



# FEDERAL ENERGY REGULATORY COMMISSION

**June 19, 2008**

**Item No. A-3**

**Chairman Joseph T. Kelliher**

## **Statement of Chairman Joseph T. Kelliher on Cost of Electric Generation Staff Presentation**

"I thank the staff for the presentation, which highlights some of the hard realities that FERC is confronting, and that are guiding the development of FERC regulatory policy. I think it is important that these hard realities be better understood by the general public and others.

FERC regulatory policy must be based on reality. The reality is that upward pressure on electricity prices – higher capital costs for new power plants, higher construction costs, and higher fuel costs – will continue for some time. That means electricity prices will be higher than many Americans would like.

We are actually confronting three realities. First, FERC and state commissions are regulating in a high-cost environment – that is not likely to change soon. Second, the U.S. needs massive investments in new electricity generation, transmission, and distribution. Third, we are beginning to confront climate change challenge, and are in period of uncertainty regarding policy. Acting on climate change will come at a significant cost – not necessarily an unreasonable cost.

There is tension among these three realities – they work at cross purposes. FERC has regulatory policies designed to encourage investments in generation and transmission. These policies have been criticized because they have some impact on cost. New coal generation has been cancelled due to climate change uncertainty, reflecting the tension between security of electricity supply and climate change.

We must accept the U.S. cannot make the massive investments necessary to assure security of our electricity supply, make additional large investments to confront climate change, and lower electricity prices at the same time. If we try to do all three, the result will likely be failure.

What can we do about price? We cannot change cost fundamentals, either for power plant costs or fuel costs. Coal prices and the costs of construction materials are set in a world market. Natural gas prices are still set on regional basis, reflecting North American market fundamentals.

The U.S. can improve energy efficiency and demand response, and FERC is acting in these areas, benefiting from the leadership of Commissioner Wellinghoff.

We can make sure that when power plants are built, they are built in a way where competitive pressures govern cost both construction cost and operating costs. There is more than one path to support new generation, and some paths more likely than others to produce lower cost electricity.

We can make sure prices are not a product of market manipulation or market power exercise. FERC's duty is to assure that wholesale electricity prices are just and reasonable. That means prices that are high enough to support continued investment in new electricity supply, environmental mitigation, and improved delivery across transmission and distribution lines.



## STATEMENT

We recognize the risks of market manipulation may be greater in a high-cost environment, and we will remain vigilant to assure the wholesale prices reflect market fundamentals, rather than manipulation. We can assure wholesale power prices do not rise any higher than they have to in order to assure security of our electricity supply and meet the climate change challenge.

The last time we were in a high-cost environment similar to this was the late 1970s and early 1980s. Back then, the high-cost environment was the product of traditional rate regulation. Competition policy was created as a direct response to the failure of regulation.

Competition policy was rooted in the conviction that competition does a better job controlling costs than regulation, that competition does a better job developing and deploying new technologies, that competition does a better job improving operating performance, and competition properly shifts risk from consumer to market participants. Those truths still apply today, and competition policy is best suited to address the hard realities we are confronting today."