A Presentation by:
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ELCON is the national association of large industrial electricity users. Our members operate throughout the world in competitive markets. They know competitive markets when they see them.

We firmly believe that real competition in the electric industry would bring significant benefits to all electricity consumers. We have been advocating truly competitive markets longer than any other organization – and still are convinced of the possible benefits.

At first we were quite optimistic. By the year 2000, half of the states formally said that they were going to "restructure." But the results have been very disappointing. The "restructuring" actually brought:

- Deregulation of generators with market power – and the market power may be much greater in the future with the repeal of PUHCA.
- RTOs that are great in theory, but, in reality are very problematic, expensive and unresponsive to consumers.
- Barriers that keep suppliers from interacting with consumers.
- A layering of revenue streams upon revenue streams for generators over a claimed concern for generation adequacy.
- Inadequate transmission and transmission rights – and disincentives to transmission owners to fix the problems.
- And federal/state jurisdictional problems that exacerbate the situation.

So where are we today?

- Regulators that design and implement both the LMP energy markets and the capacity markets have become the "customers."
- At best, we have recreated the old "competitive bidding" of generators.
- Consumers are still simply price takers and their actions do not and cannot influence the price in any way.
- Owners of coal and nuclear units that consumers have already paid to depreciate are receiving prices established by natural gas-fired units on the margin and are earning obscene profits.
- Industrial consumers are now paying much more than under cost-of-service and residential consumers are about to face substantial price increases as price freezes expire.
- Customers that try to negotiate bilateral contracts find that generators will only agree to contracts based on their estimates of LMP – Any benefits of fuel diversity are lost.
- On top of all of this, generators and "market" operators are paying tons of money to have studies done that say that consumers are saving a lot of money.

There simply is something terribly wrong with this picture!

ELCON still believes that real competition can benefit consumers. However, we recognize more than ever that it will be very difficult to actually implement real competition. At a minimum, we must:

I. Fix the LMP "Markets":

Price caps and price mitigation (rather than demand response) destroyed any pretense of "sending the right price signals." The FTR concept was oversold. Frankly, it probably is counterproductive and economically dangerous in a market in which generation and transmission are jointly owned. Real competitive markets cannot exist where both energy and capacity are traded. The energy and capacity constraint is only feasible in a cost-of-service regime. And at a minimum, consumers must be able to veto the implementation of proposals that they know are adverse to consumers' best interests.

II. Mitigate Market Power:

There cannot be efficient locational price signals as long as locational market power is ubiquitous. In the past, FERC, DOJ and FTC seem to be unable or unwilling to address market power. The greater the number of nodes in LMP structures, the worse the problems. Mergers such as Exelon-PSEG and FPL Group and Constellation both increase market power problems and erode state authority. Until regulators truly take consumers' views into consideration, market power problems will continue.

III. Require the Real Interaction of Supply and Demand:

Real competition is impossible without an interaction between suppliers and consumers. That is not the case in today's Organized Markets. Artificial, two-dimensional "demand curves" developed by regulators or RTOs do not fill the void. Consumers must be treated symmetrically with suppliers for real competition. This requires cooperation between federal and state regulators. Unfortunately, the divide between regulators seems even larger now than in the past.

IV. Restore the Consumer Benefits of Fuel Diversity:

Too much gas-fired generation was built. Demand for natural gas routinely exceeds supply creating tremendous price volatility. These factors combined caused the merchant generator sector to collapse. The price volatility, combined with regulatory uncertainty, has forced almost all electricity trades into the spot markets. The absence of a forward market in electricity nearly guarantees that most future generation will also be gas-fired. We must find ways to diversify the fuel mix. This requires either cost-of-service regulation or a structure with only a very small spot (or balancing) market and a heavy reliance on bi-lateral contracts.

V. **Fix Transmission Deficiencies:**

Today's "organized markets" rely on the "price signals" of LMP to trigger the need for and the location of new transmission. However, these "prices" actually are a disincentive to the elimination of transmission congestion. The Energy Policy Act of 2005 might help. But, alternatively, it might just take more money from consumers and give it to transmission owners without fixing the problems.

In sum, today's "hybrid" market structure (perhaps better described as flawed structure with patches placed on top of patches) certainly benefits the shareholders of vertically-integrated entities with depreciated coal and nuclear power plants located in or near the Organized Markets. However, it harms, and soon will harm even more, consumers – both large and small. Such a structure might be more tolerable if it were known to be a transition rather than the end-state. Unfortunately, we are not seeing changes that will fix the problems. Rather, the problems simply get worse as patches are added to patches which are then added to patches.