UNITED STATES OF AMERICA

FEDERAL ENERGY REGULATORY COMMISSION

Third-Party Provision of Ancillary Services; Accounting and Financial Reporting for New Electric Storage Technologies	))))	Docket Nos. RM11-24-000 and AD10-13-000

Comment of the Staff of the Federal Trade Commission

September 6, 2012

I. Introduction

The Federal Trade Commission (FTC) staff appreciates this opportunity to comment in response to the Federal Energy Regulatory Commission's (FERC's) Notice of Proposed Rulemaking (NOPR) on *Third-Party Provision of Ancillary Services; Accounting and Financial Reporting for New Electric Storage Technologies*.[1] The NOPR indicates that third parties seldom provide ancillary services outside of organized wholesale electricity markets,[2] despite

cost firms that increases overall market supply will reduce market prices and diminish the ability of all suppliers to exercise market power. In the present matter, potential third-party providers of ancillary services maintain that they lack sufficient access to non-proprietary information to determine the size of the markets for ancillary services – information that is critical to entering with FERC's permission to charge market-based rates.[4]

FERC anticipated that potential third-party providers of ancillary services would apply for market-based rates and enter the ancillary services markets. Instead, such firms have not entered. FERC has come to understand that its own market power screening process has become a regulatory barrier to competition in this situation. One reason given for the lack of entry is applicants' reported inability reliably to determine the size of the market. Consequently, potential suppliers of ancillary services may decide that it is too difficult, if not impossible, to correctly complete the process of applying for market-based rates. To address this problem, FERC proposes to change its rules to facilitate entry, with the purpose of reducing the regulatory barrier to competition in ancillary services markets posed by the usual application of its market share screen.

We commend FERC for making it easier for applicants to identify market participants and estimate the size of the market, thereby reducing regulatory barriers to entry into ancillary

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independent generators may find it advantageous to buy such services from third-party suppliers – such as those discussed in the NOPR – in order to fulfill those new requirements. In all likelihood, these independent purchasers of ancillary services will have strong incentives to minimize costs. State regulators conducting prudency reviews may be able to use the prices that independent purchasers pay as a yardstick to better detect supplier collusion or corrupt/imprudent procurement behavior by regulated utilities. In this way, the components of the NOPR that we discuss in Sections III and IV below are interrelated.

[4] If an applicant for authority to charge market-based rates passes FERC's market power screen, FERC will undertake a process to grant such authority. FERC uses the applicant's market share as one of its primary initial screens for market power. (The pivotal supplier test is the other initial screen.) To determine market share, FERC divides the applicant's size (generally measured in terms of capacity to provide ancillary services) by the size of the market.

In NOPR PP 4-11, FERC discusses the *Avista* and *Ocean Vista* cases, which rely on FERC's existing market power screens and set the framework for the NOPR. Previous comments by the FTC and its staff have advocated market power analysis that incorporates not only market shares but also other economically relevant indicia of market power. The revised Horizontal Merger Guidelines that the FTC and the Department of Justice issued two years ago (http://ftc.gov/os/2010/08/100819hmg.pdf) discuss several of these indicators of market power. As we have done previously (*see, e.g.*, http://www.ftc.gov/os/2011/06/1106ferchorizmarket.pdf, *infra* note 8), we continue to encourage FERC to adopt a more complete approach for assessing market power. The use of a more complete approach is likely to sharpen FERC's ability to gauge market power, to the benefit of consumers.

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.[7]

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capacity."[10] By contrast, FERC observes that "[t]here appear to be significant technical requirements or limitations that apply to the provision of ancillary serv

improve the quality of FERC's analysis and decision-making, both in market-based rate matters and in merger reviews.[12]

Firms that Lack the Specific Equipment Necessary to Serve a Market Should Nonetheless Be Considered Market Participants if They Would Enter Profitably and in Timely Reaction to Supracompetitive Prices

As discussed in the NOPR, FERC concludes that market power screens used for energy markets are not appropriate for assessing market power in some ancillary services markets. NOPR P 17 provides several examples in which a particular generation resource is unlikely to be able immediately to supply a specific ancillary service. As we noted above, P 21 states that "[t]here appear to be significant technical requirements or limitations that apply to the provision of ancillary services other than Energy Imbalance and Generator Imbalance such that the existing market-based rate screen may not be adequate to capture the potential ho

Supply and Voltage Control services if they have not installed the electronic controls required to supply these services.

Based on economic research as well as FTC litigation experience, the fact that a potential entrant has not installed a particular piece of equipment may not be a sufficient reason to exclude it from the range of potential suppliers to which customers can turn in response to a price increase (or a non-price diminution of competition). In appropriate circumstances, these potential suppliers should be considered existing market participants.[13] The key question is whether such a firm, *even though not currently producing*, likely would begin meaningful production in a timely fashion in the face of incumbent suppliers' exercise of market power. At one temporal extreme, there could be a very short lag between incumbents' imposition of supracompetitive pricing and meaningful new entr

regarded as an existing market participant, and its anticipated capacity, output, or sales volume should be included in the corresponding figures for the entire market. By contrast, for firms unlikely to accomplish such timely and meaningful entry, it is often inappropr

Regulation and Frequency Response services. This effect may be particularly pronounced when the higher-quality service happens to cost more per unit, even if the innovation reduces costs in the aggregate. This form of discrimination is likely to deny to transmission customers (and ultimately consumers) the benefits associated with this form of innovation. A system of setting customized reserve requirements that recognizes quality differences among reserves is likely to benefit consumers through increased innovation that lowers aggregate costs and improves reliability. Consequently, we support FERC's proposal to insist that transmission providers adjust reserve requirements for transmission customers to reflect the quality of the reserves maintained by those customers.

In summary, we agree that expanding the coverage of FERC Order No. 755 is warranted. Such expansion is likely to provide incentives in more areas to undertake innovations and investments that will lower system costs and increase system reliability to the benefit of consumers. Thus, we support the proposals in PP 47-53 designed to broaden the geographic reach of the quality-adjusted pricing reforms for ancillary services contained in FERC Order No. 755.