Thursday, August 10, 2000

JOINT HEARING
SENATE ENERGY, UTILITIES AND COMMUNICATIONS
and ASSEMBLY UTILITIES AND COMMERCE
BOWEN AND WRIGHT, Chairs
10:00 a.m. -- California Room (4203)

On "California's Electricity Market:
Making Competition Work For Consumers":

Comments of Paul Fenn
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These comments endorsed by the following local officials:
Tom Ammiano, President, San Francisco Board of Supervisors (Brad Benson 415 554 5145)
Ignacio de la Fuente, President, Oakland City Council (Lewis Cohen 510 238 7052)
Hal Brown, Marin County Board of Supervisors (Sandi Blauvelt 415 499 7331)
Albert Vera, Executive Director, Southern California Cities Joint Powers Consortium (310 391 1155)
Frank Egger, Mayor of Fairfax (415 456 6356)

California Community Choice legislation has been requested in resolutions passed by the city and county of San Francisco, Oakland, Berkeley, Marin County and Fairfax, as well as West Hollywood, Lomita, Carson, El Segundo, Hawthorne, Culver City, Lawndale, and the Southern California Cities Joint Powers Consortium.

Community Choice is supported by The Utility Reform Network (TURN, Nettie Hoge 415 929 8876), Public Citizen (Wenonah Hauter 202 546 4996) Ratepayers for Affordable Green Electricity (RAGE - same) and the Western Power Trading Forum (Gary Ackerman 650 324 3250).

California

August 10, 2000
To the California Legislature:

When California's deregulation passed in the Fall of 1996, the law was heralded as a national model, leading many of the 25 states that have subsequently passed deregulation laws to imitate its basic structure. This law promised consumers electricity choice and the end of the last great monopoly at the price of $30 billion.

These promises have not been delivered. Today, only 5% of Californians are participating in the deregulated market, and the whole idea that individual consumers can constitute a competitive market has proven to be false. Indeed, even large industrial customers are unable to find suppliers. Modeled on the telecommunications deregulation, AB1890 made the mistake of ignoring the massive capital costs that finance power plants. As a result, only the aggregation of large industrial, commercial, and government customers have been able to find suppliers.

If you look at the rules for aggregation, however, you find that they are written to prevent consumers from aggregating. A closer look reveals that AB1890 was in fact not designed to create competition, nor to offer consumers access to the market. Senator Peace has himself make public statements to this effect. Today many of the supporters of AB1890 are now calling for "re-regulation" of the retail market, implying an "undoing" of deregulation. A simple question must be asked. If the idea of competition in the electric industry is to be revoked, and if official or unofficial monopolies are to be reestablished, then we must ask the deregulated and bailed out wires companies: are you paying us back the $30 billion then?

It's a funny question because obviously the answer is "no." Our former utilities don't have the money we gave them. It has gone into their new global investment portfolios. For Edison International it is invested in new power plants in China and throughout Asia, South America, Australia. For PG&E it is in Massachusetts.

If we come to terms with the fact that the money will not be returned, then you have no choice but to actually attempt, this time around, to create a competitive industry.

Elected officials, it will not do to pretend you are protecting consumers with new "emergency" measures that actually restore monopolies free of charge and unannounced. Will we have more hearings in another four years to discuss today's follies? Will Sacramento legislators pass another bill they have not bothered to read? Will the same people who wrote AB1890 be allowed to control the process of rewriting it?

The move to restore monopolies is already evident in both legislative and regulatory proposals. The California Public Utilities Commission's recent decision to allow SDG&E to participate in Forward Block Markets in response to the doubling and tripling of electric bills in San Diego is the most disturbing because it both violates the law and yet represents the policy of the Public Utilities

Commission. Presented as a "pro-consumer" means of stabilizing the PX price, this decision amounts to reauthorizing the bailed out, "market-neutral" wires companies to reassert their retail monopolies by acting as electric supply aggregators of their former power supply customers.

Under AB1890, these companies are designated as "default suppliers" of Californians who do not find their own power suppliers. As I mentioned before, 95% of Californians have not found a supplier. By allowing these deregulated former power supply companies to hedge the state pool or California Power Exchange (PX) and offer hedged "service packages" to their former power supply customers, they are in effect being unofficially reinstated as default aggregators, which in effect amounts to re-monopolization.

Considering the $30 billion in disposable income paid by Californians since 1996 for the privilege of getting rid of monopolies, this legislature should not repeat the mistake of allowing these very former power supply monopolies to solve the problem they themselves engineered in 1996.

There are other ways for other (non-UDC) entities to manage this risk. Giving it to wires companies who are alleged to be neutral to power supply markets is another example of letting the fox guard the chicken coop.

The public of this state has paid dearly for a competitive electricity market, and it is the duty of this Legislature to make a genuine attempt to deliver it as well it can. I will repeat that this has not yet been attempted. It will not do to announce the failure of electric industry competition when it is not been tried in earnest. Until then, any measure that expands the authority of the wires companies should be regarded skeptically.

Indeed, delivering competition means reducing the role of the wires companies in power supply. Rather than authorizing wires companies to aggregate, we need to provide the remaining 95% of Californians with an opportunity to find suppliers and get off of the Power Exchange. Under AB1890 these non-participants are automatically sold power from the Power Exchange via the wires companies' AB1890-annointed status as their "default providers." The fact we face today is not merely that electricity rates have tripled in San Diego, but that San Diegans are being held captive to a market and that this market is vulnerable to speculation. The only reason that last week's decision by the Independent System Operator (ISO) to cap Power Exchange rates was needed is that the failed market created by AB1890 puts nearly all Californians in this one, noncompetitive and dysfunctional "default service" marketplace.

The Power Exchange is not – as some revisionists have recently argued - the competitive market that Californians were promised for their $30 billion in 1996. It was created as a backup system for unprofitable consumers (hence the term "default service."), much as many states have created property insurance redlining pools for poor people in "high risk neighborhoods" who often cannot find an insurer who will offer them coverage The fact that this redlining pool includes 95% of Californians does not make it a market.

Giving the wires companies authority to hedge and offer consumers hedged retail products begins to redefine this redlining pool as if it were the competitive market itself, and redefines the would-be

wires companies as virtual monopoly aggregators in a statewide consumer ghetto.

Rather than declaring "competition" a failure, we should declare AB1890 and the revisionist concept of the Power Exchange as a surrogate market to be a failure and get real about organizing demand to meet supply outside the Power Exchange

Those of you who are genuinely concerned about protecting consumers should take a lesson from the way AB1890 was written and passed, and avoid hasty, politically convenient solutions to San Diego's rate shock. AB1890 is based on mistaken economic theory, the theory that individual consumers would create a competitive market. What we have learned, above all, is that you need large blocks of consumers if they are to be adequately profitable to serve. This has come to be called "demand responsiveness."

Creating "demand responsiveness" is the key to delivering what was promised for the $30 billion. The only way to create demand responsiveness is to empower consumers to organize their demand in blocks of sufficiently large volume to be profitable to competing suppliers. This is called Community Choice.

Community Choice authorizes local governments to aggregate all market non-participants in their jurisdictions into city-negotiated contracts, much like cable television or garbage services have been negotiated for decades, but with an opt-out clause for consumers (such as McDonalds franchises and California Manufacturers' Association members) who are big enough to participate directly in the market. It also allows contiguous municipalities to join together into a commonly approved contract.

Key to Community Choice's effectiveness is its opt-out structure. If as a resident, commercial or industrial consumer you do not choose your own provider, Community Choice municipalities will include you in the community's publicly defined and competitively bid-out power supply contract. Like garbage service and cable, the municipality does not act as a wholesaler or reseller and does not assume financial and other risks of titleholder, but merely defines and negotiates contracts on behalf of their communities.

Community Choice was passed in Massachusetts in 1997 and went into effect last year. The first group of municipalities to choose a power supplier, called the Cape Light Compact, has the worst load profile in the state, but it was able to beat the "Standard Offer," their version of our Power Exchange. Recognizing California's problems as early as 1997, Ohio passed a Community Choice law in 1999 to go into effect in 2001. Since then, fifteen California cities have passed resolutions asking this legislature for a Community Choice amendment. San Francisco, Oakland, Berkeley, Marin County and Fairfax, as well as West Hollywood, Lomita, Carson, El Segundo, Hawthorne, Culver City, Lawndale, as well as the Southern California Cities Joint Powers Consortium together represent two million California residents whose local officials have asked to do this before the San Diego crisis began. Community Choice legislation was prepared in January and approved by the California Legislative Counsel, and would have been filed in January 2001 had the San Diego crisis not occurred. Community Choice is also supported by The Utility Reform Network (TURN), Public Citizen, and the Western Power Trading Forum, as well as RAGE, a national coalition of consumer and environmental groups headed by Ralph Nader and David Brower. Federal Community Choice

legislation has been introduced by Congressman Dennis Kucinich (D-Ohio).

Community Choice offers significant consumer security against fluctuations in wholesale power prices by transferring the risk to the private sector rather than to the consumer. In the Cape Light's power supply contract the winning bidder was required to provide performance bonds that are left in escrow in case the power supply is in default of contract. Under the agreement, if the supplier pulls out of a contract and the Compact must find a new supplier at a new price, the bonded supplier must pay the difference. In this way, Community Choice offers a method of assigning risk to the private sector where it belongs.

Community Choice of public Energy Efficiency and Renewables funds is also critically needed to mainstream existing summer spike-leveling technologies that will continue to remain marginal to the power supply market as long as the state's wires companies continue to control the hotly contested energy efficiency and renewables surcharge funds that are currently collected from every Californian.

The city of San Jose has led the effort in recent years to be given even limited access to energy efficiency funds, and has already done groundbreaking work, but statewide the funds continue to be controlled by wires companies which have a conflict of interest that prevents them from investing in energy efficiency on an unprecedented scale. It is time that this legislature stop ignoring the conflict of interest at hand in this issue. Wires companies they are guaranteed a return on investment, so that the higher the capacity requirements of their wires, the more they capitalize, and the more money they collect from consumers.

The Massachusetts Community Choice law includes Community Choice for energy efficiency and renewables public benefits funds, meaning that each municipality is entitled to administer the funds collected from its residents and businesses once it has submitted an energy efficiency plan and won approval from the Massachusetts Department of Telecommunications and Energy, the equivalent of our Public Utilities Commission. Cape Light Compact leaders point out that they have a huge direct interest in shaving off peak loads in the community in order to improve its load profile and secure a better price for power supply. Community Choice eliminates the conflict of interest at hand and puts these funds in the hands of agencies who have a direct interest in making them work.

Conservation can be most dramatically stimulated by Community Choice, with carries obvious implications for rate shock management. To date, the companies attempting to take over meter reading based on the penny subsidy have asked for "blocked metering," meaning reading a whole neighborhood's meters rather than driving to the dispersed homes of the odd consumer who personally chose an alternative meter reading company.
Community Choice can deliver contracts for thousands of meter reading blocks. By organizing this and other "smart technology" services such as wireless metering, solid state solar, etc., Community Choice will deliver demand to the suppliers, based on local governments doing something they have done since the beginning of the municipal franchise: defining short term (3-5 year) contracts for essential services, announcing competitive bidding, debating the desirability of different proposals, choosing a winner, and monitoring contract compliance.

No one on this commission can deny the potential of Community Choice to deliver competition to

San Diego and the municipalities surrounding it, the Bay Area, or the cities of the Southern California Cities Joint Powers Consortium. Just as it will deliver the needed margins to energy services and distributed generation, Community Choice will deliver unprecedented high volume bilateral contracts to power suppliers in unprecedented volume. As city governments discuss this option and begin to define their communities' energy needs and energy values – environmental, labor, social justice-wise – contracts will be written and companies like Enron, Calpine, Dynergy and Green Mountain will bid to win them. "Demand responsiveness" will be created. Cities will be able to cooperate with bidders to analyze their load profile, and can holistically apply distributed generation and conservation measures, as well as enhance meter reading and unprecedented community-wide spike-leveling measures over the next few years.

I will repeat that the legislature has made Californians pay dearly for the privilege of putting an end to the electricity monopoly. We paid not just for lower rates, but for the progress that is inherent in eliminating the last major monopoly, with the corrupting tendencies that all monopolies introduce. To the extent that Community Choice offers the potential for introducing competition and giving Californians more control over this industry, the most polluting of all industries and constituting the largest industrial sector, it should be tried.

Rather than following hysterical proposals thrown into the ring in a moment of panic, this legislature should enter a second phase, called for by many since 1996, to make a genuine attempt to bring competition to this industry.

Rather than declare "competition" a failure, the Commission and the legislature should declare the "California model" a failure and give Community Choice a chance.

Signature: _____ Date: _____