APPA Public Power Daily, January 10, 2008

The gap between electricity rates in regional transmission organization states and non-RTO states is widening and the Federal Energy Regulatory Commission needs to reinstate a missing benchmark to analyze the problem, says a new study, The Missing Benchmark in Electricity Deregulation. Supporters of the centralized markets often argue that fuel costs are to blame, but when fossil fuel costs are removed from the comparison, the differential in retail prices between RTO and non-RTO states is even greater, says the study by Robert McCullough and Ann Stewart of McCullough Research in Portland,Ore.

The average retail price in RTO states in January 2003 was $10.42/megawatt-hour higher than the average price in non-RTO states; and the gap more than doubled to $23.90/MWh in 2007, the study found. When fossil fuel costs are taken out, the retail price premium in RTO states was $11.26/MWh in 2003 and soared to $27.55/MWh in July 2007.

However, there is no consistent, formalized benchmark to help determine if and by what magnitude RTO prices are higher than the marginal costs of producing the electricity, McCullough and Stewart said. “Lack of data transparency (e.g. the costs of generating units) means relatively few checks and balances against strategic bidding (even FERC cannot see the entire picture),” they said.

The logical benchmark would be real-time prices in the RTOs against “system lambdas,” which represent the variable cost of the last kilowatt produced over a particular hour by a generator’s dispatchable units, McCullough and Stewart said. System lambda is closely associated with the marginal cost of producing electricity and is a good indicator of the competitive price for electrical energy, they added.

“From a public policy perspective, the absence of marginal cost information for the administered markets is a significant problem, particularly when RTOs rely on auctions and set the rules outside public view,” McCullough and Stewart said. “If we want to know whether administered markets are truly competitive, we should again require RTOs to report system lambdas.”

To ensure that FERC reviews them as it considers further measures on RTO data transparency, APPA filed the McCullough paper with the commission, along with an earlier study by utility analyst William Dunn. In an evaluation for APPA’s Electric Market Reform Initiative, Dunn said regional transmission organizations should post offer and bid data that identifies generating plants and loads within one day after the market activity occurs.