UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Allocation of Capacity on New Merchant)
Transmission Projects and New Cost-Based,) Docket No. AD12-9-000
Participant-Funded Transmission Projects)

COMMENT OF THE STAFF OF THE FEDERAL TRADE COMMISSION

June 14, 2012

I. Introduction

The Federal Trade Commission (FTC) staff appreciates this opportunity to comment in response to the Federal Energy Regulatory Commission (FERC) workshop on Allocation of Capacity on New Merchant Transmission Projects.[1]

some users to exercise market power. Providing public notice and ensuring that everyone can negotiate or bid are not sufficient competition policies, because neither bilateral negotiations nor an open season removes firms' incentive or ability to exercise market power.[2] For example, firms may seek to undersize lines in order to withhold capacity or route lines in ways that limit competition. Because entry is more difficult in transmission than in many other markets, entry may not suffice to counteract such withholding. Regulatory and environmental hurdles may also delay or prevent competitors' entry. In addition, there are substantial economies of scale in transmission, so adding capacity by building a second line is often significantly more expensive than adding the same amount of capacity to the first line at the planning stage. A small change in transmission capacity may have large effects on consumer benefits.

Energy Market Competition Task Force, which issued a Report to Congress in the spring of 2007 (available at http://www.ferc.gov/legal/fed-sta/ene-pol-act/epact-fina-rpt.pdf). In addition, the FTC has held public conferences on energy topics, the most recent of which was Energy Markets in the 21st Century on April 10-12, 2007.[6]

The FTC and its staff have filed numerous competition advocacy comments with FERC and participated in FERC technical conferences on market power issues. For example, in March 2007, the Deputy Director for Antitrust in the FTC's Bureau of Economics served as a panelist for a technical conference in Docket No. AD07-2-000 on FERC's merger and acquisition review standards under FPA Section 203. The FTC submitted comments in July 2004 and January 2006 in FERC's proceeding in Docket No. RM04-7-000 on its FPA Section 205 standards for market-based rates. FTC Staff commented on FERC's Analysis of Horizontal Market Power under the Federal Power Act (Docket No. RM11-14-000) in June 2011.[7] The FTC also has commented on FERC's initiatives to promote wholesale electricity competition and on various state issues associated with restructuring the electric power industry.[8]

III. Merchant Transmission Policy Should Be Designed To Maximize Consumer Benefit

The goal of transmission policy should be to maximize consumer benefits by optimally sizing and siting lines, making them reliable, managing construction and maintenance costs, and using the lines efficiently. Accordingly, policymakers should give the industry incentives to build and run an electricity system that offers the greatest total consumer benefit, net of cost, through efforts that may include the construction or upgrade of transmission facilities. The protection of competition is one of several important strategies to give firms appropriate incentives. The review of a proposed line should focus on the line's impact on the value of the

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http://www.ftc.gov/reports/elec/electricityreport.pdf; FTC Staff Report, Competition and Consumer Protection Perspective on Electric Power Regulatory Reform (July 2000), available at http://www.ftc.gov/be/v000009.htm (compiling previous comments that the FTC staff provided to various state and federal agencies).

[6] Conference materials are available at http://www.ftc.gov/bcp/workshops/energymarkets/index.shtml. Other programs have included the FTC's public workshop on Market Power and Consumer Protection Issues Involved with Encouraging Competition in the U.S. Electric Industry, held on Sept. 13-14, 1999 (workshop materials available at http://www/ftc.gov/bcp/elecworks/index.shtm), and the Department of Justice and FTC workshop on Electricity Policy, held on April 23, 1996.

[7] FTC Staff, Comment Before the Federal Energy Regulatory Commission on Analysis of Horizontal Market Power Under the Federal Power Act (June 1, 2011), available at http://www.ftc.gov/os/2011/06/1106ferchorizmarket.pdf.

[8] See, e.g., Federal Trade Commission, Comment Before the Federal Energy Regulatory Commission on Wholesale Competition in Regions with Organized Electric Markets (Apr. 17, 2008), available at http://www.ftc.gov/be/v070014b.pdf. A listing, in reverse chronological order, of FTC and FTC staff competition advocacy comments to federal and state electricity regulatory agencies is available at http://www.ftc.gov/opp/advocacy_date.shtm.

transmission network.[9] The line's impact on competition is an important part of the line's total

FERC asked how to structure open seasons and other fair processes to allocate capacity on proposed merchant transmission projects. It is important to structure such processes to allow the identification and construction of merchant transmission lines that provide consumers with net benefits. Those processes should allocate space on merchant transmission lines in ways that minimize the cost of equating supply and demand while meeting reliability[13] and environmental goals.[14]

Competition policy should encourage merchants to identify opportunities to improve on the regional plan while seeking to limit the extent to which merchants can profit by exercising market power, preempting more valuable projects, or imposing external costs[15] at the expense of consumers. Merchants may sometimes improve upon the regional plan's assessment of the size, pace, nature, and location of future generation and load growth. Transmission planning, however, is a fundamentally difficult problem because transmission lines are costly, long-lived assets that must be built despite considerable uncertainty about future technology, policies, demand, and supply. Uncertainty about environmental and renewable energy policies compounds the challenges of planning, as does rapid technological change in

FERC's approach to mitigating market power could parallel its effort to prevent withholding in the wholesale generation market. For example, FERC has sought to detect and prevent physical withholding that involves refusals to run operable generators. U.S. electricity markets use a variety of "resource adequacy" strategies that may prevent generators from engaging in physical withholding by building too few plants.[28] These precedents suggest that it may make sense to seek to detect and prevent efforts to engage in physical withholding by undersizing a transmission line. In other words, transmission market regulations should be consistent with FERC's policy goals. In particular, there may be reasons to avoid transmission market loopholes that allow firms to undersize lines to achieve the kind of withholding that FERC prevents in generation markets.

Market power can also create incentives to shape transmission investment in ways that keep prices high. Generators have incentives to structure transmission investments not only to get their power to regions where it can command high prices but also to keep their competitors out. Policymakers should be vigilant for a variety of transmission withholding strategies, including a firm's effort to structure contracts to prevent other firms from either using the proposed line or paying to increase the line's capacity. These strategies may include strategic routing, sizing, configuration, interconnection, or contracting. Merchant firms may seek to route lines in ways that raise the cost of connecting competing resources. They may route lines to reach new markets without increasing their competitors' capacity to deliver power to areas in which the merchants or their partners exercise market power profitably. When market power causes a firm to reroute or undersize a line, the line typically can be reconfigured to increase benefit to society. Intervention seems particularly well advised when a proposal seems to preempt a superior alternative.[29] FERC, however, needs to be alert to the possibility that firms opposed to building transmission will attempt to preempt good, feasible proposals by floating bigger proposals that are infeasible or unlikely to be financed.

The FTC has long recognized the possibility that undersized or overpriced transmission resources could reduce competition and harm consumers, as can withholding in the wholesale power market. For example, the FTC staff commented on the possibility that Entergy was protecting its high-cost generation fleet by undersizing transmission lines connected to other generation sources.[30] FTC comments have discussed the potential anticompetitive effects of

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[28] These regulations sometimes control the price and quantity that firms produce. They are more intrusive than is the norm in most markets in the United States and other industrialized democracies. Such interventions into the details of firm decision-making are likely to have unintended consequences. Several other FTC comments have expressed support for FERC's efforts to increase consumers' ability to adjust consumption in response to hour-to-hour changes in electricity prices. Such an increase in consumer responsiveness to power market conditions may reduce market power, allowing less intrusive regulation of both generation and transmission markets.

[29] Joskow & Tirole, *supra* n. 18, at 246-50, analyze preemption of transmission by other transmission projects and by generation projects.

[30] Comment of the Staff of the Federal Trade Commission Bureau of Economics Before the Public Service Commission of the State of Mississippi, Docket to Consider Competition in the

FERC might consider a proposal