

# **Electric Deregulation Issues in Texas**

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**RESTRUCTURING THE UTILITY  
INDUSTRY IN TEXAS AS A  
PRECURSOR TO DEREGULATION**

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## **THE GREAT PARADIGM SHIFT IN THE PRODUCTION AND DELIVERY OF ELECTRICITY**

There is a paradigm shift taking place in the electric utility industry. That shift will increase complexity and cost in the delivery of electric services. The complexities inherent to the new marketplace include:

1. Integrated utilities have been unbundled to form at least three new companies to separately address generation, delivery, and retail sales. The sum of the parts exceeds the whole.
2. Consumers must purchase power from retail electric providers (REPs). No matter how many power suppliers locate in Texas, a vibrant competitive market will not develop with only a handful of REPs.
3. An Independent System Operator (ISO) will control the transmission grid, dictate production, impose penalties upon transmission constrained areas, register every single meter in the State and monitor which REP serves which meter. These efforts require a new (and as yet inefficient) bureaucracy and new costs.
4. There will be an expectation that all customers will be served pursuant to written contracts. The marketplace (with few REPs) may require penalties for failure of customers to stay with specified load profiles. Thus, the economics of an offer may depend as much on the terms and conditions of a contract as the quoted price per kWh.
5. REPs may quickly terminate service for non-payment. Customers whose REP drops them for non-payment will automatically be transferred back to the regulated PTB. Customers whose REP abandons the marketplace will automatically fall to the POLR. The rates for POLR are likely to be 30 percent higher than the safe-harbor price to beat rates.

**MARKET PARTICIPANTS WHO  
ARE EXCLUDED FROM  
RESTRUCTURING AND COMPETITION**

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## DEREGULATION OUTSIDE ERCOT

- Panhandle – In 2001, the Texas Legislature passed House Bill 1692 to exempt Southwestern Public Service (SPS) from electric restructuring until at 2007.
- El Paso Area – Senate Bill 7, the 1999 retail deregulation legislation exempted El Paso Electric from electric restructuring until at least 2005.
- Golden Triangle/SE Texas – A non-unanimous stipulation between the PUC Staff, Entergy Gulf States and several other parties to delay competition until September 2002 was filed last October. The Commission approved that agreement. On May 31, 2002, the Beaumont Enterprise reported that Entergy was expected to file an agreement reached with the Staff of the Commission to delay competition until the middle of 2003. The delay continues as of March, 2004.
- North East Texas – Competition was postponed in the Southwestern Electric Power Company (SWEPCO) service territory by order of the PUC.

The speed at which the Entergy and SWEPCOI service territories are deregulated will depend upon the FERC's blessing of a Regional Transmission Organization (RTO), like the ERCOT ISO, to control the transmission grids in the power pools where those utilities are located.

## **MUNICIPALITIES AND CO-OPS**

There are 76 cooperatives and 85 municipally-owned utilities in the state. These entities participate in the deregulated wholesale market. However, Senate Bill 7 provided each cooperative and municipally-owned utility the right of self determination regarding whether to participate in the deregulated retail market. Co-ops and munis are permitted to compete in the ERCOT service territories of the investor owned utilities, but if they do they must open up their own territory to competition. Unless a muni or co-op affirmatively opts into the Senate Bill 7 deregulation scheme, the customers of that muni or co-op will not have competitive choice.

## **REGULATION OF CO-OPS**

In 1997 the Legislature granted each cooperative the right of self determination regarding whether the co-op should be deregulated. The co-ops were permitted to remove themselves from rate regulation by a majority of members voting in an election where a ballot is sent to each electric cooperative member. The Legislature gave the PUC exclusive review over cooperative rates that are challenged within 60 days of a rate change according to specifically defined conditions. The Commission may initiate a rate review on its own motion if the Commission has good cause to believe the co-op is earning more than a reasonable return. See, PURA §§ 36.251-36.309.

# **AGGREGATION**

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## **Overview To Aggregation**

Aggregation involves the joining of two or more electric customers into a single purchasing unit to purchase electricity. By joining together, these customers purchase a greater amount of electricity, and can negotiate for reduced electric rates because of their higher combined demand. An aggregator actively joins these customers together, but except in the case of political subdivision aggregation, does not take title to and may not resell electricity. An aggregator will turn the purchasing unit it creates over to a REP. In Rule §25.111, which was recently adopted by the PUC, there are two different classes of aggregators. A Class I aggregator is a person who joins customers other than municipalities and political subdivisions into a single purchasing unit, while a Class II aggregator is a person or municipality who provides aggregation services to municipalities or other political subdivisions. The rule also provides for the requirements that the aggregators must meet, as well as the registration requirements for aggregators. An aggregator may not be a REP. In regard to municipalities and political subdivisions, there are four separate classes: a person that aggregates municipalities and/or political subdivisions, a political subdivision corporation that aggregates political subdivisions, a public body that aggregates for its citizens who request the service, and an administrator of citizen aggregation. In addition to PUC Rule §25.111, Local Government Code §303 also provides requirements for aggregation by political subdivisions for other political subdivisions and/or the citizens of the political subdivisions. Aggregation is addressed in the Public Utility Regulatory Act §§§39.353, 39.354, and 39.3545.

## STATUTORY CONCEPTS

1. An aggregator is a person joining two or more customers, other than municipalities and political subdivisions, into a single purchasing unit to negotiate the purchase of electricity from retail electric providers (REPs).

Municipalities are not persons and cannot be aggregators.

Aggregators cannot sell or take title to electricity. PURA §39.353

2. A municipal aggregator is a person authorized to by two or more municipal governing bodies to create a single purchasing unit to negotiate with REPs **or** aggregation by **a** municipality under the Local Government Code. PURA §39.354

3. A political subdivision aggregator is a person or political subdivision corporation authorized by two or more political subdivision governing bodies to join the bodies into a single purchasing unit to negotiate with REPs to serve facilities of the bodies **or** aggregation by a person or political subdivision under the Local Government Code. PURA §39.3545

4. Aggregation by Political Subdivision Corporations

Political subdivision may include county municipality, hospital district or other political subdivision receiving electricity from an entity participating in retail competition.

Political subdivisions join together to create a political subdivision corporation to act as agent for the political subdivisions with respect to their own electricity use for their respective public facilities.

The corporation may negotiate, contract, and purchase electricity. It is not constrained to dealing a specific REP or turning its participants over to a REP.

The Corporation may recover its expenses through dues or a per kWh aggregation fee, or a combination of both.

The Corporation may appear on its own behalf before regulatory agencies, the courts or the Legislature.

The Corporation has all powers under the Non-Profit Corporation Act.

Local Government Code §303.001

## **OPTIONS FOR AGGREGATION**

1. Aggregate own load
2. Hire a registered private aggregator
3. Create or join a political subdivision corporation

## **MARKET ATTRACTIVENESS OF CITY AGGREGATED LOAD**

- ❑ Load diversity with substantial off-peak usage
- ❑ Geographic diversity
- ❑ Consistent usage
- ❑ Opportunities for expanded service
- ❑ Favorable market presence

## **LONG TERM BENEFITS OF POLITICAL SUBDIVISION AGGREGATION OF CITY LOAD**

1. Structure non-price factors for Cities' benefit.
2. Couple risk management with flexibility.
3. Opportunities to eliminate middle man services (i.e., scheduling, billing, customer) and reduce costs.
4. Pursuit of common strategic objectives (i.e., metering, data collection, street lighting & load management).
5. Opportunities to serve citizen load in non-competitive areas.

## POLITICAL SUBDIVISION CORPORATIONS OF CITIES

### Cities Aggregation Power Project, Inc.

Abilene	Kaufman
Addison	Kennedale
Allen	Killeen
Arlington	Lamesa
Bellmead	Lewisville
Belton	Lovelady
Benbrook	Mansfield
Benbrook Water & Sewer Authority	McKinney
Brownwood	Merkel
Burkburnett	Midlothian
Burleson	Nacogdoches
Carrollton	North Richland Hills
Cedar Hill	Odessa
Cisco	Palestine
Cleburne	Pantego
Clyde	Paris
Colleyville	Plano
Comanche	Red Oak
Commerce	Richland Hills
Crockett	Robinson
Denison	Rockwall
Dublin	Rotan
Duncanville	Rowlett
Edgecliff Village	Saginaw
Eules	San Angelo
Everman	Sherman
Frisco	Snyder
Forest Hill	Sweetwater
Fort Stockton	Terrell
Gainesville	The Colony
Grand Prairie	Trophy Club
Hamilton	Trophy Club Municipal Utility Dist.
Harker Heights	University Park
Haskell	Vernon
Heath	Waco
Henrietta	Watauga
Highland Park	Waxahachie
Howe	W. Central Municipal Water Dist.
Hurst	White Settlement
Iowa Park	Wichita Falls
Irving	Woodway

**South Texas Aggregation Project, Inc.**

Alton  
Alice  
Aransas Pass  
Beeville  
Bishop  
Carrizo Springs  
Charlotte  
Corpus Christi  
Dilley  
Edna  
Fulton  
George West  
Harlingen  
Ingleside  
Ingleside on the Bay  
Kingsville  
La Feria  
Laredo  
Lavaca-Navidad River Authority  
Lyford

McAllen  
Mercedes  
Odem  
Orange Grove  
Pharr  
Pleasanton  
Point Comfort  
Port Aransas  
Portland  
Port Lavaca  
Refugio  
Rio Hondo  
Rockport  
San Juan  
Sinton  
South Padre Island  
Taft  
Victoria  
Weslaco  
Woodsboro

## **AGGREGATION OF CITY LOAD HAS BEEN A RELATIVE SUCCESS**

- CAPP and STAP became the largest customer base for First Choice Power in 2002. CAPP switched to TXU Energy Services for 2004.
- Projected average savings above price to beat savings in 2001 for 2002 service was 13.7% for CAPP members and 12.6% for STAP members. CAPP and STAP members were guaranteed minimum savings above price to beat of 6.8% and 6.3%, respectively. Realized average savings for 2002 were 25% for CAPP and 29% for STAP. Consultants are now working on calculation of savings for 2003.
- The commodity price in the contract is one fixed price, thus fulfilling Cities' desire for simplicity.
- Terms and conditions of the CAPP/STAP contracts are more beneficial to Cities than any other contracts. No swing. No transmission constraint penalty. No surprises.
- Organizational unity will permit more favorable pricing and allow pursuit of common objectives, such as:
  - changing unfair or discriminatory rates applicable to Cities;
  - establishing a game plan in anticipation of the deregulation of street lights;
  - conservation and load management to meet the mandates of SB 5;
  - directly approaching wholesale suppliers.

# **CRITIQUE OF DEREGULATION**

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## **General Status Report After Six Months of Deregulation**

- \* Leading proponent faces disgrace and financial ruin.
- \* Many announced generation plants have been canceled or put on hold.
- \* Retail competition is but rivalry among a handful of entities.
- \* Rampant confusion exists regarding service issues.
- \* Restructuring necessary to achieve deregulation has led to economic waste, created new entities with baffling reams of new rules to control complex relationships and resulted in gross inefficiencies.
- \* Many issues are on appeal, and the Courts are not the Consumer's friend.
- \* The PUC has based T&D pricing on crystal ball estimates, and the Legislature has turned all other components of electric pricing over to neophyte hedge fund traders.
- \* Prices to consumers exceed what they would have been had the Legislature not tampered with regulation.
- \* Commodity prices must go higher for competition to prosper.

## **ADVICE FOR CITIES**

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## **Advice For Cities Not Yet Participating In The Competitive Market**

1. Know your load. Suppliers serve load. When they bid for certain load, they want to know as much about the load and its demand peaks and variability over time as possible. Price premiums are associated with gaps in information or uncertainty.
2. The market is geared toward demand data from demand meters or proxies from ISO load profiles. Very few city accounts have demand meters or demand profiles. Thus, thoroughness in presentation of electric account data is critical to attraction of market interest.
3. You need account-by-account, meter-by-meter, month-by-month kWh, kW actual, kW billed (which may differ from actual because of demand ratchets in tariffs) and amount billed data for at least the most recent 12 months (36 months would be better). This information must be placed in an electronic format. Precise location (street address and zip code) of each meter is critical for ERCOT to process a switch request.
4. Utilities have a responsibility to provide account data, but they will not volunteer information. Cities must know what to ask for and must continue to update information.
5. Ask for and review several standard form contracts from different REPs. Contract terms can be as important as the commodity price. Be aware that you may need to require: (a) billing information that permits account-by-account reconciliation; (b) waiver of swing penalties and assessment of ERCOT or PUC imposed penalties or add-on charges; and (c) designation of a specific account representative.
6. Contracting clout and pricing both improve as the size of a desirable load increases. There is a benefit in aggregation.

## **RATES IN THE COMPETITIVE ARENA**

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## Electric Accounts in the Deregulated World

### Price to Beat

- 6% reduction to January 1, 1999, rate;
- adjusted for fuel costs;
- some constraint on price volatility for 5 years.

### Non-Price to Beat

- Market determined;
- Whatever can be negotiated.

Non-Price to Beat (for any account that has demand in excess of 1000 kW or any account served by a competitive REP)

- A commodity rate from the REP which includes any payments made to a supplier.
- Non-bypassable charges paid by the REP to the T&D utility that include:
  - delivery charges established by the PUC to recover the costs of the transmission and distribution system
  - stranded costs
  - ERCOT funding
  - system benefit fund
- May include penalties for:
  - Swing – using less than or greater than a contract designated amount
  - System balancing – transmission constraint
- This is a negotiated contract rate.

## **Is Price to Beat Necessarily the Best Choice?**

1. Higher fuel prices will be charged in the summer.
2. Utilities and the PUC attempt to make PTB a market rate to provide an incentive to switch.
3. Utilities can increase fuel factor twice a year.
4. Fuel price increases will negate 6% price reduction.
5. Protection will ultimately expire.
6. Aggregation of total