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FEDERAL ENERGY REGULATORY COMMISSION

January 26, 2005

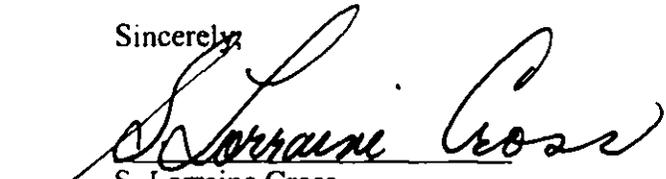
Ms. Magalie Salas
Secretary
Federal Energy Regulatory Commission
888 First Street, N.E.
Washington, D.C. 20426

Re: *Market Based Rates for Public Utilities*
Docket No. RM04-7-000.

Dear Ms. Salas:

Attached for filing is the Statement of Tractebel North America submitted for the Technical Conference of January 27, 2005 in the above captioned proceeding.

Sincerely,


S. Lorraine Cross
Attorney for Tractebel Energy Marketing

cc: All Parties on the Service List

Attachments

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**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

FEDERAL ENERGY
REGULATORY COMMISSION

Market Based Rates for Public Utilities)

RM04-7-000

**TECHNICAL CONFERENCE
STATEMENT OF TRACTEBEL NORTH AMERICA
January 27, 2005**

Robert D. Stibolt is Senior Vice President Strategy, Portfolio & Risk Management for Tractebel North America ("Tractebel" or "TNA"). Tractebel is honored to participate in this proceeding. Tractebel North America owns, operates and develops combined cycle turbine generation, qualifying cogeneration facilities and liquefied natural gas facilities in North America. It is a division of Suez-Tractebel S.A., a global energy and environmental services company.

One of Mr. Stibolt's responsibilities at TNA is forecasting the competitive dynamics of electricity markets in North America, including forecasting capacity value and energy prices in regional markets. The forecasting models Tractebel uses for investment decisions and reports to executive management are premised on competitive markets. TNA's modeling of ERCOT, PJM and NEPOOL – the regional markets Tractebel is most active in – closely agree with the results forecasted for a competitive region. In practice, Tractebel's experience has been that events at Tractebel plants, specifically forced outages, have had no measurable effect on market prices that one could determine through correlation studies. This result is not surprising as Tractebel has a market share significantly below 20%.

Tractebel has not studied alternative proposals for measuring generation market share, but the Commission's interim screens (20% market share and pivotal supplier tests) appear to be reasonable and workable. Power generation does not necessarily have economies of scale and should evolve to look, in many ways, like the natural gas E&P business in which the largest North American producer has something on the order of a 7% market share. It is desirable to have a relatively dispersed and competitive supply structure.

Mr. Stibolt's panel has been asked to address how best to define the geographic scope of electricity markets outside of RTOs or ISOs, and whether the Commission should analyze the competitiveness of the market rather than whether individual firms have market power.¹ Generally, the extent of the relevant market outside an RTO or ISO

¹ Market Based Rates for Public Utilities, *Supplemental Notice of Agenda for Technical Conference*, Docket No. RM-44-7-000, (January 21, 2005).

is somewhat ambiguous, but probably best defined by measuring the boundary at which export/import flows are at a minimum or fall below some threshold such as the largest single contingency for operational planning. This region is most likely to be larger than a control area but smaller than an entire NERC region.

More specifically, panelists were asked to address the following questions:

- a. What are the advantages and disadvantages of using a regional market approach? What would be required to implement it?

On May 13, 2004, the Commission issued an Order Implementing New Generation Market Power Analysis and Mitigation Procedures, referencing numerous dockets for market-based rate generating resources. The Order required generators to file interim market-power analyses in 6 separate tranches. We suspect that the Commission staff may be having trouble analyzing this data because the applicants were not required to use standard formats – thus the filings are not comparable. Tractebel respectfully suggests that the problem is NOT the lack of a regional market analyses, it is the inability to compare data filed by different parties. The solution to this problem is to develop a standard set of data requests.

- b. What factors should be considered at the screen stage to demonstrate that the relevant geographic market is broader than a control area?

A price premium occurring at a node within a transmission network should not be confused with market power nor viewed as evidence of the exercise of market power. While regional demand for power may be relatively inelastic, nodal demand for power will tend to be elastic in light of multiple possibilities for substitution of power from other sources within the network. This effect and its competitive benefits can be amplified by assuring that transmission systems are adequately maintained and upgraded. In non-RTO/ISO real time markets, it is highly unlikely that any seller with less than a 20% market share could effectively game the system given the opaqueness of the transmission system's operation.

One measure of an import/export limit at a control area boundary is the largest single operating contingency.

- c. What elements do buyers believe are necessary for a market to be competitive?

Locational installed capacity markets (LICAP) or regional unforced capacity markets (UCAP) address buyers' concerns about absolute scarcity. These capacity requirements ensure that a load serving entity can procure sufficient electricity from generators with access to network transmission. An analogy can be drawn from natural gas markets – local distributors of gas (LDCs) are required to hold firm transportation and then procure supplies from the competitive supply market. Since the 1980s, we've learned what a bad idea it was for LDCs to be tied to certain gas supplies and what a terrible idea it would have been to put those gas supplies into the rate base.

- d. Can a competitive market finding be compatible with a finding that competitors possess market power?

Yes, provided that the sources of market power are identified and their adverse impacts mitigated. However, a market that mixes regulated and competitive participants within the same component of the value chain is difficult to regulate. Therefore the preferred solution is still to evolve towards a fully competitive solution. A fully regulated solution is sub-optimal. The social deadweight cost of monopoly is not reduced just because a government-regulated entity is the monopolist. The social opportunity cost of capital is not reduced just because a government-regulated entity is the investor. FERC's continued move towards competitive markets is wise policy.

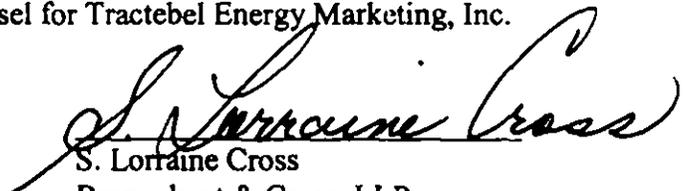
- e. If a region is found to be non-competitive, how will the interests of buyers and sellers that do not possess market power be protected?

Create day ahead and real time markets to buy/sell electrical energy and operating reserves that use a theoretically and empirically sound bid auction mechanism. Competitive sellers could participate in the auction at market-based rates and sellers with market power could participate at cost-based rates. The auction mechanism is necessary to prevent the monopolist from making forced sales of imbalance energy and other ancillary services.

- f. What types of generation market power mitigation should the Commission consider besides cost-based rates?

Cost-based rates alone are insufficient to remedy market power when the monopolist is vertically integrated. Structural reforms are necessary such as access to a day ahead and real time market to buy/sell electricity and operating reserves for participants that are not part of the vertically integrated chain. These markets can be structured to pay the sellers according to a theoretically and empirically sound auction mechanism. Sellers with generation market power would bid cost-based rates and sellers authorized to sell at market-based rates would follow the protocols appropriate for a fully competitive market. The cost-based rate participants should have the same appearance as any other market-based rate competitor to market-based rate participants.

This statement was submitted by Counsel for Tractebel Energy Marketing, Inc.


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January 26, 2005