



Public Policy and Energy Markets: “Good Intentions” Gone Astray

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Once upon a time ...

- The purpose of the electric industry was ... to provide electricity
 - Regulators set rates and tariffs, and that's about all
- Beginning in the 1970s, the electric industry changed
 - The 1973 OPEC oil embargo altered historical growth in electric demand
 - Environmental concerns and the newly expanded Clean Air Act focused on pollution from coal and oil-fired power plants
 - The specter of exhaustion of natural gas supplies led to comprehensive energy legislation in 1978, including the Industrial Fuel Use Act, the Public Utility Regulatory Policy Act, the Natural Gas Policy Act, and the Energy Conservation Act

State-level intervention in the industry followed soon thereafter

- “Least-cost” and integrated resource planning
 - Utilities were required to develop integrated resource plans based on 20-30 year forecasts of loads, “avoided” costs of generation and various “tests” to compare energy conservation measures against traditional generating resources
- Under PURPA, state regulators set “avoided cost” rates and forced utilities to sign what turned out to be hugely expensive contracts for power from renewable generation developers
- In the late 1980s-early 1990s, states tackled environmental “adders”
 - Particular focus on carbon emissions
 - Methods used to calculate environmental costs were wrong

see Dodds and Lesser, ““Can Utility Commissions Improve on Environmental Regulations?”
Land Economics 70 (February 1994): 63–76

Restructuring and competition ... sort of

- 1992 Energy Policy Act prepared the foundation for wholesale market competition
 - States followed with retail competition, but the debacle in California halted competition after the turn of the century
- Renewables again in the 2000s
 - With many utilities forced to divest generation and wholesale/retail competition, states jumped on the renewable portfolio standard bandwagon
 - Forced utilities/ratepayers to buy costly renewable resources (primarily wind) to improve the environment and create new industries and jobs
 - States could exploit a “first mover” advantage to create whole new industries (but how many first movers can there be?)
 - Multi-billion dollar investments in (some) new transmission lines

Today's landscape

- Direct intervention in wholesale energy and capacity markets (Connecticut, New Jersey LCAPP, Maryland)
 - Forces local distribution utility ratepayers to subsidize non-market generation, whether renewable or not, to drive down market prices
- Creation of state power “authorities” to negotiate “below-market” long-term contracts and incent renewables (again)
 - New England States Committee on Electricity (NESCOE) proposal
- Restrictions on retail competition (Michigan) to protect incumbent utilities
- More stringent RPS standards (California, New York)
- Changes in transmission cost allocation policy (FERC Order 1000)

The New York situation

- The Governor's "Energy Highway" proposal
 - Really just old projects repackaged ... vaporware
 - One key goal is to shut down Indian Point ... ironically, the Energy Highway website lists Indian Point as one of the projects
 - Development of upstate renewables called for is hampered by lack of transmission
 - NYRI project would have provided the exact type of transmission investment the NY Energy Plan called for
 - Yet, the legislature funded \$2 million for opposition groups and the state DPS opposed it. (So did ConEd, which under NYISO rules had effective veto power over any new transmission proposal)
- Development of new infrastructure in NY state difficult
 - Spectra gas pipeline into NYC: 45 miles long, \$800 million, 10 years
 - Shale gas development in New York state? Fuggehdaboutit!

Market intervention ... wrecks markets

- The way to benefit from market competition ... is to allow competitive markets to work
 - Market intervention becomes a self-fulfilling prophecy
 - Politicians intervene because they believe markets are not providing benefits from entry, thus frightening off potential entrants
- Subsidizes do not work
 - Subsidies provide short-term benefits for the subsidized (at the expense of everyone else) but result in higher overall long-term costs because they increase financial uncertainty
 - Arguments that “infant” industries (i.e., renewables) need protection so become fully competitive are wrong
 - Subsidies do not create jobs – they destroy them
 - High electric prices resulting from subsidized generation causes more lost jobs than are created by the subsidy

See Lesser, Gresham's Law of Green Energy, *Regulation*, Winter 2010, pp. 12-18

Are public policy arguments valid?

- Some are; most are not
- Environmental costs are a legitimate public policy concern, but the way to deal with them is through federal legislation like the Clean Air Act
 - Unless there are specific “vulnerable” populations, evaluate the costs and benefits of environmental legislation
 - Avoid “dueling” environmental laws. In the Pacific Northwest, protection of endangered salmon vs. wind generation. Such dueling laws are obviously counterproductive
- Renewable energy mandates are bad public policy
 - Job creation estimates fail to account for higher electric costs. (There is a reason why Denmark has the highest electric costs in the world)
 - Wind creates its own environmental costs (low-frequency noise, killing migratory birds, visual blight, etc.)

Policies that can move NY forward

- Reduce barriers to infrastructure development
 - Does not mean carte blanche for every project, but siting decisions should be rational
 - New York needs new gas pipeline infrastructure
 - Eliminate competitors' ability to stop projects (e.g., ConEd and new transmission into southeast NY)
- Let the market develop shale gas resources in the state
- Let wholesale and retail market competition work
 - Reduce financial uncertainty by pledging not to meddle in markets, in other words, politicians and regulators should resist the urge to “do something” to “fix” perceived problems
 - Eliminate RPS mandates – the costs far exceed the benefits
 - Eliminate ALL energy subsidies (PTC, ITC, etc.) Competition does not mean protecting favored competitors

As Marx (Groucho) famously said:

“Politics is the art of looking for trouble, finding it everywhere, diagnosing it incorrectly, and applying the wrong remedies.”

- Since the late 1970s, policy makers, politicians, and regulators have been addicted to intervening in electric markets, like heroin addicts
- It's time to end the addiction

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