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October 12, 2001

VIA HAND DELIVERY

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Re: Docket Nos.: 000824-EI; 010577-EI and 001148-EI

Dear Ms. Bayo:

On behalf of Reliant Energy Power Generation, Inc., I am enclosing for filing and distribution the original and 15 copies of the following:

- Reliant Energy Power Generation, Inc.'s Posthearing Statement.

Please acknowledge receipt of the above on the extra copy of each and return the stamped copies to me. Thank you for your assistance.

Sincerely,

Joseph A. McGlothlin

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**BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION**

In re: Review of Florida Power Corporation's earnings, including effects of proposed acquisition of Florida Power Corporation by Carolina Power & Light.

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Docket No. 000824-EI

In re: Review of Florida Power & Light Company's proposed merger with Entergy Corporation, the formation of a Florida transmission company ("Florida transco"), and their effect on FPL's retail rates.

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Docket No. 001148-EI

In re: Review of Tampa Electric Company and the impact of its participation in GridFlorida, a Florida Transmission Company, on TECO's retail ratepayers.

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Docket No. 010577-EI

Filed: October 12, 2001

**RELIANT ENERGY'S POST-HEARING BRIEF**

Reliant Energy Power Generation, Inc. ("Reliant Energy"), through its undersigned counsel, submits this, its Posthearing Brief in the above dockets.

**PRELIMINARY STATEMENT**

As it has done throughout this case, in this Posthearing Brief Reliant Energy will focus on these aspects of the proceeding: (1) Will an RTO such as GridFlorida, Inc. be cost-effective for ratepayers?

and, (2) What policy position should the Commission adopt regarding GridFlorida?

### **BASIC POSITION**

\*An RTO such as GridFlorida is needed to eliminate the inefficiencies in Florida's transmission system, improve market performance, enhance reliability, and improve planning. The RTO will facilitate the development of a fully competitive wholesale generation market, thereby lowering costs to consumers. Properly viewed, the RTO is an opportunity to produce significant net benefits for ratepayers.\*

### **ARGUMENT**

(Because Reliant Energy believes the benefits to Peninsular Florida cannot be disassociated from the benefits to ratepayers, it will address Issues 2 and 3 together. Reliant Energy will then present a consolidated argument on Issues 2,3, and 4.)

**ISSUE 2: What are the benefits to Peninsular Florida associated with the utility's participation in GridFlorida?**

**ISSUE 3: What are the benefits to the utility's ratepayers of its participation in GridFlorida?**

**Reliant Energy:** \*Such features as the elimination of pancaked rates and the independent evaluation of interconnection requests will lead to lower transaction costs, a concomitant increase in the number of economically feasible transactions, the entry of new participants, and the reduction of market power, all of which translate to a more efficient, more competitive wholesale market and lower costs to ratepayers. At the same time, market-based mechanisms for managing congestion and a regional approach to planning will enhance reliability.\*

**ISSUE 4: What are the estimated costs to the utility's ratepayers of its participation**

**in GridFlorida?**

**Reliant Energy:** \*For purposes of this case, Reliant Energy has accepted the cost estimates provided by the GridFlorida applicants.\*

**ARGUMENT ON ISSUES 2, 3, AND 4**

Understandably, the Commissioners desire a "comfort level" regarding the ability of an RTO such as GridFlorida, the incremental costs of which will be borne by ratepayers, to produce net benefits to those ratepayers. Reliant Energy believes the record of this proceeding provides the basis for the Commissioners to support the RTO with confidence and, indeed, with enthusiasm.

The interest of regulators in the relationship between efforts to increase wholesale competition and customer benefits is not new. In 1996, the FERC estimated that removing inefficiencies and increasing competition would produce benefits to customers in the range of \$3.76 billion to \$5.37 billion on a national level. (TR-245). The belief that measures to that point were insufficient to develop wholesale competition led the FERC to issue Order 2000. (TR-245).

Two convictions formed the core of order No. 2000. The first was that a fully competitive wholesale market would lead to lower costs to consumers. The second was that inefficiencies in the existing transmission regime and the opportunity for the transmission owners to discriminate in favor of their own transactions were blocking the development of that competitive wholesale market. The problems range from the potential for vertical market power abuse, which can lead to discriminatory treatment in the calculation of available transfer capability ("ATC") and total transfer capability ("TTC"), to the adverse impact of pancaked transmission rates, to less-than-optimal transmission systems that suffer from parochial planning criteria. The FERC sought to address such obstacles through the formation of RTOs. (TR-245-246).

At the hearing in this proceeding, Reliant Energy sponsored the testimony of Robert Mechler, Reliant Energy's Manager of Transmission Policy. Mr. Mechler described specific obstacles to the development of competitive wholesale market in Florida. He explained how an RTO satisfying the parameters of FERC's Order 2000 would ameliorate or eliminate those obstacles. The benefits of forming an RTO would be realized in the form of lower transaction costs, increased competition by more players, better congestion management, and a system optimized by superior planning to satisfy local needs and the need to facilitate bulk power transfers.

Lower transaction costs. Mr. Mechler explained that Florida's Balkanized transmission systems and multiple control areas stack multiple "tollgate" transmission charges on transactions that cross system boundaries. The effect of multiple charges is to render many potential transactions economically infeasible. (TR-762-763). The RTO will eliminate such "pancaked" rates, thereby lowering transaction costs and increasing the number of economical transactions. By eliminating pancaked rates, the RTO will effectively increase the geographical dimensions of the wholesale market. (TR-763). Importantly, the producers who benefit from lower transaction costs will not be limited to new generators. Existing utilities also participate in the wholesale market, and they, like new entrants, will see an increase in the number of viable, cost-lowering transactions. (TR-802).

Independent control. Former FERC Chairman Hoecker explained that independent developers are reluctant to enter markets fully because of the ability of the transmission owners to discriminate in favor of their own transactions. (TR-246-247; see also TR- 823). An independent hand at the control of the transmission system will allay any perception or fear of discriminatory treatment, thereby encouraging more generators to enter the market. Mr. Mechler explained that an increase in generators should reduce market power and can place downward pressure on wholesale

rates, thus lowering costs to consumers. (TR-762).

Improved planning. Several witnesses testified that the RTO's regional perspective will lead to a better planning process. (TR-764; 249; 111). Mr. Mechler explained that a transmission system designed and built to serve a single utility differs significantly from a system that reflects an integrated, regional approach. (TR-764) By planning with a regional perspective, the RTO will better optimize local needs with the need to facilitate bulk power transactions. (TR- 765). Over the longer term, then, the RTO's planning process should result in a more efficient, lower costing system.

Better congestion management. Presently, when a component of a transmission system becomes over scheduled, transactions must be curtailed. (TR-814) In some circumstances, this will result in a failure to serve certain customers. (TR-814) Because the RTO will be able to "see" the entire region, it will have more resources with which to manage congestion. (TR-785). Rather than curtailing service to solve congestion, the RTO will attempt to find alternative transactions that will relieve congested interfaces. The reliance on market-based mechanisms rather than curtailment will enhance the reliability of the system. (TR-763-764; 814).

The RTO will lower costs to consumers. During cross-examination, the example of California was held up to Mr. Mechler, with the suggestion that, depending on the supply/demand relationship, the effect of the RTO might be to increase wholesale prices. (TR-776). The California example was misplaced. Unlike California, the GridFlorida applicants consciously included within the RTO a provision (Installed Capacity and Energy, or ICE) designed to ensure that Florida will maintain an adequate supply of capacity over time. (TR-354-355). Independent operations and other market design features designed to attract new producers will only enhance the adequacy of supply. (TR-799).

The cost hurdle that the RTO must clear to begin to deliver net benefits is small when viewed in relative terms. During cross-examination, it was pointed out that the witnesses who support the RTO have not quantified the net benefits that the RTO will deliver to customers. It is true that benefits cannot be measured before they occur. However, it is possible to quantify the *known* facts that demonstrate the opportunity to reduce costs, and the *known* relationships that will govern the probability of receiving net benefits. As Mr. Mechler acknowledged, the incremental costs associated with forming and operating the RTO are "not small numbers." (TR-765). However, he also pointed out that the numbers must be examined in the overall context of the costs of generating and delivering electricity. (TR-765-766). Based on information provided by the GridFlorida applicants in this proceeding and in an earlier ITA presentation, Mr. Mechler showed that the costs of generation are approximately *18 times* as great as the total costs of transmission. (TR-767). Accordingly, while GridFlorida would (for example) increase TECO's costs of transmission by 23%, a reduction of only 1.3% in the generation costs paid by TECO's customers would completely offset all TO-related costs: *all reductions in generation costs beyond the 1.3% breakeven point would be gravy for the ratepayers!* (TR-766). Based on these known, *quantified* relationships, Mr. Mechler pointed out that if generation costs are reduced by a conservative 5%, then the ratio of savings to costs would be greater than four to one. (TR-767). To illustrate Mr. Mechler's point further, if RTO-related costs are in the vicinity of \$150 million, and the RTO succeeds in lowering generation costs by only 5%, then related savings to ratepayers would be approximately *\$600 million*. And, while the costs of the RTO provided by GridFlorida applicants are estimates, and Mr. Mechler used generic information regarding the relationship of total transmission costs to total generation costs, the disparity between the two categories of costs is so great that a very significant change in one or

the other would be necessary to alter the savings-favoring relationship in a material way. (TR-767).

Certainly the law of supply and demand underlies the assumption that competition lowers costs, but the confidence that an RTO will produce net benefits in Florida is not based on economic theory alone. Mr. Mechler testified that 50% of all generation capacity in Florida is more than 20 years old; 25% is more than 30 years old. (TR-767). Such aging plants are inefficient and can be economically displaced by new, highly efficient technology. For this reason, Florida is attractive to independent developers of wholesale power generation projects.(TR-767-768). The extent to which cost reductions surpass the breakeven point will be a function of the depth and liquidity of the wholesale market. Florida needs only a framework that enables efficient transactions and encourages competition, and (economic) nature will take its course.

**ISSUE 7: What policy position should the commission adopt regarding the formation of GridFlorida?**

**Reliant Energy:** \*To maximize savings to consumers, the Commission simultaneously should support GridFlorida and work to increase the depth and liquidity of the wholesale market. Like Reliant Energy, the Commission can support GridFlorida on an overall basis while reserving its right to advocate different positions on specific details.\*

#### **ARGUMENT ON ISSUE 7**

It was suggested during cross-examination that the Commission should not support the formation of an RTO until the Florida Legislature amends the Florida Electrical Power Plant Siting Act to allow merchants to construct and operate combined cycle units having a steam cycle in excess of 75 MW. The Commission should reject this argument. As was pointed out earlier, new generators are not the only entities that will benefit from a lowering of transaction costs and an



effective expansion of the geographical wholesale market in peninsular Florida. Load-serving utilities also engage in wholesale transactions, which will increase, to the benefit of end use customers, when the RTO eliminates pancaked rates. (TR-802). Further, under existing law new entrants can build combustion turbines of any size and combined cycle units that do not exceed the threshold of the Siting Act. (TR-110). As Mr. Mechler stated, this is not a "chicken and egg" situation. (TR-798). To regard a change in the Siting Act as a condition precedent to an RTO would be to forgo significant improvements that can be made to the wholesale market now under existing law.

Nor is it necessary for the Commission to agree with every choice made by the GridFlorida applicants to support the continued formation of the RTO. (In fact, Reliant Energy disagrees with the decision to allocate transmission rights to incumbents rather than to auction them.) However, representatives of GridFlorida applicants stressed that a feature of the RTO design that is in effect on "day one," can be revisited by the RTO's Board and can be changed prospectively if experience indicates a better choice is available. (TR-364-365; 485; 493; 519). Because mechanisms for change are incorporated into the structure of the RTO, the Commission -- like Reliant-- can support GridFlorida as a matter of broad policy, while it reserves the right to disagree on specific points.

**Issue 11: Is a Regional Transmission Organization for the Southeast region of the United States a better alternative for Florida than the GridFlorida RTO?**

**Reliant Energy:** \*Timing is the paramount consideration. Presently, GridFlorida appears to offer the quickest route to the realization of the benefits that an RTO will afford. The Commission should support the formation of GridFlorida until sufficient information is available to demonstrate that the Southeast RTO would be better for ratepayers.\*

## ARGUMENT ON ISSUE 11

The frustration of the Commissioners over the inability of the GridFlorida applicants to make a definitive case for either GridFlorida or the larger Southeast RTO was palpable. Currently, the situation is unclear at best. While Reliant Energy is aware that a larger RTO can increase the available benefits if properly structured, Reliant tends to agree with the witnesses who said that more details must be known about how the Southeast RTO will be structured before a decision to abandon GridFlorida can be made intelligently. (TR-796-797). Additionally, the Commission should adopt the view that no time should be lost in implementing an RTO. (TR-768). At this point, the decision should be to support GridFlorida unless and until a better alternative for Florida's ratepayers is presented.

## CONCLUSION

If GridFlorida achieves reductions in generation costs of only about 1.3%, those modest reductions will completely offset the incremental costs of forming and operating the RTO. Reductions greater than this "breakpoint" will yield net savings to customers. If the Commission has any confidence in the ability of vigorous competition to lower costs, this is not a close call. The Commission should approach the formation of the RTO as an opportunity. Because the extent to which the ratepayers benefits will depend on the extent of wholesale competition, the Commission should support GridFlorida and pursue those measures that will foster the development of a deep, liquid wholesale market.

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## CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing the Reliant Energy Power Generation, Inc.'s Posthearing Brief has been furnished by (\*) hand delivery and U.S. Mail to the following this 12th day of October, 2001:

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