

New York’s Competitive Electricity Market – and Why We Should Keep It

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Energy issues are an area of intense, if not unprecedented focus in public policy today. Ideas and debate abound for the best types of power sources and technologies for the future.

Against this backdrop, we have a unique opportunity to move forward with a progressive agenda for clean energy and competition OR to go back to the past. Assembly Bill 1563, proposes to do away with electric competition and return New York to an era where power producing monopolies and state bureaucrats were primarily responsible for driving energy policy.

A review of the legislation and its basic provisions shows that it would:

- Increase costs to businesses and consumers
- Threaten near-term reliability
- Inhibit improvements to New York’s transmission system
- Cause large-scale regulatory and administrative confusion at a time when clarity and transparency are most needed
- Lead to greater injection of politics at the New York Public Service Commission
- Invite a likely court challenge from the Federal Energy Regulatory Commission and legal defeat
- Distract from greater electricity problems that New York has to solve

Background

In 1996, the New York Public Service Commission began to implement competition in the state’s electricity markets. Within three years, competition enabled electric consumers to choose their own electricity supplier or energy service company (ESCO). This system continues to this day.

The competitive model also enabled utilities to divest their generation facilities to private operators allowed by the Federal Energy Regulatory Commission (FERC) to sell electricity at market-based rates. New York’s distribution systems, however, remain regulated by the state and operating costs and rates are still subject to New York Public Service Commission (NYPSC) approval. Electric utilities remain responsible for purchasing enough electricity to meet their customers’ needs.

New York Independent System Operator

The New York Independent System Operator (NYISO) is a not-for-profit corporation created in 1999 that replaced the New York Power Pool and established a structured marketplace for buying and selling electricity. NYISO was created by the businesses that participate in the market. It is regulated by FERC and governed by a 10-member Board of Directors. To ensure fairness and transparency, NYISO's board members and employees are independent and have no direct ties to any market participant or stakeholder.

NYISO coordinates and operates our electric system to ensure a reliable supply of power is always available. As a non-profit organization, NYISO has other important duties besides being the "umpire" of the competitive marketplace. In addition to administering the state's wholesale electricity markets, it operates New York's bulk electricity transmission grid.

Importantly, NYISO works to prevent grid congestion and ensures that various zone requirements are met for power distribution to ensure the grid stays up and running. NYISO also conducts reliability and resource planning for the state's bulk electricity system, to the benefit of all.

Thus, NYISO's structure and its operations ensure it will secure competitive prices from generators, power will be efficiently distributed over the grid, and the grid will remain reliable and improve in quality.

Marketplace Dynamics

Electricity generators bid the minimum acceptable price to run their plants in a given period. Utilities communicate their demands for the same time period. The system operator assesses these supply and demand bids and determines an orderly and fair balance.

To ensure competitive prices and grid reliability, NYISO uses a market clearing auction. This type of auction is typically used when there are multiple suppliers who will be able to offer a sufficient quantity of the product or service needed, at prices that can be modestly adjusted, within a short time.

Market clearing auctions provide a powerful incentive for producers to offer supply at the lowest possible price. Under this system, a uniform price will be paid for the supply of electricity needed. Thus, some generators may receive more for the electricity provided than their actual bid. The utilities purchasing the power benefit from the more aggressive bid process as generators are in competition with one another and have no assurance, in any given period, that the price they are asking will be acceptable.

Assembly Bill A. 1563

This legislation proposes to replace the market clearing auction with a "descending clock, pay-as-bid auction". This type of auction begins by asking a price which is lowered until a participant is willing to accept the auctioneer's price or the seller's minimum acceptable price. This is a

great system for auctioning art work or antiques but not a necessary commodity such as electricity. It has no precedent to provide assurance of sufficient supply or lower prices.

In fact, this legislation could prove quite costly. Here's why:

In addition to assuring competitive prices, NYISO is responsible for making sure that the grid operates efficiently and is maintained and improved. If there is a material reduction in the amount of power being offered to the marketplace due to short-term concerns about pricing, this will impact the free flow of electricity.

Other Ramifications of Assembly Bill A. 1563

While much of the conversation around A. 1563 has focused primarily on the auction process, the legislation's impacts are profound.

It would require the NYPSC to "Review the rates of any public utility on an annual basis ..." as well as to "Use the fullest extent of its powers to regulate the distribution of retail electricity to retail customers in the state." It would place NYISO, generators and utilities clearly under the command and control of the NYPSC on basic business matters.

This raises several troubling issues, including the following:

Pricing. By returning to a more centralized, regulated utility system, the cost savings that New Yorkers have realized will be eliminated.

Reliability. Changing the structure of NYISO's auction process and subsuming its operations to the NYPSC poses multiple risks that there will be supply challenges and that proper maintenance and improvement of the transmission grid will not occur.

FERC Challenge. FERC is responsible for wholesale power pricing, so it is likely to challenge A. 1563 legislation and its implementation because the legislation duplicates and interferes with FERC's authority.

We need to focus on real change and further enhance competition:

It has been more than six years since New York's power plant siting law expired. This streamlined approach for considering new power plants could help us increase our power supply, enhance reliability and reduce emissions through the construction of new and less polluting power stations. The absence of the law has led to a dramatic reduction in new power plant proposals, especially where the power is needed the most.

Let's enhance our competitive electric system and build. For these and other reasons, New York's competitive market for electricity should stay in place and legislation that threatens the competitive structure should be opposed.

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About the Authors:

Dr. Matthew Cordaro is a seasoned electricity industry executive who formerly served as President and CEO of the Midwest Independent System Operator, the not-for-profit operator of the region's transmission grid. In addition, he served as CEO of Nashville Electric, one of the 10 largest public utilities in the U.S. and an administrator and professor specializing in energy at Long Island University. He is presently the incoming Dean of the Townsend School of Business at Dowling College.

Arthur "Jerry" Kremer is the Chairman of the New York Affordable Reliable Electricity Alliance (New York AREA). A 23-year veteran of the New York State Assembly, he was the only Long Island legislator to ever head the prestigious Ways and Means Committee. He served in that post for 12 years, and served by appointment of the Governor on the Metropolitan Transportation Authority's Capital Review Board and the Public Authorities Control Board. Mr. Kremer is also a principal author of the state's now expired power plant siting law.

About New York AREA: Founded in November 2003, the New York Affordable Reliable Electricity Alliance (New York AREA) is a diverse group of more than 150 business, labor, and community groups whose mission and purpose is to ensure that New York has an ample and reliable electricity supply, and economic prosperity for years to come. New York AREA helps to educate policy makers, businesses, and the general public regarding the necessity and importance of safe, low-cost and reliable electricity. For additional information visit: www.area-alliance.org.

Additional Resources:

The ISO/RTO Council (RTO)

An industry organization consisting of representatives of North American ISO/RTOs

www.iso-rtc.org

ISO/RTO Council

“Myths and Facts About Competitive Wholesale Energy Markets”

http://www.isorto.org/atf/cf/%7B5B4E85C6-7EAC-40A0-8DC3-003829518EBD%7D/Myths_Facts_About_Competitive_Energy_Markets%20.pdf

ISO/RTO Council

“Increasing Renewable Resources: How ISOs and RTOs Are Helping Meet This Public Policy Objective”

http://www.isorto.org/atf/cf/%7B5B4E85C6-7EAC-40A0-8DC3-003829518EBD%7D/IRC_Renewables_Report_101607_final.pdf

New York Independent System Operator – NYISO

www.nyiso.com

Electric Power Supply Association

www.ESPA.org

William W. Hogan; Center for Business and Government, John F. Kennedy School of Government, Harvard University

“Competitive Electricity Market Design: A Wholesale Primer”

<http://ksghome.harvard.edu/~whogan/empr1298.pdf>