



RTO West Technical Conference

Background for Concern

May 24, 2001



- RTO West's Liability Issues are complex
- State law cannot be relied upon to create a balanced risk allocation package for RTO West
- Certainty as to the allocation of risks is necessary to ensure full participation in RTO West and to assure cost containment



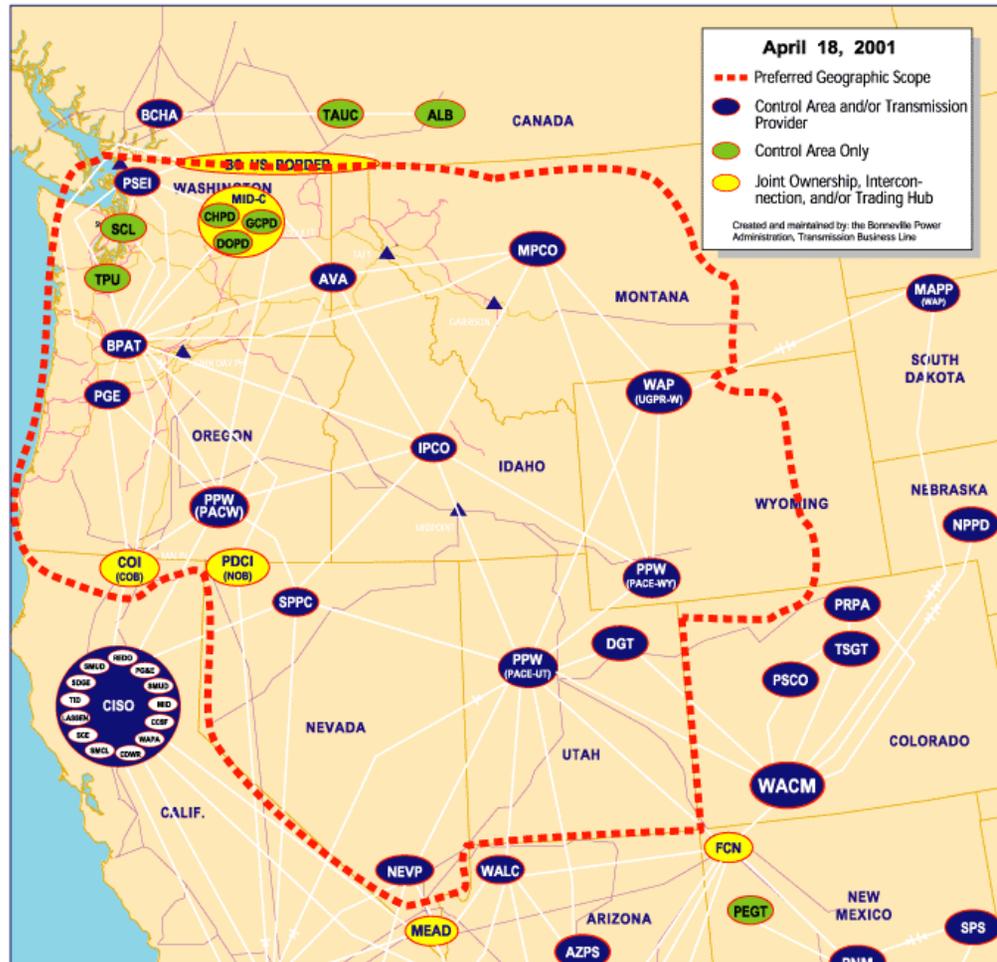
Why RTO West's Liability Issues Are Complicated

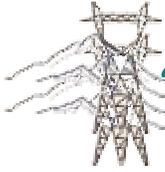
- Hydroelectric Base In NW
- Approximately 75% of transmission is owned by governmental entities
- Geographic area covers multiple states (included retail access states)
- Region wants to preserve the current benefits associated with the WIS Agreement Limiting Liability
- California conditions are increasing the potential for service interruptions and litigation
- Washington state law imposes liability for the failure to timely restore service in the event of an outage



Geographic Scope

- Includes:
 - AVISTA, BPA, PGE, PacifiCorp, Idaho Power, Montana Power, Sierra Resources, Nevada Power and Puget Sound Energy facilities.
- Covers:
 - > 90% existing high voltage facilities in proposed region
 - > 51,000 line miles
 - ~ 580,000 square miles
- BPA
 - ~ 70% high voltage in NW





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State Law Remedies Not Effective Protection

- Retail Tariff Limitations on Liability Not Applicable as States Not Setting Transmission Rates
- Multi-state Service Area
 - Different Law (e.g. punitive damages, comparative fault, rights to contribution, vicarious liability, active-passive indemnity, joint and several liability, duty to mitigate, strict liability, indemnification)
 - Impractical to go to each state
 - Potential for Discrimination
 - Muni/PUD Participants Cannot be Subjected to Law of Another State
- BPA subject to Federal Tort Claims Act



Current Liability Protection

- Duty only to one's own customers regarding service
- No duty to customers of another utility regarding service
- No duty to build facilities for another utility or entity outside of OATT



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Present Liability Protection for IOU Participants

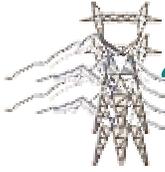
State Tariffs

- Limit liability for service interruption
- Vary by state in language and enforcement
- Effectively limit tort liability exposure as a condition of setting rates, terms & conditions of service



Present Liability Protection for Governmental Entities

- Sovereign Immunity or Limited Waivers of Sovereign Immunity (e.g., Federal Tort Claims Act)
- Appropriations limit financial obligations
- Discretionary immunity
- Limitations on Authority (Ultra Vires)
- Jurisdiction Specific Requirements



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Present Liability Protection Contracts for Participants

- Limitations on liability (consequential damages/ indemnity/concurrent negligence/ waiver of workman's comp)
- Force Majeure
- Bilateral/no third party beneficiary
- Additional Insured Requirement
- Protective Relay Requirements

Liability Uncertainty

- Duties may be created (design, installation, replacement, operation & maintenance),
- Those duties may be breached
- It is foreseeable that breach of duty may proximately cause damages to others
- Such damages may occur impacting multiple users, over a large geographic area
- Will RTOs have unlimited liability for outage events to Customers/End Users and how will such be paid if allowed to occur?



FERC's Guidance

- FERC says Order 888 not intended to preempt state liability standards (otherwise notice required) [Transmission Access v. FERC, 225 F.3d 667, 728 (D.C.C. A.; 2000)]
- Most state liability standards are based upon tariff limitations on liability; states don't set rates or approve open access transmission tariffs.



FERC's Guidance

- State law remedies include contract remedies that FERC has foreclosed (indemnity, limitations on damages)
- In RTO West Order, FERC distinguished all previous FERC precedent approving limits on liability by stating that “all predate Order 888 and do not involve open access transmission service.”



FERC's Guidance

- Contract Protection After FERC Opinion:
 - “No” on indemnification (RTO West’s Submission did not include indemnification, except for “contact” claims where RTO West is in control of Owner’s transmission.)
 - “No” on limitation of consequential damages (at least for “lost opportunity costs” for generators with redispatch order)



- Contract Protection After FERC Opinion:
 - Confuses Allocation of Liability For First Party and Third Party Claims
 - Confuses Tariff Limitations on Liability for Service Interruption with Indemnification
 - Conflicts with Existing WIS Agreement Agreement
 - Fails to Recognize Unique Makeup of RTO West Participants (Public & Private) & Multi-State Service Territory



Uncertainty Caused by RTO West Order

- Contract Protection:
 - No effective limitation with force majeure?
 - No limitation on liability to preserve system reliability?
 - No effective limitation on consequential damages?
 - No effective limitation on end user claims?
 - WIS Agreement Limiting Liability effect is uncertain



Uncertainty Caused by RTO West Order

(continued)

- Insurance Protection:
 - Appears to be only available protection -- recoverable in rates (2nd NY ISO Order)
 - Single state RTO risk assessments offer greater certainty than multi-state RTOs
- Insurance Uncertainty:
 - Will insurance remain available?
 - At what cost?
 - With what retention level?
 - What amount is adequate if there are new duties created, no tariff protection, no contract protection, no limits on damages?



Uncertainty Caused by RTO West Order

(continued)

- Without Insurance or in the event of under insurance:
 - Are liability costs recoverable in rates?
 - What working capital credit line for liability is appropriate?
 - What is the mechanism for prompt recovery of liability costs in rates?



Use Civil Actions to Promote Reliability?

- The RTO is unable to anticipate the nature and size of claims that can be incurred with service interruptions
- Customers are in better position to ascertain their potential losses with service interruption and either obtain insurance or otherwise protect themselves.

See Application of C P&L, Tex PUC (No.3198, 7 TEX. P.U.C. Bull 53 (June 22, 1981); Accord, HL&P v. Auchan, 995 SW2d 668, 672-673 (1999))



Liability Uncertainty Is A Significant Issue

- Leaving liability risks uncertain will:
 - Increase transmission costs
 - Increase insurance costs (assuming insurance is available)
 - Reduce chances of voluntary participation in RTO West because of concern that IOUs could lose assets should RTO West's liability exceed available RTO West assets



What Can Be Done?

- If RTO West has to go to each state for liability protection:
 - It will take significant time
 - We also have to have a remedy
 - It can't be a tariff limitation on liability because the state(s) won't be setting the RTO's tariff.
 - It would likely have to be in the form of legislated limited immunity
 - What is the incentive for a state to limit liability for service interruption? Different rates for those states that do?



Other Policy Issues Exist

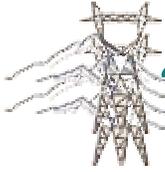
Commission Order does not provide an effective mechanism to motivate generators, distribution utilities, and end use customers to provide appropriate protection with outage events.



Other Policy Issues Exist

If RTO West were to be required to guarantee continuous service, and stand ready to pay for all damages incurred as the result of any service interruption:

- Insurance Would Not Likely be Available
- Rates Would Be Impacted Significantly
- Those With Less Sensitive Service Needs Will Pay the Costs for All
- There Would be Little Motivation for Self-Protection
- RTO Participation Level Would Be Impacted Significantly



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Other Policy Issues Exist

If No FERC Tariff Protection Available:

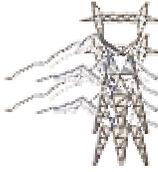
Wholesale transmission (not protected by tariff) and retail service (protected by state tariff) will not be “equal” ---- liability risk should be the same to promote “non-discriminatory” access



Other Issues Exist to Impact Liability

Impact of WSCC/WECC --- NERC/NAERO Reliability Management Standards (RMS)

- Many standards have yet to be written
- Impact of system of required information dissemination, “rules of the road,” self-reporting of “violations;” citation and adjudicative process to assess responsibility
- While this is a “coming event” RTOs will need flexibility and liability protection for implementation



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Use Civil Actions to Promote Reliability?

- Dollar damages may prove catastrophic
- All participants are not equal (liability & ability to pay)
- Liability may well result without responsibility for the initiating event
- Different results in different states
- Rates will increase significantly
- RTOs will go bankrupt if there is no adequate protection from liability--then what?



The Threat of Outage Litigation is Real

- August 1996 West Coast Outage Event
 - Maxim v. USA (BPA) and PG&E
 - Mobil Oil v. SCE
- July 1999 Outage Events in Northeast
 - Class Actions v. GPU Energy
 - Multiple Actions v. Consolidated Edison (class certification denied)



The Threat of Outage Litigation is Real

- Texas PUC Ordered Tariff Limitations on Liability for Texas Transmission Utilities (Feb. 9, 2001)
- Load Shifts Due to Market Conditions (California)
- Drought and Fish Issues Impact Hydro Conditions in NW When There are Supply Shortages



FERC Does Have Authority

- Primrose v. Western Union, 154 U.S.1 (1894)
[Limit of Liability Appropriate common law contractual remedy if no willful misconduct/gross negligence]
- Western Union v. Esteve Bros, 256 U.S. 566 (1921) [Appropriate for I.C.C. to approve rates limiting liability]
- Southwestern Sugar v. River Terminals, 360 U.S. 411 (1959) [permitted tariff limitation as part of approved rates for tugboats pulling barges]



Few Courts Have Invalidated Tariff Limitations on Liability

Kansas [McNally Pittsburgh Mfg v. Western Union, 353 P.2d 199, 203-205 (1960); but see Burdick v. SW Bell, 675 P.2d 922 (1984); Danesco USA v. KCPL, 999 SW2d 326 (1999)]

New Mexico [Sw Pub. Svc v. Artesia Alfalfa Growers, 353 P.2d 62, 68-71 (1978); effectively superceded by legislative adoption of statutory immunity for failure to supply adequate supply of gas, water, electricity or other services.]



What is Our Goal

- Have Some Effective Forum and Means to Address Risk Allocation Issues to Enable Participation
- Eliminate or Reduce Uncertainty to an Acceptable Level
- Clearly Understand FERC Guidance
- Attempt Mutually Acceptable Solutions to Allocation of Liability Risk