

**ILLINOIS COMMERCE COMMISSION
DOCKET NOS. 05-0160, 05-0161 and
05-0162 (consolidated)**

REBUTTAL TESTIMONY

OF

DR. CHANTALE LACASSE

**Submitted On Behalf
Of**

**Central Illinois Light Company d/b/a AmerenCILCO,
Central Illinois Public Service Company d/b/a Ameren CIPS,
and Illinois Power Company d/b/a AmerenIP**

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25 First, I conclude that the proposed Auction Process remains the best
26 method of procuring supply for Ameren’s customers in the post-2006 period. In
27 support of that conclusion, I review the overwhelming evidence from Staff and
28 intervenors in support of Ameren’s Auction Process. In addition, I respond to the
29 testimony of witnesses on behalf of the Citizens Utility Board (“CUB”) and the
30 People of the State of Illinois (“AG”) who recommend that the Commission reject
31 Ameren’s proposed Auction Process. I explain why the recommendations of
32 these witnesses are based on incorrect assumptions and flawed logic, and should
33 only be expected to lead to worse outcomes for Ameren’s customers.

34 Second, I conclude that the competitive safeguards built into Ameren’s
35 Auction Process, as they have evolved to incorporate the input of Staff and
36 intervenors, are sufficient to assure a competitive bidding environment. I
37 consider the alternative competitive safeguards proposed by Staff and intervenors
38 – measures that appear to be aimed at mitigating market power in the wholesale
39 market rather than assuring competition in the auction – and explain why these
40 alternative proposals should be rejected. I summarize how the competitive
41 safeguards (the load cap, the volume reduction guidelines, and the Association
42 and Confidential Information Rules) provide reasonable protections against anti-
43 competitive behavior so that the Auction Process can deliver reliable supply at
44 competitive market prices.

45 Third, I conclude that there are both costs and benefits to allowing bidders
46 to switch among products within the auction and that a careful analysis of the
47 balance of these costs and benefits is needed. I assess the proposal of Staff

48 witness Salant to permit switching across all products in the Illinois Auction. I
49 explain why the hourly-price products are sufficiently different from the fixed-
50 price products in the Illinois Auction to make switching between hourly-price
51 products and fixed-price products, in my opinion, undesirable. Similarly, I
52 provide my opinion on Ameren's revised proposal both to permit switching
53 between the fixed-price products of ComEd and the fixed-price products of
54 Ameren and to permit switching between the hourly-price products of ComEd and
55 the hourly-price products of Ameren.

56 Fourth, I conclude that the Ameren proposal is complete and contains the
57 details necessary for the Commission to make a ruling in this proceeding. I
58 respond to the positions taken by Staff witness Salant on the completeness of the
59 auction proposal, the mechanics of auction management, and the roles of the
60 parties involved. I recommend a measured approach to auction management,
61 which I believe will maximize the probability of a successful auction.

62 **Q. How is your rebuttal testimony structured?**

63 A. I present each of my four conclusions in turn. Section 2 addresses why the
64 proposed Auction Process remains the best method of procuring supply for
65 Ameren's customers. Section 3 addresses competitive safeguards. Section 4
66 addresses the costs and benefits of allowing switching across the various products
67 in the Illinois auction and explains and introduces material that provides added
68 detail concerning the Illinois auction proposal such as application forms. Section
69 5 addresses the completeness of the Ameren proposal and the mechanics of
70 auction management.

71 **2. The Proposed Auction Process Is the Best Method of Procuring Supply for**
72 **Ameren Customers**

73

74 **Q. What is the purpose of this section of your rebuttal testimony?**

75 A. In this section of my rebuttal testimony, I will:

76 ▪ Summarize the positions of Staff and intervenors with respect to the basic
77 design of Ameren’s Auction Process, highlighting those aspects that are
78 supportive of Ameren’s proposed Auction Process and identifying areas
79 where the testimony is less supportive.

80 ▪ Respond to the testimony of witnesses for CUB and the AG who recommend
81 that the Commission reject Ameren’s proposed Auction Process. In so doing,
82 I establish why the proposed Auction Process remains the best method of
83 procuring supply for Ameren’s customers.

84 **Q. I plan to ask you a series of questions asking you to identify areas where the**
85 **testimony of Staff and intervenors is supportive of Ameren’s proposed**
86 **Auction Process and to identify areas where such testimony may be less**
87 **supportive. To provide some foundation for this line of questioning, can you**
88 **briefly describe Ameren’s proposed Auction Process?**

89 A. Yes. I can best structure my description of the Auction Process by referring to the
90 eight key elements of an Auction Process developed in my direct testimony.

91 1. **Product design.** The product design fully describes what is being
92 procured at the auction. Ameren is proposing to procure full-
93 requirements supply for three categories of its customers.

94 • The first category of customers consists of residential and small
95 business (“R&SB”) customers under 1 MW of demand. These
96 customers are on a fixed-price service. For this category, which is
97 called BGS-FP, Ameren is procuring supply for 17-month, 29-
98 month, and 41-month terms beginning January 1, 2007.

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- The second category of customers consists of large commercial and industrial (“LC&I”) customers (1 MW or above) affirmatively electing a fixed price service for one year. For this category, which is called BGS-LFP, Ameren is procuring supply for a 17-month term beginning January 1, 2007.
 - The third category of customers, who are on a service priced to the hourly market, consists of LC&I customers that have not elected a fixed price service. For this category, which is called BGS-LRTP, Ameren will be procuring supply for a 17-month term beginning January 1, 2007.
2. **Auction format.** The auction format is the way in which bids are solicited and processed, the way a clearing price is determined and the way in which winners emerge. Ameren is proposing that a clock auction be used. The clock auction is an open auction format, in which bidders get dynamic information feedback through a multiple round process. In a round, the Auction Manager suggests prices for each product, and the bidders state the quantity they want to serve of each product at these prices. (A product is a load category for a given term, e.g., serving the load of BGS-FP customers for a term of 17 months). If the supply for a product exceeds the quantity needed, the price for the product ticks down for the next round. The Auction Manager announces the new prices for the next round and a measure of excess supply left in the auction. Bidders submit new bids in the next round and the process continues until the supply equals the load to be procured.
 3. **Bidder interface.** The bidder interface is the way in which bidders are provided with information about the Auction Process, the way in which data are disseminated and the way in which the auction opportunity is promoted. Ameren has proposed to engage an Auction Manager that will serve as the point of contact for bidders. Information, including data that bidders will require to prepare their

130 bids, will be disseminated through a dedicated web side. The Auction
131 Manager will answer bidder questions and provide training in the
132 auction rules and the bidding procedures. The Auction Manager will
133 assist in promoting the auction, for example by holding bidder
134 information sessions. The Auction Manager will manage the
135 qualification procedure and the bidding during the auction itself.

136 4. **Qualification requirements.** These are the requirements for
137 qualifying bidders to participate in the auction. Ameren proposes that
138 the application process be in two parts. In the Part 1 Application,
139 applicants are required to certify that they are MISO Market
140 Participants, as required by the applicable Supplier Forward
141 Contract(s). Further, in the Part 1 Application, applicants agree to the
142 terms of the applicable Supplier Forward Contract(s) and the auction
143 rules, and applicants submit financial information for a
144 creditworthiness evaluation. In the Part 2 Application, applicants that
145 have qualified under Part 1 submit an indicative offer and financial
146 guarantees to support this indicative offer. Applicants also make a
147 number of certifications regarding associations and the handling of
148 confidential information. The details of these requirements are
149 embodied in Resp. Exs. 12.1 and 12.2, which are draft application
150 forms.

151 5. **Rate Design.** The rate design parameters specify how the auction
152 results will be translated into retail rates. Ameren proposes to establish
153 four rate classes: Class 1 for residential customers; Class 2 for
154 business, commercial and industrial customers below 150 kW; Class 3
155 for business, commercial and industrial customers above 150 kW but
156 below 1 MW; and Class 4 for LC&I customers 1 MW or over. For
157 each rate class, there will be a tariff for customers taking fixed-pricing
158 service and a tariff for customers taking real-time pricing service. Each
159 fixed-pricing tariff rate will be established using conversion factors
160 that translate auction prices into retail rates. The conversion factors

161 will be calculated on the basis of a comparison between the system
 162 cost and the cost of individual customer classes. The real-time pricing
 163 tariff consists of a fixed charge determined at the auction and energy
 164 costs priced at the local hourly spot market.

165 6. **Competitive safeguards.** Competitive safeguards are features of the
 166 Auction Process that limit the scope for anti-competitive behavior in
 167 the auction, with the view to maximizing the competitiveness of the
 168 bidding environment. I review these competitive safeguards in detail
 169 in Section 3 of this rebuttal testimony, elaborating on data requests
 170 submitted by intervenors in this proceeding, and responding to
 171 alternative competitive safeguards that have been proposed in
 172 testimony. Briefly, the Illinois Auction Proposal includes three main
 173 competitive safeguards. The first is the ability for the Auction
 174 Manager to cut back the volume purchased through the auction if this
 175 is necessary to ensure a competitive bidding environment. Any volume
 176 cut back from the auction would be procured through MISO-
 177 administered markets. The second is a load cap, which limits the
 178 influence that any one bidder can have on the results of the auction.
 179 The third is a set of detailed Association and Confidential Information
 180 Rules, which are managed through the application process. These rules
 181 limit the possibility of collusive behavior, and ensure a level playing
 182 field by limiting the possibility that a bidder will have better
 183 information than another about its competitors.

184 7. **Regulatory Involvement.** This element describes the role played by
 185 the regulator and other parties in the process. My understanding is that
 186 Ameren will want the ICC Staff, with the assistance of their Auction
 187 Advisor, to be continuously informed and involved during the process.
 188 ICC Staff will participate in setting the detailed practical procedures to
 189 run the Auction Process, will monitor promotion efforts and will
 190 monitor the qualification of bidders. During the auction itself, ICC
 191 Staff, with the assistance of their Auction Advisor, will monitor the

192 bidding and evaluate the results. Other stakeholders will be informed
193 of the progress of the Auction Process through postings to the auction
194 web site and through meetings with the Auction Manager as
195 appropriate. Ameren also proposes a post-Auction Process structured
196 to provide an open forum for the continued improvement of the
197 competitive procurement rules and methods.

198 8. **Cost recovery assurances.** This element is a description of the
199 assurances sought from the regulators with respect to cost recovery for
200 supply procured to serve Ameren customers. My understanding is that
201 Ameren is asking the ICC to consider at this time the elements of the
202 Auction Process, and Ameren is asking the ICC to deem the
203 acquisition of supply through the auction to be prudent as long as the
204 ICC concludes that no grounds exist for the ICC to initiate an
205 investigation on its own motion under Section 9-250 or other
206 applicable provisions of the Public Utilities Act.

207 **Q. Are witnesses in this proceeding supportive of these elements, and of the**
208 **Auction Process as generally structured, and believe that it is the best**
209 **method for procuring supply for Ameren customers?**

210 A. Generally, yes. I have reviewed the testimony of other witnesses in this case. I
211 find that many witnesses strongly support the Auction Process as proposed by
212 Ameren.

213 Witnesses who participated in the workshop process organized by the ICC
214 rightly point out that Ameren has put forth the procurement method that best
215 meets the attributes of a procurement process that participants collectively
216 determined were desirable. Witness Smith from Constellation Energy
217 Commodities Group, Inc. (“CCG”) is particularly clear in articulating this view:

218 Q. DOES CCG SUPPORT THE OVERALL ILLINOIS AUCTION
219 STRUCTURE AS PROPOSED BY AMEREN?

220 A. Yes. CCG believes that the CPA proposed by Ameren incorporates
221 the serious and thoughtful consideration provided by numerous
222 stakeholders with differing interests during the Procurement
223 Working Group discussions. The Procurement Working Group last
224 summer developed a list of 18 attributes of a successful
225 procurement model and, of all the different structures considered,
226 the Procurement Working Group determined that the CPA best
227 meets those attributes. CCG agrees with that determination.
228 Through this proposed mechanism, Ameren will be able to bring
229 the benefits of competition to those customers who do not or
230 cannot obtain their service from an Alternative Retail Electric
231 Supplier (“ARES”). CCG Exhibit 1.0 p. 2 lines 60-61, p. 3 lines
232 62-70.

233 Similarly, witness O’Connor for the Coalition of Energy Suppliers
234 (“CES”) notes that “The auction approach has a number of specific characteristics
235 that make it a reasonable approach for Illinois at this time.” (CES Exhibit 1.0 p.
236 5, lines 95-96) and Dynegy witness Huddleston states that: “As a general matter,
237 Dynegy supports the Ameren proposal.” (Dynegy Exhibit 1.0, p.6 line 110. A
238 similar statement can be found in the testimony of Direct Energy Services, LLC
239 and U.S Energy Savings Corp. (“DES/USESC”) witness Steffes (DES/USESC
240 Exhibit 1.0 p.12 lines 237-241).

241 **Q. Do these witnesses endorse all elements of the Auction Process just as**
242 **proposed by Ameren?**

243 A. Typically, no, these witnesses do not endorse all elements of the Auction Process
244 exactly as proposed. Instead, these witnesses typically put forth suggestions that
245 they believe would further improve the Auction Process. As one example of such
246 suggestions, witnesses Huddleston on behalf of Dynegy and Smith on behalf of
247 Constellation both comment on particular terms of the Supplier Forward
248 Contracts.

249 **Q. Are other witnesses then opposed to the Auction Process as proposed by**
 250 **Ameren?**

251 A. No, not at all. Several other witnesses, even if they do not provide broad and
 252 explicit statements of support for the Auction Process like the witnesses cited
 253 above, do provide implicit support for the proposal. These witnesses do not
 254 present an alternative and do not suggest that alternative procurement methods
 255 should be considered. Instead, they embrace the Auction Process as a starting
 256 point and propose changes that they believe would further improve the Auction
 257 Process.

258 For example, witness Salant for ICC Staff believes that the selected
 259 auction under proper implementation “is an efficient mechanism for procuring
 260 supply to serve Ameren’s load at the best possible cost” (ICC Staff Exhibit 1.0 p.
 261 6, lines 124-126) and that there is support from both auction theory and practice
 262 for the approach; for example, he states: “[i]n general, the economics literature
 263 and the global experience with the SMR auction format supports Ameren’s
 264 proposal to use the SDCA for electricity procurement.” (ICC Staff Exhibit 1.0 p.
 265 12, lines 280-282). Dr. Salant nevertheless makes a number of suggestions in his
 266 testimony regarding various details of auction design and implementation,
 267 including recommendation regarding competitive safeguards. Witnesses Collins,
 268 Stephens, and Dauphinais on behalf of the Illinois Industrial Energy Consumers
 269 (“IIEC”), witnesses Zuraski, Schlaf, Ogur, Lazare, Harden, Selvaggio, Struck and
 270 Knepler on behalf of ICC Staff, witness Dornbusch on behalf of Dynegy, and

271 witnesses Domagalski, Spilky, Bohorquez, and Bollinger for CES all also in my
272 view implicitly support the Auction Process.

273 **Q. Has Ameren considered the views of others expressed in testimony and the**
274 **changes that others believe will further improve the Auction Process?**

275 A. Yes. Ameren has considered the views expressed in testimony and the proposed
276 changes that others believe would further improve the Auction Process. Ameren is
277 responding to these suggestions in testimony. In several instances, Ameren is
278 agreeing to proposals to modify certain aspects of its Auction Process. The
279 specific modifications are explained in the rebuttal testimony of Mr. Craig
280 Nelson. I review the agreed changes in Sections 3, 4 and 5 of this rebuttal
281 testimony and I explain how these modifications work within the general structure
282 of the Auction Process. I conclude that these agreed changes are consistent with
283 the structure of the Auction Process and that the Auction Process as modified will
284 fulfill its objectives.

285 **Q. You have made the point that, as a rule, intervenors and Staff either**
286 **implicitly or explicitly recognize that in general terms the proposed Auction**
287 **Process is the best procurement method for customers. Are there witnesses**
288 **that are exceptions to this rule?**

289 A. I believe that three witnesses are exceptions to this rule.

290 **Q. What do you understand is the position of each of these witnesses?**

291 A. Mr. Salgo, on behalf of the AG, believes that the Auction Process as proposed
292 should be abandoned. He recommends that Ameren be required to compare the
293 rate impact and risks of its proposal with a variety of other portfolio design and

294 procurement options. (AG Exhibit 2.0, p.23, lines 16-19). Mr. Salgo implies that
295 there is an alternative approach that would be better for consumers. The
296 foundation of this alternative approach is for Ameren to manage the supply
297 portfolio rather than leaving this function in the hands of the competitive market.
298 Mr. Salgo states: “The Company has patterned its proposal on the New Jersey
299 Basic Generation Service (BGS) model and has rejected procurement models that
300 involve active portfolio management” and “the Company should fully consider
301 other approaches, including more active portfolio management, utilization of the
302 many other standard products available in the market, . . . , and the possibility of
303 negotiating prices and other contract terms with suppliers.” (AG Exhibit 2.0 p. 11,
304 lines 8-15).

305 Dr. Rose, also on behalf of AG, believes that the Auction Process should
306 not be used by Ameren at this time because of concerns surrounding the
307 competitiveness of the wholesale market. “Given the current state of the
308 wholesale electricity market in this region and its stage of development, it is
309 premature to use an Auction Process, like the one proposed by Ameren, to
310 procure electricity for retail customers.” (AG Exhibit 1.0 p. 4, lines 12-14).
311 Based on the concentration of generation ownership in the Ameren service area,
312 constraints on entry and the demand characteristics of electricity, Dr. Rose
313 concludes that the lack of competition and maturity in the wholesale market
314 renders an Auction Process premature (AG Exhibit 1.0 p. 16, line 11 to p.17, line
315 7).

316 Dr. Steinhurst, on behalf of CUB, recommends rejection of the proposed
317 Auction Process and recommends that Ameren should “carry out the necessary
318 procurement under traditional ratemaking” (CUB Exhibit 2.0, p. 3, lines 69-70).
319 Dr. Steinhurst also objects to the fundamental approach incorporated into the
320 Auction Process whereby the ICC takes in this proceeding necessary time and
321 attention to review the elements of the Auction Process, to resolve contested
322 issues, and to ensure that the ICC will have the necessary information to proceed
323 to an expeditious decision in response to the auction results. Although the
324 alternative procurement method that Dr. Steinhurst would put forward is not
325 clearly articulated, I believe that Dr. Steinhurst’s position is consistent with the
326 positions of both Mr. Salgo and Dr. Rose. I understand Dr. Steinhurst’s
327 objections to imply that he believes that Ameren should take a more active role in
328 portfolio management. Dr. Steinhurst, referring to the testimony of Mr. Fagan on
329 the competitiveness of the wholesale markets, also objects to a reliance on these
330 markets for the procurement of supplies for customers.

331 **Q. Having considered the testimony of Mr. Salgo and Dr. Steinhurst, are you**
332 **persuaded that having the utility manage a supply portfolio would result in a**
333 **better outcome for customers?**

334 A. No, I am not.

335 At the core of Mr. Salgo’s and Dr. Steinhurst’s recommendation to
336 abandon the Auction Process is a view that Ameren’s proposed full-requirements
337 product design, whereby competitive market forces are harnessed to manage the
338 supply portfolio, will not be beneficial for customers. Mr. Salgo and Dr.

339 Steinhurst prefer the management of the supply portfolio to be in the hands of the
340 utility in a regulated environment. Mr. Salgo's and Dr. Steinhurst's supplemental
341 recommendations and views regarding the method of purchase or regulatory
342 oversight (e.g., use of an RFP or negotiations, prudence review, etc.) all stem and
343 flow from this position on product design.

344 I disagree with the view that customers will benefit if the management of
345 the supply portfolio is in the hands of the utility under ICC oversight rather than
346 in the hands of the competitive market. There is no reason to suspect, let alone
347 believe, that such an alternative would be better for customers. To the extent that
348 a service can be supplied through a competitive option as opposed to regulated
349 means, the competitive alternative can reasonably be presumed to be more
350 efficient and result in better prices in the long run. Considering the portfolio
351 management service, I believe that a competitive option is available, and that this
352 service is particularly ill-suited to regulation when it is the case that a competitive
353 option is available.

354 Experience in the New Jersey BGS Auctions has shown that there is a
355 competitive option for the supply of the portfolio management service. In the
356 New Jersey BGS Auctions, numerous entities are willing and able to compete to
357 provide a full-requirements product. These entities include financial players,
358 energy marketers and traders, as well as entities that own a generation portfolio.
359 These entities are ready to serve a full-requirements product, which necessitates
360 assembling a portfolio of supply in wholesale power markets, assessing various
361 load and market risks, and offering a fixed price for this service. Many of the

362 entities with experience in the New Jersey BGS Auctions, as well as other entities
363 active in Illinois, have participated in the Workshop Process that preceded this
364 proceeding, and have participated in various supplier meetings. A number of
365 entities with experience in the New Jersey BGS auctions are MISO Market
366 Participants. This provides a solid basis to believe that the experience in the New
367 Jersey BGS Auctions will translate to the Illinois context. The competitive option
368 is available to Illinois customers, and I believe that the auction format proposed
369 will harness this competition for the benefit of customers.

370 Regulation has its place. However, it is generally acknowledged that it is a
371 weaker force than competition in terms of achieving an efficient allocation of
372 resources and prices that track economic realities. If a competitive alternative is
373 available, it should be preferred to achieve these goals. The service of assembling
374 a supply portfolio and managing its risks is particularly ill-suited to a regulatory
375 solution. Regulation that relies on a retroactive review of portfolio management
376 provides incentives for the utility to make a decision that is within the range of
377 reasonable options, and that a reasonable person would select from information
378 that was reasonably knowable at the time. For portfolio management, these
379 incentives naturally lead to well considered decisions that avoid risks and that stay
380 with tried and true approaches. Such decisions need not be optimal or even result
381 in a favorable outcome for customers relative to other decisions that could have
382 been made at the time. Customers stand to benefit from the availability of a
383 competitive option instead. Competitive suppliers of the portfolio management
384 and price risk management service can consider all options to manage the

385 portfolio and they can use any and all hedging instruments. That there is
386 competitive pressure means that surviving in the market requires a winning
387 strategy. Competitive pressures encourage rapid decisions, encourage novel
388 approaches to hedging, and reward the taking of well calculated risks. Bringing
389 the full gamut of strategies to bear on managing the supply portfolio, and allowing
390 the competitive discipline of the market to select those entities that are best at this
391 management function, means that customers can be expected to benefit from
392 lower prices. Regulation under a prudence standard is a weak substitute for this
393 competitive option.

394 Neither Mr. Salgo nor Dr. Steinhurst recognizes the benefits of
395 competition for the portfolio management service. This is illustrated in Mr.
396 Salgo's testimony, when he compares "price fixity" to "price stability" (AG
397 Exhibit 2.0 p. 12, lines 13 to 15) and asserts that general "price stability" can be
398 achieved without full "price fixity". He states that customers may be better off if
399 customers were open to a modest amount of volatility, which would be obtained
400 by leaving a portion of the position open and subject to the spot market. I agree
401 that in considering all the sources of supply for the portfolio, leaving some of the
402 position open could reduce the cost. The point that Mr. Salgo misses is that when
403 the portfolio management service is in the hands of the competitive market, as it
404 is in the Auction Process proposed by Ameren, the competitive suppliers are the
405 ones who will decide how efficient it is to leave some of the position open. The
406 competitive suppliers will factor any such advantages directly into their bids.
407 Customers will get the benefit of such cost minimizing strategies, and they will

408 get this benefit at a fixed price. I believe that Mr. Salgo's distinction between
409 price fixity and price stability in fact reinforces and supports my view and
410 Ameren's view that there are complex trade-offs in managing a portfolio and that
411 leaving this function in the hands of the competitive market is best for customers.

412 **Q. What do you conclude about the position that Mr. Salgo and Dr. Steinhurst**
413 **put forth on utility portfolio management?**

414 A. I conclude that utility portfolio management, as a product design option, is not as
415 well suited to meeting the objective of procuring reliable supply at competitive
416 market prices and is less suited to providing protection to small customers from
417 the volatility of short-term market fluctuations. The product design of the Auction
418 Process proposed by Ameren – the procurement of the full-requirements tranche –
419 is a pillar that supports other elements of the Auction Process to fulfill many of its
420 essential objectives. The full-requirements product ensures that competitive
421 discipline is brought to bear on the cost of managing the supply portfolio and its
422 price risks. The full-requirements product ensures a broad base of potential
423 competitors, including financial players and marketers and traders without an
424 asset base in MISO, creating a viable competitive alternative. The full-
425 requirements product is essential to providing reliable supply at competitive
426 prices and to promoting the best outcome for customers.

427 **Q. Having considered the testimony of Dr. Rose and Dr. Steinhurst, are you**
428 **persuaded that the wholesale markets are neither competitive nor mature,**
429 **and that this means that the procurement of supply for customers should not**
430 **rely on the Auction Process?**

431 A. No, I am not.

432 I do not believe that Dr. Rose’s conclusions follow his analysis or from the
433 analysis of Professor Sibley on which he relies, and I do not believe that Dr.
434 Steinhurst’s conclusions follow from the analysis in Mr. Fagan’s testimony. It is
435 my understanding that these witnesses draw unwarranted statements as to the lack
436 of maturity and competitiveness of the MISO electricity markets without a
437 structural analysis of a relevant market from a wholesale energy perspective.
438 These witnesses appear to dismiss market mitigation procedures that have been
439 approved by the Federal Energy Regulatory Commission (“FERC”). These
440 witnesses believe that the Auction Process should not be used because it cannot
441 be yet shown that the wholesale market is competitive. The Ameren Illinois
442 utilities do not own a portfolio of generation that would allow them to supply their
443 customers and the Ameren Illinois utilities will have to procure supply for their
444 customers in some manner once current contractual arrangements expire at the
445 end of 2006. Regardless of the procurement method for such supply that the ICC
446 ultimately selects – whether this procurement is conducted through an auction as
447 Ameren proposes, through another competitive process, or through utility
448 management of a portfolio as some advocate – ultimately participants in the
449 wholesale markets will be supplying the inputs to such supply. In this sense,
450 reliance on the wholesale markets cannot be avoided. The selection of another
451 procurement method does not alter the state of the wholesale markets and does
452 not remove the necessity that participants in the wholesale market will deliver the
453 inputs for the supply of Ameren customers. However, the selection of another

454 procurement method such as utility portfolio management can reduce benefits to
455 customers by failing to harness the competitive pressure for the supply the
456 portfolio management service, as I explain above.

457 Q. Have you independently analyzed the claims in the testimonies of Dr. Rose, Dr.
458 Sibley and Mr. Fagan alleging that the wholesale market will not be workably
459 competitive and sufficiently mature by the start of the supply period on January 1,
460 2007?

461 A. No. Mr. Frame has analyzed those claims. I have read and concur with the
462 testimony of Mr. Frame, who concludes that the criticisms of the competitiveness
463 and state of development of the wholesale market in which bidders will operate
464 are unfounded, inaccurate and irrelevant to the procurement auction proposed by
465 Ameren. Mr. Frame's testimony demonstrates that those witnesses have made
466 unsupported claims without analyzing a relevant geographic market, without
467 considering that the MISO wholesale market is similar to other wholesale markets
468 that have been operating for a period of years, and without considering that the
469 MISO market will have been operating for 21 months before the supply period
470 begins. Further, Mr. Frame identifies several specific errors in Dr. Sibley's data.

471 Q. Are there reasons to believe that the wholesale market is workably competitive?

472 A. Yes. I understand that the MISO has a Market Monitor and has procedures for
473 load pocket market mitigation for broadly and narrowly constrained areas. Mr.
474 Fagan describes this in his testimony (See CUB Exhibit 1.0 at lines 326-327.) The
475 FERC as well has jurisdiction over the wholesale market and has personnel
476 dedicated to market oversight. As Mr. Frame notes, the MISO market is very

477 similar to other established wholesale markets including PJM. I see no reason to
478 suspect that the auction will be affected by a lack of competitiveness in the
479 markets for wholesale electricity products.

480 **Q. Even if you were presented with some evidence that market power could be**
481 **exercised in one or several relevant wholesale markets, would this convince**
482 **you that the Auction Process should be abandoned?**

483 A. No. As I testified earlier, a change in the procurement method will not change the
484 realities of the situation. Ultimately Ameren will require supply from the market,
485 regardless of whether that supply is procured through an auction, through an RFP,
486 through a managed portfolio or through the spot market. The Auction Process is
487 designed to harness the competition for the supply of the portfolio management
488 service and to bring the benefits of the competition that exists in wholesale
489 markets to the retail customers. It is the best procurement process for customers
490 whatever the state of the wholesale markets. If there is a problem with the
491 wholesale markets, that problem must be fixed directly and cannot be fixed by
492 Ameren's choice of procurement mechanism. As I explain in detail in Section 3
493 of my testimony, I believe that the competitive safeguards proposed are sufficient
494 to safeguard against anti-competitive behavior in the auction.

495 **Q. Please summarize your testimony with respect to whether the Auction**
496 **Process as proposed is the best procurement method for Ameren customers**
497 **at this time.**

498 A. The majority of testimony from intervenors and Staff either implicitly or
499 explicitly recognizes that, in general terms, the proposed Auction Process is the
500 best procurement method for customers. I agree.

501 Three witnesses offer testimony that is not consistent with this majority.
502 Mr. Salgo and Dr. Steinhurst suggest that an alternate product definition that
503 involves utility portfolio management would be better. I disagree. As explained
504 herein and in my direct testimony, the full-requirements product places price-risk
505 and responsibility for portfolio management in the hands of competitive entities
506 that are best suited to take, manage and price these risks. This assignment of risks
507 to the entities best positioned to manage them assures that the portfolio
508 management service will be performed as efficiently as possible and that
509 customers will benefit.

510 Dr. Rose and Dr. Steinhurst rely on a flawed analysis of wholesale market
511 conditions to conclude that the Auction Process proposal should be discarded. I
512 disagree with their conclusion that competition in the wholesale market is
513 inadequate and I disagree that it would follow, even if we could agree that the
514 competitiveness of the wholesale markets cannot be clearly established, that the
515 Auction Process is infeasible and that another procurement method is better.

516 Hence, while these three witnesses take issue with the Auction Process, I
517 remain unconvinced by their arguments and I remain convinced that the proposed
518 Auction Process is best suited to meeting the objectives of the procurement
519 process for Ameren customers.

520

521 **3. The Competitive Safeguards of the Proposed Auction Process, As Modified**
522 **to Take Into Account Views of Intervenors, Are Sufficient. Some Alternatives**
523 **Proposed Are Based on Objective of Controlling Wholesale Market Power and**
524 **Should be Rejected.**

525

526 **Q. What is the purpose of this section of your rebuttal testimony?**

527 A. In this section of my rebuttal testimony, I will:

528 • Review the testimony of witnesses regarding changes to the
529 competitive safeguards that they believe would improve the
530 Auction Process;

531 • Examine the objectives of the modifications to the competitive
532 safeguards as presented by witnesses from Staff and other
533 intervenors and conclude that, in some cases, these modifications
534 aim to control market power at the wholesale market level rather
535 than properly aiming to enhance the competitiveness of the
536 bidding environment at the auction;

537 • Examine in detail the proposed changes, accepting some of the
538 views proposed and rejecting others;

539 • Summarize the competitive safeguards of the Auction Process and
540 conclude that they provide adequate protection against anti-
541 competitive behavior.

542 **Q. What do you mean by the term “competitive safeguards”?**

543 A. Competitive safeguards are features of the Auction Process that limit the scope for
544 anti-competitive behavior in the auction, with the view to maximizing the
545 competitiveness of the bidding environment. In Section 2 of my rebuttal
546 testimony, I summarize the eight essential elements of the Auction Process,
547 including the competitive safeguards. These competitive safeguards consist of:

548 • The load cap;

- 549 • The auction volume guidelines; and
550 • The Association and Confidential Information Rules.

551

552 **Q. Have you reviewed the testimony from various witnesses who propose**
553 **changes to the competitive safeguards that they believe will improve the**
554 **Auction Process?**

555 A. Yes. The witnesses that have proposed changes to the competitive safeguards that
556 they believe would improve the Auction Process are Mr. Collins on behalf of the
557 IIEC, as well as Dr. Salant and Professor Sibley on behalf of ICC Staff.

558 **Q. Please start by discussing the load cap. What was the level of the load cap**
559 **incorporated into the Auction Process as presented in direct testimony?**

560 A. The Auction Process as presented in direct testimony incorporates a load cap of
561 50% of the tranches in each of the Fixed Pricing and Spot Market Segments of the
562 auction.

563 **Q. Can you please identify the witnesses who are proposing changes to the load**
564 **cap and summarize their rationale?**

565 A. All of the witnesses named above propose a change to the load cap.

566 Mr. Collins advocates that there be no load cap. (This is equivalent to a
567 proposal to increase the load cap to 100% of the tranches in a segment). He argues
568 that a load cap could result in higher prices because any load cap “might limit a
569 very efficient supplier (one who is able to offer the lowest bid price) from offering
570 into the auction the maximum number of tranches that it could serve more
571 efficiently than other bidders.” (IIEC Exhibit 3, p.8, lines 145-148)

572 Professor Sibley believes that the load cap should be set lower than 50%
573 and that the load cap has an essential role to play in the control of the exercise of
574 market power by generation owners in Illinois. Professor Sibley provides
575 information regarding generation ownership in Illinois and makes two
576 observations from this information. First, he notes that the list of owners with at
577 least 100 MW of generation provides an indication of the capacity that will bid in
578 the auction although “not all of the capacity listed in Table Two may be available
579 for Ameren’s auction due to self-generation requirements or commitments to
580 other uses” (ICC Staff Exhibit 2.0, p. 14, lines 189-191). Second, he observes that
581 “electricity generation capacity in the PJM and MISO regions in Illinois is highly
582 concentrated” (ICC Staff Exhibit 2.0, p.15, lines 213-214). He concludes that the
583 load cap and other competitive safeguards are important to the mitigation of
584 market power, which he defines as “withholding some capacity from the auction”
585 (ICC Staff Exhibit 2.0, p.17, lines 245-246). He notes that since in a 10,500 MW
586 auction, a 50% load cap is likely to constrain at most one of the generation owners
587 that he considers to be potential bidders, then the load cap should be lowered.
588 Although he does not make a specific recommendation, he does note that the New
589 Jersey BGS Auctions use a load cap in the 30-35% range.

590 Dr. Salant also views the load cap as a mechanism “that can be used to
591 mitigate the impact of market power” (ICC Staff Exhibit 1.0, p. 23 lines 512-513).
592 Dr. Salant agrees in his testimony with Professor Sibley that the load cap should
593 be analyzed in the context of the high concentration of generation resources in
594 Illinois and that the load cap should be set to control any market power that such

595 potential bidders have: “As noted by Professor David S. Sibley in his testimony
596 (ICC Staff Exhibit 2.0), the two largest suppliers own nearly 65 percent of the
597 generation capacity in the region of Illinois dispatched by PJM Interconnection
598 (“PJM”) and the two largest suppliers own more than 75 percent of the generation
599 capacity in the region of Illinois dispatched by Midwest ISO (“MISO”). Given the
600 utilities’ proposed load caps of 50 percent, it is possible that large suppliers will
601 be able to impact the auction price in the utilities’ auctions” (ICC Staff Exhibit
602 1.0, p. 35, lines 786-793). This appears to be the only study that Dr. Salant has
603 consulted in making his load cap recommendation. Dr. Salant also agrees with
604 Professor Sibley that the load cap should be lowered. He notes that “New Jersey
605 has generally had load caps of approximately 30 to 35 percent (the exact
606 percentage varies by utility and by auction)” (ICC Staff Exhibit 1.0, p. 66 lines
607 1487-1488) and he recommends “setting the load cap at a level consistent with the
608 levels used in previous SMR format auctions, i.e., in the range of 25 to 35
609 percent” (ICC Staff Exhibit 1.0, p. 70 lines 1575-1577).

610 **Q. How did you proceed to evaluate Ameren’s initial proposal of a 50% load**
611 **cap and what factors did you consider in your evaluation?**

612 A. The load cap will be incorporated in the Rider MV and will apply to all auctions
613 conducted under the tariff. I proceeded with my evaluation by primarily
614 considering the effectiveness of the load cap on what would be the “typical
615 auction” under the tariff. By the “typical auction”, I mean the second (for supply
616 starting June 1, 2008) and all subsequent competitive procurement processes. In
617 the typical auction, there would be approximately 4,300 MW in the Fixed Pricing

618 Segment and 2,500 MW in the Spot Market Segment. The first auction will be
619 atypical in that there will be a higher number of tranches in the Fixed Pricing
620 Segment.

621 I directly considered the following factors in my evaluation:

- 622 • Whether the load cap was likely to limit the participation of the
623 bulk of the anticipated pool of bidders;
- 624 • Whether the load cap was likely to be effective in limiting the
625 ability of a supplier to influence the auction results;
- 626 • Whether the load cap was likely to be effective in limiting the
627 ability of suppliers to over-represent their initial interest in the
628 auction; and
- 629 • Whether the load cap was likely to provide sufficient
630 diversification of the supplier base and limit the exposure to the
631 risk of supplier default.

632 I also drew upon my experience as Auction Manager in the New Jersey
633 BGS Auctions. I drew upon this experience to assess the likely pool of bidders
634 and the appetite that these bidders are likely to have for the fixed-price products at
635 auction. The details of this evaluation are in my direct testimony (see Resp. Exs.
636 6.0 and 6.6).

637 **Q. Did you consider that the load cap may encourage a broader participation of**
638 **suppliers?**

639 A. I did not consider this factor explicitly in my evaluation. However, I do believe
640 that smaller or newer participants will consider the load cap when deciding
641 whether to bid in the auction and will view positively a load cap that provides
642 them with a chance to compete. My experience with the New Jersey BGS

643 Auctions provides anecdotal evidence to that effect, which is confirmed by the
644 feedback from potential suppliers received by Ameren.

645 **Q. Did you come to the conclusion that a 50% load cap was an optimal level and**
646 **that no other level would be as effective?**

647 A. I believe that there is no single optimal level for the load cap and that a reasonable
648 load cap is one that appropriately balances the benefits and the costs of the
649 situation. I reached the conclusion that setting a load cap of 50% was likely to
650 strike a good balance and be effective. I did not come to the conclusion that no
651 other load cap could be effective.

652 I do not believe that there is a single level for the load cap that will ensure
653 the effectiveness of the competitive safeguards and the success of an auction.
654 Setting a load cap is a question of balance that requires the consideration of all the
655 factors that I have named above. When considering all the factors, a load cap that
656 provides additional benefits in one dimension compared to another level for the
657 load cap may well reduce benefits in another dimension.

658 **Q. Can you please explain further how a lower or higher load cap would affect**
659 **the balance of the factors that you consider in your evaluation?**

660 A. Certainly. Referring to the factors I named above:

- 661 • Limiting participation. A load cap by definition limits the amount of
662 tranches that a bidder can bid and win. A load cap set sufficiently high is
663 not material: no bidder will be interested in offering an amount in excess of
664 the load cap. A load cap set sufficiently low (e.g., two tranches) limits each
665 and every bidder's participation. In examining this factor, what is assessed
666 is whether the load cap is likely to constrain the participation of marketers
667 and financial players, which I expect to form the bulk of the pool of

668 bidders. This assessment is made by considering the number of tranches
669 that a bidder can bid on and win in the auction, and evaluating whether a
670 typical bidder's appetite for the offered product is likely to exceed this
671 level based on past experience.

672 • Influence on auction results. The auction starts with a situation of excess
673 supply, where more tranches are bid than are needed. Bidders must
674 withdraw tranches for the auction to close. Bidders withdraw tranches in
675 response to falling prices and the auction closes when there is just enough
676 supply bid for the tranches that need to be filled. In determining whether to
677 withdraw tranches, bidders seek to maximize profits. Bidders will not
678 continue to bid tranches if there are more profitable opportunities for their
679 supply arrangements elsewhere in the market. In the initial stages of the
680 auction, when there is sufficient excess supply, a bidder that elects to
681 withdraw tranches would not be expected to have an appreciable impact on
682 price, given that supply in the auction well exceeds the number of tranches
683 that need to be filled. Late in the auction, however, there will be a lower
684 level of excess supply, as the number of tranches bid approaches the
685 number of tranches that need to be filled, and a single bidder's actions
686 could impact the auction price. At these late stages in the auction, a bidder
687 could attempt to withdraw tranches strategically, i.e., not in response to the
688 opportunity cost of its supply, but because that bidder believes it has the
689 ability to close the auction unilaterally at prices that are higher than would
690 otherwise be the case. The bidder would obtain a higher price for the
691 tranches that it continues to bid, but the bidder loses the opportunity to
692 serve those tranches that it withdraws. The load cap limits the number of
693 tranches that a bidder controls at any point during the auction and therefore
694 curbs the ability for a bidder to use this strategy profitably at the end of the
695 auction. Working in tandem with the load cap in curbing the ability of
696 bidders to implement such a strategy is the limiting of the amount of
697 information provided to bidders regarding excess supply late in the auction
698 through an appropriately formulated auction rule. Generally, providing

699 more information on excess supply is beneficial to bidders as it allows
700 them to learn and revise their bids on the basis of market information. In
701 using these two instruments (the load cap and limits to the information
702 provided to bidders) to mitigate concerns about strategic bidding, reliance
703 mainly on a lower load cap means that less reliance needs to be placed on
704 restricting information at the end of the auction.

705 • Over-stating interest. The Auction Manager will make an assessment of the
706 competitiveness in the auction at the indicative offer stage, and in the first
707 round of the auction. If this assessment indicates that the level of interest is
708 not sufficient to provide assurances of a competitive result, the Auction
709 Manager can cut back the volume in the auction (I discuss the auction
710 volume guidelines mechanics further on in this section and in Section 5).
711 The volume cutback means that that a larger number of tranches bid will be
712 chasing a smaller number of tranches of load, ensuring a more competitive
713 bidding environment. If bidders' indications of early interest, which are
714 made at prices that can be substantially higher than the expected final
715 auction prices, overstate the bidders' willingness to serve at those prices,
716 the Auction Manager may conclude that there is more competition at the
717 auction than there truly is. It is possible that the Auction Manager would
718 fail to cut back the volume when it would have been desirable to do so. In
719 stating its early interest, the bidder is limited by the load cap. The higher
720 the load cap is compared to the typical bidder's appetite for the product on
721 offer, the greater is the scope for a bidder overstating interest early in the
722 auction.

723 • Diversification. The load cap, by determining the number of tranches that a
724 bidder can bid and win, also determines a minimum number of winners at
725 the auction. Any load cap below 100% assures at least two winners and
726 leads to a minimum diversification of the base of suppliers that will serve
727 customers. As the load cap is decreased, the minimum number of winners
728 at the auction increases. For example, a 49% load ensures that there are
729 three winners.

730 Evaluating a load cap level involves an assessment of each of these factors
 731 and a balance of the benefits and costs. Generally, a lower load cap could impose
 732 costs in terms of limiting participation, and these costs are weighed against the
 733 potential benefits in terms of limiting overstatement of interest, curbing influence
 734 on the auction results, and promoting diversification of the supplier base.

735 **Q. Do you believe that a 100% load cap, as suggested by Mr. Collins, can**
 736 **achieve this balance?**

737 A. I do not. Mr. Collins considers only one of the four factors that are relevant to
 738 evaluating the level of the load cap. He rightly points out that a higher load cap –
 739 and 100% is as high as a load cap gets – has the potential benefit of providing
 740 additional opportunities for some entities to bid in a greater amount of supply.
 741 However, this is only one side of the equation. Mr. Collins does not take into
 742 account that a 100% load cap has real costs. A 100% load cap would remove the
 743 needed discipline on bidders’ ability to over-represent their interest in the auction,
 744 remove the needed discipline on a single bidder’s ability to influence the auction
 745 results, and provide no assurance whatsoever of diversification of the supplier
 746 base. A 100% load cap strips the auction of essential protections against bidder
 747 strategies that can lead to higher auction prices.

748 In my opinion, there are levels of the load cap that will necessarily be
 749 superior to a 100% load cap. Unless there is a significant number of bidders and
 750 each of these bidders is willing to serve all of the load, which I find implausible,
 751 there will be levels of the load cap lower than 100% that will not meaningfully

752 constrain participation while at least providing some benefits in the other three
753 dimensions mentioned.

754 **Q. What were the levels of the load caps set in the New Jersey BGS Auctions?**

755 A. I will describe separately the load caps set in the New Jersey BGS Auction for
756 fixed-price products (“BGS-FP”) and the New Jersey BGS Auction for hourly
757 products (“BGS-CIEP”).

758 In the BGS-FP Auction, a product is the load of an electric distribution
759 company (“EDC”) for a given term. Each EDC wants to ensure a diversification
760 of its base of suppliers if it can. A load cap is thus set separately for each product.
761 The load caps for the previous BGS-FP Auctions are shown in Resp. Ex. 12.3. For
762 three of the four EDCs, the load caps in the BGS-FP Auctions vary between 33%
763 and 43%. For Rockland Electric (“RECO”), the fourth EDC, the load cap is set at
764 100% given the small number of tranches for that product (between 1 and 4
765 tranches). Calculated on an overall, statewide basis, the load cap in the BGS-FP
766 Auctions has varied between 35% and 38%.

767 In the BGS-CIEP Auction, the load cap is set on an auction-wide basis
768 rather than a product basis. The EDCs are not concerned in the same way about
769 the risk of supplier default for the replacement of supply of a product tied to the
770 hourly energy market. For the BGS-CIEP auction, the statewide load cap has been
771 set at 33% (the calculated percentage rises to 34% due to rounding).

772 **Q. Do you believe that a “New Jersey” load cap, set between 33% and 38%,
773 could be effective for Ameren and could provide a good balance amongst the
774 factors that you use for your evaluation?**

775 A. I do.

776 Compared to the 50% initially proposed by Ameren, the benefits of a
777 ‘New Jersey’ load cap (in the 33-38% range) would be as follows. A New Jersey
778 load cap, compared to the proposed 50% load cap, will be more effective in
779 curbing the influence of a single bidder upon the auction results. Furthermore, a
780 New Jersey load cap allows the possibility that more excess supply information
781 can be provided to bidders late in the auction, so that the auction would have the
782 benefit of more information, while maintaining the effectiveness of the load cap
783 in curbing the influence of a single bidder upon the auction results. A New Jersey
784 load cap, compared to the proposed 50%, would be more effective in imposing
785 additional discipline on bidders overstating their initial interest, and thus be more
786 effective in ensuring that the Auction Manager is making auction volume
787 decisions based on reliable information. A New Jersey load cap, compared to the
788 proposed 50%, would lead to further diversification of the supplier base, ensuring
789 that there is one more supplier.

790 Compared to the proposed 50%, the cost of the New Jersey load cap is that
791 it may potentially limit the participation of energy marketers, traders or financial
792 players that I expect would form the bulk of the bidding pool. I believe that the
793 auction product contains an important risk-management component. Certain
794 marketers and traders have competencies in providing that component at
795 competitive prices, and must be allowed direct participation in the auction in
796 order to do this. To the extent that a load cap is restrictive, it could limit the

797 lowest-cost risk-manager(s) from participating fully in the auction, thereby
798 resulting in higher auction prices.

799 Further, those marketers and traders with competitive advantages in risk
800 management may also simply elect to pursue business opportunities for forward
801 sales outside the Illinois Auction if the quantity of the fixed-price product that
802 they can bid is too low and does not satisfy their appetite. I believe that
803 consideration of whether the participation of these bidders is limited by the load
804 cap is important. In the typical auction, with over 4,300 MW in the Fixed Pricing
805 Segment and approximately 2,500 MW in the Spot Market Segment, a New
806 Jersey load cap would mean limiting each bidder to approximately fifteen or
807 sixteen tranches in the Fixed Pricing Segment, and nine tranches in the Spot
808 Market Segment (tranches being measured on a 100 MW basis). I believe that the
809 appetite for the offered product may well exceed these levels so that the load cap
810 would limit the participation of marketers and financial players.

811 Nevertheless, even with this potential cost, I believe that a New Jersey
812 load cap can be effective and that the cost in terms of limiting participation would
813 still be modest enough to provide a good balance. The load caps at these levels
814 have worked well in the New Jersey Auctions and I note that the load at auction in
815 the Fixed Pricing Segment of the typical auction (over 4,300 MW) is similar to
816 the load in the typical New Jersey BGS-FP Auction going forward (approximately
817 5,300 MW). In addition, the load in the Spot Pricing Segment (with 2,500 MW)
818 is also similar in size to the load in the typical New Jersey BGS-CIEP Auction
819 going forward (2,800 MW).

820 **Q. Are you saying that you believe that a load cap level set between 33% and**
821 **50% will be effective and provide a good balance amongst the factors that**
822 **you use for your evaluation?**

823 A. Yes, I am. I believe that a load cap between 33% and 50% would also provide a
824 good balance. A load cap at the lower end of this range would provide greater
825 protection against bidders over-stating their interest early in the auction and
826 against the influence that one bidder may have on the auction results, but would
827 also heighten the potential risk of limiting the participation of the bulk of the
828 anticipated pool of bidders.

829 **Q. Do you then entirely disagree with Professor Sibley's opinion that the load**
830 **cap should be set lower than 50%, and with Dr. Salant's recommendation of**
831 **a 25-35% range?**

832 A. I do not entirely disagree.

833 I agree with Dr. Salant and Professor Sibley that a load cap is needed, and
834 that a load cap lower than 50% can be effective.

835 I disagree in part with the recommendation for a 25-35% range. Given the
836 number of tranches involved in the typical auction, I believe that a load cap of
837 33% could possibly constrain the participation of some marketers and financial
838 players to levels below that which they may wish to serve, and I do not believe
839 that the other benefits that may come from this lower load cap would likely be
840 significant. Hence, I believe that 33% is on the low end of the range of
841 reasonableness for the load cap in the typical auction. However, as I have
842 testified, I believe that setting a load cap is a question of weighing costs and

843 benefits. I can readily concede that reasonable people may disagree on exactly
844 where the right balance lies.

845 **Q. Dr. Salant supports his 25-35% recommendation by pointing out two facts.**
846 **First he points out that each utility in the New Jersey BGS auction has set its**
847 **load cap in the 30 to 35 percent range (ICC Staff Exhibit 1.0, p. 69 lines 1553-**
848 **1554). Second, he points out that this range is consistent with levels used in**
849 **other Simultaneous Multiple Round (“SMR”) format auctions such as**
850 **spectrum auctions (ICC Staff Exhibit 1.0, p. 69 lines 1554-1557). Do you**
851 **agree that the load caps set for other open auctions should be considered in**
852 **setting the load cap in Illinois?**

853 A. As I testified, I believe that there is no optimal level for the load cap and that a
854 reasonable load cap is one that appropriately balances the benefits and the costs of
855 the situation.

856 I do agree that it is reasonable to consider how load caps were set in other
857 similar auctions, in situations where similar costs and benefits were faced, as I do
858 above by considering the New Jersey BGS Auctions. Dr. Salant misrepresents the
859 facts when he states that the load caps were set between 30% and 35% depending
860 on the utility. As I show in Resp. Ex. 12.3, and I have testified above, the range of
861 the load caps for fixed-price products in the New Jersey BGS Auctions is between
862 33% and 100%. The range for the load cap on hourly products in the New Jersey
863 BGS Auction is 33-34% (but for hourly products the load cap is not set on a
864 utility basis).

865 With regards to spectrum auctions, Dr. Salant points out that in the past
866 the load caps have been set at levels consistent with a 25 to 35 percent range.
867 Although I am not familiar with all of the considerations that went into setting the
868 caps in spectrum auctions, I do understand that a primary concern was to ensure
869 that this essential resource to providing communication services was not
870 concentrated in the hands of the few. In the words of the Federal Communication
871 Commission (“FCC”), as quoted from its 2000 review of spectrum aggregation
872 limits: “we recognize that spectrum is an input in CMRS (Commercial Mobile
873 Radio Service) markets. Indeed, this recognition prompted adoption of the
874 spectrum cap as a means of ensuring CMRS competition in the first place.”
875 (report and order WT Docket No. 01-14, December 18, 2001, p. 12) The
876 consideration of the state of competition in these communication markets has,
877 since 2000, prompted the FCC to relax the caps on acquiring spectrum, through
878 auctions and through other means (see
879 <http://www.wirelessweek.com/article/CA523345.html>; Cingular-AWS Merger
880 Sets Precedent for FCC Post-Spectrum Cap Merger Reviews, Communications
881 Daily, Volume 25; Issue 81, April 27, 2005; Biennial Regulatory Reviews Find
882 Little Need for Changes, Telecommunications Reports, January 15, 2005). The
883 rationale for the setting of the load cap in this context is then to ensure access to
884 an essential input for firms that use this input to sell other products to customers.
885 This rationale is not applicable to the setting of load caps in an auction for full-
886 requirements service such as the one being proposed by Ameren.

887 **Q. Do you concur with the analysis that Professor Sibley undertakes and on**
888 **which Dr. Salant relies in concluding that a load cap should be lower 50%?**

889 A. I do not. While I partially agree with their conclusions, I disagree with their
890 reasons for reaching this conclusion.

891 **Q. Can you briefly summarize the principal basis for Professor Sibley's and Dr.**
892 **Salant's conclusion that the load cap should be set lower than 50%?**

893 A. Dr. Salant's recommendations and Professor Sibley's opinion stem from their
894 evaluation of the concentration of generation capacity in Illinois. They believe
895 that generation capacity in Illinois is highly concentrated. They are concerned that
896 market power can be exercised by wholesale market players, particularly with
897 respect to generation capacity. They conclude that the Auction Process should be
898 modified to avoid the effects on the auction results of such market power. The
899 load cap is one such control, and they believe that the concentration of generation
900 ownership is directly relevant to setting the level of the load cap.

901 **Q. Do other witnesses also present recommendations on a similar basis, i.e.,**
902 **using an evaluation of an unsatisfactory level of competitiveness of wholesale**
903 **markets in MISO or the Ameren service area?**

904 A. Yes. As I have testified in Section 2, Dr. Rose and Dr. Steinhurst (based on Mr.
905 Fagan's testimony) also rely for their recommendations on a finding of a lack of
906 competitiveness of the wholesale markets. Dr. Rose, relying on Dr. Sibley's
907 concentration calculations, finds that generation capacity is highly concentrated.
908 Dr. Steinhurst relies on Mr. Fagan's conclusion that the MISO market is not fully
909 competitive. Dr. Rose and Dr. Steinhurst state that the controls necessary to

910 prevent the exercise of market power by wholesale market players are not in
911 place. The main difference is that, instead of concluding that measures in the
912 Auction Process must go directly to controlling the effect of such market power
913 on auction results, Dr. Rose and Dr. Steinhurst conclude instead that the Auction
914 Process should be abandoned.

915 As I testified previously in Section 2, I disagree with Dr. Rose and Dr.
916 Steinhurst at three levels.

917 First, I do not believe that Dr. Rose's conclusions follow from his analysis
918 or from the analysis of Professor Sibley on which he relies, and I do not believe
919 that Dr. Steinhurst's conclusions follow from the analysis in Mr. Fagan's
920 testimony. It is my understanding that these witnesses draw unwarranted
921 conclusions as to the lack of maturity and competitiveness of the MISO electricity
922 markets without a structural analysis of a relevant market from a wholesale
923 energy perspective. Considering Mr. Frame's rebuttal testimony, the presence of
924 market oversight by federal agencies and a MISO Market Monitor, and the
925 similarity of MISO to established markets such as PJM, I see no reason to doubt
926 that conditions in the wholesale market can efficiently support a competitive
927 procurement method like the one that Ameren proposes.

928 Second, it is my view that these witnesses erroneously carry their view of
929 the state of competition in particular wholesale markets to competitiveness in the
930 auction. These witnesses do not recognize that the auction is not merely a way to
931 solicit bids for a list of specific wholesale products that Ameren could otherwise
932 readily procure on wholesale markets. These witnesses miss the point that

933 suppliers, to compete in the auction, must determine which wholesale products
934 they will choose to assemble their portfolio, and they must determine how they
935 can best provide the risk management services required to serve the full
936 requirements needs of Ameren customers. The Auction Process is designed to
937 harness the competition for the supply of the portfolio management service. It is
938 designed to harness the competition in the choice of the wholesale products that
939 will be needed and to bring competitive pressures to bear to the risk management
940 function.

941 Third, the conclusion that Dr. Rose and Dr. Steinhurst draw that the
942 Auction Process should be abandoned is unwarranted, and would still be
943 unwarranted even if it could be established that market power can be exercised in
944 one or several wholesale markets. Another procurement method will not change
945 the realities of the wholesale markets or the fact that ultimately some inputs to the
946 auction products are purchased through these wholesale markets.

947 **Q. Do you disagree with Professor Sibley's and Dr. Salant's analysis for similar**
948 **reasons?**

949 A. Of course, Professor Sibley and Dr. Salant do not come to the same conclusion
950 and do not suggest that the Auction Process should be abandoned. However, I do
951 disagree with their analysis for similar reasons.

952 I believe that these witnesses' opinion and recommendations do not follow
953 from the analysis they put forth. The implication that they draw regarding the
954 ability to exercise market power is unwarranted based on summary measures of
955 concentration in an arbitrarily defined region, which Professor Sibley himself

956 admits is not a relevant geographic market. I believe that these witnesses carry
957 their view of the state of competition in particular wholesale markets to
958 competitiveness in the auction. They fail to recognize that the auction product is
959 not a simple laundry list of wholesale products that could be purchased by
960 Ameren on the wholesale markets. The auction product puts in the hands of the
961 competitive market the responsibility of determining the exact composition of the
962 portfolio of products and the exact risk management strategies that will be needed
963 to serve Ameren customers.

964 Finally, I believe that even if one were to believe these witnesses' analysis
965 of the concentration and potential for the exercise of market power by wholesale
966 market players, it would not follow that the solution is to mitigate the presumed
967 effects on the auction results of this exercise of market power by lowering the
968 load cap. A competitive safeguard in the auction is imposed on bidders who
969 supply the auction product. It is unlikely to be effective to control the market
970 power that is presumed to be exercised by wholesale market players in supplying
971 products that are inputs to the auction product. A measure imposed on bidders at
972 the auction is not going to change the realities of the wholesale markets or the fact
973 that ultimately some inputs to the auction product must be purchased by auction
974 participants through these wholesale markets.

975 **Q. Are you arguing that measures such as the load cap imposed on products at**
976 **the auction level are to ensure competitiveness at the auction, and that such**
977 **measures are not effective in controlling the competition in other markets for**
978 **other wholesale products that are inputs to the auction product?**

979 A. That is correct.

980 **Q. Did you not argue earlier that the FCC legitimately imposed caps on the**
981 **auction products (spectrum licenses) to control the competition in other**
982 **markets (communications services)? Isn't this a precedent showing that it is**
983 **legitimate to impose a load cap on the auction product as a means to**
984 **controlling the competition for wholesale products?**

985 A. I did testify that the FCC imposed caps on the auction products as a way to
986 control competition in other markets, but it does not mean that imposing load caps
987 in the Ameren auction would in any way effectively control any market power
988 that wholesale market players allegedly can exercise.

989 There is a basic difference between the two situations. In spectrum
990 auctions, as stated by the FCC, the auction product (the spectrum license) is the
991 input. It is an input for firms to be able to provide communications services to
992 customers. Access to this input is essential to becoming a competitor in the
993 market for providing communication services. If only two firms acquire spectrum
994 in a given region, there can be at most two firms providing communication
995 services in that same region. When the FCC controls the number of competitors
996 “upstream” – i.e., the number of competitors that acquire the input, namely
997 spectrum licenses in a region – the effect of this diversification of competitors
998 trickles downstream to the market for customer services (the output). But in
999 auctions such as the one proposed by Ameren, it is not true that the auction
1000 product is the input and the other market is the downstream service. It is the other
1001 way around. Bidders in the auction compete to provide the full-requirements

1002 service to customers (the output). To do so, they will assemble a portfolio of
1003 inputs from the “upstream” wholesale markets and provide risk management
1004 services. If a load cap is imposed to ensure that there are at least three suppliers
1005 for Ameren customers, this has no effect on the number of competitors of
1006 wholesale products. Imposing measures on the auction downstream will not go
1007 against the current to affect the behavior of wholesale market players upstream.

1008 **Q. Do you believe that there are other competitive safeguard recommendations**
1009 **made by witnesses in this proceeding that are based on concerns that market**
1010 **power can be exercised by wholesale market players and that aim to avoid**
1011 **the effects on the auction results of such market power?**

1012 A. Yes. The particular recommendations and observations that fall in to this category
1013 are the following recommendations made by Dr. Salant:

- 1014 • The characterization of the auction volume guidelines as a
1015 measure to control the market power of suppliers selling their
1016 generation resources; (ICC Staff Exhibit 1.0, p. 28 lines 630 to
1017 638)
- 1018 • The proposal to lower load caps generally, but allow participation
1019 above the load cap for bidders who agree to be price takers; (ICC
1020 Staff Exhibit 1.0, p. 70-75, lines 1593 to 1701)
- 1021 • The recommendation to have tranche sizes as low as 2 MW; (ICC
1022 Staff Exhibit 1.0, p. 58, lines 1298 to 1302)
- 1023 • The recommendation that bidders be required to reveal to the
1024 Auction Manager any contracts that are contingent on the auction
1025 outcome. (ICC Staff Exhibit 1.0, p. 89 lines 2016 to 2025)

1026 The recommendations regarding the tranche size and the price-taking
1027 option, as well as the interpretation of the auction volume guidelines, are endorsed
1028 by Professor Sibley.

1029 **Q. You have made clear that you disagree with the rationale that drives these**
1030 **recommendations. However, will you please consider whether these**
1031 **recommendations may, for other reasons perhaps, improve the Auction**
1032 **Process? Can you please start by considering the first of these, the view of the**
1033 **auction volume guidelines as a measure to control the market power of**
1034 **suppliers of generation resources?**

1035 A. As I stated in my direct testimony (Resp. Ex. 6.0, p. 44 lines 992-1001; 1927-
1036 1940), and as I explain in further detail in Section 5 of my rebuttal testimony,
1037 where I provide a concise summary of the auction volume guidelines as
1038 developed thus far, I believe that the auction volume guidelines have a single role.
1039 And that role is to be a safety net in case the interest at the auction is not as high
1040 as expected. If interest is not sufficient, the auction volume is reduced to ensure
1041 competitive prices at the auction, and the remainder of the volume is procured on
1042 MISO-administered markets. However, I believe that it is only in the case where
1043 there is clearly insufficient interest that there should be a consideration of
1044 reducing the volume in the auction and thereby exposing customers to the
1045 volatility of the spot market.

1046 In contrast, Dr Salant testifies as follows (ICC Staff Exhibit 1.0, p. 28
1047 lines 630-638):

1048 Ameren's CPP [sic] proposal also does not recognize the
1049 fact that Ameren has market power as a buyer in the auction. Some
1050 suppliers will have limited options outside of the auction to sell
1051 their generation resources, except in day-ahead and real-time
1052 markets. The volume adjustments, discussed in more detail in
1053 Section 6, provide the Auction Manager with the ability to not only
1054 mitigate the potential impact of supplier market power, but to exert
1055 pressure on suppliers who may have limited options for selling
1056 their generation resources in other energy markets.

1057 Dr. Salant, at this point, does not make a concrete proposal regarding the
1058 auction volume guidelines, but he describes the approach that he would take. I
1059 certainly disagree with the way Dr. Salant seems to approach the auction volume
1060 guidelines. The notion that reducing the volume at auction could mitigate
1061 wholesale market power does not seem logical. Reducing the volume procured
1062 through auction does not of course reduce the volume that Ameren will ultimately
1063 need to procure through the wholesale market to serve its default customers' load.
1064 If volume is reduced at the auction, it is procured via MISO wholesale markets.
1065 Reducing the auction volume does not mean reducing overall demand.

1066 Dr. Salant appears to believe that these auction volume guidelines are
1067 Ameren's strategy for a battle of wits between Ameren with supposedly market
1068 power on the buying side, and the sellers, who are presumed to have market
1069 power on the selling side. The true stakes – whether a portion of the supply must
1070 be procured in the spot market and whether ratepayers are exposed to this

1071 additional price volatility – are too high to approach the auction volume
1072 guidelines as such a battle of wits. I believe that Dr. Salant’s view of the purpose
1073 of the auction volume guidelines is heavily colored by his mistaken belief that
1074 competitive measures taken on the downstream auction product can fight the
1075 current to have a beneficial effect on the market power that is presumed to be
1076 exercised by wholesale market players upstream.

1077 Fundamentally, examining the idea carefully, I disagree with the notion
1078 that the auction volume guidelines can be a way to mitigate potential supplier
1079 market power. Even if we accept for the sake of argument Dr. Salant’s premise
1080 that there is concentration in ownership in generation resources, and if we accept
1081 for the sake of argument his implication that market power can be exercised in
1082 wholesale markets, wouldn’t a generator with such market power welcome the
1083 fact that, if the auction volume is reduced, Ameren would be forced to purchase a
1084 steady volume in the spot market where the generator is able to exercise market
1085 power? The generator would be able to still hedge a portion of its physical long
1086 position through sales in the auction, meeting certain fixed cash flow
1087 requirements, and leave a portion open to exploit its market power in the spot
1088 market. Customers would experience the worst of both worlds. Even if we
1089 further accept the assumption that the generator would want to limit its exposure
1090 to spot and day-ahead markets, a premise that as I testified seems illogical on its
1091 face, why would the auction volume guidelines have any appreciable impact on
1092 the ability of the generator to sell its energy forward? The generator would still
1093 be able to sell most of its energy forward through the auction as planned, and

1094 would also be able to take advantage of other market opportunities to sell forward,
1095 including selling forward products at trading hubs and selling forward products
1096 that will ultimately be used by RESs to serve Illinois customers.

1097 **Q. Would you please now consider the second point, the price-taking proposal**
1098 **for bidders that would want to exceed the load cap and assess whether this**
1099 **measure would improve the Auction Process?**

1100 A. I do not believe that the price-taking option is an improvement for the Auction
1101 Process. Before explaining why I believe that this proposal is harmful, I would
1102 like to examine Dr. Salant's logic behind the proposal.

1103 The logic underlying the proposal, that a large bidder has low marginal
1104 costs and will be willing to be a price taker if it expects the auction price to be
1105 high enough, is flawed and confuses competition in the auction and competition
1106 in the wholesale market. Dr. Salant assumes that large bidders are also likely to be
1107 those with low marginal production costs. He reasons that as a result these bidders
1108 would be willing to be price takers as the auction price will almost surely exceed
1109 their marginal costs. This analysis is incorrect. The point he misses is that the
1110 marginal cost of generation is not the marginal cost of auction participation. The
1111 true marginal cost of participating in the auction is the opportunity cost of selling
1112 in the auction. The opportunity cost of selling in the auction is the revenue
1113 foregone of the next best opportunity, most likely the opportunity of selling
1114 forward power products elsewhere, including in wholesale markets or to other
1115 auction participants. (This is another instance where there is confusion between
1116 the auction product and wholesale market products). The marginal cost of

1117 supplying the auction product is not the marginal cost of production of a
1118 generation unit. Dr. Salant’s misconception of the auction product is also evident
1119 in his response to ComEd Data Request Staff 2.40 in Docket 05-0159. When
1120 asked what is an inefficiently high auction price, Dr. Salant responded: “A price is
1121 inefficiently high if it is above the marginal cost of the marginal unit.” Dr. Salant
1122 would presumably reach the same conclusion with respect to the Ameren auction.
1123 While the notion that electricity prices should be based on the marginal cost of the
1124 marginal unit underlies much of the theory of price formation in competitive
1125 wholesale spot power markets, it is not the notion that is relevant to the auction
1126 product.

1127 At its most basic, it is not logical to believe that allowing an entity to
1128 exceed the load cap on a voluntary basis will lead to a better result for ratepayers.
1129 The entity would take the price-taking option only if it would achieve greater
1130 profit by being a price-taker than by participating in the auction. Greater supplier
1131 profits for the supplier do not mean better prices for customers, they mean worse
1132 prices for customers. If the load cap is reasonably set, and I expect it will be for
1133 the Illinois auction, there is no reason to allow it to be circumvented on an
1134 optional basis through a price-taking option as the only time the option would be
1135 exercised is if customers would be harmed.

1136 There are several additional ways in which I believe this proposal will be
1137 harmful to the Auction Process achieving its objectives. First and foremost, it is
1138 essential to point out that the goal of obtaining reliable supply for ratepayers at
1139 competitive market prices will not be fulfilled under such a proposal. In the

1140 extreme circumstance in which several suppliers come forward to be price-takers,
1141 the volume at the auction will be the greater of 10% of tranches available or 1
1142 tranche. I would submit that many suppliers will not want to incur the costs of
1143 participating in the auction for such a low volume. (How many suppliers could
1144 Dr. Salant really expect to show up to compete for 1 tranche?) The price of these
1145 tranches – and therefore the price for the entire load and to be paid by all
1146 customers – will not be set by the full pool of suppliers that would have otherwise
1147 competed in the auction. A price will be obtained at the auction, but it is unlikely
1148 to be either competitive or to be a market price. These considerations will still
1149 come to bear, albeit to a lesser extent, if there is a single price-taker, who could
1150 request up to 50% of the load. Suppliers that had made plans to vigorously
1151 compete at the auction and that had perhaps contracted forward in advance of the
1152 auction will find out after the Part 2 Application that the volume in the auction is
1153 much smaller than anticipated. Again these suppliers will re-think their
1154 participation in the auction. Will the price at the auction be a competitive market
1155 price? The price at auction will certainly not reflect the full competition of all
1156 bidders that we would have expected to participate and there is no reason to
1157 suspect, let alone believe, that the price from the competition of a smaller pool of
1158 bidders would be lower. Again, there is no reason to think that the quantity choice
1159 made by the price-taker will ignore profit maximizing considerations: the price-
1160 taker will only take the option if the resulting price is higher than it otherwise
1161 would have been.

1162 Second, I believe the price-taking option is likely to deter participation in
1163 the Auction Process. Bidders may not be willing to invest resources and prepare
1164 their bids with the possibility that, at the end of the day, they will be competing
1165 for a small auction volume. Furthermore, any benefit of the load cap in terms of
1166 maximizing the participation of suppliers, especially smaller suppliers, is lost if a
1167 price-taking option is introduced. The load cap reassures smaller or newer
1168 suppliers that each and every bidder would be limited in its ability to bid and win
1169 load, and that these smaller suppliers would be free to compete with all bidders
1170 including those that they may be perceived to be more established suppliers. A
1171 price-taking option gives the option to a supplier of reserving a portion of the
1172 supply for itself without having to compete for it. Smaller or newer suppliers may
1173 well perceive the price-taking option as a barrier that prevents them from
1174 competing with more established players on an equal basis for all the load.
1175 Knowing that such an option exists may well discourage the participation of
1176 these suppliers.

1177 Third, I believe that the price-taking option negates many of the benefits
1178 of the open auction format. The benefits of the clock auction are based on bidders
1179 being able to use information that they obtain during the Auction Process to revise
1180 their bids, and this dynamic information feedback tends to elicit the best bids. The
1181 price-taking option negates these benefits in two ways. The proposal effectively
1182 forces the price-taker to bid as it would in a sealed bid situation, and deprives
1183 customers of the better bids that could result if the large bidder had the
1184 information provided through the open auction format. By the same token, the

1185 existence of a price taker denies information to suppliers that actually participate
 1186 in the auction as well. They would not see market supply at different price points;
 1187 the supply from the price-taker is fixed at all price points and does not provide
 1188 information. This could well lead to less aggressive bids as the bidders would be
 1189 less confident of the information that they learn during the auction from others'
 1190 willingness to supply.

1191 **Q. Have you identified other ways in which the proposal is problematic or**
 1192 **appears incomplete?**

1193 A. Yes, there are also problems with this proposal from a purely practical perspective
 1194 and important details that are left unspecified.

1195 The most obvious problem is that it is not sufficient for the price-taker to
 1196 declare the number of tranches and percentage of the load that it wants to serve at
 1197 the indicative offer stage. The tranches of the load at auction are not
 1198 homogeneous. There are tranches of different durations and tranches to serve
 1199 different groups of customers. The price-taker will need to declare the number of
 1200 tranches of each product that it wants to serve. This leads to additional
 1201 practicalities that appear unresolved, for example:

- 1202
- 1203 • If a price-taker wants to serve all of the tranches of particular product
 1204 (e.g., all one-year tranches for BGS-LFP customers) how will the
 1205 price for this product be determined?
 - 1206 • If there are several price-takers so that there is just one tranche left in
 1207 the Fixed Price Segment, how will the prices for the four products in
 1208 the Fixed Price Segment be determined on the basis of the auction
 1209 price?

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There are also elements of the Auction Process that I believe could need to be re-worked to accommodate a price-taking proposal. One example is the price decrements. It is typically harder to calibrate the price decrements for smaller products (i.e., products with smaller tranche targets). The fact that the price-taker option could be exercised will require that various price decrements be developed to deal with the fact that the auction may well proceed with significantly less volume. Although the auction volume guidelines also mean that the auction could proceed with less than full volume, more attention would need to be devoted to these price decrement rules when there is a significant likelihood that the volume would be cut by 50% or more.

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Q. Has there been any experience with price-taking options for the procurement of supply for default customers?

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A. Yes. This approach was used in Connecticut in their first competitive procurement for Standard Offer Service Generation Supply in 1999. Connecticut Light & Power's affiliate, Select Energy, was the price-taker. Select Energy would take 50% of the load at the weighted average prices of the winners in a competitive solicitation.

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Q. What was the result? Do you believe that this experience provides a good basis to put forth the price-taker proposal?

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A. The RFP concluded in November 1999. NRG and Duke won the competitive solicitation for the following percentages of load:

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	2000	2001	2002	2003
NRG	35%	40%	40%	45%

1233

NRG	35%	40%	40%	45%
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1234	Duke	15%	10%	10%	5%
1235	Select	50%	50%	50%	50%

1236 After the bid was awarded, there was a series of acrimonious proceedings.
 1237 NRG (as well as Select Energy) started in 2002 to ask the Connecticut
 1238 Commission for additional revenue, based on wholesale market price movements
 1239 since the bid, on problems with ISO-NE rules, and on a Standard Offer obligation
 1240 that was larger than expected. CL&P supported the suppliers in their requests to
 1241 the Connecticut Commission for increased payment. However, these requests
 1242 were denied by the Connecticut Commission, which was unwilling to increase
 1243 short term retail rates. By May 2003, NRG declared bankruptcy. CL&P was
 1244 forced to buy replacement power at high prices. The issue was litigated at the
 1245 FERC and the FERC eventually ruled that NRG was obligated to supply power.
 1246 This ruling was upheld on appeal; both NRG and CL&P settled in November
 1247 2003.

1248 **Q. Do subsequent solicitations for Standard Offer Service in Connecticut**
 1249 **include a price-taker option?**

1250 A. No.

1251 **Q. Would you please now consider the third proposed modification, namely the**
 1252 **proposal of smaller tranche sizes?**

1253 A. The Auction Process as proposed specifies that the tranches will be roughly 100
 1254 MW of peak demand. Dr. Salant proposed that the tranche size be changed to 2
 1255 MW because he believes that “a larger tranche size would exclude some
 1256 generators” (ICC Staff Exhibit 1.0, p. 58 line 1302). Dr. Salant again identifies
 1257 bidders with generators, and identifies the auction product with generation

1258 capacity; as I have testified now extensively, I disagree with this rationale, which
1259 I believe is based on a confusion between the auction product and other standard
1260 wholesale products.

1261 I do not believe in the benefits of a tranche size as small as 2 MW. My
1262 experience as Auction Manager in New Jersey is that participation has been
1263 healthy and robust in auctions for fixed-price products that have all used a 100
1264 MW tranche (on an eligible load basis). In the past four years in New Jersey, I am
1265 not aware of any supplier or any other intervenor suggesting a smaller tranche
1266 size or arguing that this would increase competition. Furthermore, I understand
1267 that prospective suppliers in Illinois have expressed support for the 100 MW
1268 tranche size.

1269 While I do not believe that there are benefits to a smaller tranche size, I do
1270 believe that smaller tranches can unnecessarily burden the Auction Process. I
1271 would expect a small tranche size such as 2 MW to slow down the auction as
1272 bidders have more combinations to evaluate and could take more time to decide
1273 on their bids. I would expect a small tranche size to unnecessarily burden bid
1274 processing and monitoring. I understand that the possibility of winners of very
1275 small tranches may present specific administrative challenges for the RTO.
1276 Finally, as a general point, I believe that making such a change without
1277 undertaking a thorough analysis of whether it affords bidders additional gaming
1278 opportunities would be ill-advised.

1279 I understand that in response to concerns about tranche size, Ameren has
1280 agreed to a 50 MW tranche size. I believe that the observations I make above

1281 about the potential costs of a smaller tranche size do not apply to a 50 MW
1282 tranche.

1283 **Q. Do you then believe that Ameren’s proposal to revise the tranche size to 50**
1284 **MW does not present any problems for the success of the Auction Process?**

1285 A. That is correct.

1286 **Q. Would you please now consider the fourth proposed modification, namely**
1287 **the recommendation that bidders be required to reveal to the Auction**
1288 **Manager any contracts that are contingent on the auction outcome?**

1289 A. Dr. Salant’s supports this recommendation by stating that it is necessary to
1290 prevent a situation in which a single wholesale supplier enters into contracts to
1291 provide wholesale products to several independent bidders. Let’s remember that
1292 the nature of competition in the auction is to provide risk-management services
1293 from products assembled in the wholesale market. When wholesale market
1294 players make products available to bidders on a contingent basis, they enable
1295 bidders to compete by enhancing those products with their own risk management
1296 additions. Further, as Mr. Ogur explains in his testimony, remote generators may
1297 use a non-physical delivery strategy:

1298 A physical player could sell energy, capacity and ancillary services from
1299 owned units in the PJM markets and could purchase these same products
1300 in the MISO markets either before or after the auction, so as to satisfy the
1301 Companies’ tranche requirements. I refer to this general strategy as the
1302 Non-Physical Delivery Strategy (ICC Staff Exhibit 4.0, lines 301-305).

1303 Wholesale suppliers can provide to auction participants wholesale forward
1304 products. While Mr. Ogur also explains that some entities may rationally choose
1305 to bid partially naked, others will seek wholesale market players that may be
1306 offering contingent contracts or options to purchase supply. These offers would

1307 have a beneficial effect on the auction. They would enable the basic wholesale
1308 products to be available to a wide range of competitors in the auction. This
1309 enables the competitors in the auction to compete in assembling products,
1310 managing risks and assessing risks. It expands competition for the auction
1311 product and is good for customers.

1312 Dr. Salant believes that a situation where a wholesale supplier contracts to
1313 supply several independent bidders must be stopped because it allows the
1314 wholesale supplier to “circumvent the purpose of the load cap” (ICC Exhibit 1.0
1315 p. 88 line 2008) and because it is a “collusive arrangement” (ICC Exhibit 1.0 p.
1316 88 line 1998). Most emphatically, the situation considered by Dr. Salant does not
1317 circumvent the purpose of the load cap and is not a collusive arrangement on its
1318 face. First, the purpose of the load cap is explained in great detail earlier in this
1319 testimony and it certainly does not include limiting a wholesale supplier who is
1320 not participating in the auction from selling its energy on a forward basis, to
1321 auction participants or to anyone else. Second, a collusive arrangement is an
1322 agreement among several parties to act in concert for the purposes of keeping
1323 prices higher than they would be if they were to compete with each other. If the
1324 bidders that have purchased products from the same wholesale supplier were
1325 communicating with each other while participating in the auction, it would be
1326 collusion. However, bidders will, under the Associations and Confidential
1327 Information rules, certify that they will have no such communication. If these
1328 bidders were communicating with the wholesale supplier, so that the wholesale
1329 supplier would serve as a conduit to guide the behavior of the bidders toward a

1330 coordinated outcome in the auction, it would be collusion. However, again,
1331 bidders will, under the Associations and Confidential Information rules, certify
1332 that they will have no such communication. If the wholesale supplier had the
1333 ability to specify contract provisions to ensure that bidders would bid to a
1334 coordinated outcome, the wholesale supplier again could be serving as a conduit
1335 for collusion. However, again, bidders will, under the Associations and
1336 Confidential Information rules, certify that their supply arrangements do not
1337 contain provisions that direct their behavior in the auction. If each bidder was
1338 aware that the others also had contracts with the same wholesale supplier,
1339 although this would not be collusion, it could certainly bias the competition at the
1340 auction since these bidders would have superior information about each other.
1341 However, bidders will, under the Associations and Confidential Information rules,
1342 certify that they have no such knowledge. In short, the Association and
1343 Confidential Rules are designed to foresee and minimize the possibility of
1344 collusion. A situation in which a wholesale supplier competes with other
1345 wholesale suppliers to provide various auction participants with wholesale
1346 products is not a collusive arrangement. There is no reason to believe that this
1347 situation does anything except facilitate competition for the auction product as the
1348 wholesale supplier more widely disseminates its wholesale supplies. Therefore
1349 there is no reason to believe that additional disclosures under the Association and
1350 Confidential Information Rules are required to deal with this situation.

1351 What is more, I firmly believe that requiring these additional disclosures,
1352 even if these disclosures are protected, can only have a negative impact on the

1353 Auction Process. I believe that bidders will at best be reluctant to reveal their
1354 sources of supply and the Auction Manager would have no authority to require
1355 disclosure from a wholesale supplier that is not participating in the auction. Any
1356 contractual arrangements will be considered extremely sensitive business
1357 information. It will be unclear to bidders – as it is to me – what would be done
1358 with this information or how it could be effectively used to promote competition
1359 in the auction. Such disclosure requirements, if properly structured will have a
1360 chilling effect on participation as bidders will refuse to provide sensitive business
1361 information. Such disclosure requirements, if improperly structured, may well
1362 simply increase supplier costs as suppliers enter into more complicated contracts
1363 to avoid the need to disclose. The ultimate consequence on the auction of one or
1364 both of these effects of adding the disclosure requirements is to reduce
1365 competition or increase costs to suppliers, both of which can be expected to have
1366 a negative effect on price.

1367 **Q. Are there other recommendations that relate to the competitive safeguards in**
1368 **the Auction Process that are made by witnesses in this proceeding?**

1369 A. Yes. Dr. Salant offers two additional recommendations related to competitive
1370 safeguards.

1371 The first is a recommendation regarding the auction volume guidelines.
1372 Dr. Salant points out that bidders may not be interested in all products equally. To
1373 avoid a situation where one product is very competitive while another is not, Dr.
1374 Salant recommends that the Auction Manager have “the discretion to increase the
1375 auction volume for products with excess supply as well as to decrease the auction

1376 volume of products for which supply offers are limited.” (ICC Exhibit 1.0 p. 60,
1377 lines 1339-1342).

1378 The second is a recommendation regarding the Association and
1379 Confidential Information Rules. Citing the need for transparency, Dr. Salant
1380 recommends that “all relevant information should be made public except such
1381 information that would adversely affect the outcome of the auction from the
1382 perspective of ratepayers.” (ICC Exhibit 1.0 p. 52, lines 1172-1174). This relevant
1383 information would include all information provided to bidders and to the Auction
1384 Manager, including the lists of bidders, bidder associations, and round-by-round
1385 bid results.

1386 **Q. Do you believe that these recommendations will improve the Auction**
1387 **Process?**

1388 A. No, I do not.

1389 I will first consider the recommendation that the Auction Manager be
1390 allowed to change the tranche targets of the various products during the auction
1391 on the basis of the interest expressed by bidders. I can only make sense of this
1392 recommendation by presuming that Dr. Salant is considering exclusively
1393 changing the tranche targets of various BGS-FP products in the first auction, each
1394 product having a different term, but serving the same group of customers.
1395 Understood any other way, this recommendation is illogical. The recommendation
1396 cannot possibly apply to BGS-FP products in the second and subsequent auctions
1397 because Ameren is proposing a single contract term of three years for BGS-FP
1398 products. There is no opportunity to change the targets of the various BGS-FP

1399 products in the second and subsequent auction because there is a single BGS-FP
1400 product. The recommendation cannot possibly apply to changing the targets of the
1401 BGS-FP product and the BGS-LFP product. These products serve different
1402 customers. Increasing the tranche target for the BGS-FP product and decreasing
1403 the tranche target for the BGS-LFP product, for example, would mean purchasing
1404 more than what residential and small business customers need, while purchasing
1405 less than what the large commercial and industrial customers need.

1406 Narrowly interpreting this recommendation to apply only to BGS-FP
1407 products in the first auction, I believe that this recommendation should be rejected
1408 and that it is likely harmful to the Auction Process.

1409 It is my experience from various auctions that bidder interest evolves as
1410 the auction progresses. In the early stages, bidding patterns are not always
1411 indicative of final interest, and in some cases early bidding patterns can be quite
1412 misleading. Some bidders may simply not be following relative prices at these
1413 stages, some bidders will likely change their valuations of certain products as they
1414 get information regarding excess supply, while other bidders will be assessing the
1415 competition for various products in an attempt to make final strategic decisions
1416 regarding their true targets. It is not uncommon for a product for a given supply
1417 period to have relatively low interest early in the auction and to catch up with
1418 other products for other supply periods at some point in the auction. A product
1419 can also attract less interest relative to others and yet this interest is steady and
1420 continues beyond price points at which other products clear. The auction is
1421 designed so that the relative prices for the various substitute products are

1422 discovered through the auction and so that these relative prices track the realities
1423 of the market. The judgment of the Auction Manager, even if exercised in
1424 accordance with a rule pre-established on the basis of expected bidding patterns,
1425 is a poor substitute for this market mechanism. This judgment is even more likely
1426 to be mis-applied as bidders should be expected to strategically respond to such
1427 adjustments, and will devote time and effort to influence the final tranche
1428 allocation.

1429 I will next consider the suggestion that auction information be made
1430 public. I agree with Dr. Salant that the most important consideration is that such
1431 information revelation not adversely affect the outcome of the auction from the
1432 perspective of ratepayers. However, I disagree with Dr. Salant in that I believe
1433 that making auction information public will in general have just such an adverse
1434 effect. Let's remember that auction participants can be expected to be active in
1435 other energy markets, including in trading for products that will be used as inputs
1436 to the auction products. If information about their auction participation were
1437 public, it could impede their other business dealings by revealing important
1438 information regarding their competitive positions, and it could directly impair
1439 their bargaining position when making supply arrangements for the auction. The
1440 ultimate effect on the auction outcome would be to raise price – either because
1441 making auction information public would have a chilling effect on auction
1442 participation or because it could directly raise the cost of supply arrangements that
1443 bidders negotiate to participate in the auction.

1444 I understand that Dr. Salant here is again considering the spectrum
1445 auctions as the model for this recommendation. As I have testified, in spectrum
1446 auctions, bidders are acquiring an input that will allow them to participate or to
1447 expand their participation in a downstream service market; this situation is
1448 different from the proposed Auction Process in which bidders are bidding to
1449 provide a service to customers, but must acquire inputs at the best terms possible
1450 in order to participate successfully. Revealing their participation in the auction,
1451 their bids, or the auction price in a given round can negatively affect their ability
1452 to acquire wholesale market inputs or can affect their other market dealings.

1453 That being said, once the auction has concluded, and once there have been
1454 ample opportunities for any bidder that had participated “naked” in the auction to
1455 make suitable arrangements to serve load won at the auction, some auction
1456 information can be revealed without harm. Certainly, the names of the winners,
1457 with the price for each product and the amount of tranches of each product won
1458 by each winner, can be released. As well, information regarding the prices and a
1459 measure of excess supply for each round could in most circumstances be publicly
1460 released. These data would then anchor the description of the auction provided in
1461 public version of the Auction Manager Report. Such information could no longer
1462 harm bidders in the auction as bidders would have had time to make any needed
1463 supply arrangements. However, in the special case where the auction volume had
1464 been cut back, I believe that the Auction Manager should be able to recommend
1465 to Staff that some round information not be released. The Auction Manager would
1466 make such a recommendation if this round information would enable suppliers to

1467 “backward engineer” certain aspects of the auction volume guidelines. As I
1468 discuss in Section 5 below, the auction volume guidelines cannot be released to
1469 bidders without compromising the integrity of the Auction Process; by the same
1470 token, round information that allow inferences regarding the auction volume
1471 guidelines should also be avoided. I would recommend that Staff retain the
1472 ability to redact round information, and that this discretion be exercised in case of
1473 a volume cutback if round information could be used to make inferences
1474 regarding the auction volume guidelines.

1475 **Q. For most of the measures that have been proposed regarding competitive**
1476 **safeguards, you do not believe that these would improve the Auction Process.**
1477 **Which of these recommendations do you believe are potentially most harmful**
1478 **to customers and should definitely be rejected?**

1479 A. I believe that there are three such recommendations: the price-taker proposal, the
1480 modifications to information disclosures (i.e., the requirements for disclosures of
1481 contract arrangements by bidders and the requirements for public disclosure of all
1482 auction information) and the recommendation to adjust the tranche target of each
1483 product. I have testified above as to the reasons for my believing that these
1484 proposals are harmful.

1485 **Q. Do you believe that the competitive safeguards as proposed in the Auction**
1486 **Process will be effective in promoting the competitiveness of the Auction**
1487 **Process?**

1488 A. I do.

1489 I believe that a load cap set in the 33% to 50% range will be effective in
 1490 providing a degree of supplier diversification, in reducing incentives to withdraw
 1491 strategically, in reducing incentives to overstate interest, while not overly
 1492 constraining the participation of the bulk of the anticipated pool of bidders. I
 1493 believe that the main principles of the auction volume guidelines as already
 1494 specified provide a sound basis for the Auction Manager to cut back the volume if
 1495 interest at the auction is lower than expected. The contingency plan in case of a
 1496 volume cutback appropriately ensures that bidders do not have an opportunity to
 1497 contract with Ameren to serve load except through the auction. The Association
 1498 and Confidential Information Rules appropriately guard against anti-competitive
 1499 behavior while not putting undue burdens on bidders. I believe that these
 1500 measures, taken as a whole, will be effective in promoting participation, and in
 1501 ensuring that reasonable protections are in place against anti-competitive behavior
 1502 so that the Auction process can deliver reliable supply at competitive market
 1503 prices.

1504

1505 **4. The Costs and Benefits of Permitting Switching Across Products Need To Be**
 1506 **Carefully Evaluated**
 1507

1508 **Q. Please describe the purpose of this section of your rebuttal testimony.**

1509 A. In this section, I respond to the positions put forth by certain Staff and intervenor
 1510 witnesses that there should be a single auction with switching among all products.

1511 A “single auction” in this context would be mean a fully consolidated auction, e.g.

1512 same schedule, same Auction Manager, auction rules, etc. with all utility products
1513 offered simultaneously, with switching allowed across all products.

1514 **Q. Please summarize rules for switching in the Auction Process originally**
1515 **proposed by Ameren in its filing in February.**

1516 A. The Auction Process as proposed by Ameren in its direct case filed in February
1517 did not anticipate a single auction as conceived by Staff and intervenors, but did
1518 foresee that eventually there would be simultaneous joint auctions for Ameren
1519 and ComEd products. By simultaneous joint auctions I mean that all products for
1520 ComEd and Ameren would be auctioned at the same time in a joint process and
1521 on a single schedule, but that bidders would not be able to switch from a ComEd
1522 product to an Ameren product or vice-versa. Furthermore, although a bidder
1523 would be able to switch between the BGS-FP and BGS-LFP products, and among
1524 the BGS-FP products of various terms in the first year, a bidder would not be able
1525 to switch from the hourly BGS-LRTP product to a fixed-price BGS-FP or BGS-
1526 LFP product or vice-versa.

1527 Resp. Ex. 12.5 (a) summarizes in diagrammatic form the groups of
1528 products amongst which a bidder can switch under the original proposal. In this
1529 exhibit, the product “groups” delineate where switching can occur. The four
1530 groups within which switching can occur are: 1) the ComEd CPP Group within
1531 the Fixed Price Section; 2) the Ameren BGS Group within the Fixed Price Section
1532 (formerly referred to as the Fixed Pricing Segment); 3) the ComEd CPP Group
1533 within the Hourly Price Section; and 4) the Ameren BGS Group within the
1534 Hourly Price Section (formerly referred to as the Spot Market Segment).

1535 Switching is allowed within any of the four groups, but is not allowed across
1536 groups.

1537 **Q. Please describe the positions of Staff and intervenors with respect to**
1538 **switching across products in the proposed Auction Process.**

1539 A. Certain Staff and intervenor witnesses argue that the auction should allow for a
1540 greater level of switching than that originally proposed by Ameren. Staff witness
1541 Salant (Staff Exhibit 1.0 at lines 770-774) recommends that switching be
1542 permitted across utilities and across all products (including the products for large
1543 customers taking hourly-price service). Dr. Salant indicates (Staff Exhibit 1.0 at
1544 lines 919-923) that he is relying on the analysis of Staff witness Ogur to support
1545 his recommendation. Mr. Ogur argues that the reasons presented by Ameren in
1546 its direct case for switching between ComEd and Ameren products not being
1547 allowed are unconvincing. Mr. Ogur presents a number of hypothetical bidder
1548 strategies that he believes would permit bidders to effectively switch across
1549 utilities.

1550 IIEC witness Dauphinais (IIEC Exhibit 2 at lines 88-90) argues that
1551 parallel auctions (without switching across utilities) will result in higher clearing
1552 prices than a fully-integrated auction (with switching across utilities).

1553 **Q. Have suppliers active in this proceeding taken a position on switching?**

1554 A. No supplier argues that Amren's auction design proposal should incorporate more
1555 switching across products – i.e., switching in addition to what was originally
1556 proposed by Ameren and depicted in Resp. Ex. 12.5 (a). Dynegy witness
1557 Huddleston (Dynegy Exhibit 1.0 at lines 212-214) does recommend that ComEd

1558 and Ameren seek uniformity in their auction documents so as to “facilitate the
1559 eventual move to a single simultaneous and, perhaps, joint auction for each type
1560 of product.” CCG Witness Smith proposes that “separate auctions be held during
1561 the same general time period but not at the same time.” (CCG Exhibit 1.0, page
1562 4, lines 118-119). Hence, under Mr. Smith’s proposed process for the first
1563 auction, switching would not be permitted across the products of the different
1564 utilities.

1565 **Q. Is it your opinion that switching can have benefits in an auction of the type**
1566 **proposed by Ameren?**

1567 A. Yes. Switching across of the various utilities is permitted in each of the New
1568 Jersey BGS-FP and BGS-CIEP Auctions, and I believe that this yields benefits for
1569 the customers of the New Jersey utilities. I believe switching makes sense when
1570 the products in the auction are good economic substitutes for one another in the
1571 bidders’ business plans. In these cases, switching can increase competition and
1572 switching allows prices to reflect the market more accurately.

1573 **Q. Is it your opinion that switching can have costs in an auction of the type**
1574 **proposed by Ameren?**

1575 A. Yes, the benefits of allowing switching must be evaluated against its costs. There
1576 are two main costs. The first is that allowing switching across all products limits
1577 the information available to the Auction Manager to make an informed decision
1578 regarding the appropriate volume in the auction. The second is that allowing
1579 switching across a certain group of products means that the Commission will have
1580 to make a single approval decision with respect to all the products of the group.

1581 Doing otherwise would create substantial uncertainty for the bidders who in
1582 switching from one product to another would put themselves at risk of switching
1583 to a product for which the result would end up being rejected. Mr. Dauphinais
1584 raises the issue that there could be approval concerns (i.e., there would be “a risk
1585 that an unsatisfactory price result in one load zone could require the Commission
1586 to also throw out a satisfactory price result in the other load zone”; IIEC Exhibit 2
1587 at lines 156-158).

1588 **Q. Has Ameren modified its proposal to respond to concerns of Staff and the**
1589 **IIEC with respect to switching in the Auction Process?**

1590 A. Yes. My understanding is that Ameren has agreed to an Auction Process that
1591 permits switching between the fixed-price products of ComEd and the fixed-price
1592 products of Ameren, and also permits switching between the hourly-price
1593 products of ComEd and the hourly-price products of Ameren, but does not permit
1594 switching between fixed-price products and hourly-price products. This revised
1595 structure is depicted in Resp. Ex. 12.5 (b). In this structure, switching is
1596 permitted in each Section, but is not permitted across Sections.

1597 **Q. Please provide your opinion on the decision not to permit switching between**
1598 **the hourly-price product and the fixed-price products in Ameren’s revised**
1599 **proposal.**

1600 A. I believe that Ameren’s decision not to allow switching between the hourly-price
1601 product (BGS-LRTP) and the fixed-price products (BGS-FP and BGS-LFP) is the
1602 right one. The BGS-FP and BGS-LFP products are not good substitutes for the
1603 BGS-LRTP product because the products would not hold the same place in the

1604 bidder's business plan. BGS-FP and BGS-LFP products are fixed-price products.
1605 The bidder offers a fixed price to provide all components of the full-requirements
1606 service that have costs that can be highly variable. To be successful, the bidder
1607 must make good predictions of future energy costs, make the best assessment of
1608 the opportunity to serve Ameren load, and devise the best strategy to hedge the
1609 risks associated with all its future supply costs. The bidder's success critically
1610 depends on its success in predicting future energy prices and the relevant Ameren
1611 load that it will be serving in any given hour.

1612 Capacity is a component of the full-requirements service. The BGS-FP
1613 and BGS-LFP products as well as the BGS-LRTP product require the supplier to
1614 indicate the capacity resources upon which the supplier is relying. The capacity
1615 component typically represents roughly 10% of the cost of an overall fixed-price
1616 product in the New Jersey BGS context and I see no reason to believe it would be
1617 radically different for Ameren. It is possible that supply arrangements for
1618 capacity for BGS-FP and BGS-LFP products could be transferred to the BGS-
1619 LRTP product but substitutability of the supply arrangements of this one
1620 component does not imply that the BGS-FP and BGS-LFP products are economic
1621 substitutes for the BGS-LRTP product.

1622 I believe that the BGS-FP and BGS-LFP products are not good economic
1623 substitutes for the BGS-LRTP product because BGS-FP and BGS-LFP suppliers
1624 take radically different risks from BGS-LRTP suppliers and the characteristics of
1625 the revenue streams for the BGS-FP and BGS-LFP products are different from
1626 those of the BGS-LRTP product. As Mr. Parece notes in his testimony in Docket

1627 05-0159, a cost of allowing switching is that it creates opportunities for strategic
1628 bidding that can be detrimental to the auction. Bidders can send false signals as to
1629 their level of interest in specific products. While this cost is small in comparison
1630 to the benefits of switching when products are close substitutes it becomes larger
1631 as the products are not as good substitutes. I agree with this point.

1632

1633 **Q. Please provide your opinion on the decision to permit switching between the**
1634 **hourly-price products of ComEd and Ameren, as well as between and the**
1635 **fixed-price products of ComEd and Ameren.**

1636 A. I believe that there are both costs and benefits to this kind of switching and that it
1637 is reasonable to believe that switching is on balance beneficial at this time. There
1638 are certain strategies that could be employed today by bidders such that the
1639 components of the fixed-price CPP products could be substitutable for
1640 components of the fixed-price BGS products, with the same holding true for the
1641 hourly products. This is explained by Staff witness Ogur, who posits that
1642 “bidders can work around the RTO seams to effectively switch between the
1643 products of the two utilities at the current stage of the MISO and PJM joint and
1644 common market.” (ICC Staff Exhibit 4.0, lines 178-180). Mr. Ogur presents
1645 examples of how bidders with physical supply resources in PJM could use those
1646 resources to bid on the Ameren products. He also recognizes that physical
1647 resources are not needed to participate in the auction and that financial players
1648 may benefit from being able to switch between the products of ComEd and

1649 Ameren. The rationale put forth by Mr. Ogur comports with my understanding of
1650 the RTOs and potential bidder supply strategies.

1651 Furthermore, the benefits can only be expected to increase with time. The
1652 PJM and MISO RTOs have been ordered by the FERC to implement a joint and
1653 common market and they have commenced efforts to implement such a market.
1654 As the PJM and MISO markets become more aligned, the CPP and BGS products
1655 will become, in my opinion, closer economic substitutes than they are today.

1656 **Q. If switching is allowed, would it require modifications to the basic design of**
1657 **the auction?**

1658 A. Yes. I believe that the elements of the auction design that would require
1659 modifications would include the following:

- 1660 • Associations and confidential information rules;
- 1661 • Definition of eligibility;
- 1662 • Definition and report of excess supply;
- 1663 • Calculation of price decrements.

1664
1665 **Q. Are these changes incorporated in the documents filed by Ameren in its**
1666 **rebuttal testimony?**

1667 A. No. I have worked with ComEd and with Ameren to develop a single set of
1668 documentation that would be used to implement the simultaneous auction should
1669 the ICC approve the Auction Process, but such documents do not yet incorporate
1670 a single auction with switching.

1671 These documents include:

- 1672 • Draft Auction Rules for a Simultaneous Auction (Resp. Ex. 12.4)

- 1673 • Draft Part 1 and Part 2 Application Forms that accommodate applicants
1674 wishing to bid on any and all of the auction products (Resp. Ex. 12.1 and
1675 12.2)
- 1676 • Draft Appendices to Application Forms
 - 1677 ○ Description of Alternate Guaranty Process and Approval Criteria
 - 1678 ○ Pre-auction Letters of Credit
 - 1679 ○ Sample Letters of Reference
 - 1680 ○ Sample Letter of Intent to Provide a Guaranty
 - 1681 ○ Description of Process and Approval Criteria for Modifications to the
1682 Letters of Credit.

1683 **Q. Are these documents identical to those submitted in Docket No. 05-0159?**

1684 A. The Part 1 and Part 2 Application Forms and Appendices are identical. The draft
1685 Auction Rules are very similar, but not identical. I have revised the draft rules to
1686 correct for typographical errors and to highlight one of the areas where the
1687 ComEd and Ameren proposals may need to be harmonized in order to permit
1688 switching across the fixed-price products of ComEd and Ameren and the hourly-
1689 price products of ComEd and Ameren. This relates to the Bidder Participation
1690 Fee, which is included as part of the ComEd proposal but is not anticipated by
1691 Ameren. ComEd anticipates that all Registered Bidders will pay a “Bidder
1692 Participation Fee” designed to contribute to the costs of the auction. (The balance
1693 of the costs will be recouped through the Supplier Fee.) Ameren’s proposal does
1694 not anticipate a Bid Participation Fee, but anticipates that the total costs of the
1695 auction will be recovered in a supplier fee (termed “Auction and Administration
1696 Fee”). This is one of the many aspects of the Illinois Auction Rules that can be
1697 expected to be adapted to accommodate the switching that ComEd and Ameren
1698 have accepted in their respective rebuttal filings. Other auction documents will
1699 need to be adapted as well.

1700 **Q. Do you believe that the documents are responsive to the request by Mr.**
1701 **Huddleston on behalf of Dynegy?**

1702 A. Yes, I do. Mr. Huddleston argues “to the greatest extent possible, the Auctions,
1703 their rules, the supplier contracts, and the tariffs related to them should be uniform
1704 as between ComEd and the Ameren Utilities. We recognize that for various
1705 reasons (e.g., because ComEd and the Ameren Utilities operate within different
1706 RTOs and, as of now, the seams issues between those RTOs have not been fully
1707 resolved), there cannot be complete uniformity. However, there should be as
1708 much uniformity as possible.” (Dynergy Exhibit 1.0 p. 10, lines 205-210). I
1709 believe that the documents represent substantial efforts to achieve uniformity.

1710 **Q. Can you now please provide a description of the Part 1 Application Form for**
1711 **the Illinois Auction?**

1712 A. Certainly. An applicant uses the Part 1 Application to become a Qualified Bidder
1713 in any one, several of, or all of the “Groups” in the Illinois Auction.

1714 As represented in Resp. Ex. 12.5(a), the Illinois Auction consists of two
1715 Sections, a Fixed Price Section and an Hourly Price Section. Each Section has
1716 two Groups. The Fixed Price Section has a CPP Group (consisting of the 17-
1717 month CPP-B product, the 29-month CPP-B product, the 41-month CPP-B
1718 product, the 53-month CPP-B product, the 65-month CPP-B product, and the
1719 CPP-A product for ComEd), and a BGS Group (consisting of the 17-month BGS-
1720 FP product, the 29-month BGS-FP product, the 41-month BGS-FP product, and
1721 the 17-month BGS-LFP product for Ameren). The Hourly Price Section has a
1722 CPP Group (ComEd’s 17-month CPP-H product), and a BGS Group (Ameren’s
1723 17-month BGS-LRTP product).

1724 In the Part 1 Application, applicants provide basic information regarding
1725 their entities. Each applicant names an Authorized Representative and a
1726 Registered Agent. An Authorized Representative is an individual who represents

1727 the applicant in the Illinois Auction. The Authorized Representative is responsible
1728 for all confidential information regarding the auction process received from the
1729 Auction Manager and is responsible for distributing this confidential information
1730 only to other individuals who are authorized to act on behalf of the applicant. The
1731 Authorized Representative can also name a Delegate to be the point of contact
1732 with the Auction Manager for bidding in a particular Group. The Registered
1733 Agent is located in Illinois. The Registered Agent is authorized and agrees to
1734 accept service of process on the applicant's behalf.

1735 Applicants agree to the Illinois Auction Rules and to the terms of the
1736 applicable Supplier Forward Contract (depending on the service or services that
1737 they are applying to provide). Applicants declare to the Auction Manager any
1738 bidding agreements related to bidding in the auction. Applicants show that they
1739 fulfill general RTO requirements. Applicants for the BGS Groups certify that they
1740 are Market Participants in MISO; applicants for the CPP Groups show that they
1741 have executed the required agreements with PJM (or that they have no
1742 impediments to doing so in the future).

1743 An applicant who succeeds in the Part 1 Application process for a Group
1744 becomes a Qualified Bidder for that Group. Applicants will have certified that,
1745 should they become Qualified Bidders for a Group, they will hold the list of
1746 Qualified Bidders for that Group confidential.

1747 **Q. What are the appendices to the Part 1 Application?**

1748 A. Appendix A is a checklist of enclosures that should be provided with the Part 1
1749 Application.

1750 Appendix B is a sample attestation by the applicant's Chief Financial
1751 Officer to be used if the applicant cannot provide audited financial statements.

1752 Appendix C provides details concerning the Alternative Guaranty Process.
1753 Winning suppliers in the auction whose creditworthiness is assured through a
1754 guarantor can always use the standard form of guaranty appended to the
1755 applicable Supplier Forward Contract. They can also submit an alternate form of
1756 guaranty. Such an alternate form of guaranty can be approved according to the
1757 process described in Appendix C if it meets the conditions also stated in
1758 Appendix C. These conditions include, for example, that the guaranty be a
1759 financial and not a performance guaranty, and that the guaranty be unlimited (i.e.,
1760 not have a liability limit). Prospective bidders would apply to have their alternate
1761 guaranty form approved and would obtain a response from the Auction Manager
1762 before being required to submit to the Part 1 Application process. ComEd and
1763 Ameren would consider whether the alternate guaranty form is acceptable.

1764 Appendix D is a glossary of terms provided for the convenience of the
1765 applicants.

1766 **Q. Can you now please provide a description of the Part 2 Application Form for**
1767 **the Illinois Auction?**

1768 A. An applicant that has qualified for one, several, or all Groups (i.e., the Fixed Price
1769 BGS Group, the Fixed Price CPP Group, the Hourly Price BGS Group, and the
1770 Hourly Price CPP Group) uses the Part 2 Application to become a Registered
1771 Bidder for the Group(s) in question. A Qualified Bidder for a Group may (but
1772 need not) apply to become a Registered Bidder for that Group. A party that has

1773 not qualified for a Group by submitting to the Part 1 Application process may not
1774 apply to become a Registered Bidder using the Part 2 Application.

1775 Applicants for a Group provide an indicative offer for that Group. An
1776 applicant's indicative offer for a Group specifies the maximum number of
1777 tranches that the bidder is willing to serve at the maximum starting price and at
1778 the minimum starting price for the Group. Applicants in the Fixed Price Groups
1779 also provide a preliminary interest in each product at the maximum starting price
1780 and at the minimum starting price. Each applicant posts pre-auction security with
1781 the Part 2 Application to support its indicative offer at the maximum starting
1782 price. The pre-auction security includes a letter of credit of \$500,000 per tranche
1783 of the indicative offer at the maximum starting price. Applicants in Groups of the
1784 Fixed Price Section may also be required to provide a Letter of Reference from a
1785 bank or a Letter of Intent to Provide a Guaranty from their guarantor. The pre-
1786 auction security provides assurances that the applicant and/or its guarantor would
1787 be able to meet the creditworthiness requirements of the Supplier Forward
1788 Contract. This is in addition to the other role that pre-auction security fulfills,
1789 namely that of assuring serious offers at the indicative stage.

1790 Applicants for a Group make the certifications required by the
1791 Associations and Confidential Information rules (see Resp. Ex. 12.4) or disclose
1792 any information to the Auction Manager necessary to explain why the
1793 certification cannot be made.

1794 **Q. What are the appendices to the Part 2 Application?**

1795 A. Appendix A is a checklist of enclosures that should be provided with the Part 2
1796 Application.

1797 Appendix B is a glossary of terms provided for the convenience of the
1798 applicants.

1799 Appendix C provides sample Pre-Auction Letters of Credit that applicants
1800 would use to support their indicative offers at the maximum starting price.

1801 Appendix D provides sample Letters of Reference that applicants to the
1802 Fixed Price Groups would use if required to submit such a letter under the
1803 creditworthiness evaluation made in the Part 1 Application.

1804 Appendix E provides a sample Letter of Intent to Provide a Guaranty that
1805 the guarantor of an applicant to a Fixed Price Group would use if required to
1806 submit such a letter under the creditworthiness evaluation made in the Part 1
1807 Application.

1808 Appendix F provides a procedure by which Qualified Bidders can ask for
1809 non-material changes to the standard form of the Pre-Auction Letter of Credit.
1810 These changes may be requested by the applicant's bank to clarify the intent of
1811 the language in the pre-auction letter of credit. Such changes would be submitted
1812 to the Auction Manager and would be approved by ComEd and Ameren.

1813 **Q. Can you now please provide a description of the bidding rules for the Illinois**
1814 **Auction?**

1815 A. Certainly. The auction is a simultaneous, multiple round descending clock
1816 auction. The auction simultaneously procures supply for all products, namely for

1817 all load categories for both ComEd and Ameren (i.e., BGS-FP, BGS-LFP, BGS-
1818 LRTP, CPP-B, CPP-A, and CPP-H) and for all contract terms.

1819 The auction proceeds in rounds. In each round, bidders submit bids, bids
1820 are tabulated, and bidders are provided information on the general progress of the
1821 auction. The auction is a descending clock because prices tick down until there is
1822 just enough supply to meet the requirements.

1823 **Q. You mention that the auction has several products. Is a bidder able to bid on**
1824 **any and all products in the Illinois auction?**

1825 A. In general, no. A bidder only is able to bid on the products that are included in the
1826 Groups for which the bidder has qualified and registered. To bid on any and all
1827 products in the Illinois auction, a bidder would have had to qualify and register to
1828 bid for all four Groups.

1829 **Q. You mention that the auction proceeds in rounds. In the first round, can a**
1830 **bidder in a Group bid any number of tranches for that Group?**

1831 A. No. There is a maximum number of tranches that a bidder in a Group can bid for
1832 that Group. That maximum number of tranches is the bidder's indicative offer at
1833 the maximum starting price submitted in the Part 2 Application. There is no
1834 minimum number of tranches that a bidder in a Group must bid for that Group.

1835 **Q. Can you please describe how bidding will proceed for the Hourly Price**
1836 **Groups in the first round?**

1837 A. The Auction Manager announces the price for the BGS-LRTP product and for the
1838 CPP-H product. The bidding phase of the round opens. In the bidding phase,
1839 bidders in a Group submit a bid for the product in that Group. A bid is the number
1840 of tranches that the bidder is willing to serve at the round 1 price. A bidder in both
1841 Groups submits a number of tranches for each of the products, the BGS-LRTP
1842 product and the CPP-H product.

1843 When the bidding phase closes, the calculating phase begins. The Auction
1844 Manager calculates the total number of tranches bid for each product. The
1845 Auction Manager calculates the excess supply, i.e., the number of tranches bid in
1846 excess of the number of tranches needed. The Auction Manager determines the
1847 price for round 2 based on the amount of excess supply. The greater is the excess
1848 supply — the greater is the number of tranches bid in excess of the need — the
1849 more the price will tick down, and the lower will be the round 2 price.

1850 When the calculating phase closes, the reporting phase begins. The
1851 Auction Manager provides to all bidders a range of excess supply for each Group,
1852 and the Auction Manager provides the price for round 2 for each product. Bidders
1853 will then be able to submit new bids when the bidding phase opens for round 2.

1854 **Q. How does round 2 proceed in the Hourly Price Groups?**

1855 A. The round proceeds in the same way as round 1. In the bidding phase, a bidder in
1856 the BGS Group bids the number of tranches of the BGS-LRTP product that the
1857 bidder is willing to serve at the round 2 price. A bidder in the CPP Group bids the
1858 number of tranches of the CPP-H product that the bidder is willing to serve at the
1859 round 2 price. In the calculating phase, the Auction Manager calculates the total

1860 number of tranches bid for each product across all bidders, calculates the excess
1861 supply, and determines the price for the next round (round 3) based on the amount
1862 of excess supply. In the reporting phase, the Auction Manager provides to the
1863 bidders the prices for round 3 and a range of excess supply for each Group.

1864 **Q. In round 2, can a bidder in an Hourly Price Group bid any number of**
1865 **tranches?**

1866 A. No. For each Group, the bidder can either: (a) bid the same number of tranches
1867 that the bidder bid in round 1; or (b) decrease the number of tranches bid from
1868 round 1. The bidder cannot increase the number of tranches bid for a Group. This
1869 will hold true in round 3 and all subsequent rounds as well.

1870 **Q. When a bidder in an Hourly Price Group is decreasing the number of**
1871 **tranches bid from one round to the next, does the bidder have to provide**
1872 **additional information to the Auction Manager?**

1873 A. Yes. If a bidder decreases the number of tranches bid from one round to the next,
1874 the bidder is required to name an exit price for the tranches it is withdrawing from
1875 the product in a Group. An exit price is a best and last offer on the tranches that
1876 the bidder is withdrawing, given that the bidder was willing to serve these
1877 tranches at the previous price but is no longer to serve this tranche at the current
1878 price. The Auction Manager will use an exit price in the last round of bidding if
1879 the tranches bid at the price of the final round are not sufficient to meet the need.

1880 **Q. Do round 3 and subsequent rounds of the Hourly Price Group proceed just**
1881 **as round 2?**

1882 A . Yes.

1883 **Q. Can you briefly summarize how the rules for the Groups in the Fixed Price**
 1884 **Section are in part the same and in part different from the rules for the**
 1885 **Groups in the Hourly Price Section?**

1886 **A.** Each Group in the Fixed Price Section has several products (while each Group in
 1887 the Hourly Price Section has a single product). There are additional rules for each
 1888 Group in the Fixed Price Section to accommodate the presence of multiple
 1889 products, but essentially the rules that I have explained so far apply to all Groups.

1890 To summarize, these rules are the same for all Groups:

1891 – Each round has a bidding phase during which bidders submit bids, a
 1892 calculating phase during which the Auction Manager tabulates the results,
 1893 and a reporting phase during which bidders are provided a range of excess
 1894 supply for each Group and the price for each product in the next round;

1895 – In round 1, a bidder cannot bid on more tranches in total in a Group than
 1896 its indicative offer at the maximum starting price for that Group;

1897 – In round 2 and each subsequent round, a bidder cannot bid on more
 1898 tranches in total for a Group than the bidder bid in the previous round for
 1899 that Group;

1900 – A bidder, when withdrawing tranches from a product in a Group, will
 1901 name an exit price for the tranches being withdrawn.

1902 The presence of multiple products in the Groups of the Fixed Price Section means
 1903 that a bidder can switch from one product to another within the Group. The
 1904 additional rules that are required in the Groups of the Fixed Price Section can be
 1905 summarized as follows:

1906 – If the price for a product in a Group has ticked down, a bidder in that
 1907 Group can maintain, increase or reduce the number of tranches bid on that
 1908 product. But if the price for a product has not ticked down, the bidder
 1909 cannot reduce the number of tranches bid on that product either by
 1910 withdrawing these tranches completely or by switching the tranches to
 1911 another product in the Group.

- 1912 – If a bidder is switching into several products, a bidder will be asked to
1913 provide switching priorities. A switching priority is a preference among
1914 the products for which the bidder is increasing the number of tranches bid.
- 1915 – To fill the tranche target for a product, the Auction Manager first takes
1916 tranches that are bid at the going price for the round, then if necessary the
1917 Auction Manager denies requests to withdraw, and finally, if necessary,
1918 the Auction Manager denies requests to switch from that product.
- 1919 – If a request to withdraw or to switch is denied, the bidder is committed to
1920 supply these tranches the tranches at the lowest price at which the bidder
1921 has freely bid them.
- 1922 – The final price for a product is the price of the final round (if at that price,
1923 there is just enough bid to fill the need for the product), or the previous
1924 price (if the Auction Manager must deny a switch in the last round), or an
1925 exit price (if the Auction Manager must deny withdrawals in the last round
1926 and does not need to deny a switch).

1927 As I note previously, these rules do not yet provide for switching between fixed-
1928 price Ameren and ComEd products or switching between hourly-price Ameren
1929 and ComEd products.

1930
1931

1932 **5. A Measured Approach to Auction Management Maximizes the Probability of**
1933 **a Successful Auction**
1934

1935 **Q. What is the purpose of this section of your testimony?**

1936 A. The purpose of this section of my testimony is:

- 1937 ■ To respond to Staff witness Salant’s characterization of Ameren’s proposal as
1938 being incomplete. I establish that the Ameren proposal is complete and that
1939 the proposal describes the key elements in sufficient detail for the
1940 Commission to make a ruling in this proceeding.
- 1941 ■ To respond to the positions taken by Staff witness Salant on issues related to
1942 the mechanics of auction management, and the roles of the parties involved.
1943 In so doing, I describe the approach to auction management that I believe will
1944 maximize the probability of a successful auction.

1945

1946 a. Completeness of Proposal

1947 **Q. Please summarize Dr. Salant’s testimony with respect to the completeness of**
 1948 **the Auction Proposal.**

1949 A. Dr. Salant asserts that the Auction Proposal as filed is not complete, and that
 1950 “many essential details” of the auction rules and procedures have been omitted.
 1951 (ICC Staff Exhibit 1.0 pp. 27-28, lines 618-620) He concludes that since the rules
 1952 are not complete and are missing essential details, any review of the merits of
 1953 Ameren’s proposal cannot be completed. (Id. lines 574-575) Further, he appears
 1954 to equate the fact that some details have not been specified with an intention for
 1955 the Auction Manager to exercise discretion rather than specifying the required
 1956 rule or procedure. Finally he observes in discussing auction management, that
 1957 “even small details pertaining to auction management can have a significant
 1958 impact on the outcome of the auction.” (Id. lines 1591-1593)

1959 **Q. Please respond to Dr. Salant’s conclusion that essential details are missing**
 1960 **from the filed auction rules and procedures and that as a result any review of**
 1961 **the merits can not be completed.**

1962 A. I believe that the levels of detail in my testimony, the testimony of Mr. Blessing
 1963 and Mr. Nelson, the filed Competitive Procurement Auction Rules, the filed
 1964 Supplier Forward Contracts, the Rate Translation Prism, and the filed MV tariff
 1965 speak for themselves. There is a wealth of information that is sufficient to judge
 1966 whether the Auction Process as incorporated in the tariff is a reasonable and
 1967 prudent way to purchase supply for Ameren’s customers. These materials define
 1968 the auction product and provide a rationale for the choice of product, define and
 1969 describe the auction format and explain why it will achieve the objectives of the

1970 Auction Process, describe the nature of the competitive safeguards that will be
1971 built in to the process, discuss Ameren's intentions with respect to the Auction
1972 Manager, and suggest roles for the utility, the Auction Manager, the ICC Staff and
1973 their Auction Advisor, and present the method by which auction prices will be
1974 translated into retail rates.

1975 This information is sufficient to enable the ICC to decide whether the
1976 auction product is properly defined, to decide whether the auction format can
1977 accomplish the objectives, to decide on the overall adequacy of the competitive
1978 safeguards, and to decide on the roles and responsibilities of the various entities.

1979 Dr. Salant appears to suggest that the ICC cannot evaluate if the Auction
1980 Process is reasonable and prudent as proposed unless the ICC can review in this
1981 proceeding all details of how exactly the implementation of the Auction Process
1982 will unfold. This fails to recognize that the ICC will, itself and through its Staff,
1983 maintain ongoing oversight and jurisdiction over the Auction process. The ICC
1984 Staff, with the assistance of their Auction Advisor as needed, will be involved in
1985 the implementation of the Auction Process and will have the ability to review the
1986 decisions taken by the Auction Manager. I discuss this in more detail later on in
1987 this section.

1988 **Q. Are there specific elements of the Auction Process that Dr. Salant states have**
1989 **not been specified and but for which you believe the substance of the**
1990 **proposal has already been advanced?**

1991 A. Yes. I believe that the essential elements of the auction volume guidelines and
1992 that the essential approach to setting minimum and maximum starting prices have

1993 been provided through the Competitive Procurement Auction Rules and through
 1994 responses to data requests.

1995 **Q. Could you please summarize the essential elements of the auction volume**
 1996 **guidelines?**

1997 A. Certainly.

1998 Description. The Auction Manager cuts back the volume only if necessary
 1999 to ensure a competitive bidding environment. Any volume not obtained through
 2000 the auction is procured through MISO-administered markets.

2001 Purpose. These measures are a safety net. The sole purpose of these
 2002 measures is to address a situation where participation is lower than expected and
 2003 where, in the absence of a volume cutback, auction prices may not reach
 2004 competitive levels.

2005 Mechanics. The mechanics can be described as follows.

- 2006 a. The Auction Manager measures competitiveness in round 1 by means
 2007 of the “eligibility ratio” (the ratio of the tranches bid divided by the
 2008 volume). If the eligibility ratio is below its target, the Auction
 2009 Manager cuts back the volume.
 2010 b. If the Auction Manager cuts back the volume, the new volume is set so
 2011 that the eligibility ratio meets its target.
 2012 c. The value of the target for the eligibility ratio could depend on various
 2013 factors, such as the number of bidders or the characteristics of
 2014 individual bids. For example.
- 2015 • The initial auction volume is 90 tranches
 - 2016 • The number of tranches bid in round 1 is 120 tranches
 - 2017 • The target eligibility ratio is 1.5
- 2018 The eligibility ratio does not meet its target. There are 1.33 tranches
 2019 bid per tranche available ($120 \text{ (tranches bid)} \div 90 \text{ (volume)} = 1.33$) but
 2020 the target is 1.5. The Auction Manager cuts back the volume from 90
 2021 to 80 tranches. This achieves the target of 1.5 tranches bid per tranche
 2022 available ($120 \text{ (tranches bid)} \div 80 \text{ (volume)} = 1.5$).
 2023 d. The Auction Manager can further revise the volume, if necessary to
 2024 ensure a competitive bidding environment.

2025 **Q. What elements would still need to be specified for the auction volume**
2026 **guidelines to be complete?**

2027 A. The elements that have not specified are how the target eligibility ratio will be set
2028 and how the further adjustment will proceed.

2029 **Q. Why have these elements not been specified and why are the parameters to**
2030 **be used not been provided?**

2031 A. To preserve the integrity of the Auction Process, I believe that these volume
2032 guidelines must stay confidential from bidders.

2033 If bidders knew the volume guidelines, they could manipulate the system.
2034 They could bid to show a higher level of competitiveness in round 1 than is
2035 actually the case. If bidders, knowing the guidelines, are able to hide the true level
2036 of competitiveness from the Auction Manager, and if the Auction Manager, had it
2037 known the true level of competitiveness, would have cut back the volume, then
2038 the auction will close at prices higher than they otherwise would have been.

2039 **Q. Will the Auction volume guidelines be a complete set of rules or will the**
2040 **Auction Manager exercise judgment during the auction to set the volume?**

2041 A. It is proposed that the Auction Manager not have any opportunity to exercise
2042 judgment in setting the volume during the auction.

2043 **Q. Could you please summarize the essential elements of the setting of the**
2044 **minimum and maximum starting prices?**

2045 A. Certainly.

2046 Description. The Auction Manager and Ameren, in consultation with ICC
2047 Staff, set a minimum starting price and a maximum starting price for each

2048 segment, i.e., separately for the Fixed Pricing Segment under the original rules
 2049 (the BGS Group of the Fixed Price Section in the rules just discussed) and the
 2050 Spot Market Segment under the original rules (the BGS Group of the Hourly
 2051 Price Section in the rules just discussed). Bidders submit indicative offers at the
 2052 minimum and at the maximum starting prices. The Auction Manager and Ameren,
 2053 in consultation with ICC Staff, set round 1 prices between the minimum and
 2054 maximum starting prices.

2055 Purpose: The minimum and maximum starting prices should be set high
 2056 enough to encourage participation. Competition will tick prices down to their final
 2057 levels. The range between the minimum and maximum starting prices should be
 2058 narrow enough to provide bidders with meaningful bounds on the eventual round
 2059 1 prices, but wide enough that the actual starting prices will fit within the range
 2060 even given changes in the market that may occur between the time at which the
 2061 minimum and maximum starting prices are released and the start of the auction.

2062 Mechanics:

- 2063 a. The minimum and maximum starting prices will be developed
- 2064 considering recent market data.
- 2065 b. These market data would include energy forward prices for standard
- 2066 products, capacity market data as available, congestion and wholesale
- 2067 transmission rates.
- 2068 c. The round 1 prices would take the indicative offer data into account.
- 2069

2070 **Q. What elements would still need to be specified for the starting price**
 2071 **methodology to be complete?**

2072 A. The elements that have not specified are the exact data being used, the precise
 2073 calculation of the range of minimum and maximum starting prices, and the

2074 manner in which the indicative offer data will be used to inform the setting of
2075 round 1 prices.

2076 **Q. Please address the assertion that this methodology should be released to**
2077 **bidders.**

2078 A. I do not believe this methodology should be released to bidders. Such a
2079 methodology if released could provide bidders with information that could be
2080 detrimental to the auction. Bidders could interpret values used in this
2081 methodology to be values that are implicitly acceptable to Ameren and the ICC
2082 Staff and hesitate to vigorously compete at price points below these levels.
2083 Effectively, bidders would be provided a price level that could serve as a focal
2084 point for simultaneous withdrawals and a seemingly collusive result. Bidders
2085 would be given target prices that could enable them to tacitly coordinate without
2086 any direct communication. This is a possibility that just cannot be dismissed.
2087 While it may not happen it is a significant downside of providing to bidders the
2088 methodology used to determine starting prices. In contrast, there is no upside to
2089 communicating to bidders how the ICC Staff, the Auction Manager and Ameren
2090 may value or evaluate the auction product. It is best to let sellers compete without
2091 a notion of the buyers' valuation and without a beacon for tacit collusion.

2092 **Q. Are there other specific procedures and details regarding the Auction**
2093 **Process that have not yet been fully specified?**

2094 A. I do not believe that there are any elements of the Auction Process that have not
2095 yet been specified and that are needed to understand or evaluate the proposal. I
2096 recognize that changes are required to accommodate the switching between

2097 ComEd and Ameren products that has been accepted by Ameren in its rebuttal
2098 filing, but was not foreseen in Ameren's direct filing in February and is not yet
2099 reflected in the Illinois Auction Rules. These merely reflect changes to the Rules
2100 and other auction documents, and not a lack of specificity. That said, there are
2101 certainly specific procedures for the implementation of the Auction Process that
2102 have not been specified. I believe it would be premature to specify them at this
2103 time. Many of the auction management details are appropriately resolved amongst
2104 the Auction Manager and the ICC Staff at the appropriate time, and would not be
2105 expected to be the subject of an ICC decision. Especially with clarifications
2106 provided in rebuttal, the auction rules and procedures have been addressed in
2107 sufficient detail to allow the ICC to fully evaluate and approve the Auction
2108 Process.

2109 **Q. Are there additional details provided as part of this rebuttal testimony?**

2110 A. Yes. I note that added detail including application forms, decrement rules, revised
2111 auction rules for a single auction, a more detailed specification of the reports
2112 provided to the ICC once the auction is concluded, as well as a description of the
2113 roles of the parties during the Auction Process are provided with Ameren's
2114 rebuttal testimony. (These are included as Resp. Exs. 12.1-12.7 to my testimony
2115 and as Resp. Ex. 11.2 to Mr. Blessing's testimony.) While these will enhance the
2116 information available to the ICC and make some of the proposals of the Auction
2117 Process more concrete, this supplemental information in my view is not required
2118 to determine if the Ameren proposal is in customers' best interests.

2119 **Q. Dr. Salant testifies that the parameters of price decrement formulas should**
2120 **be stipulated in advance but not revealed to bidders. What do you believe is**
2121 **the concern that this proposal is meant to address?**

2122 A. I believe that the concern is that bidders will use their knowledge of the
2123 decrement rules to infer the excess supply on a product-by-product basis. Each
2124 round, bidders are told the new going prices and the amount by which the price
2125 for each product has ticked down. If there is a function that links the amount by
2126 which a price ticks down to the amount of excess supply on a product, a bidder is
2127 able to “back out” the amount of excess supply for the product on the basis of
2128 knowing by how much the price for that product ticked down. This is more
2129 precise information regarding excess supply than is provided by the Auction
2130 Manager on an auction-wide basis each round.

2131 Knowing precisely the excess supply on a product-by-product basis can
2132 present a gaming opportunity. Bidders could potentially have sufficient
2133 information at the end of the auction to know exactly how many tranches need to
2134 be withdrawn to end the auction. A bidder could then find it profitable to close the
2135 auction at prices higher than they would otherwise have been the case.

2136 **Q. Is it your opinion that Dr. Salant’s proposal of keeping the price decrement**
2137 **formulas secret addresses this concern?**

2138 A. For the most part, yes, it does. If bidders do not know the exact parameters of the
2139 price decrement formulas they cannot, on the basis of seeing the amount by which
2140 a price ticks down, “back out” the excess supply on a product.

2141 However, I believe it is important to realize that there are limits to how
 2142 thoroughly this concern can be addressed by this or any other proposal. For the
 2143 auction to work well, there must be some relationship between the excess supply
 2144 on a product and the tick down on the product. In fact, the greater is the excess
 2145 supply on a product, the larger should be the price tick down on that product. It is
 2146 this principle that ensures that the auction produces prices that are reflective of
 2147 market. If a price on a product is “too high” compared to the price of another
 2148 product, bidders can be expected to switch to the product with a higher price,
 2149 creating excess supply that then drives down the price to a market level.

2150 This principle means that, even if bidders are not provided with the price
 2151 decrement formulas, bidders will be able to make inferences about the excess
 2152 supply of each product. With enough data points, with various levels of excess
 2153 supply at the auction, with various price decrement levels, with general formulas
 2154 for the decrement, and with various combinations of the prices of some products
 2155 ticking down and some not, bidders will more often than not be able to “fit” a
 2156 price decrement function to the data.

2157 **Q. Do you see the fact that bidders will be able to “fit” the price decrement**
 2158 **function as a drawback of Dr. Salant’s proposal?**

2159 A. As I testified, bidders will make inferences because there is necessarily a
 2160 relationship between a high excess supply and a high decrement. I do not think
 2161 that this is the issue. What I see as the issue is that bidders could choose to spend
 2162 (perhaps considerable) resources and time using the data each round to “fit their
 2163 curves” and estimate the price decrement formulas. Bidders will perceive that

2164 having better information regarding the excess supply on a product-by-product
2165 basis will give them an advantage in the auction.

2166 This guessing game has potentially two important drawbacks. First,
2167 bidders may take significant time each round to extract additional information
2168 from the data in an attempt to estimate the price decrement formulas. This can
2169 only slow down the pace of the auction and distract bidders from the analysis of
2170 other information that could be more relevant to their bids. Second, more
2171 experienced bidders, or bidders with more resources to hire the right experts,
2172 could well have an advantage in the auction. These bidders can secure the services
2173 of consultants with auction expertise, who are aware of the types of decrement
2174 formulas typically used in open auctions, of likely parameter values, so that they
2175 will be better at extracting the information that was meant to be kept secret.
2176 Smaller or newer bidders could well be disadvantaged.

2177 **Q. Do you believe that there is an alternative to Dr. Salant's proposal that**
2178 **addresses the concern that bidders may be able to infer the amount of excess**
2179 **supply by product while avoiding the drawbacks that you have just**
2180 **discussed?**

2181 A. Yes, I do. I believe that an alternative is to provide bidders with price decrement
2182 formulas, but to make sure that these formulas do not allow bidders to make good
2183 inferences about the excess supply on a product toward the end of the auction. I
2184 will present a simple method to accomplish this goal, and then I will explain how
2185 this method can be made a little more complex to more thoroughly address the
2186 concern.

2187 A simple method is to set the price decrements as a series of steps. For
2188 example, the decrement could be set at a minimum of 0.25% if the excess supply
2189 is between 1 and 3 tranches, at a higher level of 0.5% if the excess supply is
2190 between 4 and 6 tranches, at another level say 1.375% if the excess supply is
2191 between 7 and 9 tranches, etc. This would mean that when a bidder sees a
2192 decrement of 0.5%, the bidder would know that the excess supply is between 4
2193 and 6 tranches without being able to pinpoint a precise amount. With this
2194 method, the bidder has less and less information as the steps are designed to be
2195 “longer”, i.e., as one increases the number of values for which the decrement is
2196 kept constant. But making the steps longer also decreases the sensitivity of the
2197 auction mechanics: there could be a significant increase in excess supply without
2198 a corresponding increase in the price decrement. For example, if the decrement
2199 stays at 0.25% for excess supply between 1 and 6, bidders have less information,
2200 but there is less opportunity for the price to adjust in response to excess supply.

2201 A slightly more complex method based on the same general principles is
2202 to set the price decrements as a series of long steps, but instead of setting the
2203 decrement as a value certain for a given range of excess supply, the decrement
2204 would be set in a probabilistic fashion. For example, the decrement could be set at
2205 a minimum of 0.25% if the excess supply is between 1 and 3 tranches. For an
2206 excess supply of 4 tranches, there would be a 75% chance that the decrement
2207 would still be set at the minimum of 0.25%, and there would be a 25% chance that
2208 the decrement would be set at a higher 0.5% level. For an excess supply of 5
2209 tranches, there would be a 50% chance that the decrement would still be set at the

2210 minimum of 0.25%, and a 50% chance that the decrement would be set at a higher
2211 0.5% level. For an excess supply of 6 tranches, there would be a 25% chance that
2212 the decrement would still be set at the minimum of 0.25%, and there would be a
2213 75% chance that the decrement would be set at a higher 0.5%. And so on. This
2214 method has overlapping steps: it has the advantage of longer steps because the
2215 bidder cannot infer the amount of excess supply on the product from the
2216 decrement, but the probability function allows some extra sensitivity to the excess
2217 supply that should be beneficial to the auction dynamics.

2218 I believe that this more sophisticated method is effective in addressing the
2219 concern that bidders can make inferences of the excess supply on a product basis.
2220 Bidders, even if they know the price decrement formulas, cannot infer the amount
2221 of excess supply per product. The fact that the Auction Manager can provide the
2222 bidders with the price decrement formulas means that the drawbacks of secret
2223 parameters are avoided. The auction can be paced efficiently because bidders will
2224 not waste time trying to infer the parameters of the price decrement formulas, and
2225 there would be no advantages provided to well-established or more sophisticated
2226 bidders.

2227 Decrement formulas of this type are included as part of the Illinois
2228 Auction Rules (Resp. Ex. 12.4). Further, a graphical illustration of the proposed
2229 price decrement method is provided as Resp. Ex. 12.7.

2230 **Q. Dr. Salant testifies that missing details in the Auction Process open the door**
2231 **to discretion which could then be used to favor Ameren affiliates and**

2232 **exacerbate market power and/or discourage participation by non affiliates.**

2233 **Do you agree?**

2234 A. Not at all. There are three distinct issues here. The first issue is whether there are
2235 decisions where the Auction Manager will be expected to exercise judgment
2236 based on the particulars of the circumstances. I address this issue further on in this
2237 section.

2238 The second issue is whether the details that Dr. Salant believes are omitted
2239 are indeed circumstances in which the Auction Manager is expected to exercise
2240 discretion. Dr. Salant is equating “not specified” or “omitted” with discretionary.
2241 This inference is not justified. For example, the Competitive Procurement Auction
2242 Rules state that formulas for price decrements would be developed. These
2243 formulas are being provided in conjunction with this rebuttal filing and it was
2244 never envisaged that the price decrements would be completely left to the
2245 judgment of the Auction Manager.

2246 The third issue is whether exercise of judgment by the Auction Manager
2247 leaves open the door for decisions that exacerbate market power and could
2248 discourage participation by non affiliates. The items that may not be fully
2249 specified have nothing at all to do with market power or affiliate preference. I
2250 would fully expect that to the maximum extent possible, any decisions with
2251 potential impacts in these areas would have little or no discretion and any
2252 judgment would be made in consultation with the ICC Staff, with the assistance of
2253 their Auction Advisor.

2254 **Q. Would you recommend that all discretion be removed from the Auction**
 2255 **Process?**

2256 A. No. In general there are both benefits and costs to setting up rules in advance and
 2257 removing the ability to exercise judgment on a case-by-case basis. Benefits come
 2258 from the fact that specifying rules ensures that the process is fair and transparent
 2259 for bidders. This favors participation, and the predictability of the environment
 2260 fosters orderly and rational bidding. Costs come from the fact that setting up a
 2261 rule in advance means that one cannot react to unforeseen circumstances and
 2262 cannot guide the auction to a better outcome by exercising judgment.

2263 **Q. What are some of the factors that should be considered in deciding whether**
 2264 **discretion is desirable?**

2265 A. Discretion cannot be painted with a broad brush. Deciding whether judgment or
 2266 discretion should be provided for in particular circumstances or whether a rule
 2267 should be specified is a question of balance and should be decided for the good of
 2268 the Auction Process. This is a question to consider in many areas to set up the best
 2269 Auction Process. The factors to consider include the following:

2270 ○ Some rules are so fundamental to the process that they must be fully
 2271 specified and no discretion used -- most of the auction rules fall in this
 2272 category. For example, the way in which bids will be received, the way in
 2273 which bids will be evaluated and the criteria for closing the auction are
 2274 essential and non discretionary rules and are fully specified.

2275 ○ Sometimes it is impractical or undesirable to specify the rules -- there a few
 2276 cases of this, but they are important. For example, it is neither practical nor
 2277 desirable to specify exactly what will happen when a bidder is unable to
 2278 make the exact certification called for in the Association and Confidential
 2279 Information section of the rules. It is not practical because all

2280 circumstances can not be anticipated. It is not desirable for two reasons.
 2281 First, specifying the solution may well encourage gaming. Second, the pre-
 2282 specified solution could in the context of the situation be overly restrictive
 2283 or not restrictive enough. Bidders have a safe harbor if they can make all
 2284 certifications. Allowing some discretion with respect to Auction Manager
 2285 actions when they cannot can increase bidders' willingness to participate in
 2286 the auction.

2287 ○ Even when it is possible to specify a rule, there are some instances where
 2288 allowing the Auction Manager to exercise judgment in place of using the
 2289 rule can be reasonable and desirable. The question of whether the rule must
 2290 be strictly adhered to or whether judgment is allowed is a matter of
 2291 balancing the costs and benefits to the Auction Process. Decrement rules
 2292 are a good example. Decrement rules can be specified in advance, but in a
 2293 multi-product auction there is no guarantee they will produce a pace that
 2294 could not be improved by an override. While all discretion could be
 2295 removed from decrement rules, the pace of the auction could suffer as the
 2296 date when the auction closes could become less predictable. Whether pre-
 2297 specifying a rule is better, or whether allowing discretion is appropriate is a
 2298 question of judgment. I believe that either can produce good results for the
 2299 Auction Process.

2300 **Q. Does the New Jersey process allow for the Auction Manager to exercise**
 2301 **judgment in specific circumstances?**

2302 A. Yes. The New Jersey Board of Public Utilities has approved the BGS process
 2303 four times and has approved the results of seven auctions. (For the last three
 2304 years, the auction for large customer supply in New Jersey has been designated as
 2305 a separate auction within the same process.) The amount of discretion and degree
 2306 of specificity in the New Jersey rules are very similar to that filed by Ameren in
 2307 its direct testimony.

2308 The FERC has also reviewed the New Jersey Auction Process in
 2309 connection with filings by affiliated suppliers for approval of sales to affiliates. In
 2310 so doing it applied the Edgar standard as recently modified and made stricter in
 2311 the Allegheny decision. In its May 5, 2005 Order in Docket ER05-703-000
 2312 approving sales by PSEG Energy Resources & Trade LLC to its affiliate pursuant
 2313 to the 2005 New Jersey BGS Auction, FERC found that the Auction Process met
 2314 each of FERC’s criteria for unbiased solicitations. These criteria are: 1)
 2315 transparency; 2) definition; 3) evaluation; and 4) oversight.

2316 Specifically, FERC determined:¹

2317 **Transparency Principle**

2318 The BGS auction achieved transparency in the design phase through a
 2319 collaborative process involving informed parties with diverse interests and an
 2320 on-the-record, public New Jersey Board proceeding. The terms of the BGS
 2321 auction were provided on the auction website and are discussed at bidder
 2322 information sessions open to all potential participants in the auction, such that
 2323 all bidders were aware of the bid selection process. This allows for easy access
 2324 to critical information such as bidder requirements and auction rules. Further,
 2325 the independent auction administrator answers questions from interested parties,
 2326 posting the questions and answers on the BGS auction website where they can
 2327 be accessed by all interested parties. Thus, the Commission believes that the
 2328 design, administration, and bid evaluation phases of the BGS auction were
 2329 transparent.

2330 **Definition Principle**

2331 The auction materials defined the products and the pro forma BGS–Commercial
 2332 and BGS–Fixed contracts. By including information such as bidder
 2333 qualification criteria and bid evaluation method in the BGS auction, the
 2334 parameters of the competitive solicitation process were clearly defined prior to
 2335 the solicitation of bids. Bidders had knowledge of the process through which
 2336 they could bid and through which their bids would be evaluated before they
 2337 were called upon to submit them. Thus, the Commission believes that the BGS
 2338 auction was clearly defined.

2339 **Evaluation Principle**

2340 ... Selecting bids based only on price ensured that affiliates were not given
 2341 preferential treatment during the selection phase of the process. After the
 2342 independent consultant evaluated the bids, the New Jersey Board reviewed and
 2343 certified the results within 48 hours of the auction closing, and all companies are
 2344 bound by the auction results. Thus, the Commission believes that the bids were
 2345 evaluated in the BGS auction based on standardized criteria and that those
 2346 criteria were applied equally to all bids regardless of affiliation.

2347 **Oversight Principle**

¹ 111 FERC ¶ 61,152, paragraphs 6 – 9.

2348 The BGS auction was monitored by an independent consultant, who developed
2349 the auction design prior to the first auction in 2002 and was responsible for the
2350 administration of the auction. The New Jersey Board also exercised general
2351 oversight authority over the auction and retained a separate independent
2352 consultant as an advisor to oversee all aspects of the conduct of the auction.
2353 This independent advisor reported directly to the New Jersey Board. Thus, the
2354 Commission believes the presence of this independent third party, as well as the
2355 involvement of the New Jersey Board and its independent advisor, provided
2356 sufficient independent third-party oversight of the design, administration, and
2357 bid evaluation stages of the BGS auction.
2358

2359 **Q. Please address Dr. Salant's assertion that even small details of Auction**
2360 **Management can make a difference to auction participation and the auction**
2361 **results.**

2362 A. I do not think it is reasonable to agree to Dr. Salant's statement in the abstract, nor
2363 do I think that it is necessarily true in practice. An item that could have a large
2364 impact is by definition not a small detail. Further, all rules pertaining to Auction
2365 Management that could have a significant effect on the auction either are
2366 specified now or will be specified before they are needed. Many of these are in
2367 fact not rules but procedures. Many of the specific examples that Dr. Salant
2368 provides do not in fact identify material issues that are properly resolved at this
2369 time.

2370 Some examples of the issues raised by Dr. Salant that fit in to this
2371 category are as follows.

- 2372 1. Mechanism for bidding -- while it is certainly necessary to specify the mechanism
2373 for bidding to bidders as they prepare for the auction, it is premature to specify
2374 that mechanism before the ICC has even approved the auction proposal. The
2375 mechanism for bidding is not essential to judge the merits of the auction proposal.
- 2376 2. Bidder information packet -- bidder information packets will be prepared to assist
2377 bidders in preparation for the auction. These will typically be provided several

2378 months in advance of the auction. It would be premature to develop these at this
2379 time as the ICC ruling in this case will affect the contents of the packets.

2380 Most of the auction issues raised by Dr. Salant in connection with his assertion that
2381 the description of the auction proposal is incomplete fall in the category of items that
2382 are not critical to the evaluation of the proposal and are premature to resolve at this
2383 time.

2384 **Q. Please summarize your rebuttal to Dr. Salant's testimony that the auction**
2385 **rules do not allow for a complete evaluation, provide for the possibility of**
2386 **affiliate favoritism, may discourage non affiliate participation and leave**
2387 **unspecified discretionary items that could have a material impact on the**
2388 **auction.**

2389 **A.** I believe the testimony overstates the case. It ignores the fact that the process as
2390 filed has extensive detail and in fact sufficient detail for the ICC to evaluate the
2391 process. It ignores the fact that the key elements of the rules are fully defined --
2392 including how bids will be specified, how bids will be evaluated, how winners
2393 will be selected and that there is no discretion on these key rules. It ignores the
2394 fact that non affiliates may well have confidence in the Auction Manager and may
2395 prefer some discretion in aspects of the rules. It fails to properly distinguish
2396 between rules on the one hand, which are central to the process and for which
2397 certainty is essential, and procedures for managing the auction on the other hand,
2398 which are not necessarily of interest to the bidders. It does not recognize the need
2399 to achieve a balance when determining when discretion should be applied. It does
2400 not recognize the natural timing of the regulatory process and the auction

2401 implementation. In regard to this last point, Dr. Salant's testimony is equivalent
2402 to a zoning board requiring a detailed blueprint and construction plan before it
2403 approves a structure on a site. While it would need to know how the structure
2404 would look and what impact construction may have, it would not need every
2405 detail and would not need to know exactly how construction would be managed.
2406 Further, until approval is gained, the expense of preparing these detailed plans is
2407 not warranted.

2408

2409 b. Appointment of Auction Manager

2410 **Q. Have you recommended to Ameren that an independent Auction Manager be**
2411 **in charge of essential functions in the Auction Process, including**
2412 **disseminating information to bidders, leading the qualification and**
2413 **registration of bidders, and managing the auction on a round-by-round**
2414 **basis?**

2415 **A.** Yes, I have.

2416 The role of Auction Manager is outlined in my direct testimony (Resp. Ex.
2417 6.0, pp. 84-85, lines 1899-1916) when I describe and assess the "bidder interface"
2418 element. In the Auction Process, the Auction Manager disseminates information
2419 to bidders, including essential documents and data necessary to prepare bids,
2420 answers bidder inquiries, provides technical help to bidders with respect to the
2421 Auction Rules and the bidding method, manages the qualification and registration
2422 of bidders, and manages the bidding procedure during the auction.

2423 I believe that an independent Auction Manager promotes the fair and
2424 equal treatment of all bidders. The Auction Manager is the single point of contact
2425 for all bidders, promoting a fair and equal process.

2426 **Q. Have you recommended to Ameren that there be on-going regulatory**
2427 **involvement from ICC Staff during the Auction Process, and that ICC Staff**
2428 **retain the services of an independent Auction Advisor?**

2429 A. Yes, I have.

2430 The roles of the ICC Staff and of their Auction Advisor are addressed in
2431 my description of the regulatory involvement in the Auction Process (Resp. Ex.
2432 6.0, lines 1452-1467). ICC Staff will be intimately involved in the activities of the
2433 Auction Process, and will have an Auction Advisor to help them monitor the
2434 process and evaluate the results of the auction. The ICC Staff, with the assistance
2435 of their Auction Advisor as appropriate, will be involved in the qualification and
2436 registration of bidders, will work with the Auction Manager to establish protocols
2437 for the implementation of the auction, and will monitor progress. During the
2438 auction, ICC Staff will monitor the bidding itself, and will assess the results, with
2439 the assistance of the Auction Advisor as needed.

2440 **Q. You then agree with Dr. Salant that an independent Auction Manager should**
2441 **manage the Auction Process and that the conduct of the Auction Process**
2442 **should involve ICC Staff and their Auction Advisor?**

2443 A. Certainly. Dr. Salant and I share the view that “the auction is being conducted on
2444 behalf of Illinois ratepayers” (Exhibit 1.0, line 2123) and that this is best
2445 accomplished if the process is conducted by an independent Auction Manager

2446 with substantial involvement and oversight from ICC Staff, with assistance from
2447 their Auction Advisor.

2448 **Q. Various intervenors in this proceeding have served data requests regarding**
2449 **the roles of these parties in the various stages of the Auction Process, is that**
2450 **correct?**

2451 A. Yes.

2452 **Q. Are you able to summarize the involvement of the Auction Manager, the ICC**
2453 **Staff and their Advisor, and ComEd for the various steps of the Auction**
2454 **Process?**

2455 A. Yes. I have summarized the involvement of these parties in the Auction Process
2456 as part of Resp. Ex. 12.6 to my testimony. This exhibit presents the major events
2457 and decision points of the Auction Process, from the time at which final
2458 documents have been provided to bidders to the end of the Auction. This exhibit
2459 illustrates that the crucial steps of the Auction Process are administered by the
2460 Auction Manager in collaboration with the ICC Staff, with the assistance of their
2461 Auction Advisor as needed. This exhibit also illustrates that although Ameren
2462 participates in the process by providing information and data to the Auction
2463 Manager, making assessments related to credit and the administration of the
2464 Supplier Forward Contracts, Ameren does not direct or even participate in the
2465 major decisions and activities of the Auction Process. In particular, the Auction
2466 Manager and the ICC Staff with the assistance of their Auction Advisor, who will
2467 all monitor the bids during the Auction and administer the bidding process, will
2468 have no contact with Ameren during the auction.

2469 **Q. On what issues then do you and Dr. Salant disagree?**

2470 A. Dr. Salant states that the Auction Process should be conducted by “an
2471 independent Auction Manager *rather than* a utility-appointed Auction Manager”.
2472 (ICC Staff Exhibit 1.0 lines 1960-1961). Clearly Dr. Salant believes that if an
2473 Auction Manager is appointed by the utility, then the Auction Manager cannot be
2474 independent. I disagree.

2475 **Q. What do you mean by an Auction Manager who is “independent”?**

2476 A. By an independent Auction Manager, I primarily mean an Auction Manager who
2477 works towards one goal, namely to maximize the probability of a successful
2478 Auction Process.

2479 What it means for the Auction Process to be successful, the criteria that
2480 will be used to judge and measure the success of the Auction Process, are issues
2481 that are being debated and decided within this proceeding. The ICC will use these
2482 criteria to guide its decision on whether to investigate or take action regarding the
2483 results of the auction. The ICC will be relying on the information it will have
2484 obtained throughout the Auction Process and the ICC will be relying on the
2485 confidential report of the Auction Manager to provide a factual description of the
2486 Auction Process and an assessment of whether the Auction Process has met its
2487 criteria for success. The criteria for success will be embodied and reflected in the
2488 questions that the Auction Manager will answer in preparing the report to the
2489 ICC. At a high level, the Auction Process aims to procure reliable supply for
2490 Ameren at the best competitive market prices, and criteria for success will
2491 necessarily center on ensuring the competitiveness and integrity of the process,

2492 and on ensuring that the process is conducted fairly and appropriately. Following
2493 Dr. Salant's suggestions (ICC Staff Exhibit 1.0 lines 2179-2242), the questions of
2494 the Auction Manager report, provided in Resp. Ex. 11.2, in my opinion reflect
2495 these objectives.

2496 The Auction Process is established to obtain supply for the benefit of
2497 Ameren customers and the criteria of success of the process will directly reflect
2498 this purpose. The Auction Manager will know the criteria that have been
2499 established for the success of the Auction Process. An independent Auction
2500 Manager is one who works to meet and exceed these criteria for success, and
2501 works for no other purpose.

2502 **Q. Do you believe that an Auction Manager that is utility-appointed can be**
2503 **independent?**

2504 A. Yes, I do.

2505 The independence of the Auction Manager is determined by the fact that
2506 the Auction Manager is retained for the sole purpose of working toward the goal
2507 of maximizing the probability of the success of the Auction. The ability of the
2508 Auction Manager to focus on this goal is provided by the clear definition of
2509 success that will be established through this proceeding, and by the clear mandate
2510 for the Auction Manager to work to achieve this goal. The selection of the
2511 Auction Manager by the utility has no bearing on the independence of the Auction
2512 Manager.

2513 **Q. You then disagree with Dr. Salant who states that a conflict of interest arises**
2514 **for the Auction Manager because "Ameren has an obligation to its**

2515 **shareholders to obtain regulatory approval to pass through its electricity**
2516 **procurement costs to ratepayers”? (ICC Staff Exhibit 1.0, lines 2102-2104)**

2517 A. Yes, I disagree. The criteria for success of the Auction Process will be established
2518 through this proceeding and will be judged by the ICC. Once these criteria are
2519 established, Ameren, the Auction Manager, ICC Staff and ratepayers all have the
2520 same goal: the success of the Auction Process and the procurement of supply at
2521 the best competitive prices. I do not see a conflict.

2522 **Q. Dr. Salant points out that the conflict could arise in the design stage of the**
2523 **Auction Process, because “getting the best rates for ratepayers can conflict**
2524 **with the goal of maximizing the probability of regulatory approval, especially**
2525 **when obtaining the best rates for ratepayers involves some risks, or involves**
2526 **a procurement process that appears complex”. (ICC Staff Exhibit 1.0 p. 93,**
2527 **lines 2104-2108). Do you disagree with that?**

2528 A. I understand Dr. Salant’s point to be that not every party will balance the twin
2529 goals of getting the lowest prices for customers and managing the risks to which
2530 these customers are exposed in the same way. Reasonable people can disagree on
2531 what the right balance is. For instance Mr. Salgo, as I testified earlier in Section 2,
2532 also argues that Ameren’s proposed Auction Process could benefit from an
2533 injection of additional risk if it could provide for the potential of lower prices.

2534 I understand the point, and I see that different parties can have different
2535 views on how best to achieve certain objectives, but I do not see a conflict over
2536 the objectives themselves. Furthermore, Ameren does not unilaterally design and
2537 implement an Auction Process. Ameren has welcomed the views of all the parties

2538 and has strived to put forth an Auction Process that would balance the interests of
2539 the parties. All parties can now provide other views and suggest modifications to
2540 the Auction Process that they believe are improvements. Ultimately, the design of
2541 the Auction Process and the best approach for Illinois customers are going to be
2542 determined within this proceeding, not by Ameren.

2543 **Q. Dr. Salant also makes the point that there could be a conflict of interest for**
2544 **the Auction Manager “when a utility’s affiliated generators participate in the**
2545 **auction”, (ICC Salant Exhibit 1.0 at lines 2108 – 2109) where there could be**
2546 **favoritism shown to the affiliate. Do you agree that this is a conflict that**
2547 **compromises the independence of a utility-appointed Auction Manager?**

2548 A. I agree that having a fair and equal treatment of all bidders is essential to
2549 encouraging the participation of all potential bidders and is essential to the
2550 success of the Auction Process. This means that there should be no favoritism
2551 shown to any bidder, whether the bidder is affiliated with the utility or not. I do
2552 not agree that the fact that the Auction Manager is appointed by the utility
2553 compromises the ability or the incentive for the Auction Manager to achieve the
2554 objective of managing an Auction Process where all bidders are treated fairly and
2555 equally. As a practical matter, I note that in New Jersey, where I have been
2556 appointed Auction Manager by the utilities for the last four years, bidders have
2557 not expressed any concerns over favoritism of any one bidder, and to my
2558 knowledge suppliers who have not put forth affiliate participation as a concern
2559 when considering whether to participate.

2560 The Auction Process is structured so that the scope for favoritism of any
2561 bidder is virtually non-existent. The evaluation of bids and selection of winners is
2562 on a price-only basis. The rules of the auction provide a method for determining
2563 the auction winners and the final prices that is completely objective. The
2564 qualification and registration requirements, as embodied in the Part 1 and Part 2
2565 Application Forms (see Resp. Exs. 12.1 and 12.2 to this testimony) are as clear-
2566 cut as possible. As indicated in Resp. Ex. 12.6, ICC Staff is kept fully informed
2567 regarding the Application Process. ICC Staff would be consulted in the resolution
2568 of any application issues and would have the assistance of their Auction Advisor.
2569 Throughout the process, all bidders would be provided with the final documents,
2570 data to prepare their bids, and other information regarding the Auction Process,
2571 simultaneously through a web site that would also be accessible to all interested
2572 stakeholder. Other auction procedures for the implementation of the Auction
2573 Process, as they would be developed by the Auction Manager in consultation with
2574 the ICC Staff closer to the time of the auction, would be designed to meet the
2575 success criteria defined for the process, which would include designing
2576 procedures to ensure the fair and equal treatment of all bidders, and to ensure that
2577 no bidder, affiliate or not, can be favored. For example, I note that in New Jersey,
2578 bidders understand that as the Auction Manager I receive and strictly maintain the
2579 confidentiality of sensitive business and competitive information that they
2580 provide, and in particular that the utility does not have access to this information.
2581 There are formal communication protocols that establish the nature of
2582 confidentiality information, and the obligations of all parties (the Auction

2583 Manager, the utilities, Board Staff, the Board Advisor) with regards to handling of
2584 such confidential information. There are also protocols that formalize the
2585 interface with bidders to ensure equal treatment of all bidders; these protocols
2586 specify, for instance, that all bidder inquiries and issues are resolved by the
2587 Auction Manager and that the utilities do not interact directly with the bidders.
2588 I would expect that similar procedures would be agreed upon by the Auction
2589 Manager and the ICC Staff with the assistance of their Auction Advisor, prior to
2590 the auction.

2591 In sum, the ability and scope for favoritism of any one bidder is, if it exists
2592 at all, extremely limited, and who appoints the Auction Manager is irrelevant to
2593 this issue. Furthermore, the Auction Manager does not have any long run
2594 incentives to favor the utility affiliate or any other bidder. The Auction Manager,
2595 even utility-appointed, has no special relationship to the utility affiliate. To
2596 believe that the Auction Manager has an incentive to effectively favor the
2597 affiliate, one would have to believe that the utility can direct the actions of the
2598 Auction Manager, that the utility would direct these actions not to benefit itself
2599 but to benefit its affiliate instead, and that the Auction Manager would have an
2600 interest in consenting in this conspiracy if such a conspiracy existed. I do not
2601 believe that the utility can direct the actions of the Auction Manager, I do not
2602 believe that the utility would do so to favor its affiliate, and I certainly do not
2603 believe that the Auction Manager has any incentives to show any such favoritism.

2604 **Q. Why do you say that the Auction Manager does not have incentives to favor**
2605 **the utility affiliate? Wouldn't such favoritism be in the economic interest of**

2606 **the Auction Manager by providing an opportunity for future business with**
 2607 **the affiliate?**

2608 A. No, it would not. The future business of an expert who manages auctions is in
 2609 managing or designing other auctions. The next auction management assignment
 2610 does not come because a bidder has been favored. The next auction management
 2611 assignment comes because the Auction Manager has led an Auction Process to a
 2612 successful conclusion in the eyes of stakeholders. The next auction management
 2613 assignment comes, and professional reputation is built and maintained, when the
 2614 results of the Auction Process meet the success criteria that are pre-established;
 2615 when the auction benefits ratepayers in the eyes of the ICC, in the eyes of other
 2616 parties representing customers, and in the eyes of the utility; and when the
 2617 Auction Process is run in a way that satisfies bidders and secures their
 2618 participation in future auctions, ensuring the success of the process in the long
 2619 run. Professional reputation is also built and maintained through the ability of the
 2620 Auction Manager to participate in the continued improvement to the Auction
 2621 Process, through the continued involvement and review of all stakeholders.

2622 **Q. Please summarize why you believe that an Auction Manager appointed by**
 2623 **the utility will act so as to maximize the probability of success of the Auction**
 2624 **Process to the benefit of ratepayers?**

2625 A. The fact that the Auction Manager is appointed by the utility does not in my
 2626 opinion impede or interfere in any way with the ability of the Auction Manager to
 2627 maximize the probability of success of the Auction Process. The ability of the
 2628 Auction Manager to maximize the probability of success of the Auction Process is

2629 assured by success criteria that will developed in this proceeding, by a clear
2630 mandate for the Auction Manager to lead the Auction Process so as to meet or
2631 exceed these success criteria, by an auction design that is transparent and
2632 objective to ensure fairness, by regulatory involvement during the implementation
2633 phase that will ensure that the fairness and transparency will extend from the
2634 design to the execution. The incentives of the Auction Manager are to have all
2635 stakeholders agree that the Auction Process was a success.

2636

2637 c. Auction Pacing

2638 **Q. Have you reviewed the testimony of Dr. Salant with respect to auction**
2639 **pacing?**

2640 A. Yes.

2641 **Q. Please summarize your understanding of that testimony.**

2642 A. Recognizing that forward power prices may change more over the course of
2643 multiple days than in a single day, Dr. Salant observes that a longer auction will
2644 lead to a risk premium being reflected in bids and recommends a shorter auction,
2645 in particular a one-day auction in order to obtain the best price for customers. He
2646 appears to view the key to holding a one-day auction as being the capability of the
2647 auction software and the expertise and effort devoted to testing that software.

2648 **Q. Are there aspects of this issue on which you agree with Dr. Salant?**

2649 A. Sure. I agree that getting the best price for customers is the issue of paramount
2650 importance and I agree that bidders will view forward prices as being subject to
2651 more change over the course of several days as opposed to over the course of a
2652 single day.

2653 **Q. Are there aspects of this testimony with which you do not agree?**

2654 A. Yes. I disagree with the conclusion that managing the auction so that it opens and
2655 closes in a single day will produce the best prices. I also disagree that software is
2656 the key to achieving a one-day auction or the constraint on not being able to
2657 achieve a one-day auction.

2658 **Q. Please explain why it is not true that the faster the auction is run the better**
2659 **the price?**

2660 A. There are several reasons. First, the fact that forward prices are subject to more
2661 change over time does not logically lead to the conclusion that there will be a
2662 lesser risk premium in bids for an auction targeted to close in one day. (This is
2663 the case even ignoring concerns about the potential loss of the benefit of the
2664 auction format, practical issues and the potential dynamic effects on entry.)
2665 Second, one cannot ignore the real and compelling concerns that a one-day
2666 auction will come at the sacrifice of many of the benefits of the open auction
2667 format. Third, there are a variety of practical issues that must be considered.
2668 Fourth, a target of a one-day auction may deter entry, reduce competition and lead
2669 to higher prices.

2670 **Q. Why is it not logical to believe that a faster auction will reduce the risk**
2671 **premium given the nature of forward markets?**

2672 A. The assertion that this will occur is based on a false assumption that all hedges
2673 will be placed from a fixed point on or before the start of the auction. Were this
2674 to be the case, one could logically reason that bidders would have concern over
2675 the length of the auction and would be hesitant to place a bid that did not

2676 compensate for the risk that forward prices may drop before the outcome of the
2677 auction is known. For example, assume that on the day the auction starts, a bidder
2678 had locked in hedges that given its assessment of risk permitted it to profitably
2679 serve BGS load at 5 cents per kWh. The bidder would face little risk if it was
2680 certain that the auction would close in one day. If the auction price was greater
2681 than or equal to 5 cents, the bidder could remain in the auction and profitably
2682 serve the load it won. If the price was to drop below 5 cents the bidder could
2683 liquidate its hedges with only one day of price risk. If however the auction lasted
2684 several days, the bidder would face more price risk with respect to liquidation. It
2685 is reasonable to infer that such a bidder may be unwilling to offer tranches on day
2686 one at 5 cents if it thought the auction may last a week. The bidder, hedged at 5
2687 cents would be fine if it won, but if it did not win would face the risk of the need
2688 to liquidate hedges at a price subject to the uncertainty of a week rather a day
2689 price decline. Hence, it would be correct that if the auction format asked bidders
2690 to make a binding bid on day 1 that would be open for one day versus one that
2691 would be open for five days, the bid open for five days would contain a greater
2692 risk premium to account for the risk of holding a position that may have to be
2693 liquidated at a loss. As best as I can tell, this is what Dr. Salant must mean when
2694 he says that bidders will reflect a risk premium in their bids.

2695 Of course, this is an overly simplistic view of the auction and is based on a
2696 rigid and unrealistic assumption as to how bidders may hedge. The auction does
2697 not require bidders to submit a price bid for a specified quantity that will be open
2698 until auction close. Rather, bidders make binding quantity bids at prices set by

2699 the Auction Rules. In a multi-day auction, these prices are likely to be above
2700 closing levels for the first day or even two. Bidders who had hedged prior to the
2701 auction will face the decision to continue in the auction at these prices or
2702 withdraw and liquidate the hedges. Staying in the auction would expose them to
2703 ongoing price risk that withdrawing would eliminate. Hence, there is still an
2704 aspect of a risk premium to staying in the auction, but it is quite different than that
2705 in the one-time open bid example. At higher going round prices, the premium
2706 would not affect a bidder's decision. It is only when the risk of a decline in the
2707 value of hedges exceeds the surplus profit in the going price that a bidder's bid
2708 would be influenced. Going back to the example, assume the bidder who had
2709 hedged on day 1 would have offered to supply for 5 cents if the decision was
2710 made on day 1 and 5.2 cents if the decision was made on day 5. If on day 3 the
2711 going price is 6 cents, there would be no effect on the bid. If on day 4 the price
2712 drops to near 5 cents and the auction appears likely to close, there would also be
2713 no effect on the bid. If on day 4, the price was approaching 5 cents and the bidder
2714 could not tell if the auction was going to last another day or another five days,
2715 then the risk premium would be a factor. The bidder may be willing to stay in at
2716 5 if they thought the auction would close that day, but withdraw at 5.2 if they
2717 thought the auction may last another five days. The risk premium issue is much
2718 more complex than Dr. Salant portrays. It is not finishing the auction in one day
2719 that is important, but rather having some predictability in the time remaining in
2720 the auction as well as the uncertainty of winning. In regard to the latter, if the
2721 auction is largely resolved in a few days, but there are a small number of excess

2722 tranches competing on a limited number of products, the vast majority of tranches
2723 are at little risk as they can not be displaced.

2724 Finishing the auction in one day would only reduce the risk premium that
2725 would influence bids if a one day auction was subject to a more certain and
2726 predictable close.

2727 **Q. Does a one day auction provide an assurance of a more certain and**
2728 **predictable close?**

2729 A. I don't believe it does. There is simply no assurance that the auction would be
2730 completed in a day even if so targeted. The Auction Rules provide for a volume
2731 adjustment, which would require a time out. The auction rules also provide for
2732 round extensions and recesses. Most important, the Auction rules provide for
2733 numerous products and switching. As these products constantly align their
2734 relative prices, bidders switch rather than withdraw. It may take many more
2735 rounds than anticipated to fully resolve an auction with multiple products and
2736 switching than a single product auction. Very fast rounds and a target to close in
2737 one day do not ensure that this will happen and hence don't eliminate a risk
2738 premium.

2739 The fact is that very fast rounds and a target of a one day auction will not
2740 minimize the risk premium as there will be no assurance to bidders that the
2741 auction will be completed in one day. It is the bidders' view of when the auction
2742 will be completed that will affect the risk premium.

2743 Further, the assumption that bidders will hedge on day 1 is unfounded.
2744 Bidders may well elect to close hedges as the auction proceeds. If bidders can

2745 expect the auction to last three days and they place hedges on day 2 or day 3, a
2746 three-day auction has no greater a risk premium than a one-day auction. If in fact
2747 the auction unfolds in a way where near the end a bidder's chance of success is
2748 clearer than in a one-day auction and the predictability of the closing time equal,
2749 any risk premium may well be lower. Hence, given the auction format, the nature
2750 of the bids and the ability to place hedges over the course of the auction, targeting
2751 a one-day auction will not logically lead to a lower risk premium.

2752 **Q. Let's not take the recommendation for a one-day auction so literally. Won't**
2753 **a very fast paced auction, even if the pace is only increased near the end,**
2754 **increase the certainty of closing and reduce the risk premium relating to**
2755 **market change exposure?**

2756 **A.** It could. For example, if the auction had been going on for three days and bidders
2757 were assured that on day 4 there would be 50 fast paced rounds, even given the
2758 possibility for extensions and recesses, they may be more confident of a close on
2759 day 4 and willing to stay in at lower prices than otherwise. This could, all else
2760 equal, get a better price. The problem is all else is not equal. While speeding up
2761 rounds late in the auction may reduce the risk premium relating to market change
2762 exposure, it does not necessarily lead to better prices. That risk is but one element
2763 of the price. Bidders will have less time to make decisions and less time to have
2764 bids in the auction reflect their hedging activities in a very fast paced auction.
2765 Bidders could lose the flexibility to time the closing of hedge positions and
2766 bidding in the auction and may well be forced to hedge earlier offsetting any risk
2767 premium reduction. My experience in managing the New Jersey BGS Auctions

2768 leads me to conclude that the worst time to speed up the auction is near the end
2769 when bidders face tough decisions. This may well lead to withdrawals that would
2770 otherwise not occur and higher prices. A very fast auction will have no impact on
2771 prices early on and will potentially lead to worse prices if the pace is fast near the
2772 end.

2773 **Q. How will a one-day auction, or an auction with a very fast pace near the end,**
2774 **sacrifice the benefits of the open auction format?**

2775 A. The open auction obtains better bids by enabling bidders to absorb and respond to
2776 market information. As prices decline and excess supply is maintained, bidders
2777 can infer how others may value the opportunity and adjust their bids. The
2778 premium built in to bids to compensate for the winner's curse can be eliminated.
2779 Bidders will have greater confidence that their bids reflect the market and can be
2780 more aggressive. This is extremely important in the multi-product auction, where
2781 bidders also have information needed to react to relative prices. However, for this
2782 information to be useful, bidders must have the ability to absorb it and react to it.
2783 Late in the auction, bidders may even need to return to management for approval
2784 to lower their offers. An auction that is too fast paced, provides bidders
2785 information but not the time to react. An auction where each round lasted just a
2786 minute would essentially reduce to a sealed bid auction. I have elaborated on the
2787 benefits of the multi-round format in my direct and Dr. Salant also does so in his
2788 testimony. In fact Dr. Salant wants more switching to take advantage of the
2789 auction format. The very fast paced auction takes away with one hand what the
2790 auction format provides with the other. The information provided by the open

2791 format, multi-round, multi-product auction will not have a beneficial effect if
2792 bidders are not given time to utilize the information. This is especially the case as
2793 the auction approaches clearing price levels. Reducing the risk premium relative
2794 to the risk of market changes is winning the battle but losing the war of getting the
2795 best price if to do so, the benefits of the auction format are sacrificed.

2796 **Q. Let's be fair. Dr. Salant recognizes that. He has a solution. Bidders can do a**
2797 **comprehensive analysis beforehand and then be able to react to the**
2798 **information given very fast paced rounds. Have you considered that?**

2799 A. Yes. In addition to managing the BGS auctions in New Jersey, I, like Dr. Salant,
2800 have provided bidding advice in multi-round auctions. These assignments can be
2801 complex and consume substantial time, effort and cost. In the case of the Illinois
2802 Auction, there are literally thousands of combinations that could result with
2803 respect to bidder activity at relative prices and to the relationship between going
2804 prices in the auction and other market indicators. Sure, bidders could hire market
2805 and auction consultants to map out all the bidding patterns that may develop, and
2806 then plot out in advance responses developed by special software to the
2807 information that comes from the auction. However, there is no guarantee that an
2808 unexamined bidding pattern will not develop. Further, the complexity of such an
2809 activity can be daunting. There is also no guarantee that the response developed
2810 in the abstract will be the same that would occur if the response was observed in
2811 the auction and there was sufficient time to react to a real situation. Auction
2812 consultants may well be better off given accelerated rounds and the need to do
2813 extensive analysis in advance, but customers won't necessarily be. Advance

2814 analysis is not a substitute for providing bidders with the time to react to how real
2815 life bidding unfolds. It cannot restore the auction format benefits that are lost
2816 from very fast rounds.

2817 **Q. Please explain any additional practical impediments to a very fast auction**
2818 **pace.**

2819 A. There are additional practical elements that would concern me if the ICC were to
2820 require that the auction be done in one day or at an accelerated pace. First, I do
2821 not believe that a fast-paced auction would give the Auction Manager sufficient
2822 time to review the data from each round and monitor the bids. The Auction
2823 Manager must do this in order to assess whether there appears to be any
2824 anomalous bidding that could reflect attempts by bidders to act anti-
2825 competitively. Careful review of the round-by-round bidding data is required for
2826 the Auction Manager to perform its job and to assure the integrity of the auction.
2827 A fast-paced or one-day auction compromises the ability of the Auction Manager
2828 to perform this important function.

2829 Second, I believe it is important for the Auction Manager to be able to
2830 check and to cross-check the round results to confirm that the software is working
2831 properly. While software can be tested extensively and should not produce
2832 erroneous results, the checking process further helps to assure the integrity of the
2833 auction and reduces the possibility of challenges.

2834 Third and finally, I generally do not believe it is good policy to rush
2835 bidders during the auction. To the extent that bidders need time, they should be
2836 allowed to take time.

2837 **Q. You mentioned that a one-day auction or an auction held at an accelerated**
2838 **pace may deter entry, reduce competition and lead to higher prices. Please**
2839 **elaborate.**

2840 A. In a very fast-paced auction, large players can be expected to have an advantage.
2841 This is because in a fast-paced auction, most of the analysis must be done by
2842 bidders in advance of the auction. Hence, those bidders with large budgets for
2843 auction consultants and large in-house resources to perform the necessary pre-
2844 auction analysis will be in a better position *vis-à-vis* smaller bidders without such
2845 resources. I believe that this could create an entry barrier for small players. If
2846 small players are deterred from participating in the auction, this will reduce
2847 competition in the auction and can be expected to raise the cost of supply to
2848 default service customers.

2849 **Q. If a one-day auction or an accelerated auction is not critical to the auction**
2850 **outcome, why is it so important to have rapid approval by the ICC of the**
2851 **auction results?**

2852 A. These are separate issues. As I have noted above, it is the bidders' view of when
2853 the auction will be completed that will affect the risk premium, not the actual
2854 length of the auction. However, at the end of auction, the bidder has an open
2855 offer and is exposed to the risk that the auction will not be declared successful, in
2856 which case it could have to liquidate any hedges it had acquired. Hence, at the
2857 end of the auction, the bids can be expected to reflect a premium for the risk of an
2858 unsuccessful auction. The size of this risk is directly related to the length of
2859 time between auction close and the declaration of a successful auction. Whereas

2860 there are many expected benefits for suppliers, the Auction Manager and the
2861 overall auction results from not overly compressing the duration of the auction --
2862 benefits which I have described above -- I do not see any benefits to the auction
2863 from lengthening the timeframe for approval.

2864 **Q. How as Auction Manager would you seek to reduce the risk premia from**
2865 **market exposure changes?**

2866 A. I would intend to run the auction at an efficient and orderly pace. By an efficient
2867 pace, I mean that the quickest pace that nevertheless ensures that bidders are not
2868 unduly rushed or prevented them from evaluating the information provided during
2869 the auction. By an efficient pace, I also mean the quickest pace that nevertheless
2870 maintains the reliability of the process and allows for any needed monitoring by
2871 the Auction Manager and ICC Staff. I believe that an efficient and orderly pace
2872 benefits bidders in that it facilitates their assessments of when the auction is likely
2873 to close, and in this way would reduce any embedded risk premia. I also believe
2874 that when bidders make informed decisions, this should yield accurate and
2875 competitive prices for each product in ways that would offset any embedded
2876 risk premium inherent in the bids.

2877 **Q. What are the main ways that you believe should be considered to make the**
2878 **auction pace more efficient?**

2879 A. I believe that the first way to make the auction pace more efficient is to ensure
2880 that any Auction Manager procedures are established with the essential goal in
2881 mind of minimizing delays in the auction. These would include, for instance,
2882 ensuring that back-up bids can be processed quickly, ensuring that data backup

2883 procedures are automated, and ensuring that any protocol for round-by-round bid
2884 data verification or monitoring is developed with speed in mind. The second way
2885 to make the auction pace more efficient is to examine how the auction rules may
2886 be modified to permit a faster pace. One option is to review the provisions for
2887 various suspensions of the auction, either by the Auction Manager (through time-
2888 outs) or by the bidders (through extensions and recesses) so as to appropriately
2889 limit their duration or their use. A second option that would require a more careful
2890 review is to change to a flexible bidding window. Currently, the time of the
2891 bidding window is fixed and bidders can, during the bidding window, submit bids
2892 and revise these bids as often as they wish. An alternative is to set a bidding
2893 window but allow bidders to submit a single bid during that window. This would
2894 allow the Auction Manager to close the bidding window and start processing the
2895 bids as soon as all bids had been submitted.

2896 There are likely other procedures or rules that can be examined with the
2897 view to optimizing the pace of the auction. Ameren has committed to making this
2898 examination along with its Auction Manager and Commission Staff to promote
2899 the best auction result possible. I note that it should be recognized, however, that
2900 in an auction with switching across products that are not perfect substitutes, and
2901 with a requirement to adhere to a pre-specified decrement rule, the time at which
2902 the auction closes may be difficult to predict. It can be necessary to tolerate some
2903 uncertainty regarding auction close in order to realize the benefits of adhering
2904 closely to fixed decrement rules and of allowing switching across products.

2905 **Q. Does this conclude your rebuttal testimony?**

2906 A. Yes, it does.

2907