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**Remarks of Stefanie A. Brand, Director
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**I/M/O of the Board's Investigation of Capacity
Procurement and Transmission Planning
Board of Public Utilities
44 S. Clinton Avenue
Trenton, NJ
Docket No. EO11050309
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Good morning, my name is Stefanie A. Brand. I am the Director of the Division of Rate Counsel. The Division of Rate Counsel represents and protects the interests of all utility consumers - residential customers, small business customers, small and large industrial customers, schools, libraries, and other institutions in our communities. Rate Counsel is a party in cases where New Jersey utilities seek changes in their rates or services. Rate Counsel also gives consumers a voice in setting energy, water and telecommunications policy that will affect the rendering of utility services well into the future. With respect to the adequacy and reliability of electricity supply – the subject of this proceeding – consumers are the parties that are directly affected if service reliability falls below acceptable levels, and ultimately bear the cost of the provision of reliable service.

It's hard to know where to begin when discussing the questions posed by the Board in its Order of May 27, 2011. Rather than simply run through the questions listed in the order, my

testimony today will outline generally what Rate Counsel believes are the impediments to the construction of new generating capacity that can serve New Jersey and the causes of those impediments. We will then discuss possible actions the Board may take to address those impediments and the relative advantages and disadvantages of those actions. I have with me today Robert Fagan of Synapse Energy Economics and we are both happy to answer your questions. We will also be submitting written comments to assist Staff with their recommendations.

Let me start by saying that there are no straightforward solutions. I believe the reason for this is that the root cause of the problem is the system that has been set up by the Federal Energy Regulatory Commission (FERC) to govern wholesale power markets. We can tinker, and we will tinker. However, while improvements can be made, we will be unable to fix the situation until the interests of electricity consumers and States are treated on a par with those of transmission and incumbent generation owners. So let me start off by saying that the number one thing the State of New Jersey should do is go to Washington and explain, complain, cajole, and apply whatever pressure it can to seek reforms that achieve a better balance of interests, that restore a State's ability to protect its citizens, and that ensure that the lights stay on and that the costs imposed on consumers are reasonable.

As you know, the Federal Power Act places jurisdiction over wholesale electricity markets with the FERC. FERC, in turn, has delegated the operations of these markets to Regional Transmission Organizations (RTOs) such as PJM. PJM is a private corporation governed by an independent Board of Directors and by its Members Committee. Although some end users, including New Jersey Rate Counsel, are members of PJM, the vast majority of members are generation owners, transmission owners, electricity distributors, or other suppliers.

Incumbent generation and transmission owners, who have much at stake in PJM's processes, are very active at PJM and FERC and outnumber and outspend consumer interests by a large margin. When PJM acts, its decisions are often afforded a presumption of reasonableness at FERC, and even where there is no formal presumption FERC tends to defer to the RTOs on matters within their purview. This process makes it very difficult for consumer advocates' voices to be heard.

Another part of the problem is that PJM's authority to address problems—even those involving reliability—is limited. While PJM can order the construction of transmission lines and can order generation facilities that are scheduled to close to continue running, it cannot order anyone to build new generation. Only through the markets it has constructed can it provide incentives for new generation to be built.

Which leads to another major part of the problem, which is that PJM and FERC have placed unjustified reliance on RPM, looking to it to perform functions that it was not designed to accomplish and that it is incapable of accomplishing. When RPM was first created, it was intended to be a residual spot market for the procurement of remaining capacity needs left unfulfilled *after* load-serving entities had had an opportunity to obtain capacity through long-term bilateral agreements and self supply. PJM itself said as much to the BPU during last summer's technical conference on these matters.

As RPM was never intended to be the primary mechanism for procuring all of PJM's needed new capacity, it should hardly be a surprise that it is incapable of fulfilling that function. RPM does not provide a secure enough long-term revenue stream to support the financing of projects by new market entrants, and it does little to overcome other barriers to entry, such as the challenge in finding new sites. For generators already participating in these markets, who control many of the readily available sites for the construction of new generation, there is a disincentive

to build, as the inability of newcomers to finance and build new facilities means higher prices and higher profits. Yet when states attempt to find ways around these barriers and provide incentives for new capacity construction, it is they who are accused of manipulating the market.

We are told that “if prices go high enough people will build,” however, this has been disproven over the past several years as high prices in New Jersey did not bring forth new generation. It is doubtful that even higher prices would produce such a result, but even if RPM could eventually elicit new supply, that process offers no assurance that new supplies will emerge in a timely and orderly way or that the particular resources selected by RPM will be the *kinds* of resources that New Jersey really needs. RPM doesn’t distinguish between baseload resources and peaking facilities. It isn’t aware of and doesn’t care about fuel diversity and resource-mix concerns. It pays no heed to the economic-development benefits of generation construction. These are legitimate concerns that state regulators have attended to for decades—and they must continue to be able to make these policy choices even in this era of organized wholesale electric markets.

Let’s not underestimate the consequences of preventing state regulators from addressing such concerns effectively. New Jersey has already been told to brace for rolling blackouts in 2012. While a more recent forecast may push that date back, New Jersey will eventually need new capacity. PJM has recently ordered a local plant that was scheduled to shut down years ago to keep running and ratepayers are being asked to foot the \$59 million bill for it to continue running until we can find our way back to a reliable supply of capacity. We are paying congestion charges and substantial capacity charges, and yet we still don’t know if the system will keep the lights on in the coming years. We have large generating facilities scheduled to

close in the next decade, others that may choose to close rather than install expensive but necessary pollution control equipment, and we are always subject to losing merchant capacity to our neighbors to the east.

In the face of this, New Jersey sought to do the right thing, basing its actions on market rules agreed to by many of PJM's members, adopted by PJM, and found to be just and reasonable by FERC. At PJM's urging, FERC's response was to change the agreed upon and "just and reasonable" rules. According to the incumbent generators, PJM and FERC, the State of New Jersey is supposed to sit back and place its economy and the welfare of its citizens in the hands of RPM, hoping—but lacking any assurance—that "the market" will provide. Based on the flawed and disproved theory that new generation will sprout if only prices spike high enough, this sovereign state is being told it must sit by while its citizens are left in the dark. Of course, you are not going to do that. I applaud you for instituting this proceeding and for investigating ways to take on this broken system and protect the State's ratepayers.

So what options are available to the Board and the State to address these concerns? First, Rate Counsel urges the Board to continue to pursue the LCAPP program. The FERC has recently granted rehearing "for further consideration," which means that FERC is still considering the arguments that were raised on rehearing of its order, and it has ordered its Staff to conduct a technical conference on certain issues raised by the protestors in their rehearing requests. The proceedings on these issues at FERC, PJM and in the Court of Appeals are by no means over and we should continue to pursue all available options to permit the LCAPP program to proceed. This could include seeking an exemption from the MOPR by filing a complaint at FERC, continuing to challenge FERC's order, or by examining any other option left open by

FERC's order. Rate Counsel urges the Board to examine all of the available options that could allow the LCAPP program to proceed.

Second, the State should examine other means to provide the revenue assurance that generators need to build new generation. A recent Order issued by FERC out of the New York ISO demonstrates that not all state financial assistance measures are viewed by FERC as impermissible. In the New York case, the City provided property tax abatements to promote the development of in-City peaking units. FERC allowed this abatement to be incorporated into the calculation of the net cost of new entry (net CONE) for facilities in the NYISO. FERC did not find that such measures led to "uneconomic" offers or require any mitigation as a result. Thus, it appears that some subsidies are allowed. While we admittedly do not know precisely which will be permitted and which will not, the decision in the New York case certainly suggests that the State should look at whether tax abatements or other more traditional State subsidies may be used to contribute to the incentives for generators to build.

In this regard, the State may also want to look at whether its Economic Development Authority (EDA) could assist in encouraging new generation. EDA has broad powers to promote economic development, and either through existing authority or new statutory authority, may be able to provide the stability needed to allow for facility financing. In addition, over the years the idea of a state power authority has periodically been discussed as a means to permit the State to self-supply. While expanding government may not be favored in these difficult economic times, and while new statutory authority would certainly be required to create a power authority, it would be worthwhile for the Board to look at the experience in other states with power authorities, such as New York, to assess the viability of such an option.

"Self-supply" is a technical term used by PJM to describe how a Load-Serving Entity provides for its own capacity needs without directly buying RPM capacity. Another means of self-supply to consider would be returning at least a portion of the capacity obligation to EDCs from BGS suppliers. Currently, no one in New Jersey - not BGS suppliers, who are short-term Load-Serving Entities - nor EDCs have an obligation to provide capacity to customers beyond the 3-year window of the BGS supply contract. This is the case even though power plants can last for 20-30 years or longer and even though RPM requirements themselves don't begin for 3 years after the auction. If self-supply becomes the only vehicle permitted by FERC under which New Jersey could decide its own course of action, we should have our BGS procurement process ready to adapt so that New Jersey can self-supply its capacity obligation using longer-term contracted resources such as the LCAPP units for a portion of the BGS load. Shifting such an obligation back to EDCs does not need to undermine competitive procurement of energy supplies using a BGS-like auction approach, and it also can work well with competitive procurements such as the one used to determine the LCAPP winners in the first place.

Finally, I note that in EDECA, the Legislature specifically stated its intent to

provide the Board of Public Utilities with ongoing oversight and regulatory authority to monitor and review composition of the electric generation and retail power supply marketplace in New Jersey, and to take such actions as it deems necessary and appropriate to restore a competitive marketplace in the event it determines that one or more suppliers are in a position to dominate the marketplace and charge anti-competitive or above-market prices.

N.J.S.A. 48:3-50 (2)(c)(5).

While much of the focus in the LCAPP debate has been on allegations that buyers or states could manipulate the marketplace to achieve below-market prices, the fact is that the supply-side of the New Jersey market may not be as competitive as hoped by the Legislature. As a result, there may be a need for the Board to invoke this authority and investigate (a) the

competitiveness of New Jersey's supply (b) the barriers to entry that inhibit the addition of new supply, and (c) the steps that the Board can take to reduce those barriers.. This may provide further information that will assist the Board in finding solutions and ways to overcome New Jersey's electric capacity challenges.

Thank you for the opportunity to testify today. As I mentioned, Rate Counsel will be filing written comments with the Board in connection with this proceeding. We are also available to answer any questions you may have.