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Address to the Federal Energy Regulatory Commission's
Conference on Competition in Wholesale Power Markets

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Good Morning. My name is Gordon van Welie. I am the President and CEO of ISO New England, the Regional Transmission Organization serving the six New England states. I appreciate the invitation to contribute to this important discussion.

Competition was implemented to provide a sound framework to reduce costs, promote private investment in wholesale electric resources, and better manage consumption to achieve the stated public policy goals of reliable and reasonably priced electricity for consumers. ISOs and RTOs are well suited to guide this change with independence and transparency. While there is strong evidence markets have met the intended policy objectives, assessments of the efficacy of these new markets vary widely. Critics are singularly focused on the recent increase in electricity prices, but those who blame competitive markets for high prices misunderstand their function and the real drivers of price increases.

Competitive wholesale markets are a means to an end, not an end to themselves.

Markets are essentially barometers, measuring the relative strengths and weaknesses of the electricity system and providing an efficient way to value the alternatives available to consumers and policy makers. Rising electricity prices are not the result of the markets, but are the result of price increases in the inputs, such as fuel, needed to produce electricity.

These price signals tell developers to invest. They help direct consumers to use more or less electricity and they ultimately prompt the development of solutions to improve the efficiency, competitiveness, and reliability of the system.

With this in mind, competitive markets should be seen as a catalyst for achieving important national and regional policy objectives to the benefit of consumers. There is mounting evidence demonstrating the value of organized markets. The qualitative benefits of RTOs and ISOs speak for themselves—namely, fair and independent markets, guaranteed open access, improved power system planning, greater grid reliability, and superior system coordination and management. The quantitative benefits are equally compelling. Studies evaluating the result of competition fostered by organized electricity markets demonstrate substantial efficiency gains at the wholesale level and considerable progress with respect to investment in needed infrastructure. To illustrate, I will use a few examples from New England.

Despite concern about rising retail electricity bills, when you factor out the increases in natural gas and oil prices, which together fuel more than 60% of supply in New England, wholesale electricity prices have dropped since 2000. This reduction results from competitive market forces, which have driven investment in more than 10,000 megawatts of new supply and improved generator availability from 81% to 89% since the beginning of markets.

Since private firms and not public utilities have made this new investment, consumers have been shielded from the investment risks they had been exposed to under a traditional cost of service system. This consumer protection was a major objective of restructuring in New England where billions of dollars in stranded costs had accumulated from poor investment decisions.

A comprehensive regional planning process and a stable cost recovery mechanism have improved the investment climate for transmission. After decades of relative inertia, five bulk transmission projects valued at more than \$2 billion are in various stages of construction and a sixth, multi-state project is being planned. In addition, we are investigating stronger ties with Eastern Canada.

For overall capacity needs, the region's planned auction-based Forward Capacity Market in 2008 will ensure resource adequacy by purchasing the resources needed to serve growing demand. Early indicators suggest investors are confident in our marketplace, with over 10,000 megawatts of new generating resources indicating interest, particularly in our highest demand centers of Massachusetts and Connecticut.

Wholesale market improvements have boosted demand response participation. We now have almost 1,000 megawatts of demand response assets, which provide the dual benefits of lowering prices and ensuring reliable operations. It is unlikely we would have achieved this level of participation in the absence of competitive wholesale markets.

We expect markets to enable the integration of initiatives as prescribed by the Federal Energy Policy Act of 2005 and the Regional Greenhouse Gas Initiative, or RGGI. While electricity markets can help further RGGI's environmental policy objectives, RGGI can likewise help the electricity markets achieve their policy objectives. The RGGI compact is designed to stabilize and ultimately reduce carbon dioxide emissions through a cap-and-trade system. If the proceeds of the proposed "cap-and-trade" auction are used to develop 'clean' resources such as energy efficiency resources, demand response, and alternative fuels, then RGGI will help diversify the region's fuel supply, as well as help meet New England's projected capacity needs. We believe there is a need to consider the potential convergence of RGGI, the regional Renewable Portfolio standards, and the wholesale markets. This coordinated development is the next stage in the evolution of wholesale markets in the region.

New England has taken an important step toward the full integration of demand response and energy efficiency into the wholesale markets with the planned Forward Capacity Market. We are not naive about the difficulties of treating demand response and energy efficiency as the equivalent of supply-side resources. It has never been tried before on this scale and there are many complexities and risks involved to make it work. But, it is also an untapped resource. Given the limited resource alternatives available to the New England region, and the reluctance to allow the siting of non-gas resources, it is essential that demand-side resources be pursued through a variety of mechanisms, including the competitive market.

Regional policy makers often ask, "What can be done to get the price of electricity in New England more in line with the national average?" The answer is to control peak demand growth and site resources that use a fuel other than natural gas or oil. Both of these solutions are easier said than done. Nevertheless, I believe markets are the most powerful tool we have available today for making problems visible and, ultimately, addressing them.

NIMBYism is a powerful force to overcome. Local politics can make it impossible for state authorities to make decisions. For example, natural gas power plants are typically the easiest to site because of low emissions, but New England has become over-reliant on it. This leaves the region with a choice to either accept alternative fuels, like new clean coal and nuclear or site LNG tanks and natural gas pipelines, but neither option has been embraced.

Controlling costs becomes even more difficult because of the current gap between the wholesale and retail markets. If we hope to harness the potential of consumer conservation to lower costs and protect reliability, it is essential wholesale market signals reach retail customers. The structure – or lack thereof – currently in place between the two markets generally precludes this. Although there is a concern on the part of many about exposing retail customers to price volatility, consumers are capable of adjusting. Education about the benefits of this change will be critical to its success.

Today's forum underscores the importance of having broad expertise within the Commission to appreciate the interplay of all the issues before us and, in particular, in emerging areas such as the integration of demand response, renewable resources, and the impacts of constraints on carbon emissions.

To educate industry representatives and government stakeholders on the implications of different resource choices in the region, ISO New England has initiated a stakeholder process called Scenario Analysis to examine the reliability, economic, and environmental performance of a range of long-term resource alternatives for the region. The goal is to provide policy makers and consumers with the information they need to make choices about their future power system.

In conclusion, I urge FERC and conference participants to think of competitive markets as a tool for meeting some of the most difficult energy policy objectives facing the industry. Evidence suggests that organized markets are working and should be the appropriate path forward to achieve the goals of reliability, energy efficiency, demand response, and the integration of renewable resources in the most efficient manner possible. I challenge others to explain alternative mechanisms that would be as effective or efficient in reaching these goals. Thank you.