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.

2.0 Team Members

Doug Bantam – Lincoln Electric System
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3.0 Introduction

3.1 Deregulation Overview

Little has changed with the development of retail choice around the nation in the past year. Most state retail choice programs are either struggling or inactive. On September 1, 2004, the State Corporation Commission of Virginia issued a press release describing the findings of its fourth annual report on retail choice in Virginia. The press release notes "that the electricity supply industry continues to struggle following price run-ups, disclosures of accounting and dated improprieties, creditworthiness issues and volatile fuel prices, particularly natural gas." The press release concludes "that Virginia is not the exception when it comes to the lack of competitive activity for electricity supply service. In other states with retail choice, energy markets are generally inactive with few customers able to purchase power at a price lower than their traditional utility company."

Because Texas continues to receive attention as the most successful retail choice state, there is a Texas update in this report, but last year's report is deemed adequate to describe the status of retail choice in other states. This report also contains a new section on federal developments. Comprehensive energy legislation passed both the House and the Senate, but the two versions had significant differences. A conference committee reached a compromise and the legislation passed the House, but has been bogged down in the Senate.

4.0 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 began 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.

It is important to note that much of the Texas region is operated as a separate electrical interconnection. This limits and confines the size of the restructured area and restricts the impact of wholesale energy deliveries from potentially lower cost resources. When Texas initiated the retail choice program, the impacted region was operating with significant generation in reserve and significant new Independent Power Producer (IPP) projects underway. In addition, retail rates are relatively high, in the 10¢/kWh range, compared to other regions of the U.S. With high reserves, new generation coming on line and high retail rates, Texas becomes somewhat of a special case. With excess generation capacity, numerous new, highly efficient, independent generation projects and a high underlying retail electric rate level, the Texas region provided a prime opportunity to initiate retail choice. This is not to discount what has been accomplished by the Texas electrical industry. It is, however, a confirmation that for retail choice to be successful, the appropriate preconditions need to be in place.

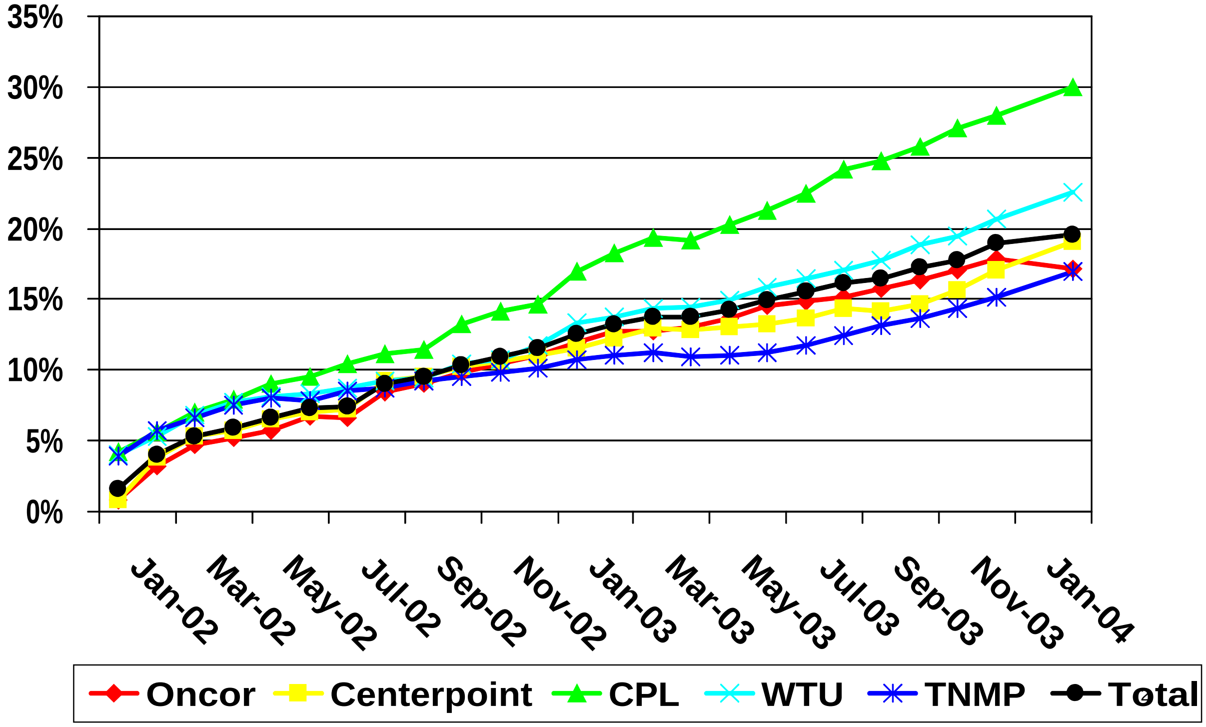
Under the Texas deregulation program, electric utilities were divided into three areas: retail, power generation and transmission and distribution. Any investor-owned companies that wish to enter the retail market must create an affiliate company. To ensure deregulation, the Texas Public Utilities Commission 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. In February of 2004 the price-to-beat in the five distribution areas ranged from 9.7 to 11.66¢/kWh and the percent of customers who have switched stands at 14% for residential and 19% for small industrial.

The Texas Public Utility Commission continues to monitor and report on the status of retail choice in Texas. These "Report Cards" remain positive. Generally, retail choice participation is growing. During 2003, participation at the residential level has grown from just over 7% to 14% and small industrial participation has increased from 11% to 19%.

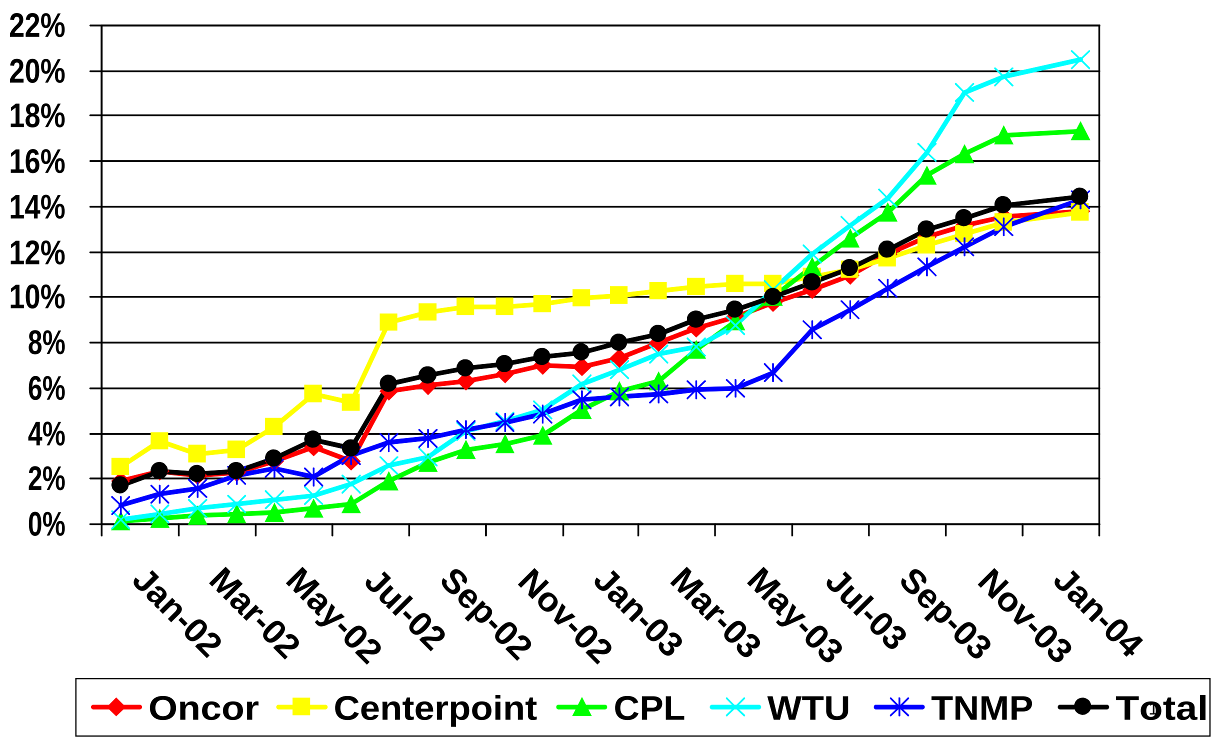
The report indicates that, as of the end of December 2003, 1,285,145 individual customer electric service provider switches have occurred. The percentage of megawatt hours (MWhs) served by non-affiliated retail electric providers (REPs) in December of 2003 included 15% of the residential load and 42% of the small industrial load. These percentages are 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.

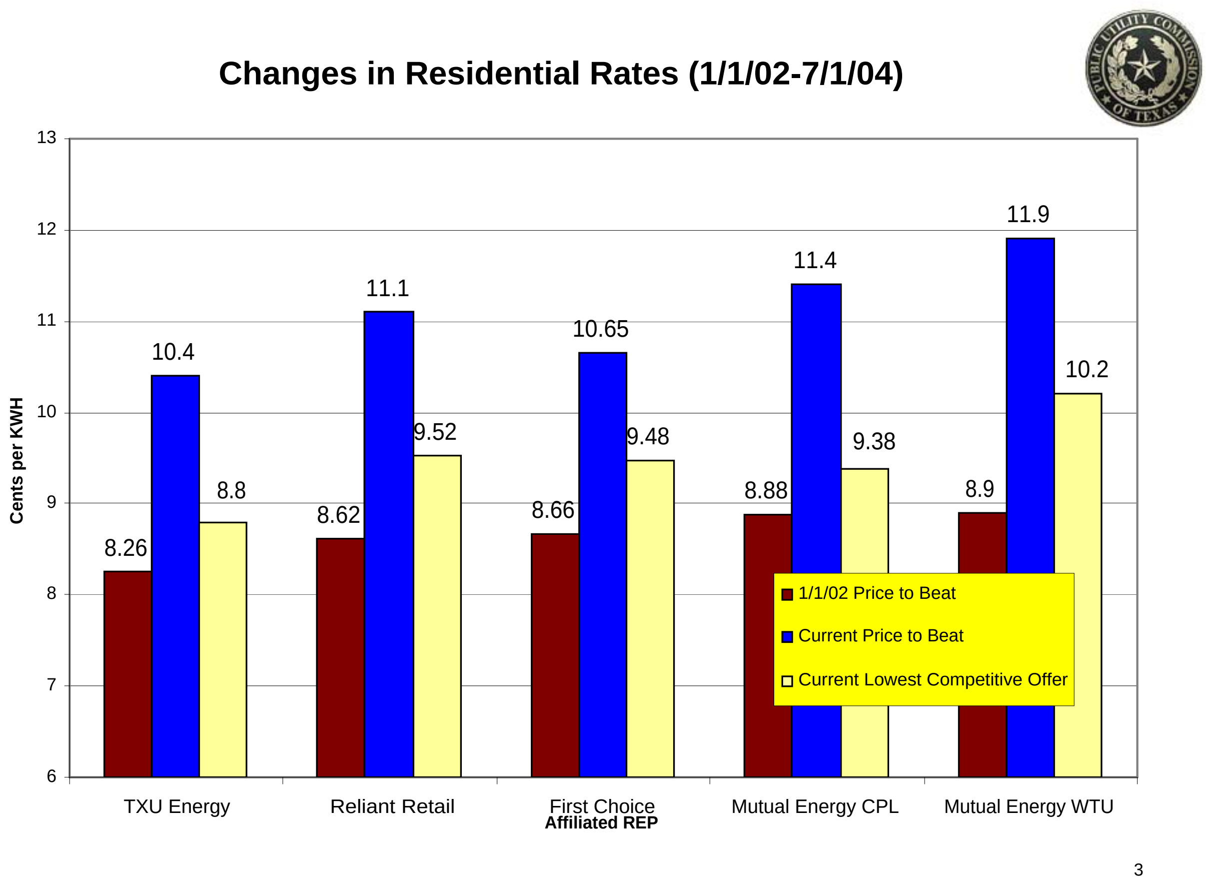
The following charts have been extracted from the most recent Texas Public Utility Commission "March 2004 Report Card on Retail Choice." The Texas Retail Choice Program continues to grow and is considered by the Texas PUC to be a successful and cost-effective program.

Secondary Voltage Level Customers Served by Non-Affiliated REPs



Residential Customers Served by Non-Affiliated REPs




Changes in Residential Rates (1/1/02-7/1/04)
Cents per KWH
13
12
11
10
9
8
7
6
8.26
10.4
8.8
8.62
11.1
9.52
8.66
10.65
9.48
8.88
11.4
9.38
8.9
11.9
10.2
1/1/02 Price to Beat
Current Price to Beat
Current Lowest Competitive Offer
TXU Energy
Reliant Retail
First Choice
Affiliated REP
Mutual Energy CPL
Mutual Energy WTU
3

5.0 Federal Issues

Driven in large part by the electricity supply and reliability problems in the western United States, as well as the large blackout in the Northeast in August 2003, the focus of restructuring has been expanded to include energy supply and infrastructure concerns, as well as reliability. 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 has 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/Status

- 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.
- House of Representatives in the 108th Congress passed H.R.6 on April 11, 2003.
- Senate passed legislation (also designated as H.R.6 after passage) on July 31, 2003.
- House/Senate Energy Conference commenced in September 2003 to resolve legislative differences with final agreement reached on November 16, 2003.
- Energy Conference Report passed by the House on November 18, 2003.
- Energy Conference Report contains XVI Titles/Sections, including an electricity title (Title XII).
- Senate cloture vote to end debate and move forward on the Energy Conference Report on November 21, 2003 failed by a vote of 57 Yeas to 40 Nays, 3 Not Voting (60 votes needed).
- Renewed efforts of passage in 2004 in the Senate have failed with energy legislation likely dead for the remainder of the 108th Congress.

Some of the Major Provisions of Interest to Electric Utilities in the H.R.6 Conference Report Include:

Repeal of the Public Utility Holding Company Act of 1935

Repeal of the Public Utility Regulatory Policy Act of 1978 – eliminates mandatory electric utility purchase requirements for electricity generated by qualifying cogenerators or small power producers.

FERC Lite – limited expansion of FERC jurisdiction over public power to promote wholesale power markets. Public power would provide transmission services at non-rate terms and conditions that are comparable to what we have for ourselves. No FERC ratemaking authority over public power.

Service Obligation/Native Load Protection – requires FERC to ensure that load service entities are allowed to reserve their transmission assets to serve native load customers before transmission capacity is made available to others.

Uniform Refund Authority – authorizes FERC to order refunds from large public power systems if short-term wholesale sales are made in violation of FERC rules.

Participant Funded Transmission – transmission upgrades would be paid for by those requesting the upgrades consistent with FERC criteria.

Transmission Reliability Standards – standards would be FERC approved, mandatory, and enforceable with penalty provisions.

Transmission Siting Authority – FERC authorized to permit and approve needed new transmission if state(s) cause obstacles.

Renewable Energy Production Incentive (REPI) – reauthorizes the REPI program for 10 years, landfill gas projects on equal funding priority as wind, solar, biomass, etc. Comparable to IOU production tax credits in that the payout for generation is over a 10-year period. Funding is dependent on annual congressional appropriations.

RTO Development – includes a sense of Congress that all transmitting utilities should voluntarily join regional transmission organizations. No formal requirement for mandatory RTO membership.

Climate change – Sense of Congress – no mandatory carbon emission reduction requirements

Standard Market Design (SMD) – FERC SMD rules delayed until December 2006

Outlook

With passage of national energy policy legislation in 2004 highly unlikely, it is unknown at this time if Congress will push for passage in the new 109th Congress next year. The outcome of the 2004 elections and Administration and Congressional priorities for 2005 will determine future efforts on national energy policy legislation.

6.0 Conclusions

- Retail choice programs have achieved mixed results ranging from failure (CA) to no impact (AZ) to some success (TX).
- Natural gas prices are at an all time high significantly increasing the cost of gas-fired generation.
- 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.
- Increased stability of fuel prices is needed for retail choice programs to function properly.
- Better customer response to wholesale price signals is needed.
- Development of comprehensive energy legislation has gained significant attention in Congress and the Bush Administration, but passage is uncertain.
- FERC is actively involved in developing and addressing the transition to a more competitive wholesale market.
- Most observers acknowledge that retail choice initiatives are generally struggling to be successful.