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McCullough Research Finds Flaws in ERCOT Nodal Cost-Benefit Study
Issued on December 18, 2008

January 7, Portland, Oregon – Reviewing a study issued on December 18, 2008 that concluded that the benefits of continuing ERCOT’s shift to nodal markets from the existing four-zone system significantly outweighed the costs uncovered problems with its accuracy and craftsmanship, according to Robert McCullough, Managing Partner of McCullough Research, who undertook the review.

McCullough notes, “These problems appear significant enough that the conclusions of the study are effectively speculative. In addition, the study is poorly documented and depends on a number of unusual assumptions.” McCullough finds that:

1. The study has only modeled two years of the ten year period under analysis. This failing affects both the estimate of production costs and consumer benefits. The current modeling ends before the year when the 2004 model appeared to have significant problems.
2. The authors have not verified their methodology by doing a backcast. In the absence of a backcast, the results cannot be depended upon to even remotely reproduce conditions in ERCOT markets.
3. Several assumptions are highly questionable. The study assumes marginal cost bidding by market participants even though this is not present in ERCOT. In addition, the study uses a natural gas forecast from a year ago, a curious choice in such volatile times. Other assumptions are undocumented or simply copied from a study four years out of date – the discount rate, for example.
4. The costs of the additional computer programming appear high – very high – and the assumptions appear inconsistent. The high maintenance costs assumed for the existing operational zonal model appear to be just a fraction of the assumed maintenance costs of the new, unfinished and vastly more complex, nodal model.

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