


# **UPDATE ON STATUS OF RESTRUCTURING: RECENT POLICY DEVELOPMENTS**

Barbara R. Alexander  
Consumer Affairs  
Consultant  
NLIEC 2007



# RETAIL RESTRUCTURING: YOU CAN NO LONGER HIDE

- Rate caps hid the problem
- Almost no retail marketing or customer choice activity for residential customers
- Default service policies are key to residential customer prices for electricity
- Key question: what policies will govern planning and acquisition for Default Service? Is this a debate about restructuring in disguise?

# PRESSURE TO USE “MARKET-BASED” PRICES FOR DEFAULT SERVICE

- Some regulators equate short term wholesale market prices as the only measure of “competitive” service
- Marketers want “ugly” default service to drive customers in their arms and “create” competition
- Utility management is risk adverse; reject responsibility and regulatory second guessing
- FERC and others pressuring for reliance on emerging wholesale market mechanisms to obtain default service--day ahead markets and not bilateral long term contracts

# WHOLESALE MARKET PRICING RULES

- EMPHASIS ON SHORT TERM PRICES (hourly and day-ahead markets) to send the proper price signal for new investment
- NO TRANSPARENT LONG TERM CONTRACT MARKET
- “BID STACK” PRICING MEANS THAT THE PRICE OF THE MOST EXPENSIVE GENERATOR (NATURAL GAS) IS DRIVING PRICES FOR ALL GENERATORS
- WE HAVE LOST THE AVERAGE PRICE APPROACH FOR THE GENERATION SUPPLY PORTFOLIO
- HIGHER PROFITS FOR NUKES, COAL PLANTS, HYDRO, RENEWABLES
- LACK OF INVESTMENT IN NEW CAPACITY so regional RTOs and ISOs are trying to create such a market with new charges

# DEFAULT SERVICE POLICIES IN EASTERN U.S. HAVE ATTEMPTED TO REFLECT SHORT TERM WHOLESALE MARKET PRICES

- NJ: Statewide Reverse Auction; 3-year fixed price contracts, 1/3 annually
- MD: 50% of customers in 1-year contract; 50% for 2-3 contracts
- MA: One half of Default Service load is bid for 12-month terms every six months
- Maine: 3-year contracts, 1/3 annually
- District of Columbia: Mix of 1-2-3 year fixed price contracts
- Delaware: same as Maryland and DC
- Illinois: ordered NJ-style auction with 2-3-year contracts
- New York: originally allowed longer term fixed rates as part of legacy contracts, but began to push for more volatile pricing in 2004
- Connecticut: series of 1-3 year contracts

# BUT SIGNIFICANT PRICE INCREASES IN 2006

- New Jersey (1/3 load)
  - PSEG \$.10251/kwh
  - Rockland \$.11114/kwh
  - Atlantic Electric \$.10399/kwh
  - JCPL \$.10044/kwh
- Delaware (100% load)
  - Delmarva \$.10 to \$.11/kwh
- Maryland
  - BG&E (100% load) \$.10 to .115/kwh

# WHAT HAPPENED IN MARYLAND?

- BG&E's rate cap ended in July 2007 so went into wholesale market for 100% of the load in late 2006
- 72% average total bill increase
- Political firestorm
- Merger pending between Constellation Energy (parent of BGE) and Florida Power & Light eventually cancelled
- Attacks on the PSC itself
- Result: phase in of rate increase; PSC replaced under new Governor in early 2007
- No clear direction on future policy re restructuring or default service, but Legislature has authorized long term procurement planning and consideration of options to continuation of retail competition

# WHAT HAPPENED IN DELAWARE?

- Delmarva's rate cap ended June 2007 and went into the market to acquire 100% of the load in late 2006
- Result is 50+% average total bill increase
- Governor's Task Force
- Legislation adopted statutory reforms to assure long term planning for Standard Offer Service; integration of energy efficiency; various contract terms; new renewable resource mandate
- Continuing controversy over implementation of new policies; Delmarva Power refuses to enter into long term contracts

# WHAT HAPPENED IN MAINE?

- Unlike other states, Maine Commission decides SOS policies and solicits and obtains the contracts on behalf of Maine's retail electric customers; utility does not have any substantive role
- Starting in 2005, decided to obtain 1/3 of load for three-year fixed price contracts
- Since 2000, there has been a 100+% in SOS price.
- In 2006, the Maine Legislature adopted reforms to procurement policies for SOS, including energy efficiency and various contract terms, and requires utilities to sign long term capacity contracts if PUC so orders
- Maine PUC has voiced significant opposition to ISO New England capacity market policies; considering seriously the "Canada" option; pending lawsuit against FERC
- Continuing studies re proposal for utility return to own generation
- Continuing controversy over default service policies; PUC refuses long term contracts in 2007 procurement, citing risks of stranded costs.

# WHAT HAPPENED IN VIRGINIA?

- First state to repeal restructuring and re-institute rate base regulation
- Utilities own generation and largest utility sought to build new generation
- Utilities dominated the legislative process and obtain numerous protections and guarantees about their rate of return and revenue protection with rate adjustment clauses

# NEW YORK HAS EMPHASIZED COMPETITION AND SHORT TERM MARKET PRICES, BUT CHANGE IS BREWING

- New York PSC adopted a “Vision” statement in 2004 for competitive markets. Long term goal is to remove the local utility from generation supply function Short term objective to eliminate fixed rate service and require monthly price changes for default service.
- Intent of PSC: drive residential customers to competitive marketers; rely on new technology and new competitive suppliers to deliver ‘efficiency’.
- New Governor and new Commissioners in 2007: approves the use of “hedging” to reduce price volatility for default service (but no change in requiring monthly price changes as the default service) AND opens new investigation into whether long term resource planning should occur and, if so, whether or how long term contracts (5+years) might be used.

# PENNSYLVANIA: 2007 Default Service Rule is a step backward

- Long Term rate caps in place for larger utilities until 2010
- Statute: POLR must reflect “prevailing market prices;”
- PUC’s new statements require POLR plans for 2-3 years and transition to increased reliance on spot market prices and quarterly price changes
- PUC supports laddered contracts, but short term contracts and use of spot markets preferred to stimulate competitive markets
- Pending legislation supported by Governor and Consumer Advocate to adopt longer term planning and portfolio management for long term lowest price.

# THE TEXAS EXPERIENCE IS UNIQUE (THANK GOODNESS)

- Unique market model
  - Distribution utility is wholesale supplier to retail electricity providers
  - Only REPs have retail relationship with customers
  - Created “affiliate” REP to serve all non-shopping customers
- Price to Beat or default service terminated January 2007 and the “affiliate” REP has no obligation to serve and can establish whatever terms for its customers
- 50-60% residential customers still served by former affiliate REP
- Tremendous public outrage over electricity prices
- Pending sale of TXU to private equity firm
- Pending legislation to reduce rates, restore low income discounts, and provide new powers to PUC to oversee market power

# IT IS DIFFERENT OUT WEST: LONG TERM INTEGRATED PLANNING

- **MONTANA:** STATUTORY POLICY IS TO REQUIRE DISTRIBUTION UTILITIES TO PROVIDE DEFAULT SUPPLY SERVICE AT “LOWEST LONG-TERM TOTAL COST”; 10-15 YR PROCUREMENT PLAN UNDER REVIEW AT PSC THAT INCLUDES DSM AND RENEWABLES
- **CALIFORNIA:** STATUTORY POLICY TO CONDUCT LONG TERM PROCUREMENT PLANNING AFTER 2000 MARKET IMPLOSION
- LINK TO TRADITIONAL INTEGRATED RESOURCES PLANNING. SEE ALSO OREGON, WASHINGTON

# STATES THAT ARE CONSIDERING DRAMATIC CHANGES BUT NO CLEAR DIRECTION

- Michigan: at least one utility has called for repeal of restructuring and seeks authority to plan and purchase new generation
- Connecticut: Legislative power struggle with no significant reform or resolution for two years; DPUC continues to buy short term power for default service and approve long term contracts for new capacity and energy efficiency paid for through distribution rates
- Illinois: 2006 auction prices resulted in firestorm of protest; consumers seek roll back in prices; utilities threaten bankruptcy and lawsuits; back room deals in Springfield?
- Ohio: Economic development forces beginning to attack deregulation due to expected high prices with end of transition in 2008; Governor calls for high level review

# WHAT POLICY CHANGES ARE BEING CONSIDERED?

- Repeal restructuring and allow the utilities to get back into long term planning and acquisition of generation
- Municipal aggregation (buy for customers)
- Municipal/state ownership of utility function
- Public Power Authority for long term generation investment and ownership
- Long term procurement planning for default service by utility without repeal of restructuring
- Do restructuring “right” and force customers to endure volatile default service prices and rely on marketers to offer better deals

# BUT CAN WE GO BACK TO RATE BASE REGULATION?

- The world has changed:
  - Wholesale regional markets and FERC jurisdiction here to stay: transmission and new capacity
  - Many distribution utilities divested of generation and expertise
  - Wholesale market players are powerful
  - Distribution utilities are risk averse and demand protections from prudence review, guaranteed income through decoupling, and will shift responsibility to the commission

# WHAT ARE KEY ATTRIBUTES FOR A CONSUMER FRIENDLY POLICY?

- Procurement planning for 10-15 year period
- Active portfolio management
- Objective: long term lowest price with reasonable price stability
- Emphasis on variety of contract lengths, contract types and risk profiles
- Compatible with competitive bidding in wholesale market and competitive RFPs for bilateral contracts
- Plan should evaluate and integrate options for energy efficiency (negawatts) and renewable energy where such resources will lower prices

# WHO SHOULD BE RESPONSIBLE FOR PLANNING AND MANAGEMENT?

- Key decision: are we going to rely on retail policies to govern price of electricity and long term capacity and reliability of service or defer entirely to wholesale market policies and FERC regulation?
- Among the retail choices, both public power and privately owned models exist and both models have pros and cons
- What matters is the policy and the oversight to ensure adherence to the policies
- No magic bullet with public aggregation or ownership: these entities can't do anything that a properly regulated utility could or should do; consider the "politics" of appointment and accountability

# WHAT FORCES THREATEN RETAIL OR STATE POLICIES TO ASSURE LONG TERM PLANNING AND PRICE STABILITY?

- DYNAMIC PRICING (DELIVERED THROUGH SMART METERS): Move to rely on wholesale market spot prices and thwart move to long term planning and average prices
- SEPARATE THE FUNDING FOR ENERGY EFFICIENCY, DEMAND RESPONSE, AND RENEWABLES FROM THE INTEGRATION AND FUNDING THROUGH DEFAULT SERVICE: If these “public benefits” are funded through distribution rates, it will destroy the linkage and potential benefits from an integrated portfolio management and pricing for default service

# WHAT WILL HAPPEN TO RETAIL ELECTRIC/GAS COMPETITION?

- Retail competitive markets are not likely to develop for residential and small commercial customers
- Some states will repeal (e.g., Virginia)
- Some states will adopt “reforms” that will have the practical effect of leaving retail shopping only a theoretical option
- Key decision: what role and responsibility will the utility or other entity have to assure longer term and active portfolio management?