

**UNITED STATES OF AMERICA
BEFORE THE FEDERAL ENERGY REGULATORY COMMISSION**

**Centralized Capacity Markets in
Regional Transmission Organizations and
Independent System Operators**

Docket No. AD13-7-000

**Comments of AARP, Public Citizen and the National Consumer Law Center, On Behalf Of Its
Low-Income Clients**

On September 25, 2013, the Federal Energy Regulatory Commission (“Commission”) conducted a technical conference regarding the private capacity markets of the ISO New England Inc. (ISO-NE), New York Independent System Operator, Inc. (NYISO), and PJM Interconnection, L.L.C. (PJM). On October 25, 2013 the Commission issued a *Notice Allowing Post-Technical Conference Comments (Notice)* inviting all interested persons to file post conference comments on any or all of the questions listed in an attachment. The questions are grouped under the following categories:

1. Role of Capacity Markets and Definition of the Capacity Product
2. Accommodating state policies and self-supply by load serving entities
3. Market Design Elements
4. Regulatory certainty
5. Next Steps

AARP, Public Citizen and the National Consumer Law Center, on behalf of its low-income clients, (Consumer Groups) respectfully submit these comments in response to the *Notice*.

Interest of AARP

AARP, a nonprofit organization, helps people over the age of 50 to exercise independence, choice, and control in ways beneficial to them and to society as a whole. Millions of AARP

members reside in the regions served by the PJM RTO, ISO-NE, and NYISO (“RTO/ISOs”). AARP members, many of whom live on low or fixed retirement incomes, need affordable, reliable electric service provided at least cost by retail utilities in accordance with state-established economic and environmental policies, such as energy efficiency and development of additional renewable power generation resources.

Interest of Public Citizen

Formed in 1971, Public Citizen has 250,000 members and supporters across the United States. Our members are households directly impacted by FERC regulations over electric power markets.

Interest of National Consumer Law Center (NCLC)

NCLC is a non-profit corporation founded in 1969 to assist legal services, consumer law attorneys, consumer advocates and public policy makers. NCLC has expertise in protecting low-income customer access to essential energy service through bill assistance and energy efficiency programs as well as traditional consumer protections such as disconnection protections. The pass-through of wholesale energy costs on residential consumer bills affects the overall affordability of essential energy services for low-income households. NCLC publishes *Access to Utility Service* (5th edition) as part of its Debtor Rights Series of legal manuals as well as NCLC’s *Guide to the Rights of Utility Consumers* and *Guide to Surviving Debt*.

Introduction

Many of the investor owned retail distribution utilities in the regions under scrutiny in this case restructured and divested most if not all of their power plants. As a consequence, they often

lack capacity resources of their own to meet the current and future needs of their retail electricity customers and reserve requirements for reliability purposes.¹ They are thus very dependent upon FERC jurisdictional wholesale purchases, the cost of which is flowed through to retail consumers, including AARP members and low-income households that are face dire choices in order to afford essential energy services.² Also, the publicly owned and cooperative utilities in the regions purchase a significant portion of their electricity in wholesale transactions.³ Prices paid by consumers in the regions under scrutiny are among the nation's highest.⁴ For the millions of AARP members and low-income households in these regions who are currently struggling to pay for essential energy services, it is critical for FERC to assure that all charges for wholesale electric services, including capacity, be just and reasonable.

AARP and Public Citizen have participated in other matters involving alleged gaming or manipulation of wholesale electricity spot markets out of concern that its members can be

¹ “Under traditional utility regulation, resource adequacy is met by load-serving entities obtaining regulatory approval to hold a portfolio of resources, the costs of which (including a reasonable return on investment) are recovered from captive customers. In areas of the country that have restructured their electricity markets, many load-serving entities compete for retail customers with other suppliers, creating financial risk for long-term resource commitments, and in many cases have divested generation to new owners that compete for sales and thus have no guarantee of cost recovery.” *Centralized Capacity Market Design Elements*, Commission Staff Report in Case AD13-7, Aug. 23, 2013, at 1.

² E.g., National Energy Assistance Directors' Association, *2011 National Energy Assistance Survey* (Nov. 2011)(to pay energy bills, 24% of Low Income Home Energy Assistance Program recipients went without food, 37% went without medical or dental care, 34% did not fill or took less than the full dose of a prescribed medication), available at neada.org/wp-content/uploads/2013/05/NEA_Survey_Nov11.pdf.

³ For example, in New York State, the publicly owned Long Island Power Authority has approximately 1.1 million customers, and there are numerous smaller municipally owned and cooperative electric utilities in the three RTO/ISO regions.

⁴ For example, even though it has significant hydro and other low cost resources, prices paid by New York electricity consumers were 19.57 cents/kwh in September 2013, second only to Hawaii. Table 5.6.A, *Average Retail Price of Electric Service to Ultimate Customers by End Use Sector, By State, September 2013 and 2012*, EIA, Electric Power Monthly with Data for September, 2013 (November 2013), available at <http://www.eia.gov/electricity/monthly/pdf/epm.pdf>.

harmed by market malfunction and left without adequate remedies.⁵ Important issues have now prompt reassessment of the function, design and operation of ISO/RTO spot capacity markets. Consumer Groups commend FERC for undertaking a review of the functions of the capacity markets operated by ISO-NE, NYISO, and PJM in this proceeding, and welcome the opportunity to participate and comment on behalf of vulnerable, fixed-income and low-income residential consumers.

Consumer Groups will not address each issue on which the Commission has solicited comments, and will instead focus on the role of the capacity markets, and the preservation of prerogatives of utilities and states to address future capacity needs consistent with least cost principles and state economic and environmental policy choices.

Summary of Comments

The Commission has authorized the private setting of wholesale electricity prices in capacity spot markets established by the three RTO/ISO utilities under review. There is a lack of consensus regarding the roles and design of capacity markets, and there is widespread concern that they are not functioning optimally. Any purchase or sale transactions in these markets by retail load-serving utilities should be voluntary and not mandatory. Utilities should retain the traditional range of options for satisfying their capacity needs, including self-supply (where permitted by state law) and bilateral contracting with various providers outside the RTO/ISO markets.

⁵ E.g., *Constellation Energy Commodities Group, Inc.*, FERC No. IN12-7 (energy market gaming). See *United States v. Morgan Stanley*, 881 F.Supp.2d 563 (2012) and *United States v. Keyspan*, 763 F.Supp.2d 633 (2011) (capacity market gaming). See Paul B. Mohler, *Has the “Complete and Permanent Bond of Protection” Provided by FERC Refunds Eroded in the Transition to Market-Based Rates?*, 33 Energy Law Journal 41 (2012).

Undue reliance on the RTO/ISO markets to establish rates for electric capacity would pose undue risk for fixed-income and low-income consumers who struggle to afford essential energy services.⁶ There are many practical reasons why retail utilities use a portfolio of resources to satisfy their obligations to have enough capacity to meet peak load and reserve requirements. Consumer Groups are concerned that measures under consideration could frustrate legitimate state and retail utility efforts to secure capacity at least cost through traditional avenues, including utility self-supply and bilateral contracts. These options should be continued and fostered by Commission policy. Also, the private spot markets for capacity should not be allowed by FERC to frustrate state options to develop new generation resources consistent with state economic and environmental policies.

Consumer Groups also raise additional steps to improve RTO responsiveness and accountability to household consumers. The establishment of permanent funding for the consumer advocate offices at all the RTOs and ISOs is a significant step towards that responsiveness and accountability. The Commission has allocated limited funding for such offices in both PJM and NYISO arising from market manipulation settlements. The establishment of an office of consumer advocate at the Commission is also needed to ensure household consumer interests

⁶ E.g., National Energy Assistance Directors' Association, *2011 National Energy Assistance Survey* (Nov. 2011); Lynne Page Snyder and Christopher Baker, AARP Public Policy Institute, *Affordable Home Energy and Health: Making the Connections* (June 2015) (discusses adverse health impacts from unaffordable home energy on the health and well-being of older people in low- and moderate-income households) available at <http://www.aarp.org/money/low-income-assistance/info-06-2010/2010-05-consumer.html>; See also, LIHEAP Home Energy Notebook for FY 2009, US HHS, Administration for Children and Families (Sept. 2011) at Tables A-3b and A-4 (low-income and LIHEAP households in the Northeast who heat with electricity pay 12.9% to 17.2% of their income on energy compared to non low-income households who pay 3% of their income on energy), available at <http://www.acf.hhs.gov/programs/ocs/resource/liheap-2009-home-energy-notebook>.

are always represented at the Commission. Consumer advocacy organizations do not have the resources to fill this important need. Finally, Consumer Groups recommend reforming the voting allocations at RTOs/ISOs so that all end-users (residential, commercial and industrial) hold at least half of the voting shares to be on equal footing with the utilities and power providers.

Item 1. Role of Capacity Markets and Definition of the Capacity Product

What is the role(s) of centralized capacity markets? Should the centralized capacity markets function as a mandatory market for procuring capacity or a residual market that entities only need to use to meet their resource adequacy obligations that they cannot otherwise meet through self-supply?

Consumer Group Response: The RTO/ISO capacity markets cannot be mandatory for procurement of all capacity. Capacity markets of the RTO/ISOs are a residual source when retail utilities do not obtain all their requirements through self-supply or bilateral contracts.

Today, PJM, NE-ISO and NYISO operate capacity spot markets under tariffs approved by the Commission. Not every state or region has them, and the three markets under review are not identical. They trace their origins to contractual arrangements among utilities in the power pools that preceded the advent of RTO/ISOs:

Early on, the eastern RTOs/ISOs, like the power pools that preceded them, employed rules requiring load-serving entities to maintain adequate capacity resources to meet the planning reserve margin, coupled with a deficiency charge assessed to members who failed to meet their capacity requirements. The original capacity market designs were voluntary balancing markets intended to provide transparent market-based mechanisms to assist load-serving entities in meeting their installed capacity obligations. These market constructs generally

procured capacity on a daily or monthly basis with a short lead time and relied on deficiency charges to set market prices.⁷

Capacity markets are primarily seen as a “mechanism supporting the procurement and retention of resources necessary to meet future reliability and operational needs.”⁸ The divestiture of power generating plants from many of the formerly vertically integrated utilities to the merchant power sector, and the emergence of new retail providers who must buy capacity to serve fluctuating numbers of their customers who might switch on short notice to other providers added to the desire for a system in which short term capacity could be readily bought and sold. Indeed, the advent of retail commodity suppliers may have weakened the interest of some traditional distribution utilities in securing long term capacity, since long term contract purchase commitments might be stranded if their customers migrate away to other retail energy suppliers.⁹

A high capacity price is thought by some to send signals that new resources are required, while a low price may discourage new building or encourage power plant retirement or mothballing. In fact, however, there is little or no evidence that decisions to build power plants are made based on price signals from the short term capacity markets. Rather, decisions to build new resources typically require financial commitments far beyond the short horizons of the capacity markets:

⁷ *Centralized Capacity Market Design Elements*, Commission Staff Report in Case AD13-7, Aug. 23, 2013, at 1.

⁸ *Id.*

⁹ An interesting solution to this problem is for the distribution utilities to maintain the obligation to secure capacity for all customers as a bottleneck service, even if commodity energy is supplied by other retail providers. See Comments of Cliff Hamal, Navigant Economics, filed December 18, 2013.

The centralized capacity markets should be understood as spot capacity markets because while new capacity is typically built in units with 20 year useful lives (in the case of power plants), the capacity markets offer only one-year commitments. Holding the spot capacity auctions years forward does not change the fact that one-year capacity transactions are best understood as spot capacity transactions.¹⁰

Capacity markets are also thought to inform buyers and sellers of the value of capacity when they negotiate long term bilateral contracts:

When there is a new unit, prices drop for a few years. When a unit retires, the prices go back up. This is a price signal that the market gives, and units come in and retire based on these price signals. ... However, the fact that you can have bilateral contracts, we expect generators to have bilateral contracts to get the financing in. But these prices inform the market and inform the prices of these bilateral contracts.¹¹

From the point of view of some, the capacity market model is seen as the complement to the energy spot market model to assure full recovery of costs and a return on investment. It is postulated as the only source for so-called “missing money” that is not received in the energy spot market model.¹² This hypothetical construct was explained at the conference by the NYISO market monitor as follows:

On slide 1, we talk about missing money. You hear about missing money a lot. The three sources of revenues that a private investor...is going to look at to decide whether to invest, is the net revenue from the energy market during shortages, the net revenue during non- shortages -- which tends to be relatively low except for base load units -- and capacity market revenues. Some combination of those three revenue streams has to produce enough revenue for an investment to break even, if you want the private investor to invest. *So you're basically making choices when you design these markets, of how much of the*

¹⁰ Technical Conference Comments of James F. Wilson, p. 4.

¹¹ Mukerji, NYISO, Transcript at 32.

¹² Under the model, winning bids in the energy markets would clear at or only slightly above the marginal cost of production of the last unit called to run, and would not provide a return on the capital investment for the marginal unit.

*revenue is going to be in the capacity market, and how much of the revenue is going to be in the energy market.*¹³

Consumer Groups do not agree with this construct. First, it omits consideration that substantial revenue above operating costs can be recovered in the energy market for many generating units which operate at costs below the clearing price set by a more expensive marginal unit. This will yield at least some inframarginal energy market revenues to the more efficient providers. For example, if operating costs of a plant are 3 cents/kwh and the clearing price is 7 cents/kwh, 4 cents/kwh is potentially available to defray sunken capital costs and possibly provide a return on investment. Second, the “missing money” scenario also assumes revenue can only be obtained in the ISO/RTO energy and capacity spot markets. Added revenue can come from bilateral contracts, in addition to the energy and capacity spot markets.¹⁴ Revenues from long term bilateral contracts can be negotiated so that, over time, the seller’s fixed and operating costs are recovered and a reasonable return on investment is achieved. In sum, it is wrong to assume that a power producer can only sell in the energy and capacity spot markets or that prices in those markets must be propped up to pay all sellers what it costs to guarantee full recovery of cost and a return on investment for the least efficient and most expensive seller.

¹³ Patton, Transcript at 55 – 56. (*Emphasis added*).

¹⁴ The PJM Market Monitor state that “[c]apacity markets are in place to address what’s called the net revenue issue or the missing money issue. That can actually be addressed using a number of mechanisms. It can and was addressed using cost of service regulation. *It could be addressed through bilateral contracts, as it is in some areas.* It can be addressed through simply letting people exercise market power. It can be addressed through administrative scarcity pricing, and finally it can be addressed through capacity markets.” Bowering, Transcript at 46. (*Emphasis added*).

The request for comments suggests that capacity sales and purchases be completely centralized, so as to effectively mandate buyers to procure all capacity through the RTO/ISOs, or to require a floor price set administratively by the ISO/RTOs for all capacity. There are numerous reasons why the Commission should not attempt to require all capacity to be sold or purchased exclusively in such a “centralized” spot market or at its prices.

First, retail utilities in the three regions may already have some capacity resources, i.e., power plants they own. Self-supply can meet or defray their obligations to have enough capacity to meet demand and reserve requirements at times of their customers’ peak usage. Self-supply is still a significant option, notwithstanding the divestiture that has occurred. In the three RTO/ISO regions, in addition to merchant power plants, power plants are also owned by publicly owned utilities, cooperative utilities, and investor utilities that divested some but not all of their generating plants.¹⁵ It would make no sense to mandate these utilities to buy all their capacity from the market, or force them to sell their own capacity into the market, when they already possess it. Utilities should retain the ability to build their own capacity in an effort to reduce the costs of purchased capacity or to avoid the risk of high or aberrant pricing in capacity markets or to meet state requirements and goals regarding certain types of energy.¹⁶

As raised throughout these comments, fixed-income and low-income households face constant

¹⁵ For example, Consolidated Edison Company of New York, Inc.’s East River Repowering Project is a 288 MW combined electricity and steam plant which became operational in 2005. Also, Rochester Gas & Electric (Iberdrola) owns and operates three hydro generation plants with 57.5 MW capacity.

¹⁶ “They’re trying to get up to the point where they’re basically resource self-sufficient if at all possible, because of what they see has gone on in these markets since their inception.” Kelly, T. 271.

challenges in paying for essential energy¹⁷ and this is why the Commission must ensure that rate are just and reasonable.

Second, retail utilities in the three regions have long term contracts for the purchase of energy and capacity.¹⁸ Again, there is no reason to require retail utilities to buy capacity in the market (or offer capacity they have bought into the market), or breach or modify their contracts, when they already have contracted for the resource. Indeed, if existing capacity contracts are properly filed, there can be no other rate, and “not even a court can authorize commerce in the [electric] commodity on other terms.” *Montana-Dakota Co. v. Northwestern Pub. Serv. Co.*, 341 U.S. 246, 251-252 (1951).¹⁹ Accordingly, bilaterally negotiated long term capacity contracts are a proper part of a retail utility’s portfolio.

Third, retail utilities may have internal or state mandated goals to obtain capacity resources from particular types of sources, e.g., renewable resources. The capacity markets of the three regions do not now differentiate among resource types. “All cleared resources receive the

¹⁷ For example, the reach of the Low Income Home Energy Assistance Program (LIHEAP), the federal bill payment assistance program has been shrinking due to funding cuts; the total number of low-income households receiving assistance has declined by 17% between FY 2010 and FY 2013. See, *Sequester Cuts 300,000 Poor Families from Low Income Home Energy Assistance Program*, available at <http://neada.org/sequester-cuts-300000-poor-families-from-low-income-home-energy-assistance-program/>.

¹⁸ The SCS Astoria Energy 500 MW power plant began operations in Astoria, Queens In May 2006. Financing of this project was enabled by a 10-year capacity purchase agreement with Consolidated Edison Company of New York, Inc. Also, the New York Power Authority built the 500 MW Poletti power plant in for its New York City area governmental customers.

¹⁹ When contracts are not filed, however, they are subject to subsequent objection, review and alteration by FERC, even *after* they have been performed. Joshua Z. Rokach, *FERC’s Jurisdiction Under Section 205*, 15 Energy Law Journal 83, 87-88. Available at http://eba-net.org/sites/default/files/elj/Energy%20Journals/Vol15_No1_1994_FERCs_Jurisdiction.pdf.

market clearing price for capacity regardless of resource type....”²⁰ As stated by Commissioner

LaFleur:

there is a resultant tension between a resource neutral single clearing price market that uses a single clearing price to decide what you pay for, and states and localities with specific resource preferences like renewable portfolio standards. They both exist. What are we going to do about that?

The FERC Staff report acknowledges that “[a]s the mix of available resources changes in response to market conditions and state and federal policy changes, centralized capacity markets face new challenges in meeting *their* goals and objectives.”²¹ While it might be *their* goal and objective to become the primary or monopoly seller of all capacity at spot market prices, it is clear from the discussion at the technical conference that options other than buying capacity in the existing RTO/ISO markets are necessary for load-serving utilities to satisfy utility goals, customer needs, state economic policies or renewable resource portfolio standards. This capacity should be obtainable through direct building of new resources, or by long term contract with resource developers, with the price of capacity set outside the spot markets. A far less desirable alternative is the proliferation of additional sub-markets, or special spot market bidding rules, e.g., for administratively pricing capacity from “new” generation built under contract, or for certain types of generation required by some states but not by others within the ISO/RTO, and ever more complex bidding rules for mini-markets based on the provenance of the generation. As stated by Commissioner Norris:

there seems to be an on-going need for administrative “fixes” to our existing capacity markets. My concern is that the more administrative fixes that we layer

²⁰ *Centralized Capacity Market Design Elements*, Commission Staff Report in Case AD13-7, Aug. 23, 2013, at 2 - 3.

²¹ *Id.* at 4. (*Emphasis added*).

on top of capacity markets, the greater the potential for inefficiencies and higher costs.²²

This problem is best addressed by encouraging utilities to satisfy their requirements for long term capacity, or for special resources such as renewables required by state law, through traditional bilateral contracts that are filed and reviewable for reasonableness outside the capacity spot market process.²³ This traditional statutory process is transparent, and allows any adversely affected parties 60 days to lodge their objections pending review. That process would enable scrutiny of any putative unfairness to others with cognizable interests affected by the contract. When it is allowed to take effect, the contract rate is then fixed and so that capacity should be excluded from the spot market auctions.

Fourth, the suggestion of mandatory centralized markets suggests that either all buyers must obtain capacity at a single RTO/ISO market price, or that a seller cannot make a private bilateral contract sale at other than RTO/ISO prices requires more elaboration and legal justification. Any proponent of such a regime should demonstrate that such a move to establish monopoly control over all capacity sales and or all capacity pricing by RTO/ISO utilities would be lawful. FERC's powers over utilities whose rates are under its jurisdiction are limited by statute.

In seeking to answer the question of FERC's authority, we start with a fundamental proposition of federal law. "As a federal agency, FERC is a 'creature of statute,' having 'no constitutional or common law existence or authority, but *only* those authorities conferred upon it by Congress.'" *Atlantic City Elec. Co.*

²² *Statement of Commissioner John R. Norris on Upcoming Capacity Market Technical Conference*, September 20, 2013, available at <http://www.ferc.gov/CalendarFiles/20130920133445-norris-09-20-13.pdf>

²³ The Federal Power Act, 16 U.S.C. §§ 824 et seq., commands that "no change shall be made by any public utility in any such rate, charge, classification, or service, or in any rule, regulation, **or contract relating thereto**, except after sixty days' notice to the Commission and to the public. 16 U.S.C. § 824d. (*Emphasis added*).

v. FERC, [295 F.3d 1](#), 8 (D.C.Cir.2002) (quoting *Michigan v. EPA*, [268 F.3d 1075](#), 1081 (D.C.Cir.2001)) (emphasis in *Atlantic City Elec. Co.*). Therefore, "if there is no statute conferring authority, FERC has none." *Id.* As the Supreme Court has recognized, "an agency literally has no power to act ... unless and until Congress confers power upon it." *La. Pub. Serv. Comm'n v. FCC*, [476 U.S. 355](#), 374, 106 S.Ct. 1890, 90 L.Ed.2d 369 (1986). It is therefore incumbent upon FERC to demonstrate that some statute confers upon it the power it purported to exercise²⁴

In this case, there has been no proffer of legal justification for the suggested mandatory procurement requirement. There is no mention in the Federal Power Act ("FPA") of any "centralized capacity markets." No provision of the FPA gives FERC power to grant RTO/ISO utilities an exclusive monopoly over capacity and its pricing. No provision of the FPA gives FERC power to tell sellers that they cannot make bilateral sales at negotiated prices, or a buyer that they cannot obtain capacity under contract from a utility other than the RTO/ISO. No provision of the FPA authorizes reliance on the outcome of single price spot market RTO/ISO auctions to satisfy the statutory requirements for advance filing and just and reasonableness of all charges.²⁵

Any proposal to fix all capacity charges in a uniform price spot market should address what the Supreme Court has said: under the Federal Power Act "the prevailing price in the marketplace cannot be the final measure of 'just and reasonable' rates mandated by the Act."²⁶ More recently, the Supreme Court described "market-based rates" as "[r]ecent FERC [i]nnovations," pointed out that "[w]e have not hitherto approved, and express no opinion today, on the lawfulness of the market-based-tariff system..." and again "reiterate[d] that we do not address

²⁴ *California Independent System Operator v. FERC*, 372 F.3d 395, 398-99 (2004).

²⁵ 16 U.S. C. §§ 824d(a) and (d) (just and reasonable rates and notice required for rate changes).

²⁶ *Fed. Power Comm'n. v. Texaco, Inc.*, 417 U.S. 380, 398 (1974).

the lawfulness of FERC’s market-based rates scheme, which assuredly has its critics.”²⁷ If the notion of “mandatory” capacity markets is pursued, all parties should have the opportunity to address a more detailed proposal which addresses why procurement in the capacity market should be mandatory and any legal justification for requiring that.

Fifth, other than the RTO/ISO representatives, who generally defend their often changing capacity market tariffs,²⁸ there is broad agreement that the capacity markets as they now exist are flawed or at least not functioning optimally. “[A] decade of experience is proving that these market designs can’t assure customer access to adequate, reliable supplies of electric generation capacity.”²⁹ States and load-serving utilities, weary of paying high prices in transmission constrained areas, and tired of waiting for merchant plants to appear in response to putative price signals of the capacity markets, have sought development of new resources through legislation and long term contracts.³⁰ The lack of merchant generator response to the capacity prices is said to be because the market price still isn’t high enough. “Buyer side mitigation” and administrative price floors based on the cost of new entry by hypothetical power plants work to deter new resources and shore up market clearing prices to incumbent

²⁷ *Morgan Stanley Capital Group Inc. v. Pub. Util. Dist. No. 1*, 554 U.S. 527, 535 (2008).

²⁸ Ethier, ISO-NE: “Our view is that the New England capacity market has actually worked well to date to get us the resources we need” (Tr. 18); Mukerji, NYISO: “What we found in the last ten years is that our markets work” (Tr. 31); Ott, PJM: “It has enabled cost-effective substitution of competition to get capacity at the lowest cost” (Tr. 45).

²⁹ Randy Speck and Kimberly Frank, *Rethinking Capacity Markets*, Fortnightly, May 2013.

³⁰ See Note, *A Call for Federalism: The Role of State Government in Federally Controlled Energy Markets*, 65 Rutgers L. Rev. 573 (2013).

sellers. Some supporters of capacity markets acknowledge that “[b]uyer-side mitigation as currently implemented by the FERC is broken.”³¹ As noted by one observer:

Not one of the 26 panelists in the technical conference could speak from first-hand experience about their decision to build a new power plant in response to the capacity market incentives. These administrative constructs are designed around a central concept— creating a price signal that will get a new power plant built when needed. And in hundreds of pages of transcript and filed comments, no one has, thus far, come forward to say, “Yes, these markets are working as desired because the price signal they provide was the basis for me building new generation when it was needed.”

Comments of Cliff W. Hamal, Managing Director, Navigant Economics, December 18, 2013.

As summed up by Commissioner La Fleur:

I believe that about the only thing that all of your testimony has in common was in some way, shape or form, every single one of you said the capacity markets might not be getting the prices right, for various reasons.³²

Under these circumstances, it would not be prudent to force greater reliance on the possibly wrong prices set in the capacity markets by making capacity procurement in those markets mandatory, or to allow barriers to the acquisition of capacity through other means such as self supply and negotiated bilateral contracts.

Item 2. Accommodating state policies and self-supply by load serving entities.

In what ways do the current centralized capacity market designs facilitate, or hinder, the ability of market participants to enter into arrangements to supply their own resource adequacy requirements? Should the Commission consider changes to the current capacity market designs to facilitate these arrangements? How would any potential changes impact capacity market prices paid by LSEs and the price signals provided to capacity resources?

³¹ Richard B. Miller, Neil H. Butterklee, and Margaret Comes, “Buyer-Side” Mitigation In *Organized Capacity Markets: Time For A Change?*, 33 Energy Law Journal 449, 469 (2012).

³² Transcript, p. 273.

Consumer Groups urge the Commission not to approve centralized capacity market rules that work to discourage self-supply or bilateral long term contracts for capacity.

As discussed above, Consumer Groups support the ability of load-serving utilities to supply their own capacity resources from self-supply or bilateral contracting outside the capacity spot markets. The capacity markets have been volatile, and their designs may be faulty, for example, in setting minimum offer prices for new resources that work to inflate the clearing prices. Utilities seeking to protect their customers over time properly seek a portfolio of capacity resources which may include long term contracts that assure development of new resources, self-supply, by directly building new resources, and some short term supply through the capacity spot markets. As the Commission stated in the context of a retail utility that relied too heavily on an energy spot market:

While the Commission has no authority over retail electricity rates nor authority to rule on the prudence of SDG&E's provision of retail electric service, we would expect any responsible retail supplier to rely on a portfolio of resources and to turn to the spot market only to engage in economy transactions or to meet portions of its load that could not be predicted well in advance or which were not anticipated due to resource outages greater than are covered by prudent reserves.³³

Just as prudent retail utility should not rely too heavily on energy spot markets, it is also unwise to rely too heavily on the capacity spot markets. Utilities should be able to meet their customers' requirements outside the capacity spot markets, fully or partially. Complete self-

³³ *San Diego Gas & Electric Company*, FERC Docket No. EL00-95-000, p. 10 (Aug. 23, 2000)(*Emphasis added*).

supply may be a viable option for only a few utilities.³⁴ Partial self-supply is an option for many others.³⁵ Negotiated bilateral contracts based on costs which assure financing and development of new resources by third parties is another method to achieve desired new capacity consistent with state economic and environmental policies.³⁶ These options should be preserved and not frustrated by RTO/ISO rules which work to discourage self-supply or bilateral contracts. Over time, stronger bilateral markets for long term capacity could lead to reduced reliance on short term capacity markets:

Centralized capacity markets are an intervention to maintain resource adequacy. The appropriate role for these constructs is to provide a residual spot capacity auction to acquire additional capacity to meet resource adequacy targets. *The goal should be for the role of these constructs to shrink over time* as the energy and ancillary services markets develop, the demand side becomes more active, and forward contracting returns.³⁷

At this stage of market development, with market design in flux, there should be no Commission erected barriers to self-supply or contracting for supply *outside* the ISO/RTO capacity markets. It is also prudent, in light of the experience of capacity market gaming and malfunction,³⁸ for a retail utility to line up much of its capacity through negotiated long term

³⁴ “Vineland had become a model of success for New Jersey’s other municipally-owned electric utilities. It brought its first new plant on line on June 1, 2012 and reduced retail rates the same day and again in October. In fact, Vineland now offers the lowest retail electric rates in New Jersey.” Jablonski, PPANJ Comments, at 5.

³⁵ See *Genesee Waters Roaring Again in RG&E Hydro Tunnel, Rebuilding 2,000’ Tunnel System Key to \$111 Million Generating Station Modernization*, <http://www.rge.com/OurCompany/News/2012/121712stationfive.html>

³⁶ The SCS Astoria Energy 500 MW electric generating facility located in Astoria, Queens obtained financing for construction with a 10-year bilateral capacity purchase agreement with Consolidated Edison Company of New York, Inc.

³⁷ Comments of James Wilson, p. 2 (*Emphasis added*).

³⁸ See *United States v. Morgan Stanley*, 881 F.Supp.2d 563 (2012); *United States v. Keyspan*, 763 F.Supp.2d 633 (2011).

contracts or self-supply, and turn to the organized short term markets only for residual capacity requirements.

Item 5. Next Steps

What Commission action would be an appropriate next step with respect to those markets?

Are there outstanding issues or questions raised by, but not fully discussed at, the conference that should be considered in this proceeding?

Are there other issues, that, if addressed, would help the centralized capacity markets ensure resource adequacy in a just and reasonable and not unduly discriminatory manner (e.g., enhancements to the energy and ancillary services markets) that should be considered by the Commission in another forum?

As part of the post-technical conference comments, the Commission allocated a “Next Steps” section to address any “outstanding issues” to improve the performance of centralized markets. The centralized markets are complex organizations, administered by not-for-profit associations, with thousands of stakeholder processes and meetings designed to develop the tariffs and market rules that help determine electricity prices for a majority of American households. Because FERC has delegated so many functions to these private organizations, it is important that they operate with transparency and accountability. The need for enhanced consumer protections and representation is also important because the Commission relies on the market monitors and other aspects of these private organizations to handle many front-line Federal Power Act enforcement duties. As long as private organizations are tasked with such law enforcement responsibilities, there should be improved consumer protections.

A greater voice for household consumers will not only help the Commission and the RTOs in their continued quest to ensure that all rates are just and reasonable, but also will enhance

Commission initiatives such as demand response, where increased involvement by consumers could make these programs more robust.

We suggest 3 reforms that will vastly improve RTO responsiveness and accountability to household consumers.

i. Establish Permanent Funding for Consumer Advocate Offices at all RTOs.

As part of a market manipulation settlement reached with Constellation Energy on March 9, 2012,³⁹ the Commission established funds "for the benefit of electric energy consumers in the affected states," and the Commission accepted two proposals to fund consumer advocacy programs in both PJM and NYISO. In the case of PJM, the Commission accepted the allocation of \$1.2 million for the creation of the Consumer Advocates of the PJM States,⁴⁰ and NYISO's proposal to allocate \$10 million over a decade "to support consumer advocacy in the NYISO wholesale electric markets."⁴¹ In both cases, the funding source is the one-time payment resulting from the Constellation market manipulation settlement.

While the Commission's endorsement of the benefits of a consumer advocate division at RTOs is welcome, the current ad-hoc approach lacks the consistency needed to ensure household consumers have adequate representation throughout all RTOs and in the years to come.

Establishing permanent consumer advocate offices at *all* FERC-jurisdictional organized markets replete with permanent funding will help accomplish this.

ii. Establish an Office of Consumer Advocate at the Commission.

³⁹ www.ferc.gov/enforcement/civil-penalties/actions/138FERC61168.pdf

⁴⁰ <http://elibrary.ferc.gov/idmws/common/opennat.asp?fileID=13085170>

⁴¹ <http://elibrary.ferc.gov/idmws/common/opennat.asp?fileID=13091829>

In addition to improving consumer representation at the individual RTOs, an office of consumer advocate should be established at the Commission. Having both an office of consumer advocate at RTOs *and* for the Commission is not redundant because the RTOs are private organizations, and a formal consumer advocate should exist at the Commission level. Indeed, recently retired Chairman Jon Wellinghoff endorsed the creation of such a Consumer Advocate office in testimony before the US Senate in 2009.⁴² In November 2010, the National Association of Regulatory Utility Commissioners passed a resolution supporting the creation of an office of Consumer Advocate at FERC.⁴³

An ideal office would include the following characteristics:

- The Office should be organized in a way to maximize independence, including financing clearly allocated to support the activities of the office.
- The office must be able to conduct its own investigations not limited to the scope of FERC dockets or proceedings.
- The office should include authority to provide intervenor funding to consumer groups to encourage their participation in FERC proceedings.
- There should be an advisory board to the Office, composed of several representatives of the non-governmental consumer advocacy community, including slots for organizations representing low-income households and the elderly, and for both national and state-based consumer organizations.

Indeed, Congress has endorsed the creation of such an office through the years. The Federal Power Act currently outlines authorities for an Office of Public Participation at the Commission, including intervenor funding.⁴⁴

iii. Reform RTO Governance To Place End-Users On Equal Footing With Utilities And Power Producers.

⁴² www.ferc.gov/EventCalendar/Files/20091027115535-Wellinghoff-10-27-09.pdf

⁴³ <http://naruc.org/Resolutions/Resolution%20Supporting%20Federal%20Office%20of%20Consumer%20Advocacy.pdf>

⁴⁴ 16 U.S. Code § 825q-1 www.law.cornell.edu/uscode/text/16/825q-1

As private not-for-profit organizations tasked with operating and regulating electricity markets, it is imperative that household consumers believe such entities are fully transparent and accountable. While the RTOs offer thousands of different stakeholder meetings on a regular basis, attending such meetings requires enormous financial and staff resources – which is normally beyond the capabilities of groups tasked with representing the needs of household consumers.

The RTOs all have internal systems where different individual stakeholders are provided the ability to vote on resolutions, proposed tariffs and other policies impacting the governance and operation of the RTO. While FERC must ultimately approve RTO tariffs, the Commission usually grants the RTOs latitude, often citing the internal stakeholder processes.

An analysis of voting allocations shows that stakeholders representing household consumers represent less than 3% of the voting rights, while Wall Street banks and other financial firms hold more than 11% of voting rights.⁴⁵ In all, entities representing utilities, power plants and power marketers control between 60 and 70 percent of the vote, leaving household consumers underrepresented. All end consumers—household, commercial and industrial—currently only represent between one-fourth and one-fifth of the voting shares.

A simple reform would be to increase the voting allocations so that all end-users—household, commercial and industrial consumers—hold at least half of the voting shares. This would place end-users on equal-footing with utilities and power providers in helping to set the rules of the marketplace.

⁴⁵ www.citizen.org/documents/Tyson-slocum-RTO-governance.pdf

Conclusion

Consumer Groups appreciate the opportunity to comment on the important matters under consideration which have great impact on the price and reliability of electric service to its members in the ISO-NE, NYISO and PJM regions. We urge the Commission to adopt the recommendations discussed above. For additional information regarding any of the points above please call Marti T. Doneghy, AARP Senior Legislative Rep. mdoneghy@aarp.org Tyson Slocum, Director, Public Citizen Energy programs tslocum@citizen.org or/and Olivia Wein owein@nclc.org for the National Consumer Law Center (NCLC), on behalf its low-income clients.

Dated: January 8, 2014

Respectfully submitted,

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