

Federal Energy Regulatory Commission
April 20, 2006 Commission Meeting
Statement of
Chairman Joseph T. Kelliher

**E-4: PJM Interconnection, L.L.C. Reliability Pricing Model
(EL05-148-00)**

"In this order, the Commission finds the existing capacity construct in PJM to be unjust and unreasonable because the current capacity markets do not support continued generation entry.

Our conclusion is driven by the fact that a new generator investing in PJM cannot expect to recover its costs through energy and capacity revenues. The existing capacity construct does not recognize the growing need to increase electricity supply in PJM or create appropriate incentives to address the problem.

This need was demonstrated dramatically at the technical conference the Commission held in February. Eastern PJM is facing serious near term reliability violations as early as this year unless electricity supply is added. Under current capacity construct, generation additions in Eastern PJM is valued the same as in areas of PJM with large surpluses. Not only will generation additions in PJM slow to a crawl, retirements may actually outpace generation additions, for a net loss of electricity supply. That is the same situation that confronted California leading up to Western electricity crisis.

The Commission has a legal duty to assure just and reasonable wholesale power rates. That does not mean we have to guarantee profitability, and that is not what we are doing here today. But a capacity market that does not recognize transmission constraints that not only exist, but are getting worse, that places no value on locating generation where it is most badly needed, that produces shortage and serious reliability problems, does not result in just and reasonable rates – nor is it good public policy.

There are similarities here to the approach we ultimately took in New England regarding its capacity market. Our original New England LICAP order adopted a particular approach towards capacity market reform, but led to a great deal of criticism of the Commission, on the grounds we ignored workable alternatives advanced by New England.

We heard the New England region's criticism and held additional oral argument last September. Oral argument proved very helpful. There was nearly universal recognition in the region that it was facing serious electricity supply problems under the status quo. We challenged the region to come together around an alternative.

This approach produced a settlement that is now before us. Most of the 100 New England parties joined the settlement, but there are some substantial nonsettling parties. Of course, we can't address the merits of the proposed settlement.

But this approach – developing consensus that the status quo was failing, encouraging the region to control its own destiny and to develop a workable alternative that is just and reasonable, while preparing to act if the region fails – is the same approach we are adopting here for the PJM region.

One reason a settlement was reached in New England was that the region took the Commission seriously when the Commission stated that it was prepared to act if the region did not develop a workable alternative. We are prepared to act in PJM as well.

The Commission strongly encourages each region to develop resource adequacy solutions that fit its particular circumstances. We recognize resource adequacy has traditionally been a state responsibility and we therefore encourage states to play the leading role in developing regional solutions in regional power markets.

Although the Commission will encourage consensus, we will not ignore a problem and simply hope it goes away. The lack of investment is a real problem that must be addressed. We have a duty to assure just and reasonable rates and a duty to assure reliability of the bulk power system. We will fulfill those duties.

I encourage the PJM region to build on the guidance provided in today's order to develop a solution to the electricity supply problem that is confronting the region."