

Written Testimony of James P. Danly
Commissioner, Federal Energy Regulatory Commission
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House Energy and Commerce Committee
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Chairman Rush, Ranking Member Upton, Chairman Pallone, Ranking Member McMorris Rodgers, and Members of the Committee: Thank you for providing us the opportunity to appear before you today to discuss the critical work that we are doing at the Commission.

As the reliability crisis in California last summer and this winter's storm in Texas sadly demonstrated—reliable, affordable supplies of energy are vital for the health, well-being, and prosperity of the American people. Right now, the Commission faces the daunting tasks of regulating an electricity sector undergoing dramatic transformation, ensuring broad access to plentiful supplies of natural gas through our pipeline certificate proceedings, protecting the reliability of the bulk power system from ever-increasing threats, and overseeing our jurisdictional markets to ensure that they produce competitive prices. We have been aggressively addressing all of these issues—in recent months, the Commission has begun a number of ambitious projects, has initiated rulemakings, and held technical conferences on a variety of topics to develop records and become better informed.

But in meeting these challenges, the Commission must keep in mind that every action we take has to be consistent with the law as enacted by Congress and interpreted by the courts. Accordingly, I would like to take just a moment to focus on the Commission's statutory responsibilities in a few key areas. These legal obligations necessarily inform all of the Commission's deliberations as we work to ensure reliable electricity and plentiful supplies of natural gas at just and reasonable rates.

The Commission is required under the Federal Power Act to ensure that wholesale rates for electricity in interstate commerce are just and reasonable. This mandate requires particular vigilance in the context of the RTOs and ISOs where FERC is obligated to ensure that our jurisdictional markets are designed to yield competitive prices. In recent decades, the move from the traditional paradigm of cost-based rate making to competitive markets has produced dramatic cost savings. As our markets have developed over time, the courts have consistently held that market rates can only be deemed just and reasonable if FERC closely scrutinizes the markets for the exercise of buyer- and seller-side market power and its resultant price distortions. When FERC finds market power, it is further obligated to adopt measures to mitigate its effects, thereby ensuring that our markets are actually competitive.

The Commission is also obligated to ensure that transmission rates are just and reasonable. The Commission recently issued an Advanced Notice of Proposed Rulemaking asking stakeholders and the public a number of questions to gather information in order to assist us in determining whether and how we might improve our regulation of interstate transmission. The Commission's decision to issue this notice was unanimous. My colleagues and I all agree that the transmission planning process is in need of reform. As we review the comments in that

docket, however, the Commission must bear in mind that the costs of transmission projects are ultimately borne by the ratepayers. We are statutorily obligated to ensure that transmission rates are just and reasonable, which means we must be on guard against policies or planning processes that encourage unnecessary build-out, or so-called “gold-plating,” of the transmission system. FERC must also scrupulously adhere to the principles of cost causation as we decide how the costs of transmission projects are to be allocated among ratepayers. The law is clear: the costs borne by ratepayers must be roughly commensurate with the benefits the ratepayer receives from the transmission infrastructure. I worry that, given the current zeal for transmission buildout, FERC may lose sight of this basic principle. Too broad a socialization of transmission costs would burden ratepayers with higher utility bills as they are called upon to underwrite the development of transmission projects from which they receive neither economic nor reliability benefits.

The Commission is also obligated to ensure the reliability of the bulk electric system. While this duty is typically discharged when the Commission reviews and approves NERC’s mandatory reliability standards, FERC’s jurisdictional markets also play a critical role in ensuring reliability and resource adequacy. FERC’s RTOs and ISOs must provide the correct price signals to incentivize the entry and retention of the correct quantity of generating resources that have the necessary attributes to ensure system stability and reliability. Not all generating assets are the same. If the markets fail to send the correct price signals, they will not incentivize the correct quantity and type of generation. The result will be the adoption of yet more cost-based, out-of-market arrangements used to plug the holes in reliability created by market failures that do not provide the proper market incentives to construct and operate the necessary generation resources. Because these out-of-market contracts are non-competitive, they are expensive to ratepayers. And because these stopgap contracts are out-of-market, they themselves cause further price distortions in the competitive markets. This cycle, once begun, ultimately leads to one outcome: flawed price signals fail to provide resource adequacy leading to reliability crises like those seen in California last summer.

Finally, the Commission administers the Natural Gas Act, the purpose of which is to ensure the orderly development of plentiful supplies of natural gas at reasonable prices. The Commission must issue certificates of public convenience and necessity to applicants whose proposed pipelines are needed and in the public interest. As we witnessed in Texas in February, constraints in the supply of natural gas can have profound consequences not only for consumers of natural gas, but also for anyone who uses electricity. If the gas supply fails, the electricity supply fails. Pipelines are fundamental, critical infrastructure. At the moment, the pipeline industry is facing profound regulatory uncertainty as the result of recent Commission actions. Because of this uncertainty, investment in pipeline projects has come nearly to a standstill. In order to ensure that this critical infrastructure can be built when needed, the Commission must establish clear policies by which it will conduct its examination and adjudication of natural gas pipeline certificate applications.

In conclusion, I want to again thank the Committee for the opportunity to appear here today and I look forward to your questions.