

**PREPARED DIRECT TESTIMONY OF DR. PAUL GRIBIK
ON BEHALF OF THE MIDWEST INDEPENDENT TRANSMISSION
SYSTEM OPERATOR, INC.
DOCKET NO. ER04-____-000 BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

Midwest Independent Transmission)
System Operator, Inc.)

Docket No. ER04-____-000

PREPARED DIRECT TESTIMONY OF
DR. PAUL GRIBIK

I. INTRODUCTION

1 Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

2 A. My name is Paul Gribik. I work at 701 City Center Drive, Carmel, Indiana 46032.

3 Q. BY WHOM AND IN WHAT CAPACITY ARE YOU CURRENTLY EMPLOYED?

4 A. I am employed as Director, FTR Markets for the Midwest Independent Transmission
5 System Operator, Inc. (the "Midwest ISO").

6 Q. PLEASE SUMMARIZE YOUR EDUCATIONAL AND PROFESSIONAL
7 BACKGROUND.

8 A. I graduated from Carnegie-Mellon University where I earned a Bachelors of Science
9 degree in Electrical Engineering in 1971, a Masters of Science degree in Industrial
10 Administration in 1973 and a PhD in Industrial Administration (Operations Research) in
11 1976. I was employed by Pacific Gas and Electric Company from 1979 to 1989, where I
12 worked on issues related to transmission, generation and fuels planning. From 1989 to
13 2003, I was employed by several consulting and systems development firms (Arthur D.
14 Little, Inc., Mykytyn Consulting Group Inc., Perot Systems Corporation and, PA
15 Consulting Group). I was engaged in consulting assignments involving the application of
16 operations management techniques, economic analysis, and engineering analysis to

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1 evaluate the market potential of new business areas, to improve operations, and to meet
2 new regulatory requirements for a variety of firms involved in the energy industry.

3 During this time, I was involved in assignments for the California Independent System
4 Operator, The California Power Exchange, and ISO-New England.

5 **Q. PLEASE DESCRIBE YOUR RESPONSIBILITIES WITH THE MIDWEST ISO**
6 **AS THEY RELATE TO THIS FILING.**

7 A. I am involved in the development of the processes that will be used to: (1) initially
8 allocate Financial Transmission Rights (“FTRs”) to Market Participants for peak and off-
9 peak periods of four seasons starting on December 1, 2004 based on transmission
10 entitlements; (2) run the FTR auctions; (3) register trades of FTRs that take place on
11 secondary markets; and (4) develop an Illustrative FTR allocation.

12 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

13 A. I will be providing expert testimony in support of: (1) the important role that FTRs play
14 in the centralized security constrained economic dispatch process; (2) the extensive
15 stakeholder discussions on this topic; (3) various options that the Midwest ISO has
16 considered to equitably distribute FTRs; (4) the approach that the Midwest ISO is
17 recommending and the support for this approach; (5) the continuing role of the
18 Organization of MISO States (“OMS”) in FTR distribution; and (6) the background and
19 the basis for the development of an Illustrative FTR allocation.

20 **II. THE ROLE OF FTR IN AN ENERGY MARKET**

21 **Q. WHAT ARE FTRS?**

22 A. FTRs are financial hedging mechanisms that Market Participants can use to manage the
23 risk of congestion charges that they may incur as a result of scheduling Energy

1 A. transactions in the Day-Ahead Energy Market. Market Participants who own FTRs will
2 be protected against paying congestion charges for scheduling power injections (*e.g.*,
3 generation, bilateral purchases, *etc.*) at one location, and power takeouts (*e.g.*, load,
4 bilateral sales) at a different location in the Day-Ahead Energy Market. FTRs will not
5 protect Market Participants from congestion charges that result from scheduling power in
6 the Real-Time Energy Market, deviating in the Real-Time Energy Market from scheduled
7 amounts in the Day-Ahead Energy Market, or from owning FTRs between source and
8 sink that differ from Day-Ahead Energy Market scheduled power injections and
9 withdrawals.

10 **Q. ARE FTRS USED IN OTHER ELECTRICITY MARKETS?**

11 A. Yes. FTRs are used in several energy markets around the world. In the United States,
12 FTRs are offered by PJM Interconnection, L.L.C., New York ISO, ISO New England,
13 and California ISO in their markets. FTRs are also offered by energy markets in New
14 Zealand and Australia, among other countries.

15 **Q. IS IT FEASIBLE TO OPERATE AN ENERGY MARKET WITHOUT FTRS?**

16 A. A system of transmission rights is necessary to operate an effective energy market.
17 Transmission constraints affect the ability of Market Participants to schedule injections
18 and withdrawals at different points on the transmission system. When the effects of
19 transmission constraints on market operations and energy prices are ignored (or
20 incompletely treated), market distortions arise and may invite inappropriate strategies to
21 take advantage of such distortions. If the effects of transmission constraints on energy
22 schedules and prices are taken into account, FTRs are needed to allow Market
23 Participants to hedge the resulting costs.

1 **Q. PLEASE DESCRIBE THE DIFFERENCES BETWEEN FTRS THAT ARE**
2 **“OBLIGATIONS” AND THOSE THAT ARE “OPTIONS”.**

3 A. FTR Options and FTR Obligations are both Point-to-Point FTRs. They both specify a
4 source and a sink and they provide their owner with the right to receive congestion rents
5 based on the difference between the Congestion Component of the Locational Marginal
6 Price (“CC_LMP”) at the source and sink that arise in the Day-Ahead Energy Market.

7 With an FTR Obligation, the congestion payment or congestion rent due to the owner is
8 the following: $(CC_LMP \text{ at Sink} - CC_LMP \text{ at Source}) \times \text{Size of FTR}$.

9 If this quantity is positive, the FTR owner receives a payment from the RTO. Roughly
10 speaking, this will occur when the transmission system experiences congestion in the
11 direction from the source of the FTR to the sink. If the calculated quantity is negative,
12 the FTR owner must pay the RTO. Again, roughly speaking, this will occur when the
13 transmission system experiences congestion in the direction from the sink of the FTR to
14 the source, or counter to the direction of the FTR. With an FTR Obligation, the owner is
15 obligated to accept the congestion payment.

16 In comparison, with an FTR Option the congestion payment due to the owner is the
17 following amount if it is positive: $(CC_LMP \text{ at Sink} - CC_LMP \text{ at Source}) \times \text{Size of}$
18 FTR .

19 If this quantity is positive, the FTR owner receives a payment from the RTO. If it is
20 negative, however, the FTR owner pays nothing to the RTO. That is, the FTR owner has
21 the option to accept the FTR payment if it is positive and reject it if it is negative.

1 **Q. WHAT ARE “COUNTER FLOW” FTRS AND HOW DO THEY WORK?**

2 A. A “Counter Flow” FTR is an FTR Obligation like any other FTR Obligation. An FTR is
3 termed a “Counter Flow” FTR only in relation to other FTRs. A simple example may
4 help explain. Consider a system consisting of two buses (A and B) and one line from A
5 to B with a maximum flow limit of 100 MW either from A to B, or from B to A.
6 Suppose that we had two 100 MW FTRs from A to B, either FTR Obligations or FTR
7 Options. The two 100 MW FTRs from A to B would give their owners either the
8 obligation or option to collect congestion rents on 200 MW from A to B. Since the
9 physical limit on the line is 100 MW, the Midwest ISO could only schedule a net flow of
10 100 MW from A to B in the Day-Ahead Energy Market. As a result, the Midwest ISO
11 would collect congestion rents from scheduling at most 100 MW from A to B. Since the
12 200 MW of FTRs require the Midwest ISO to pay congestion rents for more transmission
13 capacity from A to B than the 100 MW it can schedule from A to B, and on which it can
14 collect congestion charges in the Day-Ahead Energy Market, this would not be feasible
15 and could result in a revenue shortfall. If we were to add one 100 MW FTR Obligation
16 from B to A, we would have a feasible set of FTRs since the 100 MW FTR from B to A
17 would give its owner the obligation to collect congestion rents on 100 MW from B to A.
18 Since this FTR Obligation is from B to A, its owner will have an obligation to pay the
19 Midwest ISO when the owners of the FTRs from A to B receive payments from the
20 Midwest ISO. That is, it provides a “dollar flow” which is “counter” to the dollar flows
21 caused by the other FTRs, thereby bringing the total dollar flow resulting from the set of
22 FTRs to within the limit on congestion charges that the Midwest ISO can collect in the
23 Day-Ahead Energy Market.

1 We can check whether the Midwest ISO will collect sufficient congestion charges in the
2 Day-Ahead Energy Market by checking whether the power flows on the system that
3 would result if injections and withdrawals corresponding to the FTRs that were actually
4 scheduled are within the transmission limits. In general, assuming that injections and
5 withdrawals corresponding to the FTRs were scheduled, a Counter Flow FTR is an FTR
6 Obligation that provides a flow on some component of the transmission system that is
7 counter to the flows caused by other FTRs which would exceed the limit on that
8 component absent the Counter Flow FTR. While we can view the FTRs as placing power
9 flows on the transmission system, it is important to note that FTRs do not actually place
10 physical flows on the elements of the transmission system. Instead, FTRs are financial
11 instruments that create dollar flows that we can decompose and allocate to the various
12 elements of the transmission system. Therefore, when I refer to an FTR causing a “flow”
13 on the transmission system, this means that if an injection and a withdrawal
14 corresponding to the FTR were physically scheduled, a “flow” would result.

15 **Q. WHAT ARE “CANDIDATE FTRS”?**

16 A. In the FTR allocation process, Market Participants will be able to nominate FTRs that
17 they would like to receive. Also, under certain conditions, the Midwest ISO may
18 nominate certain FTRs that Market Participants may be required to accept if they provide
19 counter flows needed to make other FTRs feasible. These nominated FTRs will be based
20 on their existing transmission entitlements. The nominated FTRs are termed Candidate
21 FTRs since they may not satisfy a simultaneous feasibility test and thus may be prorated
22 by Midwest ISO when it determines the actual FTRs allocated to the Market Participants.

1 **Q. HOW DO CANDIDATE FTRS RELATE TO ACTUAL FTRS?**

2 A. Candidate FTRs are the FTRs that Market Participants indicated that they wish to receive
3 in the FTR allocation, or FTRs that they may be required to take in the allocation if
4 feasible. The Midwest ISO will perform a simultaneous feasibility test on the Candidate
5 FTRs and prorate them if necessary to determine a set of FTRs that satisfy the
6 Simultaneous Feasibility Test, described below. This produces the actual FTRs that are
7 allocated to Market Participants. Market Participants can acquire FTRs through the
8 allocation process, auctions, secondary market trades and purchases of transmission
9 service. For the FTRs that Market Participants own, they will collect congestion
10 revenues based on the Locational Marginal Prices that arise in the Day-Ahead Energy
11 Market.

12 **Q. WHAT ARE THE KEY FEATURES OF ANY FTR ALLOCATION PROPOSAL?**

13 A. Prior to the implementation of an LMP-based energy market, Market Participants
14 historically made use of the transmission system in the Midwest to serve load and to
15 engage in energy trades. They had existing entitlements to use the transmission system to
16 support their operations. The Midwest ISO's proposed FTR allocation method will take
17 such existing entitlements into account. There are two primary alternatives for
18 determining how Market Participants receive FTRs. At one extreme, the Midwest ISO
19 could specify the Candidate FTRs for each Market Participant based on the Market
20 Participant's historical use of its existing transmission entitlements. At the other extreme,
21 Market Participants could be entitled to nominate Candidate FTRs based on their existing
22 entitlements. It is also possible for the Midwest ISO to develop allocation approaches
23 that lie somewhere between these two extremes. Such an approach would give Market

1 Participants some freedom to nominate the Candidate FTRs that they would wish to
2 receive and would require that some Candidate FTRs based on historical usage be
3 included.

4 **Q. WHY IS IT IMPORTANT FOR THE MIDWEST ISO TO UTILIZE A**
5 **SIMULTANEOUS FEASIBILITY TEST TO EVALUATE THE FEASIBILITY OF**
6 **FTRS?**

7 A. Once the Candidate FTRs have been specified, there are several ways in which the actual
8 set of FTRs can be determined. The Midwest ISO could attempt to ensure that it will
9 collect sufficient congestion charges from Energy transactions that are scheduled in the
10 Day-Ahead Energy Market to pay the congestion rents due to the holders of the FTRs
11 absent changes in the Network Model between that used to allocate FTRs and the one
12 used in scheduling the Day-Ahead Energy Market. It could do this by ensuring that the
13 flows that would result on the network if injections and withdrawals corresponding to the
14 actual set of FTRs were physically scheduled would satisfy all transmission constraints.
15 For FTR Obligations, the flows would be calculated assuming that injections and
16 withdrawals corresponding to the FTRs were scheduled. For FTR Options, the Midwest
17 ISO would have to consider two cases for each FTR Option. In one case, the flows
18 would be calculated assuming that an injection and withdrawal corresponding to the FTR
19 Option were scheduled. In the other case, the flows would be calculated assuming that an
20 injection and withdrawal corresponding to the FTRs Option were not scheduled. We
21 must consider these two cases since the owner of the FTR Option has the option to accept
22 payment if the congestion rents are positive (first case) and the option to reject payment if
23 the congestion rents are negative (second case). All possible combinations of the cases

1 for the set of FTR Options must be considered. This is the Simultaneous Feasibility Test
2 (“SFT”). If the Candidate FTRs did not satisfy the SFT, the Midwest ISO would reduce
3 the Candidate FTRs until the SFT was satisfied. Alternatively, the Midwest ISO could
4 allocate the Candidate FTRs to the Market Participants without requiring them to satisfy
5 the SFT. This increases the likelihood that the Midwest ISO will not collect sufficient
6 congestion charges from schedules in the Energy Markets to pay the congestion rents due
7 to the FTRs. In this case, some method of reducing payments to holders of FTRs or
8 uplifting any shortfall must be implemented. These two approaches also represent two
9 ends of a spectrum; it is possible to develop an allocation procedure that lies somewhere
10 between the two.

11 **Q. WHY IS THE MIDWEST ISO INITIALLY IMPLEMENTING FTR**
12 **OBLIGATIONS IN THE ALLOCATION?**

13 A. The Midwest ISO is proposing initially to allocate FTR Obligations in its allocation
14 process because allocating FTR Obligations will likely allow the Midwest ISO to allocate
15 more FTRs on the system. This is because when two FTR Obligations cause flows on a
16 transmission element that are in opposite directions, their total flow on the element is
17 given by adding a positive flow and a negative flow. This, in turn, results in a net flow
18 that is lower in absolute value than the maximum of the absolute values of the individual
19 flows. Implementing FTR Obligations will allow other FTRs to make use of the
20 remaining transmission capacity. We can add flows of FTR Obligations that are in
21 opposite directions since an FTR Obligation has an obligation to pay if the congestion
22 component of the LMP at the sink is higher than at the source in the Day-Ahead Energy
23 Market. With FTR Options, we are not able to add the flow caused by an Option and the

1 flow caused by another FTR when they are in opposite directions. Since an FTR Option
2 does not have an obligation to pay when it is counter to the direction of congestion in the
3 Day-Ahead Energy Market, we cannot add its negative flows to those caused by other
4 FTRs. If it is counter to the direction of congestion, the holder of the FTR Option will
5 not pay the congestion rent to the Midwest ISO. As a result, the effect is as if the FTR
6 Option did not exist in terms of the payments due to the Midwest ISO.

7 In addition to enabling Midwest ISO to possibly allocate more FTRs, FTR
8 Obligations are also simpler to treat in the Simultaneous Feasibility Test. To calculate
9 the capacity required to support a set of FTR Obligations, we can simply add the flows
10 that would be caused by the set of FTR Obligations. With FTR Options, on the other
11 hand, we must model the flows caused by each FTR Option in each transmission element.
12 We must treat the flows in opposite direction on each transmission element separately.
13 To calculate the flows in a given direction, we must add flows that are in that direction.
14 We cannot subtract the flows caused by FTR Options in the opposite direction since they
15 will not pay congestion rents when congestion is in the opposite direction. Effectively,
16 we must replicate the model of the transmission system for each FTR Option treated.
17 This greatly increases the complexity of the problem to be solved and the resources
18 needed to solve it.

19 **Q. IS IT FEASIBLE FOR THE MIDWEST ISO TO DEVELOP OPTION FTRS AT A**
20 **LATER DATE?**

21 A. The Midwest ISO is working to include FTR Options in its auctions. When it is feasible
22 for the Midwest ISO to do so, it will provide Market Participants with FTR Options. For
23 example, it is theoretically feasible to add options to the auction. However, we must be

1 sure that it does not result in a problem that the Midwest ISO is incapable of solving in
2 practice.

3 A Market Participant that submits a Transmission Service Request (“TSR”) for new
4 firm Transmission Service will be able to request a corresponding FTR as well. We plan
5 to allow the Market Participant to request either an FTR Obligation or an FTR Option.

6 We will continue to work to implement FTR Options in other parts of the FTR
7 allocation and auction processes and make them available when feasible.

8 **Q. HOW LONG WOULD IT TAKE FOR THE MIDWEST ISO TO IMPLEMENT**
9 **FTR OPTIONS?**

10 A. Although we are working to have FTR Options available in the annual FTR auctions that
11 we will run prior to the start of market operations on December 1, 2004, this schedule
12 could be adversely impacted if we receive an unexpectedly large number of bids for FTR
13 Options in the auction. As described above, we plan to allow a participant to request
14 FTR Obligations or Options when submitting a TSR.

15 **Q. CAN THE MIDWEST ISO ALLOCATE SUFFICIENT FTRS TO PROVIDE ALL**
16 **MARKET PARTICIPANTS WITH AN ABILITY TO MANAGE RISKS OF**
17 **CONGESTION COSTS?**

18 A. The Midwest ISO can allocate FTRs sufficient to enable Market Participants to manage
19 their congestion risks to some extent. It is unlikely, however, that the Midwest ISO
20 would be able to allocate sufficient FTRs so that each Market Participant would never
21 have to pay congestion fees that exceed the payment to its FTRs in each one of the 8760
22 hours of the Day-Ahead Energy Market over the course of a year. Fortunately, however,
23 that goal is not necessary to enable Market Participants to effectively manage congestion

1 risks. This is because a Market Participant is not likely to schedule Energy transactions
2 that exactly match its FTRs in each and every hour. There will most likely be some hours
3 when a Market Participant's FTR holdings will exceed its transactions, and it will earn
4 more congestion rents from its FTRs than it pays in congestion fees for its scheduled
5 transactions. Market Participants could seek to obtain sufficient FTRs so that the total
6 that they pay for congestion fees in the Day-Ahead Energy Market over some time frame
7 (e.g., one year) is approximately covered by congestion rents that they receive from the
8 FTRs that they hold over such period. Even if congestion risks cannot be totally
9 eliminated, Market Participants can seek to nominate FTRs that would minimize this risk.

10 **Q. WHY WOULD IT NOT BE DESIREABLE TO "UPLIFT" ALL OF THE COSTS**
11 **ASSOCIATED WITH PROVIDING MARKET PARTICIPANTS WITH "FULL"**
12 **FTR PROTECTION?**

13 A. I will assume that full protection means giving FTRs to Market Participants that exactly
14 equal the MW sizes of their existing entitlements. In this case, it is highly unlikely that
15 the FTRs could be allocated to satisfy the Simultaneous Feasibility Test. Consequently,
16 there will likely be many hours during which the payments to the FTR holders would
17 exceed the congestion charges for schedules submitted in the Day-Ahead Energy Market.
18 That is, there would likely be many hours with FTR revenue inadequacy. This shortfall
19 would have to be funded by some sort of uplift charge. In addition, such an allocation of
20 FTRs could result in large windfalls to some Market Participants since there will likely be
21 many hours during which they will not schedule transactions equal to the sizes of the
22 FTRs that they would hold. During such hours, they would be likely to earn congestion
23 rents from their FTRs that are in excess of their congestion costs. Thus, the uplift would

1 fund windfalls to some Market Participants and could result in significant cost shifts in
2 the Energy Market to other Market Participants forced to bear the costs of the uplift
3 charges.

4 **Q. IF THERE ARE FEWER FTRS AVAILABLE THAN FTRS SOUGHT BY**
5 **PARTIES, WHAT PROCEDURES WILL THE MIDWEST ISO UTILIZE TO**
6 **PRORATE AVAILABLE FTRS?**

7 A. If necessary, the Midwest ISO will prorate some Candidate FTRs so that the transmission
8 constraints imposed by the Simultaneous Feasibility Test are satisfied. The Midwest ISO
9 plans to reduce Candidate FTRs so that the sum of the squares of the percentage
10 curtailments to the individual Candidate FTRs weighted by the size of the Candidate FTR
11 is minimized. Under this methodology, all Candidate FTRs that contribute to the flow on
12 a Binding Transmission Constraint (*i.e.*, in the direction of the binding constraint) will be
13 reduced by an amount that is proportional to the flow that the Candidate FTR caused on
14 such transmission constraint. An individual Candidate FTR will be reduced by the sum
15 of these reductions, but not any more than the size of the Candidate FTR.

16 **Q. DID THE MIDWEST ISO DISCUSS ALTERNATE PRORATION PROCEDURES**
17 **WITH THE STAKEHOLDERS?**

18 A. Yes. Alternate proration procedures were discussed with stakeholders. In one method,
19 the Midwest ISO suggested that Candidate FTRs that contribute to the flow on a Binding
20 Transmission Constraint (*i.e.*, in the direction of the binding constraint) would be reduced
21 by an amount that is proportional to size of the Candidate FTR if the percentage of the
22 Candidate FTR that flows on the constraint is above some threshold percentage (*e.g.*,
23 5%). Under this option, an individual Candidate FTR would be reduced by the sum of

1 these reductions. This procedure, however, had some problems. For one, a Candidate
2 FTR could be reduced by over 100%. In other words, the FTR awarded could be in the
3 opposite direction of the Candidate FTR. For example, a Market Participant with a 100
4 MW Candidate FTR from A to B could actually be awarded a 10 MW FTR from B to A.
5 This could result if a Candidate FTR contributed to flow on several binding constraints
6 and the sum of the percentage reductions made for each of these constraints exceeded
7 100%. It could also occur if several Candidate FTRs contributed flows less than the
8 threshold on a constraint, and so were exempt from reductions, yet the sum of the flows
9 to which they contributed on the constraint exceeded the constraint limit. Although we
10 discussed ways to try to correct the problems with this proration procedure with the
11 Midwest ISO stakeholders, the revised procedures are much more complex to implement
12 and only limited testing has been possible.

13 **Q. WHAT WERE THE STAKEHOLDER REACTIONS TO THE PRORATION**
14 **PROCEDURES THAT THE MIDWEST ISO WILL BE IMPLEMENTING?**

15 A. Some Market Participants have expressed support while others have expressed a
16 preference for an alternative methodology.

17 **Q. WILL A MARKET PARTICIPANT ONLY BE ABLE TO MANAGE ITS RISKS**
18 **OF CONGESTION COSTS BY HOLDING 100% OF THE FTRS ASSOCIATED**
19 **WITH SERVING ITS LOAD?**

20 A. No. Holding 100% of the FTR associated with serving its Load would most likely result
21 in the party collecting more congestion rents from the FTRs than it pays for its Energy
22 schedules in the Day-Ahead Energy Market. As discussed above, a Market Participant is
23 not likely to schedule Energy transactions that exactly match its FTRs in each hour.

1 There may be some hours when its FTR holdings exceed its transactions and the party
2 earns more congestion rents from its FTRs than it pays in congestion fees for its
3 schedules. Market Participants are expected to seek to obtain sufficient FTRs so that the
4 total that they pay for congestion fees in the Day-Ahead Energy Market over a period
5 such as a year is approximately covered by congestion rents that they receive from the
6 FTRs they hold over that period. Even if congestion risk cannot be totally eliminated,
7 Market Participants can seek to nominate FTRs that would minimize the risk.

8 **Q. DOES THE MIDWEST ISO ENVISION HAVING ANNUAL OPPORTUNITIES**
9 **FOR NOMINATING NEW FTRS?**

10 A. Yes. The Midwest ISO has annual allocation procedures in the Tariff.

11 **Q. CAN A MARKET PARTICIPANT OBTAIN ADDITIONAL FTRS AFTER THE**
12 **INITIAL DISTRIBUTION OF FTRS?**

13 A. Yes. A Market Participant will be able to bid to buy and offer to sell FTRs for each of
14 the upcoming four seasons in an annual auction. Market Participants also may be
15 allocated additional FTRs during a monthly allocation if forecast conditions indicate that
16 additional transmission capacity is available. In addition, there will be monthly auctions
17 in which Market Participants can bid to buy and sell FTRs for the upcoming month. If a
18 Market Participant seeks to purchase new Firm Point-to-Point Transmission Service, the
19 Market Participant will be given the opportunity to request FTRs for the Transmission
20 Service.

1 **Q. HOW WILL THE ANNUAL AND MONTHLY FTR AUCTION PROCEDURES**
2 **BE OPERATED?**

3 A. The annual auctions will consist of eight separate auctions; one auction for peak periods
4 and one for off-peak periods in each of the four seasons. Market Participants will be able
5 to bid to buy FTRs in each of these auctions and those with FTRs may offer to sell their
6 FTRs. In a bid to buy FTRs in one of the eight annual auctions, a Market Participant will
7 specify the type of FTR it wishes to purchase (source, sink, obligation or option), the
8 maximum MW that it wishes to purchase, and the maximum price that it is willing to pay.
9 In an offer to sell FTRs in one of the eight annual auctions, a Market Participant that
10 owns FTRs will specify the type of FTR it wishes to sell, (source, sink, obligation or
11 option), the maximum MW that it wishes to sell, and the minimum price that it is willing
12 to accept. The Market Participant must own an FTR that it offers to sell in an auction.
13 The Midwest ISO will clear each of the eight auctions independently. In clearing the
14 auction, the Midwest ISO will determine the set of FTR bids that it can fill and the set of
15 offers to accept so as to maximize the value of the auction as measured by the total of bid
16 price times quantity of bids filled for all of the bids filled minus the total of offer price
17 times quantity of offers accepted for all of the offers accepted. The Midwest ISO will
18 calculate market clearing prices for all FTRs and charge buyers and pay sellers the
19 market clearing price for their FTRs.

20 Each monthly auction will consist of two separate auctions; one auction for peak
21 periods and one for off-peak periods in the month. Otherwise, the monthly auction will
22 be operated in the same manner as the annual auction.

1 **Q. WILL ADDITIONAL FTRS BE AVAILABLE IN THE FUTURE IF THERE IS**
2 **NEW CONSTRUCTION OF TRANSMISSION FACILITIES OR OTHER**
3 **CHANGES IN THE MIDWEST ISO TRANSMISSION SYSTEM?**

4 A. Yes. The Midwest ISO will allow the party that is responsible for the cost of the new
5 construction to elect to either request FTRs that the construction makes feasible or to
6 receive credits under Attachment R or X of the Tariff, as applicable. As an interim
7 measure, Midwest ISO will allocate such FTRs for the allocation year on an annual basis.

8 **Q. WILL THERE BE OPPORTUNITIES FOR PARTIES TO OBTAIN FTRS**
9 **THROUGH BILATERAL MEANS?**

10 A. Yes. The Midwest ISO will maintain an electronic bulletin board where parties can post
11 bids to buy and offers to sell FTR. Parties can negotiate a bilateral trade (using the
12 information on the bulletin board or other means) and settle the trade between them.
13 When they strike a deal, the parties to the trade may request that the Midwest ISO change
14 the ownership of the FTRs from the seller to the buyer. The Midwest ISO will ensure
15 that the seller has the FTRs it is selling and it will apply its creditworthiness policies to
16 ensure that the buyer is financially able to hold the FTRs before transferring ownership of
17 the FTRs.

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III. STAKEHOLDER DISCUSSIONS REGARDING INITIAL FTR DISTRIBUTION

Q. HAS THE MIDWEST ISO BEEN WORKING WITH ITS STAKEHOLDERS TO ATTEMPT TO RESOLVE QUESTIONS REGARDING THE INITIAL ALLOCATION OF FTRS?

A. Yes. The Midwest ISO has been discussing approaches to performing an initial allocation of FTRs based on existing entitlements at the Transmission Rights Task Force meetings that occurred during 2003. After the formation of the Market Subcommittee (“MSC”) in 2003, the MSC became the forum for continued discussions with stakeholders.

Q. WHAT ARE SOME OF THE FACTORS THAT HAVE RESULTED IN DIFFICULTY IN ACHIEVING STAKEHOLDER CONSENSUS ON INITIAL DISTRIBUTION OF FTRS?

A. The stakeholders were primarily unable to achieve consensus on the following major issues:

(1) How much flexibility should Market Participants be given when nominating Candidate FTRs based on their existing entitlements? Should Market Participants be required to nominate Candidate FTRs that reflect historical usage? That is, if an existing entitlement was utilized at a high rate historically, should the Market Participant be required to nominate a Candidate FTR for that existing entitlement? Or should Market Participants be free to nominate the Candidate FTRs from among their existing entitlements based on their forecasts of economic benefit of holding the FTRs?

(2) How should a set of Candidate FTRs that does not satisfy the Simultaneous

1 Feasibility Test be treated? Should the Candidate FTRs be prorated to satisfy the SFT?
2 Or should the entire set of FTRs be allocated and any revenue inadequacy be handled by
3 an uplift? Should Market Participants who have existing entitlements with high historical
4 use be required to nominate Candidate FTRs for those entitlements if those Candidate
5 FTRs would provide counterflows that are necessary to make the nominated Candidate
6 FTRs of other Market Participants feasible if those Candidate FTRs correspond to
7 transmission entitlements with high historical usage?

8 (3) If proration is to be used to enforce simultaneous feasibility, which proration
9 methodology should be employed? These proration options were discussed above.

10 (4) What is the appropriate number and size of the tiers in a tiered
11 nomination/allocation process?

12 (5) How should Grandfathered Agreements (“GFAs”) be taken into account in the
13 allocation process? Should the Midwest ISO physically carve out the transmission
14 capacity to support the Grandfathered Agreements? Or should the Midwest ISO be
15 responsible for allocating FTRs for the Grandfathered Agreements? If so, should the
16 Market Participants scheduling GFAs receive the FTRs and pay congestion for their
17 schedules? Or should Market Participants scheduling GFAs not pay congestion and the
18 Midwest ISO use the allocated FTRs to defray the congestion fees that are not collected?

1 **Q. BASED UPON THE LENGTHLY DISCUSSIONS THAT HAVE OCCURRED TO**
2 **DATE, DO YOU BELIEVE THAT ALL STAKEHOLDERS WILL BE ABLE TO**
3 **ACHIEVE A CONSENSUS POSITION ON THESE ALLOCATION ISSUES?**

4 A. No. The extensive stakeholder discussions have revealed that while some compromise
5 has been possible, it is unlikely that unanimity or a preponderant consensus will be
6 reached on all issues.

7 **IV. METHODS FOR DISTRIBUTING FTRS**

8 **Q. WHAT ARE SOME OF THE OPTIONS THAT THE MIDWEST ISO HAS**
9 **INVESTIGATED FOR DISTRIBUTING FTRS?**

10 A. Based upon requests from stakeholders, the Midwest ISO developed a tiered
11 allocation/nomination procedure for the initial allocation of FTRs. The options that have
12 been considered differ in the number of tiers (*e.g.*, three or four). They also differ in the
13 amount of Candidate FTRs that Market Participants may nominate in each tier and how
14 the tier limits are determined. They differ in the amount of freedom that Market
15 Participants have in deciding on the existing entitlements for which they may choose to
16 nominate FTRs (or not nominate) in each tier. They also differ in whether Candidate
17 FTRs will be prorated to satisfy an SFT in each tier or whether FTRs will be provided for
18 all nominated FTRs in some tiers, and how any resulting revenue inadequacy would be
19 treated.

1 **Q. PLEASE DESCRIBE THE ATTRIBUTES OF THE THREE-TIER**
2 **ALLOCATION/NOMINATION METHODOLOGY THAT THE MIDWEST ISO**
3 **DEVELOPED AND THE STAKEHOLDERS REVIEWED ON OCTOBER 2,**
4 **2003?**

5 A. This proposed FTR nomination and allocation process would have consisted of three
6 tiers. The first tier would have consisted of a mandatory nomination of FTR Obligations
7 by each Market Participant for its minimum Load level. A Market Participant with
8 existing Network Integration Transmission Service (“NITS”) would be required to
9 nominate Candidate FTR obligations equal to its minimum Load being served by
10 Network Integration Transmission Service. A Market Participant with Firm Point-to-
11 Point Transmission Service entitlements would be required to nominate Candidate FTR
12 Obligations equal to the minimum flow for each of the Firm Point-to-Point Transmission
13 Service entitlements it held. Sources for Candidate FTRs nominated for Network
14 Integration Transmission Service would be designated Network Resources used to serve
15 the Load receiving Network Integration Transmission Service selected in order of their
16 historic capacity factors. The FTRs allocated in Tier I would be determined by prorating
17 the Tier I Candidate FTRs so that they satisfy the SFT.

18 The second tier would consist of a voluntary nomination of Candidate FTR
19 Obligations. Each Market Participant would be given the opportunity to nominate
20 additional Candidate FTRs. All Market Participants could nominate additional Candidate
21 FTRs sufficient to cover 75% of their annual energy requirement for Loads served by
22 Network Integration Transmission Service, or 75% of the annual average flow for Firm
23 Point-to-Point Transmission Service entitlements. Nominations for Tier II Candidate

1 FTRs for Network Integration Transmission Service may be from any designated
2 Network Resource used to serve the NITS Load with an historical capacity factor greater
3 than 60%. The FTRs allocated in Tier II would be determined by prorating the Tier II
4 Candidate FTRs so that they and the allocated Tier I FTRs satisfy the SFT.

5 In the third tier, each Market Participant may voluntarily nominate additional
6 Candidate FTR Obligations up to a MW limit set by its peak Load receiving Network
7 Integration Transmission Service and up to the full reservation amount for Firm Point-to-
8 Point Transmission Service. The FTRs allocated in Tier III would be determined by
9 prorating the Tier III Candidate FTRs so that they and the allocated Tier I and Tier II
10 FTRs satisfy the SFT.

11 The above allocation and nomination process seeks to require Market Participants to
12 nominate Candidate FTRs in the first tier that approximate their base load usage of the
13 system. This would require that Candidate FTRs be nominated in Tier I for transmission
14 service that was historically used at a high rate. If such service had historically provided
15 counter flows upon which other high usage transmission service relied, the Candidate
16 FTRs providing the counter flow would be nominated in Tier I. The succeeding tiers
17 gave Market Participants increasing flexibility in deciding which FTRs they might wish
18 to nominate.

19 **Q. PLEASE DESCRIBE THE ALTERNATE NOMINATION PROPOSAL THAT**
20 **WAS PROPOSED BY CINERGY ON DECEMBER 18, 2003?**

21 A. The Cinergy proposal was also a three-tiered nomination and allocation process. In the
22 first tier, Market Participants could nominate Candidate FTRs for their Network
23 Integration Transmission Service up to 35% of the peak Load served by Network

1 Integration Transmission Service. The sources of the FTRs could be any designated
2 Network Resource that serves the NITS Load. Market Participants with Firm Point-to-
3 Point Transmission Service could nominate Candidate FTRs up to 35% of the service
4 entitlement. There would be no requirement to nominate any specific FTRs or any
5 minimum level. The FTRs allocated in Tier I would be determined by prorating the
6 Tier I Candidate FTRs so that they satisfy the SFT.

7 In the second tier, Market Participants could nominate additional Candidate FTRs for
8 their Network Integration Transmission Service up to 35% of the peak load served by the
9 service. The sources of the FTRs could be any designated Network Resource that serves
10 the NITS load. Market Participants with Firm Point-to-Point Transmission Service could
11 nominate additional Candidate FTRs up to 35% of the service entitlement. There would
12 be no requirement to nominate any specific FTRs or any minimum level. The FTRs
13 allocated in Tier II would be determined by prorating the Tier II Candidate FTRs so that
14 they and the existing Tier I FTRs satisfy the SFT.

15 In the third tier, Market Participants could nominate additional Candidate FTRs for
16 their Network Integration Transmission Service up to 30% of the peak Load served by
17 the service. The sources of the FTRs could be any designated Network Resource that
18 serves the NITS load. Market Participants with Firm Point-to-Point Transmission
19 Service could nominate additional Candidate FTRs up to 30% of the service entitlement.
20 There would be no requirement to nominate any specific FTRs or any minimum level.
21 The FTRs allocated in Tier III would be determined by prorating the Tier III Candidate
22 FTRs so that they and the existing Tier I and Tier II FTRs satisfy the SFT.

1 This procedure gives the Market Participants flexibility in deciding which Candidate
2 FTRs they may choose to nominate and the amount they would nominate in each tier.

3 **Q. ARE THESE THE ONLY TWO METHODOLOGIES THAT THE MIDWEST ISO**
4 **HAS CONSIDERED?**

5 A. No. Many variations on these proposals were considered. Some variations modified the
6 selection of sources for Candidate FTRs in the method proposed by Midwest ISO on
7 October 6, 2003. For example, one variation would allow Market Participants to select
8 the sources for Tier I Candidate FTRs for Network Integration Transmission Service
9 from among the designated Network Resources with capacity factors over 70%. Tier I
10 would also include Candidate FTRs for Firm Point-to-Point Transmission Service if the
11 service had a historical scheduling factor over 70%.

12 Other variations allowed Market Participants flexibility to nominate Candidate FTRs
13 similar to that proposed by Cinergy. However, if a Candidate FTR with a high historical
14 scheduling factor were to be curtailed in Tier I (and possibly Tier II), the Midwest ISO
15 would add FTRs that would provide counterflows that would restore the curtailed FTR if
16 it could find high scheduling factor transmission service that could provide the
17 counterflow and for which the Market Participant that has the service did not nominate a
18 Candidate FTR.

19 Still other variations included considering a four-tiered allocation process.
20 Some proposals would restrict Market Participants to nominating Candidate FTRs that
21 are constant for all seasons and peak and off-peak periods in early tiers, while allowing
22 FTR nominations to vary by season and peak and off peak period in later tiers.

1 **Q. WHAT ARE THE RELATIVE MERITS OF THE PROPOSALS OF THE**
2 **VARIOUS FTRS PROPOSALS THAT THE STAKEHOLDERS HAVE**
3 **DISCUSSED?**

4 A. Some of the proposals seek to increase the probability that Market Participants will
5 receive FTRs for transmission service that they have historically used highly. These
6 proposals restrict a Market Participant's ability to nominate Candidate FTRs in the early
7 tiers and require that some minimum level of Candidate FTRs for historically highly used
8 transmission service be nominated. One goal is to ensure that Candidate FTRs will be
9 nominated if they provide counterflows that other Candidate FTRs for highly used
10 transmission service require for feasibility.

11 The proposals that tend to give the Market Participants flexibility in deciding which
12 FTRs to nominate in each tier and whether or not to nominate give Market Participants
13 greater flexibility to manage their expected congestion risks in the future market. They
14 also tend to treat all existing transmission entitlements equally in that if a Market
15 Participant pays for the transmission service, that Market Participant has the right to
16 nominate or not to nominate a Candidate FTR for the service and to decide upon which
17 tier in which to nominate the Candidate FTR.

18 **Q. ARE ALL OF THE PROPOSALS EQUALLY ABLE TO BE IMPLEMENTED BY**
19 **THE MIDWEST ISO GIVEN THE AVAILABLE TIME AND RESOURCES?**

20 A. No. Some of the methods would require development of additional capabilities or change
21 existing capabilities. These include changes to the systems for prorating FTRs to satisfy
22 the Simultaneous Feasibility Test, development of systems to calculate FTRs that must be

1 nominated in some tiers, systems to check whether the nominated FTRs satisfy
2 restrictions, etc.

3 **Q. ARE ALL OF THE PROPOSALS EQUALLY ABLE TO PROTECT EXISTING**
4 **NATIVE LOAD TRANSACTIONS?**

5 A. No. Those that have no restrictions on nominations increase the capability of transactions
6 not serving Native Load to compete with Native Load for FTRs. Many of the proposals
7 have approaches to increase the likelihood that transactions that have high historical
8 usage and thus those transactions that were used to serve Native Load will be able to
9 receive the FTRs that they nominate. Some approaches would involve assigning
10 counterflow FTRs to those who have historically provided counterflows on the system
11 that made the transactions possible. Various mechanisms to achieve this have been
12 proposed. Other approaches would simply ensure that transactions that have high
13 historical usage will receive the FTRs that they nominate and would uplift any resulting
14 revenue inadequacy.

15 **Q. DO SOME OF THE PROPOSALS OFFER POTENTIALLY GREATER**
16 **PROTECTION FOR LOAD LOCATED IN HISTORICALLY CONGESTED**
17 **AREAS OF THE MIDWEST ISO'S REGION?**

18 A. Yes for the reasons given above.
19

20 **V. MIDWEST ISO'S PROPOSAL FOR INITIAL DISTRIBUTION OF FTRS**

21 **Q. PLEASE DESCRIBE IN DETAIL THE OPTION FOR INITIALLY**
22 **DISTRIBUTING FTRS THAT THE MIDWEST ISO IS PROPOSING.**

23 A.

1 After considerable discussions with stakeholders, the Midwest ISO has
2 determined that the most equitable and efficient methodology for initially distributing
3 FTRs is the following four-tiered approach. In this approach Market Participants will be
4 given the opportunity to nominate Candidate FTR Obligations for their existing Tariff
5 service whether it is Network Integration Transmission Service used to serve designated
6 Load from designated Network Resources or Firm Point-to-Point Transmission Service a
7 with duration of one year or more. In addition, Market Participants with Pre-OATT
8 contracts (referred to as Grandfathered Agreements or “GFAs”) will be given the
9 opportunity to convert the GFA to OATT service or retain the Pre-OATT Contract. If the
10 Market Participant decides to retain the GFA, the Market Participant can choose from
11 three options related to congestion treatment. First, the Market Participant can choose to
12 nominate Candidate FTRs for the GFA in the nomination/allocation process and receive
13 FTRs, in which case the Market Participant will pay congestion fees for schedules that
14 use the GFA. This is termed Pre-OATT Converted Service. A second option is to
15 choose to be exempt from paying congestion charges for schedules submitted under the
16 Pre-OATT Contract in the Day-Ahead Energy Market, in which case the Market
17 Participant would not receive FTRs for the GFA but would have the quantities that it
18 could nominate in the various tiers affected. This option is termed Pre-OATT Congestion
19 Cost Refund, or Pre-OATT CCR Service in the Tariff. Finally, the Market Participant can
20 choose to pay congestion fees for schedules submitted under the Pre-OATT Contract, not
21 receive FTRs and not have the Pre-OATT Contract affect the availability of FTRs nor the
22 ability of the Market Participant to nominate.

23 In each tier, Market Participants will be provided with the opportunity to nominate

1 FTRs for Network Integration Transmission Service from designated Network Resources
2 to the load served or for Pre-OATT Converted Service. The tier sizes for these
3 nominations will depend upon the forecast Network Integration Transmission Service
4 peak load for the upcoming Allocation Period plus Pre-OATT Converted Service plus
5 Pre-OATT CCR Service. In addition, in each tier, Market Participants will be provided
6 with the opportunity to nominate Candidate FTRs for existing Firm Point-to-Point
7 Transmission Service with a term of one year or longer.

8 The tier size for both Network Integration Transmission Service plus Pre-OATT
9 service and for each Firm Point-to-Point Transmission Service entitlement in each tier
10 will be:

11 Tier I: thirty five percent (35%)

12 Tier II: fifty percent (50%)

13 Tier III: seventy five percent (75%)

14 Tier IV: one hundred percent (100%)

15 FTRs will only be allocated to Market Participants in each tier to the extent that the
16 Midwest ISO determines that such FTRs satisfy its Simultaneous Feasibility Test,
17 subject to restoration during a Transition Period, as described below. Allocated FTRs
18 will be obligations.

19 **Tier I Nomination and Allocation Procedures.** Market Participants will be eligible to
20 nominate CFTRs up to (1) thirty five percent (35%) of the sum of their forecast Network
21 Integration Transmission Service peak load for the upcoming Allocation Period plus Pre-
22 OATT Converted Service plus Pre-OATT CCR Service, and (2) thirty five percent (35%)
23 of the reservation MW quantity for each annual or longer term Firm Point-to-Point

1 Transmission Service. Each Tier I CFTR nomination will be for a single MW value that
2 will apply to all seasons and for peak and off-peak periods. CFTRs equal to 100% of the
3 Pre-OATT CCR Service will be automatically included in Tier I by the Midwest ISO.
4 FTRs allocated based on these CFTRs for Pre-OATT CCR Service will be held by the
5 Midwest ISO to defray the cost of refunding congestion charges for schedules submitted
6 under these unconverted Pre-OATT agreements in the Day-Ahead Energy Market. An
7 SFT will be performed for each season and time period for Tier I CFTRs and CFTRs will
8 be reduced in each season and time period as required to achieve simultaneous feasibility.

9 CFTRs for Pre-OATT CCR Service shall be included in the Tier I nomination at the
10 full MW quantity of the Existing Entitlement. CFTRs for OATT service and for Pre-
11 OATT Converted Service may be nominated in addition to the Pre-OATT CCR Service
12 CFTRs up to the Tier I cap. For example:

13 A Market Participant with 1,000 MW of Network Integration Transmission Service
14 peak load and no Pre-OATT Service would be eligible to nominate 350 MW ($1,000 \text{ MW} \times .35$) in Tier I from its designated Network Resources to its NITS Loads.

16 A Market Participant with 800 MW of Network Integration Transmission Service
17 peak load and 200 MW of Pre-OATT Converted Service would be eligible to nominate
18 350 MW ($(800 \text{ MW} + 200 \text{ MW}) \times .35$) in Tier I from its designated Network Resources
19 to its NITS Loads and from its Pre-OATT Converted Service entitlements.

20 A Market Participant with 800 MW of Network Integration Transmission Service
21 peak load, 100 MW of Pre-OATT CCR Service and 100 MW of Pre-OATT Converted
22 Service would have total Tier I nomination eligibility of 350 MW ($(800 \text{ MW} + 100 \text{ MW}$
23 $+ 100 \text{ MW}) \times .35$), less 100 MW for the Pre-OATT CCR Service leaving 250 MW

1 available to be nominated from its designated Network Resources to its NITS Loads and
2 Pre-OATT Converted Service entitlements. The 100 MW of Pre-OATT CCR Service
3 CFTRs would be automatically included in Tier I.

4 In situations where the MW quantity of Pre-OATT CCR Service exceeds the Tier I
5 limit, Tier I will include only Pre-OATT CCR Service CFTRs. All CFTRs for the Pre-
6 OATT CCR Service would be included in Tier I. The amount by which the CFTRs for
7 Pre-OATT CCR Service exceed the Tier I limit will reduce nomination limits in
8 subsequent tiers. For example: A Market Participant with 700 MW of Network
9 Integration Transmission Service peak load and 500 MW of Pre-OATT CCR Service
10 would be eligible to nominate 420 MW $((700 \text{ MW} + 500 \text{ MW}) \times .35)$ in Tier I. The
11 Tier I nomination would be for the full amount of the Pre-OATT CCR Service or 500
12 MW of Pre-OATT CCR Service CFTRs. This exceeds the Tier I limit by 80 MW. This
13 80 MW of Pre-OATT CCR Service CFTRs over the Tier I limit would be taken into
14 account in setting nomination limits in Tier II.

15 **Tier II Nomination and Allocation Procedures.** Market Participants will be eligible to
16 nominate CFTRs up to the maximum of zero and the quantity given by fifty percent
17 (50%) of the sum of their forecast Network Integration Transmission Service peak load
18 for the upcoming Allocation Period plus Pre-OATT Converted Service plus Pre-OATT
19 CCR Service, less any FTRs allocated in Tier I for Network Integration Transmission
20 Service and Pre-OATT Converted Service and less the CFTRs nominated in Tier I for
21 Pre-OATT CCR Service. Market Participants will also be able to nominate up to fifty
22 percent (50%) of the reservation MW quantity for each annual or longer term Firm Point-
23 to-Point Transmission Service less any FTR granted in Tier I for the Firm Point-to-Point

1 Transmission Service. Tier II will include eight independent nominations: one for each of
2 four seasons and two time periods (peak and off-peak). Any Pre-OATT CCR Service
3 CFTRs over the Tier I limit will reduce the amount that a Market Participant can
4 nominate in Tier II. An SFT will be performed for each season and time period for
5 Tier II CFTRs and CFTRs will be reduced in each season and time period as required to
6 achieve simultaneous feasibility. Previously allocated Tier I FTRs will be fixed (not
7 subject to reduction) in the Tier II process.

8 **Tier III Nomination and Allocation Procedures.** Market Participants will be eligible
9 to nominate CFTRs up to the maximum of zero and the quantity given by seventy five
10 percent (75%) of the sum of their forecast Network Integration Transmission Service
11 peak load for the upcoming Allocation Period plus Pre-OATT Converted Service plus
12 Pre-OATT CCR Service, less any FTRs allocated in Tiers I and II for Network
13 Integration Transmission Service and Pre-OATT Converted Service and less the CFTRs
14 nominated in Tier I for Pre-OATT CCR Service. Market Participants will also be able to
15 nominate up to seventy five percent (75%) of the reservation MW quantity for each
16 annual or longer term Firm Point-to-Point Transmission Service less any FTR granted in
17 Tiers I and II for the Firm Point-to-Point Transmission Service. Tier III will include eight
18 independent nominations: one for each of four seasons and two time periods (peak and
19 off-peak). Any Pre-OATT CCR Service CFTRs over the Tier II limit reduces the amount
20 that a Market Participant can nominate in Tier III. An SFT will be performed for each
21 season and time period for Tier III CFTRs and CFTRs will be reduced in each season and
22 time period as required to achieve simultaneous feasibility. Previously allocated Tier I
23 and Tier II FTRs will be fixed (not subject to reduction) in the Tier III process.

1 **Tier IV Allocation and Nomination Procedures.** Market Participants will be eligible to
2 nominate CFTRs up to the maximum of zero and the quantity given by one hundred
3 percent (100%) of the sum of their forecast Network Integration Transmission Service
4 peak load for the upcoming Allocation Period plus Pre-OATT Converted Service plus
5 Pre-OATT CCR Service, less any FTRs allocated in Tiers I, II, and III for Network
6 Integration Transmission Service and Pre-OATT Converted Service and less the CFTRs
7 nominated in Tier I for Pre-OATT CCR Service. Market Participants will also be able to
8 nominate up to one hundred percent (100%) of the reservation MW quantity for each
9 annual or longer term Firm Point-to-Point Transmission Service less any FTRs granted in
10 Tiers I, II, and III for the Firm Point-to-Point Transmission Service. Tier IV will include
11 eight independent nominations: one for each of four seasons and two time periods (peak
12 and off-peak). Any Pre-OATT CCR Service CFTRs over the Tier III limit will reduce
13 the amount of CFTRs that a Market Participant can nominate in Tier IV. An SFT will be
14 performed for each season and time period for Tier IV CFTRs and CFTRs will be
15 reduced in each season and time period as required to achieve simultaneous feasibility.
16 Any FTRs previously allocated in Tier I, Tier II and Tier III will be fixed (not subject to
17 reduction) in the Tier IV process.

18 During a transition period, CFTRs that are prorated in Tier II and that qualify as
19 “Eligible Base CFTRs,” as defined below, may be restored in full or in part to the
20 nominated MW quantity. After the transition period, the nomination and allocation
21 process will continue as described above, but without restoration of prorated Eligible
22 Base CFTRs. The transition period will be three years, unless the OMS requests and
23 FERC approves an extension.

1 Market Participants that are allocated an FTR in Tier II that is less than the nominated
2 CFTR MW quantity may request that the FTR be restored to the full nominated CFTR
3 MW quantity. Such requests will be granted under the following conditions:

4 If the CFTR meets the definition of an “Eligible Base CFTR,” the FTR will be
5 restored to the extent feasible by adding one or more “Counter Flow” CFTR(s) to the
6 SFT. Counter Flow CFTRS are Eligible Base CFTRs that were not nominated in Tier I
7 or Tier II by the Market Participant owner (or that were nominated but not allocated), but
8 that would provide counter flow necessary to enable an Eligible Base CFTR prorated in
9 Tier II to be restored in full or in part. Counter Flow FTRs will be added to maximize a
10 measure of the amount of prorated Eligible Base FTRs that can be restored. Where
11 multiple Counter Flow CFTRs could provide the required level of counter flow for
12 restoration of the prorated Eligible Base CFTRs, Counter Flow FTRs will be selected so
13 as to minimize a measure of the amount of Counter Flow FTRs added to satisfy the
14 Simultaneous Feasibility Test.

15 Counter Flow FTRs will be allocated directly to the Market Participant that has the
16 transmission entitlement that is the basis of the Eligible Base CFTR. Counter Flow FTRs
17 will be subject to the same settlement terms and conditions as other allocated FTRs,
18 except when the FTR source is unavailable due to scheduled maintenance.

19 Eligible Base CFTRs are CFTRs from designated Network Resources with average
20 historical capacity factors equal to or greater than 70% and CFTRs for Firm Point-to-
21 Point Transmission Service entitlements with historic scheduling factors equal to or
22 greater than 70%.

23

1 **Q. WHAT ARE THE ADVANTAGES OF THIS METHODOLOGY?**

2 A. The methodology balances two competing objectives. It gives Market Participants
3 flexibility in deciding which Candidate FTRs they wish to nominate based on their
4 existing entitlements. Market Participants will be able to take into account their forecasts
5 of Energy Market prices to determine which FTRs would have the greatest value, which
6 might have negative value and what set best helps them manage risks. A Market
7 Participant would be free to nominate the Candidate FTRs that it believes to be more
8 valuable in the earlier tiers, to nominate the less valuable Candidate FTRs in later tiers,
9 and not to nominate FTRs it estimates will have negative expected value. Since we
10 allocate FTRs that satisfy the SFT in each tier, the available transmission capacity will be
11 greatest in the first tier, which would increase the likelihood that Midwest ISO will be
12 able to allocate FTRs nominated in the first tier with less curtailment than in later tiers.
13 This would tend to use available transmission capacity for FTRs that Market Participants
14 value the most highly.

15 The methodology also takes into account that some existing entitlements to
16 transmission service may only be feasible because of counterflows created by uses of the
17 transmission system by others. Suppose a Market Participant nominates a Candidate
18 FTR based on an existing entitlement that the Market Participant has scheduled at over
19 70% scheduling factor historically and indicates that it values this FTR highly by
20 nominating the FTR in Tier I and Tier II. If that Candidate FTR is prorated by the end of
21 Tier II, the Midwest ISO will determine whether there were any existing entitlements
22 with high scheduling factors that historically provided counterflows that would have
23 made the Candidate FTR feasible if those taking the transmission service that would have

1 provided the counterflows had nominated Candidate FTRs but did not do so. The
2 allocation procedure would require those Market Participants to accept Counter Flow
3 FTRs based on their historical usage to restore the prorated Candidate FTR. So, the
4 methodology has provisions to include counterflows that could increase the allocation of
5 FTRs based on historical usage of the system. This would tend to increase the allocation
6 of FTRs for existing entitlements that were historically highly utilized in serving Native
7 Load.

8 The methodology also has provisions to enable Market Participants with Pre-OATT
9 Contracts to continue scheduling under those contracts and avoid paying Day-Ahead
10 Congestion costs.

11 **Q. DOES THE MIDWEST ISO RECOGNIZE ANY POTENTIAL**
12 **DISADVANTAGES OF THIS METHODOLOGY?**

13 A. The above process may not be able to restore an Eligible Base FTR that is prorated in
14 Tier II if there are not Eligible Base CFTRs that could provide counterflows to restore the
15 prorated FTR. If the prorated CFTR does not meet the definition of an “Eligible Base
16 CFTR”, or if the CFTR was prorated in Tiers III or IV, the FTR would also not be
17 restored by the above process. Some stakeholders expressed an interest in being able to
18 restore such prorated FTRs and uplift any resulting shortfall in congestion charges
19 collected as compared to reducing congestion rents to be paid the FTRs.

20 **Q. IS THE MIDWEST ISO PROPOSING ANY STEPS TO MITIGATE THESE**
21 **POTENTIAL DISADVANTAGES?**

22 A. If the prorated CFTR cannot be restored because there are insufficient counterflow FTRs,
23 if it does not meet the definition of an “Eligible Base CFTR”, or if the CFTR was

1 prorated in Tiers III or IV, the FTR will be restored if requested by a State Regulatory
2 Commission. Such requests will be granted if accompanied by instructions as to how the
3 required Counter Flow FTRs, or their costs, are to be allocated among State jurisdictional
4 Market Participants. This alternative process will be available at the discretion of each
5 State Regulatory Commission, and is not subject to a transition period.

6 **Q. PLEASE DESCRIBE THE FACTORS THAT THE MIDWEST ISO BALANCED**
7 **IN DECIDING TO IMPLEMENT THIS OPTION?**

8 A. Midwest ISO sought to balance a number of factors. These included:

9 - providing flexibility in the nomination process so that Market Participants could
10 request the FTRs that they deemed most valuable and better manage risk associated with
11 congestion and holding Obligation FTRs;

12 - treating all firm transmission service equally in the nomination and allocation
13 process;

14 - ensuring that Candidate FTRs would be nominated for transmission service
15 entitlements that were highly used historically and which provided counterflows that
16 made other highly used transmission service feasible;

17 - providing a tiered allocation methodology that would allow Market Participants
18 to increase the chances of receiving highly valued FTRs by nominating them in early tiers
19 when more transmission capacity is available; and

20 - minimizing uplift or the need to reduce payments to holders of FTRs by
21 allocating a set of FTRs that are simultaneously feasible.

22 We also sought to balance the ability of Market Participants with Pre-OATT GFAs to
23 schedule under their GFAs without incurring congestion costs, the Midwest ISO's ability

1 to allocate FTRs to OATT service, and any need for uplift that might result from not
2 charging congestion costs to the Pre-OATT contracts.

3 **Q. WILL THE FTR ALLOCATION METHODOLOGY ENSURE THAT EXISTING**
4 **CUSTOMERS, INCLUDING TRANSMISSION OWNERS WITH A SERVICE**
5 **OBLIGATION FOR BUNDLED RETAIL LOAD, HAVE THE OPPORTUNITY**
6 **TO OBTAIN FTRS THAT ARE EQUIVALENT TO THAT CUSTOMER'S**
7 **EXISTING FIRM RIGHTS?**

8 A. Comparing a physical firm transmission right with a financial right such as an FTR is
9 difficult. The physical right produces value when it is physically scheduled or if the
10 owner can find a buyer to purchase the right. If it is not scheduled or sold, the owner of
11 the right receives no revenue. Also, the holder of a physical right may experience some
12 costs due to TLRs. An FTR is a financial right that derives its value from the difference
13 in LMPs in the Day-Ahead Energy Market. The owner of the FTR will receive a
14 payment based on the difference in LMPs at the sink and source whether that Market
15 Participant schedules a physical flow corresponding to the right or not. Consequently, a
16 Market Participant does not have to hold FTRs equal to 100% of its firm transmission
17 entitlements to effectively hedge congestion charges that result from its schedules in the
18 Day-Ahead Energy Market over a period such as a year.

19 The allocation methodology proposed in the Tariff gives Market Participants the
20 opportunity to nominate the FTRs that they would value the most highly in the early tiers
21 when the most unallocated transmission capacity should be available. Also, the
22 methodology has a restoration step in which Market Participants can request that
23 Midwest ISO restore Candidate FTRs that were prorated at the end of Tier II if the

1 prorated CFTRs were for historically highly utilized transmission service. Consequently,
2 the proposed methodology should afford Market Participants the opportunity to receive
3 FTRs that effectively hedge their congestion costs. It also increases the likelihood that a
4 Market Participant serving Native Load will be able to receive FTRs that cover its base
5 Load.

6 **Q. WHY IS THE MIDWEST ISO NOT SIMPLY ADOPTING THE**
7 **RECOMMENDATION OF THE MARKETS SUBCOMMITTEE REGARDING**
8 **FTRS?**

9 A. On December 18, 2003, the Market Subcommittee had a vote in which the Cinergy
10 proposal was narrowly supported. The vote was very close to tied and so the Midwest
11 ISO did not consider it a clear mandate to implement that methodology. The OMS also
12 indicated a desire for the Midwest ISO to continue working to develop a compromise
13 solution, and has been working toward such a compromise methodology.

14 The Midwest ISO believes that the methodology proposed above balances the
15 competing desires of the various Market Participants in a reasonable fashion. It takes
16 elements proposed by Market Participants from different areas and with different
17 structures as well as those proposed by OMS to craft a methodology.

18
19 **VI. ROLE OF THE OMS IN FTR DISTRIBUTION**

20 **Q. WHY DOES THE MIDWEST ISO BELIEVE THAT THE OMS HAS A ROLE IN**
21 **THE INITIAL DISTRIBUTION OF FTRS?**

22 A. The Midwest ISO recognizes that FERC has indicated that States should play a role in
23 key market issues related to FTR distribution. FERC has indicated that regional
24 authorities are to play a role in crafting an approach to allocating FTRs that seeks to have

1 each existing firm customer receive FTRs equivalent to the customer's existing firm
2 rights. The regional authorities are also to play a key role in deciding whether any
3 revenue shortfalls would be recovered through an uplift charge that applies to all
4 customers in the region or over narrower class of customers, e.g., only to customers in
5 certain zones within the region. The treatment of these issues is central to formulating
6 any FTR allocation methodology. The OMS is the organization of regional regulatory
7 agencies that should play a role in making these decisions.

8 **Q. WHEN THE OMS DEVELOPES A SPECIFIC POSITION ON FTRS, WILL**
9 **THERE BE AN OPPORTUNITY TO MODIFY THE PROPOSED FTR**
10 **PROVISIONS?**

11 A. The OMS completed development of OMS RAWG Principles for FTR Allocations, a
12 Work Plan and timeline during March of 2005. As the OMS' position on FTR allocation
13 continues to be developed, the Midwest ISO plans to work with its stakeholders to make
14 any appropriate filings with the Commission.

15 **Q. WHY IS IT ESSENTIAL THAT THE MIDWEST ISO PROPOSE A SPECIFIC**
16 **FTR DISTRIBUTION PROGRAM TO FERC ON MARCH 31, 2004 RATHER**
17 **THAN DELAY RESOLUTION OF THIS ISSUE?**

18 A. Implementing any FTR allocation program will require the development of numerous
19 procedures and processes. These include:

20 - systems to prorate nominated FTRs if necessary or add Counter Flow FTRs to
21 satisfy an SFT;

22 - procedures for registration of existing entitlements;

23 - procedures for collecting and systems to analyze data regarding historical usage

1 of the existing entitlements;

2 - procedures to allow Market Participants to nominate Candidate FTRs; and

3 - systems to check whether Candidate FTRs nominated by a Market Participant
4 are consistent with its existing entitlements and satisfy any constraints imposed on the
5 ability to nominate FTRs.

6 The development of these processes, collection of data, and analyses required will
7 take several months. Also, any initial allocation of FTRs must be performed before the
8 start of the Energy Market. Prior to market start on December 1, 2004, the Midwest ISO
9 proposes to perform an initial allocation of FTRs and run an annual auction in which
10 Market Participants will be able to buy and sell FTRs. To run an annual auction that
11 consists of eight separate auctions for peak and off-peak periods in each season and have
12 the results validated prior to December 1, 2004, the Midwest ISO believes that it must
13 start the auction process by October 4, 2004. Prior to commencing the auction, Market
14 Participants must receive their initial allocation of FTRs so that they can evaluate their
15 holdings and decide on any purchases or sales that they would like to make in the
16 auction. The Midwest ISO believes that the initial allocation must be provided to Market
17 Participants by September 30, 2004, to give adequate time to evaluate their positions.
18 Given the complexity of the data collection and analyses efforts required to perform the
19 initial allocation, the Midwest ISO believes that this effort should start in July of 2004.
20 Market Participants must be given time to evaluate their position prior to each tier and to
21 develop Candidate FTRs that they wish to nominate in the tier. The time required is still
22 an open question, but we will assume one week. The Midwest ISO will require time to
23 prepare data, validate data, correct errors, perform the analyses to allocate FTR and

1 publish results. Eight business days is a minimal estimate per tier. The restoration step
2 could add another five business days. The allocation process could easily take two
3 months to complete. That is, we should start the allocation no later than July 15, 2004 to
4 complete the allocation by September 30, 2004. Assuming no major changes to the
5 allocation methodology would be required, a FERC decision would be desirable by June
6 30, 2004. Midwest ISO believes that it is prudent to file the FTR allocation methodology
7 on March 31, 2004 if it is to develop the systems to implement the allocation process and
8 perform the allocations and auctions prior to market start on December 1, 2004.

9 **Q. HOW LONG WILL IT TAKE THE MIDWEST ISO TO IMPLEMENT AN**
10 **INITIAL FTR DISTRIBUTION PROGRAM?**

11 A. It depends upon the procedures adopted. The Midwest ISO is in the process of
12 developing information systems to implement the nomination and allocation process.
13 However, there are steps beyond the development of information systems. We propose
14 to start the process of registering existing transmission service entitlements for which
15 Market Participants may wish to request FTRs in early April of 2004 and complete the
16 registration process in mid June of 2004. Registration of Grandfathered Agreements and
17 resolution of disputes should be complete by July 14, 2004. From July 15, 2004 through
18 the end of September of 2004, the Midwest ISO will run the nomination and allocation
19 process.

1 **Q. WHAT IS THE LATEST DATE FOR A FERC DECISION ON THE INITIAL**
2 **DISTRIBUTION PROCEDURES FOR FTRS TO ENABLE THE MIDWEST ISO**
3 **MARKET TO COMMENCE ON DECEMBER 1, 2004?**

4 A. As described above, Midwest ISO believes it prudent to start the nomination and
5 allocation process no later than July 15, 2004 so that it can complete the allocation and
6 annual FTR auction prior to market start on December 1, 2004. A decision by June 7,
7 2004 would enable the Midwest ISO to meet this start date.

8 **Q. WOULD IT BE FEASIBLE TO IMPLEMENT THE MIDWEST ISO MARKET**
9 **ON DECEMBER 1, 2004 WITHOUT COMPLETING AN INITIAL FTR**
10 **DISTRIBUTION PROGRAM?**

11 A. No. Without an initial FTR distribution, Market Participants would not be able to hedge
12 congestion costs to which they would be exposed in an LMP market when the market
13 commences on December 1, 2004.

14 **VII. ILLUSTRATIVE ALLOCATION OF FTRS**
15

16 **Q. WHY IS THE MIDWEST ISO PREPARING AN ILLUSTRATIVE**
17 **ALLOCATION OF FTRS?**

18 A. FERC requested on February 24, 2003 that the Midwest ISO prepare detailed information
19 on the proposed first year allocation of FTRs, including, at a minimum, each Market
20 Participants' expected allocation of FTRs based upon the proposed tariff allocation
21 method, the Candidate FTRs and any proposed prorata reduction in the Candidate FTRs.

1 ¹FERC clarified on March 28, 2003 that such an illustrative allocation should be filed
2 with the Commission at least 60 days prior to the Midwest ISO's final EMT filing.²

3 **Q. WHAT PERIOD IS COVERED BY THE ILLUSTRATIVE ALLOCATION?**

4 A. The illustrative allocation is being done for estimated peak period in July 2004.

5 **Q. WHAT PROCEDURES ARE THE MIDWEST ISO FOLLOWING TO PREPARE**
6 **THE ILLUSTRATIVE ALLOCATION?**

7 A. Several draft illustrative allocations have been produced using different methods. The
8 process of developing the illustrative allocation that will be filed began in December
9 2003.

10 **Q. IS THE MIDWEST ISO DEVELOPING THE ILLUSTRATIVE ALLOCATION**
11 **OF FTRS USING THE PROCEDURE YOU DESCRIBED ABOVE?**

12 A. The Midwest ISO is using a procedure roughly based on the allocation procedure that is
13 in the Tariff and which is described above. We are not able to precisely follow the
14 procedure that will be used in the actual allocation since the systems to implement the
15 allocation procedure are still being developed. In particular, the Midwest ISO does not
16 yet have the systems required to perform the proposed restoration step between Tiers I
17 and II.

¹ *See Midwest Independent Transmission System Operator, Inc., 102 FERC ¶61,196 at P68 (2003).*

² *See Midwest Independent Transmission System Operator, Inc., 102 FERC ¶61,338 (2003).*

1 **Q. HOW IS THE MIDWEST ISO TREATING ITS INABILITY TO IMPLEMENT**
2 **THE RESTORATION STEP IN PRODUCING THE ILLUSTRATIVE**
3 **ALLOCATION?**

4 A. For the illustrative allocation, we are modifying the proposed allocation methodology.
5 Since we cannot perform the restoration step yet, the Midwest ISO is manually
6 developing the Tier I and II nominations so that they include CFTRs for some
7 transmission entitlements that were highly utilized historically. Consequently, we plan to
8 include CFTRs for some of the Eligible Base CFTRs that provide counterflows that other
9 Eligible Base CFTRs require to be feasible. The goal is to provide stakeholders with an
10 indication of the effect that the addition of Counter Flow CFTRs in the Restoration Step
11 would have on the allocation in practice. We will allow stakeholders to submit
12 nominations for CFTRs in Tiers III and IV only in the process of creating illustrative
13 FTRs.

14 **Q. HOW ARE YOU DEVELOPING THE TIER I AND II NOMINATIONS?**

15 A. We are assuming that the Grandfathered Agreement Responsible Entity for each
16 Grandfathered Agreement would elect to retain the GFA and would elect to have the
17 GFA treated as Pre-OATT Congestion Cost Refund Service in the allocation.
18 Consequently, we plan to include a CFTR for each GFA in Tier I for the associated
19 Market Participant in the development of Illustrative FTRs Any FTRs allocated to these
20 CFTRs will be held by the Midwest ISO to help offset the cost of refunding congestion
21 charges from scheduling transactions under these GFAs in the Day-Ahead Energy
22 Market.

23 For Firm Point-to-Point Transmission Service entitlements, we will assume that the

1 Market Participant will nominate up to the limit in each tier (35% of the MW level of the
2 entitlement in Tier I and 50% of the MW level of the entitlement less FTR allocated in
3 Tier I for Tier II).

4 For Network Integration Transmission Service, we will nominate CFTRs from the
5 designated Network Resources roughly in order of their capacity factors up to the tier
6 limits for Tiers I and II. Some adjustments will be made to ensure that CFTRs less than
7 0.1 MW are not nominated.

8 **Q. WHAT PROCEDURES IS THE MIDWEST ISO FOLLOWING TO PREPARE**
9 **THESE ILLUSTRATIVE ALLOCATIONS?**

10 A. The Illustrative FTRs are being created using the information that was the best available
11 at the time that the process was commenced.

12 One of the first steps is developing a Network Model of the transmission system in the
13 Midwest ISO Region and neighboring areas. The FTR Network Model is derived from
14 the Midwest ISO Energy Management System Network Model that is used for the
15 Reliability Coordination of the transmission system. Since the FTR model is expected to
16 represent the network for a period in the future, known future network changes and
17 upgrades are incorporated in the Network Model. The required changes were assembled
18 through a collaborative effort between Midwest ISO and the stakeholders. Other
19 important data related to the Network Model include (1) flowgate data, (2) equipment
20 ratings in normal and outage conditions, (3) contingency data, (4) planned outages.

21 In addition to the network data, the FTR allocation requires commercial model data.
22 This includes the registration of generator ownership and location and definition of load
23 zones for Load Serving Entities. This provides the definition of the Commercial Pricing

1 Nodes that can be selected as the sources and sinks for the FTRs. The commercial model
2 must be in sync with the Network Model used. That is, the elemental pricing nodes
3 defined in the commercial model (generator buses, load buses, etc. that make up the
4 Commercial Pricing nodes) must be defined in the Network Model. In order to perform
5 effective market systems integration and carefully check out the various market
6 applications and interfaces, the market integration team believed that it was important to
7 work with a stable and robust Network Model. It was therefore decided in early
8 September 2003 to freeze the Network Model that was available at the end of September
9 2003 and to use this Network Model information to populate the various market
10 application databases. This decision also called for the FTR application to run on the
11 same September 2003 Network Model during the integration testing. Consequently, we
12 used the September 2003 Network Model and the corresponding commercial model in
13 setting up the illustrative allocation of FTRs

14 In addition to the Network Model and the commercial models, we collected
15 information on existing OATT Transmission Service that would be able to request FTRs.
16 We collected information on existing transmission entitlements of annual duration or
17 longer that would be in effect during July 2004 from the Midwest ISO's OASIS and
18 mapped the sources and sinks for these entitlements to the Commercial Pricing nodes of
19 the commercial model. We also collected forecasts of peak Network Integration
20 Transmission Service Loads for July 2004 and collected information on the designated
21 Network Resources that would be used to serve them.

22 We collected information on Grandfathered Agreements and for each GFA we
23 assigned a Market Participant who was party to the agreement to be the Responsible

1 Entity. For the purposes of the illustrative allocation, we assumed that the Responsible
2 Entity would elect to retain the GFA and elect to have the GFA treated as Pre-OATT
3 Congestion Cost Refund Service in the allocation.

4 Finally, we developed estimates of loopflows that would result from external
5 transactions. These estimates are based on forecasts of external Control Area Loads and
6 transmission reservations between external Control Areas.

7 Because this is an evolutionary process, constant updates and improvements to much
8 of this data has been occurring as these models are enhanced and improved. However,
9 we had to freeze the models and data as described above in order to develop the
10 illustrative allocation.

11 **Q. HOW WAS NECESSARY INFORMATION COLLECTED FROM MEMBERS**
12 **DURING THE FTR STAKEHOLDER PROCESS?**

13 A. The Midwest ISO has implemented an ongoing Network Model update process to capture
14 the transmission system changes. A web-based tool has been developed and implemented
15 and the Midwest ISO Transmission Owners are using this tool to submit their
16 transmission system changes to the Midwest ISO.

17 The Midwest ISO developed lists of transmission entitlements that were collected
18 from OASIS as well as Network Integration Transmission Service Load and designated
19 Network Resources that could be used to serve the Load for the Load Serving Entities.
20 These were sent to participants for their review and correction in December and January.
21 At that time, we also requested that stakeholders supply capacity factors for their
22 generators and scheduling factors for their transmission service entitlements.

1 **Q. DID THE MIDWEST ISO FACE ANY IMPEDIMENTS TO COLLECTING THE**
2 **NECESSARY INFORMATION?**

3 A. Yes. The Midwest ISO stakeholders did not uniformly provide the requested data to the
4 Midwest ISO in a timely manner. In addition, some of the data was provided in different
5 formats than requested.

6 **Q. DID THESE IMPEDIMENTS CAUSE ANY DELAYS IN THE PROCESS?**

7 A. Yes. Development of Illustrative FTRs has been delayed by several factors. We
8 experienced delays in receiving requested data from some participants. Also, early runs
9 of the allocation methodology uncovered some problems with modeling of resources in
10 some areas and problems in the definition of some entitlements. They also uncovered
11 some required changes to the contingency set used in the allocation. For example, some
12 contingencies that were included should have been excluded since they were treated
13 through operating guides. Working to resolve these problems takes time. Also, while we
14 were working to collect data to produce an illustrative allocation, the development of the
15 allocation methodology continued through February of 2004 and into March of 2004.
16 Changes to the methodology affected Midwest ISO's ability to produce an allocation that
17 exactly follows the proposed methodology.

18 **Q. HOW WERE THE MIDWEST ISO AND ITS STAKEHOLDERS ABLE TO**
19 **HANDLE THESE DELAYS?**

20 A. The Midwest ISO had planned to be able to distribute Illustrative FTRs to the
21 stakeholders in early March of 2004. However, in an effort to prepare more
22 representative Illustrative FTRs (recognizing all of the limitations previously discussed),
23 the Midwest ISO will be sharing Illustrative FTR allocations with its stakeholders

1 beginning on April 21, 2004 and expects to file them with FERC as an amendment to the
2 subject filing on April 23, 2004.

3 **Q. HOW REALISTIC WILL THE ILLUSTRATIVE FTRS BE?**

4 A. Although the Illustrative FTRs will provide some assistance to the stakeholders in
5 understanding actual FTR distributions, several important caveats should be considered:
6 (1) the Illustrative FTRs are in no way binding – they are for illustration only; (2) the
7 Illustrative FTRs are based on the peak period in July 2004; the actual FTRs will be
8 based upon a different period (December 2004 through November 2005) and will be for
9 peak and off-peak for each of the four seasons; (3) the actual FTR distributions will be
10 based upon the May 2004 Network Model, not the September 2003 Network Model
11 which necessarily formed the basis for the Illustrative FTRs; (4) the Illustrative FTRs are
12 necessarily based upon manual, rather than automated procedures (the automated process
13 is expected to be completed in April of 2004); (5) the Illustrative FTRs are based on a
14 combination of the Midwest ISO's best estimate as to how the Market Participants might
15 nominate for Tiers I and II and the impact of the Restoration Step (Market Participants
16 will only be nominating Tiers III and IV), whereas the actual FTR distribution will be
17 based upon Market Participants making nominations in all four tiers with a Restoration
18 Step after Tier II; and (6) there is no way predicting whether Market Participants will
19 actually nominate even Tiers III and IV during the actual process the same way that they
20 will nominate during the Illustrative FTR nomination procedures.

1 **Q. IF THE ILLUSTRATIVE ALLOCATION IS NOT ACCURATELY PREDICTIVE**
2 **OF HOW FTRS WILL ACTUALLY BE DISTRIBUTED, OF WHAT VALUE IS**
3 **THE ILLUSTRATIVE ALLOCATION?**

4 A. The Illustrative FTRs provide stakeholders with additional information as to how the
5 FTR allocation process may occur. This can be valuable in enabling them to better
6 understand the overall process.

7 **Q. SHOULD PARTIES DRAW ANY IMPORTANT CONCLUSIONS FROM THE**
8 **ILLUSTRATIVE ALLOCATIONS?**

9 A. It would be inappropriate for Market Participants to reach any firm conclusions on how
10 the actual FTRs will be distributed during the process that will commence in July of 2004
11 based upon the Illustrative FTRs, for the reasons that are described above. The
12 Illustrative FTRs do provide all parties, however, with a better understanding of the
13 process that will be employed, even if the actual results do not reflect what will occur this
14 summer.

15 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

16 A. Yes, it does.

17 **Q. DO YOU ATTEST THAT THE FOREGOING TESTIMONY IS TRUE AND**
18 **CORRECT TO THE BEST OF YOUR KNOWLEDGE?**

19 A. Yes.