

April 22, 2008

VIA ELECTRONIC FILING

Kimberly D. Bose, Secretary
Federal Energy Regulatory Commission
Office of the Secretary
888 First Street, N.E.
Washington, D.C. 20426

**RE: Wholesale Competition in Regions with Organized Electric Markets
Docket Nos. RM07-19-000 and AD07-7-000**

Dear Ms. Bose:

Enclosed please find for electronic filing Comments of American Forest & Paper Association on the Commission's NOPR in the above captioned proceedings.

Thank you for your attention to this matter.

Regards,

/s/Donald J. Sipe

Donald J. Sipe
Counsel to American Forest & Paper Association

Enclosure
CC: Service List

Preti Flaherty Beliveau & Pachios LLP Attorneys at Law

45 Memorial Circle | Augusta, ME 04330 | TEL 207.623.5300 | FAX 207.623.2914 | Mailing: P.O. Box 1058 | Augusta, ME 04332-1058

Augusta Bath Boston Concord Portland

www.preti.com

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

**Wholesale Competition in Regions with
Organized Electric Markets**

**Docket Nos. RM07-19-000
and AD07-7-000**

**COMMENTS OF
AMERICAN FOREST & PAPER ASSOCIATION
ON NOTICE OF PROPOSED RULEMAKING**

Pursuant to the Commission's Notice of Proposed Rulemaking ("NOPR") on Wholesale Competition in Regions with Organized Electric Markets, issued by the Federal Energy Regulatory Commission ("FERC" or the "Commission") on February 22, 2008 and published in the Federal Register¹ on March 7, 2008, American Forest & Paper Association ("AF&PA") hereby submits its comments on a limited subset of issues in the Commission's Notice.

In its previous comments filed in this Docket, AF&PA provided comment on two suggested market reform proposals designed to improve the competitiveness and efficiency of the markets and to promote long-term contracting.

First, AF&PA proposed the adoption of the Financial Performance Obligation ("FPO") in markets such as New York, New England and PJM where capacity products relying on a Cost of New Entry calculation are utilized. In its Order, the Commission has provided parties a further opportunity to discuss the Financial Performance Obligation in a Technical Conference to be conducted in a separate docket. AF&PA appreciates the Commission's consideration of the FPO proposal, and looks forward to working with other parties through the Technical Conference process to develop the proposal further.

¹ 73 FR 12576 (March 7, 2008).

Second, AF&PA noted that the current capacity interconnection standard used by PJM and potentially other RTOs, is unduly discriminatory towards new entrants, and inconsistent with competitive principles of open access. In particular, in areas that have adopted locational capacity constructs, the concept of deliverability improperly grants to incumbents a non-market based entitlement to exclude new entrants from the transmission system and the capacity market. AF&PA continues to believe that, consistent with the proposal in its prior comments, the Commission should initiate reforms of the capacity interconnection (a.k.a. Network Resource) study and interconnection process to eliminate such discrimination, lower barriers to entry for new resources, and promote greater competition in local and regional markets for capacity.

I. COMMENTS.

A. Demand Response.

AF&PA supports the Commission's view that the Demand Response reforms contemplated in the Rulemaking not be considered the final step in the development of what should be a comprehensive Demand Response policy. As a general matter, AF&PA has come to recognize that, although concepts such as "comparability", "efficiency", and "just and reasonable", must all, in some way, enter into the Commission consideration of the appropriate role of Demand Response in the market, none of these concepts are self-defining. This represents both challenges and opportunities as the Commission works to better define the goals of competitive market design for all customers.

AF&PA has an initial concern that the necessary policy discussions and decisions regarding the appropriate role of Demand Response in competitive markets for electricity, not be short circuited by an immediate resort to "mechanisms" and "programs". Though market rules and mechanisms are necessary to permit any product to be traded in these highly standardized markets, the mechanisms should be subservient to the purposes to be served and should be

developed to accommodate the products that will bring greatest value. Currently available mechanisms should not dictate what products are permitted. The old saying that “when all you have is a hammer, everything looks like a nail”, is an apt caution.

The first step in determining how markets need to be adjusted to accommodate Demand Response, is to gain a clear policy understanding of precisely what it is we want Demand Response to do, and the ways in which it can provide value. AF&PA believes that there are at least the following potential areas of value available through Demand Response:

Short Term

A: Lower clearing prices

B: Balance system loads in emergencies

Long Term

C: Reduce or defer capital investment and long-term capital risk.

D: Reduce market power

E: Reduce volatility and lower risk premiums for long-term contracts

F: Coordinate scheduling of generation and transmission maintenance outages

G: Optimize resource portfolio

H: Diversify “fuel” mix

As noted in our earlier comments, Demand Response is a service, not a commodity. Moreover, it is a service associated with the provision of a common good, a good which will increasingly need to be carefully allocated among the members of society in a manner which is both fair and efficient. Because it is a good affected with the public interest, there are many more policy considerations involved in proposals to restrict access to, or voluntarily or involuntarily “allocate” this product by price. The extreme cost associated with blackouts is an indication of the potential for “value of service” pricing to do real harm, not only to those unfortunate enough to be priced out of the market, but to society as a whole. Seeing the value of

Demand Response primarily in terms of allowing customers to respond to such prices, rather than as part of an economically efficient strategy for assuring they never occur, already presumes a certain policy framework that may be incompatible with fundamental conceptions of fairness that underlie the just and reasonable standard. Although proper pricing is essential to long-term efficiency, pursuing greater volatility in short term pricing as a primary method of communicating prices may increase capital risk premiums for long-term investment in Demand Response and supply technologies. Further that design choice already presupposes the type of Demand Response that will be recognized by the market and limits the value it can provide.

AF&PA concedes that it does not at this time have a comprehensive product and market definition that embodies and balances each of these policy considerations. But we are concerned that the current short-term design emphasis of the energy, capacity and ancillary services markets may not contain sufficient tools to adequately address these concerns. For these reasons, AF&PA remains extremely concerned that in the current market design context, the Commission's proposals to increase volatility in the energy markets either by lifting caps or re-pricing reserves, may result in an inefficient allocation of resources in light of the broader policy objectives of supplying a common good. For these reasons, we continue to believe that the Commission's proposals in these areas are premature.

Market efficiency can only be effectively judged in terms of what any particular market is designed to deliver. We fully support the Commission's intention of engaging in a broader discussion directed to better defining the appropriate role of Demand Response in providing safe and reliable service at just and reasonable rates. We continue to believe that it is in the context of that broader discussion that the appropriate role of short-term volatility, long-term price signals such as the capacity market, and the value to be placed upon lowering risk premiums by reduction of such volatility, can best be evaluated. As noted above, AF&PA has made a

particular proposal, the Financial Performance Obligation which, if adopted, could provide a more constructive and less socially disruptive role for price volatility in the markets by providing greater opportunities for forward hedging. But these and other ideas will require time to evaluate and, hopefully implement. We continue to believe that the current market structure contains sufficient short-term volatility at the wholesale level to incent most viable short-term Demand Response opportunities.²

AF&PA supports the Commission's proposal to require RTOs and ISOs to look at ways to accommodate Demand Response through allowing bids that limit hours of dispatchability and total energy contribution to the system. We agree with the Commission's view that such resources can provide the same sorts of value that other intermittent resources provide to the system. Many generators are limited in the hours that they may operate efficiently and the amount of energy they can provide. Further, generators can incorporate start up and other factors into their bids. We support such comparability in scheduling flexibility for Demand Response resources, because we believe it will expand the number and types of Demand Response resources that can contribute to system stability and long-term dampening of volatility.

AF&PA also supports the Commission's proposal to allow aggregators of Demand Response at the retail level to directly bid Demand Response into the wholesale markets. We recognize that this proposal requires accommodation by state law and retail rate structures to make such participation practical. We believe, however, that availability of this option at wholesale may spur the development of state level retail programs that might otherwise not be

² We note that even within these structures, there is not agreement among all Stakeholders as to what should be "done" with the price signals that are available. For example, the debate about whether customers should be "paid" the clearing price or simply allowed to avoid it, has greater potential to increase or decrease Demand Response in response to "price" than the Commission's current proposals to promote even greater volatility. This debate is but one example of the empirical and policy questions which need to be examined more closely before concepts such as "comparable treatment" can be usefully applied.

considered. The potential for such participation may encourage the development of state law or retail structure to accommodate participation where none currently exists as customers at the retail level seek to avail themselves of the greater opportunities afforded by larger markets.

AF&PA also supports the removal of the deviation charge for customers who consume less during a system emergency. The Commission's rationale for this change is sound. Given the extremely high cost of outages, the existence of a charge that would discourage LSE's or retail customers from responding to requests by system operators for reductions in usage during emergencies bears an extremely heavy burden to justify its continuation. Although scheduling accuracy is an important consideration, effective and efficient response to emergency situations is a much higher priority.

B. Market Monitoring.

AF&PA supports the proposal to have the MMU report directly to the RTO/ISO Board and not to management. We agree that this change will increase independence and provide direct and unfiltered information to RTO/ISO Board members who have a responsibility to oversee management activities, including the design and performance of markets.

AF&PA continues to believe that the Market Monitor is the appropriate place to vest market mitigation responsibilities. AF&PA does not support removing such duties from the Market Monitor and placing them instead in the RTO. As noted in our initial comments, AF&PA is concerned that RTO Staff and personnel who have designed and implemented the markets, and whose compensation may be based upon these tasks, may have a vested interest in not identifying or correcting potentially problematic bidding or other behavior. A well-functioning market should be the pride of any RTO or ISO, but pride should not be a consideration, even subconsciously, in personnel designated to intervene when those markets do not function as expected. RTO/ISO personnel are highly professional, but it is nonetheless

sometimes difficult for even highly professional people to candidly assess the potential failures and the need for correction in their own work product.

Further, we believe that removing the MMU's role in mitigation may deprive the MMU of much of the hands-on administrative interaction with participants that is essential to customer protection. The role of mitigation flows naturally from the investigation and oversight of market behavior, market function and efficiency. We do not believe that there is an inherent conflict between this role of inquiry and investigation and mitigation activities, rather we believe that there is a natural synergy. The Commission has taken steps in several recent Orders to limit the range of discretion of the Market Monitor in applying mitigation. If there is any continuing concern that inappropriate discretion could be employed by MMUs, this is a better way of addressing the issue than removing the Market Monitor from mitigation activities.

II. CONCLUSION.

AF&PA greatly appreciates the opportunity afforded by the Commission to comment on issues surrounding possible improvements to the structure of the competitive markets for electricity.

Dated at Augusta, Maine this 22nd day of April, 2008.

Respectfully submitted,

/s/ Donald J. Sipe

Donald J. Sipe, Esq.
Counsel to American Forest & Paper
Association

Preti Flaherty Beliveau & Pachios
P.O. Box 1058, 45 Memorial Circle
Augusta, ME 04332
Telephone: 207-623-5300
Fax: 207-623-2914