Summary of Testimony of Braith Kelly, Senior Vice President, External Affairs

Competitive Power Ventures, Inc.

Hearing Before the House Subcommittee on Energy & Power on Draft Electricity Legislation

Title IV – Energy Efficiency and Accountability; Subtitle B – Accountability

The competitive power sector will continue to play a substantial role in developing the new generation resources needed to replace aging infrastructure, and to meet the nation's emerging reliability and environmental objectives. Competitive power has relied for thirty years on long-term power contracts as an important tool in financing and constructing power plants. Most of the authority for authorizing and licensing new power plant construction resides at the State level, with FERC and the capacity markets providing an important additional means to secure shorter-term power needs. State competitive procurements will continue to be a valuable means to enable the States to meet their resource needs in the years ahead.

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June 4, 2015

Mr. Chairman, Subcommittee Members, thank you for the opportunity to comment on the Subcommittee's discussion draft legislation on energy efficiency and accountability. I represent Competitive Power Ventures, Inc. (CPV), a Maryland-based developer, owner and operator of non-utility power plants, including both natural gas-fired and wind-powered facilities. I will limit my comments to the discussion draft's proposals in connection with resource planning in the wholesale electricity markets.

Background on the Competitive Power Industry

The competitive power industry has been a vital component of the nation's electric power supply for over thirty years. Since the Public Utility Regulatory Policies Act of 1978 (PURPA), competitive power has proven to be a viable alternative to what had until then been the only regulatory model for developing power plants: construction, on a sole-sourced basis, by state-regulated monopoly utilities which had the exclusive right to develop these resources within defined service territories. Competitive power companies today own almost half the operating power plants in the United States.

The competitive power industry gave rise to a powerful tool that has been used by states since the 1980s to help develop needed resources: competitive procurements, where non-utility developers were given the opportunity to bid to provide resources. The electric power sector is the most capital-intensive industry in the world. In order to secure and finance these needed infrastructure investments, a stable revenue source was required and winning bidders were awarded long-term contracts (power purchase agreements) that enabled owners to access the capital markets to finance these massive investments at a reasonable cost of capital.

The Role of Regional Transmission Systems and Independent System Operators

Regional Transmission Organizations (RTOs) and Independent System Operators (ISOs) are private corporations that are governed by their stakeholders and regulated by FERC. RTOs and ISOs were formed in order to place the control of the transmission system in independent hands, to ensure both that needed transmission facilities were planned for, and that transmission would be made available on equal terms and conditions to all power generators.

Nearly fifteen years ago, some of the larger RTOs and ISOs began to develop capacity markets as a valuable adjunct to their core responsibilities in the transmission arena. These RTO/ISO capacity markets currently operate in twenty states: the New York ISO, PJM Interconnection (thirteen states plus the District of Columbia) and the New England ISO (six states). Since "reliability" requires both adequate transmission and adequate generation, the capacity markets serve the important function of providing a price signal for capacity needs over a short-term planning horizon (typically one month to three years) that helps identify what estimated demand is expected to be. The price signals developed through these capacity markets incentivize developers to construct needed resources; as the market clearing price rises to a level

that might support new generation, developers will be more inclined to invest the substantial capital needed to actually build these facilities. Price signals alone have not proved sufficient in all cases to cause the investment to be made; states have in many instances provided additional support to ensure the development of needed resources such as renewables or reliability-based projects.

The RTO/ISO wholesale capacity markets serve several important functions. They help to forecast short-term demand by providing a snapshot of the anticipated demand for electricity within a region, typically one month to three years in the future. They generate price signals that can incentivize project development. And they provide a regional pool of wholesale electricity where wholesale sellers and buyers can transact to meet short-term needs.

But these capacity markets, as FERC has repeatedly stated, are "a" market, not "the" exclusive market. They are, more specifically, a residual market that is intended to complement bilateral contracts and State resource planning. To begin with, the capacity markets provide an undifferentiated product, i.e. electrons only, without consideration of the types of factors typically considered by a State in meeting its needs, such as complying with state and federal environmental laws, meeting national air quality standards, plant location, land use planning, water and air quality impacts, other environmental objectives, age-of-plant, etc.

In addition, neither FERC nor the RTOs/ISOs have authority to cause a power plant to be built or retired. They have no siting authority, no licensing authority, no ability to order a developer like CPV or a local utility to construct needed resources. Indeed, RTOs and ISOs that identify particular reliability needs that are not being met in the region, for whatever reason,

typically alert the state regulatory commissions of the problem so that the State may exercise its authority – authority the RTOs/ISOs do not have – to ensure that the resources are developed.

That is no gap or accident. It has been a core precept of the Federal Power Act since 1935, when Congress, while giving FERC plenary authority over wholesale electric rates, specifically reserved to the States jurisdiction "over facilities used for the generation of electric energy." That basic principle has been reaffirmed in almost every federal electricity law enacted by the Congress since 1935, including PURPA, the 1992 Energy Policy Act and the 2005 Energy Policy Act. As most recently stated in the 2005 Act, "[n]othing in this section shall be construed to preempt any authority of any State to take action to ensure the safety, adequacy, and reliability of electric service within that State." It is the State – not FERC or the regional transmission organizations – that has had ultimate responsibility for over a century to ensure that retail customers enjoy safe, reliable electric service.

This division of labor has been fundamental to the nation's energy policy since at least 1935. Energy policy is a shared responsibility between the federal and state governments. And while disputes have arisen over the years as to the precise dividing line between federal and state authority, most of those disputes have been resolved practically and amicably, with each entity bringing to the table an informed understanding of its role and the importance of the task to be addressed. For example, FERC has on several occasions addressed the need to harmonize its rules governing the capacity markets with the states' need to support the development of facilities that also compete in the FERC-regulated markets, striking a balance to accommodate the legitimate objectives of both.

Initial Comments on the Draft Legislation

The nation is embarked on a fundamental transformation of the electric power infrastructure, probably on a greater scale than ever before. Tens of thousands of megawatts of aging coal plant have announced their retirements, whether as the result of emerging state and federal environmental regulation, or by virtue of competitive pressures that have rendered those resources uneconomic to continue operating. In addition, twenty-nine states and the District of Columbia have enacted or promulgated renewable portfolio standards, i.e. requirements that the state's electric power needs be met by a certain percentage of renewable resources by a date certain. And the Administration's proposed Clean Power Plan looks to the States to develop state implementation plans to reduce the greenhouse gas emissions of existing power plants. Even if not all these initiatives are finalized, the nation, through its retail ratepayers, will invest trillions of dollars over the next two decades in the reformation of an already aging electric power infrastructure. State and federal regulators will need to utilize every available tool to ensure that the goals are ultimately met, and in an efficient and cost-effective manner.

The draft legislation's goals in this regard are laudable, but appear to be guided by a perception that core infrastructure resource decisions, including fuel diversity, resource adequacy and reliability are determined by the RTOs and ISOs, with FERC oversight, rather than by the States.

As discussed earlier, FERC, and the wholesale markets that FERC regulates, perform an important but only a supporting role in the development of these resources. Section 4221 of Chapter 2 (Market Reforms) of the discussion draft directs "each regional transmission entity" (including presumably those that have not developed capacity markets) to assess whether its

"current market rules" meet a designated list of criteria, to identify "specific actions" to revise its rules so as to meet those criteria, and to then "establish[] a timeframe for implementation" of those "specific actions."

The criteria include numerous subject areas that are expressly and exclusively reserved to the States, including resource adequacy and fuel diversity. As noted earlier, neither FERC nor the RTOs have authority to ensure resource adequacy or fuel diversity. To be sure, FERC's unquestioned authority over wholesale rates can impact private and public resource decisions, but that is a far cry from a statutory mandate. As noted in yesterday's testimony by FERC's Arnold Quinn, Section 4221 could accordingly "cause unnecessary conflicts between federal and state regulatory efforts." For example, opinions can and will differ as to what fuel diversity is appropriate in a given market. Each state typically has unique fuel diversity requirements, as evidenced by their RPS requirements and other resource choices, and there is no federal mandate with regard to fuel diversity. How, then, is an RTO to second guess or even supersede state choices on these questions?

Of potentially even greater significance is the draft bill's direction that the RTOs "identify and address regulatory barriers to entry, market-distorting incentives, and artificial constraints on competition." Simply stated, many of the significant resources that the states (through their resource plans or as directed by the federal government through the proposed Clean Power Plan) are seeking to develop may be extremely difficult to build without state incentives such as long-term contracts. Indeed, FERC's evolving capacity market rules have specifically acknowledged this reality, creating market entry rules for these resources that balance FERC's administration of a wholesale competitive market with the states' legitimate reliability and environmental objectives. As Mr. Quinn notes, "some states may assert that what

an ISO or RTO deems to be a 'market-distorting incentive' is in fact a legitimate policy adopted by a state to meet its specific policy needs." FERC has repeatedly exercised its authority to seek to ensure that such needed, state-supported projects are allowed to compete in the wholesale markets without "distorting" those markets, and has refrained from passing judgment on the states' wholly legitimate exercise of its prerogatives. Section 4221 arguably pulls FERC and the RTOs into an unnecessary and potentially divisive debate, with no discernible upside, and the considerable downside of states coming to rely increasingly on the volatile short-term markets.

In summary, the scale of the task confronting the United States to replace its aging infrastructure and to confront new market and environmental requirements is enormous and unprecedented. The state and federal governments will need to mobilize all the tools in their tool kits to meet these crucial objectives. Some of those needs are being and will be met in some markets through the development of merchant plants, i.e. power plants that are built on "spec," with no underlying long-term contract to establish a stable revenue stream. Others will require substantial state and federal support, through tax credits, long-term power contracts, or other incentives. The center of this development will continue to be at the state level, with FERC and the RTOs playing the strong and necessary supporting roles that they have traditionally performed. The draft legislation appears to shift this center toward FERC and the RTOs, in an area where they lack authority under existing law. FERC has adequate authority under existing law to address and minimize potential "distortions" to the RTO markets that might arguably be caused by state policies or directives, while allowing the reliability and diversity objectives of the states to be met.

My company will continue its efforts to compete at the state and federal level to contribute to developing the new power generation resources that country will need in the years ahead.

CPV thanks the Subcommittee for the opportunity to present its views, and welcomes any questions you might have.