

The Regulatory Challenge for 2002: Getting Stable Markets to Support Needed Investment

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4th Annual
Financing US Power Plants Conference
Center for Business Intelligence
New York, NY
November 18, 2002

Strong Access to Capital Markets is Essential for US Electric Markets

- **Why Access to Capital Markets is Vital**
 - Capital Intensive Industry
 - Moderately Long Lead Times
 - Shortages can be Catastrophic
 - Low Demand Response Increase Market Vulnerability
 - Political and Economic Fallout Severe
- **But It's Not Working Well Now**
 - Crisis in Generating Sector
 - Crisis in Marketing Sector
 - A Glut?
 - Quite Possibly
 - But Other Factors at Work
 - And Gluts Turn Around Fast
 - Crisis of Confidence

Once Upon a Time In the West

- **The Key Question in Early 2001, Western US**
 - Not: What Will the Future Price Be
 - Not Even: Who Will Set the Price?
 - But: Who Will Own the Assets?
 - International Players Recognize This as Country Risk

- **The Key Questions in Early 2002, Western US**
 - Can You Trust Anyone in the Market?
 - Will Anyone be Left to Play?
 - Another Form of Country Risk?

The FERC Strategic Plan: Making Markets Work

Given What Happened in the West, We Need to:

- ***Make Markets Possible:*** Promote a Secure, High Quality, Environmentally-responsible Energy Infrastructure Through Consistent Policies
- ***Make Markets Work:*** Foster Nationwide Competitive Energy Markets as a Substitute for Traditional Regulation
- ***Make Sure Markets Work:*** Protect Customers and Market Participants through Vigilant and Fair Oversight of the Transitioning Energy Markets

Two Key Initiatives

- Standard Market Design
- Market Oversight and Enforcement

Standard Market Design

- **Key Features**

- Independent Transmission Providers
- More Standardization in Markets
- Better Market Pricing
- Better Market Safeguards

- **Timing**

- Rule in 2003
- Implementation in Stages
- RTOs Already in Progress

Standard Market Design

Independent Transmission Providers

- **Purpose**
 - No Discrimination
 - Greater Credibility
- **Nature**
 - Same Basic Requirements as RTOs
 - Except for Scope
 - Mandatory, not Voluntary
 - Keys are True Independence and True Operation of System

Standard Market Design

More Standardization in Markets

- **Purpose**
 - Facilitate Trade Around the Continent
 - Lower Engagement Costs
- **Provisions to Get Similar Market Structures**
 - Day Ahead
 - Real Time
 - Transmission, based on Locational Marginal Pricing
 - Alleviate Seams as Much as Possible
 - Encourage Standardized Business Practice
 - But: Balance with Regional Flexibility

Standard Market Design

Better Market Pricing

- **Purpose**

- Increase Efficiency in Operation
- Get the Right Investments at the Right Place at the Right Time

- **Provisions**

- Day Ahead and Real Time Markets
 - Makes prices Transparent
 - Solves Short-term Dispatch Issues
 - Provides Basis for Long-term Prices, Settling Derivatives
- Locational Marginal Pricing
 - Gets the Right Operational Price Signals
 - Gives Signals for Investment
- Participant Funding for Transmission

Standard Market Design

Better Market Safeguards

- **Purpose**
 - Avoid Market Meltdowns
 - Avoid Market Power
 - Re-establish Confidence in Energy Markets
- **Market Mitigation**
 - Load Pocket – Must Run, Constrained Bids
 - Safety Net Bid Cap
 - Resource Adequacy Requirement
 - Optional Mitigation of Persisting Problems
- **Market Monitoring**

Market Oversight and Enforcement

- Two Tiered System
- Market Monitoring Units (MMUs) for Individual Electric Markets
- FERC Office of Market Oversight and Investigation (OMOI)

MMUs

- **What Are They?**
 - Independent Market Experts at Market Level
 - Independent of all Market Participants
 - Independent of ITP Mangers
 - Report to ITP Board and FERC
- **What Do They Do?**
 - Market Performance (Annual Reports)
 - Problems as They Arise (Real-time Reporting)
 - Investigations within the Market
- **Where are They Now?**
 - PJM
 - NYISO
 - ISO-NE
 - CAISO
 - MISO

OMOI

- **Who Are We?**
 - New Office Within FERC
 - Staff of 120 by FY '04
 - Wide Range of Expertise to Understand Markets and Remedy Problems
- **What Do We Do? Goal 3 of Strategic Plan:**
 - Promote Understanding of Energy Market Operations and Technologies
 - Assure Pro-Competitive Market Structure and Operations
 - Remedy Individual Market Participant Behavior as Needed to Ensure Just and Reasonable Market Outcomes
- **OMOI and MMUs are Strategic Partners to Ensure**
 - There is a Cop on the Beat
 - The Cop Understand the Beat

Conclusion

- Where are We Now?
 - Much Better Off than 18 Months Ago
 - But a Long Way to Go
 - Curious Situation
 - Markets On the Ground in Many Areas
 - But Public and Political Backing Unclear
- Where are We Going?
 - Strong, Transparent, Regional Markets You Can Rely On
 - Market Power Under Control
 - Market Interventions Known Beforehand
 - Pricing that Reflects Value of
 - Time
 - Location
- ***This Matters to You and You Matter to Us***
 - ***Good Markets Make Investment Feasible***
 - ***Good Investment is Vital to Electric Markets***