

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

Centralized Capacity Markets in  
Regional Transmission Organizations and  
Independent System Operators

Docket No. AD13-7-000

**Prepared Statement of Richard B. Miller  
of Consolidated Edison Company of New York, Inc.**

Good morning Mr. Chairman and Commissioners. I am Richard B. Miller, Director of the Energy Markets Policy Group at Consolidated Edison Company of New York (Con Edison) and am here this morning representing Con Edison and its regulated affiliate, Orange & Rockland (O&R). I commend the Commission for hosting this timely conference on centralized capacity markets in RTOs/ISOs. I am pleased to be here to discuss capacity market design elements and their contribution to achieving the centralized markets' goals of providing reliability at a reasonable cost.

Con Edison provides electric service to around 3.3 million customers in New York City, and most of Westchester County, an approximately 660 square mile service area. O&R provides electric service to 301,000 customers in southeastern New York and adjacent areas of northern New Jersey and eastern Pennsylvania, an approximately 1,350 square mile service area. We are committed to supporting competitive energy markets and have divested all of our electric generating facilities, other than about 700 MW of mostly cogeneration units that also produces steam to serve Manhattan steam customers. We also provide our customers with the choice to buy electricity from other suppliers –approximately 58% of our delivery customers' capacity purchases are from a supplier other than Con Edison.

We have been active participants in the NYISO and PJM wholesale electricity markets, and believe that a capacity market is a necessary component of such markets. It benefits reliability by assuring that capacity is available to meet peak customer demand, provides needed compensation to suppliers, and also provides a price signal for the entry and exit of resources. Capacity markets have been supportive of both conventional generation as well as demand response. Con Edison strongly believes that competitive capacity markets are an appropriate structure, and moreover, that in an environment where supplier competition exists, it is necessary. Alternatives, such as requiring regulated utilities to enter into long-term contracts with generators, do not work well in such a competitive structure. Such contracts do not allow competitive suppliers to take on the potential risks and rewards of providing new resources.

The Commission Staff Paper on Centralized Capacity Markets (“Staff Paper”) correctly notes that central capacity markets were implemented by eastern RTOs/ISOs to create a market mechanism to provide more lead time and certainty for investment in new resources to help ensure resource adequacy. Early on, they were also identified as a means for units to have a reasonable opportunity to recover their costs over the long run. We believe that the markets’ experience in the three eastern ISOs/RTOs have now yielded sufficient information to identify the minimum, best-practices that are characteristic of a competitive and well-functioning capacity market. To this end, we urge the Commission to consider a minimum level of standardization in the capacity markets, as you have done for transmission planning, which would lead to greater regulatory stability for capacity markets and aid in realizing inter-regional benefits.

## **Capacity Market Effectiveness**

In order for capacity markets to meet a region's resource needs, such markets should provide, together with energy and ancillary service markets, sufficient revenue over the long-term for the development of new resources, and compensation for needed existing resources. Capacity markets must also provide developers with advance price signals that account for (a) the lead time necessary to develop resources; (b) investor time horizons; and (c) region-wide and locational capacity requirements. Further, an effective capacity market provides developers with incentives to build needed or more efficient resources when there are no barriers to new entry and when they are able to access neighboring markets through standardized capacity products. The markets can also provide information for reliability planning purposes when units fail to clear.

We believe that capacity markets are most effective when resources are procured in advance of when they are expected to deliver energy. Capacity is not a short term product. It is a longer term product that is primarily geared to providing reliability at a just and reasonable cost. An advance auction provides a better opportunity for the entry of new resources, because it helps to avoid the short-term price volatility that could otherwise result between the decision to develop and commercial operation. We also note that it appears that new resources are more likely to be built based upon capacity market revenues when the commitment period duration is at least one year (multi-year commitments should also be considered for new resources). A longer term market helps to provide a level of price stability that improves a new resource's ability to secure financing. It can also provide more certainty for reliability and information for reliability planning. Recent experience has demonstrated the benefits of

forward auctions and one-year commitment periods. The PJM market has attracted in excess of 4,000 MW of new generation (excluding demand-side resources or imports) in each of the last two auctions representing more than 3.5% of the forecast peak, while the NYISO market that utilizes a 6 month forward structure has seen an increase of less than 675 MW (or around 1.7% of the peak) over the last two years. Also, PJM has noted that its forward capacity market has provided it with needed information to help it plan for generator retirements that are the result of Federal and State clean air requirements.

In short, Con Edison believes that this is an area that merits consideration for standardization, whether it is the 3-year forward market design in PJM and New England, or another period that could be reasonably justified as a new standard.

### **Capacity Market Efficiency**

A key design element of the capacity markets is the establishment of a demand curve that estimates the value of reliability by balancing reliability needs with customer costs. The driver of the demand curve, particularly for sloping demand curves, is an administratively determined Cost of New Entry (CONE) of a new reference resource that would be built to meet a reliability need. The CONE has typically been based on combustion turbine technology because a peaking resource is most likely the one to be added to maintain reliability.

But, the capacity markets do not result in a peaking unit, and recently a new unit is more likely to be one that can earn more energy and ancillary services revenues. Capacity markets are most efficient when the proxy technology used in the determination of the CONE is based on (a) the most cost-effective contemporary

technology, which in some regions today is the combined cycle technology and, (b) the recent experience with actual new capacity resources that are being proposed or built. We urge the Commission to develop a standardized process defining attributes of a proxy resource in a manner that accommodates technological flexibility. We note that the Commission has previously agreed with the NYISO's view [in 134 FERC ¶ 61,058 at ¶25, 37 (2011)] that the proxy unit should be a "reasonably large scale, standard generating facilit[y]." The proxy unit, however, should not be limited to a generating facility. The definition should be flexible enough to include the most appropriate marginal resource in a region, which could also include demand response in the future.

Maintaining a static definition of technology in the face of new realities would result in a distorted, backward-looking capacity market designed to meet future reliability needs and would not meet the demand curve goal of balancing customer and investor interests. The Staff paper correctly notes that "[a]s the mix of available resources changes in response to market conditions and state and federal policies, the assumptions used to determine the CONE value may become more critical considerations for ensuring that centralized capacity markets provide appropriate price signals for capacity resource investment when needed."

### **Capacity Market Buyer Mitigation**

All three eastern capacity markets have rules designed to prevent buyers and sellers with market power from affecting capacity prices. NYISO has had seller mitigation in NYC since the market's inception. The Commission has also instituted buyer-side mitigation rules, and those rules are evolving. In PJM, the Commission recently approved reforms that provide categorical exemptions for classes of resources,

such as competitive entrants and renewable resources, which have no intent and ability to suppress capacity prices. The NYISO rules currently require a minimum offer price for *all* developers of new capacity, including competitive entrants, unless the developer can demonstrate that its facility is economic based on the NYISO's assumptions. As has been pointed out by the NYISO's market monitor, this does not promote competitive markets. For example, a developer should be allowed to go forward and build a new facility without the risk of being subject to mitigation as long as it is making its decision based on its competitive market view. The developer may have varying short and long-term market views which may be different from the NYISO's assumptions, for example, as to whether existing generating facilities will retire or not.

We believe that a competitive exemption targeted at projects that are not built by or under contract with utilities or state agencies presents no concerns of unwarranted price suppression and should not be subject to buyer-side mitigation. We also believe that a standardized exemption for competitive entry would enhance the ability to attract new resources because developers would not be discouraged by an overbroad buyer-side mitigation rule, and instead would know that they would have an opportunity to collect capacity market revenues. Further, such an exemption will allow an ISO/RTO to focus limited resources on subsidized entrants by eliminating the need to scrutinize every new entrant.

In addition, exempting renewables from buyer mitigation would be appropriate as development of renewable resources is not aimed at, and unlikely to result in, capacity market prices below competitive levels, and therefore the exemption would be supportive of overall energy policies and consistent with Order 1000's determination

that transmission planning can consider public policy. Finally, we note the exemption for self-supply adopted in PJM and that it should also be considered for an exemption. We believe having such standards for exemption across all ISO/RTO capacity markets will make it easier for new resources to be developed, and to participate in regional and inter-regional markets.

### **Capacity Markets and Changing Resource Mix**

The Commission has asked whether there is a need for new capacity market products with specific operational characteristics such as fast-ramping or load-following ability given the increase in variable and intermittent resources. Currently, energy and ancillary service markets account for some operational differentiation; through, for example, additional compensation for faster regulation or scarcity pricing for fast-start or fast ramping resources.

We believe that capacity markets must retain their focus on providing a competitive price signal for new resources in general and specific operational attributes should be compensated through the energy markets. Additional segmentation of the capacity markets could (a) contribute to increased volatility from diminished liquidity and (b) introduce additional complexity into the reliability construct underlying the current market design without comparable reliability or operational benefits. Moreover, we do not believe that this is an area where standardization would be appropriate, at least not at this time. Each ISO/RTO would potentially have its own special resource needs based on the particular resource mix that it encounters in its region. For example, the NYISO's wind integration study found that its system could accommodate up to 8,000 MW of wind –New York currently has 1,600 MW -- with only a need for an additional

225 MW of regulation service to deal with short term system variability. We do not envision a need for a special capacity product in the NYISO due to an increase in wind. We understand that California's experiences are different, and we accordingly believe that flexibility in approach should be allowed.

### **Capacity Markets and Transmission**

The Commission asks whether more can be done to integrate transmission planning with capacity markets. In this regard, we believe that it would be beneficial if the conditions under which capacity zones are created and eliminated were standardized. Zones can play a significant role in capacity pricing, contributing to price volatility for both customers and investors. There is currently regulatory uncertainty due to differences in how zones are created and eliminated. This is another area where the market could benefit from a degree of standardization.

Thank you again for the opportunity to participate in this conference today and I look forward to our discussion.