Testimony of Jackson Reasor

President and CEO - Old Dominion Electric Cooperative

Before the Subcommittee on Energy

Committee on Energy and Commerce

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"Powering America: Examining the State of Electric Industry through Market Participant Perspectives"

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Summary of Statement of Jackson E. Reasor
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- Old Dominion is a not-for-profit power supply electric cooperative that owns and operates electric generation facilities that it uses, together with long-term wholesale contracts, to "self-supply" power to its members. Old Dominion supports competition in wholesale electric markets and the ability to self-supply when we determine this is the best long-term resource option.
- PJM's wholesale energy markets are working reasonably well. Plentiful natural gas supplies and improved generation technology have driven down wholesale energy prices.
- Repeated and significant changes to PJM's capacity procurement model have raised costs and undermined the ability of load-serving entities to self-supply power.
- Federal policies should focus on reliable wholesale service at just and reasonable rates for consumers.
- Federal policies should honor and encourage long-term investments in generation by load-serving entities like Old Dominion. Consumers will fare better if competitive wholesale power markets allow load-serving entities to first self-supply the generation capacity they need, by building it or purchasing it in voluntary long-term bilateral contracts, and then turning to the RTO centralized capacity and energy markets for their residual needs.
- Federal policy should ensure that load-serving entities are able to develop the portfolio of generation resources that they believe best meets their needs, based on their economic and non-economic criteria.
- FERC and the RTOs are beginning to address needed reform to these federal policies. Congress should monitor this process, but it does not need to amend the Federal Power Act at this time.

My name is Jack Reasor. I am President and CEO of Old Dominion Electric Cooperative in Glen Allen, Virginia. Old Dominion is pleased that the Energy Subcommittee is holding this hearing and that it has been invited to present its perspective as a wholesale market participant.

Old Dominion is a not-for-profit power supply electric cooperative, organized and existing under the laws of Virginia. Old Dominion provides capacity and energy to eleven electric distribution cooperatives in Virginia, Maryland, and Delaware ("Members"). Our Members provide retail electric service to end-use consumers. Old Dominion and its Members have obligations to serve their consumer-owners. In the taxonomy of wholesale market participants, Old Dominion is a "load-serving entity."

Old Dominion also owns and operates electric generation facilities that it uses to supply power to its Members. This business model, whereby a load-serving entity like an electric cooperative also owns generation used to serve its consumer-owners, is sometimes referred to in the industry as "self-supply."

All of our Members are located within the PJM Interconnection, a large regional transmission organization (RTO). Old Dominion is a network transmission customer of PJM as well as a PJM Transmission Owner. Unlike most electric cooperatives, however, Old Dominion is subject to the jurisdiction of the Federal Energy Regulatory Commission (FERC).

Old Dominion has long supported federal policies to promote greater competition in wholesale electric markets. Old Dominion and other electric cooperatives were among the early proponents of unbundled transmission service on the interstate grid. Old Dominion supported FERC's Order No. 888, which mandated unbundled, open-access transmission service in 1996. Old Dominion welcomed the conversion of PJM into a regional transmission organization (RTO) with a single control area and single tariff, because that would ensure more economical, non-discriminatory transmission service over the entire PJM region and thus provide more wholesale supply alternatives for load-serving entities.

In short, we support vigorous competition in wholesale electricity markets. We want wholesale suppliers to compete for our business, and we want the ability to "self-supply" when we determine this resource option is the best long-run alternative. Such competition within the wholesale market is good for our Members, and good for the consumer-owners they serve.

Old Dominion's Perspectives on Current Wholesale Electricity Markets

In general, the wholesale energy and ancillary-services markets in PJM are working reasonably well for Old Dominion and its member cooperatives. The plentiful and inexpensive supplies of natural gas that have resulted from technical advances in shale gas drilling techniques, coupled with the high efficiency of modern combined-cycle gas generating units, have driven down wholesale electric energy prices. And while the resulting lower wholesale electric prices may be causing financial hardship for some participants in the industry, this is how competitive markets should work. While the PJM energy and ancillary-services markets are working well, they are not perfect. We support efforts by PJM and FERC to examine ways to improve their efficiency during certain periods. Nonetheless, we should be steadfast by allowing these competitive markets to work as designed by permitting them to send the proper signals for market exits where appropriate.

On the other hand, Old Dominion's experience with PJM's capacity procurement mechanism, the Reliability Pricing Model, or "RPM," has been mixed at best. This is not a market in the usual sense of that word: PJM does not provide an opportunity for willing buyers and sellers to enter into voluntary capacity transactions, by which load-serving entities could procure the capacity to meet their capacity obligations at competitive market prices. Instead, RPM is a complex administrative construct through which PJM procures capacity to ensure regional grid reliability on a centralized basis. PJM allocates the resulting costs to load-serving entities like Old Dominion.

FERC initially approved RPM as a residual procurement mechanism for PJM to ensure resource adequacy at the least cost. FERC stated that "after [load-serving entities] have had the opportunity to procure capacity on their own, it is reasonable for PJM to procure capacity in an open auction at a time when further delay in procurement could jeopardize reliability." But it added, "This, however, should be a last resort."[1]

The RPM annual capacity auction is still called the "Base Residual Auction." But over time, repeated and significant design changes have made RPM more complex and costly and have undermined the ability of load-serving entities to use their resources to meet their capacity obligations.

In the ten years since RPM was put in place, it has undergone continuous revisions. According to PJM, during the period from 2010 to 2016, there were 24 significant filings at FERC to revise RPM, and the 2016 Base Residual Auction was the first such auction with no rule changes from the prior year.[2] But that is small comfort, because in that prior year, FERC approved a complete overhaul of RPM into its current form, "Capacity Performance," which imposes onerous performance requirements on capacity resources. These performance requirements are simply impossible for some resources to meet and result in costly non-performance penalties.[3]

Several RPM revisions have involved its Minimum Offer Price Rule, or "MOPR." This rule is intended to mitigate buyer-side market power that would lower the auction clearing price below an administratively determined competitive price floor. In its original form, the MOPR guaranteed that a load-serving entity's self-supplied capacity resource would clear the auction

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[1] *PJM Interconnection, LLC*, 117 FERC ¶ 61,331 at P 71 (2006).

[2] http://www.pjm.com/~/media/committees-groups/committees/mrc/20160825/20160825-item-07-pjm-capacity-problem-statement.ashx

[3] *PJM Interconnection, L.L.C.*, 151 FERC ¶ 61,208 (2015), *order on reh'g and compliance*, 155 FERC ¶ 61,157 (2016), *aff'd sub nom. Advanced Energy Mgt. Alliance v. FERC*, No. 16-1234 (D.C. Cir. June 20, 2017).

and the load-serving entity would receive auction revenues at the clearing price—even if the MOPR prevented that self-supplied capacity from setting the clearing price. In 2011, however, FERC approved rule changes that eliminated the guaranteed clearing for self-supplied resources.[4] This meant that a load-serving entity's self-supplied capacity might not clear the auction, and the load-serving entity could end up paying twice for capacity—its self-supplied capacity *plus* its share of PJM's capacity costs under RPM.

In 2013, FERC approved further revisions to the MOPR, including a new, albeit imperfect, self-supply exemption.[5] But earlier this month—over four years later—a federal court vacated and remanded FERC's approval of this new self-supply exemption as well as other MOPR revisions.[6] This ruling puts a cloud over the results of the Base Residual Auctions and leaves the MOPR rules for the 2018 Base Residual Auction in limbo until FERC issues an order on remand.

Given the constant churn of revisions to RPM, and particularly the MOPR, load-serving entities like Old Dominion are finding it increasingly difficult to make their own long-term procurement plans and to integrate them with RPM.

Principles for Federal Policies on Wholesale Electricity Markets

From its experience as an active market participant in PJM, Old Dominion has concluded that federal policy governing wholesale electricity markets should reflect several key principles. Old Dominion respectfully presents these principles to the subcommittee for its consideration.

[4] *PJM Interconnection, LLC,* 135 FERC ¶ 61,022, *order on reh'g*, 137 FERC ¶ 61,145 (2011), *order on reh'g*, 138 FERC ¶ 61,194 (2012), *aff'd sub nom. N.J. Bd. of Pub. Utils. v. FERC*, 744 F.3d 74 (3d Cir. 2014).

[5] *PJM Interconnection, LLC,* 143 FERC ¶ 61,090 (2013), *order on reh'g and compliance*, 153 FERC ¶ 61,066 (2015), *vacated and remanded sub nom. NRG Power Mktg. LLC v. FERC*, No. 15-1452 (D.C. Cir. July 7, 2017).

[6] *NRG Power Marketing, LLC v. FERC,* No. 15-1452 (D.C. Cir. July 7, 2017).

1. *Federal policies should focus on reliable wholesale service at just and reasonable rates for consumers.*

The bedrock requirement of the Federal Power Act is that wholesale electric rates should be just and reasonable.[7] Old Dominion believes that federal policy should focus on ensuring that wholesale electricity markets are effective in providing reliable service at just and reasonable rates. If wholesale markets achieve this objective, load-serving entities like Old Dominion will be able to meet their service obligations to consumers in the most economical manner.

A focus on just and reasonable wholesale rates will necessarily involve providing the right price signals needed for new generation resource development. Competitive wholesale electricity markets provide efficient price signals for market entry and exit.

Until now, PJM's MOPR has only been applied to capacity bids by *new* capacity resources. Recent proposals to apply the MOPR to *existing* generation resources would greatly exacerbate the problems facing load-serving entities seeking to use self-supplied capacity. Moreover, extending the MOPR to existing resources would also transform it from a mechanism to prevent the exercise of buyer market power into an all-purpose mechanism for artificially propping up capacity prices above competitive, just and reasonable levels.[8]

2. *Federal policies should ensure that load-serving entities' long-term investments in generation are honored and encouraged.*

The key federal policy objective should be to ensure that long-term investments in generation resources by load-serving entities are honored and encouraged. Electric power generation and transmission is a capital-intensive business. These assets are costly and have long operating lives. Planning horizons are long. Accordingly, Old Dominion invests in or procures

[7] 16 U.S.C. § 824d(a).

[8] *See, e.g.*, Protest and Request for Rejection or, in the Alternative, Request for Suspension and Further Procedures of the PJM Load Group, *PJM Power Providers Group v. PJM Interconnection,* FERC Docket No. EL11-20-000 *et al.* (filed Mar. 4, 2011).

resources with a view to meet its long-term service obligations to its consumer-owners in a reliable and economic manner.

In our view, consumers will fare better if competitive wholesale power markets allow load-serving entities to meet their capacity obligations by first building generation resources or procuring them through voluntary long-term bilateral contracts, and then turning to RTO-administered capacity and energy markets for their residual needs. For this reason, it is important that RPM be restored to its proper and original role as a residual procurement mechanism—one that is subordinate to load-serving entities' long-term investment or procurement of resources to self-supply their capacity obligations.

3. *Federal policies should foster stability in market designs.*

Restoring RPM to its original residual function would help achieve another important goal—stability of wholesale market designs. The history of RPM's many revisions is a cautionary tale. These revisions moved RPM away from its original residual function, but they also introduced unnecessary uncertainty for all market participants. This uncertainty makes long-range planning and procurement difficult. Wholesale markets will have to be adapted to changing market forces, technologies, and state policies. But the fundamental aspects of wholesale market designs should not be in a constant state of flux as they have been over the last decade in PJM. Changes to a residual capacity market would be much less disruptive, however, since long-term investments and procurement would ensure greater market stability, which is their purpose.

4. *Federal policies should ensure that load-serving entities' choices of generation resources are honored and encouraged.*

Federal policy should ensure that load-serving entities are able to develop the portfolio of generation resources that they believe best meets their needs, based on their economic and non-economic criteria. Load-serving entities should be free to choose the mix of generation (and non-generation) technologies that meet their specific needs.

Centralized capacity markets like RPM will never be able to replicate this complex decision-making process. Currently the centralized capacity markets price one generator attribute, which is capacity. It may be possible to price other attributes, such as carbon emissions, but trying to price multiple state policies soon becomes unworkably complex and inevitably controversial. And centralized capacity markets will never become an adequate substitute for a true wholesale market where individual load-serving entities determine the amount, the kind, and the location of the generation resources they need to reliably and economically meet their service obligations.

Federal policy should ensure that load-serving entities can achieve the resource diversity they need. Resource diversity is the primary responsibility of the states. Load-serving entities are the primary implementers of state policies. Wholesale electricity markets should not impede state resource policies or load-serving entity resource investments or procurement decisions. Instead they should provide a non-discriminatory, competitive wholesale market for all types of resources.

Old Dominion's Conclusions and Recommendations

Fortunately, the RTOs and FERC are beginning to respond to these salient facts. Market forces, technological advances, changing consumer preferences, and changing state policies are forcing changes to the organized wholesale markets in PJM and the other eastern RTOs. FERC held a technical conference on this subject on May 1 and 2, 2017.[9] Old Dominion participated in

[9] State Policies and Wholesale Markets Operated by ISO New England Inc., New York Independent System Operator, Inc., and PJM Interconnection, L.L.C., FERC Docket No. AD17-11-000.

this technical conference and has filed post-technical conference comments making these same points.[10]

Old Dominion appreciates the attention the Energy Subcommittee is giving to these important wholesale market issues and the opportunity to present our perspectives. At this time, however, we do not believe there is a need for Congress to intervene by amending the Federal Power Act to give FERC additional authority or additional duties.

The Federal Power Act has proven to be a flexible statute over its 80 years of existence. It appears RTOs, including PJM, are beginning to address the emerging issues of accommodating state policies in wholesale markets, and this process is requiring them to take a close look at basic issues of market design. Hopefully FERC will also be able to address these issues. Old Dominion believes that there is no one-size-fits-all solution to the many issues now being discussed in different states and regions. We believe FERC and Congress should allow for regional flexibility in fashioning new policies that meet the basic principles outlined above.

Above all, Old Dominion believes that Congress should keep load-serving entities and their state and local regulators in the driver seat on resource acquisition to power America.

[10] See Pre-Conference Statement of Michael Cocco, FERC Docket No. AD-17-11-000 (Apr. 25, 2015); Initial Comments of Old Dominion Electric Cooperative, FERC Docket No. AD17-11-000 (June 22, 2015). The transcript of the conference and all pre-conference written statements are available at https://www.ferc.gov/EventCalendar/EventDetails.aspx?ID=8663&CalType=%20&CalendarID=116&Date=5/1/2017&View=Listview.