: How close are you to developing such thresholds?

MR. WOOD: We are starting on that but we haven't gone very far into it.

MR. MATTHEWS: Let me make a comment that it is an element that is required of us and we have looked and addressed it in each SER that we have issued associated with the proposed restructuring or change in ownership. So it is an essential element because it is a prohibition in the Atomic Energy Act. We just have not seen one that would challenge our judgment in that regard. Namely, there just hasn't been a case in which we have uncovered any foreign ownership.

So it is an explicit part of our review and we have been addressing it in each instance. Where the challenge will come is the first time that we see one with some material ownership and then we are going to have to evaluate its significance. To say that we have criteria would be a strong overstatement; we don't.

I believe it is something that could be factored in, appreciating that it might take some additional time, into our standard review plan. That may be an appropriate mechanism to do it. But it is one of those many emerging issues that the staff has yet to articulate any clear standards on.

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MR. WOOD: Yes, we do have a statement in the current standard review plan that went out on foreign

ownership but it is very broad and very general and that was the best we could do, given the time constraints at that time. We are going to have to revisit that.

CHAIRMAN JACKSON: Commissioner McGaffigan.

COMMISSIONER MCGAFFIGAN: On the definition of electric utility, as states go about passing retail competition statutes, will that move utilities from being an electric utility under our definition into the other category at some point in time?

MR. WOOD: It all depends on the specific state proposal.

COMMISSIONER MCGAFFIGAN: So you are going to have to audit each state proposal?

MR. WOOD: Well, yes. And in the proposed rule that will be coming up we do try to address the issue of those states that do have dedicated nonbypassable charges that take care of decommissioning funding. We would want to handle that in our regulations so that I think the staff's

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thinking is for that purpose they would still be considered an electric utility even though for other purposes they may not be. So you could have a divergence.

COMMISSIONER MCGAFFIGAN: Depending on how decommissioning funds are handled in the state statute?

MR. WOOD: Right.

COMMISSIONER MCGAFFIGAN: Have we conveyed that tentative position to the states?

CHAIRMAN JACKSON: We just did, if we did not before.

[Laughter.]

COMMISSIONER MCGAFFIGAN: Fair enough.

MR. WOOD: You would have -- you could be considered to be an electric utility from the point of view of decommissioning funding assurance if states had mechanisms for that. Whereas, the same entity might not be for general financial qualifications to operate the plant.

Slide 4, please.

The emerging issues as we see that, I am not going to mention any more about grid reliability and ISOs. You had a very detailed meeting yesterday afternoon on that subject.

We do see some issues with respect to unique ownership and operating arrangements which gets back to Dave's earlier remarks about non-owner operators and how

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they might play out in some of our considerations.

CHAIRMAN JACKSON: What are some of the issues that you are considering?

MR. WOOD: I think I will really -- if I may, I will use the recent Maine Yankee Entergy agreement as kind of a template for what we have done and we looked at that proposal particularly. Because Maine Yankee had retained responsibility and ultimate authority to shut the plant down and control over ultimate spending, we didn't see any real problems with that.

Other proposals may come along that may not have all those elements in them and we may raise our level of concern as a result. There again, I think we have to be concerned about future partnership forms and we are just not sure what those are. I think we would certainly be concerned about -- that the licensee has to maintain control in some way or that whoever takes the authority gets put on the license.

There, as you know, there are two issues involved in this, in this 50.80 transfer process. It is both financial qualifications and technical qualifications. We do have to look at those.

As Dave mentioned, we will be addressing this whole issue in more detail in the paper that will be coming up to the Commission in the near future.

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CHAIRMAN JACKSON: You mentioned the issue with respect to future partnership forms of whoever takes on the authority. You mean the operational authority?

MR. WOOD: Right.

CHAIRMAN JACKSON: Gets put onto the license?

MR. WOOD: Right.

CHAIRMAN JACKSON: Was Entergy put onto the license?

MR. WOOD: No, because of Maine Yankee's retaining of the ultimate authority and control, we did not do that in that case.

CHAIRMAN JACKSON: Okay.

Commissioner McGaffigan.

COMMISSIONER MCGAFFIGAN: Are we going to suggest templates for partnership forms that will pass muster? Are we going to do this sort of case by case and let a body of case law build up so that people will recognize what we approve and what we don't approve?

MR. WOOD: I think we probably are going to end up doing it case by case because I don't think we can visualize at this point all the potential permutations of what might come in.

We do have antitrust issues that we are going to look at, of course, statutorially required to do so. As I did mention earlier also, we have seen a number of state

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initiatives now where, in most cases, they have provided for a secure source of revenue streams, at least for decommissioning. There is also the broader issue of resolution of stranded costs in general, including recovery of capital costs, which I think we are probably less concerned about unless it gets to the point where the lack of that recovery stresses a utility -- a licensee enough financially that they would have trouble running the plant safely.

As I mention also, a lot of these approaches that the states are using in terms of nonbypassable charges seem to be a good surrogate for the existing approach to rate regulation and rate recovery. If that process continues to hold, I think we will be in pretty good shape. Of course, we don't have a crystal ball and some states may not choose to go that route.

CHAIRMAN JACKSON: So a key to avoiding our having to take direct action with respect to our licensees is the issue of nonbypassable charges?

MR. WOOD: I believe so, yes.

CHAIRMAN JACKSON: Okay.

MR. WOOD: Next viewgraph, please.

There are a number of issues that we have already -- Dave has already covered and I have touched on the issues that have to be addressed and possibly resolved.

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As I mentioned earlier, there is this broad look that we are initiating now in terms of the general 50.80 review process and even our -- the financial qualifications review process under 50.33(f) and we will be at some point coming up with

the policy options on that for the Commission's consideration.

CHAIRMAN JACKSON: At some point, what does that mean?

MR. WOOD: Sometime this summer, I believe.

CHAIRMAN JACKSON: Okay.

MR. WOOD: We have a concern, we have gotten several comments both on the draft policy statement and the standard review plans and the regulatory information conference earlier this month on industry's concern about having very specific defined NRC position on what we expect in our financial qualifications review. We thought we did that in the policy statement and in the standard review plans. I think they want an even firmer line in the sand.

I am not sure how we can do that, given that we don't really know what is going to happen in the future and there are many variations on restructuring but we will be considering that, of course.

We are, of course, concerned about the acceptability of the level of decommissioning funding assurance that might come out in some state restructuring

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approaches and we will have to look at those as they develop. We are concerned also about the availability of funding assurance mechanisms to nonelectric utilities as they get kicked out of this category into being a nonelectric utility, they would no longer be allowed to put money aside annually over the projected life of the reactor; they would have to come up with some sort of guarantee mechanisms for any unfunded balance. To do that, they would either have to prepay or use a surety bond or a letter of credit or a guarantee coupled with a financial test. It is not clear in all cases where those would be available to those licensees that need them.

Finally, we are looking at the possible need for federal legislation in various areas of restructuring.

CHAIRMAN JACKSON: Which areas do you feel need perusal with respect -- are you perusing with respect to the need for federal regulation?

MR. MATTHEWS: Let me speak to the issue of federal legislation. It is one that we have become increasingly involved in, in concert with Karen's staff.

We met with the Department of Energy within the last few weeks and received an explicit invitation to participate with them in even to the point of drafting legislative proposals in concert with their staff. We are proceeding next week to sit down for our first meeting to

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examine the alternatives.

So we have just at this point in time come up with some areas to discuss with them jointly and I will just give you the flavor for what those areas are. These aren't in any order of preference; they are just areas that have been raised by the staff and outside interest as being an area where there may be a need for federal legislation to backdrop or give a statement of congressional intent or support as state-specific and FERC initiatives in the restructuring area go forward.

I say it that way because I don't believe we have identified, with the possible exception of one area any areas that we think we need bolstering in terms of our regulatory authority in this area as we move forward in the sense that we have some large gap. I look to Karen to

correct me on that statement if that is not true. So it is along the lines of providing support.

One area is bankruptcy priorities, as you may see bankruptcies coming out of some of these restructurings, particularly those in the Chapter 11 category. We certainly would like to see some support for the view that decommissioning funding would have a priority associated with any such cases, even in advance of preferred creditors. So that is one of the -- one of the areas for discussion.

Certainly, the treatment of decommissioning funds

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in the overall context of stranded costs as we have discussed here is important. Given the variability of some of those proposals, some statement of federal intent in that regard, possibly deferring to an agency such as ours and FERC to address that issue, might be a possible proposal.

The antitrust area is one that we think it is worth examining. There have been calls for us to remove ourselves from the antitrust arena given the number of people that do look at that area. One of the consequences of an antitrust or the removal of antitrust review responsibilities from the Atomic Energy Act as it applies to the NRC's responsibilities is that we have a number of licensees, those licensed since 1970, that have existing antitrust license conditions and we would have to do an assessment of what the impact of removing our statutory authority in that area would be on those existing conditions so the issue is not as simple as just eliminating the review requirement. That is one that is at least ripe for discussion.

CHAIRMAN JACKSON: Have we begun to take that look?

MR. MATTHEWS: We have gone so far as within the next few weeks you will see a NUREG document published that will at least collate all of the existing antitrust license conditions in one location in order to at least have a

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baseline of reference to begin that assessment. That is a companion piece to the one we issued very recently which, for the first time, collated a current listing of all of the known owners of nuclear power plants and their operators, as reflected in today's licenses as well.

We felt when we entered into this 18 months ago that we had our data distributed throughout licenses and, although it was retrievable, it certainly wasn't immediately accessible so that is the foundation we have laid for those two reviews.

One area I will mention that certainly is worthy of possible further discussion is the grid reliability issue. It wasn't explicitly addressed by DOE when they discussed this issue with me several weeks ago but it is one I think the staff has to consider for possible -- let's put it this way. Putting it on the table in the short term, and I look to other members of the staff to support me in that regard as we go forward with DOE. My intent was to give DOE a call, in fact, this morning and ask them if that is something that would be appropriate in their view to add to the agenda.

CHAIRMAN JACKSON: Commissioner McGaffigan?

COMMISSIONER MCGAFFIGAN: May I follow up on the question on the case-by-case review? I interpret what you said later as industry would prefer to have a little more

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certainty.

Have you considered doing a reg guide saying here is one possible approach? We do that in other areas. If you divert from the reg guide, you know, you are into case-by-case country but if you stick to a reg guide or we endorse some NEI or whatever document, FSAB document, then you are in good shape, has that been thought about in the restructuring area?

MR. WOOD: Yes, in fact we thought we did that with the standard review plan and we did have a specific framework for reviewing financial qualifications and --

CHAIRMAN JACKSON: Does that standard review plan have an associated reg guide?

MR. WOOD: No, no it doesn't. But I think it had enough detail that it provided how we actually do review and the benchmarks that we do use --

CHAIRMAN JACKSON: Might you be able to promulgate out of it a reg guide?

MR. WOOD: We certainly could.

CHAIRMAN JACKSON: Certainly, they are companion pieces, aren't they?

MR. WOOD: We certainly could. It may be somewhat redundant, but --

CHAIRMAN JACKSON: To try to lay, as Commissioner McGaffigan says, on the table at least an acceptable

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approach?

MR. WOOD: Yes.

We only got six comments back on the standard review plans and, even among those six comments, they were all from industry, and there was some divergence of opinion as to the process that we were using and in a couple of cases I felt that they basically agreed with it but wanted some fairly minor modifications to it and in other cases they felt it didn't go far enough in laying out a specific position.

The last bullet on page 5, I think we pretty much covered earlier in our remarks so I won't belabor that.

COMMISSIONER DIAZ: Let me ask a loaded question on this instance. Since this is a new global economy, has somebody even asked a question is it -- will the Atomic Energy Act be changed in this respect?

MR. WOOD: Yeah, I think clearly there have been some initiatives on the part of, or consideration at least on the part of industry and others to amend the act in that way to eliminate that prohibition.

COMMISSIONER DIAZ: How hard would that be?

MR. WOOD: I'm sorry?

COMMISSIONER DIAZ: How hard would that be?

MR. WOOD: I don't know how high on Congress's priority list it would be.

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COMMISSIONER MCGAFFIGAN: Do we know whether other nations have similar -- I know from Congress it is usually if everybody else will allow American utilities to own, then it is one thing. If there are prohibitions on American ownership, then there is a tendency to want to be --

MR. WOOD: Clearly, there are a number of U.S. utilities that have invested in overseas utilities so, obviously, the prohibitions --

CHAIRMAN JACKSON: Do they own nuclear assets?

MR. WOOD: I think in a couple of cases they do. You know, certainly this prohibition was part of the security efforts at the beginning of the Cold War so, from

that standpoint, some of the reasons for it may be obviated.

CHAIRMAN JACKSON: Have we thought through what would be an appropriate NRC position? You know, what the policy considerations are or should be that would guide a stance that we might take on the issue?

MR. WOOD: I don't think we have thought it out in any detail on this point.

COMMISSIONER DIAZ: I think it might be worthwhile to start thinking. If we start getting into this area to have some idea which way we would go.

CHAIRMAN JACKSON: We have to start thinking about which way we would go.

COMMISSIONER DIAZ: Yes.

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[Laughter.]

MR. WOOD: Slide 6, please.

In our summary and conclusions, we have noticed kind of a divergence of states. There has been some acceleration or quite a bit of acceleration in several states in terms of taking deregulation initiatives. However, other states don't -- and those are generally states with lower cost power, don't seem to have it as high a priority. So most states are at least in the study phase but some states are moving ahead quite a bit more rapidly than other states.

We believe that we have taken, through our action plan and some other initiatives, those actions that would cope with these changes that are going on. I think we believe that our current regulatory framework and requirements are adequate to cope with the changes that are going on, both with respect to providing assurance for plant -- safe plant operations and also for safe decommissioning.

But, obviously, we are going to have to be on our toes and continuing to monitor the situation as it develops. I think because of that, because each state's approach is somewhat different and unique, that we have got to look at how each state and their licensees in those states approach the problem and make the determination as to whether they

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actually in fact do provide adequate assurance for operations and decommissioning.

That concludes my prepared remarks.

CHAIRMAN JACKSON: Commissioner Dicus had a question.

COMMISSIONER DICUS: Yes, I wanted to address that with you a little bit. On your comments which you have made on the rate at which economic deregulation appears to be accelerating and I think it is, and there are indications it may go at an even faster rate. My base question follows up on a comment or a question the Chairman had a little bit earlier and I want to broaden it a bit.

Are we as an agency, and you have addressed this a little bit, but do you really think we as an agency are prepared or looking down the road far enough for this accelerating rate that we can stay in front of the curve? Because I think this is an area we clearly do not need to fall beyond -- behind the curve.

MR. WOOD: Right.

COMMISSIONER DICUS: And things like evaluating some of these unique ownership operator arrangements that come up on a case-by-case basis, I tend to agree at this point in time that is probably what has to occur. But when three or four of these things start occurring very quickly,

that is very time consuming to do it.

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My question, what are you planning, where are we in ensuring we are thinking six months ahead, a year ahead or whatever so that we can keep pace? Another part of the question would be for example, I think I read in some of the documents that we were going to be somewhat dependent if not entirely dependent on the FASB standard to tell licensees how to do the reporting or accounting for some of the financial arrangements and that standard is clearly not coming down the pike for quite some time. Can we wait for that or do we not need to go ahead and be prepared on the front end so that everyone knows what is expected of us?

I know it is a very broad question. Maybe it is more of a statement than a question but I need to know where we are with this.

MR. WOOD: I think there are two things in answer to your question. The first is, we do have the default framework now on this dichotomy between electric utility licensees and nonelectric utility licensees and it really does depend on the rate treatment they receive. We need to fine tune that definition. But the basic definition and the basic concept, I think, is there.

So I think with that and, you know, for decommissioning and with our historic approach to inspections for operating plants and maintaining safety that way, I think we will be in pretty good shape. That doesn't

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mean that we can't do more but I think while we are looking at these things we have that already in place.

With respect to the FASB standard, there were two elements in the action plan and there was one element that was trying to do something short of rulemaking to get information on the status of decommissioning funds. It was almost serendipitous the way FASB's standard came out just about the time of that proposal and we decided that we would try to hook onto that as a good vehicle for getting that information. But it wasn't the only approach we had.

A second element in the action plan was to consider a reporting requirement that we would put in our regulations and that is considered in the proposed rule that you will be getting in a while.

So if the FASB standard doesn't go through, we still have that if you agree that that is an appropriate thing to do. We can have that approach too.

COMMISSIONER DICUS: What about resources? If we get into this much more intensive effort with acceleration, where do we stand with resources to cover it?

MR. MATTHEWS: Although that wasn't an item specifically identified in the action plan, it was obvious when the action plan was spawned that it was going to demand additional resources, not only from the standpoint of the immediate tasks that we had undertaken but as has happened,

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there are many collateral issues that have arisen.

The list that I keep on my desk of things that I need to look into or that the staff needs to review that we haven't had time to review gets longer by the day.

CHAIRMAN JACKSON: Where do we stand on the human resources?

MR. MATTHEWS: We've got two additional staff members that have been hired, authorized. One is on board, one will be here May 5. We have a third staff member who is

expected to be selected and hopefully come on board by the end of the summer.

CHAIRMAN JACKSON: At least one or more of these will be individuals with the kind of financial backgrounds that we need to do this?

MR. MATTHEWS: We would hope they all have that kind of background. They were specifically --

CHAIRMAN JACKSON: Well, at this stage of the game, we'll take --

MR. MATTHEWS: No, I understand. But we have some very qualified people that responded to our request. These were people outside the NRC. The first two individuals that we have hired came from the industry. One had a recent history with Entergy and Mid South in the financial planning and strategic planning area and another was an engineering economist most recently working with New York Power

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Authority but prior to that with PSE&G so they come from that background and have been involved are familiar with the kind of issues we are talking about in their current jobs before they came to work for us.

CHAIRMAN JACKSON: Okay.

Commissioner Rogers?

COMMISSIONER ROGERS: No, I have no more additional questions.

CHAIRMAN JACKSON: Commissioner Diaz, Commissioner McGaffigan?

Thank you very much.

We will call the federal and state regulatory panel. Thank you.

I think we will begin with Ms. Tomasky, the General Counsel of the Federal Energy Regulatory Commission.

Good morning and thank you for coming.

MS. TOMASKY: Thank you, Madam Chairman. It is a pleasure to be here.

CHAIRMAN JACKSON: You have to press the button. Thank you.

MS. TOMASKY: Madam Chair, members of the Commission, I appreciate very much the opportunity to come here today and share with you some information about the recent activities of the Federal Energy Regulatory Commission. I think everyone in this room, perhaps everyone

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in the country well knows that the FERC is strongly committed to developing competitive markets for electricity. Toward that end, we have initiated fundamental changes in our approach to regulation.

These changes we expect will encourage the development of competition in wholesale power markets and we believe will provide very significant benefits to consumers. We also believe that our rules will ensure a fair and rational transition to a competitive and reliable wholesale marketplace.

We understand that the NRC is vitally interested in the potential effects of these changes on the nuclear power industry. You have asked that I provide you an overview today of what the Commission has been doing and I would like to talk about four major policy areas of the Commission's activities. These are our requirements for open access transmission service, the recovery of stranded costs, recent actions with respect to market-based rates for wholesale sales of electricity and our merger policy.

I am sure you have a number of very specific questions concerning the intersection of our programs and

yours and I look forward to discussing those specific issues with you in questions after the overview and after we have heard from other panelists, if you like.

The centerpiece of the Commission's electricity

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policy initiatives is Order Number 888. In Order 888, the Commission has required all public utilities under the Federal Power Act to file nondiscriminatory open access transmission tariffs. Under these tariffs, transmission owning public utilities are required to provide transmission service to wholesale buyers and sellers on the same terms and conditions that apply to the transmission owner itself. In other words, the transmission owning utility can no longer restrict access to its transmission system to favor its own generation.

To ensure that access to the transmission system is not subject to manipulation, the Commission in Order 889 has also required public utilities to functionally separate their power marketing and transmission functions. A public utility is also required to have in place an Internet accessible computer information system known as an OASIS. This permits perspective transmission customers to know what transmission capacity is available on the system and at what price.

Open access transmission is now a fact of life across the industry. There are a number of many difficult issues yet to be resolved. I am sure we will be discussing many of them today because they do affect the nuclear industry. However, there is little dispute, I think, over the fundamental principle of open access. Most

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jurisdictional utilities have timely implemented their open access tariffs and they are really busy figuring out how to do business in an open access environment.

Let me now then turn to another critical element of the Commission's open access policy, which is the treatment of stranded costs. In the coming competitive marketplace we believe that utilities sellers ultimately are going to have to compete on the same basis as other sellers. But we are also aware that in the past utility investment decisions including nuclear investment decisions were made under wholly different expectations and within a different regulatory framework. That is, of course, the cost-based regulatory framework with which you are familiar and with which for many years we have regulated the utility industry.

There is no question that a competitive marketplace and, in particular, the Commission's requirements for open access create the prospect that customers are going to depart the system. The consequence of them leaving the system is that some of the costs associated with the utilities providing power to their traditional customers can be stranded. There is no question that the stranded cost issue, which is the price tag for open access in our view, is the most hotly contested issue associated with Order 888.

In Order 888, the Commission studied thousands of

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pages of comments on this issue from over 400 commentators and we came to the conclusion very firmly stated several times in various iterations of the rule that utilities should be given an opportunity to recover all verifiable and prudently incurred stranded costs. In our view, stranded costs associated with the rule are costs that occur when a

customer departs the system and then uses the supplier's transmission system to access new supplies.

Recovery of stranded costs from a particular customer is going to be determined on a case-by-case basis under the Commission rules and, as a result, many of the questions I think we will likely explore today about what stranded cost recovery really means we expect to evolve in the case-by-case process. As a general matter, the utility will bear the burden of demonstrating that it had a reasonable expectation of continuing service beyond the term of a contract in order to receive what we call the extra contractual stranded cost recovery.

But I think it is important to note that the Commission in Order 888 did not abrogate existing requirements contracts so that customers who are obligated contractually to stay on the system would do so and continue to bear their cost responsibility. Again, on a case-by-case basis, the Commission could consider opening up those contracts and, in that context, we would expect to deal with

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the stranded cost issues if we were going to permit the customer to depart that system early.

Clearly, we think that a fair transition to competition includes stranded cost recovery but, as the prior panel's discussion, I think, made very clear, the vast majority of stranded costs are likely to be generation costs incurred to serve retail load that will be stranded as a result of state retail choice programs and, as a result, the vast majority of the challenges involved in dealing with stranded cost issues are going to fall to the states.

We have done a number of things in Order 888 that we think accommodate the states' move to retail access if they chose to do so and we have certainly encouraged the state commissions to address these issues up front as they proceed with retail choice.

Let me mention briefly the FERC's policies governing market-based rates for wholesale sales of electricity. For several years now the Commission has been ruling on applications of wholesale sellers including power marketers to sell electric power at market-based rates. We have some complicated proof procedures that are required for utilities who need to demonstrate the lack of generation market power in order to sell from existing generation but we do have a number of utilities including some nuclear utilities who are selling off system at market-based rates.

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We generally expect this trend to continue. Our review process for market-based rates really has to do with issues of generation market power, whether or not we believe that if a seller sells into a particular market it is likely to dominate that market and therefore it will be able to elevate the price for a sustained period of time. If we are satisfied that generation market power is not present, we will permit -- or it has been mitigated, we will permit the seller to move to market-based rates.

Let me mention one last area which is the Commission's actions with respect to its merger policy which your staff had indicated that you had an interest in.

In December 1996, the Commission issued a statement of policy that will govern future review of applications for public utility mergers. We are doing a fairly brisk business in merger application review recently. It is certainly something that many in the utility are understandably turning to and is something that business

typically turns to under -- when economic circumstances change in order to realign themselves in order to face new challenges. That is something that our Commission certainly expects from the utility industry.

We do not want to discourage that. At the same time, mergers that actually reduce the number of sellers in a marketplace do have the possibility of raising competitive

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concerns. We have worked for a number of years attempting to open up these marketplaces to a variety of sellers so it is natural that we would want to look at these mergers to be satisfied that the anticompetitive effects are not so significant that the merger should be disapproved.

The merger policy statement lays out the criteria by which we are going to evaluate these mergers in some detail. I think it provides expedited procedures for mergers that don't raise competitive concerns and it also provides hearing and other procedures and certainly a more scrupulous inquiry where our initial screen suggests there are concerns.

The last issue I want to mention, Madam Chair, has to do with the issue of reliability which I know you have addressed extensively yesterday. The FERC very much supports the efforts of the North American Electric Reliability Council to take the lead on reliability issues. There are some challenges, unquestionably, that restructuring of the utility industry will pose and we have certainly encouraged NERC to take the lead in attempting to address them.

The Chair of our Commission recently testified before Congress on these issues and she stressed in particular her concern with the fact that NERC membership is not mandatory. She recommended that Congress ought to put

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the FERC in the position of ensuring that NERC standards do become mandatory and to be able to provide mechanisms for enforcing those standards and for compliance. We do not have a specific proposal on this issue and we have again continued to encourage the efforts of NERC to open up its memberships to all the likely participants in power markets so these issues can be addressed.

That concludes my general remarks. Madam Chair, members of the Commission, I would be happy to answer questions.

CHAIRMAN JACKSON: Thank you very much. I think I would like to ask you a couple of questions.

With respect to FERC's position on the stranded costs issue, and you mentioned a case-by-case approach and your prepared, submitted remarks spoke of FERC as being a forum for stranded cost disputes, would you expect to have explicit consideration of decommissioning funding costs as part of your consideration of stranded cost issues?

MS. TOMASKY: We certainly would, Madam Chair. The Commission did mention in Order 888 and in our rehearing order that we believed that nuclear decommissioning costs were appropriately considered to be stranded costs and would be dealt with on a case-by-case basis. I would imagine as those case unfold we would continue to observe the traditional relationship with your Commission. I do not

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imagine that our Commission has any interest in second-guessing issues of how decommissioning occurs.

We have traditionally looked at, in determining

how decommissioning costs are put into rates now, we have traditionally looked at issues, the estimates, and those are frequently litigated amounts. We actually just set for hearing a case involving Connecticut Yankee in which we expect those issues to be resolved.

That was not a classic stranded cost case, a restructuring stranded cost case in the sense that departing customers were leaving the system and therefore we were being asked to address how to tread nuclear decommissioning costs in that context. But I have every confidence that our Commission takes that very seriously and we would expect those issues to be worked out along with others in these proceedings.

It is, admittedly, a somewhat more difficult issue than simply attempting to figure out what the present value is of a remaining obligation, reduce it to a current form and then decide how it is going to be paid. We understand that there are uncertainties.

But I just want to stress that we had enormous success in the natural gas restructuring with settlement of many of these issues. We have in fact in front of us a case with NEPCO that is currently in hearing and I understand

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that technical conferences with an eye or a hope for settlement are going on and that many of those -- that indeed involves a dramatic restructuring of the buyer/seller relationships for that company and we are very hopeful that these issues will be resolved.

CHAIRMAN JACKSON: Do you have a position with respect to the issue of foreign ownership control or domination, as you know, the different business forms occur?

MS. TOMASKY: Our Commission doesn't have a position with respect to that. If I could interpret a bit from our merger policy statement, I can say that it is something that gave us very little concern. We believe and fully expect that ownership is going to move all over the place, quite frankly, with respect to the electric utilities and we think that the movement of capital is a pretty good thing.

We do not attend to issues of national security as you do. Not that we don't think they're important but we understand it is your job, not ours. And those are the kinds of things that would inform those kinds of concerns.

What we have dealt with in the context of foreign investment have been issues of reciprocity with respect to transmission access. Those are policy concerns that are pertinent to us and our considerations.

We also understand, obviously, that the SEC

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regulates sort of quantities of investments and there are issues with respect to foreign holdings under the Public Utility Holding Company Act but that is not something that our commission has gotten into and, quite frankly, given our focus on competitive concerns and concentrations of generation market, it may well be that the farther away the merging entity is from the utility the better our Commission likes it.

CHAIRMAN JACKSON: You mentioned that FERC should have the authority to make, for instance, compliance with NERC standards mandatory. This is on the issue of grid reliability, et cetera.

Have you proposed, and I think maybe you did address this but I am going to ask again, specific legislative language that relates to any kind of a federal

backstop for NERC's activities and actions?

MS. TOMASKY: We have not proposed specific legislation. We have certainly recommended to the Department of Energy that they address these issues and I would expect that the Chair of our Commission who we expect to be headed that direction will carry that general policy initiative with her.

I do understand that it has been very much on DOE's mind. There are lots of debates that go on about how much authority we do and don't have. We had suggested that . 46

we be the repository for it because we have certainly attempted to recognize NERC standards in the context of our open access tariffs and, in recent discussions with DOE, as they were talking about downsizing, they seemed to want some of the interconnection authority that they have, or at least they were discussing the possibility of interconnection authority with the FERC. It is a job we think we can do. We do not have specific legislation in mind and I assume that the ultimate formulation will work its way through with the Administration interagency review process.

CHAIRMAN JACKSON: Do you have any specific positions with respect to ISOs, their formation, membership, mandating their formation, et cetera?

MS. TOMASKY: Our Commission was encouraged, in the context of Order 888, to mandate ISOs as a means to remedy undue discrimination. In essence, to separate the generation function from the transmission function. We decided not to do that.

We went a regulatory path that we call functional unbundling where we required that as an operational matter that the generation and transmission functions be separated within a utility and impose standards of conduct to be imposed by employees to ensure that that separation was effective. Nevertheless, the Commission has strongly encouraged the formation of ISOs and the investigation of . 47

ISOs, particularly in the context of the reform of tight power pools, which is going on in several regions of the country.

We have ordered the tight power pools to restructure their transactions to unbundle transmission and generation transactions and also to address other aspects of our undue discrimination rules and most of them are turning to some form or the other of ISOs to go forward. There are legitimate -- you know, ISOs are a dream in pursuit of realization in a lot of parts of the country and we think a very useful dream. There are legitimate debates over whether an ISO makes sense except on a broad regional basis and certainly in terms of pricing efficiencies and operational efficiencies, we see a lot of benefits in ISOs.

We have been asked to mandate it. We have declined to do so, so far. The issue of mandating ISOs arises in several merger cases we have and that is another context in which we would examine them. So I guess the short way of saying it, we think they are a good thing and we are doing our best to encourage them but we haven't mandated them yet.

CHAIRMAN JACKSON: Okay. Let me ask you one last question for the time being.

We are North America.

MS. TOMASKY: Yes.

CHAIRMAN JACKSON: And that implies interconnectivity of the electrical network to the north and to the south. Are there any government-to-government activities or initiatives that need to occur to deal with the issue? Again, I am thinking from our point of view having to do with the interconnectivity and its effect on the reliability of the grid.

MS. TOMASKY: Well, first of all, we absolutely agree with you and I think while we do not believe, I think that there are specific issues associated with restructuring and reliability that are critical, clearly exchange of information is absolutely essential.

We would like to see and have taken some steps to try to encourage the Canadian provinces and the publicly owned utilities up there to make open access a rule of law for them as well. We -- in particular, if they are trying to do business in the United States and marketing their power down here.

We have essentially imposed a reciprocity requirement, a do-onto-others requirement, in effect. If they want to do business down here, they have to make their transmission systems available. We would like to see dialogue on those issues.

With respect to reliability, it seems to me that NERC is quite aware of the interconnection issues and we

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have, although we have challenged NERC in a number of significant respects to open up their membership, to attempt to evolve their standards to meet some of the new and different issues associated with restructuring, for example, the multiplicity of sellers that they will be facing moving power into the grid, the issues that I know have been identified by you, Chairman Jackson, over the question of incentives for maintenance.

But we ultimately believe that NERC needs to take the lead and that the FERC has appropriately a follow-up role in enforcement.

CHAIRMAN JACKSON: Commissioner Rogers, Dicus, Diaz?

COMMISSIONER DIAZ: Based on what little I know about Mexico's grid and rates, has a thought come through about the difficulty there would be to bring Mexico into some common standard as far as free market? Because they really don't.

MS. TOMASKY: I know about this, Commissioner, only anecdotally, actually. We have had some conversations with Mexican officials who have come to our Commission seeking sort of structural advice on how to deal with rate regulatory issues.

I know that they are attempting to make some progress but I understand it is a very difficult and slow

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process there. They have very significant infrastructure issues that would make -- that have raised some concerns about interconnection with the United States. I also know that there is a lot of interest in simply locating power plants along the border to move power into the United States and that that has created some environmental controversies.

But I do not know of a systematic approach to these issues other than, I think, the very good faith efforts of Mexican regulators to try to develop a regulatory system for them that makes sense.

COMMISSIONER DIAZ: Thank you.

CHAIRMAN JACKSON: Commissioner McGaffigan?

COMMISSIONER MCGAFFIGAN: To follow up on the Chairman's question, you basically are proposing that NERC membership be made mandatory in this country and that there be an enforcement and compliance mechanism that is also mandatory through NERC. My recollection yesterday is that we have most of Canada and just a little piece, around Tijuana or whatever, of Mexico in NERC.

Does Canada have to do the same thing in terms of mandating NERC membership and mandating that if we want to ideally get the system, mandating a compliance structure? I think to just be more specific in following up the Chairman's question.

MS. TOMASKY: To be fair, Commissioner, I don't

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know that we have or that Chair Moler has formed a view. We certainly have been reluctant to tell Canada what to do in terms of handling these issues. But I certainly see the benefits of symmetry are certainly attractive.

The issues aren't going to change when you go north of the border. I do not know that Canada is facing the same questions associated with restructuring but I would also emphasize that the reliability issues that have come to attention recently are not necessarily associated with restructuring. The outages that happened in the West, for example, have nothing to do with the Commission's restructuring initiatives or, for that matter, the proposed restructuring initiatives in California.

So the reliability issues are there. They don't stop at the border and it strikes me that the prudent thing to do would be to engage in discussions with the Canadian government if our administration decides that is the right course, to let them know what is going on and to suggest to them that comparable requirements on the other side could be useful.

COMMISSIONER MCGAFFIGAN: The other question I have is you regulate wholesale transmission and you are very careful to point out that on the retail side, that's the states' responsibility. Although in a paragraph you didn't read, you said there is work to be done on the federal/state relationship.

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If you go to the decommissioning cost issue, when you look at an individual case, are you looking at the part of decommissioning costs which you say in your statement is the smaller part that relates to wholesale and what is the mechanism for looking at the total, the totality of decommissioning costs? If you are regulating 10 percent and the states are regulating 90 percent, how does that work?

MS. TOMASKY: The answer -- the simple answer to your question is, yes, we have the small piece of it. The larger answer to the more important piece of your question, which is how does it all work together, is we've got to figure that out.

We actually have jurisdiction over transmission in interstate commerce, which would actually include unbundled retail transmission. But with respect to stranded costs, the critical jurisdictional issue under Order 888 is jurisdiction over the generation.

We basically regulate wholesale sales and, as a result, costs incurred to serve wholesale requirements customers and coordination customers are the basically are the kinds of utility costs that we are talking about and that we regulate. It is a small piece of the pie. There is

no question about that.

With respect to some utilities, some nuclear

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utilities have structured themselves as wholesale suppliers and, in those cases, those issues come before us entirely and we would handle --

COMMISSIONER MCGAFFIGAN: Connecticut Yankee is that sort of case, isn't it?

MS. TOMASKY: Yeah, the NEPCO case is an example of that. There are -- most of the utilities around the countries, however, are not structured that way. State commissions can intervene in our proceedings. We have indicated that in the context of state restructuring proposals, we would give considerable deference to what the states do.

I don't think there is going to be a big overlap but there may well be questions of how to deal with gaps in the numbers between what the states would do and what we would do.

The Commission traditionally on costs, we have dealt with these things strictly as cost allocation issues. It is not, in that sense, a new rate issue for the Commission. Generation facilities are often shared and we do an allocation that we think makes sense and states do an allocation that they think makes sense and sometimes it adds up to more than 100 percent and sometimes it adds up to a bit less.

We are probably going to have to pay a bit more

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attention to that number in the context of nuclear decommissioning and I would expect that to certainly be something that would be pursued. I also do expect, though, that as you have seen, that most of these restructuring proceedings that states undertake are going to, if they are done with the full cooperation of the utilities and the local parties, they are going to end up with a solution to these issues and something that our Commission could easily defer to if there were a settlement or at least something approaching a settlement that appeared to make sense.

CHAIRMAN JACKSON: At this point, is FERC considering any additional actions or any legislative changes that would clarify the issues? I guess I am trying to get you to elaborate a little even beyond what you have already done on the clarification of questions of state versus federal responsibilities.

MS. TOMASKY: There are some issues that I don't -- don't necessarily go to the issues of stranded costs that we have been interested in having dealt with in legislation. I think that it would probably be useful for me to elaborate a bit on the kind of jurisdiction that FERC is asserting under 888 because it is a matter of some controversy. It is not categorically true that we would never deal with retail stranded costs. Essentially what we said was that stranded costs arising from the departure of a

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wholesale customer is our job.

If we had indicated that there is a gray area, which is what happens when a previously retail customer leaves the retail system, becomes a wholesale customer through a municipalization or something like that, and strands retail assets, in that circumstance, our Commission has determined that it would assert primary jurisdiction with respect to the recovery of those stranded costs.

The theory for doing that is that we believe that

the stranded costs are the result of the availability of open access tariffs that the Commission created. If there were not open access tariffs available, the municipalization and the opportunity to leave the system would not be available. And on that basis, the Commission has indicated it would assert primary jurisdiction there although, of course, if a state had already acted to deal with the stranded cost recovery in some fashion we wouldn't permit double recovery on the part of the utility, we would deal with it through some sort of crediting mechanism.

With respect to what we call pure retail stranded costs which are occasioned by a state retail access program, we have indicated that the only instance in which we would step in would be to fill a regulatory gap where the state commission determined it lacked authority to deal with this. I should point out that all of the states that have been

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pursuing retail access programs thus far have understood that the stranded cost issue was an important one and one to deal with and dealt with up front and so there hasn't been any occasion for people to come to us and say, it's time for you to get involved.

We also tried to make clear in 888 that we weren't a forum for second guessing the substantive decisions of the state but, simply, a forum to deal with stranded costs if the state lacked the authority to do so. So that is the context, sort of the detailed context that I have sort of broadly summarized before.

CHAIRMAN JACKSON: Right, thank you.

You know, FERC and the NRC have established a -- I could have called it NURC but it would have caused confusion -- a valuable working relationship and it has allowed us to share safety concerns with you as you make your economic regulatory decisions. And it has been effective, we think, to the NRC in addressing areas of mutual interest.

But do you see any additional steps that might need to be taken to assure that areas of shared concern are incorporated in our respective policies and are there any areas of overlap or duplicative review that you think could be eliminated to provide more efficient and effective regulatory oversight in these areas?

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MS. TOMASKY: Well, I totally agree with you, Chairman Jackson, that we have taken the most important step which is that we are now talking to each other a lot and our staffs continue to talk and I know the discussions that have happened recently where we just explore issues and come to an understanding have actually revealed, I think, that there are fewer problems than people might think in ensuring that your responses to competition and our responses to competition are entirely consistent.

I think that in terms of potential overlap, I think that when we get into case-by-case determinations of stranded costs and decommissioning that the NRC undoubtedly has a vital interest and we would expect to hear from you from those cases, in those cases, and we certainly would value your contribution and your judgments very highly in those cases. We have, I am sure you well know, rigid rules about ex parte communications and things like that but, within, we can certainly work out appropriate ways for you to contribute your views in those cases and I think it would be very useful. Yes, there is always a potential conflict,

potential for conflict, but I think that they are completely reconcilable.

There has been a lot of talk in terms of overlap about your antitrust review and our competition review. I do not have a judgment as to whether or not one or the other .

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is duplicative. I know we think ours is pretty valuable and we would like to hold onto it. As to whether or not you believe that your antitrust review remains appropriate, let me emphasize that we have never found it to conflict with the exercise of our jurisdiction in any way.

I think that my understanding of some of the open access license conditions with respect to transmission have probably been overtaken by our open access tariffs. I understand most of them to be company and perhaps even transaction specific and our open access tariffs which are available to all comers are probably the best way to move power right now under a tariff. I think that is what most people are doing.

I think that, ultimately, you are in the best position to judge and to recommend to the Congress the enduring validity of your antitrust considerations.

CHAIRMAN JACKSON: Thank you.

Further questions?

I think we will -- we don't mind if you stay.

MS. TOMASKY: I'm happy to stay. Thank you.

CHAIRMAN JACKSON: I am going to turn to Mr. Ellsworth, president of NARUC, to talk about your part of the presentation.

MR. ELLSWORTH: Thank you very much Chairman Jackson, members of the Commission. On behalf of NARUC, we .

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appreciate the opportunity to come and share with you our overview of the status of restructuring among our members.

If it is acceptable to you, the presentation this morning will be made by Commissioner Gee of Texas, who chairs our Committee on Electricity. Commissioner George from Iowa who chairs our subcommittee on nuclear issues and I will stand ready to answer any questions that you may have of us following Commissioner Gee's presentation.

CHAIRMAN JACKSON: Thank you.

MR. GEE: Thank you, Chairman Jackson and members of the Commission.

It has been almost a year since the NARUC leadership had an opportunity to visit with you to talk about restructuring activities and I think it is fair to say, as you know, based upon the presentation of your staff this morning, much has occurred.

CHAIRMAN JACKSON: Yes. And I must say, I have to insert, and you knew I was going to zing you on this, because I think when we met you said nothing much is going to happen for a while.

[Laughter.]

CHAIRMAN JACKSON: So I just had to put that onto the table.

MR. GEE: There is a lesson there; never say never.

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In fact, a great deal has occurred and I would like, in a few brief moments today, just to hit the high points of our prepared statement so that we can entertain questions that I know that you have of President Ellsworth as well as Commissioner George with respect to what has happened.

Since we last met with you, the National Association of Regulatory Utility Commissioners has adopted a statement of principles to guide our member commissions in the path of restructuring and that is accompanied in our prepared remarks today. It sets out some guideposts as a recommendation for our member commissions to follow as they go about the process of restructuring. You will note that it touches upon such critical matters as maintenance of reliability in a restructured market, the need for states to address fairly and equitably the concerns related to stranded costs as well as maintaining the imperatives of continuing to provide universal service to all customers.

Since we last met, 10 states have adopted statutes or the state commissions already have proposed reforms to restructure the retail markets. Nine of these 10 have acted within the last 10 months. This represents fully one-third of our nation's population which is now being subjected to significant restructuring of these retail markets.

I am told and my information that we provided to

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you so indicates that all states except one in the United States are at least considering or have already adopted reforms of retail markets. That single state that has not done so, I believe, is Tennessee which, as you know, is generally made up of the Tennessee Valley Authority, which is not subject to state regulation.

Generally, restructuring has occurred initially from what are known as high-cost states, that is states that have a great deal of embedded generation cost that are above current market prices. The process began generally in the northeastern states as well as California. Since then, however, a number of what are known as low-cost states have also begun taking the initiative.

I would update our prepared remarks to inform you that since we prepared our remarks the state of Oklahoma, its legislature, both the house and the senate, have approved a bill that would open up their retail markets by the year 2002. It is anticipated that their governor will probably sign that into law within the next 30 days. Also the legislature of the state of Montana also has adopted restructuring legislation, also to provide for retail competition by the year 2002.

Those two states are generally known as low-cost states. They have some flexibility by way of moving to open up the retail markets primarily because they bear minimal

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stranded cost concerns. Neither state, I am told, has any nuclear power capacity and I believe that they are moving forward to open up their retail markets in order to provide competitive opportunities because they see that that is generally the trend that is occurring in those states that have higher cost responsibility.

My own state is also within the category of states that are low cost. There are bills that are being actively debated and considered as we speak in my state legislature and the time frame that is under discussion is around 2001 and 2002 by which my own state may open up its retail markets.

Turning to the critical issue of stranded costs, as I indicated, NARUC's position is that its member commissions should all address fairly and equitably the concerns raised by utilities with respect to their having incurred verifiable stranded costs that would be rendered

uneconomic in a competitive market. With respect to the nuclear industry, as you know, those stranded costs generally fall in two categories, those representing embedded fixed plant costs and decommissioning costs.

The critical question being addressed at the state level as they move about restructuring is to what extent should such costs be placed -- the recovery of such costs be placed at risk in the market or should there be other

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mechanisms to make more certain the cost recovery for those concerns.

I am pleased to report and I believe your staff alluded to this that two states that have addressed the question of decommissioning cost recovery, California and Pennsylvania, have opted to maintain the revenue stream for collection of those costs through a nonbypassable wires charge. I am told that in California that is already explicitly provided for in their statute.

In the Pennsylvania case, the statute provides the commission to make a determination of the extent to which those costs should be included in a nonbypassable wires charge. That decision, as I understand, is still pending. It has not been made yet but it is certainly something that is critical on the agenda within the state of Pennsylvania to address.

I think it is fair to say that in my conversations individually with state regulators as to the activities going on in their commissions, each of them places a very high priority on the continued recovery of decommissioning costs under any restructured scheme. In terms of critical issue priority, I would say that is probably at the highest level, among the highest levels if not the highest level in all of the restructuring discussions.

Additionally, measures to address the fixed cost

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recovery concerns associated with restructuring have also been addressed by either the state commissions or the legislatures. One means of addressing a potential uneconomic fixed plant cost is to accelerate those costs. That is a measure that has been undertaken in California. I believe also South Carolina has opted for that approach to ease the transition.

In my own state, even though our legislature has not yet decided to open up its retail markets, our commission has made a decision in one major utility case to permit acceleration of potentially stranded costs on a current basis to ease the transition to the potential competition in retail markets.

Another measure being used to provide for better means of cost recovery is the concept of securitization. I know you have a presentation on that later today. Suffice it to say at least two states have already adopted that approach.

The state of California has adopted an approach whereby the state has enacted a statute that provides for the backing, the assurance of a revenue recovery through a competitive transition charge. That would enable the utility to sell an asset of a revenue stream representing a share of these uneconomic costs in order to be able to recoup a measure of cash in order to buy down those

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uneconomic costs.

The state of Pennsylvania also has adopted a similar approach and it is my understanding that this

approach is being under -- is under consideration in a number of states and state legislatures where restructuring is being contemplated.

Also, again, returning to the issue of decommissioning, NARUC itself as an association is placing a high priority on attempting to provide its members guidance with respect to the treatment of decommissioning costs in a restructured environment. We are currently within NARUC attempting to put together a dialogue on decommissioning cost recovery in a restructured market.

As part of that dialogue, we have directed our staff to come up with an issues list and to make recommendations on what would be the proper forum by which we could gain a broad-based cross-section of representation of all interests to see if a consensus can be reached within a collaborative forum to make some recommendations that our member commissions could use as guide posts. Your staff is part of that process within the NARUC staff. We welcome their participation, we think it is critical.

Commissioner Emmitt George is leading that process and I am sure he can fill you in on the details. We do anticipate that that dialogue will be getting under way

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within a matter of the next few months.

Finally, in closing, let me address some of the matters with respect to the concerns of reliability and also with respect to adoption of the approach, as we have seen, of adopting an independent system operator. I know that you devoted a great deal of time to the question of reliability in your workshop yesterday and I won't cover new ground.

NARUC has not yet taken a position endorsing the concept of an independent system operator. There have been a number of our member commissions that are active in NARUC that have individually endorsed the concept of an independent system operator that is truly independent from the ownership and control of transmission owners.

One of the critical concerns in moving toward adoption of an ISO approach is the question of what is truly independent and I know that that is a matter that is under debate in various forums since there is no common model of what an independent system operator ought to look like.

Another concern I have heard is the question of how does reliability mesh, the imperatives of reliability mesh with the desires to shift control and operation away from those that own the transmission grid to a new entity that does not have ownership but may well have responsibility for also playing a part in maintaining reliability through dispatch decisions. That is also an

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issue that I know is being addressed in a number of areas where the discussion of how the shape of an ISO is to occur, how can reliability be maintained consistent with the need to attain a measure of independence of control of the grid apart from ownership.

In my own state, in Texas, we adopted a rather simplified approach to that because we have a reliability council that is wholly contained within our state. We simply allowed our reliability council to become the independent system operator. That approach has worked well thus far but we are closely monitoring that to ensure that all concerns of the users of the grid are met and are handled in a manner which is perceived by them, anyway, to be done in a fair and nondiscriminatory basis.

Again, let me thank you for the opportunity to address you today. As I indicated previously, we appreciate the continued participation of your staff in NARUC's efforts to give us guidance on the imperatives of your Commission as we attempt individually to try to address these critical concerns of restructuring our retail markets.

I am available to answer questions as are President Ellsworth and Commissioner George.

Thank you.

CHAIRMAN JACKSON: Thank you.

Let me preface my questions to you with a comment

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which I probably should have prefaced everything with today. And that is that in a certain sense we have a nice, clean task. You know, we are health and safety regulators and so we are trying to ensure that our issues are dealt with because if they aren't then that triggers the need for us to take some action the way we can, which is with respect to our licensees.

In doing that, and this is as much a comment as a question to you, have you considered that in a certain sense, in mandating competition, that to the extent that there aren't either transition or overarching strategies for dealing with what are health and safety related issues, that in the end you propagate into how competitive an environment you will or will not have?

What am I saying? I am saying, for instance, if we take the issue of decommissioning costs, that that is something that absolutely we have a responsibility to ensure is available. It is ultimately a health and safety issue and it is an issue that impacts your individual states. That is, to see the nuclear facility is completely and appropriately and safely decommissioned.

If, in fact, there aren't strategies to either create continuing revenue streams and the like, that triggers requirements we have to place on the nuclear utilities. If that is the case, one could argue that that

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puts them at a competitive disadvantage. I am dealing strictly with the narrow issue of decommissioning costs as opposed to the larger issue of stranded costs. But it is something that is an absolute health and safety requirement. So I just kind of give you that, you know, in the background.

So my question, first question to you is, what are -- you mentioned NARUC guidance to its members with respect to decommissioning costs. What are the key elements of that guidance as it has evolved to this point?

MR. GEE: Right now, our efforts are only informative because we are attempting to catalogue the host of different policy concerns related to restructuring as they may affect decommissioning costs.

I can say that among them would include, automatically with or without restructuring, the sufficiency of decommissioning cost funding and whether, in a restructured environment, which might lead potentially to premature retirement of plant, whether we would aggravate what might already be an insufficient level of funding that has been accrued in a going-forward basis. That is of deep concern to many of us who have not yet made the restructuring call in our individual states and would like to look, by way of example, to what is being done in other states to address both the sufficiency of existing funding

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as well as maintaining a common level of guaranteed funding in a restructured environment, such as the adoption of an approach as in California, for instance, and whether that is the way that most states ought to be headed as they open up their markets for retail competition and decide that a measure of generation is going to be placed within the market and susceptible to market forces.

We are hopeful that we can identify these issues and then from that make recommendations to our member commissions who have not yet made restructuring decisions that they can then take back to their respective state legislatures who, ultimately, are the ones that have the say so, whether or not to open up retail markets, and that those recommendations can be given sufficient weight or a heavy degree of weight in any restructuring proposal that is ultimately adopted by state legislature.

Commissioner George, I think, can speak more specifically on some of the issues that have already come up on the screen with respect to decommissioning funding that our staffs, our respective staffs, are looking into.

MR. GEORGE: I think that the issue that brought this to our attention and I dictated that we needed to address the notion of decommissioning in a generic sense was the conference in Ft. Meyer last January.

There was a presentation there by one of the
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speakers with regard to the tax credit associated with decommissioning and if there is accelerated decommissioning, as has occurred in California, that a company would not be able to recover the accelerated cost but would have to only take the depreciation over the planned life of the facility.

That raised the question that there are a number of issues surrounding decommissioning that commissioners will have to face as we go forward with this process. Many states have not taken any action or addressed these issues in any way while several have actually gone through legislation.

But what I suggested is that we needed to sit down and identify all of the issues and, in terms of the guidance that Commissioner Gee suggests NARUC gives to its membership, that that guidance is or at least in this instance will be an identification of what the issues are and a discussion of what the potential resolutions might be, leaving to the state commissions or state legislatures the policymaking decisions in the final analysis as to how they might proceed.

It is an opportunity and an effort to inform as opposed to direct what is done at the state level.

CHAIRMAN JACKSON: What kind of time line are you operating on to come forward with this guidance?

MR. GEE: We initially thought that we might start
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this process prior to our summer meeting in July. Whether that occurs or not really will depend on our full electricity committee which this matter will be presented to within the next 30 days. We have actually discussed it at that level but a formal presentation will be made to them in the next couple of weeks.

CHAIRMAN JACKSON: This is an example of where there is a nexus between the issue. You know, your consideration in the economic realm, such as a tax credit for decommissioning costs, and how that might get impacted by an accelerated amortization schedule for decommissioning

funding because that, in fact, is something that we would have to consider for those entities that no longer meet our definition of an electric utility. In a certain sense, it is already built into our existing regulatory framework.

So I would urge you in a timely manner to move along with what guidance you might come forward with for your members because we are going to move along in terms of what we have to do but we are not looking to put those utilities that happen to own nuclear assets at a competitive disadvantage relative to those that are not.

At the same time, we have a health and safety responsibility. But I think it is a shared responsibility that, in the end, you also have. Because the nuclear assets in your states were built under certain presumptions about . 73 cost recovery and the like. But, in the end, we have to do what propagates into our regulatory regime.

Mr. Ellsworth?

MR. ELLSWORTH: Madam Chairman, if I can take off my NARUC hat for a minute and put on my New Hampshire hat, although we recognize your legal responsibility for health and safety, I assure you that we have at the state level at least a moral obligation because it was we who assisted or participated in the bringing of those power plants on line in the first place. So if there were health and safety problems, it would be our reputations as much as yours if there was a failure.

I can tell you in New Hampshire even in the absence of the specific principles that we at NARUC are working toward, that the state regulators have principles of their own in mind to assure the decommissioning costs are going to be covered. We have state laws to require that decommissioning costs are identified and provided for. We, in our restructuring orders, have made provisions to assure that they are nonbypassable.

So even in the transition, states have those issues very much in mind and have health and safety very much at the forefront of those decisions.

CHAIRMAN JACKSON: Are any of you dealing with the issues of where in the creditor queue decommissioning costs . 74 should stand or where in the queue they should be relative to bankruptcies in your states?

MR. GEE: That is a very good question. I will give you as honest an answer as I can give you.

Ironically, it has not come up yet, even though we have had a bankruptcy in our state of an electric utility that had some nuclear generation. And the same, I know, holds true with Commissioner Ellsworth.

You have before you two commissioners from the two states where there have been major utility bankruptcies. I don't recall, frankly, the question of exactly where the priority of decommissioning funding falls within this bankruptcy queue priority. I do know that the way the restructured bankruptcy occurred in our state, it did set out a list of priorities and I would have to go back and check the record, and I can provide that information to you.

But I do know that while the bankruptcy was pending and ultimately after it emerged from bankruptcy, there was no immediate concern that the impaired financial integrity of this particular company was going to harm the continued and safe operation of the nuclear power plant. I believe that it owned a fractional share of this plant.

CHAIRMAN JACKSON: Right. I think that's the

reason.

MR. GEE: Seventeen percent, I believe, of Palo

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Verde was held by El Paso Electric.

MR. ELLSWORTH: In terms of collection of decommissioning costs, my recollection, in our bankruptcy, because we have a separate statute that requires the collection of those costs that the bankruptcy did not affect the collection of those costs.

CHAIRMAN JACKSON: Does --

MR. GEORGE: Commissioner Jackson?

CHAIRMAN JACKSON: Yes.

MR. GEORGE: If I might comment, Iowa does not have a utility in trouble but I think that the priorities that are set with regard to a bankruptcy are set by Congress. States have some provision with regard to personal effects that are protected from bankruptcy but the state laws are all preempted.

CHAIRMAN JACKSON: Right.

Does NARUC endorse the concept of mandatory NERC membership by whomever operates transmission facilities?

MR. GEE: We have not taken a position on that specific matter. What we have said, and I think our statement of principles does indicate and, in fact, it is probably the one of the first principles there, is continued reliability above all else must be maintained in a restructured economic market.

We have been working very closely with our

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utilities to ensure that no matter what economic decisions we make with respect to opening up market opportunities to new entrants, that the imperatives of reliability must continue to be met and, to the extent that there is a cost associated with maintaining that reliability, we will make efforts to ensure that, if need be, those costs are commonly borne and shared by all rather than simply subject to recovery in a competitive market.

But, no, we have not officially taken a stance on recommending mandated membership in NERC.

CHAIRMAN JACKSON: You mentioned with respect to the ISO concept a good question is what is truly independent. And you talked about how reliability would mesh with the shift of control to, you know, an entity without ownership.

Do you view the efforts going on in terms of the Midwest ISO to be a potential model for how to address the issue?

MR. GEE: I am not that familiar with that particular ISO and the discussions that they have been having other than what I generally read through the trade press to be able to respond adequately to your question.

As I indicated, the concept of an ISO varies from region to region and what we are seeing grow out of this process is a variety of different approaches. I do know

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that a common concern that I have heard is who is ultimately responsible for making sure that the grid is maintained and whether reliability is -- whether the grid ultimately continues to have the same degree of reliability when you try to divorce control and ownership.

CHAIRMAN JACKSON: Does it present the state utility commissions with an inherent conflict of interest in the sense that, you know, to truly have an independent

system operator may require some transference of regulatory authority with respect to grid management, planning, et cetera?

MR. GEE: I think that is a very good question. I think, in fact, it does pose a question of to what extent can a state commission or a state regulator have sufficient jurisdiction to cover what is essentially a regional entity that is making control and operations decision across the grid. I do know that generally the FERC has been authority that has asserted jurisdiction over the ISO approval process so I would anticipate that there is some regulatory oversight but I also know that individual states may also have different imperatives in making sure that their segment of the grid is maintained in an adequate fashion and that reliable service continues to be provided and that states, for example, have jurisdiction over the siting of new transmission or additional transmission facilities. That is

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a province that has traditionally been held within state jurisdiction.

CHAIRMAN JACKSON: I accept that if you are talking about regional grid management, there are issues having to do with congestion?

MR. GEE: Yes.

CHAIRMAN JACKSON: Vulnerability of the grid that plays in the large to planning, which may be beyond a given state interest.

MR. GEE: I agree. And I think that the questions that you raise point up the unfortunate infirmities of the existing state/federal scheme that, in fact, the Federal Power Act and the respective state statutes are not well suited to what is essentially now becoming more and more a regional market which is beyond the individual authority of a state and certainly something which is going to have to be balanced with a need for continued federal oversight.

CHAIRMAN JACKSON: What is the resolution of this dichotomy?

MS. TOMASKY: There is -- you very accurately, I think, describe a natural tension that occurs as we are moving forward on a couple of different fronts. The first really has to do with the tension between the desire for separation for business purposes between generation and transmission and when you get into the retail side

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distribution, and the desire to make sure that the people who are in charge actually are enough in charge that they can make the decisions necessary to turn the lights on and keep them on.

I think that we are going to be engaged, as ISO proposals come before us, in a very nitty gritty debate that will come to us in filings from people on all sides over very specific issues about management and control of the transmission systems and we will have to decide. Everybody who has an interest in that is going to have to participate and tell us.

We have already begun to see circumstances in which marketers, independent sellers who are interested in maximum separation will tell us that specific kinds of decisionmaking need to be separated from the sellers. We have also had utilities tell us that that is not going to work.

From a reliability perspective, I think that our Commission has tended to be, in the end, although we test the assumptions and the claims of the utilities, I think in

the end we care most about reliability and so far we haven't done anything, I don't think and I don't think we would be inclined to make a specific decision that would impair that. Although we would have a tendency to question claims, to be sure that we are not facing a situation where someone claims .

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it is reliability and it's not.

You are absolutely right about the regional planning issue and I know it is something our colleagues in the states are dealing with. Our Commission at times in the past has encouraged the formation of regional transmission groups but we have been, I think, disappointed that RTGs have not assumed a more prominent role in regional planning because we do think that there are enormous efficiencies to be gained in managing congestion and managing planning from that perspective.

But it is a legitimate issue of concern for the state, citing issues for state concerns. They involve a host of environmental and power supply issues that states have been traditionally in charge of.

I do know that folks at NARUC are talking about it a lot and they understand it is a tension. It hasn't gotten much play at this point in the congressional debate but I think it is a very, very important and difficult issue.

CHAIRMAN JACKSON: Mr. Ellsworth?

MR. ELLSWORTH: Let me just offer my perspective and it is a personal one and it is limited to NEPOOL and our New England experience.

It is my personal opinion that no one can run the transmission grid as well as the utility industry itself can. It is my opinion that the value of the ISO is not .

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necessarily to run the system but it is to make sure that the system is open to everybody and I think that is the direction that we have gone.

There has been an opportunity in New England for the regulatory community to participate in the organization and establishment of the ISO to make sure that that independence is maintained. The regulatory community has opted, although it has been invited, not to be a part of the ISO but to monitor it closely and be a close part of it, to see that it is being done openly and properly. I think that's the way it should be.

In terms of siting, New Hampshire has had a number of siting issues before it and a number of the siting projects that have been brought to the state's attention, and we have a separate siting law that looks at each one, a lot of those projects have not been for the sole purpose of benefitting the state of New Hampshire. But our law requires that we have the region in mind and each one of our decisions has had that region in mind.

Having said that, though, I can tell you that our state is not prepared to relinquish siting authority to someone else beyond our control.

CHAIRMAN JACKSON: Commissioner Rogers?

COMMISSIONER ROGERS: I have no additional questions.

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CHAIRMAN JACKSON: Commissioner Dicus?

COMMISSIONER DICUS: No.

CHAIRMAN JACKSON: Commissioner Diaz?

Commissioner McGaffigan?

COMMISSIONER MCGAFFIGAN: I do have two.

Given the importance of decommissioning costs, I read through your NARUC principles and I couldn't find any reference to it. I mean, stranded costs get mentioned toward the end.

Are you going to consider reissuing the principles at some point with some bolstered discussion of the importance of taking care of decommissioning costs?

MR. GEE: I don't know if we would necessarily amend our statement of principles. The statement of principles was adopted almost a year ago before some of our states and state legislatures began acting on decommissioning.

COMMISSIONER MCGAFFIGAN: Right.

MR. GEE: It does address, within the context of the statement, the need for states to weigh the concerns of stranded costs and to make sure that stranded costs are addressed in a fair and equitable fashion. So we would -- just using the perspective of that language, we have regarded that as broadly inclusive, to include the questions occasioned by decommissioning cost recovery.

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The separate question of how to recover decommissioning costs and whether they are sufficient, I think, is something that is going to be the subject of our dialogue and what would happen out of that is if we can reach a consensus within the national association to make a recommendation to our member commissions, that would then be reflected in a resolution that we would then take up by our executive committee and would formally become a position of the association which would have the strength of essentially being a part of the statement of principles by virtue of a second resolution.

So the short answer is the association will have an opportunity to examine more specifically all of the host of policy issues with respect to decommissioning cost recovery and then take up through the form of a resolution a position that would be given equal weight as though it were part of the original statement of principles.

COMMISSIONER MCGAFFIGAN: The other issue I just want to clarify, tax code issues came up in the discussion and is there any need in terms of in the decommissioning cost area of looking at the interaction of how these costs are recovered with the federal or state tax codes?

I am just trying to understand when plants are prematurely retired, is Connecticut Yankee or Zion or whatever have been or are going to be, was that foreseen in the tax code and are there problems that come up in the tax code that we haven't previously foreseen?

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MR. GEORGE: I don't think it was anticipated in the tax code and I think it will require attention in terms of legislation. I think the reason it was raised at our January meeting was to solicit support from NARUC in terms of making the tax change.

Our response was that we should probably talk about the entire issue of decommissioning in such that we can respond not only to the tax issue but the other issues that are associated with it.

COMMISSIONER MCGAFFIGAN: Thank you.

CHAIRMAN JACKSON: Yes.

MS. TOMASKY: I did want to mention that we did deal with this issue briefly but we somewhat directly in Order 888, the question of deductibility of nuclear decommissioning costs in particular and stranded costs was

raised before us and we were asked to clarify that if someone is recovering stranded costs that that is part of the utility's cost of service and it was suggested to us if that were the case that that would help shore up continued deductibility of those costs. Indeed, we did make that clarification.

Now, I can't testify whether or not that is sufficient for the IRS for those purposes but we did make

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that clarification at the request of some utilities.

CHAIRMAN JACKSON: Thank you. Thank you very much.

Let me call the industry panel and to thank them in advance for their patience. I think the next time, if we have another meeting on this subject, we will begin with the industry panel.

Let me make a comment that I was going to make as part of my closing remarks while the groups are changing. That is particularly I am thinking of the various regulatory entities, that I would ask you not to finesse or back away from the issues related to decommissioning costs and grid reliability and security from the point of view of the public health and safety implications or figuring it into and taking a more direct and proactive stance because we are not going to back away from it.

So I would just like you to keep that in the back of your mind.

Mr. Colvin, I thank you, and Mr. Draper, Mr. Harris and Mr. Asselstine. And however you wish to structure this. We're all ears.

MR. COLVIN: Madam Chairman, thank you and good morning.

I would like to really begin with Dr. Draper's presentation and followed by mine and work down in that

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order, if that is acceptable?

CHAIRMAN JACKSON: Sure.

MR. COLVIN: Thank you.

DR. DRAPER: Good morning, Chairman. Thank you for the opportunity to be here. Members of the Commission. This is I guess the second time I have appeared on this subject, the first being about 18 months ago at the first of these sessions and we appreciate the chance to talk about the important subjects.

In terms of regulatory actions, the starting point is the NRC's action plan and initial draft of proposals to position the NRC for the restructuring of the electric power business. The draft policy statement, the advanced notice of proposed rulemaking on decommissioning and the draft standard review plans published last year raise some of NRC's major concerns and allowed the industry to provide its perspective on these important issues.

I am here today representing a cross-section of the electric power industry. As a member of the NEI executive committee and since last June as Chairman of the Edison Electric Institute, I will address the electric industry's policy objectives as restructuring proceeds and outline the more specific goals and objectives established by the nuclear power industry. Joe Colvin will then discuss some of the more significant nuclear regulatory issues.

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I think it is fair to say that the restructuring of the electric power industry is proceeding more slowly at

the federal level and more quickly at the state level than many people expected even a year ago. At the federal level, I believe the 105th Congress and the Administration are beginning to recognize that we must approach electricity deregulation and restructuring carefully and deliberately because the economic and social costs of mistakes would be very high.

The national interest demands that we get it right. We must ensure that all consumers of electricity, large and small, will benefit from restructuring in terms of cost, service and reliability. We must ensure that the transition to competition recognizes past regulatory commitments, providing for the opportunity for the recovery of prudent, legitimate stranded commitments through the Federal Energy Regulatory Commission and the states.

For policymakers, the first step is to establish broad areas of responsibility, what decisions should be made at the federal level, what authority should be reserved to the states and what determination should be left to the market.

We believe the federal government should articulate general principles and guidance and address those issues that only the federal government can address such as .

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possible amendments to the Atomic Energy Act, repeal of the Public Utility Holding Company Act, the Public Utilities Regulatory Policy Act, which are major impediments to competition.

Recognizing that states have differing circumstances, we continue to think that the majority of the issues are best handled at the state level. We believe that some issues, corporate structure, for example, should be left to the market. Government-imposed divestiture, in particular, we believe, would be inappropriate.

Turning to the state level, based on what we have seen in states like California and Pennsylvania which have significant nuclear capacity, we are generally encouraged by the responsible manner in which state government officials, regulators, legislators and governors are approaching restructuring. We are particularly encouraged by the explicit recognition in both California and Pennsylvania that nuclear plant decommissioning is a public health and safety imperative and decommissioning funding must be assured.

We recognize that decommissioning funding assurance is one of NRC's major concerns and rightly so. We believe the NRC can and should take considerable comfort in the way the states have handled this issue so far. Let me assure you that the nuclear industry also regards

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decommissioning as a national public health and safety imperative and considers assurance of decommissioning funding is one of our highest priorities.

Let me turn now to the nuclear industry's major goal as restructuring proceeds and the objectives we have formulated to the achievement of that goal.

The goal is very simple, to maintain the excellent safety performance and ensure that nuclear plants are not placed at a competitive disadvantage as restructuring of the electric power industry proceeds. To reach these goals, the industry has established four specific objectives. These are not in any particular order; they are equally important to us.

First, we must provide the industry with maximum

possible certainty and clarity about future nuclear regulatory requirements as companies consider restructuring options such as consolidation of nuclear operations, ownership transfers and the like.

Second, we want to ensure that companies have maximum possible flexibility to reposition their nuclear generating assets without subjecting those nuclear units to unnecessary economic penalties or financial stress.

Obviously, NRC regulations and requirements, particularly in the area of financial assurances, will play a major role here.

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Third, in federal or state legislation, the industry believes that nuclear utilities should have a reasonable opportunity to recover stranded costs, including unrecovered capital and unfunded decommissioning obligations.

Finally, we believe it is appropriate to undertake a critical examination of certain provisions of the Atomic Energy Act, to determine whether the conditions that justified those provisions still prevail. If conditions have changed then we believe that the Atomic Energy Act should be clarified or amended.

Joe will cover several specific nuclear regulatory issues. NRC requirements and regulations are one of the critical factors that will influence the nuclear industry's business decisions going forward, including the degree of flexibility available to licensees as they consider how best to position their nuclear plants for a competitive environment. One of the major tasks as we move forward will be to define those issues in areas which involve nuclear safety and are thus within NRC's purview and those critical issues that fall outside NRC's statutory mandate.

Recovery of statutory commitments is a critical issue that falls outside NRC's statutory mandate. Various NRC officials have expressed concern recently about recovery of those stranded commitments. Although recovery of

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standard commitments is one of the industry's major issues and although we would welcome NRC's support for the general principle that companies should be allowed a reasonable opportunity to recover prudent, legitimate and verifiable stranded commitments, we don't believe recovery of stranded commitments is a legitimate NRC safety issue.

Recovery of stranded commitments involves whether or not a company will be able to meet its fiduciary obligations to its shareholders and bondholders. It is entirely separate from operating economics which will determine whether or not a nuclear plant or any power plant will continue to operate.

We believe the public interest is best served if the NRC focuses on results, on answering the key question, what are we trying to achieve. The answer, we would assume, is to continue to ensure the adequate protection of public health and safety.

So how do we separate the success path for this objective? The NRC might have started this process by articulating the issues on its mind regarding nuclear power plants operating in a restructured competitive market. Now the NRC must engage the industry in a substantive discussion about whether or not those issues are important and then develop practical mechanisms and techniques to address the important issues.

Let me now turn the microphone over to Joe Colvin, NEI's president and CEO, for the second half of our presentation after which we will be happy to answer your questions.

MR. COLVIN: Madam Chairman, commissioners, good morning again.

As Linn indicated, I would like to spend a few moments and talk about some of the specific aspects of the Commission's interest related to restructuring that are specific to the nuclear energy industry and that need the Commission's attention.

The U.S. nuclear energy industry is a mature industry and it is a natural evolution for it, as part of the larger electricity industry, to move toward deregulation and associated restructuring. Restructuring presents unique challenges for the industry and for the agency that regulates it, but it also presents opportunities for positive change. It is forcing us to look at the most efficient ways to meet our respective responsibilities.

Our number one goal, of course, is to maintain excellence and safety performance while ensuring that restructuring does not place nuclear power plants at a competitive disadvantage and Linn outlined the industry's four key objectives related to restructuring. I would like to elaborate on those just a bit.

As he mentioned, one of the industry's objectives is to ensure as much clarity and certainty as possible, in particular concerning future regulatory requirements for plant ownership, license transfer and related issues. Another objective which is closely related is to ensure that utilities have the flexibility to reposition their nuclear generating assets without undue regulatory burdens.

The industry needs as much certainty as possible in advance concerning what financial assurance and requirements in that area will be necessary and acceptable to the NRC to fulfill its safety responsibility.

This is essential to allow consolidation of nuclear units into new operating entities, ownership transfers and other restructuring arrangements. Regulatory requirements must allow utilities the flexibility to make the changes they deem best in order to compete. If they cannot reposition their nuclear generating assets without lengthy regulatory proceedings, nuclear energy will not be able to compete with generating sources that are not similarly burdened. In order to provide the clarity and certainty, we believe changes are needed in the license transfer process as well as how the atomic safety and licensing board proceedings are conducted.

Any requested license amendment involving a change in ownership or control of a commercial nuclear power plant

involves NRC reviews and likely, in most cases, will involve a formal hearing. Certainly, the NRC and its licensing boards must fully explore the important safety issues that might be raised.

We believe changes are needed to ensure that the existing process does not give competing factions an open-ended opportunity to manipulate the NRC's regulatory process to the disadvantage of the nuclear power plant operators and owners and to the NRC's disadvantage as well. We believe the Commission should provide direction to its licensing boards to ensure that their inquiries are limited to issues

that arise within the context of the proposed license amendment or transfer being sought. The boards should also ensure that a clear safety basis exists for issues that intervenors seek to raise in NRC proceedings.

The industry also believes it is time to reexamine certain provisions of the Atomic Energy Act to ensure its applicability to a mature industry. In particular, the requirement for NRC to conduct antitrust reviews and the current restrictions on foreign ownership of nuclear power plants that have been discussed earlier today, in our view, need to be eliminated. Antitrust and market power considerations are already examined extensively in cases involving mergers and acquisitions, transmission tariffs and other corporate restructuring by the Federal Trade

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Commission, the Department of Justice, the Securities and Exchange Commission, the Federal Energy Regulatory Commission and state regulatory commissions. The Act's current restrictions on foreign ownership of nuclear power plants represent an unnecessary impediment to responsible foreign entities that are willing and eager to invest in commercial U.S. facilities.

We believe the NRC should examine the Atomic Energy Act and initiate legislation where appropriate to amend the act. The industry will work with you to support necessary legislative changes.

Another objective involves the recovery of investment and, in particular, recovery of decommissioning and stranded costs. While Linn thoroughly discussed this, I would like to add that the industry continues to encourage the NRC to support legislative or regulatory proposals that would allow nuclear plants to recover decommissioning costs and other prudently incurred costs that may become stranded in transition to a competitive environment.

I have discussed several of the industry's objectives related to restructuring. But the fundamental issue important to restructuring is the regulatory process. In scheduling these two days of briefings, the NRC invited comments on how it can best address issues related to restructuring.

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I believe the agency would provide tremendous value to its customer, the American public, by creating a more efficient, safety-focus regulatory process. Regulatory requirements must have a clear nexus to safety, the NRC's statutory mandate and the industry's highest priority.

As I mentioned earlier, the U.S. nuclear industry is a mature industry and is a benchmark for the rest of the world's nuclear programs. Overall, U.S. nuclear power plants are performing at very high levels of safety, reliability and cost efficiency and the NRC has ample regulatory mechanisms to address any safety issue that might arise at any plant. Yet even top performing plants are struggling today with a regulatory process that has become excessive, a process that tends to regulate to the lowest common denominator and that frequently extends, in our view, beyond the agency's safety mandate.

In regulating the cost of service environment, the cost of excessive NRC requirements is recovery with the approval of the state regulators and, frankly, consumers have paid for meeting requirements that in some cases do not have a clear link to improving plant safety. In a competitive market, NRC and the utilities must reexamine the

cost/benefit relationship of regulation more closely.

Today, the rules are changing. The industry and the NRC have the responsibility and, in fact, the

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opportunity as well to reexamine how nuclear power plants are regulated. In a regulated industry, inefficient or excessive regulation can place nuclear power plants at a competitive disadvantage and the NRC's regulatory process must be clearly defined and sharply focused on safety.

When it is not, it creates confusion and misunderstanding for both the industry and the regulator about what each other's respective responsibilities are. This has a tremendous impact on how nuclear energy is viewed by the Congress, policymakers, the public, the financial community and it creates the economic uncertainties for companies that own and operate these plants.

The top performing plants in the United States today both in safety and operational performance are typically the most cost efficient as well. They are competitive today but, in light of the uncertainties in the current regulatory process, even these utilities face significant challenges and the risk of being placed at a competitive disadvantage.

As I indicated earlier, I think restructuring presents many challenges but it gives us a lot of opportunities to ensure that we continue the economic and environmental benefits of nuclear and they will continue to be realized by our nation.

Thank you.

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MR. HARRIS: Thank you, Madam Chairman. We are pleased to be here this morning to present to you some of PJM's perspective on some of the restructuring issues. We think we do have a specific and unique perspective to be able to do this.

PJM is the oldest tight power pool in the world. We are also the largest and most sophisticated entity of its kind in the world. Over the past two years, for example, we have had 48 different countries come to visit PJM and we are larger than most countries in the world trying to implement these solutions.

Over four years ago, we became a separate company that administered this power pool, separate and distinct from the member companies, so we have crossed those problems. On February 28 of this year, the FERC approved operations in PJM for the nation's first bid-based energy market. They also approved in operations for PJM the first multiple company, multiple state regional transmission tariff administered by a single entity and this is the first of its kind in the world.

We also have, within Pennsylvania and New Jersey, beginning this year, substantial pilot programs on retail choice and these programs will be in place over the next three years.

We also have effective right now a pure

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independent board running PJM. One of the FERC mandates for having an independent board was that you have expertise on that board in the operations of the power grid. We are pleased that two of our board members, one, Dr. Richard Leahy, Dean of Engineering at Rensselaer Polytechnic, who is a nuclear expert in his own right, and another one, Mr. Lynn Eury, former executive vice president and chief operating officer of Carolina Power and Light, is on our board and

brings us some special nuclear perspectives.

In operations of PJM, if you look at the total number of units, there is only one other entity that operates as many units as we do to maintain grid reliability. But part of that is our history in knowing how to deal with the complexities of separate operations with a separate control center with multiple companies in multiple states.

We have 13 nuclear facilities of over 13,000 megawatts that we have to deal with. One of the things that we have, for example, in learning in practice of how to deal with is the coordination between a central operator between the local control center and the nuclear facility. We have procedures and plans in practice that we rehearse on emergency procedure drills, procedures in plans and practice on emergency restoration that we coordinate.

One of our key committees in PJM, for example, is . 100
a nuclear coordination committee that can consist of the plant operators, plant managers from each of the nuclear power plants, the operators of the local control centers and my operations staff. They meet regularly on the nuclear coordination issues involved in this kind of an environment.

As we began to go along and look at how we are going to proceed to the future -- next slide, please -- one of the things that the states had wanted to maintain was the benefits of this kind of arrangement that has been enjoyed by this region over the years. Just energy alone last year was going to be \$100 million savings for that year alone. The states of Maryland, the states of New Jersey, have looked at PJM in separate analysis and said the annual savings of being able to operate over multiple states, multiple jurisdictions, multiple companies as essentially a dispatch entity has savings in excess of \$1.2 billion a year. As we move ahead, we want to be able to maintain this kind of savings and yet be able to ensure that competition takes place in a robust way, which is national policy.

Next slide, please.

In looking at the power grid, what I wish to draw to your attention here is the real interest, if you look at the daily load shape, which I put up here for a typical winter for PJM is, one, the size. Our minimum load of 26,000 megawatts is larger than the peak of every other

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entity in the world except for eight. We will ramp, which is the way that you move each hour, often over 4,000 megawatts an hour, which is larger than 115 other control areas in North America.

In operations of this power grid, however, we have to pay attention as to what's happening instantaneously. In looking at it from that perspective is why we would suggest to you that there are four cornerstones to look at, cornerstones you may think are kin to a SALP report on power grid operations, based on our experience.

Quite simply, we are flying an airplane that never lands and you just can't stand still, the power grid, to solve the problems of restructuring.

If you look at what takes place in restructuring, you have a central operator, as I mentioned, where a separate and distinct entity that operates an energy market and a regional transmission tariff and the control area for this grid. We are not technically an ISO at this point. All the government structures are still being debated among

the participants. But as transmission is separated from the load entities, as you get into retail choice and generation becomes fully competitive, there are certain things that have to be maintained in that functionality.

As you look at the different functionality and you look at what is transpiring 24 hours a day, seven days a

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week, it is a daunting task. For example, every three-and-a-half seconds we have dispatch signals sent back and forth between all the generation plants and our control center. Every 10 seconds, we share over 500 data points from the control areas around us and as far away as Canada to make sure the integrity and security of the power grid of the Northeast is in place.

Every 14 seconds, we have nearly 10,000 telemetered values sent in across the system that we look at to maintain the status, to make sure the system is still secure. Every 30 seconds, we have over 800 flows analyzed on a full load flow that are checked against their limits on the system to see if they are still in place.

Every 10 minutes, we have thermal contingencies analyzed for nearly 1,200 points on the system to make sure they are still in place and within their limits. Every 10 minutes we analyze the 300 worst voltage conditions on the system and we take the top 15 expected contingencies and do full load flows on those and that takes place every 30-minute interval, 24 hours a day, seven days a week.

So if you look at it from this unique perspective of a fully functioning and operating central operator over multiple states, multiple districts and a very large entity, we think that there are four cornerstones to look at as you evaluate restructuring, whether it is occurring in this

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country or the other countries that came by and worked with PJM.

The first of these is you have to look at the capability to reliably operate the grid. We can do that now but the capability is extended because you have to have capability to reliably operate the grid in a rapidly changing environment. What the environment is going to be next year when you get into full competition is going to be different two years from now so your capability to operate in the context of that is a must, as you restructure.

The second thing is information exchange. Information exchange is critical. There is an interesting article in the Electricity Journal this week talking about how information exchange may be the Achilles heel as people take self-interest and protective interest on the information. Information is our lifeline. Without all the information necessary, we can't operate the grid reliably.

Authority. You have to have authority to maintain steps to maintain security of the system and it needs to be clear and it needs to be stated. Within PJM, for example, each local control center has clearly stated authorities and what they need to do to protect the integrity of their system on a local basis, including their nuclear facilities. That is directly coordinated with the authority that my dispatchers have in order to operate and be able to shed

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load within the system.

In the new operating agreement we are operating in right now, the president, myself, has clear authorities to direct an emergency, declare an emergency and direct all actions of entities out of that emergency. It is very

important that those authorities are clearly stated and carried out when you have emergency conditions.

And, finally, if all of these things are met, the important thing is that as you go forward, you have predictable behaviors. Without having predictable behaviors that you can make sure that you are going to have in the grid, then you will have problems and you will have faults. All of these are building blocks to ensure that that will take place.

If we look at the first one, capability to reliably operate the grid, I can't under stress the importance of this in training. In PJM, we have five percent of our budget in training. We train all the system operators throughout the grid.

In starting up the bid-based energy market and the regional transmission tariff that FERC approved for us on February 28, from that time to date we have trained over 1,000 people. Over 400 operators have been trained and over 600 market participants. We have conducted training classes throughout the mid-Atlantic region, we have conducted

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training classes in Houston, Texas, for the marketers down there on how to participate in this market.

I can't underscore the value of having comprehensive training programs. NERC is very concerned about this also and, as you probably heard yesterday, they were talking about certification of training programs, certification of operators and so forth. We support all of these and think they are a must.

It is so important that you have all of the communications telemetering and so forth in place. For PJM, this stuff is already in place.

In other areas, as they develop into the various functionalities, like in California, they have many elegant consultants and firms that are ensuring that whatever processes and procedures come in place, the hardware and the software and so forth will work. Again, you are flying an airplane that can't land. You can't stand it down so the systems have to be in place and have to work as they change and as they go forth.

The emergency procedure drills are extremely important, particularly as new players come in and come out. PJM conducted an exhaustive emergency procedure drill before we began our bid-based market and regional tariff that involved not only the states but Department of Energy and also involved the market participants to make sure that

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should something have happened after we began our new energy market that everyone was qualified and understood what would take place during the emergency procedures.

Twice a year, we also conduct system restoration after a blackout. We simulate a blackout of the entire East Coast and go through restoration procedures that are heavily involved. It takes about two days to go through the drills but we found them exceedingly productive.

Madam Chairman, we would certainly welcome any of this Commission or the staff to come by and observe our drills and procedures as we go forward.

Information, as mentioned, you know, may be the Achilles heel. As market participants begin to do their thing and as generation becomes unbundled, it has to be crystal clear and understood in whatever form that the information to the grid operator has all the information

they need in order to operate the grid reliably. There is many elements of these but I just want to highlight three that would have to be put into the proper context of whatever restructuring takes place in whatever portion of the country or the world.

One is there is certain before-the-fact information. In order to get the grid in a position to operate reliably, you have to have data and information on what is transpiring, what is taking place and so forth so

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you can plan for the next day and up to the next week's events. As we learned in January of '94, fuel levels, for example, are very important, as we begun to run out of fuel in January of '94 and the emergencies we had there.

Sometimes we wonder, when we get into a full generation market, that could be extremely market sensitive to know what the fuel levels are. Well, those are elements we feel have to have contractual rights to make sure we have all that information before the fact so we can make sure the grid is positioned reliably.

You have transactions, as I elucidated earlier, real time transactions of things you have to do as you operate the grid hour by hour, day by day. And then you have after-the-fact. You have to have all the information necessary to analyze reliably and productively a fault should it occur to determine what are the lessons learned. And, as your industry knows very well, root cause analysis is the key to be able to go forward and learn from mistakes that will be made and to do this you must have exhaustive amounts of data.

We have found in PJM our historical database right now is in the terabytes and growing on the amount that we have to capture and keep in stored level and I think the ability for a central entity to be able to capture that, store it, have it available for others to look at and so

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forth is critical to the success.

This next slide on ISO functions, a little bit busy and I won't go into that. But, again, we would certainly welcome you to come and tour the center and we will spend more time on this. But I just wanted to point out, this is the operations that take place on the floor. And you will see up at the top two separate networks. We are in place, operating today with a bifurcated information system where we have information that goes on what is termed the OASIS for all the market participants. And, since we operate both, the pool in and of itself does not participate in the market; we strictly administer the market and make sure it is operated according to the rules.

We have a separate information network that concerns all of the security data. And I think as this thing gets into place and works throughout North America that we will be able to solve those information requirements so we can operate the grid reliably. Confidentiality agreements have been stressed and other sorts of things are being put in place to ensure that this kind of communications can continue.

The third element has to do with clear authority. I had mentioned authorities that we currently have in PJM but authorities must be tied to the developing role of sanctions. One of my worst nightmares is that even though

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you might have sanctions with penalties on the sanctions, a party could take a commercial position that the penalty or

the sanction is just a cost of doing business and when you are dealing with a real time system where you have to make -- where you have a product that is instantaneously generated and consumed, you can't have someone making a commercial interest when you need that plant on or off or whatever condition it may be.

So second guessing and self help is something that could obviate the authority. So as these sanctions are developed and put in place throughout North America and are looked at for what the requirements are for various entities to comply with those, could be the one that will make sure the authority is clear and crisp or the one that could undermine it.

Finally, we deal, have to deal with predictable behaviors. We think that as the restructuring is taking place through various places throughout this country and the world, everyone is very concerned with reliability. I have not come across one individual from the most avid marketer to the most conservative that is not saying that reliability must stay in place. Everyone recognizes the severe impacts of an outage and, certainly, in this region for PJM that serves arguably the world's political capital and in our hip pocket has a city that on any given day can have 12 million .

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people in 10 square miles, you know that we have to have reliability for this area. It is extremely important and everyone is very sensitive to that.

But these four cornerstones, we feel, are what needs to be developed and, as you look at the various restructuring options, you need to ensure that the capability is there and there are ways to measure the capability through training, experience and so forth, to make sure that takes place, certification.

Information is necessary and that comes through the contracts that you have. The authority is there, which is clear and crisp through the sanctions, the mandatory rules and guides and so forth that have to be in place.

And, finally, with all of these together, we feel that it can be a vibrant and a healthy new industry as it moves forward and will meet the terms and conditions of reliability that we all expect.

Thank you, Madam Chairman.

CHAIRMAN JACKSON: Thank you very much.

Rather than addressing specific questions at this point, I am going to let Mr. Asselstine make his presentation and then we can have a discussion.

MR. ASSELSTINE: Thanks, Chairman Jackson.

What I would like to do this morning and in the next few minutes is just touch on a few topics that I

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addressed before the NARUC meeting when I was on a panel with Commissioner Rogers and I thought I would touch briefly on some of the changes that we have seen as the competitive framework is developing both at the federal level and at the state level, talk about stranded cost recovery and securitization which we view as a useful concept or tool that can assist the utilities in recovering their stranded costs, offer a few comments on disaggregation and then close with just a few points on the effects of competition on the operation of nuclear plants in the country.

If I could have my first slide, please?

At the federal level, there are a number of legislative initiatives that are either being considered or

potentially could be considered over the course of this year and next year. Certainly the industry has strongly advocated repeal or modification of the Public Utility Holding Company Act and also some of PURPA requirements that utilities purchase power from independent power producers.

As you have heard already today, nuclear decommissioning cost recovery is certainly a potential candidate for legislation at the federal level and, finally, there are a series of broader industry restructuring proposals that have been introduced both in the Senate and in the House that cover a fairly broad range, including legislative proposals that would provide more of a one-

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size-fits-all federal solution for retail competition and stranded cost recovery to other proposals that would be more of a safety net to help ensure the states all reach the same ultimate objective in terms of retail competition.

If I could have my next slide, please?

As you have heard, there has been a very substantial amount of activity at the state level. We expect that trend to continue over the course of this year and on into next year. By around the end of this year we expect that many, if not most of the higher cost states in the country, will have instituted industry restructuring plans and proposals and we are also seeing, although we are at a relatively earlier stage in the process, a growing convergence among many of those state plans to include the points that I have outlined here.

First, a reasonable transition period of on the order of five years to get to full retail competition. Second, the opportunity, although clearly not a guarantee, for stranded cost recovery. Third, the phase-in of retail competition over the transition period. Fourth, in many instances the institution of a wholesale competitive market to try to capture some of the incremental efficiencies and cost savings from competition as we are working through the transition period. The use of independent system operators and I think you have heard a fair amount of that yesterday

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and today. And, finally, in a number of states, the use of securitized financing as a tool to accelerate competition transition charge recovery.

If I could have my next slide, please?

We have listed here a number of states where we expect to see activity. We have seen two states thus far that have enacted comprehensive statutory frameworks for industry restructuring. Those are California and Pennsylvania. A number of other states are actively engaged in the process and, with few possible exceptions, our expectation is at this point that those frameworks will be balanced and reasonable.

If I could have my next slide, please?

I have summarized a few of the key points from the California statute. We do view the California legislation as a fairly significant milestone in the transition to a more competitive environment in the utility industry in the country and we expect that it will continue to serve as a model for state consideration in a number of other states. I am not going to go through all of the elements in the California statute.

A few that I would point to, first, the phase-in of direct access or retail competition subject to the implementation of a nonbypassable competition transition charge that would be paid by distribution customers.

If I could have the next slide, please?

Second, and a trend that we are seeing among a number of other states, emphasis on some near-term rate reductions to provide some tangible benefits in many instances, particularly for small customers, at the outset of the process so that customers will see some near-term benefits from the competitive marketplace and, finally, the use of securitized financing as a mechanism to accelerate at least a portion of the recovery of stranded costs by the California utilities.

If I could have the next slide, please?

On stranded cost recovery, there are just a few points that I would make. First, in terms of the magnitude of the problem and the role that nuclear power plays in the problem, there are basically three sources of stranded costs. Those are, first, investment in above-market generation, and that is really a sunk cost recovery question. Second, above-market power purchase obligations, which is really an ongoing operating expense for the utilities. And, third, deferrals, regulatory assets and funding of social programs such as demand-side management.

There are a variety of estimates of the magnitude of the problem. Moody's Investor Service has put out a recent update of their -- in 1996 of their estimate and they continue to believe that the total amount of stranded costs

for the industry are about \$136 billion.

A few other factors pointed out by Moody's, and I think you have heard a bit of this already. Stranded costs tend to be concentrated by region. The Northeast, the West and portions of the Midwest are the regions that have the largest concentration of stranded costs. Also the greatest exposure in general is with the lower rated companies and that is also not surprising since those were the companies that had large plant construction programs under way in the 1980s.

A few key points in terms of stranded costs. First, not all stranded costs are for utility-owned generation. There are very substantial exposures to stranded costs for power purchase obligations and we see this probably most clearly in California and in New York.

Second, not all generation related stranded costs are nuclear. There are some expensive coal units around that were built in the '80s and those are a portion of the stranded cost problem as well.

But, third, I think it is fair to say that nuclear units and, particularly, many of the large current generation units that were licensed in the 1980s do represent a substantial component of the problem.

When we look at stranded cost recovery, and actually if you could go back one slide, I think, great --

when we look at stranded cost recovery, we see it really as a function of three components. The first of those is where are the utility's rates today and where will those rates be during the course of the transition period as you move to full retail competition?

Second, if you use securitization as a tool for stranded cost recovery, what benefits can you derive from securitization?

And, finally, what a lot of regulators are referring to these days as mitigation savings. What other

cost reduction savings can you wring out of the business?

Those are really the three components.

If I could move to the next slide, please?

This chart really just shows the revenue path for California for the California statute. I think the significance here is simply to point out that there are some immediate cost savings that can be achieved in California and we expect will be achieved through the use of securitized financing. Those cost savings will cover most but probably not all of the 10 percent rate reduction that was mandated for small customers in California to begin on January 1, 1998.

Over the course of the five-year transition period, the continued benefits from securitization as well as some of the other cost savings that the California

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companies will achieve really provide the mechanism for recovering a substantial portion of their stranded costs and most stranded costs really are expected to be recovered by the end of the transition period. With few exceptions, unrecovered stranded costs at that point would become the obligation or liability of the shareholders.

There is one significant benefit in California that is a big plus for the California utilities. That is, the structure of their independent power contracts. Those contracts move to a substantially lower cost over the next couple of years. By keeping rates at current levels or 10 percent lower for small customers, the utilities will be able to keep those savings and apply them to stranded cost recovery. Unfortunately, that is not a financial benefit that exists in any other part of the country.

If I could have the next slide, please?

In terms of securitization itself, let me start with just a brief description of what it is. It is really the use of an asset-backed financing which is a nonrecourse financing to the utility. Therefore, not a direct obligation of the utility. This financing would have very high credit quality, AAA credit ratings and that credit quality would be derived from a statutory authorization to impose an irrevocable and nonbypassable charge on the utility's distribution customers which would then be used to

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repay the debt. These bonds would not be obligations of the state or obligations of the utility but would really be backed by that statutory ability to collect revenues.

The utility would transfer their stranded costs for securitization to a trust which would issue the bonds and the utility would receive the cash proceeds from the sale of the bonds. Those cash proceeds would then be used by the utility to reduce their costs, typically by retiring their existing debt and also by repurchasing some of their existing common equity.

When we look at securitization, we really see six benefits from it for the utilities and for their ratepayers. The first of those is you can accelerate stranded cost recovery and, effectively for the portion that is securitized, you immediately recover those stranded costs.

The second and related benefit is that the utility no longer bears any risk or uncertainty in terms of stranded cost recovery for the portion that is securitized.

Third, the securitization permits the financing of at least some stranded costs over a longer time period than otherwise might be permitted. In California, for example, securitized financings are likely to be over 10 years. The

normal period for stranded cost recovery is five. So it gives the utilities the ability to extend out stranded cost recovery over a longer period of time for at least a portion . 119

of those costs.

Fourth, there are economic savings that can be provided and translated into rate reductions. Those rate reductions really help, I think, allow the states arrive at a reasonable transition period for competition. Those savings are really as a result of shrinking the utility's capital structure. In effect, what the utility is doing is taking assets that are currently on their books, financed roughly half with equity and half with debt, refinancing those very efficiently with 100 percent debt financing using the guarantee of recovery of the revenues.

Finally, there should be benefits to the utility through recovering their stranded costs in terms of enhancing their credit quality by removing the uncertainty for stranded cost recovery.

If I could have the next slide, please?

Just a moment on disaggregation and I think, at that point, I probably will stop given the lateness of the hour.

There are a variety of stages in terms of changes that will take place in the organizational structure within the industry. Most utilities have already established strategic business units and the states are moving rapidly to unbundle rates and separate rates out for the different categories of the business.

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As we move forward with competition, it is likely that utilities will either separate their businesses into separate subsidiaries within a holding company structure or, ultimately, potentially sell or spin off some of their assets.

If I could have the next slide, please?

In terms of spinoff of the assets, we tend to think that most utilities would continue to prefer either functional unbundling or structured unbundling within a holding company system. Nevertheless, market power concerns are likely to drive utilities more toward disaggregation and, ultimately, utilities may agree to sell or spin off assets in order to achieve unregulated status for their generation. We see a number of examples of this at this point both in California, in New England and also in New York with Niagara Mohawk.

I think with that, I am going to stop at this stage and turn it back over to you, Chairman Jackson.

CHAIRMAN JACKSON: Thank you very much.

In fact, I will begin with a comment and then a question to you, Mr. Asselstine.

As you are aware, the NRC does not see its role as directing how the amount or components of stranded costs are to be defined or recovered. In fact, we will stop talking about it and spend our time talking about decommissioning . 121

funding since that is our issue.

But it is essential that we fully understand what decisions are being made in establishing those definitions and how they impact the availability of resources both for operation but especially for decommissioning of nuclear power plants. And the concept of securitization as you have outlined it rests on an economic regulatory structure that

ensures a stream of revenue from ratepayers.

Can you -- you focused a lot on California but can you extract from what you said two or three key issues you think have to be clearly addressed, either in state legislatures, by state legislatures or orders from PUCs or others so that the revenue streams are, in fact, assured that would back this approach?

MR. ASSELSTINE: Sure.

There are a few key ingredients that are really necessary and I think our belief and this is true I think for most of the firms that are involved in the asset-backed financing business, is that you really do need, in order to obtain the highest credit quality rating for these bonds, AAA ratings, you really are going to need the statutory underpinning to support these transactions.

The key legislative components that we are looking for is the statutory creation of the ability to recover stranded costs. Second, the authorization to impose a

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nonbypassable and irrevocable charge so that once the bonds are issued, you really know that the revenues will be there until the debt is fully repaid. Third, what is called a true-up mechanism and that is a tool to ensure that as you move through the term of the debt, you have the ongoing ability to adjust the size of the charge to make sure that you continue to collect enough money so that all of the debt is repaid. And a final provision is really a state covenant that the state will agree both at the legislative level and at the regulatory level not to do anything to disrupt or impair the revenue stream that would be used to recover the cost of this financing.

Those are really the core elements. At the legislative level, there are also a corollary set of requirements that we would look for in terms of the individual state commission orders that implement the legislation which basically track the same components.

If you have those elements, institutional investors who invest in the asset-backed market would look at this as a very stable and dependable asset class and they would be willing to invest in these securities in the amounts that are likely to be available. And as we look out over the next say three or four years, we see a potential size for this market of on the order of \$50- to \$100 billion.

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CHAIRMAN JACKSON: You talked about the establishment of a trust. Can you elaborate a little bit more on the role that a trust plays in this financing approach and, in your opinion, having been an NRC commissioner, is this a critical factor in ensuring that funds, particularly for decommissioning, would be available when they are needed?

MR. ASSELSTINE: In terms of the asset-backed financing, the trust is really a special entity, it is a special purpose vehicle which only exists to receive the transition cost asset and to issue the debt and then collect the money and repay the debt. The objective here is to ensure that it is bankruptcy remote, that nothing can be done to impair the availability or access of those funds.

On decommissioning costs, I think the point that I would make, I am actually quite encouraged. We are at an early stage in developing the competitive frameworks through many of the states but I am encouraged so far that state regulators and legislators have really recognized that

decommissioning is a safety issue, it is an obligation and a requirement that has to be met and there has been a pretty clear willingness to impose the same kind of nonbypassable and irrevocable charge to be paid by distribution customers to meet ongoing decommissioning funding obligations over the remaining operating life of the plant.

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We have seen that in the statute in California, we have seen the statutory authorization to the Pennsylvania commission to deal with it and, although the Pennsylvania commission hasn't acted at this point, I would expect that they would follow the same path as in California and recognize that this cost should be recovered along the same lines as any other stranded cost. Perhaps this is a separate item.

As long as the states continue to do that, that ought to provide a fair amount of comfort to all of us, both investors and to the Commission, that the decommissioning funding requirements will continue to be met even if the structure of the industry changes.

CHAIRMAN JACKSON: Can you just speak for a moment in terms of what the financial impact you think would be, the relative financial impact of the spinoff or sale of assets as compared to a holding company?

MR. ASSELSTINE: That is a very interesting question and I think all of us, both the utilities, those of us who follow utilities from the financial side, the rating agencies, are beginning to struggle with how do you evaluate the individual pieces of the business as the utilities restructure themselves. The next four or five years are going to be a fairly interesting time in this industry and I think, literally, you are going to see the shape of many

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utilities change fairly significantly.

We have started to look at the individual components. If you take the average vertically integrated U.S. electric utility which has a single A credit quality today, what you tend to see is a capital structure that is roughly 50 percent equity, 50 percent debt, which reflects a blended business risk position for that consolidated entity. We tend to believe and our informal conversations with the rating agencies tend to confirm that if you looked at the distribution part of the business, the risk profile of that business is probably lower than the vertically integrated utility. It will continue to be a regulated monopoly. In all likelihood we are going to see performance-based ratemaking for that part of the business. So utilities will have an incentive to lower their costs, they will be allowed to keep at least a portion of any economic savings that they are able to achieve.

Given the lower business risk profile of the distribution business, it ought to be possible to maintain single A credit quality by increasing leverage, for example, to say a debt-to-total-capitalization ratio of on the order of 60 percent rather than 50 percent. You can also probably operate that business with lower cash flow coverages or earnings coverages for your interest requirements than you would normally see for a vertically integrated utility.

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I think generation is the flip side of the coin. The generation business is likely to be a competitive market-priced business. If stranded cost recovery goes as we expect it to, at the end of the transition period we

should have most of the generation assets marked either at market or very close to the market price that those assets need to have to be able to compete effectively in the marketplace. But it will be a competitive market, your revenues will depend upon your ability to sell power at competitive prices and therefore that business probably has a higher risk profile.

Our rough cut there is that you probably won't be able to leverage that business as much as the vertically integrated utility. Perhaps the right capitalization is a 40 percent debt to total cap of larger equity component for that business and you may need higher cash coverages of interest along the lines of other commodity-based kinds of industries in the country.

If you begin to parse out nonnuclear and nuclear generation, I think that the equation shifts even more dramatically as you look to the nuclear units. Again, if we get through stranded cost recovery, what you really are focusing on in the nuclear units is an avoided cost issue, how competitively can those plants operate, and I agree with the comments that Linn and Joe made.

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Well run, larger nuclear units in this country should be able to compete very effectively. If you look at the top quartile performers in the industry, those plants can generate power taking into account fuel and O&M costs of well below 2 cents per kilowatt hour. That is a very competitive price, in my view, given where the market is likely to be in virtually any part of the country.

If you go down the performance scale and look at plants in the lower quartile of the industry, I think there may be a different story there and my suspicion is those plants are really going to have to move up more toward the mid range or the higher portion of the industry if they are going to be able to compete effectively on a long-term basis.

You also have problems with smaller, single-unit sites like a Connecticut Yankee where I think even if it is basically a sound plant, the economics may weigh against the plant on a variable cost basis.

CHAIRMAN JACKSON: Well, one thing that seems to come out of what you are saying, though, is the question of who or what kind of entity securitizes the stranded costs in the sense that since you are basically talking debt financing here, this whole issue of cash, higher or lower cash covenants is part of -- coverages, rather, as part of some kind of covenants could be harder to securitize that

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debt could be impacted, you are basically saying, by the structure of the company?

MR. ASSELSTINE: Well, I think as long as you have the statutory provisions you can deal with the stranded cost problem regardless of the organizational structure of the company. Where the organizational structure will really come into play, I think, is on an ongoing basis what financial capabilities will the company really need to compete effectively and how do you factor that in also on the generation side in terms of where they are going to have to be able to produce power to be competitive with other sources.

CHAIRMAN JACKSON: Okay, thank you.

I just have a quick question for Mr. Harris. In your discussion of restoration procedures, you have specific protocols with respect to nuclear plants.

MR. HARRIS: Yes, ma'am, we do.

CHAIRMAN JACKSON: Could you just give a few words to say something about that?

MR. HARRIS: Well, we have the protocols embodied in our operating procedures in accordance with the NERC protocols and guidelines. They have a high priority for restoration.

CHAIRMAN JACKSON: Okay.

MR. HARRIS: In our emergency restoration where we

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black out the grid, one of the things we look at is how quickly can the units come back on. One of the things that we are looking at and having discussions, for example, is if you assume a total blackout how quickly, in an emergency condition, can you get the plants back on line.

That hasn't been totally solved but, for PJM, for example, in our drills, assuming they can come back readily will make the difference in having the grid back on line within 24 hours as opposed to five days. So this is something that is continually looked at as we do these drills and rehearsals. It is very important to us.

CHAIRMAN JACKSON: You talked about before the fact, real time and after the fact communication and you spoke about intra and interregional communication from an after-the-fact point of view. Are there key elements from a before-the-fact point of view in terms of interregional communication as far as the interface with other regional grids and issues of degradation of voltage on the grids? Are there some operating or governing protocols in that area?

MR. HARRIS: Yes, ma'am. In the NEPOOL, PJM, New York Power Pool, Ontario Hydro, Hydro Quebec area, we have protocols for us, Allegheny Power System and Virginia Power. For years we have shared data. We have over 500 data points that we share every 30 seconds that we share amongst

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ourselves automatically that is folded into the analysis that we do on the power grid. It is a very robust and probably the most robust sharing of data in and amongst the region in the whole of North America.

CHAIRMAN JACKSON: Do you see any of that as being unnecessarily threatened by any of the competitive pressures?

MR. HARRIS: No, ma'am, I do not. I see it being enhanced, actually, with the advent of security centers which I think you were briefed on yesterday.

CHAIRMAN JACKSON: Okay. Commissioner Rogers?

COMMISSIONER ROGERS: Well, we have heard so much today that I think we are pretty well saturated.

I just want to make a remark for Mr. Colvin and that is I think some of his observations are very interesting but I think they need to be more explicit and today at this time is not the time to do that. But I think when you are talking about the need for more efficient safety-related regulation, then I think it is important for you as a representative of the industry to be more explicit, exactly what you are talking about, because I firmly believe that no changes of any sort are going to come about unless there is a very clear identification of exactly what you are talking about and why. But I wouldn't expect an answer to that right now.

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CHAIRMAN JACKSON: Right.

MR. COLVIN: All right, I understand.

[Laughter.]

CHAIRMAN JACKSON: Right.

Commissioner Dicus.

COMMISSIONER DICUS: But some day.

A question, two real quick ones, I think, to Mr. Harris. I think I heard you say this, I'm not sure, but you believe in mandatory membership in NERC?

MR. HARRIS: We think that that is a wise goal. We do not know whether it is achievable when you have full generation competition, people can choose their directions. What we do believe in, however, is the contractual conditions to do business in our pool contractually obligates you to obey the rules of NERC and MAAC, the regional council we are in, and the directions of the control center.

By having a contractual relationship that captures that, we think we can cover that gap. It would be laudable if we get to that point but I don't know if in the full generation context you can without some sort of legislative mandate.

COMMISSIONER DICUS: That was my follow-up question. If it isn't done by contract, then do you think it has to be done by legislation?

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MR. HARRIS: Yes, ma'am.

CHAIRMAN JACKSON: Commissioner Diaz.

COMMISSIONER DIAZ: I have three small questions and maybe some comments.

I listened to Mr. Colvin and it follows up on the comments by Commissioner Rogers that I wrote in here, the industry is requiring a defined, stable, safety-focused regulatory infrastructure and you need that for an undefined, deregulated electric marketplace. It seems to be a very tough issue.

And then, you know, reasserting what Chairman Jackson, Commissioner Dicus said, I think this coming years, maybe starting now, the value of frequent in-depth communications and advanced probing of this area will be very necessary because we realize that the industry needs some framework but the situation is continuously changing. I think that will require maybe an added incentive for us to be very aware of what your concerns are and those need to be very well stated.

If you want to comment to that, fine.

MR. COLVIN: Commissioner Diaz, if I might provide one example, to leave the Commission with a concept of what we are discussing, and I might use the discussion that we have had on grid stability and grid reliability over the past seems probably like days to the participants.

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But if we tie that to the issue of station blackout, I think that this is an issue which the Commission is rightly looking at and needs to look at and assure itself that the safety from the grid reliability standpoint is, in fact, assured.

At the same time, however, if you look at the process by which we implemented the safety requirements, the implementation of the station blackout rule, there is a basis, a safety basis which is based upon risk and if you just take a simple look at that and its assumptions, as decided by the rule, you can quickly come to the conclusion that we would have to have more than 50 grid disturbance events in a year to be even starting to penetrate the basis

under which that regulation was implemented by the Commission. And you will recall that grid disturbance is only one small portion of the real concern about initiating events, the loss of off-site power. The main disturbance and concern is from a loss of off-site power initiation event is a plant-centered event. So that is the largest portion.

So we are really looking -- I think there are many indicators that we have here to look at where we have in the past envelope from a safety basis the real risk to public health and safety. The Commission dealt with that appropriately, the industry dealt with that appropriately,

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the Commission monitored that activity and, unless there is a significant change that goes outside, puts us outside the envelope under which that safety case was made, then there is no reason to go through and review that safety case and reevaluate and reanalyze that.

So I just encourage the Commission from a process standpoint, I think you have in that situation we have the ability to determine today that we are in full compliance with the Commission's safety risk and would do so for some time to come unless grid reliability got to a very significant point of where it was unreliable. I think you have heard the discussions from Mr. Harris and others today to that we are putting in a lot of steps to ensure that doesn't occur.

So I was somewhat disappointed in yesterday's discussion of that, that that question was not addressed fairly quickly and fairly easily because, in fact, it is a fairly simple matter to look at the bounding conditions as an industry on what the safety case is.

So it is from the process standpoint and if that process now entails each licensee to go reevaluate and reanalyze, I think that is an area where the licensee's resources as well as the Commission's is not well focused because the safety is -- it is easy to determine that that is assured. So it is in that context that my comments

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should be taken.

COMMISSIONER DIAZ: Thank you.

The second point was on the Atomic Energy Act. I think we realize that foreign ownership is really becoming an issue and I think that the fuel cycle market is going to become an issue on that and that is another aspect that we are going to really need to look at because it is not only uranium now; it is uranium and plutonium and it is enrichment abroad and it becomes an issue that I think the industry needs to bring if they are going to be going into that area so we can get an early look at it.

To accelerate, you talk about grid reliability and I had a comment and maybe a question for Mr. Asselstine. When we wrote, you know, the Atomic Energy Act and the Commission got charged with maintaining national security, it actually meant something. It meant that we were going to control special nuclear materials, that we were going to make sure that technologies that were critical to the proliferation issues were controlled and all those kinds of things that were clearly identified.

Now, you know, we are shifting into an area which practically national security is established also in terms of grid reliability and the economics of the country. In that sense, you know, the issue of base plants and nuclear

power plants become like a stationary component that has

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additional importance in determining what national security is as far as economics and grid reliability.

Have you dealt with this issue in any way that identifies what a clear contribution of nuclear power plants is in this area?

MR. ASSELSTINE: I think to some extent. I think my reaction would be certainly if you look at the number of units that we have and the role that those units play as base load generating units, they are a pretty essential component of the system, now and in all likelihood going to have to continue to be for the most part under a competitive system.

That is partly why I am encouraged by the information, at least, that we have available to us that if you have well run plants, those plants should be competitive on a long-term basis under virtually any scenario and, at this stage at least, our own assessment is that relatively few plants should really be vulnerable to early shutdown if they are able to achieve the kind of performance levels that are being achieved by the stronger performers within the industry and you shouldn't see large-scale or at least the risk of large-scale shutdowns of the units simply due to competition.

Again, if you break the pieces down, if decommissioning costs are dealt with as a separate matter,

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if you deal with stranded cost recovery so that you get the capital investment in the plant down to a reasonable level relatively quickly, then you are left with a variable cost analysis. If you run the plants well, they should be competitive on a variable cost basis going forward. If they aren't, then those plants are likely to be as vulnerable or more vulnerable in a truly competitive marketplace.

I spoke at another meeting a week or so ago looking at the economic effects on nuclear issues and one of the points that I made was if you begin to separate nuclear out as part of your generation, you need to focus not only on decommissioning costs but also on what happens if you have an extended shutdown of the unit.

Somebody in the audience said, basically, you really don't have to worry about that because in a truly competitive marketplace if you have a nuclear generating company and the unit is down for two years, you know what the answer is going to be. That unit won't resume operation.

So, if anything, the competitive pressures, I think, are going to put more emphasis on the challenge of running plants well and efficiently and the strong performers are going to be the ultimate survivors.

COMMISSIONER DIAZ: Thank you.

CHAIRMAN JACKSON: Commissioner McGaffigan?

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COMMISSIONER MCGAFFIGAN: I hate to do this but just three quick questions and I think the answers can be answered quickly.

You talked, Mr. Draper, about the need for flexibility in repositioning nuclear assets. You heard the staff earlier say that they are going to basically look at those issues on a case-by-case basis. And if you are looking for flexibility, maybe we have to be case by case.

How do we square what you are saying and what the staff said earlier?

DR. DRAPER: I am not sure they are inconsistent. It seems to me that we don't want undue delays, we don't want artificial constraints on the way the organizations can be configured as we go forward because one thing we do know is as we go forward people will wish to array their assets in quite different ways from the way they are now.

So it seems to me that case by case is fine as long as it is done expeditiously and there are no artificial constraints.

COMMISSIONER MCGAFFIGAN: And that gets to Mr. Colvin's point about the expeditious nature of the licensing board processes. But how do we give the licensing board, if we don't have reg guides, you know, some template that says, this is okay? How do we give them some way to judge when something comes in?

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MR. COLVIN: Well, I think we need, and let me follow up on your question if I might. I think we need to look at some templates or some models and we have done that in part with the staff to date to look at some of those. We have identified a lot of other questions that came up. I mean, the whole issue of ISO and its nexus to safety and grid reliability came out of one of those earlier discussions so I thought that was very healthy, so we are going to work with the staff.

I think from, just following up on Linn's comment, if you think about the various arrays and the combinations and permutations that you can have, it seems to me the way we've got to start that is not trying to identify all of those but to try to identify some bounding conditions. What are the major factors that are important to the NRC from its safety perspective that relate to the financial ability of the utility to operate within the financial constraints that ensure its safety? If we could identify those in a fairly direct way, I think they are somewhat, and at least in the industry's view, somewhat mushy is probably the best way to talk about it.

I mean, they are up there in the eye of the beholder and I think we ought to figure out a way to work together to have the dialogue in this type of forum or whatever forum is appropriate to more crisply define those

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and do those from the safety perspective.

COMMISSIONER MCGAFFIGAN: A second question that we have avoided today and I will just ask you. Decommissioning costs we treat as if we know what they are and we have now gone through some decommissionings and as I understand it we have been surprised on the up side as to what the actual costs are. I think at the moment, people just lay aside whatever money we have said might be needed without even a final rule on decommissioning, which we are simultaneously working on.

If this is the last chance to get decommissioning costs treated as stranded costs, is anybody looking at whether the numbers are right at the moment? Any of you can answer that.

MR. COLVIN: Let me take a crack at that. We have worked hard on that issue with the Commission to try to define that. Mainly, the uncertainties in the decommissioning costs come primarily from uncertainties in low-level waste disposal cost. And given our failure from a national policy perspective to cite low-level waste compacts, then it is all a very interrelated problem.

I will say that there are some good methods that are out there and to come up with the best estimates that are available today and then bound those from an uncertainty about the cost of low-level waste disposal. So I think we

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can get there, here from there. I think that there are discussions in those areas about periodically truing up, I think was the word that Mr. Asselstine used to true up those features. Through that process, we will have to make the appropriate adjustments.

It is a true health and safety issue. It is an issue which I think all parties agree needs to be dealt with through nonbypassable or overall charges, wire charges. We just need to figure out the mechanism to deal with that. So I am confident that we can do that.

COMMISSIONER MCGAFFIGAN: My last question is more a comment. I took during Commissioner Rogers' noting Mr. Colvin's statements about need to align our regulatory framework to safety and the future, and I think it goes to sort of a fundamental issue, if these folks are going to be in a competitive environment, they are going to have to be agile. That is what all the Microsofts and the successful American corporations have to be agile.

In the past, we had a ponderous industry dealing with a ponderous regulator and I think there is sort of a challenge to us to figure out how to be a more agile regulator while they are trying to be more agile companies while also preserving safety. So there is a real fundamental issue there but we don't have time today to talk about it, I don't think.

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I'll leave it at that.

CHAIRMAN JACKSON: Well, picking up on that, I would like to thank the NRC staff and members of the two panels representing regulators and the various industry sectors for taking the time to come today to brief the Commission on the developments in the electric utility restructuring.

The Commission will continue to gather information about developments in this area and interact with the various sectors to be able to adequately address safety concerns that might arise as a result of any of the issues. I concur with Commissioner McGaffigan's comments and my only parenthetical remark is that presumably we are on that path. It may not be fast enough for everybody and it may not cover everybody's issues all the time. So if we are not on that path, it is our fault.

So I would like to think that the actions that are already under way, some completed, as well as the meetings like the ones we have had today and the one on grid reliability contribute to both a comprehensive and a cohesive understanding of the evolving environment which should allow us to respond effectively and in a timely manner to carrying out our public health and safety mission.

So we do welcome your input and thank you again and so that we all can continue to enjoy the benefit of a

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safely operated, soundly and fairly regulated nuclear generated electricity along with the economic benefits of deregulation. I think we have gotten some good input that our staff should fold into any proposed rulemakings or any other initiatives that are under way.

So unless my fellow commissioners have any closing comments, we are adjourned.

[Whereupon, at 12:18 p.m., the briefing was concluded.]