

April 30, 2002

North American Energy Standards Board  
1100 Louisiana Street  
Suite 3625  
Houston, Texas 77002

Attn: Ms. Rae McQuade

Dear Rae:

We are writing on behalf of National Grid USA to express concerns and submit suggestions on the wholesale electric industry negotiations regarding formation of a standards setting organization (“SSO”), which are currently being hosted by NAESB. While our suggestions call for some departures from the approach used at the April 5, 2002 meeting in Houston, we believe that these changes will greatly improve the negotiation process.

Please do not interpret our concerns as criticism of your indispensable work in support of the wholesale electric industry negotiations over the past several months. Indeed, we look forward to continuing to work with you, as well as the other NAESB staff. Nor do we attribute any partisan or obstructionist agenda to NAESB itself. It appears to us that the problems we have identified arise from a well-intentioned but ill-considered effort to expedite the process of formation of the NAESB Wholesale Electric Quadrant (“WEQ”). Unfortunately, in ignoring certain procedural guidelines that were established and committed to earlier in the negotiation process, this well-intentioned effort threatens to disrupt and derail, rather than expedite, the WEQ formation process.

#### Meeting Procedures

NAESB has already made a good start toward resolving several of the problems that arose at the April 5 meeting. In response to the complaints of meeting participants, NAESB has (1) given timely notice of the upcoming May 8-9 meeting, (2) circulated a “straw man” draft of proposed WEQ procedures well in advance of that meeting, and (3) proposes holding a “confirmation vote” on the matters “approved” on a “straw vote” basis during the April 5 meeting’s rather chaotic voting process. We endorse all of these steps, and are heartened by NAESB’s manifest willingness to correct past errors. We are also encouraged by your agenda’s inclusion of an initial period for discussion of procedural matters at the May 8-9 meeting. We believe that an agreement on procedure is essential to the sound progress of the negotiations, and to the parties’ confidence in their fairness. While such a procedural discussion could require a greater investment of time than that reserved on the agenda, we believe that allowing this time will pay handsome dividends in the avoidance of disruptive and time-consuming procedural quarrels later on.

There are several other important issues that we believe should be resolved during the procedural discussion. We address each of these briefly below.

## Conduct of Meetings

First, we believe it is crucial for the Joint Industry Group to agree in advance upon a clearly defined set of fair and workable rules regarding how issues shall be raised and decided during the negotiations. During the April 5 meeting, it appeared that the meeting facilitator took up issues for discussion and decision based on purely subjective criteria, even ignoring motions that appeared properly brought and seconded if they did not fit his preferences. Furthermore, the lack of clarity surrounding the voting rules invites opportunism as many participants are unable to fully exercise their rights under an ill-defined system. Such meeting management is a prescription for controversy, virtually guaranteeing that some participants feel disenfranchised, and compelling them to find other – and potentially more fractious – ways of injecting their views into the process.

Consequently, it is important during the threshold procedural discussion on May 8 that the group reach consensus on an orderly and fair mechanism for deciding what issues shall be taken up for discussion and decision. This should be presented not as a *fait accompli*, but as a proposal for discussion and ratification by the group. There are well-established models of “parliamentary procedure” that can be adapted to our negotiations, and which should be acceptable to the group.

Second, we believe that a truly fair and neutral process cannot give one or a small group of participants a greater opportunity for input than others. In light of some of the remarks made publicly on April 5<sup>th</sup>, it should now be abundantly clear to NAESB that permitting any stakeholder faction, let alone a single participant, the opportunity to present and take questions on an un-vetted “straw man” proposal is highly inappropriate and entirely unacceptable. While we recognize that NAESB sees itself as a volunteer organization, the apparently arbitrary elevation of one of the negotiation parties to the level of formulator and moderator suggests that NAESB may not be sufficiently aware of how seriously many participants take this process, and how strongly they wish to preserve its fairness and evenhandedness.

Pursuant to this, it will be important for NAESB to present one or more neutral and thoroughly-vetted “straw man” WEQ procedures proposals at the May 8-9 meeting. The person or persons collecting and incorporating comments and presenting the “straw man” proposals to the group should be a neutral party, and certainly not anyone affiliated with any of the negotiation participants, or who has an agenda with respect to the outcome. This role was played (quite successfully, in our view) by Ken Kearns during the period that EEI hosted the wholesale electric negotiations. NAESB needs to identify a similar neutral, trusted, and experienced facilitator to be responsible for presenting the “straw man” proposals.

Third, we strongly recommend that the same neutral, trusted, and experienced facilitator also be engaged to run the negotiation sessions themselves. While the gentleman who acted as facilitator at the April 5 meeting was undoubtedly well-meaning, his apparent lack of experience managing contentious negotiations created unnecessary friction and ill feeling. In such meetings, well-intentioned attempts to expedite discussion may too easily manifest as apparent disrespect for or partiality among participants. Because of his long experience, Ken Kearns was usually

able to move discussions along without making any participant(s) feel slighted or unfairly dismissed. We would favor hiring either Ken or some other neutral and experienced facilitator to run the May 8-9 meeting and subsequent meetings.

### Consensus Orientation

Even more important than the foregoing is the absolute necessity for the wholesale electric industry group to return to the consensus orientation it has maintained from the beginning of its discussions, but which was abruptly jettisoned without notice or justification at the April 5 meeting. As the very close votes at the April 5 meeting (34 to 16 and 35 to 17, which latter result would have been reversed by a single vote) emphasized, the arbitrary two-thirds voting rule does *not* represent a consensus process. This abandonment of the consensus process violates both the letter and spirit of FERC's order regarding the formation of a standard setting organization, as well as commitments previously made by the wholesale industry group, as we show below.

First, as you know, the FERC Order mandating the wholesale electric industry discussions required that the industry reach a "consensus" position regarding the wholesale electric standards-setting process, with consensus defined in the Order. *See* Electricity Market Design and Structure, 97 FERC ¶ 61,289 (2001) slip op. at 1. Nothing has happened in the interim to change the FERC mandate, or to weaken the consensus requirement. Even if the wholesale electric industry group were now functioning as the WEQ within NAESB (which, according to the NAESB Bylaws, will not happen until the procedures presently under discussion are accepted by the NAESB Board, *see* NAESB Bylaws, Sec. 19.3), this would certainly not have the effect of changing or weakening FERC's consensus requirement. As you know, industry participants are obligated to comply with FERC orders without regard to the extent with which they are at odds with the rules and procedures of other organizations.

Second, NAESB's own Certificate and Bylaws provide that decisions within the organization be made by "consensus." *See e.g.* NAESB Certificate, Art. III, Sec. 5(a); NAESB Bylaws, Sec. 2.2(b). While it is true that a two-thirds voting mechanism is used in some parts of NAESB's decision processes, this mechanism exists within the context of many other checks and balances (including multiple votes in multiple venues, subcommittees, comment opportunities, approval steps, etc.), which, taken together, ensure that resulting decisions really do reflect a consensus of participants. The two-thirds voting mechanism alone, stripped out of this overall process, cannot make the same claim; as a result, the use two-thirds voting mechanism alone in forming the WEQ procedures does not satisfy NAESB's own policy of reaching decisions by consensus.

Third, both the EEI-sponsored Joint Industry Filing and the EPSA Filing, submitted to FERC on March 15, 2002, which filings were either signed or supported by most of the utilities filing on March 15, contain language committing the wholesale electric industry group to post-March 15 negotiations on segments and voting procedures that protect minority interests. *See* Joint Industry Filing at 13; EPSA Filing at 19. Consequently, most of the wholesale electric industry group has already committed to such procedures. This commitment cannot simply be discarded now. For the group to now take an approach that will inevitably strip away rather than

retain minority interests – as the abandonment of the consensus mechanism will do – is a violation of this prior commitment.

Finally, from a practical point of view, abandonment of the consensus orientation of the wholesale electric industry group will ultimately result in undue delay of the process for developing the standards setting procedures. This is because many of the participants in the current negotiations agreed to enter these negotiations and support one or more of the March 15 filings on the express understanding that the standards setting process would be developed on the basis of the consensus process mandated by FERC and adopted and committed to by the industry group. If this condition is violated, some participants may no longer see either the process or its probable results as just or broadly representative of the industry's vision of a fair and effective standards setting organization. Rather, the likely outcome of NAESB's acquiescence in the abrogation of the participants' commitment to truly balanced voting will be the disenfranchisement of entire sectors of the industry. Those that occupy those sectors will be compelled to seek an alternative venue that offers every stakeholder a meaningful and effective voice in the formation and approval of wholesale electric standards. Surely the appeal that expedition offers to the process does not merit such a result and its attendant consequences for NAESB's solid record of achievement in providing a forum for development of procedures that accomplish true industry consensus.

Consequently, we strongly urge NAESB to reverse its abandonment of the consensus process. While reaching consensus can involve an intense process of discussion and compromise that may seem somewhat less than expeditious, we should be encouraged by the progress that was achieved on many difficult issues during the EEI-sponsored meetings prior to March 15. Proposals and cross-proposals on segments, sub-segments, and voting rules had been circulated, and a compromise was nearly reached, though the completion of a final agreement on such matters needed to be postponed to the period after March 15 mainly because there was not enough time to work out all the details before the FERC filing was due. Nevertheless it was clearly understood that the industry would proceed on the principle that minority interests will be protected, something that was explicitly acknowledged in the Joint Industry and EPSA filings.

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We sympathize with your position as interlocutor between the diverse and strongly held positions of the wholesale electric industry negotiation participants. However, we believe that your task will be greatly facilitated if NAESB adopts rigorously fair and neutral meeting rules that are supported by as large a majority as possible of the participants. We pledge to do whatever we can to assist you in realizing this vital objective.

Sincerely,

Jamil E. Nasir  
Swidler Berlin Shereff Friedman (for National Grid)