Chapter 5

"Any other information the board believes to be beneficial to the Governor, the Legislature, and Nebraska's citizens when considering whether retail electric competition would be beneficial, such as, but not limited to, an update on deregulation activities in other states and an update on federal deregulation legislation."

1.0 Purpose

Provide information on deregulation activities in other states, an update on federal deregulation legislation, and other public policy developments relating to electric deregulation.[1]

2.0 Team Members

Doug Bantam – Lincoln Electric System
Jay Holmquist – Nebraska Rural Electric Association
John McClure – Nebraska Public Power District
Tom Richards – Omaha Public Power District

3.0 Introduction

3.1 Deregulation Overview

The material presented below is an addendum to last year's update on the status of actions to implement retail choice in the electricity industry. Proponents of deregulation argue that competitive markets are more efficient than government regulated economic activities. Professor Willis Emmon's recent book on deregulation and privatization states: "Deregulation is a broad concept that encompasses easing or eliminating government restrictions in three major areas: a firm's freedom of entry into a market, its freedom of action within a market, and its profitability (maximum or minimum) within the market."[2] One of the biggest public policy challenges in achieving successful deregulation is the creation of truly competitive markets. The LR 455 Phase II Report, December 1999, analyzed the driving forces of retail electric deregulation and discussed the impacts of deregulating other industries in Nebraska such as airlines and telecommunications. See pp.8-16. As the Report clearly pointed out, in Nebraska "competitive markets" often bypass rural or sparsely populated areas, especially when the deregulating industry is capital intensive such as airlines, railroads, and telecommunications.

Skepticism about the consumer benefits of electric deregulation in Nebraska, along with Nebraska's competitive energy costs, were two key factors leading to the "condition certain" approach recommended in the LR 455 Phase II Report and adopted in LB 901 (2000).

Retail deregulation gained considerable popularity between the late 1990s and January 2001 with 25 state legislatures or regulatory agencies committing to various forms of retail customer choice. This trend reversed considerably by June 2003 when only 18 states and the District of Columbia were pursuing such action and some of these states have retail choice on only a very limited basis. See groups of states below and Exhibit V-1.

Pursuing Retail Choice (19)

Arizona	New Hampshire (to commence in 2004)
Connecticut	New Jersey
Delaware	New York
District of Columbia	Ohio
Illinois	Oregon (non-residential only)
Maine	Pennsylvania
Maryland	Rhode Island
Massachusetts	Texas
Michigan	Virginia
Nevada (non-residential only)	

Retail Choice Suspended or Repealed (5)

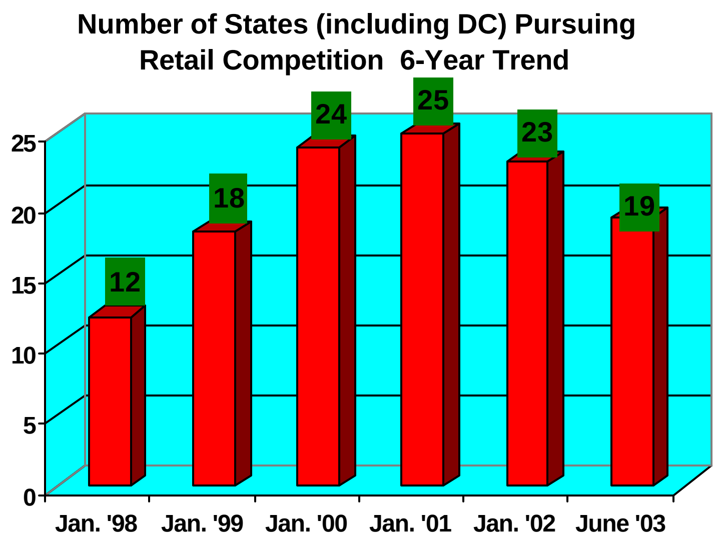
Arkansas
California
Montana
New Mexico
Oklahoma

[1] This report reflects deregulation developments through August 20, 2003.
[2] Willis Emmons, *The Evolving Bargain*, "Strategic Implications of Deregulation and Privatization," 2000: p. 2.

Retail Choice Not Being Pursued (27)

Alabama	Missouri
Alaska	Nebraska
Colorado	North Carolina
Florida	North Dakota
Georgia	South Carolina
Hawaii	South Dakota
Idaho	Tennessee
Indiana	Utah
Iowa	Vermont
Kansas	Washington
Kentucky	West Virginia
Louisiana	Wisconsin
Minnesota	Wyoming
Mississippi	

Exhibit V - 1



4.0 Status of Retail Competition in Selected States

Each year, the Center for the Advancement of Energy Markets (CAEM) -- a Virginia based energy think tank that advocates for retail customer choice -- releases its annual RED Index ranking the 50 states (and DC) and a number of foreign countries on the development of competitive energy markets. In 2001, Pennsylvania was identified as the leading state because of the development of its electricity market. George Spencer, publisher of *RestructuringToday* wryly observed, "To be number one in the nation today isn't saying very much with all the retail markets effectively closed."[3]

This year (2003), Ken Malloy, CEO of CAEM noted that Texas is now at the "head of the class" as number one among competitive electricity markets in the US. But Malloy quickly qualified his observation of Texas by noting, "But it's a pretty stupid class. The sad truth is that in the war for competitive energy markets, we're losing."[4]

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[3] George Spencer, Publisher of *Restructuring Today* commenting on the relative "success" of Pennsylvania's retail competition scheme. June 22, 2001.

[4] "Malloy sees Texas leading in retail power", *Restructuring Today*, March 20, 2003, p.2.

The CAEM Red index ranked the state of Nebraska (for the sixth straight year) as last among the 51 jurisdictions in the United States for the development of a competitive retail electricity market. The report notes that, "as a result of the California crisis -- the (Nebraska) legislature is even less likely to enact legislation creating retail choice."[5]

4.1 Significant Legislative Actions Affecting the Implementation of Retail Choice

- Arkansas – During 2003, legislation (HB 1114) was enacted to repeal retail choice provided however that the Arkansas PSC would study the possibility of retail choice for the largest power users.
- New Mexico – Legislation was enacted during 2003 (SB-718) to repeal the implementation of retail choice.
- Oregon – Retail choice has now commenced for non-residential customers only after prior delay imposed by legislature. There are no immediate plans to implement retail choice in the residential market.

A number of internet web sites contain comprehensive state-by-state summaries of the status of electric retail competition. The sites provide the status of restructuring legislation and regulation and details on the structure of the approach taken. However, because much of the recent regulatory and legislative activity on electricity restructuring has been to delay and/or repeal prior initiatives toward retail competition, none of these web sites was completely up to date as of the drafting of this report. Despite the many limitations of these sites regarding timeliness and accuracy, one can find useful information on the status of restructuring.

American Public Power Association
    www.appanet.org

Edison Electric Institute
    www.eei.org

C.H. Guernsey & Company
    www.chgeconmics.com

National Association of Regulatory Utility Commissioners
    www.naruc.org

National Rural Electric Cooperative Association
    www.nreca.coop

US Department of Energy (Energy Information Administration)
    www.eia.doe.gov

William Spratley Associates
    www.spratley.com

The following pages contain a brief summary of the status and implementation of retail competition in several states. The reader is encouraged to review the updates contained in this addendum in conjunction with the material published in last year's report. Proponents of retail choice now look to Texas as their best hope of demonstrating how retail choice can achieve the many promises that have been made with respect to market competition.

4.1.1 Arizona

On August 27, 2002 the Arizona Corporation Commission unanimously voted to eliminate a key provision of the state's electric competition plan that would have required Arizona Public Service (APS) and Tucson Electric Power (TEP) to move their power plants into a separate subsidiary or sell them to another unrelated company. A press release of the Arizona Corporation Commission quoted Commissioner Jim Irvin as saying, "This should now set the

[5] "2003 Red Index", Center for the Advancement of Energy Markets, (www.caem.org).

course for what is vitally necessary, which is a process that protects ratepayers from the kind of disaster that befell California utility customers."[6]

4.1.2 California

By late June 2003 new developments were emerging in California's efforts to restore stability to its electricity markets. First, the state's largest utility, Pacific Gas & Electric, reached a tentative settlement with the staff of the California Public Utility Commission on a plan to allow the company to emerge from bankruptcy and once again pay dividends to common stockholders. Under the terms of the accord, the utility would issue some $8 billion in new debt and electric consumers would pay higher rates over the next nine and a half years. However, residential customers would see some rate relief as early as 2004. The plan still needs the blessing of the PUC Commissioners as well as a federal bankruptcy court but it does send a strong signal that regulators in the state are serious about allowing the utility to return to financial stability. Consumer activists in the state are criticizing the plan as, "a massive bailout of PG&E…developed entirely behind closed doors," and "a strategy to make ratepayers pay for every penny of deregulation."[7]

Also, in late June 2003, the California Legislature was working on a proposal to dismantle the state's retail choice law and return to traditional rate regulation. Some 50,000 commercial and industrial customers who succeeded in locking in lower priced power under retail choice were working to retain the right to receive electricity under the preferential rates and to continue to shop for power under the new regime. The Legislature is experiencing enormous difficulty in writing the new law in the face of significant opposition from consumer, business, and utility interests.

In June 2003, the State of California's legal effort to recoup nearly $12 billion in energy costs under contracts signed during the height of the 2000-2001 wholesale power crisis was set-back when the Federal Energy Regulatory Commission (FERC) voted 2-1 to uphold the contracts despite massive evidence of market manipulation during the time frame under which they were entered into. The State PUC has vowed to fight on in court on the matter.

Despite the legal, regulatory, and legislative developments mentioned above, the Bay Area Economic Forum, a public-private partnership of senior business, government, university, labor and community leaders, found in a May 2003 report that, "Despite California's aggressive response to the 2000-2001 energy crisis and the ongoing work of regulators to reach policy consensus, there is still a meaningful risk that future power supplies will come up short. One of the key drivers of this risk is a highly uncertain investment climate. In addition, the State's power policy still has significant flaws that will challenge long-term reliability and will contribute to continued high retail electricity costs for consumers."[8]

4.1.3 Montana

On March 24, 2003, the Montana Public Service Commission (PSC) approved guidelines for NorthWestern Energy to follow as the company procures electricity on behalf of its 290,000 mostly residential and small business customers who have not chosen an alternative supplier. In its role as default supplier, NorthWestern must assemble a portfolio of supply contracts to provide electricity to these retail customers. By law, the company must be able to recover its prudently incurred costs for that service. The guidelines will provide the basis for PSC reviews of the prudence of NorthWestern's default supply resource planning and procurement actions and, if followed by the company, will enhance the likelihood of the PSC granting the company full recovery of its default supply-related costs.

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6 "Divestiture Rule Dies After Unanimous Vote, Commission Ushers in Changes in Direction of Electric Competition", Press Release, Arizona Corporation Commission, August 28, 2002.

7 "PG&E Bankruptcy Judge Distributes Settlement", Dow Jones Newswires, June 20, 2003.

8 "California is Still Coming Up Short on Electricity: The State's power sector remains troubled and is at risk of a future supply shortfall", published by the Bay Area Economic Forum, May 2003.

Key elements of the approved guidelines include:

- Identifying NorthWestern's default supplier responsibility to plan and manage its electricity resource portfolio in a manner that results in adequate, reliable, efficient and long-term default supply services at the lowest total cost.
- Provisions that promote the incorporation in the portfolio of cost-effective energy conservation and efficiency resources.
- An emphasis on the importance of NorthWestern using an open and transparent planning and procurement process that produces resource plans that can be understood by everyone. NorthWestern should document its default supply portfolio planning, management and procurement activities to justify the prudence of its decisions.
- Direction to NorthWestern to establish and consult with a default supply portfolio advisory committee comprised of representatives of a broad array of stakeholders in the procurement process.[9]

4.1.4 Pennsylvania

Exhibit V-2 provides the latest statistics compiled by the Pennsylvania Office of Consumer Advocate on the extent to which customers are switching to competitive electricity suppliers.

Exhibit V-2

Percentage Switched As of April 2003

	Residential	Commercial	Industrial	Total
Allegheny Power	**0.2**	**.1**	**0.0**	**0.2**
Duquesne Light	**26.3**	**18.8**	**34.8**	**25.6**
GPU Energy	**0.3**	**0.3**	**2.2**	**0.3**
PECO Energy	**7.3**	**9.7**	**5.2**	**7.5**
Penn Power	**0.4**	**0.2**	**0**	**0.4**
PPL	**0.2**	**2.1**	**3.0**	**0.4**
UGI	**0.1**	**0.04**	**0**	**0.1**

A measure of the deterioration of retail choice in Pennsylvania can be seen in the following two graphs that show the number of megawatts of energy sold by competitive providers. Exhibit V-3 shows the energy sold by competitive providers to all customers and Exhibit V-4 shows the quantity of energy sold by competitive providers to industrial customers. In both instances, the more recent sales are considerably below that of three years ago.

According to statistics published by the Energy Association of Pennsylvania, the state generates well over 33,000 megawatts (MW) of energy per year -- about 5% of the total US capacity. Pennsylvania is second only to Texas in the amount of electric energy generated. Thus, as shown in the graphs, the quantity of energy sold by competitive providers is not a substantial factor in the total state market.

Pennsylvania's retail market is also experiencing other difficulties. In December 2001, the Pennsylvania Office of Consumer Advocate announced that about 800 former customers of "Utility.com" would be receiving approximately $50,000 in refunds. Refunds of about $70,000 had previously been distributed to 1,000 former "Utility.com" customers. "Utility.com" was an electric generation supplier located in Emeryville, California that did business primarily over the internet until it abruptly stopped serving customers and went out of business.

[9] Press release of the Montana Public Service Commission dated March 24, 2003.

The residential market in Pennsylvania once had some 500,000 customers being served by alternative energy providers. Today, that number has been cut in half and continues to fall quarterly. The number of MW of power sold by alternative providers to residential customers is now only 568 -- a mere fraction of what it was two years ago. Sonny Popowski, Pennsylvania's State Consumer Advocate -- and a chief proponent of retail choice -- acknowledges that the residential choice market is essentially a niche market for customers seeking green power.[10]

Exhibit V-3
Total Customer Load (MW) Served by Alternative Suppliers in Pennsylvania

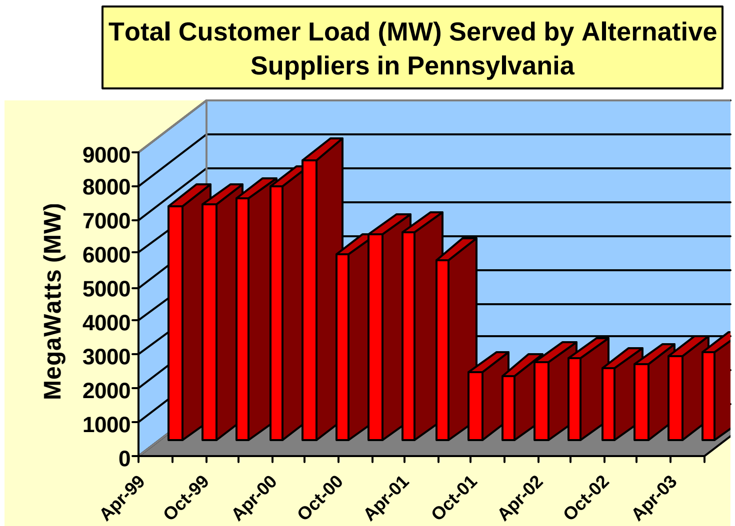
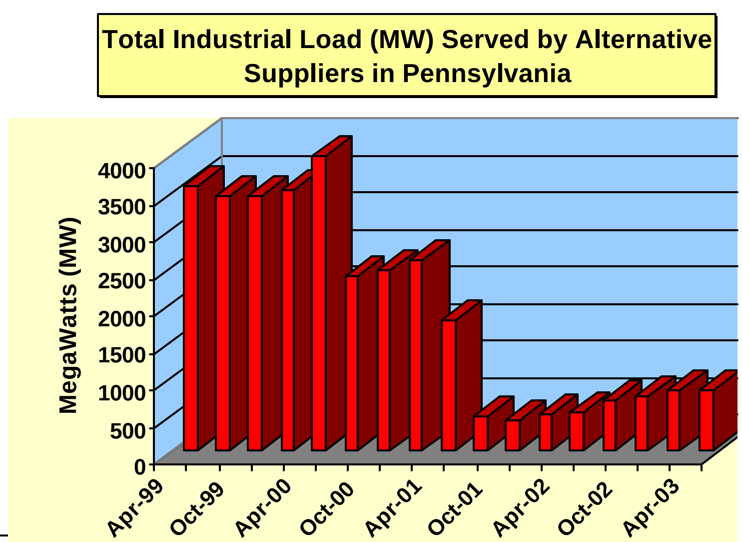


Exhibit V-4
Total Industrial Load (MW) Served by Alternative Suppliers in Pennsylvania



[10] "Pennsylvania homes buy less power in market"; Restructuring Today; January 6, 2003, P.3.

In an effort to artificially "jump start" the moribund residential market, the Pennsylvania Public Utility Commission voted 3-2 in May 2003 to approve a plan devised by the Philadelphia based, PECO Energy Company to re-assign about one third of PECO's residential customers to service by alternative energy providers. The customers will be selected at random and will have the opportunity to opt-out of the switching plan. PUC Chairman Glen Thomas remarked that, "Revolutionizing Pennsylvania's electricity markets will take time and, occasionally, a little prodding."[11] However, the plan to re-assign customers is running into significant difficulties and as to date, no competitive supplier has shown an interest in serving them.

The *Philadelphia Inquirer* noted that, "An earlier attempt to shed residential customers under the deregulation requirement failed when the chosen alternative supplier -- New Power Co., an ENRON Corp. spin-off -- bailed out of the market in April 2002. Nearly 300,000 New Power customers, who had been guaranteed a 2 percent discount from PECO's rates, were returned to PECO because New Power could not afford the climbing wholesale price of electricity. PECO honored the 2 percent discount.[12]

Pennsylvania, like many jurisdictions, has experienced some initial reduction in retail electric rates. However, rates have recently been increasing.

4.1.5 New York

The website of the New York Public Service Commission provides the following data as of March 2003 on the extent of customer switching in the New York retail electric market (see Exhibit V-5).

Exhibit V-5

New York State Customer Migration as of March 2003	TOTAL		Non-residential		Residential	
	Customer Accounts	Load (MWh)	Customer Accounts	Load (WMh)	Customer Accounts	Load (MWh)
Customer and load migration	394,094	2,142,549	70,970	1,930,779	323,124	211,769
Total Eligible	7,336,567	9,506,947	918,605	5,741,332	6,417,962	3,765,615
% Migration	5.4%	22.5%	7.7%	33.6%	5.0%	5.6%
% Change from March 2002	7.9%	29.6%	26.9%	31.1%	4.4%	17.4%

4.1.6 Connecticut

Although retail choice has technically been in effect since July 2000, the concept remains more theory than reality as most suppliers have shown little interest in the Connecticut market. According to one of the state's leading

[11] "Electricity customers set for transfer"; *Philadelphia Inquirer*, May 2, 2003.
[12] "Electricity customers set for transfer", *Philadelphia Inquirer*, May 2, 2003.

newspapers, *The Connecticut Post*, "companies aren't exactly jumping into the Connecticut market and those that are in are getting out. Green Mountain Energy Co. announced it was pulling out of the market as of Friday (Jan. 17, 2003), … after less than a year of being in Connecticut."[13]

A second news article from Connecticut found that, "The much debated, discussed and ballyhooed restructuring of the electric industry has so far provided very little change for the average customer. Prices have remained stable and the vast majority of consumers are buying electricity as they always have. It appears that none of that is likely to change any time soon."[14]

Much of the difficulty in the Connecticut market relates to the manner in which the original deregulation statute was written by the legislature. In order to protect consumers, the legislature required that the incumbent utilities sell electricity at a "standard offer" price set at 10% below the 1996 retail price of power. Thus, consumers, by simply doing nothing different, reaped benefits from the new law and competitive suppliers were discouraged from entering the market.

However, in May 2003, the Connecticut legislature enacted a statute that extends the retail choice program and revises the calculation of "standard offer" price upwa rd in a manner designed to attract competitive suppliers into the market. Under the new law, the previous timetable for the implementation of a renewable portfolio standard is extended and the definition of "renewable resource" is expanded. In addition, the law revives customer education programs and requires the Connecticut Department of Public Utility Control to post information about competitive suppliers on its website.

4.1.7 Maine

The chart below, taken from the web page of the Maine PUC, shows the progression of the percentage of load served by competitive suppliers for the three customer classes for the period July 2000 through January 2003 (see Exhibit V-6 and V-7).

The citizens of Maine have historically been favorable to the development of renewable energy resources that are abundant in the state but are not fully utilized due to cost. Maine's new Governor John Baldacci has pledged to commit the state government to purchasing at least half of its electricity needs from renewable sources and a coalition of two-dozen organizations known as the Maine Green Power Connection is attempting to sign-up 60,000 customers for a green pricing program by 2008.[15]

[13] "Some Fear Changes to Connecticut's Energy market Will result in Higher Bills", *The Connecticut Post*, January 19, 2003.
[14] "Electric Industry remains Relatively Unchanged in Connecticut", *The Day*, December 31, 2002.
[15] "Maine target -- 5% green by 2008", *Restructuring Today*, March 17, 2003, p.2.

Exhibit V-6

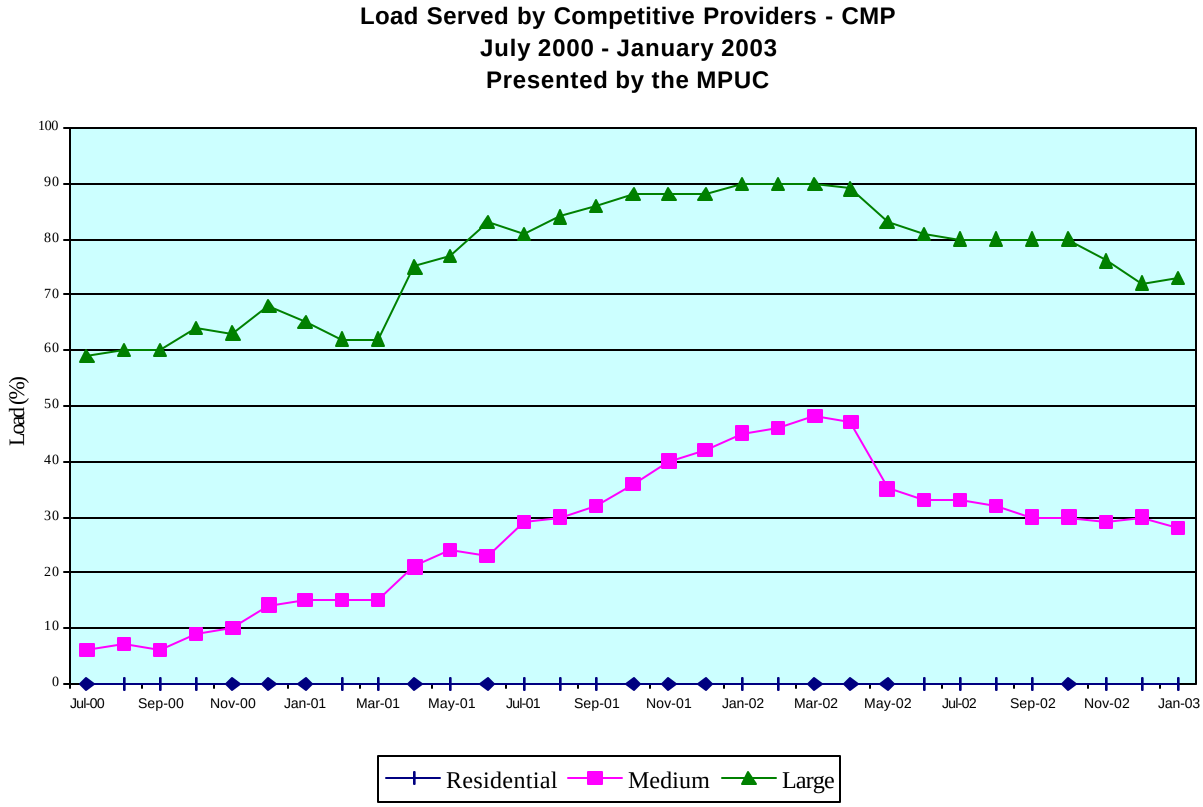


Exhibit V-7

Maine's Electricity Load Served by Competitive Providers Expressed as a Percentage of Total Load As of June 1, 2003			
	Central Maine Power	Bangor Hydro Electric	Maine Public Service
Residential/Small Commercial	<1%	<1%	34%
Medium	25%	27%	68%
Large	77%	36%	100%
Total	34%	17%	60%
Total state load served by competitive providers: 33%			

4.1.8 Rhode Island

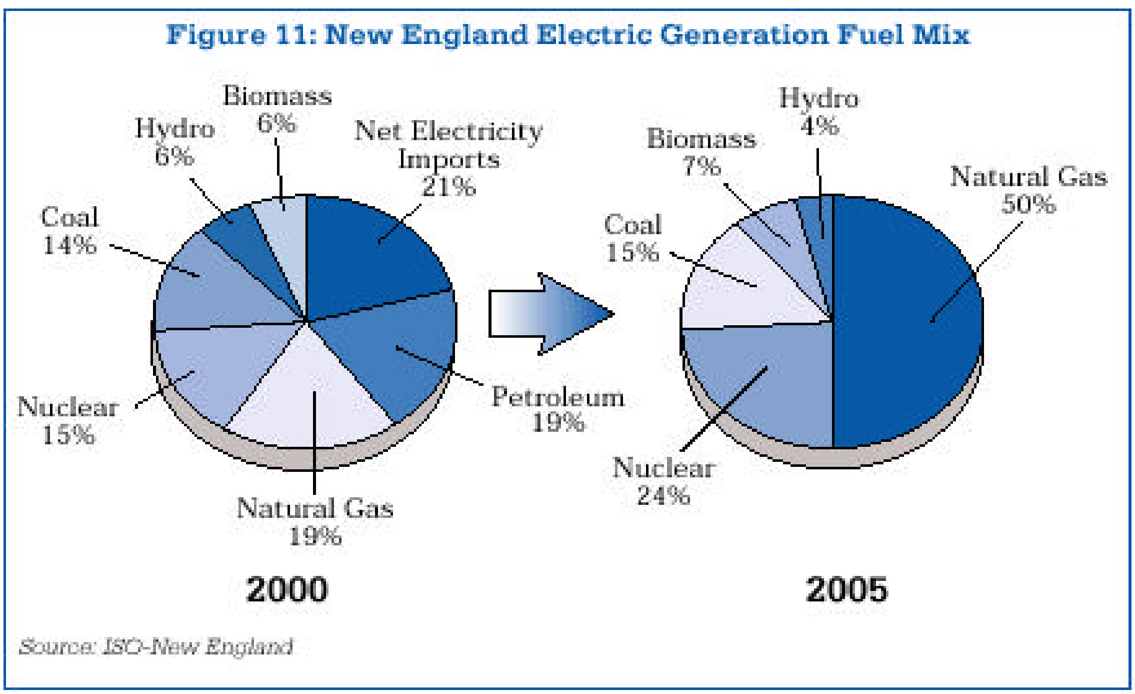
The Rhode Island PUC web site contains no recent information on retail choice in the state. Their web page continues to show a report to the Rhode Island Legislature dated February 2001 -- no update has been prepared. A phone call to the agency confirmed that there is only very minimal retail competition in the state and that it is limited to the largest customers with the most attractive load profiles. For all practical purposes, there is no competition in the residential or commercial markets.

4.1.9 Massachusetts

As a percentage of the total electricity market, retail choice in Massachusetts is quite small -- probably in the range of about 15% of all electricity sold. The overwhelming percentage of energy sold in the competitive market is sold to the largest customers (see Exhibit V-9). There has been some minimal success in marketing to residential customers via a municipal aggregation program in the Cape Cod region of the state. As shown in the graphic below (see Exhibit V-10), the competitive market suffers from wide swings due to the volatility of wholesale prices. As a result, many suppliers have found that marketing to customers other than those with ideal load profiles is far too expensive with too little pay-back.

Some analysts of the New England electricity market are now raising flags of caution on the region's increasing reliance on natural gas as the fuel of choice for new generating facilities. The region's fuel diversity is now undergoing substantial revision due to environmental concerns and the cost of construction associated with coal and nuclear generation. According to a 2003 report of the Associated Industries of Massachusetts, "New England's reliance on natural gas to fuel all new plants (see Exhibit V-8 below) has raised concerns that new plants may cause existing natural gas pipeline capacity to be approached or exceeded within a few years. In addition, up to 75% of the new power plants being built or currently in operation are located on just two of the region's five major pipelines. As a result, the security of the gas grid is becoming increasingly important to the reliability of the electric grid."[16]

Exhibit V-8



[16]"Electric Industry Restructuring in Massachusetts: After the Revolution, the Evolution ", published by the Associated industries of Massachusetts, Winter 2003, p.28

Exhibit V-9

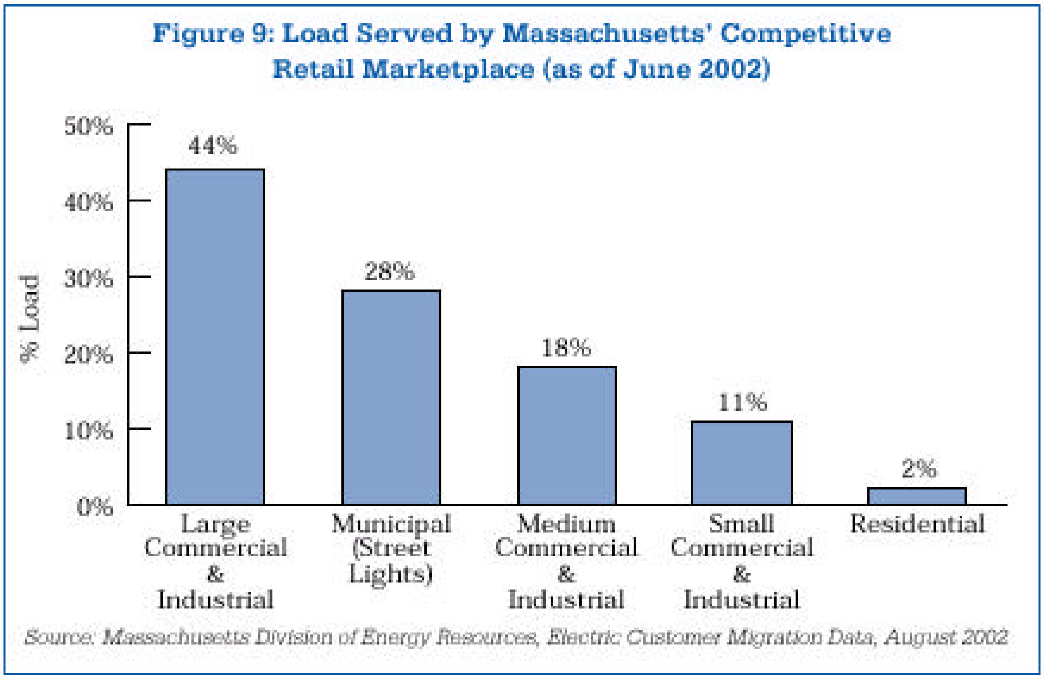
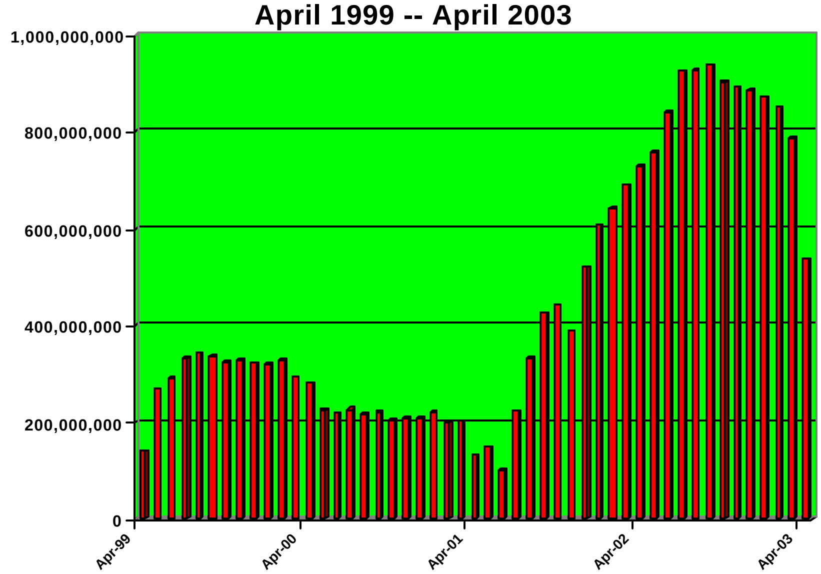


Exhibit V-10

Monthly kWh Sales by Competitive Suppliers in Massachusetts
April 1999 -- April 2003



5.0 Recent Adopters of Retail Choice

5.1 Ohio

In May 2003, the Ohio Public Utility Commission issued a progress report to the Ohio Legislature on the status of retail choice in the state. The Executive Summary of the report indicates that most of the success reported by the Commission to the Legislature is a result of the customer aggregation provisions of the retail choice law in Ohio. For example, the report notes that in the first two years of retail choice…

> • More than 150 local governments passed ballot issues and were certified by the Public Utility Commission of Ohio to allow local units of government to represent their communities in the competitive electricity market. Ohio is home to the Northeast Ohio Public Energy Council (NOPEC), the largest public aggregator in the United States. NOPEC represents 112 communities in eight counties and more than 350,000 residential customers.
>
> Of those customers who have switched in Ohio, aggregation programs account for:
>
> • Nearly 93 percent of residential customers who have switched in Ohio (see Exhibit V-11).
>
> • More than 88 percent of commercial customers who have switched in Ohio.
>
> • Nearly 20 percent of industrial customers who have switched in Ohio.
>
> • In the residential market, the megawatt hours sold by alternative suppliers reached 60 percent in the Cleveland Electric Illuminating Company territory, 36 percent in the Toledo Edison Company territory, 22 percent in the Ohio Edison company territory, and 2 percent in the Cincinnati Gas and Electric Company territory.
>
> • In the commercial market, the megawatt hours sold by alternative suppliers reached 50 percent in the Cleveland Electric Illuminating Company territory, 51 percent in the Toledo Edison Company territory, 38 percent in the Ohio Edison Company territory, 32 percent in the Cincinnati Gas and Electric Company territory, 9 percent in the Dayton Power and Light Company, and 6 percent in the Columbus Southern Power Company territory.
>
> • In the industrial market, the megawatt hours sold by alternative suppliers reached 32 percent in the Ohio Edison Company territory, 28 percent in the Dayton Power and Light Company territory, 20 percent in the Cleveland Electric Illuminating Company territory, 18 percent in the Cincinnati Gas and Electric Company territory, and 5 percent in the Toledo Edison Company territory.[17]

A press release issued by the Ohio PUC dated May 28, 2003 quotes PUC Chairman Alan Schriber as stating that, "Of the twenty-four states in the United States that have adopted electric choice, Ohio's experience has been among the best. While it is difficult to argue that

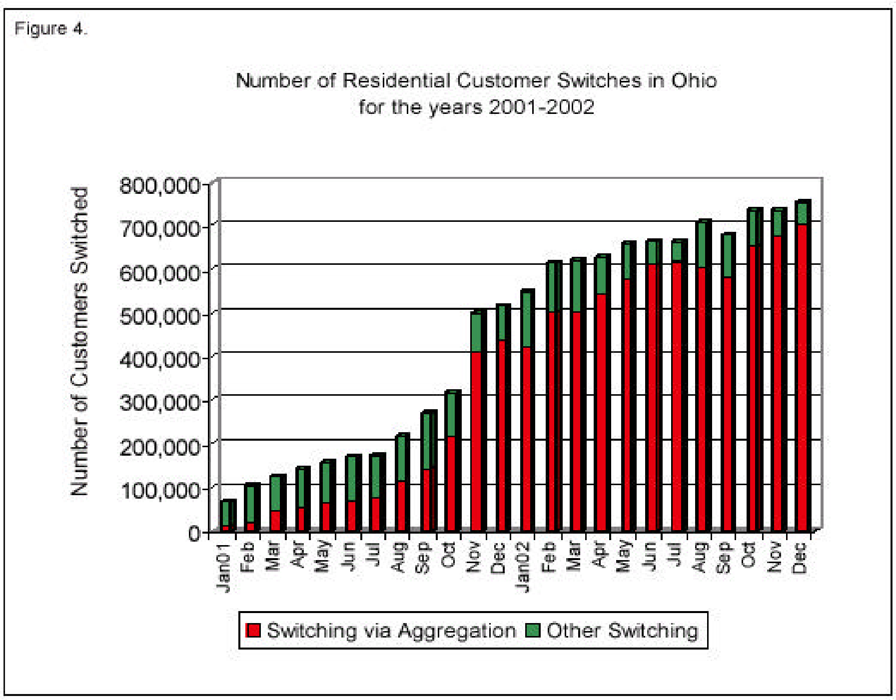
[17] The Ohio Retail Electric Choice Programs Report of Market Activity 2001 - 2002, published by the Ohio Public Utilities Commission, May 2003, Executive Summary.

electric choice has been pervasive anywhere, under the circumstances, Ohio's program has so far been a success."[18]

However, Schriber's view is tempered by statements from others including Schriber himself. Richard Marsh, chief financial officer for Akron-based FirstEnergy the parent company for Toledo Edison, said commercial, industrial, and residential customers are being served at rates far below even wholesale rates because Ohio's deregulation plan locked them into such prices through 2005. Customers of FirstEnergy could be in for "rate shock" after 2005 when deregulation in Ohio is complete and the utility can raise rates, possibly well above current locked-in prices. PUC Chairman Schriber concurred and acknowledged that his agency is "very concerned" about the potential for rate shock. "We're thinking about it a lot. It consumes us actually."[19]

David Hughes, Executive Director of Citizen Power -- an Ohio citizen watchdog group -- dismisses all of the talk of success in the Ohio retail electric market. "The numbers (on switching) look good because PUCO does not tell us who those alternate suppliers are. If you look closely, you will see that the vast majority of customers have not switched to a real alternative because PUCO counts switches to utility affiliates as a competitive switch. That's one way to inflate the numbers and make it look like there is competition." Hughes also contends that the fear of "rate shock" just around the corner, "is warranted because there is nothing to stop unregulated monopolies like DP&L and Ohio's other utility companies from charging whatever they want once the market development period ends."[20]

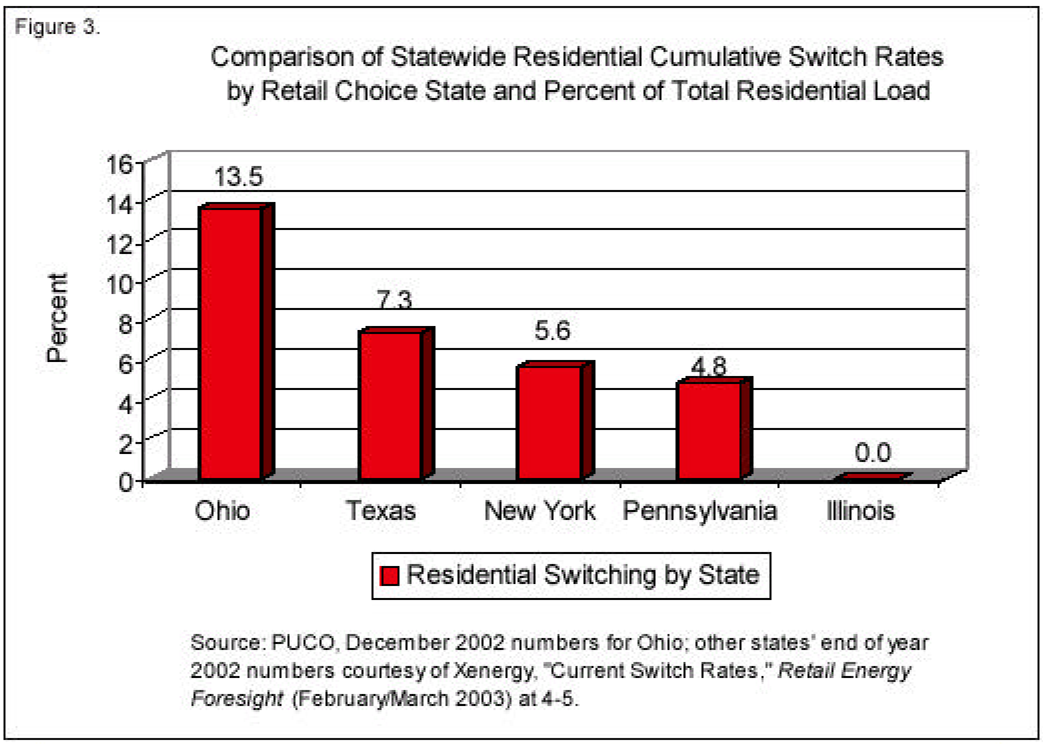
Exhibit V-11



[18] Press release of the Ohio PUC dated may 28, 2003: "PUCO Issues Electric Choice Market Activity Report to Ohio General Assembly".
[19] "Electricity Rate Shock Predicted when Ohio Deregulation Expires", *The Toledo Blade*, March 27, 2003.
[20] "Consumer watchdog calls for end of Ohio deregulation", *Restructuring Today*, June 3, 2003.

Exhibit V-12 below displays an estimate of the percentage of total residential load purchased from alternative suppliers as of year-end 2002 in five selected states according to an analysis conducted by the Xenergy consulting firm.

Exhibit V-12



5.2 Illinois

The May 2003 report of the Illinois Commerce Commission to the Illinois General Assembly presents data (see Exhibit V-13) on the extent to which customers have switched to alternative suppliers. On the surface, the data seem to show that the two largest investor-owned companies serving Illinois (Commonwealth Edison and Illinois Power) have suffered significant losses of revenue due to customer switching. However, these two companies are controlled by holding companies (Exelon and Dynergy respectively) that also own non-regulated energy marketing companies who have been certified by the Illinois Commerce Commission to "compete" with the incumbent utilities. The Illinois Commerce Commission provides no data on the percentage of revenue "lost" by the incumbent utilities that is actually due to the switching of customers from the incumbent to a sibling marketing company owned and controlled by the same parent energy holding company. In any event, of the 15 alternative energy suppliers certified by the Illinois Commerce Commission, none have requested certification to serve residential customers.

Exhibit V-13

Table 1: Customer Switching and Transition Charge Data

Electric Utility	Number of Customers That Have Elected Delivery Services		Amount of Usage Switched to Delivery Services (kWh million)		Revenue Loss Resulting from Customers Switching to Delivery Services ($ million)		Transition Charge Revenue Collected ($ million)	
	2002	2001	2002	Cumulative[2]	2002	Cumulative	2002	Cumulative
Ameren CILCO	AmerenCILCO reported no activity.							
AmerenCIPS	747	770	1,462	2,165	0.0	3.5	2.5	5.1
AmerenUE	0	0	0	3	0.0	0.1	0.0	0.0
ComEd	21,652	18,268	22,710	54,081	566.2	1,308.8	309.5	576.6
Illinois Power	1,051	853	5,106	10,978	86.1	202.9	32.7	54.4
Interstate	Not applicable; no customers have selected delivery services from Interstate.							
MidAmerican	9	82	1	74	0.0	2.8	0.0	0.0
Mt. Carmel	None reported.							
South Beloit	Not applicable; no customers have selected delivery services from South Beloit.							
Total	23,459	19,973	29,279	67,301	652.3	1,518.1	344.7	636.1

5.3 Texas

Because of the national significance of the public policy choices adopted in Texas, the material below contains background on the Texas retail electric program as well the most recent results of their efforts.

Legislation was enacted in 1999 to begin the process. Under the new law, the Texas PUC will begin the process of certifying competitive retail electric providers. On June 1, 2000 a pilot retail competition program commenced and on January 1, 2002 full retail choice began for all customers at which time retail rates were reduced by 6%.

Following are the key provisions of the new law:

- Froze electric rates for investor-owned electric utilities in Texas through 2001.
- Prohibits large utilities from lowering their rates for residential and small commercial customers before 2005, or until 40 percent of their customers are served by competitors.

- Exempts electric cooperatives and city-owned electric companies from customer choice unless their governing boards decide to open their markets to competition.
- Allows customers the choice of using renewable energy (wind and solar power for example).
- Requires older electric generators to meet current environmental rules by 2003 or be shut down.
- Creates a fund to pay for lower rates for low-income families and property tax losses for affected school districts.
- Provides for automatic enrollment of qualified low-income families in low-income assistance programs.
- Prohibits disconnection of service for nonpayment during periods of extreme weather.
- Allow customers to receive one bill for their electric service in an easy-to-read format and understandable language.
- Creates a Do Not Call list for customers who do not wish to be called by telemarketers on behalf of electric service providers.
- Provides customer protection against discrimination, against being billed for unauthorized charges (cramming), against unauthorized change of service provider (slamming) and other unfair, misleading and deceptive practices.

Texas has noted it is considerably different than California in its approach to retail deregulation. Generation capacity has been expanded within the state, so it does not rely on imports of electricity. Peak demand for the summer of 2001 was approximately 67,000 megawatts and statewide capacity was at 83,000 MW which provided a 24 percent reserve margin according to a June 20, 2001, news release from the Public Utility Commission of Texas. However, transmission investment has not kept up with generation expansion. Also, more than 45 percent of the generation is gas fired, leading to some concerns about future volatility in gas prices.

Deregulation of retail sales of electricity in southeast Texas was delayed until 2003 due to the lack of a regional transmission organization (RTO). Investor utilities serving southeast Texas did not draw competition during the pilot program. With an RTO there are hopes to get out-of-state competitors to ship electricity into southeast Texas. Also in northwestern and southwestern Texas, deregulation has also been delayed because those were not considered ready.

Under the Texas deregulation program, electric utilities were divided into three areas: retail, power generation and transmission and distribution. Any investor-owned companies that wish to enter the retail market must create an affiliate company. To ensure deregulation, the Texas Public Utilities Commission created a price-to-beat for investor-owned affiliates that will remain in place until 2005 or until 40% of customers switch to another retail company.

On January 15, 2003, the Texas PUC published a comprehensive report to the Texas Legislature on the status and progress of retail competition in the state after one full year of implementation. The cover letter to the report makes the following observations:

- "The Commission's estimates in this report show that retail customers have saved, at a minimum, over $1.5 billion in electricity costs during the first year of competition as compared to the regulated rates in effect during 2001. Additionally, low-income customers have received almost $70 million in discounts through the System Benefit Fund through October 2002."

- "In all areas open to competition, there are multiple retail electric providers (REPs) offering service to all customer classes, with as many as ten REPs offering service to residential customers in some areas. Customers are continuing to exercise their opportunity to choose an electric provider in increasing numbers."

- "The Commission has administered a customer education campaign to inform customers in Texas about the choices available to them in the new market, including the distribution of over 5 million copies of the *"Power Guide to Electric Choice"* to customers throughout the state."[21]

The PUC's glowing letter is backed up with data and graphical presentations of a competitive market that is small but trending upward. The report notes that, "as of the end of September 2002, 400,837 individual customer premises were being served by a REP other than the incumbent affiliated REP in their service area. This number represents approximately 6.8% of all customers in areas open to customer choice. Of these premises, 319,297 (80%) are residential customers. Approximately 18% (71,691 customers) of the customers are commercial and/or industrial customers that take service at the secondary voltage level (predominately smaller commercial customers eligible for the price to beat." (See Exhibit V-14)

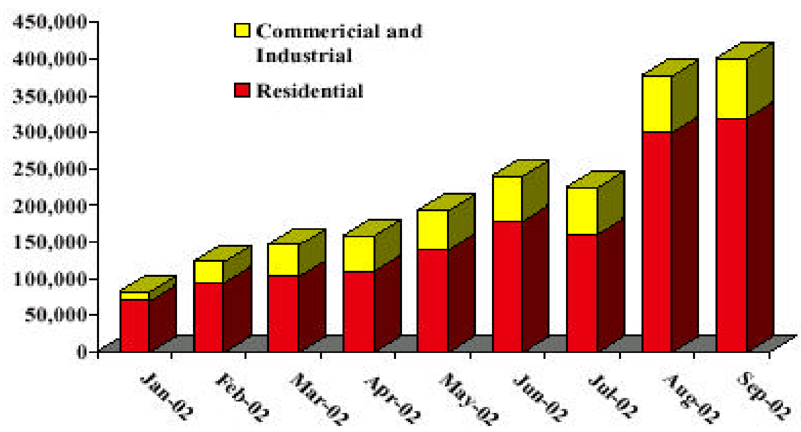
"A total of 6,070,477 megawatt hours (MWhs) were served by non-affiliated REPs in September 2002. This represents approximately 25% of the total MWhs sold in September. This number is higher than the percentage of customers who have switched because the larger commercial and industrial customers comprise a significant portion of the energy consumption in the state. While commercial and industrial customers only account for 20% of the customers who have switched, these customers comprise over 90% of the megawatt hours (MWh) served by non-affiliated REPs in areas open to competition."[22]

"What I look for as a measure of success is a continuing trend line," says Rebecca Klein, chairwoman of the Texas PUC. "I'm not looking for a spike or a double-digit figure today; rather, I would like to see the switch rate trend upward over the course of time. Competition is here to stay and it's not an experiment."[23]

"By-and-large, we have done it right…and have accomplished what we set out to do," says Tom Noel, CEO for the Electric Reliability Council of Texas (ERCOT), an independent system operator. "However, until customer's issues have been resolved satisfactorily and until we can say that every time a customer decides to switch that the process is done quickly, efficiently and smoothly, we won't be satisfied."[24]

Exhibit V-14

Figure 14: Number of Customers Served by a Competitive REP in ERCOT

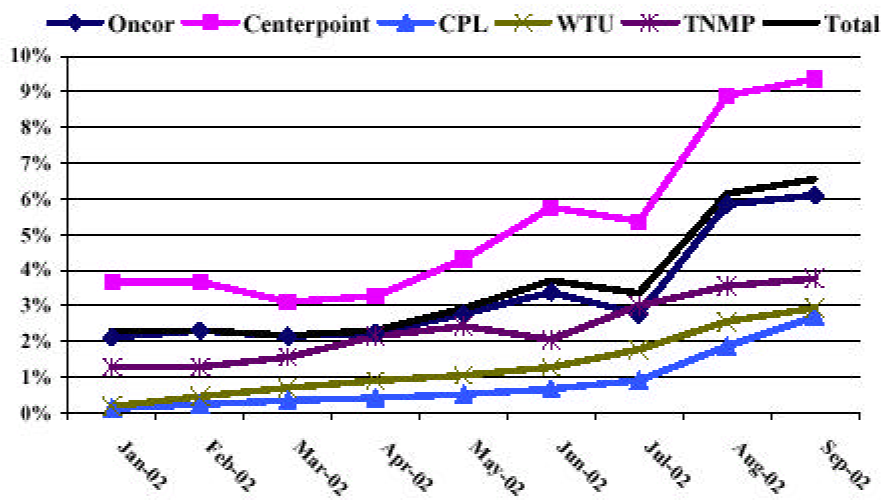


SOURCE: Texas PUC 2003 Electric Scope of Competition Data Responses from TDUs.

[21] January 15, 2003 letter from the Texas PUC to the members of the Texas Legislature
[22] "Scope of Competition in the Electric Market in Texas", 2003 report of the Texas PUC to the Texas Legislature, January 2003, pp. 88-89
[23] "Texas Committed to Deregulation", by Ken Silverstein, Utilipoint Issue Alert, December 20, 2003
[24] "Texas: The Turning point for Energy Deregulation", by ken Silverstein, Scientech Issue Alert, July 18, 2002

Exhibit V-15

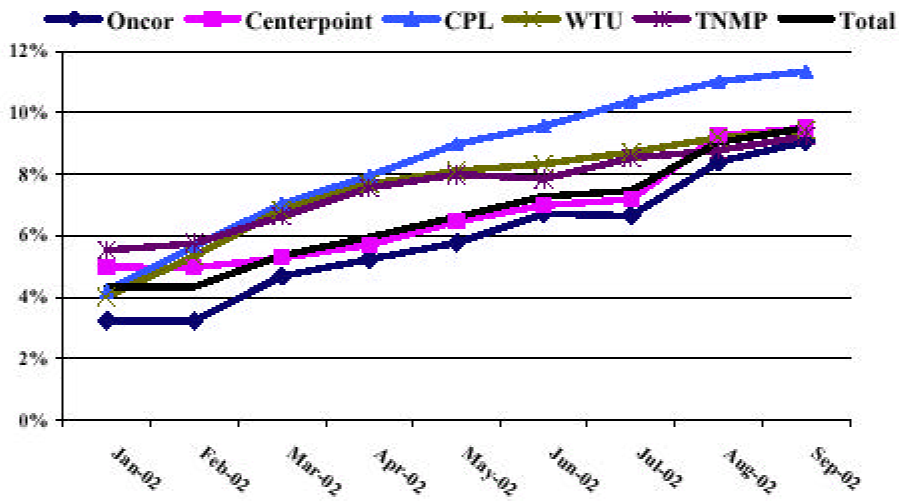
Figure 16: Percentage of Residential Customers Served by a Competitive REP



SOURCE: Texas PUC 2003 Electric Scope of Competition Data Responses from TDUs.

Exhibit V-16

Figure 17: Percentage of Small Commercial Customers Served by a Competitive REP



SOURCE: Texas PUC 2003 Electric Scope of Competition Data Responses from TDUs.

The progress shown in the above two charts (Exhibits V-15 and 16) is further corroborated by more recent information from the Texas PUC (see Exhibit V-17). In a June 12, 2003 conference call with financial analysts, Texas PUC Chair Rebecca Klein released the data in the chart below that shows that the percentage of residential and small commercial customers who are switching to competitive suppliers continues to grow. In many instances such customers are taking advantage of a web site (www.powertochoose.org) that allows customers to enter their zip code and then be presented with instant information on competitive supply offers including price and fuel mix of the various providers.

Exhibit V-17

	Percentage of Residential Customers Served by Non-affiliated Retail Electric Provider		Percentage of Small Commercial Customers Served by Non-affiliated Retail Electric Provider	
TDSP Service Area	Sept 26, 2002	June 2, 2003*	Sept 26, 2002	June 2, 2003*
AEP Texas Central	2.7%	9.2%	11.5%	17.1%
AEP Texas North	2.9%	9.2%	9.4%	13.9%
Centerpoint	9.4%	10.5%	9.5%	14.5%
Oncor	6.1%	10.8%	9.1%	14.8%
TNMP	3.8%	6.5%	9.2%	9.1%

The Texas retail choice model has not been without its problems. The *Houston Chronicle* reported that, "when the Texas electricity market opened in January 2002, New Power was one of the more aggressive marketers. It signed up about 78,000 customers in the Dallas and Houston areas. The company, based in Purchase, NY, filed for Chapter 11 bankruptcy protection in June (2002). It struck a deal to give its 34,000 Houston-area customers to Dallas-based TXU Energy."[25]

Technical glitches have delayed hundreds of thousands of bills and blocked some switching requests. The *Dallas Morning News* reported that in November 2002 the Texas PUC received 1,500 complaints, five times more than it received in November 2001. PUC Chair Rebecca Klein said that, "the increase is to be expected when you consider the fact that we've transformed significantly in the electricity market."[26]

A far more serious problem emerged in March 2003 when a surge in wholesale power prices indicated evidence of market manipulation. Jess Totten, director of policy at the Texas PUC told Reuters News Service, "I hate to say it, but I think we need some regulation of people in the merchant energy business. Some merchants are using 'gaming' practices including taking advantage of congestion in the design of the power line system to help drive prices higher. In a sense, they were playing some of the same kinds of games that people out in California were doing. Traders have also overstated expected trading volumes, then revised those volumes lower when officially registering the deals, which can drive up average prices."[27]

6.0 Reconsideration of Retail Choice

6.1 Nevada

In 2001, Assembly Bill No. 369 was enacted that effectively repealed the implementation of retail choice. The preamble of the repeal legislation provides insight into the view of the state legislature on this question. Here are some excerpts from the preamble of the repeal legislation.

[25] "Texas Commission Fears Bankrupt Electric Company Will Leave Customers in Lurch", *Houston Chronicle*, September 12, 2002.

[26] "Texas Electricity Firms, Consumers Voice Deregulation Concerns", *The Dallas Morning News"*, December 13, 2002.

[27] "Texas power market hit by price spikes, gaming", Reuters News Service, March 13, 2003.

- *Several of the major industries in this state are particularly dependent upon electricity. Under present market conditions in the electric industry, comprehensive and effective regulation of electric utilities in this state is vital to the economy of this state and is essential to protect the health, safety and welfare of the residents of this state. Until present market conditions have changed and adequate mechanisms have been developed to allow this state to adjust its comprehensive regulation of electric utilities in Nevada, this state has a compelling interest in continuing its comprehensive regulation of electric utilities to protect the consumers in this state, to safeguard the economy of this state and to ensure that the electric utilities in this state provide adequate and reliable electric service at just and reasonable prices.*

- *In recent years, the western United States has experienced a severe and ongoing crisis in the electric industry marked by critical shortages in the supply of electricity and extreme volatility in the price of electricity in the wholesale and retail markets. The severe and ongoing crisis in the electric industry in the western United States is both an immediate threat and a continuing danger to the economy of this state and to the health, safety and welfare of the residents of this state.*

- *Until the severe and ongoing crisis in the electric industry in the western United States has sufficiently abated, this state must maintain its comprehensive regulation over electric utilities and its traditionally broad jurisdiction and control over electric generation assets to promote stability and predictability in the electric industry, to foster confidence in the financial markets, to ensure that consumers have adequate and reliable electric service and to protect the public from unjust and unreasonable utility rates.*

Also enacted in the 2001 legislative session was AB 661 that allows larger customers (annual consumption of 1 MW or more), as well as educational institutions, local governments and hospitals, to choose an alternative supplier. Such customers must document a public interest benefit and win state regulatory approval before exiting. On May 29, 2003, The Palms Casino became the 12th large customer to win regulatory approval to purchase power from a competitor of Nevada Power Company. Not all of these customers have actually switched providers but Reliant Resources of Houston, Coral Power (an affiliate of Shell Oil Co.), Arizona Public Service, and Sempra Energy are all actively marketing to the large users in Nevada with varying degrees of success.

6.2 Arkansas

The Arkansas General Assembly enacted retail choice legislation in 1999 and amended it during the 2001 session. The amended bill postponed the start of retail competition in Arkansas from Jan. 1, 2002, until at least October 2003 and no later than October 2005. Then, in early 2003, the Arkansas Legislature spoke again on this question and enacted HB 1114, the Electric Utility Regulatory Reform Act that repealed the 1999 law.

The preamble to the new legislation provides that retail choice should be repealed because, "the environment in the electric utility industry has changed, and it is in the public interest to continue regulating electric rates for the foreseeable future and the Arkansas Public Service Commission has determined that Arkansas' electric ratepayers would be unlikely to benefit from, and could be harmed by, retail electric competition for the foreseeable future, and has recommended to the General Assembly that implementation of retail electric competition in Arkansas either be delayed for a significant period of years or be repealed."[28]

Section 17 of the bill provides that, "The Arkansas Public Service Commission shall conduct a collaborative meeting to study the feasibility of a large user access program for electric service choice, including a commitment to insure there is no cost shifting to any other class of customers, and report to the General Assembly on or before September 30, 2004."

[28] HB 1114 (2003), introductory language, Arkansas State Legislature.

7.0 Federal Issues

This section is intended to replace section 9.0 of last year's report.

Driven in large part by the electricity supply and reliability problems in the western United States, the issues of restructuring have now been expanded to include energy supply and infrastructure concerns. Transmission across the United States is frequently inadequate to support retail deregulation. Legislation addressing regional transmission entities, eminent domain, transmission reliability standards, and other issues have been the focus of both Congress and the FERC. Infrastructure/pipelines for natural gas supply have not kept up with growing demand for natural gas which has become the most common fuel for generating facilities built in the last 10 years.

A major focus of both the Bush Administration and Congress has been on development and passage of national energy policy legislation.

Background

- Bush Administration National Energy Policy Development Report Released – May 2001
- House of Representatives responded quickly and passed H.R.4 – August 2, 2001.
- Senate delayed consideration of energy policy legislation until early 2002. S.517 passed Full Senate – April 25, 2002.
- House/Senate Energy Conference failed to reconcile differences between H.R.4 and S.517 – legislation died at the end of the 107th Congressional Legislative Session in November 2002.
- Lack of consensus on electricity provisions contained in S.517 was largely responsible for the failure of last year's House/Senate energy conference.

House Energy Legislation – H.R.6

- Draft legislation, released on February 20, 2003, contained 10 Titles/Sections, including an electricity title (Title VII).
- Markup of H.R.6 at the House Energy and Commerce Committee was concluded quickly and the legislation passed the Full House on April 11, 2003.

Some of the Major Electricity Provisions in H.R.6 Include:

- Repeal of the Public Utility Holding Company Act of 1935
- Reform of the Public Utility Regulatory Policy Act of 1978
- Transmission reliability standards
- Continuation of Renewable energy production incentives – REPI
- Consumer protections – FERC merger review authority
- FERC-lite (see below)
- Uniform Refund Authority (see below)
- Service Obligation (see below)

Some of the Major Public Power Priorities in H.R.6 Include:

- FERC-lite – provisions are included that provide limited extension of FERC jurisdiction over public power to ensure non-discriminatory open access to the nation's transmission system.
- Uniform Refund Authority – provisions are included that would grant FERC new authority to order refunds from public power in the event that a utility violates market rules in place at the time of the sale. Limited to spot market sales of 24 hours or less.
- Service Obligation – provisions are included that attempt to protect transmission capacity for those customers whom utilities have an obligation to serve and also paid for the transmission assets.

Senate Energy Legislation – S.14

- S.14 passed the Senate Energy and Natural Resources Committee on April 30, 2003.
- S.14 contains 11 Titles/Sections, including an electricity title.

Some of the Electricity Provisions in S.14 Include:

- Transmission reliability
- FERC-lite
- PURPA reform
- Service Obligation
- Voluntary RTO development – FERC's Standard Market Design (SMD) rules delayed until July 2005
- Consumer Protections

Status

- S.14 was passed by the Senate Energy and Natural Resources Committee by a partisan vote of 12 to 11.
- Senate floor action on S.14 has begun with action likely on an "on-again, off-again" basis until final Senate passage, which is anticipated in late July 2003 or after the August Congressional recess; numerous amendments are expected.
- House/Senate energy conference to resolve differences between H.R.6 and S.14 is not likely to conclude until sometime this fall with anticipation of the final bill being forwarded to the President for his signature in October or November 2003 (if agreement can be reached).

8.0 Conclusions

The establishment of the "condition-certain" approach in LB 901 has proven to be a wise policy decision by the State of Nebraska. This approach recognized the necessity of conditioning retail choice upon the establishment of adequate regional wholesale energy markets and adequate transmission networks, among other issues. Several of the states which opened retail electricity markets or were scheduled to do so on a "date certain" basis have retrenched and are now paying far greater attention to the need to establish viable regional wholesale markets prior to further implementing retail choice.

The following summarizes the conclusions of the report of Technical Group No. 5.

- Rates in retail choice states have been reduced primarily through regulatory mandates and capped during transition periods
- Wholesale prices have increased throughout most of the nation but declined significantly in June 2001 across the western United States
- Marketers have withdrawn or scaled back in many states with retail choice programs
- Few customers have switched suppliers in most retail choice states (and many of them have returned to their incumbent utility)
- California/West Coast Energy Crisis has slowed national interest in retail choice
- Retail choice has taken a back seat to energy supply and other wholesale issues at the federal level
- Promises of wholesale or retail competition driving down energy prices have been generally unfulfilled thus far
- Retail choice is still alive and continues to evolve
- Must get wholesale markets right prior to implementing retail choice legislation
- Adequate power supply and reserves are crucial
- Adequate transmission is crucial
- Increased stability of fuel prices is needed for retail choice programs to function properly
- Better customer response to wholesale price signals are needed
- Development of a comprehensive energy policy has gained significant attention in Congress and the Bush Administration, but details are far from decided due, in part, to narrow political majorities
- FERC is actively involved in developing and addressing the transition to a more competitive wholesale market