



NEW ENGLAND CONSUMER LIAISON GROUP

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Spring CLG Meeting

Topic: High Gas Prices –
Impact on Your Business
and Possible Solutions

March 5, 2014

12:00 - 3:30 p.m.
Eastern CT

Free. Registration required.

Watch for details at:

<http://www.iso-ne.com/clg>

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Overcoming Energy Challenges

At the December CLG meeting in Boston, speakers grappled with a changing energy marketplace, the need to diversify away from overdependence on natural gas and the impact on prices of different planning options. Federal Energy Regulatory Commission member John Norris cautioned against overinvestment in gas since we may not meet our environmental goals if we use too much gas for generation. A panel of experts examined the cost-saving desirability of moving away from investment in transmission infrastructure by emphasizing non-transmission alternatives like energy efficiency, energy storage and on-site generation. The need for timely communication to consumers about projected price fluctuations was stressed so enterprises can pursue better budget planning. Some panelists highlighted the increasing amount of risk shifted onto consumers in the context of current political and economic instability. We need leadership, some political harmony and clarity in energy planning to overcome current challenges.

Return of Winter Electric Price Spikes

There was turmoil last winter in the wholesale energy market and we are again seeing price spikes this winter. Natural gas is New England's major fuel for power generation, which is generally good for wholesale prices and for the environment. However, when there are high heating loads in the winter, there is a scarcity of available pipeline capacity for power plants. Wholesale gas prices spike due to this scarcity. This causes wholesale electricity price spikes.

ISO New England, the region's wholesale markets and grid operator, filed a winter preparedness plan with the U.S. government. The 'feds' projected that, nationwide, this winter's electricity cost would climb 2.3% over last winter's, but this projection now looks optimistic. The ISO is advocating for better communication and operating alignment between the gas and electric industries to help ameliorate the situation. Some CLG members are pressing for additional steps, including more advanced warning from ISO of price spikes. As will be discussed at the March 5 CLG meeting, solutions may include fuel diversification and/or infrastructure development.



Recent Operational and Market Improvements at ISO New England

This year, ISO New England has made a number of operational and market improvements to address the risks associated with increased reliance on natural gas and inadequate resource performance. To better align the day-ahead energy market and the gas trading day, the ISO shifted the day-ahead market timeline, giving generators more time to make fuel and transportation arrangements. The ISO made changes to the rules governing energy market supply offers, giving resources more flexibility to modify their offers during the operating day and better reflect real-time fuel prices. To address resource underperformance, the ISO strengthened its ability to maintain adequate reserves and initiated a stakeholder process to develop greater performance incentives in the Forward Capacity Market. The ISO has developed these operational and market rule changes as part of an ongoing Strategic Planning Initiative with stakeholders to improve system reliability and market efficiency.

Electricity Generation and the Environment

Power plants are the largest source of CO2 emissions in the country. In 2012, 1600 facilities emitted over 2 billion metric tons of CO2, accounting for roughly 40% of total U.S. carbon pollution. But that level of emissions is down 10% from earlier levels. The primary causes of decreased emissions are the onset of natural gas in place of coal, decreased electricity usage and increased use of renewables (wind, solar) for generation. ISO New England's draft 2012 Electric Generator Air Emissions Report shows that CO2 emissions in the region decreased by almost 8% over 2011.

Looking to the future, a U.S. Energy Department study shows that in order to accommodate more wind and solar power on the electric grid, utilities will need to start/stop or ramp up/down conventional power plants more frequently. Nonetheless, the study found that with 25% of power coming from wind and solar by 2020, the projected cost of increased adjustments to plant output is far outweighed by expected cost savings from decreased use of conventional fuels.

Electric Grid Security

We hear about the need to protect our grid against sabotage. In November, the North American Electric Reliability Corp. conducted its second grid security exercise. The exercise played out a mock cyber and physical attack on the electric grid and evaluated the responses of various entities. ISO New England participated in the exercise, following and reacting to the external cues and actions as they unfolded and identifying shortcomings in people's responses. Actual operations of the electric system were not impacted.



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Note: The views expressed here are the author's and do not necessarily reflect the views of the CLG or Coordinating Committee members.

Federal Courts Thwart State Efforts to Develop New Generation for Reliability

Two decisions recently issued by federal district courts in New Jersey and Maryland have thwarted efforts by state regulators to develop new generation facilities to resolve electric reliability concerns. The decisions, which hold that certain state actions are preempted by federal law,¹ have significant implications for the way regulatory commissions in states with deregulated retail electric supplies fulfill their historic responsibility to assure customers' access to sufficient, reliable electric service.

New Jersey and Maryland both sit within the footprint of the regional grid administrator, PJM Interconnection. PJM administers a centralized capacity market called the Reliability Pricing Model (RPM) – similar to New England's Forward Capacity Market – that is intended to use "price signals" to provide incentives for development of new capacity resources, when and where needed. Yet despite this stated purpose, merchant investment in capacity did not materialize in high-load, transmission-constrained regions of New Jersey and Maryland year after year. Both states ultimately decided that it would be imprudent to continue waiting for the market to deliver the new capacity needed to ensure reliability and took proactive measures to facilitate investment in new generation facilities.

The New Jersey legislature passed the New Jersey Long-Term Capacity Pilot Project (LCAPP) Act, which authorized the development of gas-fired generation and gave the State's regulator the authority to manage the competitive procurement for new capacity. Utilizing LCAPP, the Board of Public Utilities selected three generation projects totaling about 1,900 MW of electric capacity.

In Maryland, the Public Service Commission already had the authority to require utilities to enter into contracts that could finance new generation investment. After careful evaluation of the State's needs, the Commission initiated a competitive procurement and, later, selected a gas-fired facility.

Both state programs contemplated that new generation investments would be anchored by long-term contracts-for-differences, with the states' regulated utilities as counterparties.² Those contracts also required the new plants to sell capacity in the PJM capacity market.

PPL Energyplus and other merchant generation companies participating in PJM's capacity market filed lawsuits in federal courts in New Jersey and Maryland, claiming that the state initiatives were preempted by federal law. Specifically, the generators contended that the states' procurements were "field preempted" because they allegedly established prices for energy and capacity sales, and thus regulated in an area reserved exclusively to the Federal Energy Regulatory Commission (FERC). Alternatively, the generators argued that the state actions were "conflict preempted" because they purportedly posed an obstacle to FERC's implementation of the RPM.³

Both the New Jersey and Maryland district courts agreed with the generators that the actions were field preempted, and the New Jersey District Court found the LCAPP to be conflict preempted. These decisions adopt an extremely broad view of FERC's authority and upend the long-established recognition that a state's administration of competitive procurements – such as the fair, open and competitive procurements that these courts struck down – are lawful exercises of state authority. These decisions are particularly significant for states with competitive retail energy supplies, where state regulators have fewer tools at their disposal to ensure reliability for customers. Furthermore, if these decisions stand, other types of state procurements – such as standard offer service, demand response and some renewable procurements – may also be construed as wholesale transactions, and may be equally vulnerable to challenges on preemption grounds.

This is not the end of the story, especially because both decisions are subject to appeal and may be modified or reversed. Nevertheless, states may proceed cautiously until the courts or FERC provide more guidance regarding these issues.

¹ PPL Energyplus, LLC v. Hanna, No. 11-745 (D.N.J. Oct 11, 2013); PPL Energyplus, LLC v. Nazarian, No. 12-1286 (D. Md. Sept. 30, 2013).

² Contracts-for-differences are financial arrangements whereby a buyer and seller agree to a set price, and one party becomes liable to the other party for the difference between the contract price and the prevailing market price. Contracts-for-differences do not require the buyer to take title of the underlying product and are generally considered to be purely financial arrangements.

³ Under the Supremacy Clause of the U.S. Constitution, federal law displaces or preempts state law in certain circumstances. In the absence of express preemption language in the federal law, field preemption may be found if the scheme of federal law and regulation is "so pervasive as to make reasonable the inference that Congress left no room for the States to supplement it." *Rice v. Santa Fe Elevator Corp.*, 501 U.S. 597, 604-605 (1991). Conflict preemption may also be found if a state law "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Gade v. Nat'l Solid Waste Mgmt. Ass'n*, 505 U.S. 88, 98 (1992).