



House Public Utilities and Energy Committee

The Status of
Electric Restructuring

Submitted by:
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Consumers' Counsel

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Mr. Chairman and members of the Ohio House Public Utilities and Energy Committee, my name is Janine Migden-Ostrander and I am the Ohio Consumers' Counsel. My office represents the interests of 4.5 million residential households with respect to their utility services.

Ohio's effort to utilize competitive electric generation markets, commonly called restructuring or deregulation, was ushered in after years of hard work by the General Assembly in 1999. In general, SB3 provided an administrative framework for a five-year transition from a fully regulated retail generation rate for consumers to an environment where consumers' retail generation rates were to be the result of their own choices in a competitive market. At the time, there was the hope and desire that the benefits from such forward thinking would cross all boundaries of customers – the industrial class, the small business user and the residential class.

It should be obvious to everyone here today, however, that the benefits of retail generation competition envisioned by SB3 have not been realized by Ohio's residential consumers. The benefits envisioned from restructuring were to be rate uniformity throughout Ohio, competitive options on the wholesale and retail level, more customer choices among an array of suppliers and customer savings through competitive market forces. For the residential class these benefits have not materialized. Even aggregation, which had enormous success in Northern Ohio for most of the Market Development Period over the last five years, has collapsed.

There are a myriad of reasons for these failures which include very little competition in the residential retail market. Extreme difficulties in creating a competitive wholesale market and

its attendant costs crippled the development of a competitive market. Unexpectedly high fuel prices exacerbated the problem. Added to this, were utility rate structures that left very little room for competitive suppliers to provide a competitive product. The adage that we have to learn to walk before we run is applicable here. We ran to retail competition before considering how to make the wholesale market work. This is critical because the ability of competitive suppliers to bring in power hinges on a functioning wholesale market.

The appropriate question before us today, however, is to determine where does Ohio go from here? Do we re-regulate and try to put the proverbial “genie back in the bottle”? Do we continue to develop the hybrid regime between regulation and restructuring, which is where we sit today? Or do we modify the existing “hybrid” framework while working on the “fixes” required for true retail competition to work.

I believe there were some very good reasons for moving away from regulation towards a new structure. Those reasons have not changed. By the same token, the hybrid method, embodied in the PUCO’s Rate Stabilization Plans (RSPs) – which the Office of the Ohio Consumers' Counsel has appealed to the Ohio Supreme Court – will continue the uncertainty of floating somewhere between regulation and deregulation. These plans will not get Ohio any closer to achieving full retail competition or providing the regulatory oversight needed to protect Ohioans. Some will argue that going to the competitive market now would cause price volatility but the Rate Stabilization Plans have resulted in significant rate increases on a yearly basis, thereby belying the stated goal of stable rates. Further, in the wake of significant rate increases for customers – and more to come in generation, transmission and distribution – the impact on all classes of Ohioans is less than sanguine. Industrial customers claim that further increases will drive business out of Ohio. Commercial businesses cannot absorb significant increases either.

And residential customers are finding themselves increasingly challenged to make ends meet and pay their bills. If the increases were confined to just electric rates, maybe the average customer could find a way to manage it, but these increases are compounded by huge increases in natural gas, gasoline and other necessities.

While utility service is just one element, albeit a significant one, in economic development, the impact of these rising costs present a serious challenge to our state's economy and the well-being of its citizens.

So what do we do? There are no magic bullets, but there are potential solutions worth trying that can perhaps salvage the situation we find ourselves in. I will briefly identify several needs and subsequently, several potential solutions to those needs.

First, when SB3 passed, we all focused on the retail market. Had we developed the wholesale market first we might have a different picture today. Second, Ohio needs to address its concerns relating to generation adequacy. SB3 eliminated parts of Chapter 4935 of the Ohio Revised Code that contained the requirement for utilities to annually file a forecast report which set forth the utility company's best efforts at documenting the growth in demand in its service territory and its plan for meeting that demand. These reports were subject to a hearing every five years. Without this information, it is difficult for consumers or regulators to know whether there is adequate capacity and whether new generation is necessary. It is a leap of faith to expect customers to pay for new generation without knowing for sure that it is really needed. The repeal of sections of ORC Chapter 4935 discontinued the regulatory process known as "integrated resource planning." What this means is that we no longer take a holistic view of generation adequacy to ensure that we have a good mix of generation resources that represents the lowest cost option for consumers. Ohio now seeks to address its generation needs through

questionable means. In short, customers could be asked to pay for relatively expensive new generation without the old regulatory “safeguards” or the assurance that the generation plant in question is needed, prudently built, and represents the lowest cost option for consumers. Nor are there any protections through a price cap which would result from a competitive bid for that generating plant. I would submit that such practices are not good for residential customers or for economic development.

Some solutions. There are no guaranteed solutions, but there is the opportunity to embark on a sound, carefully conceived plan that can set Ohio in the right direction.

Early on we ran to the retail market without focusing on the wholesale market, which is regulated by the Federal Energy Regulatory Commission (FERC). In Ohio we have the misfortune to be divided into two Regional Transmission Organizations (RTOs) with American Electric Power and Dayton Power & Light having joined PJM and FirstEnergy and Cinergy belonging to the Midwest Independent System Operator (MISO). This dichotomy complicates the development of a fluid, low-cost wholesale market in Ohio. Each RTO has its own issues and problems that are adding to the costs customers must pay. Moreover, political pressures have resulted in FERC moving too slowly in resolving issues that impact Ohioans. Certainly, the PUCO and the Consumers’ Counsel are actively participating in the laborious debate over the proper shape (and costs) of these markets. I’d like to encourage the PUCO to continue, and even expand, its efforts in that regard. The Consumers’ Counsel will be doing so as well.

However, I would urge the Ohio General Assembly to help as well. The Ohio legislature needs to expand its dialogue with Ohio’s Congressional delegation about our needs relating to wholesale market development.

Some areas that need to be addressed include:

1. Strongly urging FERC to conduct a cost/benefit analysis of RTO structures, expenses and policies.
2. Urging FERC to consider performed-based ratemaking.
3. Ohio should encourage the RTOs to add consumer representation on their governing boards.
4. FERC should be required to develop a plan to eliminate costly and chronic transmission congestion.
5. In order to promote the development of additional generating capacity in Ohio on a competitive basis, project developers should be able to obtain long-term transmission rights that will enable them to sell the output from their generating facilities. In as much as the Energy Policy Act appears to encourage movement in this direction it would certainly be helpful for Ohio leaders to communicate the importance of this issue to our Congressional delegation.
6. The State of Ohio needs to oppose PJM's Reliability Pricing Model and other proposals that would penalize customers because of their location and ultimately will not create the incentives touted for the construction of new generation.

To protect its citizens and spur economic development, it is important that we take a holistic approach to generation adequacy by looking at the entire system in the state as opposed to taking a piecemeal, project by project approach. What we are doing now provides no assurance that what is being built is really needed or is least-cost. Armed with the proper information as to what is truly needed, a plan can then be put in place for adequate resources

fairly priced now and into the future. A plan for the generation needs of customers should combine both short and long-term power options. This diversity in the supply portfolio allows the utility company as the Provider of Last Resort (POLR) to hedge against changes in energy costs. Bidding the entire load out for a two or three year term is simply putting too many eggs in one basket and does not guarantee lower prices. Providing a portion of the bid to cover a long term allows competitive including the utility companies to bid to build new generation. This guarantees that the plant will be built at the lowest cost. It places a cap on the price so that consumers are protected from paying for uneconomical decisions or price overruns.

Ohio should embrace competitive bidding of all generation resources to achieve the best market outcome at the lowest price for the consumer. Doing so, can promote a diversity of options, such as clean coal technologies, renewable energy and energy efficiency. It can provide a mechanism for suppliers or independent power producers to build lower cost generating units capped at the bid price. This protects customers from cost overruns.

This kind of fuel diversity in the portfolio of options, hedges against any one fuel cost – like natural gas today – significantly increasing electric costs. This approach provides protection and balance as well as assurances that there is cost accountability and cost-containment. Our goal should be to provide the best market outcome with the lowest price through competitive bidding. We should help economic development by assuring lower cost options and price stability. We should assure adequate resources for Ohio to guarantee reliability, and we should provide utility companies with options to sell their power competitively.

In our personal finances, I would guess that most of us have a diverse portfolio of many different investments. That way, if one turns out badly, we hopefully have another investment that will offset the loss. Generation planning is no different.

Importantly, the process outlined above for resource acquisition will allow Ohio to either re-regulate its retail rates or continue its pursuit of retail competition in the future.

At the same time, generation adequacy is assured and ratepayers are protected through the use of regulation and competitive market forces.

The proposal OCC advances today may or may not be the best solution, but it is a step towards trying to find answers that work and that protect customers. This proposal recognizes that first we must get the wholesale market right and then look down the road to see if there are steps to be taken to advance the retail market. It lets the retail market develop as it may while the wholesale market improves. Further, this plan promotes well-conceived planning for our energy needs, which is so critical, and it does so in a manner that assures supply diversity and least-cost options for each supply.

Finally, the General Assembly can address the problem of funding for the Energy Efficiency Revolving Loan Fund by re-establishing the original funding rate.

As always, my office stands ready to work with the General Assembly, the administration, the PUCO and other stakeholders in addressing Ohio's needs as we move forward. Thank you very much for the opportunity to share these ideas with you.