

**PERSPECTIVE AND PROPOSALS CONCERNING
INTEGRATING MARKETS AND PUBLIC POLICY**

This Statement of Position is submitted on behalf of the
Eastern New England Consumer-Owned Systems:

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I. INTRODUCTION

The three plenary sessions conducted thus far – on August 11, August 30 and September 14 – have produced a number of proposals for the creation of new, ISO-administered, centralized auction pricing, single purchaser constructs for the region-wide procurement of renewable and carbon-free generating resources. Four principal constructs have been proposed, typically with elements in common: (1) carbon “shadow pricing” or a carbon “tax”; (2) a Forward Clean Energy Market (a centralized, forward procurement auction for unspecified quantities of carbon-free energy); (3) a Carbon Integrated Forward Capacity Market (the familiar FCM, combined with a “Zero Emission Credit” or “ZEC” product with additive pricing); and (4) one or more two-tiered pricing constructs that would be superimposed on either the current FCM or some future FCM with a no-carbon component.¹

No cost allocation mechanisms have been discussed explicitly. The cost allocation mechanism generally associated with such procurement and pricing constructs is some variation of all-load-pays. This kind of approach would be difficult to reconcile with NESCOE’s June 21, 2016, Goal Post “E” – “Consider mechanisms to ensure consumers in any one state do not fund the public policy requirements mandated by another state’s laws.”

One foreseeable result of the adoption of any of these proposals would be the introduction of an argument that, by accepting an ISO-administered, single buyer, centralized auction procurement construct, under a FERC-regulated tariff, the New England states have “turned over the keys” for regulating renewable generating resources procurement to the FERC. Without accepting that argument, it is worthwhile to examine the consequences of introducing it on the ability of the six

¹ Representatives of the Alternative Energy Resources Sector have proposed a fifth construct: installing battery storage at PTF substations and recovering the costs of the batteries and related equipment through Regional Network Service (“RNS”) rates. Storage operates more like a generating resource than like a transmission resource, and is more likely to be effective at load-serving and improving reliability if it is located behind the retail meter. For this reason, storage is more appropriately treated as a capacity and energy resource and more appropriately priced by competitive market conditions than treated as a fixed cost subject to cost-of-service cost recovery. This is particularly true given that RNS transmission service currently costs \$103 per kW-year and is predicted to continue to increase at a steady clip for the foreseeable future – without adding the cost of battery storage.

New England states to control their progress toward a lower carbon future. Laying a foundation for arguing that policy decision-making on renewable generating resources procurement has been shifted from Hartford, Providence, Boston, Montpelier, Concord and Augusta to Holyoke is a major step. The people who are actually empowered to take that step – the legislative and executive authorities of the six States – have given no indication that it is one they are prepared to entertain. Nor, in reality, is the animating principle behind renewable procurement mandates, the protection and promotion of the public health and welfare in the six New England states, one that ISO New England is empowered to pursue or prepared to undertake.

On a more local level, all of the proposals advanced thus far in this process offer New England’s consumer-owned utilities something that they neither need nor want – higher costs and yet another centralized, single-buyer auction to acquire resources that they can and do acquire quite capably on their own. The same rationale that justifies exempting consumer-owned utilities from cost support for the NEPOOL Generator Information System would require exempting them from the various new “market” proposals advanced to date in the IMAPP process. Unfortunately, history here and elsewhere demonstrates that accommodation of different business models tend to be transitory, at best.

Against these considerations, proposals to create and impose new single-buyer, centralized auction, all-load-pays procurement constructs fall short of providing a constructive path for the integration of the ISO-NE administered “market” system and the public policy objective of a lower-carbon future. An alternative approach, under which ISO-NE market rules are revised as necessary to accommodate state-mandated renewables procurement is more likely to provide a durable and effective means of “integrating markets and public policy” than attempts to impose new product definitions, new costs and new complications in an already over-complicated system. Elements of such an alternative approach could include the following, among others:

- (1) targeted revisions to the ISO-NE ancillary services procurement, designed to make ISO-NE’s existing ancillary services procurement structures, particularly for regulation and reserves, more accessible to variable energy, carbon-free, resources;
- (2) revisions to the Forward Capacity Market rules to accommodate capacity bidding by storage resources (batteries, flywheels, pumped storage hydro and other forms of chemical and mechanical energy storage);
- (3) introduction of a hybrid capacity product combining (i) a renewable, carbon-free resource and (ii) a firming component

to manage intermittency and substantially mitigate risks of incurrence of Pay-for-Performance penalties that may present an obstacle for intermittent resources; and

- (4) targeted and carefully phased procurement of fast-start/fast-ramp generation needed to manage the intermittency of the most abundant forms of zero-carbon generation in New England (wind and solar).

It is also possible that some revision to the price formation mechanics of ISO-NE's existing centralized auction, single-buyer constructs may (or may not) be needed in order to permit those constructs to operate in parallel with large-scale, state-mandated resource acquisitions. The "two-tiered" pricing proposed thus far assumes that such acquisitions are subject to ISO-administered procurement. The jurisdictional argument that would follow from that step makes it unsound to subject state-mandated renewable resource acquisitions to ISO-administered procurement. A preferable solution would be to address the question of price impacts of state-mandated renewable resource acquisitions by simply removing the reliable capacity value of the state-mandated resources from the supply stack, and simultaneously removing an associated amount of demand from the calculation of the regional Installed Capacity Requirement. This should leave the ISO auction pricing function unaffected, while allowing the state-mandated acquisition to operate as intended, unencumbered by jurisdictional arguments.

Any of these modifications could be implemented in the relatively near future. The major procurements directed under the Massachusetts Energy Diversity Act (H. 4568) are not scheduled to be contracted until June 30, 2022 (9,450 million MWh of clean energy, as defined in the statute) and June 30, 2027 (1,600 MW of off-shore wind capacity), respectively. The urgency of Participants Committee voting on "framework documents" by December 2, 2016, may be driven by RFP dates in the recent Massachusetts legislation (or by other considerations). But the actual "integration" of the resources envisioned by that legislation seems far enough in the future to permit a more measured approach to preparing for their arrival.

II. SOME PRACTICAL CONSIDERATIONS

Those who have relied on RTOs to as agents of implementation for state policies have been frequently and severely disappointed.² This is largely because the RTOs' embrace of "market-driven" (more accurately, bid-based pricing driven) outcomes ultimately conflicts with the non-economic considerations that drive state-mandated renewable resource acquisition. As the Publicly-Owned Entities Sector has pointed out from the start of this discussion, the role that ISO-NE has assumed in Section 2.3 of the Participants Agreement simply does not encompass the implementation of state policies concerning renewable resources or de-carbonization of the regional generating portfolio. Attempting to forcibly superimpose "market-driven" outcomes on acquisition requirements that are not economically driven (at least in the near term) is a futile exercise, and ultimately a destructive one.

The sound and workable path toward integrating markets and public policy is a less drastic and more feasible approach: ensuring that the market rules and structures can either accommodate or, preferably, work around state-mandated resource acquisitions. This approach could avoid much of the divisive jurisdictional argumentation, as well as a great deal of unnecessary effort in pursuing complicated efforts to superimpose centralized auction, single-buyer design constructs on a field of procurement that they fit poorly. Put another way, the only tool is not a hammer, and not every problem is a nail.

A. State and Federal Jurisdiction under the FPA

Efforts to expand the RTO mission into areas that have traditionally been the function of the states, particularly the promotion and protection of the public health and welfare, present an array of consequences that are both unforeseen and irretrievable. In earlier stages of the electric power industry's organizational evolution, it was been said that in Section 201(b)(1) – the FPA's central jurisdictional provision – "Congress meant to draw a bright line easily ascertained, between state and federal jurisdiction . . . by making FPC jurisdiction plenary and extending it to

² See, e.g., *New Eng. Pwr. Gen. Assn. v. FERC*, 757 F.3d 283, 295 (D.C. Cir. 2014) ("FERC made the judgment that encouraging renewable energies was less important than allowing such out-of-market entrants to depress capacity prices. Such is FERC's prerogative. That it is unfortunate does not make it arbitrary"); *N.J. Bd. of Pub. Utils. v. FERC*, 744 F.3d 74, 102 (3rd Cir. 2014) ("It is more than mildly disturbing that, by endorsing a state-mandated exemption with perfectly predictable incentives, FERC would allow sovereign states and private parties to be drawn into making complex and costly investments, only to later pull the rug out from under those who were persuaded that the exemption was somehow real. That FERC has done so based on little more than the claim that the agency had an 'ah ha' moment when foreseeable outcomes approached fruition only makes matters worse. Our power to rein in bureaucratic behavior like this is, however, constrained").

all wholesale sales in interstate commerce except those which Congress has made explicitly subject to regulation by the States.”³

RTO-administered markets have tended to blur that “bright line” because FERC’s jurisdiction also extends to rules, regulations, practices and agreements that “affect” FERC-jurisdictional rates.⁴ The combination of the breadth and complexity of RTO-administered markets and FERC’s authority over matters “affecting” rates has led to jurisdictional conclusions that can be counterintuitive. Thus, for example, the decision of a retail customer not to consume electricity can be subject to FERC jurisdiction because it can “affect” rates in RTO-administered markets. *FERC v. Elec. Pwr. Supply Assn.*, 577 U.S. ___, 136 S. Ct. 760, 774 (2016). For another example, an order of a state public utility commission directing retail distribution companies to enter into an agreement with a power plant developer to hedge their costs in an RTO capacity market is preempted by the Federal Power Act “because it disregards an interstate wholesale rate required by FERC.” *Hughes v. Talen Energy Mktg., LLC*, ___ U.S. ___, 136 S. Ct. 1288, 1299 (2016).

Counterintuitive results are compounded by imperfect foresight. It is easy for a federal appellate judge to remark, as one did in an earlier stage of the case that became *Hughes v. Talen Energy Mktg.*, that “Maryland’s decision [abandon the vertical integration model and] to participate in the federal scheme and enjoy its benefits was necessarily accompanied by a relinquishment of the regulatory autonomy the state had formerly enjoyed with respect to traditional utility monopolies.”⁵ There is no evidence that the Maryland General Assembly ever actually gave the matter much thought when it enacted restructuring legislation in 1999, and Judge Wilkinson’s “relinquishment” announcement certainly came as a surprise to the Public Service Commission when his decision issued in June 2014. The fact that the Supreme Court upheld the conclusion, if not the quote, came as an even greater surprise.

³ *FPC v. So. Cal. Edison Co.*, 376 U.S. 205, 215-216 (1964).

⁴ 16 U.S.C. § 824d(a) (“All rates and charges made, demanded, or received by any public utility for or in connection with the transmission or sale of electric energy subject to the jurisdiction of the Commission, and *all rules and regulations affecting or pertaining to such rates or charges* shall be just and reasonable”) (emphasis added); 16 U.S.C. § 824e(a) (“Whenever the Commission . . . shall find that any rate, charge, or classification, demanded, observed, charged, or collected by any public utility for any transmission or sale subject to the jurisdiction of the Commission, *or that any rule, regulation, practice, or contract affecting such rate, charge, or classification* is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order”) (emphasis added).

⁵ *PPL EnergyPlus, LLC v. Nazarian*, 753 F.3d 467, 473 (4th Cir. 2014).

The New England states litigated successfully to establish the authority of the Environmental Protection Agency to regulate greenhouse gasses,⁶ and organized the Regional Greenhouse Gas Initiative (along with New York and certain Mid-Atlantic states) in the absence of any organized federal response to global warming. The suggestion that those states ought to “turn over the keys” to renewable generating resources procurement to a system that is the creature of federal regulation seems pretty far off-key, particularly in light of the predictable and unpredictable consequences of doing so. Consider, for example, whether any of the proposals introduced in the IMAPP discussions to date for carbon “shadow pricing” could coexist with the present Regional Greenhouse Gas Initiative, and which might be required to give way in the event that a disappointed market participant were to prevail in a federal preemption argument.

B. Consumer-Owned Utilities and State Renewables Procurement

The implementation of renewable generating resources procurement (or other forms of financial support) by consumer-owned utilities has, by law and by custom, been a function generally delegated to local policy makers selected by the consumer-owners of those utilities. Even in those New England states that do not leave carbon reduction in generating resource procurement to the autonomous discretion of consumer-owned utilities, state law accommodates the consumer-ownership business model in renewables acquisition.

This model of accommodation tends to place smaller, consumer-owned utilities in the market for smaller, more geographically diverse, and self-supplied renewable resources. Municipal systems as diverse as Stowe, Vermont, Sterling, Massachusetts, and Hull, Massachusetts (to give but three of many examples) have made significant and successful investments in local renewables projects that now serve significant portions of their loads. What treatment would await these investments in a centralized auction, single-buyer, all-load-pays procurement construct? Historical experience with self-supply in the Forward Capacity Market does not provide much reason for optimism.⁷ In order to be viable, integration of markets and public policy needs to: (1) respect and acknowledge both the existing and future levels of autonomous investment by consumer-owned utilities in renewable resources, at the direction of their local governing bodies; and (2) ensure against the duplicative imposition of costs.

⁶ *Massachusetts v. United States*, 549 U.S. 497, 528-534 (2007).

⁷ In 2011, at the urging of ISO-NE and various supply-side interests, FERC eliminated the self-supply feature that had been the bedrock principle behind public power’s agreement to the original FCM settlement in 2006, based on stated concerns that self-supply could cause “price suppression” in the FCM. *ISO New England, Inc.*, 135 FERC ¶ 61,029 (2011), *reh’g denied*, 138 FERC ¶ 61,027 (2012).

Experience raises a further cause for concern with the proposals brought forth so far in the IMAPP process. Even if those proposals had contained elements accommodating existing and future autonomous investments by consumer-owned utilities, experience show that any such accommodation is only as durable as the next FPA Section 205 proceeding by ISO-NE or a Section 206 proceeding by another market participant (or FERC itself) to modify or eliminate it. The ephemeral nature of any “accommodation” extended at the initial extension of a centralized auction construct ought to give the New England states pause as they consider the current array of proposals in this process. Simply put, given the emerging law on RTOs and federal preemption under the Federal Power Act and our own past experiences (particularly in the 2011-2012 “reforms” for the FCM), we are unable to envision a legal structure that would provide an appropriately durable assurance for the continuity of the authority of the New England states (and their political subdivisions) over renewables acquisition.

For these reasons, in addition to concerns about the erosion of state autonomy in establishing renewable energy policy, proposals for new centralized auction constructs for renewables acquisition offer New England’s consumer-owned utilities a solution they do not need for a problem they do not have.

III. ALTERNATIVES

As suggested earlier in this position statement, we believe that an alternative approach to integrating markets and public policy – one that does not contemplate the imposition of a centralized auction, single-buyer construct on state-mandated renewable resource acquisitions – offers a more durable and effective way forward than the proposals advanced to date in this process. We specifically suggest the following four market design modifications and, recognizing the possibility that state-mandated renewables acquisitions could impact the price formation process in ISO-administered markets, suggest a least-intrusive adjustment to deal with that possibility. These proposals by no means define the universe of accommodations available to accomplish a real integration of markets and public policy, as opposed to a subversion of one by the other. But they do represent a worthwhile start.

The four proposals for rule modifications are:

- (1) targeted revisions to the ISO-NE ancillary services procurement, designed to make ISO-NE’s existing ancillary services procurement structures, particularly for regulation and reserves, more accessible to variable energy, carbon-free, resources;
- (2) revisions to the Forward Capacity Market rules to accommodate capacity bidding by storage resources (batteries,

flywheels, pumped storage hydro and other forms of chemical and mechanical energy storage);

- (3) introduction of a hybrid capacity product combining (i) a renewable, carbon-free resource and (ii) a firming component to manage intermittency and avoid incurrence of Pay-for-Performance penalties that present a significant risk for intermittent resources; and
- (4) targeted and carefully phased procurement of fast-start/fast-ramp generation needed to manage the intermittency of the most abundant forms of zero-carbon generation in New England (wind and solar).

As also discussed above, to the extent that some adjustment of the price formation mechanics of existing ISO-administered markets is needed to facilitate their working around state-mandated renewable resource procurements, the question of price impacts of state-mandated renewable resource acquisitions is best addressed by simply removing the reliable capacity value of the state-mandated resources from the supply stack, and simultaneously removing an associated amount of demand from the calculation of the regional Installed Capacity Requirement. This should leaving the ISO auction pricing function unaffected, while allowing the state-mandated acquisition to operate as intended, unencumbered by jurisdictional arguments.