

ALASKA LEGISLATURE COMMITTEE FILES 1999-2000 8672

9908 HOUSE LABOR & COMMERCE

underscored material = new
~~[bracketed material] = delete~~

1 procedures are in place to maintain safe and reliable electric
2 service;

3 (5) ensure that residential and small
4 business customers are not unduly harmed by restructuring;

5 (6) require that customer information about
6 customer choice be appropriate and adequate to ensure informed
7 decisions by the state's citizens;

8 (7) ensure that all retail customers continue
9 to be offered electric service; and

10 (8) protect the financial integrity of public
11 electric utilities during the transition to a competitive
12 marketplace.

13 Section 3. DEFINITIONS.--As used in the Electric Utility
14 Industry Restructuring Act of 1999:

15 A. "ancillary services" means those services that
16 are auxiliary to basic generation, transmission or
17 distribution services, but are determined by the commission to
18 be necessary for the provision of the basic generation,
19 transmission or distribution service being provided;

20 B. "affiliate" means a person who directly or
21 indirectly, through one or more intermediaries, controls or is
22 controlled by, or is under common control, with another
23 person. Control includes the possession of the power to
24 direct or cause the direction of the management and policies
25 of a person, whether directly or indirectly, through the

Ohio

Signed
6 July 1999

To be Reported by the Senate Ways and Means Committee

May 18, 1999

123rd General Assembly
Regular Session
1999-2000

Sub. S. B. No. 3

SENATORS JOHNSON-FINAN-BLESSING-HERINGTON

A BILL

To amend sections 113.061, 133.04, 715.013, 718.01, 1551.33, 1551.35, 3317.028, 4905.01, 4905.02, 4905.03, 4905.10, 4905.14, 4905.34, 4905.40, 4905.42, 4905.70, 4906.10, 4909.01, 4909.05, 4909.15, 4909.161, 4911.18, 4933.33, 4933.81, 4935.04, 5117.01, 5117.02, 5117.03, 5117.04, 5117.05, 5117.07, 5117.08, 5117.09, 5117.10, 5117.12, 5701.03, 5703.052, 5703.053, 5703.14, 5705.34, 5727.01, 5727.02, 5727.05, 5727.06, 5727.11, 5727.111, 5727.15, 5727.30, 5727.31, 5727.311, 5727.32, 5727.33, 5727.38, 5727.42, 5727.45, 5727.47, 5727.53, 5727.60, 5727.61, 5727.72, 5727.99, 5733.04, 5733.05, 5733.06, 5733.09, 5733.98, 5739.011, and 5739.02; to enact sections 4928.01 to 4928.20, 4928.31 to 4928.45, 4928.51 to 4928.58, 4928.61 to 4928.63, 5727.03, 5727.80 to 5727.95, and 5733.39; and to repeal sections 4905.301, 4905.66, 4905.67, 4905.68, 4905.69, 4909.157, 4909.158, 4909.159, 4909.191, 4909.192, 4909.193, 4913.01, 4913.02, 4913.03, 4913.04, 4913.05, 4913.06, 4913.07, 4933.27, 4933.34, 5727.231, 5727.391, and 5727.73 of the Revised Code to provide for competition in retail electric service, including provisions regarding market structure, consumer protection, competitive auctioning, and transition revenues; to levy a kilowatt-hour excise tax on electric distribution companies; to revise taxes for electric companies and rural electric companies; and to reduce tax assessment rates on certain electric company and rural electric company tangible personal property.

BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF OHIO:

AUTHORIZE THE ELECTRIC DISTRIBUTION UTILITY, THROUGH THE FILING OF REVISED DISTRIBUTION SERVICE SCHEDULES UNDER SECTION 4909.18 of the Revised Code, TO RECOVER UP TO SUCH AMOUNT OF THE LOSS AS THE COMMISSION CONSIDERS REASONABLE UPON A DETERMINATION THAT THE UTILITY SUPPLIED THE SERVICE AT THE LEAST COST GIVEN MARKET CONDITIONS AT THE TIME.

(H) THE COMMISSION SHALL ADOPT RULES UNDER DIVISION (A) OF SECTION 4928.06 of the Revised Code ENSURING FAIRNESS IN THE AUCTION PROCESS AND THE PERFORMANCE OF A WINNING BIDDER, AND PROVIDING FOR DEFAULT SERVICE IF A WINNING BIDDER FAILS TO PERFORM UNDER THE TERMS AND CONDITIONS APPLICABLE TO ITS PROVISION OF SERVICE.

(I) AN AUCTION CUSTOMER MAY OPT OUT OF AN AUCTION POOL UNDER THIS SECTION AT ANY TIME UPON PAYMENT OF ANY APPLICABLE SWITCHING FEE, WHICH FEE SHALL BE A NOMINAL AMOUNT BASED ON THE WINNING BIDDER'S ADMINISTRATIVE COSTS. THE SWITCHING FEE SHALL BE DISCLOSED IN ANY BID SUBMITTED UNDER THIS SECTION.

(J) COMPETITIVE AUCTIONING UNDER THIS SECTION IS WITHIN THE AUTHORITY OF THIS STATE UNDER SECTION 722(g) OF THE "ENERGY POLICY ACT OF 1992," 106 STAT. 2776, 16 U.S.C. 824k(g).

Sec. 4928.45. (A) NOTWITHSTANDING SECTIONS 4933.81 TO 4933.90 of the Revised Code, THE PUBLIC UTILITIES COMMISSION MAY DETERMINE, BY ORDER AND AFTER REASONABLE NOTICE AND OPPORTUNITY FOR HEARING, THAT CUSTOMERS THAT ARE NONFIRM ELECTRIC SERVICE CUSTOMERS OF ELECTRIC UTILITIES ON THE EFFECTIVE DATE OF THIS SECTION WOULD BE ASSISTED BY THE IMPLEMENTATION BY EACH SUCH UTILITY OF A SERVICE SCHEDULE THAT COMPLIES WITH DIVISION (C) OF THIS SECTION. IN THE ORDER, THE COMMISSION SHALL SPECIFY THE PERIOD OF TIME, ENDING NOT LATER THAN DECEMBER 31, 2005, DURING WHICH THE SERVICE OFFERING WOULD BE AVAILABLE TO ANY SUCH NONFIRM ELECTRIC SERVICE CUSTOMERS OR A GROUP OF SUCH CUSTOMERS. UPON THE ISSUANCE OF THE ORDER, ANY SUCH NONFIRM ELECTRIC SERVICE CUSTOMER OR A GROUP OF SUCH CUSTOMERS SHALL BE, FOR THE PURPOSES OF THIS SECTION, ELIGIBLE CUSTOMERS IN EACH ELECTRIC UTILITY'S TRANSMISSION TARIFF SUBJECT TO THE JURISDICTION OF THE FEDERAL ENERGY REGULATORY COMMISSION FOR THE PERIOD SPECIFIED IN THE ORDER, AND EACH ELECTRIC UTILITY WITH NONFIRM CUSTOMERS SHALL FILE A SERVICE SCHEDULE PURSUANT TO SECTION 4909.18 of the Revised Code TO EFFECTUATE THIS SERVICE OFFERING.

(B) THE SERVICE SCHEDULE AUTHORIZED UNDER DIVISION (A) OF THIS SECTION, FOR THE PERIOD ENDING NOT LATER THAN DECEMBER 31, 2005, AS SPECIFIED IN THE COMMISSION'S ORDER UNDER THAT DIVISION, SHALL PROVIDE FOR BOTH OF THE FOLLOWING:

(1) FOR SERVICE AND BILLING PURPOSES, CONJUNCTIVE METERING FOR A

GROUP OF CUSTOMERS THAT ARE NONFIRM CUSTOMERS ON THE EFFECTIVE DATE OF THIS SECTION;

(2) DIRECT, COMPARABLE AND NONDISCRIMINATORY ACCESS TO THE TRANSMISSION AND DISTRIBUTION SERVICES, CAPACITIES, FUNCTIONS, AND FACILITIES OF THE ELECTRIC UTILITY BY ANY CUSTOMER THAT IS A NONFIRM ELECTRIC SERVICE CUSTOMER ON THE EFFECTIVE DATE OF THIS SECTION OR BY A GROUP OF ANY SUCH CUSTOMERS, FOR THE PURPOSE OF SECURING FROM A SUPPLIER OR SUPPLIERS OF THE CUSTOMER'S OR GROUP'S CHOICE ALL OR A PORTION OF THE CUSTOMER'S OR GROUP'S ELECTRIC POWER AND ENERGY REQUIREMENTS IN EXCESS OF ANY REQUIREMENTS SUPPLIED BY AN ELECTRIC UTILITY ON A FIRM BASIS.

THE FAILURE OF AN ELECTRIC UTILITY TO FILE SUCH SCHEDULE CONSTITUTES INADEQUATE SERVICE UNDER TITLE XLIX of the Revised Code.

(C) THE SERVICE OFFERING AUTHORIZED PURSUANT TO THIS SECTION SHALL BE IN ADDITION TO ANY SERVICE OPTIONS OTHERWISE AVAILABLE TO A NONFIRM ELECTRIC SERVICE CUSTOMER OR GROUP OF NONFIRM ELECTRIC SERVICE CUSTOMERS. IF A CUSTOMER THAT IS A NONFIRM ELECTRIC SERVICE CUSTOMER ON THE EFFECTIVE DATE OF THIS SECTION OR A GROUP OF SUCH CUSTOMERS ELECTS TO MEET ALL OR A PORTION OF THE CUSTOMER'S OR GROUP'S ELECTRIC POWER AND ENERGY REQUIREMENTS IN EXCESS OF ANY REQUIREMENTS SUPPLIED BY AN ELECTRIC UTILITY ON A FIRM BASIS, BY PURCHASING ELECTRICITY AND RELATED SERVICES FROM A SUPPLIER OR SUPPLIERS OTHER THAN THAT ELECTRIC UTILITY, ANY EXISTING SERVICE ARRANGEMENT UNDER SECTION 4905.31 of the Revised Code OR ANY EXISTING SCHEDULE UNDER SECTION 4905.30 of the Revised Code SHALL BE MODIFIED TO PERMIT THIS ELECTION TO OCCUR WITHOUT ECONOMIC PENALTY AND TO FACILITATE THE CUSTOMER'S OR GROUP'S ACCESS TO THE ELECTRIC MARKET FOR THE PURPOSE OF MANAGING SUPPLY AND PRICE VOLATILITY RISKS.

(D) NOTHING IN DIVISIONS (A) TO (C) OF THIS SECTION AFFECTS ANY OBLIGATION OF AN ELECTRIC UTILITY TO CURTAIL OR INTERRUPT ELECTRIC TRANSMISSION OR DISTRIBUTION SERVICE TO THE EXTENT REQUIRED TO PROTECT THE INTERESTS OF FIRM ELECTRIC SERVICE CUSTOMERS FROM AN INJURY THAT IS OTHERWISE UNAVOIDABLE BUT FOR THE CURTAILMENT OR INTERRUPTION. NOTHING IN THOSE DIVISIONS SHALL BE CONSTRUED OR APPLIED TO INCREASE RATES AND CHARGES FOR FIRM ELECTRIC SERVICE CUSTOMERS INCLUDING RESIDENTIAL FIRM ELECTRIC SERVICE CUSTOMERS.

Sec. 4928.51. (A) THERE IS HEREBY ESTABLISHED IN THE STATE TREASURY A UNIVERSAL SERVICE FUND, INTO WHICH SHALL BE DEPOSITED ALL UNIVERSAL SERVICE REVENUES REMITTED TO THE DIRECTOR OF DEVELOPMENT UNDER THIS SECTION, FOR THE EXCLUSIVE PURPOSES OF PROVIDING FUNDING FOR THE LOW-INCOME CUSTOMER ASSISTANCE PROGRAMS AND FOR THE CONSUMER EDUCATION PROGRAM AUTHORIZED UNDER SECTION 4928.56 of the Revised Code, AND PAYING THE ADMINISTRATIVE COSTS OF THE LOW-INCOME CUSTOMER

ASSISTANCE PROGRAMS AND THE CONSUMER EDUCATION PROGRAM. INTEREST ON THE FUND SHALL BE CREDITED TO THE FUND. DISBURSEMENTS FROM THE FUND SHALL BE MADE TO ANY SUPPLIER THAT PROVIDES A COMPETITIVE RETAIL ELECTRIC SERVICE TO A CUSTOMER WHO IS APPROVED TO RECEIVE ASSISTANCE UNDER A SPECIFIED LOW-INCOME CUSTOMER ASSISTANCE PROGRAM AND TO ANY AUTHORIZED PROVIDER OF WEATHERIZATION OR ENERGY EFFICIENCY SERVICE TO A CUSTOMER APPROVED TO RECEIVE SUCH ASSISTANCE UNDER A SPECIFIED LOW-INCOME CUSTOMER ASSISTANCE PROGRAM.

(B) UNIVERSAL SERVICE REVENUES SHALL INCLUDE ALL OF THE FOLLOWING:

(1) REVENUES REMITTED TO THE DIRECTOR AFTER COLLECTION BY AN ELECTRIC DISTRIBUTION UTILITY BEGINNING JULY 1, 2000, ATTRIBUTABLE TO THE COLLECTION FROM CUSTOMERS OF THE UNIVERSAL SERVICE RIDER PRESCRIBED UNDER SECTION 4928.52 of the Revised Code;

(2) REVENUES REMITTED TO THE DIRECTOR THAT HAVE BEEN COLLECTED BY AN ELECTRIC DISTRIBUTION UTILITY BEGINNING JULY 1, 2000, AS CUSTOMER PAYMENTS UNDER THE PERCENTAGE OF INCOME PAYMENT PLAN PROGRAM, INCLUDING REVENUES REMITTED UNDER DIVISION (C) OF THIS SECTION;

(3) ADEQUATE REVENUES REMITTED TO THE DIRECTOR AFTER COLLECTION BY A MUNICIPAL ELECTRIC UTILITY OR ELECTRIC COOPERATIVE IN THIS STATE NOT EARLIER THAN JULY 1, 2000, UPON THE UTILITY'S OR COOPERATIVE'S DECISION TO PARTICIPATE IN THE LOW-INCOME CUSTOMER ASSISTANCE PROGRAMS.

(C) BEGINNING JULY 1, 2000, AN ELECTRIC DISTRIBUTION UTILITY SHALL TRANSFER TO THE DIRECTOR THE RIGHT TO COLLECT ALL ARREARAGE PAYMENTS OF A CUSTOMER FOR PERCENTAGE OF INCOME PAYMENT PLAN PROGRAM DEBT OWED TO THE UTILITY ON THE DAY BEFORE THAT DATE OR RETAIN THE RIGHT TO COLLECT THAT DEBT BUT REMIT TO THE DIRECTOR ALL PROGRAM REVENUES RECEIVED BY THE UTILITY FOR THAT CUSTOMER.

(D) THE PUBLIC UTILITIES COMMISSION SHALL COMPLETE AN AUDIT OF EACH ELECTRIC UTILITY BY JULY 1, 2000, FOR THE PURPOSE OF ESTABLISHING A BASELINE FOR THE PERCENTAGE OF INCOME PAYMENT PLAN PROGRAM COMPONENT OF THE LOW-INCOME ASSISTANCE PROGRAMS.

Sec. 4928.52. (A) BEGINNING JULY 1, 2000, THE UNIVERSAL SERVICE RIDER SHALL REPLACE THE PERCENTAGE OF INCOME PAYMENT PLAN RIDER IN EXISTENCE ON THE EFFECTIVE DATE OF THIS SECTION AND ANY AMOUNT IN THE RATES OF AN ELECTRIC UTILITY FOR THE FUNDING OF LOW-INCOME ENERGY EFFICIENCY PROGRAMS. THE UNIVERSAL SERVICE RIDER SHALL BE A RIDER ON RETAIL ELECTRIC DISTRIBUTION SERVICE RATES AS SUCH RATES ARE DETERMINED BY THE PUBLIC UTILITIES COMMISSION PURSUANT TO THIS CHAPTER. THE UNIVERSAL SERVICE RIDER FOR THE FIRST FIVE YEARS AFTER THE STARTING



Ohio Consumers' Counsel



Consumer Assistance Handbook

Electric Information

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The Electric Industry

The way utility service is provided is starting to change. One such change is the movement toward a more competitive environment. In the near future, consumers may be able to choose among electricity providers.

Competition in the generation market of the electric industry is sometimes referred to as retail wheeling, retail access or restructuring. This topic is receiving much attention from the Ohio General Assembly, utility companies and consumer representatives. In mid-1997, a joint study committee conducted a series of hearings in the legislature. The committee's task was to study the electric industry restructuring and how it would impact Ohioans. Legislation was then introduced in the spring of 1998 in the House by Rep. Priscilla Mead (R-Upper Arlington) and in the Senate by Sen. Bruce Johnson (R-Westerville), both of whom had co-chaired the committee.

Today, consumers purchase "bundled" electric service, which includes the power generated by a plant, the transmission of the power to your community and the wires and poles that carry the power from an electric company to homes. In the future, customers may obtain the opportunity to choose among various "generators" of electricity. The introduction of competition into the electric industry could happen in the next several years.

While the precise structure of electric deregulation is not yet known, electricity transmission would most likely be overseen by the federal government at regulated rates. Customers' existing electric distribution companies would probably continue to operate at rates regulated by the Public Utilities Commission of Ohio (PUCO).

Ohio is not the first state to consider a restructured electric environment. Many other

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OHIO IS NOT THE FIRST STATE TO CONSIDER A RESTRUCTURED ELECTRIC ENVIRONMENT. MANY OTHER states are currently working on this issue. Illinois, Massachusetts and Pennsylvania have passed restructuring legislation and have begun the transition to competition. New Hampshire and New York have already implemented pilot programs.

Hopefully, a competitive environment will bring you meaningful choices. If done correctly, it may also bring lower prices for utility service. However, there are many important issues that must still be addressed before competition can begin. The OCC is dedicated to helping you understand these upcoming changes. Contact us if you have any questions about this or any other utility issue.

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Electric Consumers' Bill of Rights

Ohio Consumers' Counsel supports consumers' rights to safe, reliable and affordable electric service. Always. In a restructured environment, consumers of electric service should have the following rights:

Quality Service -- Consumers have the right to safe, reliable and reasonably priced electric service.

Meaningful Choice -- Residential consumers should be able to choose electric service providers when business customers choose. Restructuring should produce immediate benefits for all consumers.

Equity -- Consumers' interests and those of utility shareholders should be equitably balanced in any resolution of who pays for the transition to a competitive market. For example, incumbent utility companies may seek to recover the cost of uneconomic assets. There is no strong argument for full recovery of these costs.

Effective Competition -- A market structure that supports and promotes active participation by residential consumers and their suppliers at the earliest possible date should be developed. Safeguards should be adopted that protect consumers in case a competitive market does not evolve.

Comprehensive Consumer Protection -- As electric generation is deregulated, distribution and transmission services will continue to be regulated. Consumers should have protection against fraudulent, deceptive, unfair, unconscionable and anti-competitive practices. Consumers' rights to privacy should be protected.

Safety and Reliability -- Safety standards and system reliability should be maintained or enhanced.

Timely and Accurate Information -- Consumers should receive timely and accurate information about products and services in order to participate effectively in a competitive market. This information should be readily available and should be communicated in clear and understandable language.

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Universal Service -- All customers should have access to electric service. No customer should be excluded or jeopardized by the transition to competition. Assistance programs for low-income consumers should be maintained.

Effective Representation -- Residential consumers should continue to have representation in all forums where restructuring of the electric industry is debated and where policy is established.

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Understanding Your Electric Bill

Your electric usage is measured in kilowatt hours (KWH). One KWH is equal to 1,000 hours of electricity (the equivalent of burning of a 100-watt light bulb for 10 hours). Most electric bills include the following information:

A = Customer Identification - The customer's name and address appear on the bill along with their account number.

B = Customer Rate Code - The customer is billed according to a tariff (a government-set price for service) identifying the class or type of service they receive.

C = Service Period - Bills to residential customers are sent out at regular intervals. The beginning and ending dates for the service period or the ending date plus the number days in the service period must be included in the bill.

D = Billing Determinants - If applicable to the company, the following will appear on your bill: beginning meter readings, ending meter readings, demand meter readings, multipliers, consumption and demand.

E = Total Charges Due For The Period - The amount of any late payment charges or gross or net charges, previous balances, customer credits and total balances must be stated. Budget plan customer bills must show the current balance of the account.

F = Date Due - This is the date by which the bill must be paid to keep the account current.

G = Company Contact - A customer contact number must appear on the bill. If a number for reporting emergency outages does not appear in the local telephone directory, it must appear on the bill.

H = Inquiries - A statement should be included that inquiries should be made initially to the company and that unresolved inquiries should be made to the Public Utilities Commission of Ohio (PUCO) at its toll-free number. A company with multiple customer service offices must indicate that the customer can obtain a customer service telephone number in the local

telephone directory.

I = Statement - By law, a statement must appear on your bill indicating the amount of your total bill that is a result of compliance with the Clean Air Act Amendments of 1990 mandated by federal action.

Sample Electric Bill

SERVICE AT:	Questions About Bill or Service, Call 1-800-XXX-XXXX or 1-XXX-XXX-XXXX	Account Number SJ98-3949-849																					
CONSUMER NAME Street Address City, OH Zip																							
<table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="text-align: left;">PREVIOUS CHARGES</th> <th style="text-align: left;">Account balance</th> <th style="text-align: left;">Amount</th> </tr> </thead> <tbody> <tr> <td>Balance at Last Billing</td> <td>\$ 121.36</td> <td></td> </tr> <tr> <td>Payment-Thank you</td> <td><u>121.36 CR</u></td> <td></td> </tr> <tr> <td>Previous balance</td> <td>\$0.0</td> <td>\$0.0</td> </tr> </tbody> </table>			PREVIOUS CHARGES	Account balance	Amount	Balance at Last Billing	\$ 121.36		Payment-Thank you	<u>121.36 CR</u>		Previous balance	\$0.0	\$0.0									
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Total Amount Due		\$196.70																					
Due Date		Jan 09																					
\$6.14 is your average daily cost for current electric service																							
USAGE:																							
	Service Period	Meter reading																					
<u>Meter Number</u> 84939349 KWH	<u>From</u> 11/16/95	<u>To</u> 12/18/95																					
	<u>Prev CD</u> 13942 A	<u>Pres CD</u> 17965 A																					
	<u>Multiplier</u> 1.0000	<u>Metered usage</u> 4023																					
CD - Read Code: A= Actual Reading 32 Billing Days Next Read Date 1/19/XX																							
MESSAGES:																							
\$0.01 or 0.00029000 cents/KWH of this bill is attributable to compliance with Phase I acid rain control requirements under title IV of the Clean Air Act Amendments of 1990. This charge is attributable to federal, not state action.																							
Due date does not apply to the Previous Balance Due.																							

H—On this particular bill, the inquiry statement was listed on the back of the bill

If you have questions about your bill, contact your utility company or call OCC at 1-877-PICK OCC (1-877-742-5622 toll-free).

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Conjunctive Electric Service

What is Conjunctive Electric Service?

Conjunctive Electric Service (CES) is a program offered by some Ohio electric utility companies. The program allows individual customers to join together to form customer groups and enter into written service agreements with aggregators to potentially reduce their electric cost.

Who can participate in this program?

Customers of Cincinnati Gas & Electric, Dayton Power and Light and First Energy (Ohio Edison, Toledo Edison and Cleveland Electric Illuminating Company) may participate.

What is an aggregator?

For residential customers, an aggregator is the authorized representative of an aggregated customer group. The aggregator accepts responsibility for forming and administering the customer group. The aggregator must register with the Public Utilities Commission of Ohio (PUCO). The aggregator enters into a written agreement with the customers in the group. The aggregator then negotiates with the electric utility for a CES rate to be charged to the customer group.

An aggregator for residential customers must register with the PUCO and must meet all of the requirements for aggregators contained in the electric utility's tariff.

A list of registered aggregators is available through your utility company, the PUCO or the OCC.

How do I participate?

Contact an aggregator that is providing aggregation service to residential customers in your area. Remember, you must be willing to change your electricity usage patterns, reduce your usage or change your billing arrangements. For example, you may agree not to use certain electricity using items like a dishwasher at "peak" hours.

You will enter into a written contract with the aggregator for a minimum of one year.

What role will my utility play?

The electric utility is still the provider of electricity. The utility will negotiate with registered, authorized aggregators in the development of a CES rate for the customer group. After the rate is established and service under the CES rate has begun, the utility may permit the aggregator to accept payment for the utility service from the customer group. Because the members of the customer group will still owe the utility for its provision of electric service, the aggregator will be entrusted by the customer group to collect payment from group members and then pay the utility.

What dispute resolution process is available?

The PUCO has set up a dispute resolution process for the CES program. Each aggregator will cooperate with the utility, the PUCO and OCC to answer inquiries and resolve disputes. Each aggregator will provide a toll-free telephone number to customers who need to obtain account information.

Why might I want to join a CES group?

In the future, when electric service is deregulated in Ohio, residential customers may need to form groups (or aggregations) in order to bargain for lower cost electric generation service. The CES program will allow residential customers the opportunity to participate in the process of forming customer groups and negotiate for rates that reflect the cost to serve the group. Residential customers may also obtain benefits by altering their electric usage patterns and creating cost savings for the providers of electric energy.

Why might I not want to join a CES group?

Your electric utility remains the monopoly provider of electric service in its service area. The CES rate will be designed to provide the utility the same revenues from the customers in your CES group as the utility received prior to the group's formation. Therefore, in order to pay less, the group as a whole or individuals within the group may need to alter their usage patterns or otherwise act to create cost savings for the utility. If you are unable to change your usage pattern or otherwise assist the aggregator in creating cost savings for the utility, your bill might be higher under CES than it might have been under your present residential rate.

Need more information?

Call an aggregator or contact:

- Cincinnati Gas and Electric at 1-800-544-6900
- Cleveland Electric Illuminating Company at 1-800-589-3101
- Dayton Power & Light at 1-800-929-8646
- Ohio Edison at 1-800-OEDISON (1-800-633-4766)
- Toledo Edison at 1-800-447-3333

77 South High Street, 15th Floor, Columbus, OH 43266-0550
1-877-742-5622 (toll-free in Ohio) or 614-466-9605

<http://www.state.oh.us/cons/handbook/5electric.html>
This page was last updated on February 16, 1999.
Information believed accurate but not guaranteed.
The State of Ohio disclaims liability for any errors or omissions.
If you spot any errors in these pages, please fill out a Feedback Form.

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Texas

BILL ANALYSIS

SB7 signed 18 June 1999

Office of House Bill Analysis

S.B. 7
By: Sibley
State Affairs
4/8/1999
Engrossed

BACKGROUND AND PURPOSE

Currently, the Public Utility Regulatory Act of 1995 (Act) authorizes the Public Utility Commission (PUC) to regulate the electricity market and ensure that only one electric energy provider serves each area of the state. S.B. 7 amends the Act by deregulating the electricity generation market and permitting providers to compete for customers who choose their electricity supplier in competitive areas. This bill restructures electric utility service. It also authorizes the PUC to develop and promulgate customer protection rules during and after a transition to a competitive market.

RULEMAKING AUTHORITY

It is the opinion of the Office of House Bill Analysis that rulemaking authority is expressly delegated to the Public Utility Commission in SECTION 35 (Sections 39.101, 39.153, 39.153, 39.155, 39.157, 39.157, 39.262, 39.601, 39.603, 39.603, 40.003, 41.003, Utilities Code); to the commissioner of education in SECTION 35 (Section 39.601(g), Utilities Code); and to the comptroller of public accounts in SECTION 35 (Sec. 39.601(g), Utilities Code) of this bill. Rulemaking authority previously delegated to the Public Utility Commission is modified in SECTION 35 (Section 39.101, Utilities Code) of this bill.

SECTION BY SECTION ANALYSIS

SECTION 1. Amends Section 11.003, Utilities Code, as follows:

Sec. 11.003. DEFINITIONS. Defines "electric cooperative," and redefines "affected persons," "cooperative corporation," "person," "ratemaking proceeding," and "service." Redesignates Subdivisions (10)-(20) to Subdivisions (11)-(21), respectively. Makes nonsubstantive changes.

SECTION 2. Amends Section 12.005, Utilities Code, to provide that the Public Utility Commission of Texas (PUC) is subject to Chapter 325, Government Code (Texas Sunset Act). Provides that unless PUC is continued in existence as provided by that chapter or by Chapter 39, PUC is abolished and this title expires September 1, 2005, rather than September 1, 2001.

exercise of control over resource acquisition and any related expansion programs;

(7) establish and enforce service quality and reliability standards and consumer safeguards designed to protect retail electric customers consistent with the provisions of this chapter;

(8) determine whether a base rate reduction is appropriate for the municipally owned utility;

(9) determine any other utility matters that the municipal governing body or body vested with power to manage and operate the municipally owned utility believes should be included; and

(10) make any other decisions affecting the municipally owned utility's participation in customer choice that are not inconsistent with the provisions of this chapter.

(b) Prohibits a retail customer, in multiply certificated areas, including a retail customer of an electric cooperative or a municipally owned utility, from avoiding stranded cost recovery charges by switching to another electric utility, electric cooperative, or municipally owned utility.

Sec. 40.056. ANTICOMPETITIVE ACTIONS. (a) Requires PUC, upon a complaint by a retail electric provider and a finding by PUC that a municipal rule, action, or order relating to customer choice is anticompetitive or does not provide other retail electric providers with nondiscriminatory terms and conditions of access to distribution facilities or customers within the utility's certificated retail service area that are comparable to the utility's and its affiliates' terms and conditions of access to distribution facilities or customers.

(b) Requires the municipally owned utility be given three months to cure the anticompetitive or noncompliant behavior described in Subsection (a), following opportunity for hearing on the complaint. Authorizes PUC, if the noncompliant behavior is not fully remedied within that time, to prohibit the municipally owned utility or affiliate from providing retail service outside its certificated retail service area until the rule, action, or order is remedied.

Sec. 40.057. BILLING. (a) Authorizes a municipally owned utility that opts for customer choice to continue to bill for transmission and distribution services of electric customers located in its certificated retail service area, as that area exists on the date of adoption of customer choice. Authorizes the utility to bill directly for generation services and customer services provided by the municipally owned utility to those customers.

(b) Prohibits a municipally owned utility that opts for customer choice from adopting anticompetitive billing practices that would discourage customers in its service area from

T E X A S

R atepayers'
O rganization to
S ave
E nergy

Retail competition, restructuring, deregulation, re-regulation, retail access, direct access and retail wheeling all refer to the same thing :

- utilities losing their monopoly service areas, allowing customers to choose their electricity suppliers.

If the wrong policies are set, there are pitfalls for the consumer and the environment whether we have competition or if the industry remains regulated. Texas Ratepayer's Organization to save Energy (Texas ROSE) is helping to see that consumers and the environment are protected regardless of who profits from electricity sales. Texas ROSE has been in the thick of the debates, filing comments at the PUC (Public Utility Commission) and attending meetings and legislative hearings to establish long-term protections for consumers and the environment.

Texas ROSE and ten other public interest groups have presented and signed a Residential Electric Consumer Bill of Rights. The rights apply without exception to customers of a monopoly utility, customers being served by a utility making a transition from monopoly status to a competitive market and customers served by a fully competitive utility.



The Residential Electric Consumer Bill of Rights

requests that the PUC guarantee:

- Residential customers will benefit from the same opportunities to reduce their rates and bills and to choose suppliers and service options as are available to large customers
- Universal service, meaning an affordable, basic package of service is available to all residential customers regardless of income or residence in rural areas
- Lifeline rates for low income customers
- All providers have a duty to serve all customers and must meet Public Utility Commission-approved standards
- Billing and service protections will be equal to those in effect today and protections will increase as necessary as the number of suppliers increases
- Business transactions will be regulated to prevent anti-competitive behavior (such as favoritism, self-dealing, and cross subsidization among affiliates) and anti-competitive domination in any

- geographic area or service market served by a limited number of competitors
- Reliable and safe electric service for all consumers, and improved reliability in areas where it is needed
 - Continued availability of cost effective energy efficiency programs
 - A balanced mix of energy resources, including renewable energy and energy conservation programs
 - A market which reduces inefficiencies and lowers prices for all customer classes, thus creating opportunities for economic development
 - Continued regulation of franchised utilities until a fully competitive market is in operation
 - Utilities are not guaranteed the right to recover all of their excess costs over market (stranded investment). As soon as possible, costs resulting from inefficient and/or obsolete operations should be eliminated from all customer bills

**Contact us to add your name to the list of supporters of the
Residential Consumer's Bill of Rights**

Texas Ratepayers' Organization to Save Energy
Carol Biedrzycki, Executive Director
815 Brazos Street, Suite 1100
Austin, Texas 78701-2509

512-472-5233

Send email to sharrush@mail.utexas.edu

Back to [Texas ROSE home page](#)

last updated September 12, 1998
<http://www.main.org/texasrose/rights.html>

VIRGINIA ACTS OF ASSEMBLY -- 1999 SESSION

CHAPTER 411

An Act to amend the Code of Virginia by adding in Title 56 a chapter numbered 23, consisting of sections numbered 56-576 through 56-595, relating to the Virginia Electric Utility Restructuring Act.

[S 1269]

Approved March 25, 1999

Be it enacted by the General Assembly of Virginia:

1. That the Code of Virginia is amended by adding in Title 56 a chapter numbered 23, consisting of sections numbered 56-576 through 56-595, as follows:

CHAPTER 23.

VIRGINIA ELECTRIC UTILITY RESTRUCTURING ACT.

§ 56-576. *Definitions.*

As used in this chapter:

"Affiliate" means any person that controls, is controlled by, or is under common control with an electric utility.

"Aggregator" means a person licensed by the Commission that purchases or arranges for the purchase of electric energy as an agent or intermediary for sale to, or on behalf of, two or more retail customers.

"Commission" means the State Corporation Commission.

"Cooperative" means a utility formed under or subject to Chapter 9 (§ 56-209 et seq.) of this title.

"Covered entity" means a provider in the Commonwealth of an electric service not subject to competition but shall not include default service providers.

"Covered transaction" means an acquisition, merger, or consolidation of, or other transaction involving stock, securities, voting interests or assets by which one or more persons obtains control of a covered entity.

"Customer choice" means the opportunity for a retail customer in the Commonwealth to purchase electric energy from any supplier licensed and seeking to sell electric energy to that customer.

"Distribute," "distributing" or "distribution of" electric energy means the transfer of electric energy through a retail distribution system to a retail customer.

"Distributor" means a person owning, controlling, or operating a retail distribution system to provide electric energy directly to retail customers.

"Electric utility" means any person that generates, transmits, or distributes electric energy for use by retail customers in the Commonwealth, including any investor-owned electric utility, cooperative electric utility, or electric utility owned or operated by a municipality.

"Generate," "generating," or "generation of" electric energy means the production of electric energy.

"Generator" means a person owning, controlling, or operating a facility that produces electric energy for sale.

"Incumbent electric utility" means each electric utility in the Commonwealth that, prior to July 1, 1999, supplied electric energy to retail customers located in an exclusive service territory established by the Commission.

"Independent system operator" means a person that may receive or has received, by transfer pursuant to this chapter, any ownership or control of, or any responsibility to operate, all or part of the transmission systems in the Commonwealth.

"Market power" means the ability to impose on customers a significant and nontransitory price increase on a product or service in a market above the price level which would prevail in a competitive market.

"Municipality" means a city, county, town, authority or other political subdivision of the Commonwealth.

"Period of transition to customer choice" means the period beginning on January 1, 2002, and ending on January 1, 2004, unless otherwise extended by the Commission pursuant to this chapter.

person subject to the requirements of subsection D that is also subject to the requirements of Chapter 5 of this title may be exempted from compliance with the requirements of Chapter 5 of this title.

§ 56-591. Application of antitrust laws.

Nothing in this chapter shall be construed to exempt or immunize from punishment or prosecution, conduct violative of federal antitrust laws, or the antitrust laws of this Commonwealth.

§ 56-592. Consumer education and protection; Commission report to Legislative Task Force.

A. The Commission shall develop a consumer education program designed to provide the following information to retail customers during the period of transition to retail competition and thereafter:

1. Opportunities and options in choosing (i) suppliers and aggregators of electric energy and (ii) any other service made competitive pursuant to this chapter;

2. Marketing and billing information suppliers and aggregators of electric energy will be required to furnish retail customers;

3. Retail customers' rights and obligations concerning the purchase of electric energy and related services; and

4. Such other information as the Commission may deem necessary and appropriate in the public interest.

B. The Commission shall complete the development of the consumer education program described in subsection A, and report its findings and recommendations to the Legislative Transition Task Force on or before December 1, 1999, and as frequently thereafter as may be required by the Task Force concerning:

1. The scope of such recommended program consistent with the requirements of subsection A;

2. Materials and media required to effectuate any such program;

3. State agency and nongovernmental entity participation;

4. Program duration;

5. Funding requirements and mechanisms for any such program; and

6. Such other findings and recommendations the Commission deems appropriate in the public interest.

C. The Commission shall develop regulations governing marketing practices by public service companies, licensed suppliers, aggregators or any other providers of services made competitive by this chapter, including regulations to prevent unauthorized switching of suppliers, unauthorized charges, and improper solicitation activities. The Commission shall also establish standards for marketing information to be furnished by licensed suppliers, aggregators or any other providers of services made competitive by this chapter during the period of transition to retail competition, and thereafter, which information shall include standards concerning:

1. Pricing and other key contract terms and conditions;

2. To the extent feasible, fuel mix and emissions data on at least an annualized basis;

3. Customer's rights of cancellation following execution of any contract;

4. Toll-free telephone number for customer assistance; and

5. Such other and further marketing information as the Commission may deem necessary and appropriate in the public interest.

D. The Commission shall also establish standards for billing information to be furnished by public service companies, suppliers, aggregators or any other providers of services made competitive by this chapter during the period of transition to retail competition, and thereafter. Such billing information standards shall require that billing formation:

1. Distinguishes between charges for regulated services and unregulated services;

2. Itemizes any and all nonbypassable wires charges;

3. Is presented in a format that complies with standards to be established by the Commission;

4. Discloses, to the extent feasible, fuel mix and emissions data on at least an annualized basis;

and

5. Includes such other billing information as the Commission deems necessary and appropriate in the public interest.

E. The Commission shall establish or maintain a complaint bureau for the purpose of receiving, reviewing and investigating complaints by retail customers against public service companies, licensed suppliers, aggregators and other providers of any services made competitive under this chapter. Upon

the request of any interested person or the Attorney General, or upon its own motion, the Commission shall be authorized to inquire into possible violations of this chapter and to enjoin or punish any violations thereof pursuant to its authority under this chapter, this title, and under Title 12.1. The Attorney General shall have a right to participate in such proceedings consistent with the Commission's Rules of Practice and Procedure.

F. The Commission shall establish reasonable limits on customer security deposits required by public service companies, suppliers, aggregators or any other persons providing competitive services pursuant to this chapter.

§ 56-593. Retail customers' private right of action; marketing practices.

A. No entity subject to this chapter shall use any deception, fraud, false pretense, misrepresentation, or any deceptive or unfair practices in providing, distributing or marketing electric service.

B. 1. Any person who suffers loss (i) as the result of marketing practices, including telemarketing practices, engaged in by any public service company, licensed supplier, aggregator or any other provider of any service made competitive under this chapter, and in violation of subsection C of § 56-592, including any rule or regulation adopted by the Commission pursuant thereto or (ii) as the result of any violation of subsection A, shall be entitled to initiate an action to recover actual damages, or \$500, whichever is greater. If the trier of fact finds that the violation was willful, it may increase damages to an amount not exceeding three times the actual damages sustained, or \$1,000, whichever is greater.

2. Upon referral from the Commission, the Attorney General, the attorney for the Commonwealth, or the attorney for any city, county, or town may cause an action to be brought in the appropriate circuit court for relief of violations within the scope of (i) subsection C of § 56-592, including any rule or regulation adopted by the Commission pursuant thereto or (ii) subsection A.

C. Notwithstanding any other provision of law to the contrary, in addition to any damages awarded, such person, or any governmental agency initiating such action, also may be awarded reasonable attorney's fees and court costs.

D. Any action pursuant to this section shall be commenced within two years after its accrual. The cause of action shall accrue as provided in § 8.01-230. However, if the Commission initiates proceedings, or any other governmental agency files suit for the purpose of enforcing subsection A or the provisions of subsection C of § 56-592, the time during which such proceeding or governmental suit and all appeals therefrom is pending shall not be counted as any part of the period within which an action under this section shall be brought.

E. The circuit court may make such additional orders or decrees as may be necessary to restore to any identifiable person any money or property, real, personal, or mixed, tangible or intangible, which may have been acquired from such person by means of any act or practice violative of subsection A or subsection C of § 56-592, provided, that such person shall be identified by order of the court within 180 days from the date of any order permanently enjoining the unlawful act or practice.

F. In any case arising under this section, no liability shall be imposed upon any licensed supplier, aggregator or any other provider of any service made competitive under this chapter, who shows by a preponderance of the evidence that (i) the act or practice alleged to be in violation of subsection A or subsection C of § 56-592 was an act or practice over which the same had no control or (ii) the alleged violation resulted from a bona fide error notwithstanding the maintenance of procedures reasonably adopted to avoid a violation. However, nothing in this section shall prevent the court from ordering restitution and payment of reasonable attorney's fees and court costs pursuant to subsection C to individuals aggrieved as a result of an unintentional violation of subsection A or subsection C of § 56-592.

§ 56-594. Net energy metering provisions.

A. The Commission shall establish by regulation a program, to begin no later than July 1, 2000, which affords eligible customer-generators the opportunity to participate in net energy metering. The regulations may include, but need not be limited to, requirements for (i) retail sellers; (ii) owners and/or operators of distribution or transmission facilities; (iii) providers of default service; (iv) eligible customer-generators; or (v) any combination of the foregoing, as the Commission determines will facilitate the provision of net energy metering, provided that the Commission determines that such

*from Kentucky Public Service
Commission Web page.
30 Sept 1999*

KENTUCKY PUBLIC SERVICE COMMISSION

**PRINCIPLES AND GUIDELINES ON THE
RESTRUCTURING OF THE ELECTRIC INDUSTRY**

A nationwide dialogue has begun among federal and state legislators and utility regulators, electric utility companies, non-utility electricity suppliers, and wholesale and retail electricity consumers on the need to fundamentally restructure the electric industry. This is a very important and complex issue that will have profound implications for every American household and business.

The Kentucky Public Service Commission has been following the development of these issues and urges all affected parties to give careful and thoughtful consideration to all aspects of this industry restructuring. The Commission is especially interested in examining the possible impacts that such a restructuring will have on states, like Kentucky, with low electric rates.

The citizens of the Commonwealth of Kentucky currently enjoy some of the lowest electric rates in the nation. In fact, according to the Energy Information Administration's electric sales and revenue data for 1995, Kentucky had the lowest electricity prices in the nation, as measured by average revenue per kilowatt-hour for all sectors of all utilities. The average electric rate in Kentucky in 1995 was 4.07 cents per kilowatt-hour compared to the national average of 6.89 cents per kilowatt-hour.

Kentucky's low electric rates can be attributed to many factors. Among these factors are, (1) close proximity to coal-producing areas; (2) a state ban on nuclear generating units, which have proven to be tremendously expensive to construct and maintain; (3) beneficial corporate management and efficient operations by utility companies; and (4) fair and reasonable regulation and oversight by state authorities. As the nationwide dialogue on electric industry restructuring continues, the Kentucky Public Service Commission will focus intently on maintaining the low electric rates that have developed in Kentucky over a long period of stable and beneficial utility regulation. The Commission urges the Kentucky General Assembly and all affected

parties to adopt a cautious and prudent approach toward electric industry restructuring.

The Commission has identified the following principles that will serve to guide the Commission in its activities and consideration of issues pertaining to the restructuring of the electric industry. The principles are in no particular order.

1. Ensure the reliability and safety of electricity systems and services

The reliability and safety of electric systems and services is of utmost concern to the PSC. If decisions on how a utility system is maintained and operated are based solely on economic, competitive or market-based considerations, the likelihood of a deterioration of service quality and reliability is increased. Furthermore, if decisions regarding the need for and types of new power supply or generation capacity are based solely on the vacillations of a competitive marketplace, the reliability of electricity supplies in hard-to-serve and less lucrative regions could be compromised. The restructuring of the electric industry must be accomplished in a manner that preserves the reliability, safety and quality of electricity systems and supplies for all consumers.

2. Ensure that any benefits and advantages resulting from retail competition are shared equally by all consumers

The restructuring of the electric industry should result in fair and equitable benefits for all consumers. All consumers should be guaranteed equal access to reputable and non-discriminating electricity suppliers. These concepts should be the cornerstone of any restructuring of the electric industry. Unless all consumers share equally in the benefits, changing the way in which electricity is supplied and purchased simply does not make sense from a public protection perspective.

3. *Institute sufficient safeguards to protect Kentucky consumers against undue discrimination and unfair business practices*

In a competitive environment, the current safeguards that protect customers against undue discrimination and unfair billing and disconnection practices could be compromised or even eliminated. Other consumer abuses that could result from a competitive utility industry include deceptive and discriminatory market practices. Electric industry restructuring must provide sufficient consumer protections and address the serious issues of service quality, obligation to serve, and providers of last resort for all retail customers. In addition, retail consumers must be fully informed and educated regarding any significant changes taking place in the electric industry.

4. *Guarantee universal electric service at reasonable prices for all Kentuckians*

Few would dispute the position that electric service has become a basic human need. Reliable electric service is crucial for the continued health, safety and economic well-being of Kentucky's citizens. For these reasons, universal service is a very important concept that must be considered in a restructured industry. Consumers should be entitled to non-discriminatory access to reasonably priced power. An electric market that is driven strictly by competitive and economic considerations will not necessarily protect the interests of small consumers, particularly rural and low income households. The availability of affordable and adequate electricity for all Kentucky consumers should be preserved in any restructured electric industry.

5. *Encourage environmentally sound resource allocation strategies in a competitive generation market*

The generation and delivery of electricity significantly affects the environment in Kentucky and elsewhere. Under the present regulatory framework, utilities are encouraged and occasionally required to pursue environmentally responsible expansion plans. A marketplace driven strictly by competitive and economic

considerations may be very limited in its ability to promote environmentally sound resource allocation strategies. A restructured electric industry should ensure that the environmental implications of all electric resource decisions are thoroughly considered by electricity suppliers and consumers.

6. *States should have the authority to handle all matters pertaining to utility retail stranded costs*

In a competitive electric market, utility assets that were originally constructed or acquired under the current regulatory regime in order to serve the utility's electric load could become stranded in a restructured market. These costs and expenditures that were traditionally recovered through utility rates could be greater than the prices established in the marketplace. Individual states must have the authority to consider utility claims to recover net, verifiable and non-mitigatable retail stranded costs. States are in the best position to develop fair and equitable verification and recovery methods that consider the interests of utility shareholders and ratepayers. Currently it appears that utilities in Kentucky will have little or no costs that will be stranded in a competitive marketplace.

7. *Establish fair cost allocation methodologies between utilities' regulated and unregulated energy services*

The Commission will be very concerned about the allocation of costs by utilities between regulated and unregulated energy services and subsidiaries and cross-subsidies between utility profit centers. At the present time, the Commission has instituted safeguards to monitor cost allocation between vertically-integrated utility holding company subsidiaries. If utilities unbundle services and certain aspects of utility operations become unregulated or federally regulated, the Commission could have some difficulty in protecting Kentucky consumers against the misallocation of costs between regulated and unregulated activities. A restructuring plan must provide the Commission with access to all appropriate books and records.

8. *Institute a reasonable code of conduct for all electricity providers in a restructured electric industry*

In a restructured electric industry, many types of electricity providers and purchasers will be interacting and competing. These providers will likely include investor-owned utility companies, rural electric cooperatives, municipalities, power marketers (agents for generation projects who market power on behalf of the generator), power brokers (retail agents who buy power on behalf of a customer), aggregators (entities that aggregate customers for a market), self-generators, and non-utility generators. The objectives and motives of each of these entities are different and possibly at cross purposes from those of other parties. Instituting a code of conduct for all electricity providers that, among other things, fully protects customers from unscrupulous agents and transactions will be very important. Equally important in the restructured electric industry will be the need for fair and equitable rules and policies which provide for a "level playing field" among the various electricity providers. Differences currently exist between the investor-owned utilities, rural electric cooperatives, and municipals. The participation of additional providers in the restructured electric market will add complexities to these differences. To the extent possible, the participants in this market should be distinguished by the product and services they offer, and not by differences in the rules under which they operate.

*Louisiana
Public Service
Commission*

Public Interest Determination

Executive Summary

The LPSC has been actively considering whether the restructuring of retail electric service is in the public interest. A generic wheeling docket, U-21453, was opened in May of 1995, with official notice published in the LPSC Bulletin in June of 1995. Intervening parties have filed first and second rounds of comments on the important issues. Staff, having reviewed the filed comments, prepared a list of issue questions to which intervening parties responded to at evidentiary hearings held in October. After the hearings, the information obtained was analyzed and used in preparing this document and recommendation.

The first section of this document gives a brief review of those hearings, discussion of the issues presented and a summary of the Staff's recommendation.

The second section of this document includes Staff's discussion of the various issues presented for resolution in consideration of whether retail competition is in the public interest.

Also attached is a select bibliography of the resources relied upon by the Staff in compiling its recommendation.

The primary objective of electric industry restructuring is to produce prices lower for all Louisiana consumers than would have been available under the current system by increasing reliance on the forces of competition. Restructuring of the electric utility industry should be implemented in a manner that benefits all consumers and does not benefit one customer class to the detriment of another. Changes to corporate, operational and regulatory structure of the electric utility industry should be based upon a careful and comprehensive analysis of the impact of such changes before they are set in motion. Only if a level playing field is established can enhanced economic efficiencies be realized. Nondiscriminatory delivery, back-up and inter-connection services must be assured.

Discrete markets sectors must be analyzed to determine whether they are inherently competitive or monopolistic. The integrity of the marketplace in competitive sectors must be assured, and mechanisms should exist to identify and correct anti-competitive behavior. Where monopolies remain, regulation should continue. The distribution system is, and is likely to remain, a monopoly service subject to regulation, and accordingly, distributors should have the obligation to provide distribution service to all customers in the distribution service area.

Increased customer choice of service and pricing options should be a critical element of a restructured industry. For purposes of evaluating retail access, consumer bills should be desegregated or "unbundled" into individual services in order to provide improved information to the consumers and Commission and facilitate educated choices that are in the best interest of all consumers.

The Public Interest determination is perhaps the most important issue for the Commission to consider. Should the Commission decide that restructuring is not in the public's interest, then the subsequent issues are immaterial. For this reason, Staff considers it important to give a general description of the public's interest. It is evident through the testimony that all parties are not referring to the same thing when they refer to "public interest". Staff believes that for the Commission's purposes, the public must include all relevant customer classes. For this reason, it is not sufficient to allow retail competition on the grounds that society will be better off. That type of reasoning allows for one class of customers to gain at the expense of others, as long as the net effect is positive. The public's interest must be defined to mean that all customer classes benefit from restructuring, or at a minimum, no customer class benefits at the expense of another class. Everyone seems to agree that the large industrial customer class will benefit from retail competition. Therefore, it seems the Commission's responsibility must be to insure that other customer classes including residential and small commercial, will also see a benefit from restructuring.

While Staff continues to research the appropriate issues, it is noted that it would be irresponsible to issue a blanket statement saying that restructuring is or is not in the best interest of Louisiana's electric consumers at this time. Numerous issues must be individually researched, resolved and implemented in a manner consistent with public interest. If this is not done, one issue handled in a manner inconsistent with the public's interest could corrupt the overall process of restructuring and make retail competition inconsistent with the public's interest. For this reason, Staff believes it is important for the Commission to evaluate continuously, the restructuring process as it unfolds, and the Commission needs to retain the authority to make adjustments and additions to existing plans, when deemed necessary, to insure restructuring stays on track and remains in the public's best interest.

Summary of Staff Recommendation

As is more fully detailed in the attached Staff Report, Staff would recommend a finding that the restructuring of the retail electric industry may be in the public's interest, contingent on numerous issues being individually and adequately researched, then implemented in a manner that remains consistent with the public's interest. Consistent with this finding, Staff further recommends that it be authorized to proceed with the investigation of the appropriate issues. Among the issues that must be considered and resolved are:

- ! Stranded Costs;
- ! Reliability;
- ! Consumer Protection;
- ! Consumer Education;
- ! Universal Service;

Throughout the hearing, parties (both utilities and other intervenors) agreed on two distinctions regarding reliability which would be made in a restructured environment: operating reliability and planning reliability. Operating reliability covers general security arrangements which are currently required under standard NERC operation criteria. Planning reliability concerns the adequacy of future generation supplies.

Parties indicated that operating reliability would continue to be maintained within the various NERC reliability regions/councils. Future operating reliability would be provided by an Independent System Operator (ISO). Parties indicated that competitive providers would face a number of strong incentives to maintain reliability in a competitive market. First, competitors would have a financial incentive to provide generation because failure to provide generation services would result in lower revenues, and hence, profits. Second, competitors would be faced with economic penalties for failing to meet generation reliability standards. Here, expensive backup power would have to be procured by the ISO (or entity serving an ISO function) which in turn would be paid for by the competitive provider failing to serve its promised load. In addition, penalties could be extracted from these parties, which could provide an additional deterrent for failing to meet committed obligations. Some parties thought that future planning reliability would be dictated by a competitive market. Competitors would presumably forecast load projections and prices in future markets (much like utilities do today), and make capacity addition decisions based on these forecasts. Increased prices would send signals for the capacity decisions.



Consumer Protection

The fundamental issue with respect to electric industry restructuring is the potential impact on Louisiana consumers. Unfortunately, the Staff, and no one else, can confidently predict the resulting impact at this time.

As a result of the uncertainty surrounding potential impacts, any restructuring transition plan should recognize the development of adequate consumer protection measures as integral to the public interest. Consistent with the Staff's recommendation that a transition process should be evolutionary, each stage of the process may require development of new protection measures.

There are several difficult obstacles to overcome in moving toward a more competitive industry structure. Significant concerns, including potential reliability impacts and market power, arise from the current industry organization and infrastructure, the physical and economic characteristics of electricity, and the essential social nature of this energy service, which has limited practical substitutes. In fact, the Staff believes it is premature to conclude with absolute certainty that these concerns can be effectively resolved in a publicly acceptable manner.

There are significant costs associated with industry restructuring. Such costs include both direct costs and indirect or opportunity costs. While these potential costs cannot be quantified any more accurately than potential competitive benefits at the present time, they should be recognized and subjectively evaluated. As competitive restructuring proceeds further along the spectrum of options

(i.e., from expanded competition in the wholesale generation market to full retail customer choice), associated costs are likely to grow exponentially.

In recognition of the complex and significant obstacles to effective restructuring, the Staff, in this report, recommends a deliberative and evolutionary restructuring process if the Commission decides to pursue such a course. Because consumer impacts cannot be accurately predicted, it is critical that adequate consumer safeguards are established for each step of the process.

Initial consumer protection from potential market power concerns may take the form of rate caps or freezes as competitive structures (e.g., ISOs and power exchanges) are developed to allow for increased competition among generators. The introduction of increased generation competition will require the further establishment of rules or regulations governing standards of conduct for suppliers in order to protect the integrity of the interconnected grid.

If restructuring proceeds to include full retail competition, consumers will need vastly expanded protections. Since certain consumers may be unable or unwilling to choose a supplier, a supplier of last resort will need to be established to ensure that service is available for all consumers. This supplier is likely to be the local distribution utility during a transition period, but other options may be considered after markets fully developed. Because some customers may be considered "undesirable" the provision of a supplier of last resort may have to be continued indefinitely.

Additionally, a mechanism needs to be developed to ensure that marketers and suppliers are financially solvent and technically reliable. This may require establishment of a state registration process. It is likely that during the transition process, extended rate caps and freezes will need to be maintained at least until reasonable evidence exists that market power concerns have been alleviated. Standards governing marketing and advertising practices should be established to prevent misleading or deceptive practices. Requirements for standardized billing formats should be considered to ensure sufficient information for consumer analysis. Additional protection measures will need to be developed to prevent the unauthorized switching of power suppliers. Rules for customer deposit requirements, late payment charges, and service disconnection procedures must be established. Priority of claims on partial consumer payments among the distribution, transmission, and power supplier companies must be determined.

Many small users may lack the knowledge and sophistication necessary to make informed decisions when contracting for electric supplies. Therefore, it may be appropriate to establish consumer education and information programs if retail competition is deemed appropriate in Louisiana. Such programs could be administered through utilities or public agencies and may require special funding mechanisms.

The above consumer protection measures may do little to protect the customers of low cost utilities subsequent to a transition period if prices increase as a result of restructuring. One possible measure for protecting such customers is to allow such customers to continue to purchase supplies at capped or embedded cost rates from their current utility over an extended transition period. Transition periods of this nature would also provide additional time for the development and maturation of

competitive market structures, information technologies, consumer protection measures, and consumer education programs.

Consumer Education

Most retail customers, especially residential and small commercial customers, are probably not aware that electric industry restructuring is underway or that they may soon have both the opportunity and responsibility to select their own electricity services provider. The potential for public confusion, annoyance and even fraud is present. For these reasons, it is desirable for public policy to undertake a public education effort directed at preparing the public for retail customer choice.

Competing retailers will also provide customers with the sort of product and services information that characterize all retail markets but retailers may not be the best source of information about the transition to choice and basic description of how the new market will work. Government could either do the more fundamental consumer education on its own or direct the monopoly distribution company to do it.

Universal Service

Universal service refers to the ability of all Louisiana citizens to obtain essential electricity, which is a necessity of modern life.

Retail choice will allow customers and sellers to select each other, and if these sellers are unregulated they may elect never to serve low-income customers, or may choose to stop service in whatever manner the unregulated retail power sales agreement provides. Provisions for universal service should be an integral part of a retail choice scheme, at least until it can be determined that competitive retailers will voluntarily achieve acceptable levels of universal service.

Accordingly, any restructured electric utility industry should provide adequate safeguards to assure universal service. Minimum residential customer service safeguards and protections should be maintained. Programs and mechanisms that enable residential customers with low incomes to manage and afford essential electricity requirements should be included as a part of industry restructuring.

Stranded Benefits

Competition in electricity sales will put pressure on utilities to cut costs. Although this should push electricity prices down overall, it may squeeze out some vital functions performed today by the electric industry. Some of the first expenditures on the chopping block may be services for the public at large, such as the previously discussed uniform consumer protections or investments in energy efficiency.

HB

82

HOUSE COMMITTEE REPORT

(7)

Date Referred to Committee: February 5, 1999

FURTHER REFERRALS:

Judiciary

Date of Committee Action: 3 Mar 1999

The LABOR AND COMMERCE Committee considered:

HB 82

HOUSE BILL NO. 82

IMMUNITY: CLAIMS ARISING FROM Y2K PROBLEMS

"An Act relating to immunity for certain claims arising out of or in connection with the year 2000 date change; and providing for an effective date."

recommends it be replaced
with the following committee substitute

CSHB 82 (L+C)

the same title
 a new title

additional referral to _____ Committee
 attached amendment(s)

ADOPTS: _____ Letter of Intent

ATTACHES NEW FISCAL NOTE(S): (Dept)

APPROVES PREVIOUS: (Dept/Date)

fiscal note(s) _____

fiscal note(s) _____

zero fiscal note(s) Levt

zero fiscal note(s) _____

Coert

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CHAIR'S SIGNATURE

[Signature]

3-3-99

FISCAL NOTE

STATE OF ALASKA
1999 LEGISLATIVE SESSION

BILL NO. HB 82

Revision Date/Time (Note if correction)	Dept. Affected	Law
Title	BRU	Civil Division
out of or in connection with the year 2000 date change; ..."	Component	Governmental Affairs
Sponsor		Transportation
Requester	Component Serial No.	2207/2214

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2000	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005
Personal Services						
Travel						
Contractual						
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL EXPENDITURES						
-----------------------------	--	--	--	--	--	--

CHANGE IN REVENUES ()						
-------------------------------	--	--	--	--	--	--

FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type)						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY99) cost: _____

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

HB 82 provides immunity for claims against persons engaged in business arising out of or in connection with the year 2000 date change.

Enactment of this legislation will have no fiscal impact on the Department of Law.

Prepared by Joan M. Kasson
 Division Attorney General's Office
 Approved by Commissioner Bruce M. Bielecki, Attorney General
 Agency Department of Law

Phone 465-5370
 Date/Time 2/11/99, 9:20 AM
 Date 2/11/99

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FISCAL NOTE

STATE OF ALASKA
1999 LEGISLATIVE SESSION

BILL NO. HE 82

Revision Date _____ Dept. Affected Alaska Court System
 Title Immunity from Y2K Claims BRU Alaska Court System
 Component Trial Courts
 Sponsor Rep. Rokeberg
 Requester House Labor & Commerce Component Serial No. 769

Expenditures/Revenues (Thousands of Dollars)

OPERATING EXPENDITURES	FY 2000	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005
Personal Services						
Travel						
Contractual						
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL EXPENDITURES						
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CHANGE IN REVENUES ()						
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FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF	0.0	0.0	0.0	0.0	0.0	0.0
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type)						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY99) cost: None

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: *(Attach a separate page if necessary)*

No fiscal impact.

Prepared by: Doug Wooliver, Administrative Attorney
 Agency: Alaska Court System
 Approved by: Stephanie J. Cole, Administrative Director
 Agency: Alaska Court System

Phone: 264-8265
 Date/Time: 2/8/99 8:58 AM
 Date: 2/8/99

CS FOR HOUSE BILL NO. 82(L&C)
IN THE LEGISLATURE OF THE STATE OF ALASKA
TWENTY-FIRST LEGISLATURE - FIRST SESSION

BY THE HOUSE LABOR AND COMMERCE COMMITTEE

Offered:
Referred:

Sponsor(s): REPRESENTATIVES ROKEBERG, Dyson

A BILL

FOR AN ACT ENTITLED

1 "An Act relating to certain claims arising out of or in connection with the year
2 2000 date change; amending Rule 23, Alaska Rules of Civil Procedure; and
3 providing for an effective date."

4 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

5 * Section 1. AS 09.65 is amended by adding a new section to read:

6 Sec. 09.65.260. Claims against persons engaged in business arising out of
7 or in connection with the year 2000 date change. (a) A business or a member of
8 the board of directors of a business is not liable for damages arising from the year
9 2000 date change and caused directly or indirectly by a failure of an electronic
10 computing device used in the business if the business shows by a preponderance of the
11 evidence that

12 (1) the business made the following efforts to avoid the damages
13 claimed in the civil action:

14 (A) inventory the electronic computing devices used by the

1 business that may experience year 2000 date change failures;

2 (B) identify critical electronic computing devices necessary to
3 conduct the operations of the business;

4 (C) identify the potential for year 2000 date change failures
5 associated with electronic computing devices used by the business;

6 (D) prepare a plan to reprogram, fix, repair, replace, or
7 otherwise remedy the electronic computing devices necessary to avert failure
8 resulting from the year 2000 date change;

9 (E) comply with industry regulations or requirements related to
10 the year 2000 date change, including testing information systems for
11 compliance with the year 2000 date change; and

12 (F) develop contingency plans in the event of an electronic
13 computing device failure; or

14 (2) the business, by following generally accepted standards of care and
15 effort in the business activity in which the business was engaged, exercised due
16 diligence and reasonable care to prevent or remedy damages arising from the year
17 2000 date change and caused directly or indirectly by a failure of an electronic
18 computing device.

19 (b) The defense in (a) of this section may not be asserted

20 (1) by a business that develops or manufactures software, firmware,
21 microcode, hardware, or embedded microchips that create, read, write, calculate,
22 compare, sequence, or otherwise process data that consists of dates, times, or both
23 dates and time if the business represented that the software, firmware, microcode,
24 hardware, or microchips were year 2000 date change compliant; this paragraph does
25 not apply to a business that only sells, rents, or leases software, firmware, microcode,
26 or hardware that is developed or manufactured by another person; or

27 (2) in an action based on a contract.

28 (c) A civil action against a business, or member of the board of directors of
29 a business, for damages arising from the year 2000 date change and caused directly
30 or indirectly by a failure of an electronic computing device used in the business may
31 not be brought as a class action unless each member of the class has a claim for

1 economic loss that exceeds \$50,000.

2 (d) In a civil action against a business, or member of the board of directors of
3 a business, for damages arising from the year 2000 date change and caused directly
4 or indirectly by a failure of an electronic computing device used in the business,

5 (1) damages may be awarded for economic losses only unless the
6 business against whom the action is brought committed fraud;

7 (2) the civil action may not proceed to trial until the person bringing
8 the action

9 (A) provides written notice to the business that describes the
10 failure of the electronic computing device arising from the year 2000 date
11 change; and

12 (B) gives the business the opportunity to fix the problem,
13 including reasonable access to electronic computing devices or software
14 affected by the failure described under (A) of this paragraph;

15 (3) the civil action must be submitted to mediation conducted under the
16 Alaska Rules of Civil Procedure, unless all the parties agree to waive mediation.

17 (e) In this section,

18 (1) "business" means a person or a for profit or a nonprofit entity
19 engaged in a trade, service, profession, or activity with the goal of receiving a financial
20 benefit in exchange for the provision of services, goods, or other property;

21 (2) "electronic computing device" includes any computer hardware or
22 software, a computer chip, an embedded chip, process control equipment, or other
23 information system that is used to capture, store, manipulate, or process data;

24 (3) "year 2000 date change" includes processing date or time data from,
25 into, and between the Twentieth and Twenty-First Centuries, and leap-year
26 calculations; in this paragraph, "processing" includes calculating, comparing,
27 sequencing, displaying, and storing.

28 * Sec. 2. AS 09.65.260 is repealed January 1, 2006.

29 * Sec. 3. AS 09.65.260(c), enacted by sec. 1 of this Act, has the effect of amending
30 Rule 23, Alaska Rules of Civil Procedure, by requiring, in a class action relating to the year
31 2000 date change, that each member of the class have a claim for economic loss that exceeds

1 \$50,000.

2 * Sec. 4. APPLICABILITY. This Act applies to a cause of action arising from any failure
3 described in AS 09.65.260, enacted by sec. 1 of this Act, that accrues on or after the effective
4 date of this Act but before January 1, 2006.

5 * Sec. 5. This Act takes effect immediately under AS 01.10.070(c).

The United States Senate
Special Committee on the Year 2000 Technology Problem

Senator Robert F. Bennett, Chairman
Senator Christopher J. Dodd, Vice Chairman



**Investigating the Impact of
the Year 2000 Problem**

*Competing pressures tempt one to believe
that an issue deferred is a problem avoided;
more often it is a crisis invited.*

Henry Kissinger

Summary of the Committee's
Work in the 105th Congress

February 24, 1999

For Full Report:

<http://www.senate.gov/ny2K/>

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INVESTIGATING THE IMPACT OF THE YEAR 2000 PROBLEM

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EXECUTIVE SUMMARY

The Committee has found that the most frustrating aspect of addressing the Year 2000 (Y2K) problem is sorting fact from fiction. Reports from even the most reputable news sources fall prey to polarizing forces—either over emphasizing a handful of Y2K survivalists, or downplaying the event as a hoax designed to sell information technology equipment.

The Internet surges with rumors of massive Y2K test failures that turn out to be gross misstatements, while image-sensitive corporations downplay real Y2K problems. The good news is that talk of the death of civilization, to borrow from Mark Twain, has been greatly exaggerated. The bad news is that Committee research has concluded that the Y2K problem is very real and that Y2K risk management efforts must be increased to avert serious disruptions.

Y2K is about more than the failure of an individual's personal computer or an incorrect date in a spreadsheet. As one examines the multiple layers of systems and technologies that support our everyday lives, the potential Y2K problems increase exponentially. The interdependent nature of technology systems makes the severity of possible disruptions difficult to predict. Adding to the confusion, there are still very few overall Y2K technology compliance assessments of infrastructure or industry sectors. Consequently, the fundamental questions of risk and per-

sonal preparedness cannot be answered at this time.

On the positive side, Y2K awareness is growing. In the past year, both public and private institutions have doubled their efforts to find, evaluate, and address Y2K risk exposure. The Committee has seen a significant amount of progress since its inception. However, Senate hearings, interviews, and research have not produced convincing evidence that the Y2K problem is well in hand.

The biggest Y2K impact may occur internationally. While the U.S. should have started its Y2K preparations earlier, worldwide preparations generally lag even further behind.

OVERALL OBSERVATIONS

Many organizations critical to Americans' safety and well-being are still not fully engaged in finding a solution.

For example, over 90% of doctors' offices and 50% of small- and medium-sized businesses have yet to address the problem. Larger firms have, in general, grasped how a Y2K failure could severely impact their businesses and are taking steps to remedy the problem. Smaller firms remain more focused on what they perceive as more immediate concerns, which in many cases do not include Y2K.

INVESTIGATING THE IMPACT OF THE YEAR 2000 PROBLEM

Most affected industries and organizations started Y2K remediation too late.

As a result, many organizations must exercise "triage"—focusing on what is critical to sustain the life of the enterprise as opposed to finding long-term solutions.

Self-reporting has yielded unreliable assessments for most industry sectors. With few exceptions, disclosure of Y2K compliance is poor.

Analogous to letting students grade their own tests, self-reporting offers data of varying reliability. Nonetheless, it has become the standard in both private industry and government. Industry surveys are currently the most widely utilized tool to measure compliance. Unfortunately, the results of many surveys have been kept from public and Special Committee view (see "Transportation" in this report). Despite an SEC rule requiring Y2K disclosure of public corporations, companies are reluctant to report poor compliance levels.

Fear of litigation and loss of competitive advantage are the most commonly cited reasons for bare-bones disclosure.

Although sharing Y2K data could save time in companies' remediation and contingency planning efforts, such cooperation has not been forthcoming. To encourage greater disclosure, the Committee spearheaded a bipartisan effort that passed the Year 2000 Information Readiness and Disclosure Act (S.2392) and in-

troduced the CRASH Protection Act (S.1518). The Year 2000 Information Readiness and Disclosure Act provided a basic level of protection for Y2K statements made in good faith. The CRASH Protection Act pressured the SEC to require more meaningful Y2K corporate disclosure to shareholders.

More legislation may be necessary to address Y2K litigation. Some liability cost projections are as high as \$1 trillion. Serious doubts exist as to whether or not the present judicial system could handle a potentially monstrous wave of litigation.

The Committee plans to address certain key sectors in 1999 where there has been extreme reluctance to disclose Y2K compliance.

National emergency and security planning for Y2K-related systems failures is just beginning.

FEMA contingency plans are in draft form, but there is no national, strategic plan to assure that critical infrastructures will continue to function.

This is partially due to varying levels of state and local government preparedness. State and local governments represent the first line of defense in emergency situations, and emergency planning is difficult without their full involvement. A recent Labor Department report stated that several states are lagging in specific Y2K system repairs relating to federally funded programs.

Leadership at the highest levels is lacking.

A misconception pervades corporate boardrooms that Y2K is strictly a technical problem that does not warrant executive attention. Some government sectors lack clear directives and policies on Y2K.

SECTOR ASSESSMENTS

Since its establishment in April 1998, the Special Committee has held nine hearings on seven critical economic sectors:

- Utilities
- Health care
- Telecommunications
- Transportation
- Financial institutions
- Government
- General business

The eighth sector, Litigation, will be addressed in early 1999.

The Committee plans to revisit each of the sectors in 1999, with emphasis on litigation and the addition of international concerns to the list of critical sectors. The Committee will assess the nation's progress toward Y2K compliance and pinpoint problem areas. The Committee will also continue to provide recommendations to Congress for legislative action.

UTILITIES

While some compliance efforts are behind, the utility industry as

a whole is configured to handle interruptions, blackouts, and natural disasters. A prolonged, nationwide blackout is not likely to occur. However, local and regional outages remain a distinct possibility depending upon the overall preparedness of the individual electric utility serving a given area.

The nation's electric power industry comprises 3,200 independent utilities. Overall remediation of the electric power industry is slow. According to NERC, only about 50% of the utilities had completed Y2K remediation as of December 1998. Failure of some parts of the electric industry's system is likely, but the Committee does not expect the integrity of the overall power grid to be compromised. Of greatest concern are approximately 1,000 small, rural electric utilities that may not have the resources to devote to Y2K compliance.

Compliance among oil and natural gas utilities is also progressing slowly. A survey by the Committee, while limited in scope, indicates a lack of contingency planning, overly optimistic assertions that compliance will be complete, and a lack of knowledge about suppliers' Y2K status.

HEALTH CARE

The health care industry lags significantly in its Y2K preparations compared to other sectors. Because of limited resources and lack of awareness, rural and inner-city hospitals have particularly

high Y2K risk exposure.

Health care is the nation's single largest industry, generating \$1.5 trillion annually. There are 6,000 hospitals, 800,000 doctors and 50,000 nursing homes, as well as hundreds of biomedical equipment manufacturers and suppliers of blood, drugs, linens and bandages—and health care insurers—that may be unprepared for the year 2000.

According to a report by the Gartner Group, 64% of hospitals—primarily smaller hospitals—have no plans to test their Y2K remediation efforts. In addition, 90% of physicians' offices are unaware of their Y2K exposure. Struggling compliance efforts by HCFA (the agency that oversees Medicare) and unaddressed concerns about medical devices are major roadblocks to the industry's Y2K readiness.

TELECOMMUNICATIONS

A massive industry-wide effort is underway to assess the impact of Y2K on telecommunications. The initial interoperability testing indicates that the U.S. communications will transition without significant problems. Currently, more than 80% of public network systems have been tested and are considered compliant.

The telecommunications industry has spent billions on Y2K fixes and should have 99% of access lines in compliance by the fall 1999. Currently, industry and government are working together to coordinate contingency plans in case there are fail-

ures. Industry in U.S. and overseas has established warning networks to alert each other of Y2K problems.

TRANSPORTATION

The transportation sector is the linchpin for just-in-time inventory management across most every sector, from health care supplies to food. The Y2K readiness of this sector is critical to our global economy. Planes will not fall out of the sky, but disruption of flights and global trade between some areas and countries may occur.

On average, the nation's 670 domestic airports started Y2K compliance too late. The Federal Aviation Agency has made great strides in the past year, but remains at risk. The situation with international air traffic control and airports is much more severe. The maritime shipping industry has not moved aggressively toward compliance. Public transit could be seriously disrupted.

FINANCE

ATMs are expected to function correctly and banks should have adequate cash to meet consumer demand, based on a Federal Reserve estimate that each American household will withdraw an average of \$500. The securities industry has responded well to its internal Y2K issues and has undertaken expansive testing. However, fund managers and brokers have only recently started to consider the implication of corporate Y2K vulnerability on investment decisions.

INVESTIGATING THE IMPACT OF THE YEAR 2000 PROBLEM

The financial services sector ranks ahead of nearly all other industries in its remediation and testing efforts. Legislation in Congress and action by the Committee have led to legal requirements on broker-dealers and publicly traded companies to disclose compliance information.

Federal regulators have made considerable progress in tracking compliance among banks, thrifts and credit unions, of which 95% have received satisfactory government ratings.

GOVERNMENT

Several state and many local governments lag in Y2K remediation, raising the risk of service disruption. The federal government will spend in excess of \$7.5 billion and will not be able to renovate, test, and implement all of its mission critical systems in time. However, wholesale failure of federal government services is not likely to occur.

The Committee's work in this sector includes national emergency planning as well as federal, state, and local government preparedness. After a late start, FEMA is now engaged in national emergency planning in the event of major and minor Y2K disruptions.

State and local governments vary widely in their Y2K preparations. Several states are not prepared to deliver critical services such as benefit payments. Of greatest concern to the Committee is the ability of local communities to provide 911 and emergency services.

The federal government also varies widely in its Y2K preparations. The Social Security Administration started early and is prepared, while other agencies, like the Department of Defense, are lagging. To its credit, the federal government publicly displays its Y2K status through quarterly and monthly reports to the Office of Management and Budget.

GENERAL BUSINESS

In general, large companies have dealt well with the Y2K problem, due to greater resources. Very small businesses may survive using manual processes until Y2K problems are remediated. However, many small- and medium-sized businesses are extremely unprepared for Y2K disruptions. One survey shows that more than 40% of 14 million small businesses do not plan to take any action.

The heavily regulated insurance, investment services, and banking industries are furthest ahead in their efforts: health care, oil, education, agriculture, farming, food processing, and the construction industries are lagging behind. The cost to regain lost operational capability for any mission critical failure will range from \$20,000 to \$3.5 million, with an average of 3 to 15 days necessary to regain lost functions.

LITIGATION

The prospect of litigation arising from Y2K-related failures has shadowed the Committee's work from the very beginning. Some estimates project litigation cost in excess of \$1 tril-

INVESTIGATING THE IMPACT OF THE YEAR 2000 PROBLEM

lion. The Committee plans to hold hearings and work closely with the Judiciary and Commerce Committees to make legislative proposals in this area.

INTERNATIONAL

Several U.S. trading partners are severely behind in their Y2K remediation efforts. For example, the Gartner Group estimates that Venezuela and Saudi Arabia (two of the largest U.S. oil importers) are 12 to 18 months behind the U.S. in their Y2K remediation efforts.

The Committee is greatly concerned about the international Y2K picture. The U.S. is dependent on a healthy global economy. It is in the interest of the U.S. to encourage Y2K remediation worldwide.

* * * * *

The challenges posed by the Y2K problem are numerous and daunting. The Special Committee conducted

extensive research and held numerous hearings in 1998, but still cannot conclusively determine how extensive the Y2K disruptions will be. The Committee has no data to suggest that the United States will experience nation-wide social or economic collapse, but the Committee believes that some disruptions will occur, and that in some cases Y2K disruptions may be significant. The international situation may be even more tumultuous.

There are reasonable steps individuals may take to prepare for the Year 2000. Consumers are urged to keep copies of financial statements and ask local banks what efforts are being made toward Y2K compliance. Individuals should research companies' compliance levels before making investment decisions. The Y2K problem has been likened to a winter storm, with the implication that similar preparation is appropriate. Americans should prepare for Y2K based on facts and reasonable predictions about the problem's effects on vital services.

Subject: Fwd: Y2k Testimony

Date: Wed, 3 Mar 1999 13:37:30 EST

From: Thyes@aol.com

To: Representative_Norman_Rokeberg@legis.state.ak.us, Janet_Scitz@legis.state.ak.us

Following is a copy of Y2K testimony of an NFIB member to the Senate Judiciary Committee in Washington DC.

Thyes

Subject: RE: Y2k Testimony

Date: Tue, 2 Mar 1999 08:29:16 -0600

From: "Cameron, McCall" <McCall.Cameron@nfib.org>

To: "'Thyes.Shaub@NFIB.ORG'" <Thyes.Shaub@nfib.org>

Testimony of B.R. McConnon
President, Democracy Data and Communications

Before: Senate Judiciary Committee

Date: 1 March 1999

Subject: Year 2000 Fairness and Responsibility Act

Good morning, Mr. Chairman and members of the Committee. My name is B.R. McConnon and I am from Alexandria, Virginia. I am the President and owner of Democracy Data and Communications, a grassroots database management company located in Old Town. We currently have 18 full time employees who manage a variety of databases for our clients, which include many of the nation's largest corporations.

I am pleased to be here today testifying on behalf of the National Federation of Independent Business regarding potential problems resulting from Year 2000 failures. NFIB is the nation's largest small business advocacy organization, representing more than 600,000 small business owners in all 50 states and the District of Columbia. The typical NFIB member employs five people and grosses \$350,000 in annual sales.

Nationwide, the small business community is making progress towards inoculating itself against "the millennium bug." A recent NFIB Education Foundation study found that, as of November 1998, 1.9 million small firms have addressed their Y2K problems. I am proud to say that I am among them. Considering that I am in a computer-based business, it should come as no surprise that becoming Y2K compliant was very important to the survival of Democracy Data. We have nearly 30 computers that run dozens of software packages simultaneously every day. I depend on these systems to store and process data and to make it accessible to clients through the Internet. Because I was concerned about their operation after the millennium date change, my chief technology officer and I initiated a series of intricate tests to ensure that each of our systems and software packages would continue to operate without Y2K problems. Although it cost my company several thousand dollars and took several days, it was worth it, considering my

business would fail to operate if not Y2K compliant.

Like most businesses, however, Democracy Data does not operate in a vacuum. I am dependent upon numerous vendors and suppliers who provide my company with the input data necessary for us to create several of our core products. These vendors include commercial data providers who supply Geographic Information Systems (GIS) or electronic mapping data, state governments who supply us with a range of geographic and other data, and other commercial vendors who rely on the United States Postal Service and the Census Bureau as primary data sources. I also rely on our clients' information systems staff to supply us with the data that we store and manipulate -- an absolutely essential function if we are to be able to do our part. Without the services these vendors provide and the data provided by the companies themselves, I would not be able to serve my clients as they expect. And at the end of the day, their failure is my failure.

Though my own systems and software may be "bug-free," I am still at risk should Y2K problems afflict my suppliers, clients or financial institutions. In a perfect world, every business would take steps to fix their problems now, but that is not happening. There will be failures. There will be late shipments, damaged goods and failed data delivery. For example, should the Postal Service fail to supply current, accurate data to our commercial vendor, that vendor in turn could not add their critical component to the data we use. Consequently, Democracy Data would not be able to supply our clients with the data and service that they expect and need. While it is impossible to know the extent to which any one of us will be impacted, I do believe that we must prepare to be affected.

That is why I am so pleased to see the Congress taking action on this issue. I work hard every day to deliver on my promises to clients. If one of my vendors has a Y2K failure that impacts my ability to serve clients, I could have a serious problem on my hands -- possibly even a lawsuit. I could be sued by a client who is displeased with my services. If the situation could not be resolved any other way, I may have no choice but to sue my vendors. I have worked hard to build good relationships with my clients and the other businesses I depend on. Going to court is the recourse of last resort -- especially since Y2K problems can most likely be avoided.

Now, I am not a lawyer, but I do know from my own experience that it wouldn't take much of a lawsuit to knock a small business out of business for good. Two years ago, I was involved in a lawsuit that was not only expensive, but took up valuable time and kept me from running my business. While I ultimately triumphed, the lost revenue during the time that I spent with lawyers on interrogatories and depositions far exceeded the legal fees. My experience just goes to show that lawsuits can seriously burden a small business, regardless of whether you are a plaintiff or defendant and regardless of whether the suit is legitimate. The emphasis should be on quick resolution of disputes, not on expensive and time consuming litigation.

For these reasons, I believe that any legislation Congress enacts should do three things:

First, Congress must create incentives to mitigate, not litigate. It is essential that businesses of all sizes are urged to address their Y2K problems NOW. Otherwise, 2000 will go down in history as the Year of the Lawsuit. Every business depends on other businesses. The more problems we can anticipate and fix, the better it will be for

everyone.

Second, Congress must encourage the settlement of Y2K disputes to happen as quickly as possible. For a small business, it all comes down to the bottom line -- cash flow. If my vendors do not provide me with the data and access I need, I cannot operate. If my clients aren't satisfied with the service I provide, they will stop using my company. It doesn't take long for a company operating in a competitive environment such as ours to go out of business. Disputes should be settled as quickly as possible and outside of court when feasible. Getting a court date can take months if not years. What it may cost small business owners is their livelihood.

Third, Congress must curb the desire to file frivolous lawsuits by placing limits on punitive damages. 93% of NFIB members support capping damage awards for this very reason. If I am forced to enter into Y2K legal action with one of my vendors, I would do so only to recover what is owed to me. I don't want to "punish" my vendors -- I want to continue working with them! The relationships I have built over time are essential to the operations of my business and no Y2K glitch should endanger them. Limiting punitive damages will keep unnecessary lawsuits at a minimum, allowing businesses to recover their actual damages more quickly.

I believe the bill introduced by Senators Hatch and Feinstein, the Year 2000 Fairness and Responsibility Act, will accomplish these three important goals. Although some may argue that we don't need federal legislation to address these issues, I disagree. Businesses need a push to get their own Y2K house in order, and the reward should be quicker dispute resolution and fewer lawsuits.

I would like to thank the Committee for the opportunity to testify before you today and hope that you will act quickly on this bill. I would be pleased to answer any questions you might have.

Testimony of

B.R. McConnon

President

Democracy Data and Communications
Alexandria, VA

Before: Senate Judiciary Committee

Date: March 1, 1999

Subject: Year 2000 Fairness and Responsibility Act

-----Original Message-----

From: Thyes.Shaub@NFIB.ORG [SMTP:Thyes.Shaub@NFIB.ORG]
Sent: Monday, March 01, 1999 6:20 PM
To: McCall.Cameron@NFIB.ORG
Subject: Re: Y2k Testimony

Please fax to my office at: 907-463-5128.

Thanks!

Thyes

CONTACT: Thyes Shaub @ 907463-5118 or Jim Weidman @ 202/554-9000

NFIB/ALASKA SEEKS SMALL-BUSINESS IMMUNITY FROM Y2K LAWSUITS

JUNEAU, Feb. 24, 1999—The state chapter of the National Federation of Independent Business (NFIB) is urging lawmakers to inoculate Main Street business owners from lawsuits spawned by "the millennium bug."

"Small-business owners aren't seeking any special privileges," said Thyes Shaub, director of the 3,700-member NFIB/Alaska. "But we are asking that the Legislature extend to the private sector, whatever level of immunity they think is appropriate to offer state and municipal governments."

The Alaska Chapter of the National Federation of Independent Business supports HB 82, introduced by St. Rep Norm Rokeberg, R-Anchorage. The bill would limit small-business owners' liability in suits filed because of problems created by "Year 2000" computer glitches. The House Labor and Commerce Committee will hold a hearing on the bill Friday.

Shaub noted that state and local government officials have been pressing for immunity from Year 2000-related lawsuits. "NFIB believes public **and private entities** that make legitimate efforts to address the Y2K problem should be removed from any legal liability for unanticipated and wholly unintended failures," she said. An NFIB/Alaska survey last October found 73 percent of the group's members favored limiting Y2K-related liability.

The small-business advocate stressed that her group has no intention of squelching legitimate legal efforts to recover losses that may arise from computers or other equipment that malfunctions due to time/date devices that cannot accommodate the Year 2000 date change. "Small businesses are as much at risk as anyone of suffering second-hand damage from the millennium bug," she said. "They can be crippled or destroyed by problems originating in suppliers' or customers' operations."

-more-

Because small firms are as likely to be potential plaintiffs as they are to be named as defendants in a Y2K liability suit, "NFIB is merely asking for a level playing field for litigation," Shaub said. "We will not support legislation that gives a clear advantage to either plaintiff or defendant. Nor will we support immunity for government entities without comparable immunity in the private sector."

Should public agencies receive immunity, she warned, "it will be open season on the business community, as far as trial lawyers are concerned." Suppose a business is unable to deliver goods because of a Y2K problem originating in a government agency, she suggested. "If the agency is off-limits, lawyers will train both barrels on the business, who's only 'crime' is being let down by the agency's failure."

Shaub also predicted granting immunity now would help prevent Y2K problems. "Some businesses have been reluctant to share Y2K 'fix' information with others, for fear of lawsuits if there is a problem. A limited immunity provision would thaw the chill that now hampers information exchange, helping more people fix their problems before the New Year rolls around."

A special report on "Small Business and the Y2K Problem" is available on the Internet at www.nfibonline.com.

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Senate Y2K watchers sound muted alarm

By Anne E. Kornblut, Globe Staff, 03/03/99

WASHINGTON - Forget Y2K. Now, it's all about TEOTWAWKI.

The dire acronym for "the end of the world as we know it," which predicts what will occur at the stroke of midnight, Jan. 1, 2000, is in vogue on Web sites. Yesterday it made its way at last into the Senate, as lawmakers met in a closed session to discuss the potential Year 2000 crisis.

Most said afterward that there was no reason to panic. But as senators discussed the contents of a 160-page report on the topic, they occasionally uttered warnings that made the Y2K problem seem like a legitimate threat.

Senator Christopher Dodd, Democrat of Connecticut, advised citizens to stock up on canned goods. Senator Gordon Smith, an Oregon Republican, suggested that passengers ask airlines about Y2K before boarding a plane this New Year's Eve. Senator Robert Bennett, Republican of Utah, said there was a great likelihood of economic disruptions around the world as a result of computer glitches accompanying the millennium, though he said national-security concerns appeared to be less of a threat.

"There is a low probability of a nuclear launch," Bennett said. The head of the Senate's Special Committee on the Year 2000 Problem, however, would not rule out the possibility of intercontinental warfare as a result of Y2K.

The remarks followed a private session devoted in part to informing senators about the Y2K problems faced by other countries, particularly Russia and China, whose military forces appear ill-equipped to handle a possible computer breakdown.

Bennett said Russia faced the threat of "deterioration of their military capabilities because Y2K simply adds to their problems," such as their inability to pay the salaries of members of the military in recent months.

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Bennett said there is a "medium probability of economic disruptions that will lead to civil unrest."

"We think the chances of difficulty are much higher internationally," said Bennett.

To address the potential threat of international war, lawmakers are considering establishing a center in Colorado Springs where officials from various countries would gather at the millennium. Dodd referred to the facility, where officials would observe one another to ensure no nation was launching a military offensive, as the Center for the Year 2000 Strategic Abilities. He said Russia was the only nation on the guest list so far.

To address potential problems in this country, the Senate yesterday unanimously passed legislation to help guarantee loans to small businesses in order for them to fix their computer systems. The House has yet to act on the legislation.

Senator John F. Kerry of Massachusetts, the ranking Democrat on the Small Business Committee, said that "unless businesses deal with that issue now, they can wind up losing money and being hurt."

But in general, Kerry said, "in this country, I think the effects" of Y2K "will be negligible."

"I think there are much greater dangers abroad," he said.

Although domestic companies may be far better equipped for the millennium, many medical centers are still unprepared. About 64 percent of the nation's 6,000 hospital facilities have yet to adjust their computer systems, according to a report by the Gartner Group.

About 80 percent of all doctors offices, many of which would qualify for assistance through the loan bill the Senate passed yesterday, are unprepared for the end of 1999.

Telecommunications and energy systems are far better off, Bennett said. He downplayed a test failure at a power plant in York, Pa., last month as "not in any way life-threatening or safety-threatening."

The failure, Bennett said, occurred when power plant officials turned the clocks forward during a Year 2000 test. The failure mystified plant officials for several hours.

"That's why you do tests," Bennett said. "Let's not overreact to that."

Senators, however, did hint at fears about traveling on the night the century turns. Smith said airlines are likely to hold their computer systems to a higher standard than the government recommends, but cautioned that passengers should contact airlines before taking a flight.

And Dodd said travelers going abroad for New Year's Eve "might want to go a few days early and stay another couple of days."

"The analysis we've been given here is that about 90 percent of the problems that we could face at home should be remediated or resolved within 72 hours. ... So I wouldn't be discouraging people from foreign travel," Dodd said. "But if I had to make reservations today ... I'd certainly leave a little leeway on either side."

This story ran on page A03 of the Boston Globe on 03/03/99.
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Subject: HB 82 Information

Date: Mon, 01 Mar 1999 17:58:20 -0900

From: "Scott Thorson" <SCOTT@nbsys.com>

To: Representative_Norman_Rokeberg@legis.state.ak.us

MAR 03 1999

First let me thank you for allowing me to testify in front of your committee on Friday afternoon. I feel that you have the best interests of our state and our economy at heart as far as this bill is concerned.

If I can be of any further assistance, I would be happy to do what I can to help you move this bill. I think this is a win - win for business here.

I thought it might be helpful if I provided additional information for you regarding Y2K issues. Attached to this message are the following files:

HB 82.doc

This is a copy of the remarks I had prepared for you. As you may recall, I did not read these into the record. I am providing them for you in case you think it would be helpful to add them to the record.

y2k#1.doc

This is an article about the efforts some states are making to do something similar to what you are doing. I thought it might be helpful in that there is some discussion about why some people do not like imunity bills. I am providing this to you so you might be able to think about a response to negative responses.

y2k#2.doc

This is a whitepaper I found on <http://www.vear2000.com/>
This is a web site called the Year 2000 Information Center and I find it helpful when researching Y2K issues. Sadly this document is about 30 pages long and it is not exactly a riviting read. I found it helpful in understanding some of the more major components of the Y2K issue.

y2k#3.doc

This is an article written by an attorney that explains some things businesses can do to prepair for Y2K problems.

I am not sure what kind of computers you have on your desktop, so I saved these documents in Microsoft Word version 2.x for Windows. This is one of the oldest versions of Word. Word for Macintosh or newer versions of Word running on PCs should open them as well as WordPerfect.

If you have problems opening these documents, please let me know and I will fax them to you.

Once again, thank you for the opportunity to work wittth you on this very important bill.

Scott Thorson

Sent e-mail asking Scott to fax. - See attached

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From: SCOTT THORSON

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HERE ARE THE DOCUMENTS YOU REQUESTED. I WROTE
THE FILE NAME ON EACH DOCUMENT FOR YOU.

SCOTT

Testimony of Scott Thorson in Support of HB 82

Chairman Rokeburg, members of the committee, ladies and gentlemen, good afternoon. My name is Scott Thorson. I am the President and Owner of Network Business Systems (NBS), which is one of the largest computer networking companies in Alaska. There are currently 45 employees at NBS, most of who are technically certified by at least one of many manufactures such as Microsoft, Novell or Compaq. I am speaking today on behalf of my company. NBS is one of the few Alaskan owned and operated companies that operate in our market space, as most of our competitors are owned by large companies from outside Alaska. All of our employees live here in Alaska, and many of our people are life long Alaskans.

I am here today to offer my support for HB 82. I would like to thank Representatives Rokeburg and Dyson for having the foresight to think this issue is important enough to be addressed with legislation. I very much agree with them and I am happy to see this kind of proactive thinking coming from the Legislature.

I feel HB 82 is valuable and should be enacted into law. I support the section of the bill that requires an organization to not be negligent in order to be afforded the protection from unnecessary and frivolous law suits this bill looks like it provides.

As I understand the intent of the bill, this protection is being afforded to organizations who operate computing devices in support of their business operations. I agree with the concepts in this bill such as; if an organization does what a manufacturer recommends and the system still fails to operate due to Y2K problems, that organization should be held harmless. The manufacturer, not the organization who deployed the technology, caused the problems.

I believe however, there some things missing from the bill. Service providers like NBS, who in good faith exercise due diligence and followed manufacturer or industry standards should be included in this protection when customer equipment fails to operate properly after the change of the millennium. If a service provider does not perform due diligence at the time of the engagement for a customer, that service provider should not be protected. However if at the time a Y2K issue is addressed by a service provider is done in accordance with the manufacturer's recommendations in effect at that time, the service provider has done its job, and should not be exposed to legal risk.

People in my industry are doing the best we can do for our customers to solve this difficult and evolving problem. The manufacturers and developers are not making compliance on Y2K solutions very easy. As an example, many of you may be aware that Microsoft recently released an operating system for computers

called Windows 98. During the process of releasing Windows 98, Microsoft said Windows 98 was Y2K compliant. Recently, Microsoft released a patch for Windows 98 to address Y2K problems that they found in the software after it was released. This release was not well publicized.

I want to stress that Microsoft is not alone in this kind of problem, nor do I think that they are negligent. I am only using this as an illustration to show you that solutions for this problem are a moving target and companies like NBS cannot be held liable for a problem they did not create.

This is not a problem that Microsoft has alone. It is a problem that is industry wide. Most manufacturers have released updates or changes to the procedures to make each product Y2K ready. Many of the procedures to make a product Y2K compliant are revised regularly. This makes it very difficult to be sure that a customer's product which is made Y2K compliant today will be compliant tomorrow, since there generally is no schedule for releasing these updates. These updates are handled on an as needed basis as the manufacturer sees fit.

If you multiply this across the number of manufacturers, multiply it against the vast number of products that each manufacturer has released over the last several years it is easy to see that keeping track of this is impossible for a small company. If you look at how many revisions and updates there have been to each product's Y2K compliance instructions, one soon realizes how difficult it is for an organization like NBS to guarantee that all devices and software are compliant.

This is a big problem for our industry, and I can tell you that I cannot insure my company against these problems. My insurance agent told me last week there is no way he can get an Errors and Omissions policy with a Y2K rider to cover me. Errors and omissions insurance specifically excludes Y2K coverage.

We are still doing Y2K repair work for our customers today because I do not feel good about leaving them unprotected from this problem. I am considering removing us from this line of business however because of the undefined risk. As the various Y2K issues including the risk of litigation evolves, it is becoming clear to me that to continue in this line of business, I am risking everything I own. Getting out of the business of addressing Y2K problems would not be good for our customers. If other companies in my business took this same tact, it would seriously impact the Alaskan economy. Leaving our customers hanging is not an option that I am comfortable with, but I may be faced with no other choice if I cannot properly protect my business from this significant risk.

If I can be of help with some of the technical details in the bill, I would be happy to make myself available to the committee to do so at a later time. Thank you for

your time today and for the opportunity to let you know how important this effort is. I will answer any questions that I can for you.

States seek protection from Y2K suits

INDIANAPOLIS (AP) - Dozens of states are preparing for the new millennium by seeking to protect governments from being sued for problems caused by the Y2K computer bug, a legislative trend critics say gives public agencies a license to procrastinate.

Lawmakers fear multimillion-dollar lawsuits filed by people harmed by glitches in government computers when internal clocks hit 2000. That's when experts say computers could get confused because they're programmed to read dates as two digits.

States are spending millions to check and fix computers that control such services as dispensing government checks, operating elevators and switching traffic lights from red to yellow to green.

Many lawmakers believe taxpayers shouldn't also be saddled with fat verdicts. But skeptics say immunity takes away a big incentive for government to fix computers.

"If you give them blanket immunity, they're not going to do anything," said Michael Aisenberg, a Washington lawyer who represents computer companies. "They're going to wait for failure, see what happens and have a triage for the worst-case problems."

Lawyers, consumer protection advocates and some lawmakers are fighting immunity bills. But bills are passing, in state after state.

Six states have Y2K immunity laws. Nevada was first, giving state and local government protection in 1997. California, Florida, Georgia, Hawaii and Virginia followed with varying forms of Y2K immunity, according to the National Conference of State Legislatures.

At least 32 more state legislatures are considering laws.

Immunity supporters say fear of lawsuits may hamper Y2K programs by shifting attention away from repairs to legal preparations.

"Instead of fixing the problem, we would be fortifying our defense," said Bill Pierce, head of Indiana's Y2K office.

Indiana senators voted Jan. 26 to give state and local government immunity from

Y2K lawsuits unless a plaintiff proves gross negligence, a higher-than-normal burden of proof.

State Sen. Luke Kenley said taxpayers should not get hit with frivolous lawsuits against public agencies that are making good-faith efforts to fix Y2K problems.

But immunity leaves injured people without legal recourse, said Sen. Joe Zakas. The family of someone killed in a crash because a stoplight malfunctioned Jan. 1 would have good reason to sue if they prove government workers didn't do their jobs, he said. "These are the people we are supposed to protect," Zakas said.

Many states have laws setting a higher burden of proof for suing the government. And lawyers say jurors, who would pay a share of verdicts, will reject frivolous suits against agencies that made an honest oversight.

But David Bender, a New York lawyer who writes extensively about computer law, believes some immunity laws are unconstitutional. "I can't approve of bills that on a grand scale remove the burden of liability from the guy who caused the problem and leave the innocent bystander who got injured without any remedy," he said.

Bender prefers laws granting limited immunity to companies or agencies that share information about fixing Y2K glitches - details some companies withhold for fear plaintiffs might use the information against them later.

Congress passed such a law last year. So did California. Other legislation is pending. For example:

- A bill in Minnesota would give the Mayo Clinic immunity if it shared successful Y2K strategies with smaller hospitals that needed help.
- A Maryland proposal would grant protection to governments or businesses - as long as they've done everything within reason to make computer systems compliant.

"It's possible for business to not live up to reasonable expectations, but this shouldn't become a happy hunting ground for lawyers," Maryland Chamber of Commerce president Champe McCulloch said.

Immunity opponents believe lawmakers should use oversight powers to boost Y2K compliance of computers used by government and regulated industries like utilities and banks. Wisconsin state Sen. Bob Jauch said lawmakers are acting before they know enough about Y2K's impact. "This isn't a race to take credit and pretend we're doing something," Jauch said. "This is a complicated issue and we can't simplify it with a simple symbolic act."

Wyoming's Senate Judiciary Committee killed a Y2K bill in January.

"I'm always uncomfortable when we rush to immunity every time something comes up," said state Sen. John Hanes. "I see a creeping trend toward more and more people and more and more entities immune to liability."

In reply, Sen. Steven Youngbauer said, "You have a little bit more faith in mankind than I do on frivolous lawsuits. I see them every day."

November 30, 1998

Y2K coverage for damages, losses is mired in debate

Benjamin Love Guest Columnist

By now, virtually everyone has become aware of the Y2K bug and the potential -- real or speculative -- for damage to occur in the form of loss of data, failure of computer hardware and microchips, and resulting property damage and business interruption costs.

Most businesses are well on the way to fixing their Y2K problems, testing solutions and surveying their most important customers, vendors and other interdependent business entities to assure compatibility of Y2K solutions. The potential litigation threat from Y2K issues has caused some to speculate that the costs of litigation and damages from Y2K problems may well exceed the combined cost of all environmental and asbestos litigation in the United States. How will Corporate America pay for this litigation? Even if the estimates are half-wrong, the expense will be exorbitant. What resources are available to respond to this problem? Insurance coverage?

Businesses are beginning to look to their Commercial General Liability and their Property and Business Interruption policies for potential coverage for Y2K damages and losses and costs of defense.

The insurance industry has loudly proclaimed that there can be no coverage for these types of damages since the Y2K problem has been known for many years and that damages and losses caused by this "planned programming glitch" will not be accidental. The insurers argue that current policies will not provide coverage for such losses.

Within the past year, the Insurance Services Office, an industry trade organization, has promulgated several endorsements to be added to current forms of CGL and other policies.

The endorsements provide exclusionary language for damages and losses resulting from the Y2K bug. In response, lawyers for policyholders have pondered the question of why the insurance industry feels the need to provide special endorsements to specifically exclude Y2K losses and damages if there is already no coverage under existing policies.

Perhaps there really is coverage -- or not? Such debates will undoubtedly be played out in courtrooms across America in coming years.

My review of the CGL policy forms currently approved for use in Texas cause me to believe that there very well may be coverage for some losses and damages caused by the Y2K bug.

Steps to take

To the extent that any such losses may be covered, policyholders should be taking steps now to review their insurance program. These steps may be useful for any business contemplating presenting a claim under a Commercial General Liability policy:

Identify all policies of insurance for the last 10 years.

Gather all underwriting information and application material.

Get a copy of every policy that was issued to the organization, including every endorsement and every declarations page.

Identify any and all excess and umbrella policies that may also have been in effect for the last 10 years and conduct the same analysis.

Identify all policies in which the organization is named as an additional insured and get copies of all policies from the primary insured on the policy. The policies may be available from the broker or agent, or the insurance carrier itself.

Conduct a review process in which the corporate risk manager, general counsel and an experienced insurance coverage attorney reviews all policies, coverages and exclusions.

Make certain that all insurance policies are included in the inventory -- directors and officers, CGL, first party and Y2K specific policies.

Have coverage counsel prepare a detailed risk assessment analysis for each policy for each policy year. Such analysis will identify the most likely claims under each available policy and the potential of coverage for each policy.

Write all insurance carriers with an enclosed survey prepared by counsel to determine if the organization's carriers are Y2K compliant.

Get copies of SEC 10-K and 10-Q filings and all filings with the Texas Insurance Commissioner regarding Y2K for each and every insurance carrier on the policies that are identified.

The Texas Insurance Commissioner is requiring carriers to issue reports or statements concerning loss control programs for policyholders. Carriers on some lines of insurance are required to provide loss control information based on risk, exposure, loss experience and other considerations.

While we may be a long way from litigating insurance coverage issues, policyholders that follow these steps will be placing themselves in a good position for the future.

Love is the owner and principal in his own law firm and Y2K Consulting Practice in the Metroplex. His Web site address is <http://www.benlove.com>. He can be contacted on Y2K matters and other insurance-related issues at ben@benlove.com.

LEGAL ISSUES CONCERNING THE YEAR 2000 COMPUTER PROBLEM: AN AWARENESS ARTICLE FOR THE PRIVATE SECTOR

by Jeff Jinnett

A serious computer problem, variously known as the "Year 2000," "Y2K," "Century Date Change" or "Millennium Bug" problem, faces many companies. This article is intended to provide a summary discussion of some of the major legal issues which may arise due to the Year 2000 problem and is written with non-lawyers as well as lawyers in mind.

BACKGROUND

The Year 2000 problem arises because most business application software programs (mainframe, client/server and personal computer) written over the past twenty years use only two digits to specify the year, rather than four. Therefore, on January 1, 2000, unless the software is corrected, most computers with time-sensitive software programs will recognize the year as "00" and may assume that the year is "1900". This could either force the computer to shut down (a "hard crash") or lead to incorrect calculations (a "soft crash"). Two digits were used by programmers in the past instead of four digits to designate the year to save (then-expensive) memory during processing. The Year 2000 computer problem can also affect embedded microcontrollers in non-computer equipment such as elevators, HVAC and security systems (see, e.g., "The Millennium Problem in Embedded Systems," located at the Internet Uniform Resource Locator (URL) of "<http://www.iee.org.uk/2000risk>" and M. Frautschi, "Embedded Systems and the Year 2000 Problem (the OTHER Year 2000 Problem)," located at <http://www.tmn.com/~frautsch/y2k2.html>).

As an example of the type of incorrect calculation which can be produced due to this problem, when a computer sorts dates by year, "00" (for the year 2000) could be identified as an earlier date than "99" (for the year 1999). A financial spreadsheet or projection therefore might show the financial trend for the 1999-2000 period running backwards rather than forwards. Insurance company computers might report a policy running through the year 2001 as having instead expired in 1901. A non-compliant bank computer calculating interest for a financial instrument for the six year period of 1995 through the year 2000 might instead calculate the interest for the period of 1900 through 1995, for a ninety-six year period instead of a six year period. More detailed information concerning the Year 2000 problem and available Year 2000 conferences and seminars can be found at the Internet URL of "<http://www.year2000.com>".

Year 2000 Problem Corrective Costs In the Billions

Gartner Group, Inc., an Information technology research firm, has estimated that it will cost between \$300 billion to \$600 billion to correct the Year 2000 problem worldwide. The software corrective work frequently is very time-consuming, requiring considerable programming effort to examine millions of lines of source code (software code readable by a human programmer) in order to locate the six digit date fields and correct them. For example, of the 128 companies surveyed in the Rubin Systems, Inc. March, 1998 Y2K survey, a majority of the companies surveyed expect to spend over \$100 million on their Y2K remediation plans. Although the costs of corrective action vary from company to company, it is not unusual to find reports of approximately \$1.10 per line of source code to correct the date field problem.

Modification of Existing Computer System Versus Migration to New Systems

In some cases, a company may have to make the initial decision as to whether to (a) modify its existing hardware/software system, or (b) migrate to new hardware/software platforms or architectures. It has been said that behind every crisis lies an opportunity. As an example of this, a company with an aging mainframe system may decide to migrate to a decentralized client/server system with local area networks and wide area networks. Alternatively, a company with an existing client/server environment may decide to create an "intranet" where its computers communicate with each other using the standards and protocols of the World Wide Web, the graphical portion of the Internet. For a company with an existing Internet site, the creation of an "intranet" or "private corporate web" would serve to add scalability to the company from its "intranet" through to its Internet site.

In making the above cost-benefit analysis, the company may wish to take into account the accounting and tax treatment of the possible alternative plans. It should be noted that The Emerging Issues Task Force ("EITF") of the Financial Accounting Standards Board ("FASB") decided on July 18, 1996 in its EITF Issue No. 96-14 "Accounting for the Costs Associated with Modifying Computer Software for the Year 2000" that companies in the process of implementing a Year 2000 corrective plan should currently deduct the cost of software corrective modifications rather than capitalizing it. The EITF minutes did not address purchases of new software to replace existing non-compliant software. Also relevant to this issue is the Internal Revenue Service Rev. Proc. 97-50, 1997-45 Internal Revenue Bulletin 1, which offers guidelines for the amortization of Y2K software corrective work, under certain circumstances, pursuant to IRS Rev. Proc. 69-21, 1969-2 CB 303 (see "<http://www.comlinks.com/itaa/itaa240.htm>").

No "Silver Bullet" Solution

Given the multitude of computer programming languages in use and the variety of business uses for date fields, computer experts have advised that no single "silver bullet" exists to correct the Year 2000 problem. In fact, over 40 vendors currently market

In excess of 125 software tools to correct the Year 2000 problem (see, e.g., the URL of "<http://www.mstnet.com/year2000/vr2000.htm>" for information about *The Year 2000 Resource Book* published by Management Support Technology, which profiles most of these vendors and their products).

Although it appears that any company can become Year 2000 compliant if it starts corrective action soon enough and devotes sufficient resources to the effort, Year 2000 experts recommend that corrective action begin as soon as possible and not be delayed until there may not be enough time left to complete the requisite reprogramming and testing. Companies may face unexpected technical delays, as where they discover that portions of their old "legacy" mainframe software have no source code documentation and the original programmers have died, retired or are otherwise no longer accessible. Companies may also face delays due to legal difficulties, as discussed in more detail below.

Many Companies Will Not Become Year 2000 Compliant in Time

According to a March, 1998 survey by Rubin Systems, Inc. of 128 IT directors and managers in major companies (the majority of which expect to spend more than \$100 million on their Y2K projects), about 78% of the 128 companies surveyed reported that their rate of missing milestones in implementing their Y2K remediation plans is increasing and 37% of the companies surveyed have already encountered a Y2K-related systems failure. Gartner Group, Inc. has estimated (with a probability of 0.7) that approximately 50% of the companies with this software problem may not become Year 2000 compliant in time and will have all or part of their computer systems shut down (or start producing incorrect data) on or after January 1, 2000. The Gartner Group estimate appears to conform with a survey conducted by Arthur Andersen in July of 1997, which predicts, based on an extrapolation of current data, that only 50% of companies will be fully compliant by the year 2000. The Y2K projects of European companies are further complicated by the additional need to implement Euro conversion projects at the same time (see, e.g., Meta Group Advisory: META Group Warns Global 2000 of Worldwide Y2K/Euro Convergence," located at the URL of "http://f2.yahoo.com/bw/971121/meta_group_1.htm"). Major software vendors such as IBM are in the process of issuing Year 2000 upgrades to existing software products (see, e.g., the URL of "<http://www.vr2k.raleigh.ibm.com>"). For major companies with heavily customized software systems, however, much of the corrective work will have to be done by the companies themselves.

TECHNICAL/LEGAL INVENTORY

Software Inventory/Data Processing Flow Chart

The first step a company should take to become Year 2000 compliant is to prepare an inventory of the hardware and software being utilized in its business. Although the Year 2000 problem is primarily a mainframe software problem, it can also exist in computer hardware (e.g., clocks in the BIOS code located on the PC (ROM)

chips), in client/server environments and in PC software (for further information on the Y2K problem in Real Time Clocks and BIOS code, see the URL of "<http://www.boq.frb.fed.us/v2k/octestlno.htm>") In addition to utilizing scanning software (which searches a networked system to locate and identify software packages on the system), the company should prepare a data processing flow chart with supporting documentation showing specific processing steps being performed by the company's computer system in order to accomplish the required business functions.

All software programs known to be owned or licensed by the company should then be identified to the flow chart in order to determine if any processing steps are revealed which have no software programs identified to them, thus revealing previously unknown, undocumented software in use. In some cases, undocumented software can enter a computer system if staff computer technicians use third party applications, tools and utilities to solve pressing processing problems and neglect to notify higher management that new software has been inserted into the system.

Some companies reportedly are foregoing the inventory step, proceeding directly to corrective Year 2000 work on their computer systems. In the final testing phase, however, this may result in the computer system refusing to test as Year 2000 compliant due to undocumented software applications, tools or utilities which have not been fully corrected. As noted below, moreover, a failure to conduct the initial inventory phase in conjunction with a legal audit may lead to problems in preserving the company's legal rights against software vendors.

Legal Audit

Once all software packages are identified, the company's general counsel and/or outside counsel should locate and review the license agreements and long-term maintenance agreements relating to all third party licensed software. The company will then be able to identify the appropriate vendor to contact in order to request information as to the availability of Year 2000 software upgrades. (See Richard Raysman and Peter Brown, "Preparing for a Y2K Compliance Audit", in the *New York Law Journal*, January 13, 1998, at pg. 3, col. 3; see also, M. Scott, "Legal Audits for Year 2000 Compliance", *Cyberspace Lawyer*, March 1998, at p. 6; see also Year 2000 upgrade informational sources such as the URL of "<http://www.auditserve.com/yr2000/yr2ktrk.html>").

It has been reported in the press that companies have begun sending letters to all of their software vendors requesting information as to when their software will become Year 2000 compliant. In some instances the software licensed has undergone a product name change during the years, or the owner/licensor of the software has changed its name or been the subject of an acquisition. In that case, a search of various computer databases such as Lexis®-Nexis® may be necessary in order to determine the correct current vendor and product name.

Potential Obligation of Maintenance Vendors to Fix Year 2000 Problems

A further purpose is served by locating the relevant license agreements and maintenance agreements for all third party licensed software. If the third party license agreement is accompanied by a long-term maintenance agreement surviving past January 1, 2000, the vendor may have an obligation to make its software Year 2000 compliant at the vendor's expense. Counsel will need to review the relevant license and maintenance agreements in this regard, but until recently, many such agreements were silent as to the Year 2000 problem.

Some vendors may disclaim liability for providing Year 2000 upgrades at no additional cost under the maintenance agreements, arguing that the Year 2000 problem was well-known in the computer industry and constitutes an "assumed risk" of the customer. The failure to at least request a vendor in writing to make its software Year 2000 compliant at its own cost under the long-term maintenance agreement may constitute a waiver by the customer of its right later to seek reimbursement for the costs it incurs in making the changes itself. It would also, in that event, deprive the customer's insurer of subrogation rights against the vendor.

Potential Obligation of Outsourcing Vendors to Fix Year 2000 Problems

Companies should also review all their data processing outsourcing agreements in order to determine if the outsourcing vendors may have an obligation to undertake the Year 2000 compliance work at their cost. It has been suggested that key provisions in the typical outsourcing agreement which may be relevant to this analysis are the sections dealing with the scope of facilities management and the size of anticipated workload.

Company counsel should also examine any provisions in the outsourcing agreement whereby the outsourcing vendor agrees as part of its fixed fee to cure any "defects", "bugs" or "viruses" found within the software programs used in processing the company's data. The "Millennium Bug" might not technically be viewed to be a virus, since a virus is typically understood to be a software program that can "infect" other programs by modifying them to include a version, possibly evolved, of itself. The Year 2000 problem might, however, be viewed to constitute a "defect" or "bug" within the program, which interferes with the program's intended operation.

The obligation for an outsourcing vendor to cure software defects in the system sometimes is found in a systems software maintenance provision in the data processing outsourcing agreement. A typical provision of that type might read essentially as follows:

"Systems Software Maintenance. As part of the Base Services, Vendor shall provide Customer with Systems Software maintenance and Systems Software production support services as described in Exhibit ____, including but not limited to (1) preventive and corrective maintenance to correct defects and failures in the Systems Software and any third party systems software, (2) installing, testing and maintaining upgrades to the Systems Software and any third party systems software and (3)

changes, enhancements and replacements of the Systems Software or additional Systems Software, as Vendor deems necessary, in order to perform the Services in accordance with the Performance Standards."

As in the case of long term maintenance providers, outsourcing vendors may strongly resist the suggestion that year 2000 corrective costs be absorbed as part of their fixed fee. Companies in this situation still may decide to make the demand of their outsourcing vendor in writing rather than waive it. The company then would proceed to correct the Year 2000 problem at its expense while expressly preserving its right at a later date to seek reimbursement of its costs from the outsourcing vendor.

Product Switches

Some software vendors may abandon hardware and/or software products rather than incur the cost of creating Year 2000 upgrades. Hardware vendors may also decide to abandon products in order to kill off a second-user market and force customers to upgrade to more expensive equipment. A careful review of the relevant agreements with the vendor will then be necessary in order to determine the vendor's legal ability to force such a product switch.

Contaminated Third Party Data

A company's computer system, even if Year 2000 compliant, may fail to process, produce error messages or generate incorrect data if the company receives contaminated programs and/or data from third party suppliers which are not Year 2000 compliant. In this respect, the Year 2000 "Millennium Bug", even though not created with malicious intent and possibly not technically constituting a "virus", may still be thought of as acting in the manner of a "virus" that can re-infect a computer system even after it has been made Year 2000 compliant.

A complete data processing flow chart of the company's computer systems would help to resolve this difficulty by identifying where third party software programs and/or data is input and processed. Companies which are vulnerable to non-Year 2000 compliant software or data from outside suppliers should (a) contact their suppliers at an early date in order to determine their suppliers' Year 2000 compliance plans and (b) monitor their suppliers' progress in actually becoming Year 2000 compliant. Company counsel should also analyze what legal recourse may be available in the form of indemnification provisions and similar provisions in the company's contracts with the suppliers which could serve to protect the company in the event the suppliers do not become Year 2000 compliant in time.

GENERAL CONTRACT ISSUES

Year 2000 Compliance Warranties

Various companies and governmental agencies have reportedly revised their standard contract forms to require that any new software proposed to be sold or licensed

to them be Year 2000 compliant. The following are a few sources for examples of Year 2000 compliance warranty language: (a) GSA Year 2000 contract language presented to the Year 2000 Interagency Committee, at the URL of "<http://www.itpollcy.gsa.gov/mks/vr2000/contlang.htm>"; (b) "Year 2000 Warranty", located at the URL of "<http://www.year2000.com/archive/NFwarranty.html>"; (c) Michael Krieger, "Drafting Tip: The Threat of 2000: Calendar Clause Protection", in the May, 1996 issue of *Cyberspace Lawyer*, Vol. 1, No.2; (d) National Institute of Standards and Technology, Department of Commerce: FIPS PUB 4-1, "Representation for Calendar Date and Ordinal Date For Information Interchange" and related Change Notice, located at the URL of "<http://www.nist.gov/itl/div879/vr2000.htm>"; (e) the ITAA definition at the URL of "<http://www.ita.org/definition.htm>", and (f) APT Data Services, "Pain or Gain in the Year 2000?", *Computer Business Review*, March 1, 1996, No. 36, vol. 4. For an adaptation of the Federal Acquisition Regulation (FAR) Y2K warranty language to a private sector contract, see Jeff Jinnett, "Legal Briefs: Y2K Contract Clause" in the December, 1997 issue of *Purchasing Today*, at p. 18. For Year 2000 compliance definitions developed outside of the U.S., organizations should review those published by the British Standards Institute (see, e.g., DISC PD2000-1, "A Definition of Year 2000 Conformity Requirements", at the URL of "<http://www.bsi.org.uk/bsi/disc/year2000/2000.html>") and the Central Computing and Telecommunications Agency (CCTA) in the United Kingdom (see, e.g., CCTA's "Tackling the year 2000", located at the URL of "http://www.open.gov.uk/ccta/mill/cct_guid.htm"). Unfortunately, there is no single, universally accepted definition of what it means to be Year 2000 compliant.

One technical problem which agencies should avoid is taking two computer systems which interface well, but are not Year 2000 compliant, and then making the two systems Year 2000 compliant by two different techniques, resulting in the two computer systems both being compliant, but no longer interfacing properly. For example, a vendor could utilize a date field expansion technique for the first system. Another vendor might correct the second system utilizing a "100 year sliding window" technique. Both computer systems are technically Year 2000 compliant in and of themselves. But since incompatible corrective techniques were used, they no longer interface with each other as they did prior to corrective action and a "bridge" will have to be developed for the two systems to be able to interface again.

The Mitre Corporation, a computer systems engineering company, has suggested that instead of warranty language mandating blanket compliancy, that agencies utilize performance standard language which could request the details as to *how* the software was made compliant (see "http://www.mitre.org:80/research/cots/Y2K_QUESTION.html"). The Mitre performance standard language could be used to augment a general Year 2000 compliancy definition such as the GTE definition (see, e.g., "GTE 2000 Proposed Criteria for 'Century Compliance'", located at the URL of "http://www.mitre.org:80/research/cots/GTE_CRITERIA.html"; see also Table 6, which identifies the various dating standards now in use in connection with different business

applications, such as with ATM cards, SQL databases and telephone systems). The Information Technology Association of America (ITAA) has also made available a model Y2K Compliance Questionnaire (see "<http://www.itaa.org/questmain.htm>".)

It should also be noted that the vendor should be required to both "represent" and "warrant" as to its product being Year 2000 compliant so that the customer is legally entitled to both equitable remedies (such as rescission of the contract) for a breach of the "representation" and remedies at law (such as money damages) for breach of the "warranty".

"Millennium Bug" as an Event of "Force Majeure"

Many contracts contain a "force majeure" clause which protects a contract party from a claim of default when it fails to perform due to an Act of God or other event beyond the party's reasonable control. It is unlikely that the Year 2000 problem involving hardware or software would be viewed as an Act of God, since it is a known problem, which can be corrected with enough planning and resources. A more difficult issue would be presented if the contract party claiming force majeure was unable to perform due to a down-stream supplier's failure to become Year 2000 compliant. Embedded micro-controllers in non-computer equipment (especially where the manufacturer has gone out of business) may also present a difficult issue. Depending on the particular language used in each force majeure clause and the facts and circumstances surrounding the failure to perform, the Year 2000 problem may be claimed to constitute an event of "force majeure" in some contract disputes. Some companies may wish to alter their standard force majeure language to rule out the Year 2000 problem specifically.

Software License/Copyright Restrictions

As the time remaining for corrective work becomes short, some companies may decide to simply provide an off-line copy of all of their computer applications, tools and utilities to a Year 2000 service provider. The service provider would then load the software onto its computer system in order to perform the Year 2000 corrective work. One legal issue which should be kept in mind is that many software licenses contain confidentiality restrictions barring the licensee from disclosing, or providing a copy of, the software to any third party without the consent of the licensor.

Even if the service provider were to copy the company's software onto an off-line computer system at the licensee's premises, the vendor may argue that the creation of this maintenance copy, despite its retention on the licensee's premises, constitutes a breach of the license agreement and an infringement of the vendor's copyright in the software program.

Further, if the Year 2000 service provider were to decompile, disassemble or otherwise reverse engineer a software application where it had been given only an

"object code" version of the software (i.e., software in a format readable only by the computer and not by a human programmer), this would also violate a related software license agreement which prohibited such reverse engineering. Although Section 117 of the U.S. Copyright Act arguably permits the *purchaser* of a copy of software to modify the copy in order to be able to correct the Year 2000 problem, a *licensee* of software who is prohibited from modifying the licensed software would be expected to honor the license restrictions. This may also present a legal issue under national laws in the European Union that implement Directive 91/250/EEC which deals with the protection of computer programs (see Council Directive of 14 May 1991 on the Legal Protection of Computer Programs, available at the URL of "<http://www2.echo.lu/legal/en/lpr/software/software.html>"). The licensee in that instance would normally contact the vendor for a Year 2000 upgrade or modification or obtain the vendor's consent to make the modification itself.

In addition, some maintenance agreements provide that warranties as to system performance automatically become void if any party other than the software maintenance vendor modifies the system. Care should be taken to avoid this result, where possible.

A difficult legal issue arises if the licensor indicates that it will issue a Year 2000 upgrade in mid-1999 and the "object code only" licensee doubts that the licensor will meet even that late deadline. It is conceivable that in cases where the licensee cannot replace the defective software, the licensee may decide to reverse engineer the software in order to obtain access to source code and modify it, taking the risk of a breach of license agreement lawsuit from the vendor, rather than the risk of not receiving a Year 2000 upgrade in time. In such a case, the licensee's breach of the agreement might appear less egregious if the licensee made the modifications itself, rather than have an unaffiliated third party service provider make the modifications.

In light of the above issues, service providers offering Year 2000 corrective services may attempt to provide their services on an "as is" basis and may require indemnifications from their customers against third party licensor suits for infringement.

Export Restrictions on Encryption Software

Companies may decide to retain the services of an overseas Year 2000 service provider, such as a programming facility in India, the Philippines or South Africa, in order to obtain the services of less expensive programmers. Also, programmers experienced in COBOL ("COmmon Business Oriented Language") and other relevant programming languages may become scarce in the next few years as their services are booked up for Year 2000 corrective work by individual companies and Year 2000 service providers. Companies starting their Year 2000 corrective work late may be forced to retain programmers outside the U.S. in order to gain access to the quantity of personnel needed.

In that event, the company should be careful to examine any cryptographic software applications in its software system portfolio prior to export. Encrypted applications might include wire transfer systems, communications systems or any other software application where the processed data is encrypted to make it secure. (For additional information on cryptography and encryption software, see "RSA's FAQ 4.0 on Today's Cryptography", at the URL of "<http://www.rsa.com/rsalabs/newfaq>").

Under the Arms Export Control Act, certain encryption software is listed on a U.S. Munitions List and is prohibited from being exported. The prohibition is enforced by the Office of Defense Trade Controls ("DTC") in the U.S. Department of State pursuant to its International Traffic in Arms Regulations ("ITAR"). Under certain circumstances, the DTC may decide pursuant to a "commodity jurisdiction" procedure that the software proposed to be exported has both a commercial and military potential use and is governed by the less restrictive Export Administration Regulations ("EAR"). The exporting company then may apply for a license to export the encryption software from the U.S. Department of Commerce. If jurisdiction remains with the State Department, however, the export request might also have to be reviewed and approved by the National Security Agency. Certain low-strength encryption software has recently been transferred by Executive Order from the U.S. Munitions List to the Commerce Control List (see, generally, John R. Liebman and Kristen Green, "Encryption Software Export Regulations and Free Speech," *Los Angeles Lawyer*, October, 1997 issue, at p. 21.)

Due Diligence on Acquisitions

In connection with all due diligence investigations of target companies, the acquiring company should investigate the target company's Year 2000 compliance status. Some companies may decide to sell divisions or subsidiaries before the Year 2000, because it would cost more to make the division or subsidiary Year 2000 compliant than its net revenues justified. The acquiring company should make this same analysis and either reserve the right to adjust the purchase price to reflect this Year 2000 compliance cost or reserve the right to "walk" in the event the acquiring company's post-due diligence estimate of the Year 2000 compliance cost exceeds a pre-agreed minimum (for an article discussing the potential impact of Y2K on mergers and acquisitions activity for 1998 and 1999, see William Lewis, "Millennium Threat to Takeovers").

In addition, lenders will likely begin to include Y2K-related questions as part of their normal lending due diligence questionnaires given to borrowers (see, e.g., Brad Peterson and John Brockland, "Negotiating Year 2000 Provisions in Finance Transactions", In *Understanding, Preventing and Litigating Year 2000 Issues: What Every Lawyer Needs to Know Now* (PLI No. 506 and Supplement No. 521). Loan documents may also be amended to include Y2K-related representations and covenants, such as the following:

"Year 2000 Compatibility. The Borrower shall take all actions reasonably necessary to assure that Borrower's computer based systems are able to operate and

effectively process data which includes dates on and after January 1, 2000. At the request of the Lead Agents, the Borrower shall provide reasonable assurances satisfactory to the Lead Agents of the Borrower's Year 2000 compatibility." (See Exhibit 4 to Quarterly Filing on Form 10-Q of LCI International, Inc., filed on November 14, 1997).

DISCLOSURE ISSUES

The Wall Street Journal, in an article entitled "The Year 2000 and the CEOs' Big Secret", reported that companies with significant Year 2000 problems were reluctant to talk about the magnitude of their Year 2000 corrective work, for fear of providing damaging information to future plaintiffs in the event the Year 2000 problems were not corrected in time. As is discussed in more detail below, companies may not be able to safely hide their Year 2000 problems, because disclosure may be required under various accounting standards, securities laws and bank examination policies.

Accounting Standards Which May Mandate Disclosure

The guiding principles for the *preparation* by a company of its financial statements are "generally accepted accounting principles" ("GAAP"). These standards are promulgated by FASB and the American Institute of Certified Public Accountants ("AICPA"). One of the GAAP principles promulgated by FASB is Statement of Financial Accounting Standards No. 5 ("SFAS 5") ("Accounting for Contingencies"), which provides that contingencies which are reasonably possible, whether or not the amount can be calculated or estimated, must be disclosed in a note to the financial statements.

Statement of Financial Auditing Standards

SFAS 5 defines a "contingency" as an existing condition, situation, or set of circumstances involving uncertainty as to possible gain or loss to an enterprise that will ultimately be resolved when one or more future events occur or fail to occur. SFAS 5 uses three classifications:

- (A) Probable—the future contingent event is likely to occur.
- (B) Remote—there is only a slight chance that the future event will occur.
- (C) Reasonably possible—the chance of the event occurring is more than remote, but less than probable.

SFAS 5 gives as an example of a "loss contingency" the "risk of loss or damage to enterprise property by fire, explosion or other hazards", which definition arguably could include the crippling of an enterprise's computer system by the "Millennium Bug". If it is reasonably possible that the company will not become Year 2000 compliant in time, SFAS 5 appears to require the company to disclose this fact in a note to the audited financials.

Moreover, if (a) it is "probable" that the company will not become Year 2000 compliant in time, (b) an asset has been impaired or a liability incurred as of the date of the financial statements, and (c) the amount of the loss can be reasonably estimated,

then a charge against earnings for the estimated loss may be required under SFAS 5 and the liability would be reported in the body of the financial statements.

Statements on Auditing Standards

At some time prior to January 1, 2000, a company's independent public accountants ("auditors") may feel obliged in their audit of the company's financial statements to examine the likelihood of the company's failing to become Year 2000 compliant in time. Auditors may wish to document their assessment of the Year 2000 disclosures by their clients in order to show compliance with applicable Statements on Auditing Standards ("SAS"), promulgated pursuant to the AICPA's Generally Accepted Auditing Standards ("GAAS"), the guiding standards for the *audit* of financial statements.

SAS No. 53 ("The Auditor's Responsibilities to Detect and Report Errors and Irregularities") imposes on auditors the duty to plan each audit to provide reasonable assurance of detecting "errors", defined as unintentional misstatements and omissions, and "irregularities", defined as intentionally false or misleading statements, that reach a "financial statement" level of materiality. SAS No. 59 ("The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern"), which relates to a company's ability to remain a going concern for a "reasonable period" not to exceed one year, may also force the auditor (commencing in 1999) to consider the effect on the company of a failure to become Year 2000 compliant.

The auditors therefore may be obligated, in order to demonstrate compliance with SAS Nos. 53 and 59, to review the company's Year 2000 compliance plan and the status of its implementation. Other Statements of Auditing Standards, such as SAS No. 54 ("Illegal Acts By Clients"), may also raise significant issues with respect to the impact of a failure to become Year 2000 compliant on a company's financial reporting.

Pressure to Disclose Due to Potential Securities Law Liability of Auditors

An auditor is considered to be an "expert" under Section 11(b) of the Securities Act of 1933 ("1933 Act") for purposes of the financial statements reported on by the auditor and included, together with the auditor's opinion, as the "expertised" portion of the issuer's registration statement in connection with the sale of securities. As is discussed in more detail below, auditors have securities law liability for material misstatements or omissions in the company's financial statements.

In particular, auditors are held to a higher obligation to exercise "due diligence" with respect to their portion of the registration statement than non-experts, such as the issuer and the underwriter, are held to with respect to the entire registration statement. With respect to the "expertised" financial statement portion of the registration statement, the issuer and underwriter are not required to have made an investigation but must establish that they had no reasonable grounds to believe and did not believe that there was a material misrepresentation or omission in the "expertised" financial statement portion.

As a result of the auditors' higher "due diligence" obligation (and in light of the potentially disastrous impact on a company's business operations if it failed to become Year 2000 compliant in time), auditors are likely to become more cautious in the next few years in dealing with a company's Year 2000 compliance problem in the course of auditing the company's financial statements.

Disclosure in Auditors' Opinions

In a standard unqualified opinion, the auditors would typically state, among other things, that (1) the financial statements are the responsibility of the company's management, (2) the auditors' responsibility is to express an opinion on these financial statements based on their audit, which audit was conducted in accordance with GAAS, (3) GAAS requires the auditors to plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, and (4) in the auditors' opinion, the financial statements present fairly, in all material respects, the financial position of the company as of a particular date, and the results of its operations and its cash flows for the year then ended in conformity with GAAP.

If a note were added to the company's financial statements concerning the Year 2000 problem and the auditors were to decide that a departure from the standard unqualified opinion is required due to uncertainty concerning the company's Year 2000 problem, the auditors might add an additional explanatory paragraph to their standard unqualified opinion reading something like the following:

"As discussed in Note ___ to the financial statements, a material portion of the Company's hardware and software computer system used in the conduct of its operations requires correction with respect to the so-called "Year 2000" problem, as is more fully described in Note ___. The Company has adopted a Year 2000 corrective plan and is in the process of implementing that corrective plan. The ultimate success or failure of the corrective plan and the extent of such success or failure cannot presently be determined. Accordingly, no provision for any liability that may result from the failure of the Company to implement fully its Year 2000 corrective plan has been made in the accompanying financial statements."

If the financial statements were to fail to include a note with respect to the Year 2000 problem and the potential liability arising with respect to the problem, despite the auditors' recommendation to the company that such a note be added, the auditors may decide to issue a qualified opinion which states that the financial statements present fairly, in all material respects, the financial position of the company, "with the exception of" the effects of the Year 2000 matter, as described in an explanatory paragraph preceding the opinion paragraph of the report. Highly recommended in this regard as further reading is the AICPA report entitled "The Year 2000 Issue-- Current Accounting and Auditing Guidance", issued on October 31, 1997 (see ["http://www.aicpa.org/members/v2000/intro.htm"](http://www.aicpa.org/members/v2000/intro.htm).)

Securities Laws Which May Mandate Disclosure

Public companies are required to file an annual report on Form 10-K and quarterly reports on Form 10-Q with the U.S. Securities and Exchange Commission ("SEC"). Pursuant to Reg. S-K, Item 303, each such annual report and quarterly report must include a section entitled "Management's Discussion and Analysis of Financial Condition and Results of Operations" ("MD&A"). Instruction 3 to Item 303(a) provides that:

"The discussion and analysis shall focus specifically on material events and uncertainties known to management that would cause reported financial information not to be necessarily indicative of future operating results or of future financial condition. This would include descriptions and amounts of (A) matters that would have an impact on future operations and have not had an impact in the past, and (B) matters that have had an impact on reported operations and are not expected to have an impact upon future operations."

On May 12, 1997, the SEC issued a statement as part of a "Current Issues and Rulemaking Projects" release concerning the potential obligation of public companies to disclose information in their annual reports and quarterly reports about their year 2000 problems. Any public company which knows that the costs of addressing its Year 2000 problem or the consequences of incomplete or untimely resolution of the problem represents a known material event or uncertainty that would affect future financial results, or cause reported financial information not to be necessarily indicative of future operating results on future financial condition, is required to disclose this event and uncertainty in the MD&A section of its annual report and quarterly reports.

Illustrative of this is the SEC's Securities Act Release No. 6385, implemented in Financial Reporting Release No. 36 (May 18, 1989), which provides that a disclosure duty exists when "a[n]... uncertainty is both presently known to management and reasonably likely to have material effects on the registrant's financial condition or results of operations." Essentially, disclosure would be required in the MD&A unless management decided that "a material effect on the registrant's financial condition or results of operations is not reasonably likely to occur." This current obligation to make disclosure under existing laws was made even more clear by the issuance on October 8, 1997 of SEC Staff Legal Bulletin No. 5, as updated on January 12, 1998 (see "<http://www.sec.gov/rules/other/slbcf5.htm>"), which itself was superseded by the SEC "Disclosure of Year 2000 Issues and Consequences by Public Companies, Investment Advisers, Investment Companies, and Municipal Securities Issuers", an interpretative release located at "<http://www.sec.gov/rules/concept/33-7558.htm>"; see also, Prepared Testimony of SEC Commissioner Laura Unger before the Senate Banking, Housing and Urban Affairs Committee, Subcommittee on Financial Services and Technology, June 10, 1998, located at the URL of "http://www.senate.gov/~banking/98_06hra/061098/witness/unger.htm"; see also, E. Brodsky, "Y2K Disclosure: Safeguard Against Liability or Smoking Gun?", *New York L. J.*, September 9, 1998 at p. 3).

The SEC interpretative release provides "specific disclosure guidance" to public companies as to what must be disclosed, for example, in the companies' Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A"). The SEC indicated in its release that a company has an obligation to address Y2K preparedness in its MD&A if (a) its assessment of its Y2K readiness is not complete, or (b) the company's management determines that the Year 2000 problem would have a material effect on the company's business, results of operations, or financial condition, without accounting for efforts to avoid Y2K-related consequences. Given this standard, most reporting companies are likely to have to make the disclosures required by the SEC release. (see, e.g., S. Radin, "SEC Details Disclosure Requirements for Year 2000 Consequences", *New York L. J.*, August 11, 1998, at p. 1, col. 2). The SEC has also amended Rule 17a-5 to require certain broker-dealers to file Y2K compliancy reports on Form BD-Y2K. A companion rule was amended to require similar reports from certain transfer agents.

Potential Liability of Officers and Directors of a Public Company Which Fails to Disclose a Year 2000 Problem and Then Fails to Become Year 2000 Compliant In Time

As noted above, under certain circumstances, a public company would be required to disclose its Year 2000 problem in the MD&A section of its annual report, quarterly reports and in the company's financial statements. If the company were to fail to disclose a Year 2000 problem when required to do so, the securities law consequences could be significant.

The annual report is often incorporated by reference into a company's registration statement pursuant to the SEC's "Integrated Disclosure System", for purposes of registering stock for issuance to the public. Section 6(a) of the 1933 Act requires that every registration statement (which includes the prospectus) be signed by the issuing corporation's principal executive officers and financial officers, its principal accounting officer and a majority of the board of directors.

Section 11(a) of the 1933 Act makes every signatory to the *registration statement* (and every director of the issuer, whether a signatory or not) liable for material misstatements and omissions to any person who acquires securities issued under it. Underwriters, auditors and lawyers involved in the issuer's stock offering may also be held liable under Section 11. Evidence of "due diligence", however, can provide a defense against a Section 11 action. (See, e.g., Rule 176 ("Reasonable Investigation and Reasonable Grounds for Belief Under Section 11"), promulgated by the SEC under Securities Act Release No. 6335).

Further, under Section 12(2) of the 1933 Act, an issuer may be held liable to a shareholder in a private action for any untrue statement in a *prospectus* of a material fact or failure to state a material fact necessary to make the statements made in the

prospectus not misleading. Section 12(2) applies to any public offer or sale of a security (*whether registered or not*) "by means of a prospectus or oral communication". The issuer is afforded a "due diligence" defense if it "did not know, and in the exercise of reasonable care could not have known" of the falsity.

In addition, Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act"), as interpreted by Rule 10b-5 of the SEC, essentially makes it unlawful for any person (which may include the issuer, underwriter, auditors and attorneys) to sell any security in interstate commerce while employing a "manipulative or deceptive device", which term includes making any untrue statement or omitting any statement of a material fact.

A private action by a purchaser under Section 10(b) and Rule 10b-5 must allege a material and false representation or omission by the issuer in connection with the purchase and sale of securities, the use of means and instrumentalities of interstate commerce, scienter (intent to deceive, manipulate or defraud, or in certain cases, recklessness), reliance by plaintiff and damages suffered by plaintiff. A private action under Section 11 of the 1933 Act need not allege intent to deceive.

The SEC itself may institute enforcement actions with respect to registration statements which contain material and false representations or omissions under Section 17(a) of the 1933 Act (which covers any fraudulent scheme in an offer or sale of securities, whether in the course of an initial distribution or in the course of ordinary market trading) and under Rule 10b-5 under the Exchange Act. Section 24 of the 1933 Act provides for criminal penalties for securities law violations.

Purchasers of securities may also avail themselves of the protection afforded by the disclosure and liability provisions of the securities laws ("Blue Sky" laws) enacted by the various states.

Standards of Care of a Director

The laws of the state of a company's incorporation typically impose standards of care on the company's directors, which could be breached if the directors are grossly negligent in dealing with the Year 2000 problem, resulting in potential personal liability for the directors. The Model Business Corporation Act (Section 8.30(a)), adopted by some of the states, defines the director's duty of care as the duty to act in good faith with the care an ordinarily prudent person in a like position would exercise under similar circumstances and in a manner the director reasonably believes to be in the best interests of the company.

Some states, like Delaware, have not codified the duty of care, but Delaware courts have held that directors should act with the care of an ordinary prudent person. Some state due care codifications add a requirement that the director use "reasonable

inquiry". Section 309(a) of the California Corporation Code sets forth an example of such a provision, providing that:

"A director shall perform the duties of a director, including duties as a member of any committee of the board upon which the director may serve, in good faith, in a manner such director believes to be in the best interests of the corporation and its shareholders and with such care, including reasonable inquiry, as an ordinarily prudent person in a like position would use under similar circumstances."

Shareholder Suits

If a public company fails to adequately disclose its Year 2000 problem in its annual report on Form 10-K, quarterly reports on Form 10-Q and in its registration statements and subsequently has to substantially curtail or shut down its business on or after January 1, 2000 due to the problem, produces incorrect data commencing on that date, or otherwise experiences substantial operational difficulties, resulting in damage to its business, the company's stock price is likely to drop. Shareholder suits based on one or more of the above federal and/or state securities laws are likely to follow. Civil and/or criminal enforcement action by federal and/or state securities authorities might also occur.

In addition, irrespective of whether adequate disclosure of the Year 2000 problem was made or not, in the event a public or private company fails to become Year 2000 compliant in time, the shareholders may institute individual suits, or derivative suits in the name of the company, against the directors alleging breach of their duty of care under state law.

Documentation of Year 2000 Compliance Program to Establish Due Diligence Defense and Protection Under the Business Judgment Rule

Directors are permitted to rely on the reports of the company's officers, counsel and third party experts in the course of making corporate decisions. In the event a company's board of directors adopted a Year 2000 corrective plan, but the company unexpectedly failed to become Year 2000 compliant in time and the directors were sued by the company's shareholders, the directors would likely find it useful to be able to produce detailed documentation as to the company's Year 2000 corrective plan and the diligence with which it was pursued.

The "Business Judgment Rule" essentially protects directors from court review and liability for an honest mistake of business judgment, so long as the challenged board decision was intended to serve the business purposes of the corporation and did not involve fraud, illegality or conflict of interest. The exact formulation of the Business Judgment Rule varies from state to state and some courts require the directors to show that they performed appropriate "due diligence" in informing themselves of the merits of the business issue before reaching a decision.