

Transition to Retail Competition and Enabling Customer Choice in New York

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Topics

- Retail Choice Models
- Drivers of Retail Choice
- Benefits and Drawbacks of Retail Competition
- Metering, Billing & Collection, Customer Service
- Economic Characteristics

Topics (contd)

- Retail Infrastructure
 - Wholesale Granular Pricing
 - Sophisticated Metering
 - Rules and Procedures
 - Unbundling
 - Price to Beat
 - Electronic Data Exchange
 - Uniform Business Practices
 - Consumer Protections
 - Utility Cooperation
 - Sophisticated Customers
 - ESCO Industry
 - Regulatory Support
- Status of Retail Choice
- Provider of Last Resort

Retail Choice Models

- Customer does not rely on incumbent utility any longer even for delivery; relies on competitor sources
- Customer purchases commodity partly or completely from competitor; delivery service still from utility
- Customer has no relationship with utility; competitor provides commodity and metering, billing, customer service; utility provides delivery

Drivers of Retail Choice

- Different entities have different interests in advocating Retail Choice
 - Large Customers
 - Incumbent utilities
 - Competitors
 - Regulators

Drivers of Retail Choice

Large Customers

- With increased global competitive pressures, many large customers want to reduce their energy costs to stay competitive; utilities generally provide one-size fits all type of tariff that is not attractive to some customers
- Historically large customers have subsidized other customers; they are interested in reducing cross subsidies to reduce their costs
- Some large customers want better service quality than what a utility can provide
- Some large customers seek “behind the meter” services that utilities cannot offer
- Some large customers believe monopoly utilities are inefficient and have not been responsive to their needs; they need a choice of providers

Drivers of Retail Choice

Incumbent Utilities

- Where wholesale competition is introduced, in many places utilities do not own generation assets; they only own delivery assets
- Utility purchases commodity from competitive generators and market and the associated costs are simply passed on to end use customers with no profit margin built in
- Utilities face only downside risk - potential regulator disallowance of imprudent costs - and no upside profits. Utilities thus have no incentive to be in the commodity business; they would like not to have the obligation to serve commodity to customers

Drivers of Retail Choice

Competitors

- As retail competition is introduced, new players - wholesale and retail energy service companies and marketers - are an integral part of the market place
- Competitors are offering choices to customers and “value added” products
- Competitors come in different sizes (small organizations to international companies) and serve different market segments (specialized industry segments to mass markets)
- In the process of serving customers, many are making profits; thus they have an incentive to increase their market share and are promoters of retail competition

Drivers of Retail Choice

Regulators

- Some regulators genuinely believe in the effects of vibrant competition - to increase efficiency in the industry, for competitors to offer value added products, and generally to improve service and to reduce costs, compared to what the traditional utility can offer. Some regulators, however, question whether electric industry is suitable for retail competition
- Competition could bring innovation, technological advances and economic development
- Some believe retail competition can squeeze subsidies out of the system faster than regulators can accomplish

Benefits and Drawbacks

- Price
- Quantity
- Value Added Services

Benefits and Drawbacks

Price

Benefits

- Utility tariffs are based on customer classes and do not necessarily differentiate individual customer load characteristics
- There are cross subsidies between customer classes and within a customer class
- Some customers are paying higher prices than the costs they impose on the system
- Retail choice could squeeze out those cross subsidies faster than regulators can
- Potential increase in consumption efficiency with improved price signals
- Customers could be more competitive in their businesses with reduced energy costs

Benefits and Drawbacks

Price

Costs

- With the elimination of cross subsidies, some customers who have been subsidized before could be adversely affected
- Setting up retail competition infrastructure costs money and unless those that benefit from retail choice pay for those costs others could end up paying some of those costs

Benefits and Drawbacks

Quantity

- Another ingredient in the customer bill is the quantity consumed
- Many customers, particularly large ones, can benefit from advice on how to optimize their consumption to reduce costs to themselves and to the system
- Utilities typically do not provide “behind the meter” services; competitors can analyze and provide services to optimize customer usage

Benefits and Drawbacks

Value Added Services

- Competitors can offer billing, customer service choices that utilities typically cannot offer given their tariff restrictions
- Some competitors may offer demand side services that utilities cannot to optimize their usage and reduce costs
- Many believe that the option to choose someone other than the utility by itself is a valuable tool

Metering

- Metering is considered a potentially competitive service in some places, for large customers.
Consists of
 - Meter Service Provision (procurement, installation, maintenance)
 - Meter Data Services Provision (extracting data from the meter, validating, transmission, analyzing data)
- Verdict on whether there could ever be a vibrant competitive service is not known yet

Metering

- MSP services need scale to succeed, given the small margins involved; it is unclear whether competition can take hold
- The role of Automated Meter Reading is evolving. Many utilities are in the process of adding AMR features to reduce meter reading costs, reduce errors, to get bills out faster, to provide other services (outage notification etc) to assist them in maintenance. However, more sophisticated Advanced Metering Infrastructure and Smart Grid initiatives are under consideration presently.
- Should utilities be allowed to install more sophisticated meters to facilitate more time variant tariffs (Time Of Use, Hourly Pricing etc.) – voluntary basis; mass saturation?

Metering

- MDSP service perhaps may show more promise for competitors to play a role
- However, it may still be a niche market limited to some large customers
- Again, AMI and Smart grid initiatives are being considered that will impact MDSP construct

Billing & Collection, Customer Service

- Many competitive entities like credit cards, insurance companies do B&C today and provide customer service
- Should utility B&C and customer service also be made competitive?
- Competitors could get the metering data from utility; bill & collect; remit delivery portion of the bill to utility
- However, are there unique issues associated with electric industry that may make this more difficult?
- New business processes, discussed later, needed to accommodate these changes

Economic Characteristics

- Unlike generation, cost of entry and exit into providing commodity service is not huge
- Lead time to enter and exit is not too long
- Skill set needed to be in the retail business is not very hard to acquire
- A competitor profitability depends on the type of customers he serves and concomitant cost structure and revenue stream. Generally, given the small potential profits, large number of customers is needed, particularly if it serves mass markets, to be profitable

Retail Infrastructure

Wholesale Prices

- More granular wholesale prices would be helpful for customers to adopt demand side response measures and take advantage of pricing signals
- In NY, largest customers (size varies by utility) default tariff is hourly price based on NYISO Day-Ahead market price; about 6,000MW on these tariffs soon; customers can buy risk mitigation products from ESCOs
- Forward/Future electric markets are helpful as well to get future price signals and to hedge for reducing risk of price volatility; these will also facilitate bilateral contracts between buyers and sellers

Retail Infrastructure

Metering

- More sophisticated metering is needed if more granular pricing scheme is to be reflected in tariffs for customers to take advantage of
- Retail pricing should be able to accommodate customer specific load shape as opposed to system/class based load shapes
- Competitors may also provide behind the meter services that are tied with pricing, to optimize consumption and reduce customer bills

Retail Infrastructure

Rules and Procedures

- Unbundling
- Price to Beat
- Electronic Data Exchange
- Uniform Business Practices
- Consumer Protections

Retail Infrastructure

Other requirements

- Sophisticated customers
- Willing Competitors
- Supportive Regulatory Structure

Retail Infrastructure Rules and Procedures Unbundling

- Typically utility prices have been bundled for generation, delivery and customer services
- If some elements are going to be made competitive, then the price/bill has to be unbundled to show the true cost of each service
- Customer pays delivery company only for the service delivery company provides
- Customer could end up paying twice for the same service, if unbundling is not properly done

Retail Infrastructure
Rules and Procedures
Price to Beat

- If utilities stay in the commodity business, then sometimes utility's commodity price could become a target for competitor to beat; utility pricing scheme is a very important variable that affects success of retail competition
- Ensure that utility commodity price includes all commodity related costs; burying some in the delivery costs may not provide a level playing field for competitors

Retail Infrastructure
Rules and Procedures
Price to Beat

- If utilities have a profit motive in providing commodity, then they may not embrace retail competition that threatens their profitability
- Utility pricing schemes can affect competition; ensure that there is no undue advantage for any player
- Typically utilities have captive ratepayers that competitors do not; utilities have capability of passing costs on more easily, subject to regulatory scrutiny
- Competitors have extra costs such as marketing and attracting new customers that utilities do not

Retail Infrastructure
Rules and Procedures
Electronic Data Transfer

- In order for retail transactions to take place between utilities and competitors, some form of electronic data exchange is needed, particularly as the volumes get bigger
- Transactions could include exchanging customer switching; adds/drops; metering data; payment transactions etc.

Retail Infrastructure
Rules and Procedures
Uniform Business Practices

- UBPs deal with common business practices to conduct retail transactions among the utilities and competitive players
- They cover rules associated with providing information in areas such as customer historical usage information; customer switching; meter reading data; billing and collections; service turn on/off etc;

Retail Infrastructure
Rules and Procedures
Consumer Protections

- Typically, utilities have to offer consumer protections and they are codified in the law and/or regulations. Consumer protections deal with deposit requirements; when service needs to be provided, service turn off requirements; billing & collection periods etc.
- What level of consumer protections should competitors offer? Same as utilities or something different? In NY, by law, consumer protections offered to residential customers by competitors is similar to utilities' for residential customers, except for the obligation to serve

Status of Retail Choice

- In USA, about 160,000MW is eligible to participate in retail choice programs; about 1/3 or 59,000MW participating
- Dozens of ESCOs participating
- In New York State, over 70% of the large TOU customer load; about 50% of the other business customer load; and just over 10% of the residential load has migrated to ESCOs

Retail Access in NY

- As of January 2008, the following percentages of customers have migrated from the utilities to Energy Service Companies (ESCOs)
- 50% of large commercial / industrial customers (78% of load)
- 24% of small commercial / industrial customers (50% of load)
- 14% of residential customers (14% of load)

– Number of Migrated Customer Accounts by Utility

» Con Edison	498,387
» National Grid	226,693
» NYSEG	131,322
» RG&E	71,275
» Orange & Rockland	61,950
» CHG&E	7,870

Provider of Last Resort

- Different models
 - Utility continues to be the POLR (current NY approach)
 - No one has POLR responsibility
 - Every competitor has the POLR responsibility
 - Every competitor has limited POLR responsibility in terms of customer class and/or geographic area
 - A chosen entity (through a competitive process) is assigned the POLR responsibility

Provider of Last Resort Issues

- What should be the pricing scheme for POLR service? The remaining Qs assume the incumbent utility is not the POLR
- What should be the duration of POLR responsibility (1 year, 3 years..)?
- Should POLR be different for different service classes?
- Should the POLR footprint be the same as the incumbent utility?
- What value does a nonincumbent utility bring to the table?
- What should be the transition mechanism be for moving customers from incumbent to new POLR?
- What are the ramifications of eliminating incumbent as POLR?

Utility POLR Pricing

- Commission August 2004 Policy statement and subsequent Orders provides guidance
 - Large customers--> reflect more market based pricing
 - Recent action - very large customers default tariff will be the Day-Ahead NYISO market price for energy
 - Smaller customers--> offer more stable pricing, until competitive market provides alternatives
 - Utilities provided flexibility in structuring supply portfolios - the portfolios vary by utility - portfolios typically include spot market purchases, short-term contracts and remaining long-term legacy contracts entered into at the time of sale of power plants
 - Reducing price volatility is one criterion in structuring portfolio
 - Where should the value of future supply hedges go - in the delivery rates for all utility customers or only assigned to full-service commodity customers? We decided that legacy hedge values would go in delivery, and new hedge values would go in full-service commodity