McCullough Research

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To: McCullough Research Clients

From: Robert McCullough

Subject: “Instant Request” to the Federal Energy Regulatory Commission

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Today, a national coalition has petitioned FERC to “expand the scope” of its proposed Federal Power Act Section 206 “investigation”. The coalition is requesting that the Commission “address the core issue of whether RTO markets are producing unjust and unreasonable wholesale power prices.”

This is a healthy sign given the increasing differential between RTO and non-RTO states. Our current research indicates that the differential – even after the costs of fossil fuels have been removed – is continuing to expand. One fact that FERC has not yet realized is that removing fuel costs from the calculation makes the relative position of the RTO states even worse.

Recognizing that FERC initially “sought comment on four RTO-related issues: (1) the role of demand response in organized markets; (2) increasing opportunities for long-term power contracting; (3) strengthening market monitoring; and (4) RTO responsiveness to customers and other stakeholders”, the coalition remarks:

> “While the Commission correctly perceives that fundamental changes are required in these areas, electricity consumers of all stripes recognize that the problems in the organized markets run much deeper. The common position that leads the Undersigned Parties to file the instant request is this: ***a rulemaking proceeding confined to the four enumerated topics will not resolve the deep systemic problems in RTO-run centralized markets.”*** [Emphasis in original]

The coalition then adds “Given the serious challenges facing the country in coming years to construct needed infrastructure, while addressing converging environmental concerns and retaining our economic competitiveness, the limited scope of reform outlined in the ANOPR is insufficient.”

The five major issues presented are the following:

“Certain large, vertically integrated generation suppliers in RTO regions are earning supra-competitive returns that are not commensurate with returns on investments in other enterprises having corresponding risks”

“Rates that consumers are paying in RTO regions where these supracompetitive returns are being earned are consistently higher than rates in regulated markets and are increasing faster”

“Increases in prices in RTOs’ organized markets are only partially due to increases in fuel prices, and other non-cost-of-service related factors, including the exercise of market power, also play a significant role”

“Increases in prices and supra-competitive rates of return have not attracted new investment and supply, and have, therefore, not reduced prices, as would be expected”

“The Commission’s ratemaking methodology in RTO-run organized markets is based on presumed conditions that are at variance with reality. These presumed conditions include:

> the absence of significant market power;
>
> the existence of free entry to and exit from the market by suppliers in response to ‘price signals;’
>
> the existence of an optimized resource mix to assure inframarginal revenues earned by generators are just and reasonable;
>
> the absence of significant structural and behavioral impediments to long-term contracting in a Locational Marginal Pricing (‘LMP’) environment price-responsive demand, short-term substitution alternatives, and demand elasticity to price.”