Assuring Resource Adequacy

Introduction

As described in the recent FERC order, the purpose of the Resource Adequacy Requirement (RAR) is to help ensure development of infrastructure needed for reliable transmission system operation, including adequate generation and demand-side resources.

The perceived need for a regulatory mechanism to accomplish the goal of reliability is based on recent shortages in California and elsewhere, and on political reaction to those shortages. Moreover, dozens of new power plants that were planned several years ago have been cancelled, due in large part to the declining price of electricity. With wholesale prices for forward years nearly half what they were just two years ago, coupled with inadequate spark spreads to justify investment in new generation, policymakers are understandably concerned that new development will lag and reserve margins will fall, creating an energy crisis that no one wants "on their watch."

Green Mountain Energy Company respects that concern and supports the goal of assuring resource adequacy. However, it is essential to the competitive operation of markets that resource adequacy be obtained through fair, open processes that do not favor one competitor over another. Further, the costs of resource adequacy should be collected through a competitively neutral charge to all end-use customers that is the same regardless of who supplies their electricity.

Challenges Associated with Resource Adequacy Requirement

Green Mountain supports the goal of resource adequacy, but there are problems posed by the RAR, as designed, for competitive retail LSEs.

- Significant costs and risks are added to low-margin retail businesses that they are ill- equipped to absorb, and that they may not be able to pass on to customers because they compete against capped retail rates.

- Contracting 3-5 years in advance imposes large costs and risks on retail suppliers who do not know what their load will be 3-5 years from now - thus increasing costs, incurring prohibitive credit requirements, and violating prudent risk management policies.

- The requirement for generator-specific contracts to meet the RAR inhibits development of competitive wholesale markets because it limits participants and transactions in the market, enhancing the market power of generators, and creates special challenges for LSEs required or desiring to utilize renewable energy resources.

- There is inadequate protection against corporate practices that could provide a cost advantage to incumbent utilities and their unregulated LSE affiliates who now own existing generating resources. As a result, a higher share of the costs of developing new resources needed for all customers could fall on newer LSE entrants.

- These new costs and risks will be placed upon competitive retailers who have succeeded in reliably meeting customers' demand in recent years even as many competitive LSEs have left the market.

A Better Alternative: the New Resource Assurance Plan

It is possible to develop a resource adequacy mechanism that avoids these problems, while better assuring resource adequacy. To ensure adequate resources, it is necessary to encourage the development of new resources that bring the newest technologies to the market.

When forward prices fall, a project that was formerly projected to be profitable can quickly become unprofitable. A plan to install a new peaking plant that made sense in 2000 might not make sense in 2002 due to changing market conditions. Green Mountain proposes a market mechanism to ensure timely development of needed, new resources under these market conditions.

1. Hold an auction to determine how much incentive (New Resource Payment) is necessary to encourage new resources to develop for availability in the planning year, three-to-five years out. Such an auction will happen in any year that the ITP determines that there is a gap between the desired level of resource adequacy in the planning year and resources currently on line and in development.

2. Newly developed and repowered power plants, demand resources and transmission resources will be qualified to bid.

   Green Mountain could consider a phase-in of this exclusive provision over a specified period of time only in regions where existing resources are already receiving capacity payments and when such units are necessary to minimize the long-run costs to customers.

3. Payment to the winning, qualified New Resources will be made over five years beginning with the first year the New Resource is available, but starting no earlier than the planning year.

4. Costs of the New Resource Payments will be recovered from all customers in the region as the cost to ensure resource adequacy for the good of all the public. One method of cost recovery is to treat the cost of the New Resource Payment as a transmission-related charge.

Resource Adequacy Ensured in Market Supporting Retail Access

- Buyers and sellers continue to rely on bilateral contracts to meet customer demand, including contracts for resources under development.

- Market liquidity is enhanced compared to SMD RAR and market power problems are not perpetuated.

- The cost is minimized because it is established by a fair, open auction at a competitively efficient level.

- The cost of assuring resource adequacy is passed on to customers in a competitively neutral manner.

- Sufficient new resources will enter the market, allowing robust energy markets to reliably meet customers' demand at all times of the year.

- Entry of new and the most efficient technologies will be facilitated.

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