

ILLINOIS COMMERCE COMMISSION

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 Commonwealth Edison Company )  
 )  
 Petition for Expedited Approval of )  
 Implementation of a Market-based )  
 Alternative Tariff, to Become Effective )  
 on or before May 1, 2000, Pursuant to )  
 Article IX and Section 16-112 of the )  
 Public Utilities Act )  
 )  
 Central Illinois Public Service Company )  
 Union Electric Company )  
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 Petition for Approval of Revisions to )  
 Market Value Tariff, Rider MV )  
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 Illinois Power Company )  
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 Proposed New Rider MVI & )  
 Revisions to Rider TC )  
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Docket No. 00-0259

(cons.)

Docket No. 00-0395

Docket No. 00-0461

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 ILLINOIS COMMERCE COMMISSION

ILLINOIS POWER COMPANY'S OPENING BRIEF

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**STATE OF ILLINOIS  
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**ILLINOIS POWER COMPANY'S OPENING BRIEF**

Pursuant to the Hearing Examiner's Ruling on October 17, 2000 and § 200.800 of the Commission's Rules of Practice, Illinois Power Company ("Illinois Power," "IPC" or "IP") hereby submits its Opening Brief in the above-referenced, consolidated dockets.

**INTRODUCTION & SUMMARY**

In these consolidated cases, Commonwealth Edison Company ("ComEd," "CE" or "Commonwealth"), Central Illinois Public Service Company and Union Electric Company (collectively, "Ameren") and Illinois Power each submitted proposals to replace the market

values reported by the Neutral Fact-Finder (“NFF”) process with market values based on indices. The NFF process is now recognized as flawed by most parties,<sup>1</sup> and the values that flow from that process are viewed as one reason competition is not taking hold as strongly as it could in Illinois. Market values are used to determine the Transition Charges (“TC” or “CTC”) paid by customers who take delivery service. In general, higher market values lead to lower TCs. Thus, if the market values used to establish TCs are low in comparison to the actual market prices, customers will be faced with higher-than-expected TCs and will also face higher than expected energy prices from alternative suppliers (because those suppliers will likely be providing energy at the actual market price). The result is a price that is above the artificially low NFF price that the customer can obtain by staying with the incumbent utility (either on bundled tariffs or on the power purchase option (“PPO”), if eligible). Faced with this economic reality, customers do not switch and competition is hindered.

Although the three proposals differ in many respects from one another, each seeks to replace the NFF with a better methodology. Illinois Power does not object to the Commission approving the Ameren and CE proposals *for those respective companies*. While those proposals do not have all of the benefits inherent in ours, the constraints contained in the law and the ability of each proposal to serve as an experiment to see which features in fact prove most appropriate counsel against an attempt to craft a uniform solution. The remainder of this brief focuses on IPC’s proposal and the benefits that flow from that proposal; where necessary, however, we refer to specific features of the Ameren and CE proposals to explain why we would or would not be willing to accept certain modifications suggested by other parties.

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<sup>1</sup> “[N]o participant [in the ICC Chairman’s Fall 2000 Roundtable Discussions] believed the Neutral Fact Finder’s process for determining a market value could result in an accurate and appropriate market value.” Report § XII(B) (footnote omitted).

IPC's basic proposal replaces the NFF values with market-based values derived as follows:

(1) *On-peak* values for firm energy are based on into-Cinergy forward contract data derived from two electronic exchanges and one published source, with a Basis Adjustment applied to the values to address any differences between into-Cinergy prices and Lower MAIN prices.<sup>2</sup> The data is collected for the last five business days of the preceding month and the first five business days of the current month.

(2) *Off-peak* values are derived from historical data for the day-ahead market.

(3) *TCs* are calculated in the same manner that they are calculated using the NFF values, including the PJM load-shaping adjustment known as the Zuraski adjustment. IPC's intent was not to alter the methods already used to adjust the NFF values, but rather was merely to replace the NFF values with the new MVI values.

(4) The resulting *Market Values* and *TCs* will be published by the 8th Business Day of each month to be effective for customers who begin delivery service in the following billing month and for customers whose anniversary dates are in the following billing month. These values will be submitted to the Commission and will be available on IPC's website.<sup>3</sup> Furthermore, these values will be in effect for those customers to whom they apply for an entire 12-month period.<sup>4</sup> Thus, although new values will be re-

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<sup>2</sup> Non-firm prices are derived by dividing the firm values for any given month by 1.15.

<sup>3</sup> For customers who have individually-calculated TCs, a password will be required to obtain the information.

<sup>4</sup> TC values might change due to other factors (such as the distribution charge) changing, but the market values used to set the TC would not change for that customer until the customer's next anniversary date.

calculated the next month, those new values will only apply to the customers with anniversary dates in the following billing month and will not alter the values applicable to customers who had anniversary dates the preceding month.

IPC's methodology combines a liquid trading hub, a market basket of data sources, data collection close to the time the resulting values become effective and sufficient time for customers to make decisions. This combination balances the needs of all parties. Nonetheless, we are not adverse to making modifications to our proposal; indeed, through-out this proceeding (and even before we filed our tariffs), we actively sought out the opinions of many interested parties and modified our proposal in light of some of the comments we received. While we remain open to even further suggestions, we are not willing to change the core of our proposal. Therefore, at this time, we are not willing to:

- (1) Use an into-CE hub and data sources;
- (2) Change our load shaping adjustment methodology or adjust our off-peak values due to the type of data used in pricing that energy;
- (3) Adjust our values for what have been termed "optionality," "planning reserve," "energy imbalance" or "capacity backed" adjustments; or
- (4) Change the time periods during which data are collected and market values & TCs are effective, including the monthly re-collection of data and the recalculation and publication of values for the subsequent 12-month period.

None of the above adjustments and modifications are warranted given the evidence in the record in this case. Finally, the law is clear that IP cannot be required to offer PPO service to a customer who has a 0 TC. Any other conclusion is contrary to the law and to sound public policy.

## PROCEDURAL HISTORY

On March 31, 2000, Commonwealth filed its proposal, which became ICC Docket No. 00-0259. Various parties intervened, with some also filing substantive comments. An Interim Order was issued by the Commission on April 27, 2000. This Order is currently on appeal to the Fourth District Appellate Court. *See* Docket Nos. 4-00-0570, 4-00-0595 & 4-00-0596 (cons.).<sup>5</sup> On May 1, 2000, CE filed tariffs conforming with the modifications required in the Interim Order. *See* Advice S-25.

On May 31, 2000, Ameren filed its market value index proposal, which became ICC Docket No. 00-0395. On June 5, 2000, IPC made its initial filing, which, after the tariffs were suspended, became ICC Docket No. 00-0461.<sup>6</sup> IPC supplemented its tariff changes with its Direct Testimony. Certain proposed changes in IPC's tariffs (1) are un-related to its Market Value Index ("MVI") proposal (such as the removal of Appendices 1-3 of Rider TC and changes to Section 7(d) of Rider TC); (2) are intended to streamline and update other aspects of IPC's tariffs; and (3) have not been challenged by any party to this proceeding. We, therefore, will not be addressing them further in this Brief. We do, however, reserve our right to respond to any issues raised in the initial briefs filed by other parties in this docket.

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<sup>5</sup> The parties appealing the Interim Order are the companies comprising the Illinois Industrial Energy Consumers ("IIEC"), Enron Energy Services, Inc. ("Enron") and the People of the State of Illinois ("AG"), with various other parties at the Commission intervening at the appellate stage, including IPC. The appeals are currently in the briefing stage. Recently, Enron's appeal was dismissed on its own motion.

<sup>6</sup> A Resuspension Order was entered on October 18, 2000.

On July 6, 2000, the three dockets were consolidated on the Commission's own motion.<sup>7</sup> Thereafter, a schedule was set under which pre-filed testimony and exhibits were submitted. Workshops were also held to help the parties clarify the proposals and understand the issues. Cross-examination hearings were held from October 2 through October 5 in Springfield. After evidentiary motions were argued, the record was marked "Heard & Taken." The remainder of the schedule calls for Briefs to be filed on November 3, with Replies on November 22. Thereafter, a Hearing Examiner's Proposed Order is expected on December 22, with Exceptions due on January 12, 2001 and Replies to Exceptions on January 26, 2001. A Post-Exceptions Proposed Order is anticipated on February 9, 2001, with a final Order expected in time for the parties to implement the final tariffs before the Summer season of 2001 (assuming they agree to any modifications required in the final Order).

### ARGUMENT

The following uses the outline attached to the Hearing Examiner's Ruling of October 17, 2000 with the modification that the headings have been re-cast as sentences.

#### **I. The Applicable Statutory Provisions and Requirements Support IPC's Positions.**

In late 1997, Illinois enacted landmark legislation (*i.e.*, the Electric Service Customer Choice and Rate Relief Law of 1997 ("Customer Choice Law")) that called for an orderly transition during which customers of electric utilities become eligible to buy power and energy from alternative retail electric suppliers ("ARES"). *See* Public Act 90-561. As a part of opening the Illinois electric markets to competition, electric utilities are permitted to collect a transition

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<sup>7</sup> For the most part, intervenors are parties in all three dockets, although in a few instances, specific parties only intervened in one or two of the proceedings.

charge. *See* §§ 16-102 & 16-108.<sup>8</sup> In theory, the TC represents the revenue an electric utility loses when a customer switches from traditional bundled service to competitive service. In actuality, with the inclusion of a mitigation factor in the calculation, the TC represents only a portion of the revenue an electric utility loses when a customer switches to competitive service. The TC is calculated as follows:

$$\text{TC} = \text{Bundled Rate} - \text{Delivery Services Rate} - \text{Market Value} - \text{Mitigation Factor}$$

*See* ICC Staff. Ex. 3.0 at 5; IP Ex. 2.1 at 5.<sup>9</sup> If the calculation yields a value of 0 or less, the TC is set to 0, *see* ICC Staff. Ex. 3.0 at 6, and the customer pays no TC. The Bundled Rates are frozen (and, for residential customers, significantly reduced by the Customer Choice Law). Between delivery service rate cases, the Delivery Service Rates will be relatively fixed, but may occasionally change in small increments. The Mitigation Factor is a statutorily-set amount that can vary by year, but for any given customer at any given time, is essentially set. *See* § 16-102. Therefore, the parameter with the highest degree of variability in setting a customer's TC is the market value used. The method of determining this value is set forth in § 16-112(a):

The market value to be used in the calculation of transition charges as defined in Section 16-102 shall be determined in accordance with either (i) a tariff that has been filed by the electric utility with the Commission pursuant to Article IX of this Act and that provides for a determination of the market value for electric power and energy as a function of an exchange traded or other market traded index, options or futures contract or contracts applicable to the market in which the utility sells, and the customers in its service area buy, electric power and energy, or (ii) in the event no such tariff has been placed into effect for the electric utility ..., a tariff incorporating the market values resulting from the neutral fact-finder process set forth in subsections (b) through (h) of this Section.

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<sup>8</sup> All references to statutory provisions are to the Public Utilities Act ("PUA"), 220 ILCS Part 5, unless otherwise noted.

<sup>9</sup> All references to Exhibits are in the form "[Party] Ex. [No]. at [p.]" unless otherwise noted. Also, references to the transcripts are in the form "Tr. [p.] ([date])" unless otherwise noted.

The market value is also critical in setting the price a customer pays for PPO power and energy, if eligible:

a non-residential delivery services customer that is paying transition charges to the electric utility shall be permitted to purchase electric power and energy from the electric utility at a price equal to the sum of (i) the market values that are determined for the electric utility in accordance with Section 16-112 and then used by the electric utility to calculate the customer's transition charges and (ii) [an administrative fee].

§ 16-110(b). Of course, to be eligible, a customer must be "paying transition charges." *Id.* IPC's policy with respect to PPO eligibility is fully consistent with the statutory eligibility requirement that a customer be "paying transition charges to the electric utility" in order to receive PPO service.

Under Article IX, which is cross-referenced in § 16-112(a), utility rates must be just and reasonable. *See, e.g.,* §§ 9-101 & 9-201(c). As described below, the evidence demonstrates that IPC's MVI proposal is just & reasonable and sets "the market value for electric power and energy *as a function* of an exchange traded or other market traded index, options or futures contract or contracts applicable to the market in which the utility sells, and the customers in its service area buy, electric power and energy." § 16-112(a) (emphasis added).<sup>10</sup>

The General Assembly specifically permitted the Commission to make modifications to a utility's MVI proposal, but if the utility could not accept the modifications, they could not be imposed unilaterally; rather, the NFF process would continue. § 16-112(m). Therefore, the Commission must carefully consider which, if any, modifications will be accepted by each utility

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<sup>10</sup> It is important to note that § 16-112(a) speaks of "customers" and not "retail customers" (which the PUA specifically defines in § 16-102). The use of the term *customers* instead of *retail customers* makes perfect sense when one examines the context: when a utility has power to sell because a retail customer has decided to obtain power from an ARES, the most likely buyer will not be another retail customer, but rather a wholesale buyer, especially one who has load to serve because it is now serving retail customers in the utility's service area.

or face a continuation of a process that almost every party now acknowledges should be replaced.

See ICC Staff Ex. 3.0 at 14-16.

**II. Illinois Power's Methodology for Determining Prices under its Market Index Proposal should be Approved by the Commission.**

A. No Party Has Raised Any On-Peak Issues That Warrant Modifying Illinois Power's Proposal.

Illinois Power's proposal for calculating On-peak prices is straight-forward and has survived the attacks of the few parties who are not satisfied with it. Under Rider MVI, monthly On-peak prices are derived from two electronic exchanges (Altrade™ and Bloomberg Power-Match, the same exchanges used by Ameren and CE) and from one published survey (Power Markets Week).<sup>11</sup> IP Ex. 2.1 at 6. The data collected are for into-Cinergy hub forward prices. *Id.* The values used to calculate the On-peak market value are selected based on a hierarchy that uses actual transactions wherever possible and only uses bid-offer averages when no transactions are available for use. *Id.* at 8-9.

A Basis Adjustment is then applied to the market values because "while IP's and Cinergy's markets are closely correlated, they are not exactly the same." *Id.* at 12. Illinois Power's Basis Adjustment is a multiplicative one that creates a monthly ratio of the average On-peak Lower MAIN price over the On-peak Cinergy price using historic data. *Id.* at 12-13. Each monthly On-peak market value is then multiplied by the Basis Adjustment ratio for that month. *Id.*

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<sup>11</sup> Although IPC continues to be willing to consider other On-peak data sources, no party has come forth in their testimony with any additional sources of such data for the into-Cinergy hub.

1. *The Evidence is Overwhelming that the Appropriate Hub for IPC is Into-Cinergy (Into-ComEd v. Into-Cinergy).*

Currently, a viable into-IP hub does not exist. *See* IP Ex. 2.8 at 3. Therefore, some other trading hub must be used if parties are to move away from the NFF process. Through-out IP's case, only two trading hubs have been actively advanced by the parties: into-ComEd and into-Cinergy.<sup>12</sup> The choice is, and remains, clear: into-Cinergy is by far the best choice for IPC. First, the into-Cinergy hub "is reasonably close to the IP service area." IP Ex. 2.1 at 9. Indeed, "[m]arket participants in Illinois commonly trade in the Cinergy market." *Id.* The analyses of the Staff's witnesses Zuraski & Christ bear out the close relationship between prices for Cinergy and Illinois Power. *See* ICC Staff Exs. 3.0 at 23-28 & 4.0 at 10-26.

Second, the liquidity of the into-Cinergy hub exceeds that of the into-ComEd hub. ICC Staff Ex. 3.0 at 25. Indeed, during IPC's sample period (when we collected data from April 24-May 5), "we observed at least 103 actual trades in the sample and only one contract—April 2001—did not have any actual trades." IP Ex. 2.1 at 10.<sup>13</sup> During a similar period for CE, the Staff "noted the predominance of bids and asks as opposed to actual trades." ICC Staff Ex. 3.0 at 25. As many parties agree, the use of actual trade data is a better representation of the market's perception of value. *See, e.g.,* IIEC Ex. 1 at 12.

Third, the reasons noted above become even more important when one recognizes that "ComEd itself appears to dominate" (ICC Staff Ex. 3.0 at 26) the into-ComEd market in terms of trading activity. The same is *not true* of the into-Cinergy market, where not even a company as

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<sup>12</sup> In Subsection C below, we respond to the IIEC's arguments for either retaining the NFF values or delaying the current case while other alternatives are discussed and examined.

<sup>13</sup> Each snapshot looks separately at prices for each of the 12 subsequent months or "contracts."

large as CE would be in a position to control the pricing information that would be obtained from the data sources used in the tariffs. *Id.* at 27. Indeed, Staff's concerns are so great that they recommend that even CE use an into-Cinergy index. *Id.* at 27-28. While we offer no opinion on whether CE should do so, we certainly see no reason to change our index away from one that has more benefits than problems.

2. *Concerns Regarding the Manipulation, Thinness & Transparency of Electronic Trading Platforms Are Misplaced.*

The IIEC in particular has raised concerns about the use of electronic trading platforms as the source of data for the market value index. *See* IIEC Exs. 1 & 2. At the outset, it should be noted that IPC's proposal is to use more than just the two electronic exchanges—we also use a published survey—and we remain open to adding other reliable data sources. IPC's market basket approach dampens, if not eliminates, any concerns about the electronic exchanges:

Taken together, the basket of index sources creates a reliable supply of information that provides an adequate basis to establish a market value index. We believe that it is more likely to capture a greater percentage of the over-the-counter volume and reduce the ability of a single participant to bias the index. It also provides market participants with a variety of sources to obtain information, so regardless of their specific circumstances, they will have useful resources by which to track changes in the most volatile piece of the market value. Furthermore, Illinois Power has crafted Rider MVI to include only references to Appendix 1 so that as new reliable sources of information become available, we will be able to add them by altering the Appendix (upon proper approval from the Commission) and not have to change the underlying tariff language when we do so.

In combination with our monthly updates of the market values, IP's proposal surveys 120 business days worth data from three sources each to arrive at market values.

IP Ex. 2.1 at 12.

Nonetheless, even if IPC's proposal did not have this additional feature, concerns about the electronic exchanges are misplaced. The electronic exchanges serve as a reflection of the

overall market. *See* Tr. 808-09 (10/04/00). This is so even if the exchange does not include 100% of the trades made for any given trading hub. If the electronic exchange prices are not reflective of the prices obtainable from other sources (including those not posted publicly), traders will actively seek out opportunities to use those price differences to their economic advantage. *See* IP Ex. 2.6 at 14. Furthermore, even if someone thought he could manipulate the exchange prices, he would face a daunting task in light of the monthly re-valuations used in IPC's MVI. *See* IP Ex. 2.6 at 2-3. Finally, as even the IIEC's witness acknowledges, there are laws (which include criminal sanctions) addressing price fixing and other inappropriate use of market power. Tr. 201 (10/02/00).

Next, thinness is a relative concern. The market values set by the NFF for the year 2000 were based on a total of 32 contracts (and for some categories as few as 3). IP Ex. 1.1 at 6.<sup>14</sup> As noted above, in just one sample period, we observed 103 actual trades. Because IPC re-samples the data every month, this number represents only a fraction of the likely number of transactions that will be used to set IPC's market values over the course of a year.

Finally, transparency is unlikely to be a substantial problem for the customers likely to be buying the freed-up power and energy directly from Illinois utilities. *See* n.10, *supra*. "These exchanges are relatively low cost tools for trading desks, and it would not be unlikely to have both available within a given trading shop." IP Ex. 2.1 at 11. Furthermore, even some retail customers may have access to the trading platforms. *See* Tr. 726 (10/04/00) ("there are some IIEC members who have affiliates that are in the power marketing business."). IPC is also willing to work with the Commission's Staff to put in place an audit process that would help

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<sup>14</sup> While the NFF values for 2001 were based on more contracts, the NFF process itself has significant flaws that we detail in subsection C below.

Staff be satisfied that IPC's published values were accurate while nonetheless adhering to any restrictions imposed by the electronic exchanges. And, as we noted above, our inclusion of a printed survey that any party may purchase makes at least that portion transparent to all.

Given the above, the concerns regarding manipulation, thinness and transparency are not substantial enough to reject IPC's proposal.

3. *Illinois Power's Basis Adjustment is Supported by Staff and Should be Approved.*

Because of the lack of a viable into-IPC trading hub, Illinois Power proposed a non-IPC based index. To address concerns about differences between the chosen hub (into-Cinergy) and IPC's service area, we also proposed a basis adjustment. The adjustment compares historic Lower MAIN (in which IPC's territory is located) on-peak prices to into-Cinergy on-peak prices for the same months and creates a ratio that is then multiplied by the into-Cinergy forward prices to create adjusted market values. See IP Exs. 2.1 at 12-13 & 2.2.

The Commission's Staff performed a rigorous and thorough analysis of various possible basis adjustments. See ICC Ex. 4.0 at 11-28. In sum, Staff found that "the 'best' basis adjustment, among those I examined, is a multiplicative basis adjustment applied to monthly into-Cinergy forward on-peak prices," *id.* at 26, which is exactly what IPC proposed. See *id.* at 28.

Because no party seriously challenges IPC's basis methodology and because a rigorous analysis has found it the best, IPC's Basis Adjustment should be approved as proposed.

4. *IPC's Proposed Data Hierarchy Focuses on Actual Trades and Should Be Approved.*

In selecting data from the available sources, IPC's MVI proposal uses actual trades (as opposed to bid-offer averages) whenever an actual trade is available for the contract month at issue. IP Ex. 2.1 at 8-9. Where multiple trades occur for the month at issue, they are averaged

(and where possible, weighted averaged by volume). *Id.* When only one trade is reported, then it will be used. And, only if no trades are reported through-out the entire snapshot period will bid-offer averages be used. *Id.* Because of concerns when a single trade occurs for a particular contract, some have suggested that IPC be open to using more bid-offer averages. *See, e.g.,* NewEnergy Ex. 2 at 4. No one, however, has suggested that IPC's (or any other party's) proposal should be rejected due to hierarchy concerns.

Illinois Power's proposed hierarchy focuses on actual trades because an actual trade "clearly demonstrates a level at which agreement was reached on value, whereas the bid/offer represents a range in which one would expect to see eventual agreement." IP Ex. 2.8 at 4. Others concur in this assessment. *See, e.g.,* IIEC Ex. 1 at 12 (where Dr. Bowyer agrees that actual trade data is a better representation of the market's perception of value). And, with actual trades displacing bid-offer averages, it will be harder for someone to attempt to manipulate the market price. *See* IP Ex. 2.6 at 2. Thus, IPC believes its proposed hierarchy should be adopted.

One concern with using bid-offer averages is the fear that they may be manipulated. However, as some have noted, concerns of manipulation are less of an issue when an into-Cinergy index is used. *See, e.g.,* NewEnergy Ex. 2 at 8. Furthermore, we can understand the concerns of having a single contract trump a larger number of bid-offer averages. Therefore, if there is sufficient support for a change that incorporates more bid-offer averages, IPC would be willing to consider adopting that modification, depending on the exact details of the modification. *See* IP Exs. 1.6 at 3 & 2.8 at 4.

B. Off-Peak Prices are Less Volatile and the Use of Historical Data in that Context Should be Approved.

For the Off-peak period, IPC's proposal uses historic day-ahead data. *See* IP Ex. 2.2 at 5. While it might be preferable to use forward prices to set the Off-peak price, the data do not exist. IP Ex. 2.8 at 6. Rather, historic data is used, especially because Off-peak prices "have never been as volatile as On-peak prices which have experienced increased volatility in recent years." IP Ex. 2.1 at 13. We note that no party disagrees with this and the only debate is over whether the historic data should be adjusted to reflect different parties' perceptions of what the historic data represent. We address those issues in Section III.F, below, in accordance with the outline circulated by the Hearing Examiner.

Because more appropriate data do not exist and because Off-peak prices are relatively stable, IPC's use of historic data to set Off-peak prices should be adopted.

C. The Only "Other" Two Alternatives Presented in This Case Should be Rejected.

The IIEC has attempted to support two alternatives to the use of IPC's MVI: (1) continued use of the NFF; and (2) a yet-to-be-developed alternative. Both should be rejected.

One major reason IPC filed its MVI proposal was because the "NFF process, by its very nature, is flawed." IP Ex. 1.1 at 4. Thus far, the NFF has used stale and possibly distorted data to produce a single market price state-wide that (with the exception of the 2001 NFF values)<sup>15</sup> is derived from a very limited pool of contracts. *Id.* at 5-6. As designed by statute, the NFF process uses contracts that are months (and quite possibly years) old to determine the market

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<sup>15</sup> The additional contracts used to derive the 2001 NFF values do not save the NFF process. Indeed, the process used to set the 2001 values may have been the clearest example of how much of a black box the NFF process is. *See* ComEd Ex. 8 at 6. The NFF process is a statutorily-prescribed process over which the ICC has little influence or oversight. *See* § 16-112(b)-(j). Indeed, had the NFF itself not caught its own error, the 2001 NFF prices would have been over 50 mills/kWh in error on an around-the-clock basis. ComEd Ex. 8 at 6.

price for the future. *Id.* at 5. Furthermore, even though the statute (§ 16-112(d)) permits the NFF to create market values that vary by utility, thus far, the NFF has chosen to set only state-wide values, that are thereby inaccurate for all parts of the state. *Id.* In addition, the NFF sets prices on an annual basis, but the contracts he reviews may be multi-year contracts that are front-end or back-end loaded in terms of price. When this occurs, the distorted contract pricing can effect the NFF's price. *Id.* at 5-6. Finally, the NFF has historically had to rely on a very limited pool of data. For example, the entire 2000 NFF values were set using a total of 32 contracts (and in some sub-categories, as few as 3 contracts were used). *Id.* at 6.

These flaws in the NFF process have led to repeated years of inappropriate values being used for both TC calculations and PPO pricing. This is not to say that the NFF is not doing the best that can be done given the statutory process. But, the inappropriately low NFF values the last few years have been a direct hindrance to the development of competition in Illinois. *See id.* at 7. For example, IPC's sample MVI calculation performed at the beginning of the Summer showed that the 2000 NFF values were low by about 13.6 mils/kWh on a combined basis, with a low from about 9.5 mils to 15.1 mils depending on the class of customer at issue. *See IP Exs. 2.1 at 15 & 2.5.* The 2001 NFF values are higher than the 2000 values, but they are even "more problematic" because they have not properly taken into account the very large seasonal variation in electricity prices in the Illinois market. *IP Ex. 2.6 at 15.*

Given the significant flaws inherent in the process and the poor results produced by the flawed process, the *status quo* must be rejected. Indeed, the IIEC appears to begrudgingly acknowledge this by floating its alternative to the NFF process: an amorphous "combination index" that the IIEC would be willing to work with various parties to develop. *IIEC Ex. 2 at 14.* However, the need to replace the NFF process cannot wait if competition is to develop in Illinois.

IPC, like the Commission Staff, does not want “indefinite delay” (ICC Ex. 6.0 at 2) in selecting a better path than the current NFF process. If the IIEC wishes to discuss its concept with IPC, we would be willing to do so, but in the meantime, IPC’s MVI proposal should be allowed to help all retail customers eligible for choice in Illinois Power’s service area.

Because the NFF process is flawed (and cannot be fixed by this Commission) and because the IIEC’s alternative has not been sufficiently developed to even be debated in this case, the only viable alternative presented to the Commission in IPC’s case is Illinois Power’s MVI proposal. To help advance competition, IPC’s proposal should be adopted.

**III. None of the Pricing and Market Definition Related Issues Raised by Various Parties Warrant a Change in IPC’s Proposed Methodology.**

Several parties have raised a number of modifications to IPC’s MVI proposal. The evidence presented in this case, however, does not support any of these modifications.

**A. NewEnergy’s Optionality Adjustment (Load Uncertainty) is Unwarranted Based on the Evidence.**

NewEnergy proposes an adjustment for what it terms “optionality” which it describes as an adjustment to address load uncertainty. NewEnergy Ex. 4 at 9. This adjustment, however, should not be accepted for two fundamental reasons: (1) it is not warranted based on the record; and (2) even if the evidence could be read as demonstrating the need for such an adjustment, NewEnergy’s proposed methodology is flawed beyond repair.

Essentially, NewEnergy would like an adjustment to handle the fact that when it agrees to serve a customer’s load, the load to be served is not certain. *Id.* Whether couched as load variability insurance or optionality, the concept is the same: because no one can predict with perfect foresight the exact amount of electricity a customer will consume in a future period, the

ARES must (NewEnergy argues) be compensated for the risks it incurs in agreeing to serve that customer's electricity needs. *Id.* at 9-10.

Based on the record evidence, however, NewEnergy has failed to prove the need for any adjustment beyond those already incorporated in IPC's methodology. First, IPC already has a price shaping adjustment that "when applied to the customer's or class' load shape already adequately accounts" for the variability NewEnergy describes. IP Ex. 2.6 at 19. Furthermore, NewEnergy appears to only be concerned with the cost it might face. In taking this single-focused approach, it ignores the value an ARES may receive from a customer: "the customer by signing a fixed contract with the ARES bears a similar risk - which is in fact a potential benefit for the ARES." *Id.* at 20. The customer's usage may not be driven by market price. Thus, the ARES may well reap substantial benefits when a customer consumes less in a higher priced hour or more in a lower priced hour. *Id.* And, NewEnergy provides no evidence that when properly netted, any additional adjustment is warranted. These evidentiary problems with NewEnergy's concept are a sufficient basis to reject it.

Even if there were better evidence on the need for an "optionality" adjustment, the methodology proposed by NewEnergy to value the option is flawed. NewEnergy proposes the use of Black's model. NewEnergy Ex. 4 at 11-14. But, that model is inappropriate for use in this context. Black's model assumes that the option will be exercised every time there is money to be made in doing so. IP Ex. 2.6 at 21. This, however, is not how electric usage decisions are made. Rather, a change in customer "consumption is not influenced by the spot market price of electricity." *Id.* Furthermore, other facets of the model do not fit into the way electricity is consumed: because usage varies, a fixed, defined block of the underlying commodity does not exist; there is no public data source by which to price the price volatility component of Black's model;

and NewEnergy's proposal does not attempt to value the times when an ARES may benefit from the option (as opposed to have higher costs) as described above. *See id.* at 21-22. NewEnergy appears to realize that its use of Black's model leaves much to be desired. Indeed, it felt compelled to offer an "arbitrary adjustment factor" to the model, ComEd Ex. 4 at 17, in a further effort to get the model approved. However, the evidentiary voids left by NewEnergy's proposal cannot be filled by such a fudge factor.

In sum, the "optionality" adjustment should be rejected.

B. An Energy Imbalance Adjustment Is Not Warranted.

Both NewEnergy and CILCO argue for an adjustment to IPC's market values to reflect imbalance costs. *See* CILCO Ex. 1 at 3-4; NewEnergy Ex. 1 at 14-15. Imbalance charges are the charges a supplier incurs when the amount of load consumed by a customer does not match the amount scheduled for that customer. IP Ex. 2.8 at 1.

The most remarkable feature of these requests is that both recognize that this Commission has already decided the issue in the context of the delivery services cases and yet neither presents a single new piece of evidence in this case to warrant a departure from the Commission's prior decision. *See* CILCO Ex. 1 at 3-4; NewEnergy Ex. 1 at 14-15. Nonetheless, NewEnergy goes so far as to suggest that IPC is consciously underpricing its PPO service due to the way imbalance charges are handled in the PPO context. *See* NewEnergy Ex. 1 at 15-16.

First, imbalance is not always a cost, it may represent a credit to the ARES, a point that the ARES ignore (as with optionality) in arguing for an adjustment. IP Ex. 2.8 at 2. Second, imbalance is already handled in the price shaping adjustment. *Id.* Third, because imbalance is based on the difference between scheduled load and actual load, while TCs are based on the customer's historic usage (and not scheduled load), there is a mismatch in the ARES' proposals

and IPC's tariffs. Finally, any suggestion that IPC is somehow underpricing PPO service due to imbalance is inaccurate: "IP is following the Commission's approved tariffs." IP Ex. 3.7 at 3. And, no party has pointed to any place where IPC is not following its filed tariff on this issue.

In sum, the record evidence does not support an adjustment to account further for imbalance issues.

C. The Record Does Not Support a Planning Reserve Adjustment.

Based on a misunderstanding of IPC's requirements, some parties have requested an adjustment to account for a supposed requirement that the ARES carry a 15% planning reserve. CILCO contends that IPC requires "the retail supplier to obtain Planning Reserves." CILCO Ex. 1 at 3. The basis for this assertion is IPC's Network Integrated Transmission Service ("NITS") Application. *Id.* When properly understood, there is no basis for such an adjustment.

CILCO misreads our NITS Application and misunderstands the process. First, transmission service is not at issue in this case; market values for power and energy are. Nonetheless, even if transmission requirements and costs were relevant, even CILCO admits this topic is a non-issue with respect to point-to-point transmission service. CILCO Ex. 2 at 1. Finally, even with respect to network service, IPC's NITS Application states (as even CILCO does not deny): "MAIN currently *suggests* a 17 - 20% planning reserve margin of each year's maximum demand projection." IP Ex. 2.6 at 7 (emphasis added). IPC certainly believes that planning requirements help ensure system reliability, but the fact that we point out a *suggestion* made by MAIN on this topic is hardly evidence that we *require* such a reserve by an ARES. *Id.* Thus, CILCO's concern is a non-issue in all possibilities.

In surrebuttal, CILCO further confuses the issue by pointing to a conversation with an IPC representative and a contract CILCO signed with Ameren. *See* CILCO Ex. 2 at 2-5. Even

assuming CILCO's characterization of these events is accurate, they do not undercut the validity of IPC's position. Tr. 224 (10/02/00). The conversation bolsters IPC's point that the ARES is not the party who must provide an additional 15% reserve; rather, it is the seller of the wholesale block of energy. Tr. 225-26 (10/02/00). And, the Ameren contract essentially proves the point: CILCO had only to buy 100% of its needs, while the seller (Ameren) provided the reserves. Tr. 226 (10/02/00).

Notably, to provide a market value adjustment in such a case would be double counting. *Id.* In setting our non-firm energy price, IPC divides the firm number by a factor 1.15. This factor was set based on planning reserve issues. IP Ex. 2.1 at 8. By removing the planning reserve value from firm prices (a point to which no party has objected), all parties should also recognize that the firm price implicitly includes any planning reserve value and that an additional adjustment for this factor would be a double count.

The planning reserve adjustment should be rejected.

D. A Capacity Backed Adjustment Is Unwarranted.

In addition to its planning reserve adjustment, CILCO argues for an adjustment to account for capacity. CILCO Ex. 1 at 3-4. This adjustment also proceeds from a fundamental misunderstanding of IPC's proposal. In using into-Cinergy forward contracts, IPC is already using firm contracts. *See, e.g.*, IP Ex. 2.6 at 7-9. No party has presented any evidence that the value of the "Marketer Firm" energy that forms the basis for the forwards contracts is less valuable than other forms of firm energy. Indeed, given the financial ramifications of failing to deliver Marketer Firm energy, the value of such energy "is equal to or greater than the financial value" of other forms of firm energy and power. *Id.* at 8.

“[T]he supplier of Firm Energy is required to provide power to the customer unless a ‘force majeure’ event has occurred, and should it fail to do so, it is required to make the customer financially whole by reimbursing the customer for any replacement power costs.” IP. Ex. 2.6 at 8-9. On the other hand, “[i]f the Native Load or System Firm supplier curtails (System Firm) or proportionally curtails (Native Load Firm) as a result of system conditions, then the supplier does not incur any additional financial penalty.” *Id.* at 9. In sum, “[s]ince the supplier of Firm Energy has financial responsibility in situations in which Native Load Firm and System Firm suppliers do not, the financial value of Firm Energy is equal to or greater than the value of the Native Load or System Firm Products.” *Id.*

While the physical characteristics of the different types of firm energy may differ, this case is not about those physical differences but rather about value. Because the value of Marketer Firm is the same as or higher than other forms of firm energy, a further upward adjustment is unwarranted.

E. No Party Has Objected to IPC’s Non-Firm Adjustment.

No party has objected to IPC’s adjustment of firm prices to reach non-firm prices (by dividing firm prices by 1.15). This adjustment should be approved.

F. The Evidence Does Not Support an Adjustment to Historical Off-Peak Prices (“Dump Energy” Issue).

NewEnergy in particular argues that Off-peak prices should be adjusted upward because of the type of sales used to set that price. NewEnergy Exs. 4 at 3-7 & 3 at 10-15. IPC’s proposal sets Off-peak prices based on day-ahead historic values. IP Ex. 2.2 at 5. As explained above (at p. 15), historic data is a suitable proxy for future Off-peak prices because of the relative lack of