

**BEFORE THE STATE OF MARYLAND
PUBLIC SERVICE COMMISSION**

In the Matter of Whether New Generating)
Facilities Are Needed to Meet Long-Term) Case No. 9214
Demand for Standard Offer Service)

COMMENTS OF THE ELECTRIC POWER SUPPLY ASSOCIATION

I. Introduction

The Electric Power Supply Association (“EPSA”)¹ respectfully submits these comments in response to the Maryland Public Service Commission’s (“PSC” or “Commission”) December 29, 2010 *Notice of Comment Period on Request for Proposals for New Generating Facilities* (“Notice” and “Draft RFP”) in the above captioned proceeding. EPSA supports fair and efficient markets that produce competitive results and enable grid reliability. In that light, EPSA cautions against out of market activity that skews competitive markets, threatens long term investments and puts market risks on consumers instead of investors.

Should the Commission determine that out of market activity of the type suggested by the Draft RFP is necessary, EPSA commends the Commission for correctly identifying that it should first determine a need for new generating facilities to serve Maryland prior to action on any RFP proposals that may be received in this proceeding. However, despite the fact that the Draft RFP

¹ EPSA is the national trade association representing competitive power suppliers, including generators and marketers. These suppliers, who account for 40 percent of the installed generating capacity in the United States, provide reliable and competitively priced electricity from environmentally responsible facilities. EPSA seeks to bring the benefits of competition to all power customers. The comments contained in this filing represent the position of EPSA as an organization, but not necessarily the views of any particular member with respect to any issue.

indicates an evidentiary hearing would be undertaken to develop the record and support such a finding, it is unclear when or how that will occur.²

EPSA strongly submits that such a reliability finding is a threshold determination. EPSA notes that the most recent reports from PJM continue to indicate that there, in fact, is no reliability need.³ Furthermore, since its inception, PJM's Reliability Pricing Model ("RPM") capacity market has produced significantly enhanced reliability for consumers across the PJM region, including Maryland, by attracting least-cost supply to meet reliability mandates. The PJM Independent Market Monitor ("IMM") has consistently found RPM auction results to be competitive. In sum, the RPM is working, as designed, to assure grid reliability through least-cost investment.

EPSA is generally concerned with proposals such as the Draft RFP that would not include existing generation and consider all possible resources or solutions; if the Commission conclusively determines the State of Maryland faces a reliability threat and proceeds with seeking additional supply for reliability, it should consider all forms of supply and procure them in a competitive manner. EPSA vigorously opposes any state-specific remedy that results in out-of-market subsidies, and artificially suppresses capacity prices below competitive levels. Such out-of-market actions will foist costs upon end users for incremental supply and will discourage other investors of supply (generation, demand response,

² Draft RFP at 2.

³ See, e.g., *2010 Quarterly State of the Market Report for PJM: January through September*, Monitoring Analytics, LLC (avail. at <http://pjm.com/documents/reports/state-of-market-reports.aspx>) at p.140 (revealing that the current PJM reserve margin of 16.5% exceeds the minimum Installed Reserve Margin of 15.5%).

energy efficiency and incremental transmission upgrades) that rely upon fair and competitive markets to support their investments. Such out-of-market action could ultimately result in higher costs, among other detrimental outcomes, for Maryland ratepayers as investors shy away from the market and hold out for these type of out-of-market contracts.

II. Maryland’s Reliability Need For New Generation Must First Be Established Through An Evidentiary Hearing

EPSA appreciates the Commission’s clarifying statement that “the fact that the Commission issued this Notice or has prepared a draft RFP **should not be construed as a finding by the Commission that new generation is required** or that the Commission has decided to order any party to construct, acquire, lease or operate new capacity resources in or around Maryland.”⁴ The Commission appropriately establishes that it “will conduct an evidentiary hearing to evaluate” the issue of whether there exists “a need for additional generation in Maryland.”⁵ The Draft RFP further states that “the Commission may need to invoke its authority under §7-510(c)(6) if, **after an evidentiary hearing**, the record in this case demonstrates that a projected capacity shortfall. . . . may affect Maryland.”⁶

The Notice or Draft RFP does not, however, state when or how this evidentiary hearing will be conducted to determine if such a need exists. It does set a detailed schedule for the entire RFP process, including the date by which

⁴ Notice at 2 (emphasis added).

⁵ Draft RFP at 2.

⁶ Id. (emphasis added).

contracts would be signed. Issuing detailed RFPs for new generation before first conclusively determining whether there is even a need for that capacity appears to be the classic case of putting the cart before the horse.

Although EPSA does not believe the underlying facts indicate a reliability need exists, EPSA asserts the Commission's critical next step in this process must be an evidentiary hearing to evaluate and conclusively establish through the record that the State of Maryland faces a reliability threat that cannot be addressed through the existing PJM markets, before issuance, if any, of an RFP. Accordingly, establishing a revised timeline that provides a detailed schedule for the evidentiary hearing process, followed by the RFP if it is deemed necessary, is important to ensure that necessary investment decisions can be made in a timely manner with adequate information and to prevent undue regulatory uncertainty. The Commission should make the data and analysis from the hearing available for review throughout the course of this proceeding. The Commission should also provide an opportunity for written comments by all interested parties, to provide a full record and further inform the Commission's final decision.⁷

III. PJM Has Maintained Reliability, Both Regionally And For Maryland, And Current Data Reflects There Is No Reliability Threat

EPSA notes the Commission's stated intent that the "[p]urpose of this RFP is to ensure the continued, long-term reliability of electricity supply to

⁷ EPSA is not commenting on the specific provisions of the Draft RFP, but believes there are numerous substantive concerns associated with contemplating and conducting an out-of-market procurement process and the long-term ramifications for the competitive marketplace and consumers.

Maryland customers.”⁸ EPSA appreciates the Commission’s role and responsibility in ensuring that Maryland’s consumers continue to have access to reliable, competitively priced electricity. EPSA believes that Maryland has derived such significant benefits – and will continue to do so – from its broader regional participation in PJM, and in particular, through participation in the RPM capacity market. Given this, it seems likely that the Commission’s evaluation and analysis in the hearing process will support a finding that the State of Maryland’s reliability needs have been and will continue to be adequately addressed through the PJM markets.

As PJM recently noted, RPM performance to date demonstrates there has been a significant increase in incremental new generation and Demand Resources, as well as a significant number of deferred generation retirements, across the PJM footprint that have provided reliability benefits in a cost-effective manner to the Mid-Atlantic (“MAAC”) region and to Maryland specifically.⁹ With regard to historic price performance of RPM, PJM noted:

On average over the seven [Base Residual Auctions] conducted, RPM prices in Maryland have been below the Net Cost of New Entry (“Net CONE”) signifying that it has been more cost-effective for Maryland customers to rely on lower cost options such as energy efficiency and demand response and imports using available transmission capacity rather than on new natural gas combustion turbines built within Maryland to maintain resource adequacy.¹⁰

⁸ Draft RFP at 1.

⁹ See Comments of PJM Interconnection, LLC at 3, *In the Matter of the Reliability Pricing Model and the 2013/2014 Delivery Year Base Residual Auction Results*, MD PSC Administrative Docket No. PC22 (filed October 1, 2010).

¹⁰ Id at 2.

In outlining the reliability benefits derived by Maryland as part of the MAAC region, PJM specifically calculated the incremental capacity available within Maryland since the inception of RPM and the associated economic benefits. These newly available in-state levels of demand response (1629 MW), energy efficiency (117 MW), new generation (275 MW), uprated generation (271) and canceled retirements (1,260 MW) – resulting in 3,552 MW of incremental benefits to Maryland – are, collectively, a lower cost, lower risk alternative to building 3,552 MW of all new generation in Maryland based on the Independent Market Monitor’s (“IMM”) 2009 State of the Market Report’s average capacity pricing.¹¹ Also, PJM’s comments noted “if the Commission’s previous reliability concerns were about to be realized, this would be reflected in RPM prices in Maryland’s constrained LDAs being well in excess of the Net CONE in the most recent BRAs, which has not been the case.”¹²

The Brattle Group has also done extensive analysis of the seven RPM BRAs and concluded the market design has “demonstrated its ability to procure adequate resources to meet reliability requirements on an RTO-wide basis, as well as ensuring that sufficient resources are deliverable to transmission-constrained [local deliverability areas],” and has done so at prices consistent with locational market fundamentals.¹³ In enumerating the benefits of RPM, including attracting and retaining substantial capacity resources at or below the cost of

¹¹ Id. at 9-13.

¹² Id. at 13.

¹³ See Comments of Johannes P. Pfeifenberger and Kathleen Spees, of The Brattle Group at 5, *In the Matter of the Reliability Pricing Model and the 2013/2014 Delivery Year Base Residual Auction Results*, MD PSC Administrative Docket No. PC22 (filed October 1, 2010).

new generation, Brattle also cautioned about the need for stability in the RPM market design for price signals to attract and retain capacity at reasonable costs in the long-run. This is necessary as RPM “has a demonstrated history of setting appropriate market-based capacity prices and ensuring reliability at an appropriate location-specific level.”¹⁴ Brattle further commented:

Regulatory intervention in response to rising prices would signal to investors that sufficient returns on investment cannot be realized even during times of scarcity. This type of intervention would undermine confidence in the market and result in higher required returns on investment, thereby resulting in lower reliability and increased costs to consumers in the long run...We recommend that possible improvements to RPM be evaluated carefully and be approved with a long-term perspective to ensure the efficient evolution of the regional electricity market.¹⁵

Additionally, EPSA notes that the collective PJM wholesale market results, including the RPM auctions, have repeatedly been deemed competitive by the PJM IMM and producing just and reasonable prices as determined by the FERC.

IV. Out-Of-Market Procurement Artificially Suppresses Competitive Prices And Represents An Exercise Of Buyer-Side Market Power

While EPSA will not address the specific proposed elements in the Draft RFP, EPSA questions here as it has elsewhere whether such a proposal truly represents sound electricity policy.¹⁶ EPSA generally welcomes a discussion of

¹⁴ Id. at 12.

¹⁵ Id. at 12-13.

¹⁶ See Testimony of EPSA President & CEO John E. Shelk, regarding Assembly Bill 3442, before the State of New Jersey Assembly Telecommunications and Utilities Committee (December 9, 2010); *Comments of the Electric Power Supply Association regarding Senate Bill 2381*, before the State of New Jersey Senate Committee on Energy and Environment (November 15, 2010); and, also, *Motion for Leave to Intervene and Protest of the Electric Power Supply Association*, regarding ISO-NE’s proposed FCM Revisions in Docket No. ER10-787-000 (filed March 15, 2010) (raising concerns regarding price suppressing effects of out of market capacity on the ISO-NE FCM). All documents are available at www.epsa.org.

how to ensure that public policies are consistent with necessary investments, particularly with several extensive and expensive environmental regulations on the horizon that will lead to a combination of retrofits and replacement power as plant retirements occur.

However, EPSA strongly opposes the Draft RFP in principle because, if implemented, the resulting long-term contract(s) would establish a significant multi-year financial commitment(s) that will ultimately be paid by consumers and stems from the premise that out-of-market subsidies are justified because doing so will increase supply to drive down capacity prices. This exercise of state-sanctioned buyer-side market power to manipulate prices would have an artificially depressing impact on short-run prices, and dissuade investors from making long term investments in the state absent similar ratepayer guarantees.

There are at least three reasons why such an approach is mistaken: first, there are several ways to challenge the RFP on constitutional and other legal grounds; second, the RFP may very well run afoul of federal requirements governing wholesale power markets; and third, any short run savings could well be offset by higher energy prices and higher longer term capacity prices while distorting the regional price signals necessary for future private sector investment and jobs.

As to the first two reasons, the Draft RFP would require that eligible projects participate in and clear PJM's RPM auctions. As a result, the RFP seeks to dictate bidding behavior in a federally-overseen regional wholesale electricity capacity auction that must, under the Federal Power Act, be conducted

consistent with being just and reasonable and not unduly discriminatory or preferential.

As to the third reason, policies subsidizing select new generation and upgrades at existing plants invariably impact both the current and future economics of **all** existing and **all** potential new resources. Other market participants will factor in the existence of any such long-term commitments that may ultimately result from the Draft RFP and the potential for future market intervention here and elsewhere into their decision-making.¹⁷ As a result, future energy and capacity prices could well end up higher as a result of the Draft RFP if it were to be implemented.

To highlight the potential negative unintended consequences of a similar recent action, EPSA points to the analysis of the PJM IMM regarding New Jersey Assembly Bill 3224,¹⁸ which addresses the construction of new subsidized generation capacity in-state and its impacts:

The Bill would require New Jersey to procure 1,000 MW of new capacity when it is not needed for reliability, require the new capacity to clear in the auction through an offer price below its costs and provide subsidies to the new capacity in the form of additional out of market revenue. These features of the Bill are not consistent with the PJM market design. If implemented, the market results would not be consistent with a competitive outcome.

¹⁷ The investment risk and anticompetitive outcomes associated with the Legislation recently passed by the State of New Jersey (Senate Bill No. 2381) was noted by Citi Investment Research & Analysis' Brian Chin as follows, "...the broader issue is that if New Jersey successfully builds a power plant through market intervention, this undermines the cyclical integrity of the power market." Capacity Markets Update at 4 (issued November 19, 2010).

¹⁸ See *State of New Jersey Senate Bill No. 2381 (Fourth Reprint)*, State of New Jersey 214th Legislature (*introduced* Oct. 18, 2010) (the Bill, S2381, has been passed by the New Jersey Legislature and is awaiting action by the Governor of New Jersey).

The result of such a subsidy by New Jersey ratepayers would be to artificially depress the Reliability Pricing Model (RPM) auction prices below the competitive level, with the result that the revenues to generators both inside and outside of New Jersey would be reduced as would the incentives to customers to manage load and to invest in cost effective demand side management technologies...

...This substantial reduction in revenue would affect the investment decisions of current owners of capacity and potential investors in capacity both in New Jersey and in areas outside of New Jersey. The likely result is less investment in new and existing capacity, in the form of generation resources and demand response. Depressing the price in New Jersey would also mean that the required direct subsidy by New Jersey ratepayers would increase for the specified procured MW, with perhaps significant unintended consequences for the business and residential customers who would have to pay the mandatory subsidy. The result of depressing RPM prices in New Jersey would also be to increase the probability that additional subsidies by New Jersey ratepayers will be required for any future capacity additions, either in the form of generation or demand side resources, needed to maintain reliability in New Jersey. The result of depressing RPM prices over a broad section of PJM would be to increase the probability that subsidies by ratepayers in other states will be required for any future capacity additions, either in the form of generation or demand side resources, needed to maintain reliability in that area.¹⁹

EPSA submits that consumers are best served by acquiring the least cost resources within applicable environmental requirements, regardless of location or vintage, which is the purpose of RPM. As proposed, the Draft RFP and the genesis of this proceeding still arise from the faulty premise that regional supply issues should be addressed by state-specific remedies. If RPM results are accurate market signals, then no additional resources are needed at this time. Competitive forces will signal through the RPM when and where new generation

¹⁹ See *Impact of New Jersey Assembly Bill 3442 on the PJM Capacity Market*, the Independent Market Monitor for PJM at 3-4, (Jan. 6, 2011) (avail. at http://www.monitoringanalytics.com/reports/Reports/2011/NJ_Assembly_3442_Impact_on_PJM_Capacity_Market.pdf).

is necessary. If the results are incorrect due to a flaw in RPM, then changes should be implemented for **all** market participants.

EPSA recognizes that improvements will continue to be needed to PJM's RPM and competitive suppliers are committed to working with PJM, FERC and the individual states to ensure that RPM continues to deliver reliability while sending accurate price signals for investment decisions.²⁰ As part of this process, it is important to also review potential barriers to entry into the marketplace of economically justified new facilities. Changes to RPM should be considered, but purposely manipulating the price in the market should not be allowed to occur – and will ultimately stifle investment, innovation and job creation in Maryland.

²⁰ There are several near term efforts underway in PJM that provide a vehicle for stakeholder concerns regarding RPM to be considered, including those of the State of Maryland: First, the PJM Members have recently approved the creation of a Task Force to address RPM “low hanging fruit” issues that may facilitate more investment in the region. Second, PJM is conducting a comprehensive review of the RPM, which it intends to provide to shareholders in August 2011.

V. Conclusion

EPSA appreciates the opportunity to submit these written comments and looks forward to being constructive participants in the debate on these important matters. EPSA respectfully suggests there is time to continue to work together on a regional basis to address the concerns that give rise to the Notice and Draft RFP.

Respectfully Submitted,



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