

The Transition to Competition in the Electric Industry

A Presentation by:

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Excerpt

WITHOUT RETAIL ACCESS, INDUSTRIALS MUST BE CREATIVE

- Self-Generation/Cogeneration
- Inside-/Outside-the-Fence Exempt Wholesale Generators
- Affiliate/Quasi-Retail Wheeling
- Fuel Switching
- Utility-Brokered Power
- Joint Ventures with Gas LDCs
- Non-Sham Wholesale Entities
- Power Purchasing Cooperatives
- Distributed Generation
- Reallocation of Production to Other Plants
- Municipalization
- Privatization
- Franchise Competition
- Franchise Loopholes
- Switching Franchises
- Energy Efficiency

SWITCHING FRANCHISES

- The telecommunications giant, Motorola, Inc., is building a new \$100 million, cellular phone plant in Harvard, Illinois. The plant will employ 3,000 people when it opens in 1996.
- Motorola announced plans to buy low-cost power from Wisconsin Power & Light and transmit the power over a seven-mile, privately-owned transmission line from Wisconsin to the Illinois site. ComEd would be bypassed; its average 1993 industrial rate was 6.27¢ per kWh compared to WP&L's 3.74¢ rate.
- Motorola estimates savings of about 30% on a power contract with an estimated value of \$5 million per year.
- So long as the power lines used in the transaction are privately owned, the sale and transmission of electricity by WP&L to Motorola is legal. ComEd avoided the "long extension cord" by significantly lowering its price to Motorola.

NON-SHAM WHOLESALE ENTITY

- On June 9, 1994, Suffolk County, Long Island announced its intent to end the monopoly enjoyed by LILCO and desire to begin buying low-cost power in the wholesale markets for resale to residential homes and businesses in the county.
- The Suffolk County Electrical Agency began buying about 5 MWs of power from the New York Power Authority in 1985. The county hopes to increase its wholesale purchases to 400 MWs, or about one-third of the county's total requirements.
- The Agency is a "political subdivision of the state." Therefore, under the Energy Policy Act of 1992, it qualifies as a non-sham wholesale entity that can buy power in wholesale markets for resale to end-users.

FRANCHISE LOOPHOLE - I

- 127 school districts on Long Island, New York have formed the Education/Electric Buying Group (EEBG), a member-owned, nonprofit purchasing cooperative. Collective purchasing groups are allowed under New York's General Municipal and Education Law.
- In May 1994, the EEBG petitioned the New York Public Service Commission for permission to purchase power in the wholesale market to replace the power the schools currently purchase from LILCO. LILCO's average commercial class rate in 1993 was over 15.5¢ per kWh. The U.S. average was 11.7¢.
- The group estimates that its 1994-95 school year power purchases from LILCO will exceed \$60 million. They estimate that they can save \$55 million over a three-year trial period if the NYPSC approves the request.

FRANCHISE LOOPHOLE - II

- On August 1, 1994, the Freedom Electric Power Company filed a petition with the New Hampshire Public Utilities Commission (NHPUC) for permission to do business on a limited basis as a public utility in New Hampshire. Freedom would not have a specific franchise area.
- Freedom proposes to purchase power at wholesale under the jurisdiction of the FERC for delivery to Public Service of New Hampshire's (PSNH) system for resale to certain large end-users that are directly served off of PSNH's transmission system.
- Freedom does not plan to utilize any distribution facilities that are under the jurisdiction of the NHPUC to effectuate the resale of electricity on a retail basis to the end-users.

MUNICIPALIZATION - I

- Whirlpool Corporation is the largest employer in the City of Clyde, Ohio, where 3,800 employees manufacture automatic washing machines. Whirlpool's load is approximately 16 MW, or roughly 75% of the city's total load of 21 MW.
- With Whirlpool's support, the city municipalized the electric system and terminated service with Toledo Edison Company (TE), an operating subsidiary of the Centurion Energy Corporation. TE's average 1993 rate was 8.73¢ per kWh.
- Clyde build an 8.8 mile, 138-kV transmission line to interconnect with the Ohio Power Company's system.
- Since municipalization, rates have declined by over 25% compared to TE's rates.

MUNICIPALIZATION - II

- The Ford Motor Company is a major employer in the City of Brook Park, Ohio, and one of Cleveland Electric Illuminating Company's (CEI) five largest customers. Ford's three plants annually purchase approximately \$30 million, or 75% of all the power provided by CEI to Brook Park.
- Brook Park officials estimated that CEI customers in the city could save up to 30% on their electric bills if the city municipalized the electric system. Ford had estimated similar savings based on studies it conducted.
- At the last minute, CEI agreed to offer Ford an immediate rate reduction of over 20% in return for an 8-year contract to remain on the CEI system. Ford accepted the offer and shared the benefits of its rate reduction with other CEI customers in Brook Park.

MUNICIPALIZATION - III

- West Valley City, Utah (WVC), is Utah's second largest city. WVC recently annexed adjacent territory and created the WVC Industrial Park.
- WVC plans to form a municipal electric utility to serve the Industrial Park's first tenant -- Frito-Lay -- and any new tenants. WVC would purchase power from the Utah Associated Municipal Power System (UAMPS) and seek wheeling from Utah Power & Light.
- Utah Power and its parent, PacifiCorp, have refused an interconnection agreement with WVC. The utilities believe that FERC will not order an interconnection agreement under Section 211 of the FPA.

MUNICIPALIZATION - IV

- Anyone owning or controlling transmission or distribution facilities can request a §211 wheeling order from FERC!
 - * Neither the EPAct nor FERC states either the magnitude or the type of facilities necessary to request the order.
- Any city can attempt "municipalization lite:"
 - * Purchase a "few" residential meters -- thus making them owners of distribution facilities.
 - * Issue a RFP for power supplies.
 - * Make a "good faith" §211 request for wheeling services from the selected power supply to the residential meter.
 - * If refused, the requestor can ask FERC to order wheeling.

MUNICIPALIZATION - IV - CONTINUED

- "Municipalization lite" is very real:
 - * The City of Falls Church, Virginia is now trying this approach.
 - * The Mayor, an executive with APPA, is pushing the effort.
 - * Six bids were received on December 15, 1994 from :
 - Allegheny Electric Cooperative
 - American Electric Power
 - Enron Power
 - Louis Dreyfus Electric Power
 - National Power Management Co.
 - Public Service Electric & Gas Co.
 - * A good faith request for transmission service has been made of Virginia Power and Electric.
 - * The 60-day clock is running.

MUNICIPALIZATION - IV - CONTINUED

- There are tremendous advantages to "municipalization lite:"
 - * Low cost.
 - * Optional participation.
 - * Can include all classes of customers.
 - * The state PUC continues to regulate most of the distribution wires.
 - * There is no violation of state franchise laws because the city only sells to the customers who elect to transfer themselves to the new municipal system.

COMPETITIVE SOURCING: The Client/Server Model

- The Sithe/Independence project is near completion in Upstate New York. The project will sell steam to end-users and electric capacity and energy to utilities and end-users.
- The Independence project is a 1040-MW, gas-fired combine-cycle cogeneration facility. The plant has two power blocks, each consisting of two 160-MW, GE frame 7FA combustion turbines with two heat recovery steam generators and a 208-MW steam generator.
- On September 8, 1994, the New York Public Service Commission approved the sale of power from Sithe to Alcan and Liberty. Sithe will be required to reimburse Niagara Mohawk for a portion of the stranded costs claimed by NIMO.

COMPETITIVE SOURCING: The Client/Server Model (Cont'd.)

- Alcan Rolled Products Company, one of Niagara Mohawk's largest customers, switched suppliers and began purchasing its entire 44-MW load from Independence in January 1995. Alcan also takes steam from one of the two power blocks.
- The Independence project will serve another industrial customer -- Liberty Paperboard Recycling Mill -- which will be constructed near the plant. New jobs and an expanded tax base will result.
- Independence has a 20-year, base gas sales agreement with Enron Power Services, Inc., who will manage and supply the project's natural gas requirements. Firm transportation will be provided by seven U.S. and Canadian pipeline companies.

COMPETITIVE SOURCING: The DuPont Model

- In early 1994, E. I. du Pont de Nemours & Co. and LG&E Power Marketing Inc. (LPMI) agreed to form a partnership under which LPMI would operate and maintain power plants at nine DuPont fiber manufacturing facilities in five states. Each partner would own 50% of the power facilities.
- LG&E Energy (LPMI's parent company) committed to invest up to \$300 million in the partnership. LPMI would plan future upgrades or enhancements to the power plants which currently range in size from 15 to 30 MWs. Future off-site sales of power were contemplated.
- The deal subsequently collapsed, but not because the concept wasn't viable. However, we expect other such deals in the future.

CONTROLLING ELECTRICITY COSTS: LONG-TERM GOALS

- Power requirements should be procured on an unbundled, competitive basis, i.e., electricity products and services should be "competitively sourced."
- The vertically integrated industry structure is obsolete and should be restructured. A new industry structure must be fully competitive at both the wholesale and retail levels.
- Large industrials do not seek "special deals" under current regime as an alternative to deregulation. Special rates or deals are transitory. They will not stop deregulation.
- But, many laws and regulations will have to be changed.

THE BENEFITS OF RETAIL COMPETITION

- Competition brought significant benefits to other industries:
 - * Telephone: 66% reduction in long distance rates -- with only a 13% increase in local service prices.
 - * Airlines: 22% decline in fares on average -- although it now costs more to fly into high-cost areas.
 - * Natural Gas: 33% decline in gas prices for all customers.

THE BENEFITS OF RETAIL COMPETITION - CONTINUED

- The planning process will be greatly improved:
 - * Planners will become risk takers.
 - * The question will be asked:
Can I sell the output or product that I produce?
- A benchmark price will be provided for non-shoppers --
 - * It will be politically difficult for non-shoppers to pay significantly higher prices when the differential is not cost-based.

THE EMPIRE STRIKES BACK !

- The U.S. Department of Energy opposes retail competition in the electric utility industry. It filed comments in California which basically argued that States do not have the jurisdiction necessary to promote direct access.
- The "just-say-no" utility crowd will likely seek federal legislation in the 104th Congress to maintain, if not, expand their monopoly power:
 - ① Impose a complete ban on retail wheeling
 - ② Amend or repeal PURPA
 - ③ Amend or repeal PUHCA
- Utilities are attempting to coerce the FERC into marking up the book value of their transmission assets. Other gimmicks to shift generation costs on to the "wires" are also being pursued.

THE RED HERRINGS



Low Income Customers



DSM



Renewable Resources



The Environment



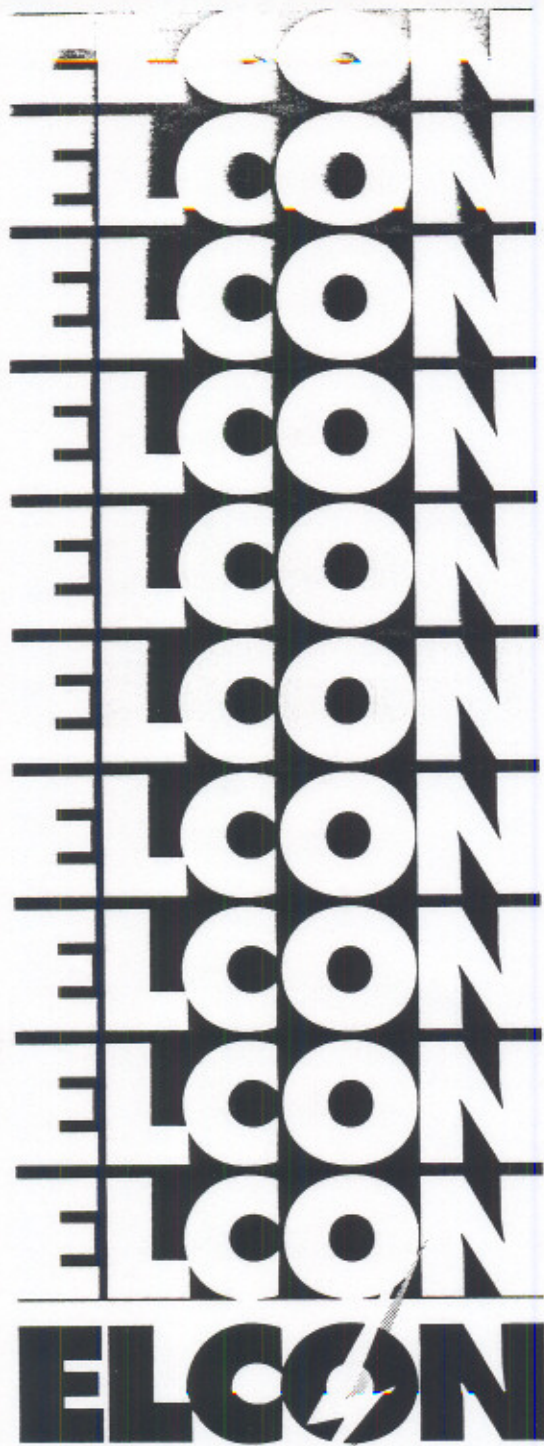
Reliability



Planning

CONCLUSIONS

- The California initiative is hard evidence that the existing utility industry structure is flawed and beyond repair. Market forces have begun an irreversible process to correct this situation.
- Industrials and other supporters of free markets will keep up, if not increase, the pressure. The forces of reaction -- incumbent utilities, incumbent regulators, and incumbent consultants -- will continue to resist change.
- Nonetheless, the potential for large customers, or groups of small customers, to seek alternatives to traditional electric utility service will mean that competitive markets -- not command-and-control -- will ultimately prevail, at no sacrifice to the environment.
- Those who are aggressive will benefit; those who sit idly by, may get hurt.



WHO WE ARE...

ELCON is an association of large industrial consumers of electricity. Our members have facilities in most of the fifty states and in many foreign countries. These companies produce a wide range of products, including aluminum, steel, petroleum, chemicals, industrial gases, glass, motor vehicles, electronics, textiles, paper products and food. Our 23 member companies consume over four percent of all of the electricity in the United States. These companies require an adequate and reliable supply of electricity at competitive prices.

MEMBER COMPANIES

AIR PRODUCTS AND CHEMICALS, INC.
ALCAN ALUMINUM CORPORATION
AMOCO CORPORATION
ANHEUSER-BUSCH COMPANIES, INC.
ARMCO INC.
BETHLEHEM STEEL CORPORATION
BOC GASES
THE CHEVRON COMPANIES
CONE MILLS CORPORATION
DOW CHEMICAL, U.S.A.
EASTMAN CHEMICAL COMPANY
E.I. DU PONT DE NEMOURS & CO.
FMC CORPORATION
FORD MOTOR COMPANY
GENERAL MOTORS CORPORATION
LTV STEEL COMPANY
OWENS-CORNING FIBERGLAS
PRAXAIR, INC.
PROCTER & GAMBLE PAPER PRODUCTS CO.
REPUBLIC ENGINEERED STEELS, INC.
A.E. STALEY MANUFACTURING COMPANY
THE TIMKEN COMPANY
WCI STEEL

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