

COMMENTS OF THE DIVISION OF CONSUMER COUNSEL,
OFFICE OF THE ATTORNEY GENERAL, TO THE
MEMBERS OF THE JOINT SUBCOMMITTEE STUDYING
ELECTRIC UTILITY RESTRUCTURING (SJR 91) ON THE
ISSUES OF MARKET POWER AND TRANSMISSION CONSTRAINTS

The Division of Consumer Counsel, Office of the Attorney General (“Consumer Counsel”), appreciates this opportunity to present comments on behalf of consumers to the Members of the Joint Subcommittee Studying Electric Utility Restructuring (SJR 91) (“Joint Subcommittee”) concerning the related issues of market power and transmission constraints. Consumer Counsel is charged with representing the interests of the people as consumers; part of this responsibility entails making recommendations to the Governor and General Assembly concerning legislation that is necessary to promote and protect those interests. See *Va. Code* § 2.1-133.1. The comments being presented today are an overview designed to identify issues of concern to consumers in the areas of market power and transmission constraints.

I. Introduction

A. The Objective Should Be To Have Effectively Competitive Electricity Markets.

Most everyone can agree that the goal of electric utility restructuring in Virginia should be to have effectively competitive electricity markets that produce maximum value from capital investment, while offering customers a wide variety of choices of reliable, efficient energy products and services at reasonable prices. If done correctly, restructuring should produce a better, more efficient, allocation of resources by increasing the role of market forces where conditions permit, while simultaneously decreasing the role of regulation. The expected results of an effectively competitive electricity market include lower prices,

greater efficiency and reliability, improvements in products and services, and innovation. The task before the members of this Joint Subcommittee is how to translate that vision into reality. This task includes identifying those features that are necessary, both during and after the transition to competition, to ensure that effectively competitive electricity markets develop and thrive, and that consumers are protected in the interim. Depending upon how industry restructuring is designed and implemented, the end state may reflect the economic conditions of competition, monopoly or oligopoly.

B. In Order To Develop Effectively Competitive Electricity Markets, The Present Industry Structure Must Be Carefully Analyzed And Understood In The Context Of Possible Future Market Structures. This Analysis Should Produce Recommendations For Structural Implementation And Appropriate Regulations.

1. Some Working Definitions

In order to provide some focus to these comments, a series of working definitions are needed to understand the economic similarities and differences between and among competition, monopoly and oligopoly behaviors. Each is a possible end state following restructuring.

2. Monopoly¹

A monopoly is said to exist when one firm controls all or the bulk of a product's output, and no other firm can enter the market, or expand output, at

¹ For a more comprehensive discussion of the nature and economic consequences of monopoly, see Phillip E. Areeda, Herbert Hovenkamp & John L. Solow, *Antitrust Law*, Volume IIA, ¶ 403 *et seq.* (1995).

comparable costs.² Such a monopolist has the power to raise price above competitive levels by restricting its output, because the output reduction cannot be offset by expanded output of others.³ The courts have long recognized that a public service corporation, with the limited monopoly obtained through its exclusive franchise, may be said to operate in restraint of trade or competition in its assigned territory as a matter of public policy. See *Kempsville Util. Corp. v. Wills*, 213 Va. 679, 194 S.E.2d 740 (1973).

3. Competition⁴

At the other end of the spectrum from monopoly lies perfect competition. The term “perfect competition,” when used in describing a product or service, implies that all of the following conditions are present:

1. Sellers and buyers are so numerous that no individual’s output or purchasing decision has a perceptible impact on price (to satisfy this condition, the product or service of each seller in the particular market must be “homogenous;” that is, there must be a large number of sellers of the product or service that buyers view to be perfect substitutes for each other);
2. Each seller and buyer makes decisions independently, without agreement with or influence from others;
3. All productive resources are freely mobile among markets; there are no barriers to entry or exit;
4. All sellers and buyers have complete knowledge of all production techniques, input costs, prices and other relevant market facts;

²² See *id.* at ¶ 403a.

³ *Id.*

⁴ For a more comprehensive discussion of the nature and economic consequences of a perfectly competitive economy, see Areeda, Hovenkamp & Solow, *Antitrust Law*, Volume IIA, ¶ 402 *et seq.*

5. Producers make input-output decisions solely to maximize return on capital – that is, they seek minimum-cost production techniques and net-revenue maximizing levels of output; and
6. There are no “externalities”: producers pay all social costs incurred in the production of goods and services and receive payment for all social benefits conferred.⁵

The economic consequences of producing a good or service in a perfectly competitive environment are that producers would maximize operating efficiency by producing the good or service at least cost.⁶ A firm that failed to produce the good or service at the least possible cost permitted by known techniques may be able to temporarily break even or make small profits if demand is high enough, but it would eventually incur losses, lose market share and be replaced by more efficient producers.⁷

4. Oligopoly⁸

An oligopoly market for a product or service is one in which a few relatively large producers account for the bulk of the output. While an oligopoly market may include what has been referred to as a “competitive fringe” of numerous smaller sellers, who may behave in a competitive manner because they are individually unable to affect market prices or output, oligopoly is

⁵ See *id.* at ¶ 402a.

⁶ In a perfectly competitive economy, resources would also be allocated among the production of various goods and services so that no reallocation of inputs and outputs could increase overall consumer welfare by making some consumers better off without making other consumers worse off. In economic parlance, this is known as “Pareto efficiency.” See *id.* For purposes of this discussion, however, we focus on operating efficiencies.

⁷ See *id.*

⁸ For a more comprehensive discussion of the nature, economic consequences and measurement of oligopoly, see Areeda, Hovenkamp & Solow, *Antitrust Law*, Volume IIA, ¶ 404 *et seq.*

distinguished from competition in that the decision to significantly vary production or to withhold production by any one of the leading sellers has a large impact on the market price and on the behavior of rivals. Oligopoly is distinguished from monopoly in that no one firm may unilaterally determine market price by varying the level of the firm's output because larger rivals can either offset or magnify the effect by changing their own output.⁹ As Professors Areeda, Hovenkamp and Solow explain, "the distinctive characteristic of oligopoly is the recognized interdependence among the leading firms: the profit-maximizing choice of price and output for one depends on the choices made by others."¹⁰

In order to develop effectively competitive electricity markets, the present industry structure must be carefully analyzed and understood in light of possible industry outcomes. This analysis should produce recommendations for structural implementation and appropriate regulations.

II. Defining Market Power and Defining Markets¹¹

⁹ Oligopoly is also distinguished from cartel behavior in that the latter is expressly coordinated behavior by agreement. Otherwise competing firms form a cartel when they replace independent decisionmaking on matters such as price and output with an agreement. While decisionmaking in an oligopoly context produces tacit coordination because firms make individual decisions that are interdependent, cartels reflect collective decisionmaking that seeks to maximize aggregate revenues over aggregate costs. See *id.* at ¶ 405.

¹⁰ *Id.* at ¶ 404a (footnote omitted).

¹¹ For a more comprehensive discussion of market power and market definition, see Areeda, Hovenkamp & Solow, *Antitrust Law*, Volume IIA, Part II Chapter 5.

A. Basic Definitions¹²

1. Market Power Defined

In its most basic terms, market power is defined as the ability to raise price by restricting output.¹³ Market power is of concern because it can reflect the ability of one or a few firms to profitably maintain the price of a product above competitive price levels for a significant period of time. Courts often define market power as the ability to control prices or to exclude competition. *See, e.g., United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 391-92 (1956). This characterization recognizes that market power has both short- and long-term implications, and that market power exists in degrees. Market power is relatively small when even a slight increase in price would lead to a significant loss of sales. Market power is large when a firm can substantially raise prices without losing many sales.

If a firm is able to control prices, distribution systems, and/or other crucial resources, or to wield other types of power, the result can be to weaken or eliminate existing competitors or inhibit new market entrants. As competition is discouraged or eliminated, the firm gains monopoly power and is able to raise the prices of its goods and services in a sustainable manner. These principles apply whether market power is held by a single firm or a few firms operating in a manner reflecting oligopoly.

¹² Portions of this Section are based largely on a May 1997 Market Power Discussion Paper Draft prepared by Scott Hempling, Esquire, for the Electric Division of the Michigan Public Service Commission.

¹³ *See id.* at ¶ 501.

In an effectively competitive market, by contrast, prices are believed by many economists to be self-regulating. From the consumer's perspective, if prices become too high, customers will be able to select another supplier that will offer the same or substitutable product less expensively. From the producer's perspective, if profits are too high, new competitors will enter the market in an attempt to gain market share. If, on the other hand, one or more firms has sufficiently unchecked market power, market distortions may appear. Such distortions reflect two kinds of market power, characterized as vertical and horizontal market power. As the Staff of the State Corporation Commission explained in its *Draft Working Model for Restructuring the Electric Utility Industry in Virginia* ("Staff Restructuring Model Draft" or "Staff Report"), issued to the Senate Joint Resolution No. 259 Joint Subcommittee on November 7, 1997,

Conceptually, there are two types of supplier market power concerns--vertical market power and horizontal market power. Vertical market power arises from single-firm or affiliate ownership of two or more steps in a production and market delivery process where one of the steps provides the firm with control of a bottleneck in the process. Such control enables the firm to give preference to itself or its affiliate over competitive firms. Horizontal market power arises from a firm's local ownership concentration of a single process step within a defined market area. If such concentration is sufficient with respect to certain other market conditions, the firm can influence the supply-demand equilibrium, and hence prices, simply by withholding production. Both vertical and horizontal market power concerns are present with respect to electric industry restructuring.^[14]

¹⁴ Staff Report at 63.

With the production of a complex manufactured good such as electricity,¹⁵ many sequential and related activities are involved, including the processes of generation, transmission, and distribution. If successive production stages are not vertically integrated, prices tend to be set by competitive markets, provided no single stage is capable of being used as a bottleneck¹⁶ to block competitors. On the other hand, when a firm controls two or more successive stages of production, such as generation, transmission, and/or distribution, this vertical integration may lead to two possible market distortions, described by Mr. Hempling as follows: (1) products pass from one process to the next with prices being set internally, and those prices may reflect motives and incentives internal to the firm, rather than reflecting production costs; and (2) there is at least some danger that a market may be foreclosed, and new entrants excluded.

Horizontal market power can result from market concentration when control of a large portion of the competitive resources at any particular level of production is held by one or a small number of firms. It is often associated with a geographical component, for a variety of reasons (mostly centered around transportation and transaction costs). In the electric utility industry, the transmission function raises the most concern for the exercise of horizontal market power.

¹⁵ For purposes of this description, electricity is referred to here as a single product. In reality, the electric utility industry produces many distinct products and services, many of which are interrelated.

¹⁶ This, of course, has been a persistent claim with regard to the transmission function.

2. The Importance Of Market Power

Market power can be used to prevent new market entrants or eliminate competitors, not through the provision of superior products at lower costs, but through manipulation of the market. The means for accomplishing this include predatory pricing; using cross subsidies from captive customers with relatively inelastic demand for their service in order to lower prices to those customers with elastic demand; using tying arrangements; engaging in joint ventures that exclude competitors; and -- perhaps most important for the electric utility industry -- controlling access to markets through delivery channels (for example, limiting access to the transmission or distribution grids).¹⁷ Firms with market power have ability to extract excess profits from customers, to the overall detriment of society.

As the General Assembly is fully aware, electricity is not just another commodity -- it is one of life's necessities. For most customers, there are few options, if any, to electricity. Therefore, exerting market power over an essential service may leave many customers facing higher prices without reasonable alternatives.

3. Departures From The Competitive Model: Implications For Legislators And Regulators

¹⁷ In the context of transmission constraints, market power can arise due to the fact that utilities designed their transmission systems to serve their own customers, and without any attempt to corner a competitive market. In a competitive environment, transmission systems are increasingly being used in ways that do not reflect the way they were designed to operate.

The model of perfect competition as described above includes conditions that resist practical application, particularly in the electric utility industry. These departures from the perfect model are basic limitations that reflect real market conditions. They include, but are not limited to, economies of scale; barriers to entry; immobility of resources; product differentiation; information asymmetries; agency problems; and externalities. All of these departures should be considered as part of the restructuring process.

The Federal Power Act, and most state laws regulating electric utility operations and service, were enacted at a time when electric utilities were essentially self sufficient and vertically integrated. A single entity typically owned generation, transmission, and distribution facilities, and electric energy was sold as part of a bundled service, referred to as delivered electric energy, to both wholesale and retail customers. Most electric utilities built their own power plants and transmission systems to serve the needs of their franchised service areas, and the Federal Power Act encouraged them to enter into voluntary interconnection and coordination arrangements with neighboring utilities for the generation, transmission and sale of electric energy.¹⁸ Utilities entered into long-term contracts to make wholesale requirements sales (so-called “bundled sales” of generation and transmission) to municipal, cooperative, and other investor-owned utilities (IOUs) connected to each utility's transmission system. Each system covered limited service areas. This structure of separate systems

¹⁸ See FPA § 202; 16 U.S.C. § 824a.

arose naturally due primarily to the cost and technological limitations on the distance over which electricity could be transmitted.

In addition to economic changes, the electric utility industry has been transformed by significant technological changes in both generation and transmission that have occurred since 1920. Through the 1960s, the conventional wisdom was that “bigger is cheaper” in the generation sector. The industry capitalized on economies of scale that enabled progressively larger plants to produce power at lower per-unit costs. Consequently, large utilities developed a price advantage over smaller companies because they could finance and manage construction projects on a larger scale.

By the 1970’s, however, “bigger is better” no longer was the case. The greater maintenance and longer downtimes associated with large power production facilities, and the inability to find increasing economies of scale in generation, reversed the trend that had flourished through the 1960’s. In addition, technology advances, including combined cycle units and conventional steam units utilizing circulating fluidized bed boilers, allowed smaller generating units to achieve scale economies. These new, smaller plants were able to be brought on line much less expensively, and with smaller lead times, than their large counterparts from the earlier era.

Significant technological advances in transmission have also made it possible to economically transmit electric power over long distances at higher voltages. It is now technically feasible (if not operationally feasible due to transmission constraints) for distant utilities with lower cost generation sources

to reach previously isolated customers that presently pay for higher cost generation. In fact, since the passage of the Energy Policy Act of 1992¹⁹ and the promulgation of the Federal Energy Regulatory Commission's ("FERC") *Order No. 888*,²⁰ substantial amounts of electricity now move between different regions of the country, as well as between interconnected utilities.

4. Defining Markets

Market power is a spectrum that depends upon the product being considered, a correct assessment of appropriate geographic boundaries, and the time period being examined. In order to understand whether market power exists, it is essential that the market being examined be accurately defined in terms of product, place and time. Professors Areeda, *et al.*, explain that

[t]o define a market is to identify producers that provide customers of a defendant²¹ firm (or firms) with alternative sources for the defendant's product or service. A properly defined market excludes other potential suppliers (1) whose product is too different (product dimension of the market) or too far away (geographic dimension of the market) and (2) who are not likely to shift promptly to offer defendant's customers a suitably proximate (in both product and geographic terms) alternative. Those who can make such an offering only after some time are not treated as market incumbents, but their potential entry may nevertheless limit the power of the incumbents.

¹⁹ Pub. L. No. 102-486, 106 Stat. 2776 (1992), codified at, among other places, 15 U.S.C. § 79z-5a and 16 U.S.C. 796 (22-25), § 824j-l.

²⁰ *Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities*, Order No. 888, 61 Fed. Reg. 21,540 (May 10, 1996), FERC Stats. & Regs. ¶31,036 (1996), *order on reh'g*, Order No. 888-A, 62 Fed. Reg. 12,274 (March 14, 1997), FERC Stats. & Regs. ¶31,048 (1997), *order on reh'g*, Order No. 888-B, 81 FERC ¶61,248 (1997).

²¹ The authors use "defendant" as a shorthand indicator of the firm or firms whose market power is being examined – quite apart from any actual or prospective litigation. See Areeda, Hovenkamp & Solow, *Antitrust Law*, Volume IIA, ¶ 530a, n.1.

Thus, a market is the arena within which significant substitution in consumption or production occurs.^[22] That arena tends to exhibit uniform prices throughout. Indeed, “the more nearly perfect a market is, the stronger is the tendency for the same price to be paid for the same thing at the same time in all parts of the market.” With less perfect substitution, a range of prices may appear, though changes in each are closely correlated.^[23]

III. The Relationship Between The Electricity Transmission System And Market Power

A. The Transmission Function Is Critical To Competition

The transmission function is critical to competition. FERC’s *Order No. 888* recognized the close relationship between the ability to deny transmission service and the ability to exercise market power. Accordingly, FERC ordered all public utilities with transmission facilities used in interstate commerce to file tariffs containing minimum terms and conditions of non-discriminatory service, because

We have identified a fundamental generic problem in the electric industry: owners, controllers and operators of monopoly transmission facilities that also own power generation facilities have the incentive to engage, and have engaged, in unduly discriminatory practices in the provision of transmission services by denying to third parties transmission services that are comparable to the transmission services that they are providing, or are capable of providing, for their own power sales and purchases. These practices drive up the price of electricity and hurt consumers. Furthermore, the incentive to engage in such practices is increasing significantly as competitive pressures grow in the industry. It is within our discretion to conclude that a generic

²² The authors explain that supplier *entry* broadens the market to include the product or area from which the additional supply comes, and consumer *exit* broadens the market to include the substitute product to which consumers go. See *id.* at ¶ 530a n.5.

²³ *Id.* at ¶ 530a (footnote omitted).

rulemaking, not case-by-case adjudications, is the most efficient approach to take to resolve the industry-wide problem facing us.

* * *

We conclude that unduly discriminatory and anticompetitive practices exist today in the electric industry and, more importantly, that such practices will increase as competitive pressures continue to grow in the industry, unless the Commission acts now to prevent such practices. It is in the economic self-interest of transmission monopolists, particularly those with high-cost generation assets, to deny transmission or to offer transmission on a basis that is inferior to that which they provide themselves. The inherent characteristics of monopolists make it inevitable that they will act in their own self-interest to the detriment of others by refusing transmission and/or providing inferior transmission to competitors in the bulk power markets to favor their own generation, and it is our duty to eradicate unduly discriminatory practices.²⁴

While *Order No. 888* may have resolved the inability to obtain non-discriminatory transmission service by tariff, it did not resolve inability to obtain transmission service due to physical constraints. As discussed in the *Staff Report*, these transmission import constraints and related market power concerns represent serious barriers to true competition in Virginia that must be resolved for deregulation to be beneficial to Virginia consumers. Consumer Counsel believes it is extremely important that the General Assembly understand the seriousness of these barriers and find solutions to these problems as a first step in the restructuring process.

For example, H. Charles Liebold has identified existing constraints with respect to Virginia Power's ability to import firm power into its system.²⁵ His

²⁴ *Order No. 888*, FERC Stats. and Regs. ¶ 31,036 at 31, 679 and 31,682.

²⁵ See Commonwealth of Virginia, at the relation of the State Corporation Commission, *Ex Parte: Investigation of Electric Utility Restructuring – Virginia Electric and Power Company*, Case No. PUE960296, Direct Testimony of H. Charles Liebold submitted on behalf of the Division of Consumer Counsel.

testimony discusses Virginia Power's available transfer capability ("ATC"), which is the amount of transfer capability remaining on the transmission system for a given set of system conditions.²⁶ Virginia Power's transmission system is discussed here for illustrative purposes. Such analysis must be performed for each electric utility doing business in Virginia to determine whether the existing transmission systems will support competition.

According to Mr. Liebold's analysis, Virginia Power has interfaces with four major transmission systems.²⁷ Mr. Liebold concludes that the ATC levels reported by Virginia Power are constrained both by the actual physical limits of the transmission system and by Virginia Power's discretion in the quantification and reporting of its ATC for power imports from other regions.

Mr. Liebold's findings indicate that the total existing ATC for firm power imports into Virginia is in the range of 2,800-3,100 MW, which is approximately

²⁶ "ATC" is the measure of the capability to transfer power between two areas or regions allowing for the weakening of the transmission system caused by the loss of the most critical single element of the electrical system, after reductions for all firm uses, reservations and margins. Mathematically, the ATC is the amount of transfer capability remaining after these reductions in the total transfer capability. A utility has great discretion to control ATC by altering assumptions in transmission studies, changing the dispatch of generating facilities, reserving transmission capacity for itself, and other such actions. As long as a utility controls the operations and planning of its transmission system, it will have substantial ability to control the level of imports into its system from other regions, and therefore to limit competition from off-system competitors. The ability to alter reported ATC values creates uncertainty that will likely translate into higher costs for power delivered from other regions.

²⁷ These systems are the Allegheny Power System ("APS") and the Pennsylvania – New Jersey – Maryland ("PJM") interconnections in the northern part of Virginia Power's system; the American Electric Power ("AEP") interconnections in the western part of Virginia Power's system; and the Carolina Power and Light ("CP&L") interconnections in the southern part of Virginia Power's system. Mr. Liebold estimates that these interfaces currently provide a total of up to 1,800 MW of Available Transfer Capability ("ATC") for firm power imports from the northern and western part of Virginia Power's system, and a total system simultaneous import ATC of 2,800-3,100 MW. Mr. Liebold's analysis further indicates that Company's transmission studies also conclude that power transfers to Virginia Power from regions to the west, north and east will rely heavily on the APS interface. That interface presently has *no* available ATC according to information provided by Virginia Power to potential transmission customers.

20% of Virginia Power's total system retail peak demand (15,145 MW).²⁸

Therefore, unless substantial additional transmission import capability is added between now and the time that generation markets are deregulated in Virginia, there may not be extensive competition within Virginia Power's service area from other regional suppliers. It may not be feasible for more than a small percentage of total peak requirements to be imported into Virginia on a firm basis.²⁹

²⁸ The source of Virginia Power 1997 peak demand is Virginia Power's Market Power Study filed with the Federal Energy Regulatory Commission on July 1, 1997.

²⁹ There is other evidence that Virginia Power will have substantial market power within the Virginia market it currently serves. In addition to the Commission Staff's concern noted in the *Staff Report*, Virginia Power presented a market power analysis in conjunction with its recent application to the Federal Energy Regulatory Commission for authority to charge market-based rates. The Company's analysis assumes that some 46,890 MW from outside utilities could be accessed by Virginia Power transmission dependent utilities ("TDUs") through Virginia Power's Open Access Tariff. On September 11, 1997, the FERC conditionally accepted for filing, with certain modifications, Virginia Power's tariff amendment under which the Company proposed to sell electric energy and capacity at wholesale at market-based rates, and to reassign transmission rights. See *Virginia Electric and Power Company*, 80 FERC ¶ 61,278 (1997) ("September 11 Order"). The Commission also set for hearing the limited issue of the impact of any transmission constraints on Virginia Power's ability, if any, to exercise generation market power in localized markets in its service area. *September 11 Order*, 80 FERC at 61,996, 61,999.

This analysis, using the hub-and-spoke method of measuring generation market power, does not reflect the present potential for importing power, since the firm ATC for imports into Virginia Power's system currently is at most 3,100 MW. The FERC has consistently held that the hub-and-spoke test is the appropriate test for analyzing market power in the context of requests for market-based rates, notwithstanding many requests from State Public Utility Commissions, State Attorneys General, transmission customers and others that the Commission discard this method in favor of more comprehensive methods, such as the Competitive Analysis Screen used for evaluating market power issues in merger proceedings. See, e.g., *New England Power Company, et. al.*, 82 FERC ¶ 61,179 (1998); *New York State Electric & Gas Corporation and XENERGY, Inc.*, 78 FERC ¶ 61,309 (1997); *XENERGY, Inc. and New York State Electric & Gas Corporation*, 79 FERC ¶ 61,303 (1997); *Consolidated Edison of New York, Inc. and ProMark Energy, Inc.*, 78 FERC ¶ 61,298 (1997). The FERC has responded that "the Merger Guidelines analysis need be submitted only if the applicant is *unable to demonstrate a lack of generation dominance* with the hub-and-spoke test." *New England Power Company, et. al.*, 82 FERC at 61,662 (emphasis added)(footnote omitted). The primary shortcoming of the FERC's approach is that the hub-and-spoke analysis fails to account for the very parameters that *restrict the scope of trade*: relative generation prices, transmission prices, losses, and transmission constraints. If the hub-and-spoke method *fails to demonstrate a lack of generation dominance*, use of the more restrictive parameters will likely serve to magnify such generation dominance, because the hub-and-spoke method overstates the extent of the market and the number of competitors, while understating the potential for market power. The more central issue for the Commission is whether the hub-and-spoke method *masks or distorts the measure of generation dominance, as measured in economic terms*. Unfortunately, under the

The implications of such high market power ratios are that, unless existing transmission import limits are removed or other mitigation measures are implemented, Virginia Power or any similarly situated utility may be able to exert considerable control over the price of power charged to its customers when and if generation markets are deregulated. If this is allowed to occur, deregulation could result in higher prices for Virginia consumers.

B. Transmission Constraints Must Be Alleviated For Customers To Benefit.

Transmission import limits may be alleviated by adding new transmission facilities, but this is problematic given present conditions, and it is not a short term solution. In many cases, new transmission facilities require multiple state approvals and in some cases federal approval to address siting and environmental concerns. That is not to say that there are no solutions to the issue of transmission limitations; however, the issue of transmission limitations and appropriate mitigation of their impact must be resolved first if benefits from restructuring are to be realized by consumers.

If not addressed at the outset, the effects of transmission constraints, as well as “must run” generation, may inhibit the development of effective competition by allowing market participants to exercise undue market power. To

Commission’s present standard of review, the burden shifts to intervenors to demonstrate that a hub-and-spoke analysis masks or distorts the true measure of generation dominance in economic terms. *See, e.g., Delmarva Power and Light Company*, 83 FERC ¶ 61,157, slip op. at 3-4 (May 14, 1998)(“*Delmarva*”). Even assuming no ATC import limits, Virginia Power’s installed

this end, Consumer Counsel has recommended to the Commission that a study be prepared to determine whether structural, price or other regulatory controls, separately or in combination, are needed to address market power concerns associated with “must run” generation and transmission constraints. The General Assembly and the Commission should also give careful consideration to identified market power issues and their effects on ISO and RPX structures. Such analysis is necessary to assure that restructuring will result in effective competition for Virginia, and protection for Virginia consumers.

capacity share of the Virginia market is 26.9% with the NUG capacity and 22.5% without the NUG capacity. Both of these figures exceed the FERC’s maximum market share target of 20%.