

ELECTRIC UTILITY RESTRUCTURING AND THE LOW-INCOME CONSUMER

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Different Types of Competition: What is Being Proposed?

When policymakers speak of bringing "competition" to the electric industry, their reference may be to wildly different notions of how the electric industry should operate. These different concepts of a "competitive electric utility" have significant implications for consumer protections, particularly for small users.

Two Types of "Competition"

Two different types of "competition" are being discussed for the electric utility industry, including:

- o Retail competition; and
- o Wholesale competition.

The differences between these different approaches are discussed below and the implications for consumers will be noted.

Retail Competition

Most proposals for restructuring the electric industry today involve proposals to allow for retail competition. While these proposals come under many names --direct choice, direct access, retail wheeling-- they all mean basically the same thing: that consumers would no longer be obliged to purchase their power from the local electric utility company. Instead, just as in the telecommunications industry, consumers could shop from amongst all of the various companies offering electricity for sale and decide to buy from whomever they choose.

Under retail competition, however, there still would be a role for the local electric company. Even under retail competition, the job of actually

delivering electricity to each consumer would remain with the local utility. This utility, called the "distribution company," would simply deliver electricity that was produced by any of the various competitors in the electric market. Under this form of competition, the exclusive service territory previously enjoyed by the local electric company would no longer exist.

Under a retail competition framework, the local utility might decide to keep its own power plants and compete for the sales of its existing customers. In contrast, it might decide to sell all of its generating plants to someone else and get out of the business of producing power altogether, preferring simply to stay in the business of delivering power.

Wholesale Competition

In contrast to retail competition is competition at the wholesale level. Wholesale competition would maintain the exclusive service territories of local electric utilities, but would force those utilities to compete for power on the open market. Rather than owning their own generating plants, the local electric companies would spin-off --the technical term is "divest"-- their power plants into separate companies. The utility would then be free to purchase power from any company that was offering wholesale power on the market.

In the wholesale competition framework, competitors would not sell electricity directly to retail customers (such as individual businesses or individual homes) but would instead sell electricity to local utilities. The cost savings that the local utility would find through such competition at the wholesale level would then be passed on to consumers in reduced rates.

The Reason for Wholesale Competition

The thinking behind proposals to move electric utilities to wholesale competition involves two related ideas.

First, the part of the business in the existing electric industry that has been most subject to high costs in the past has been the generation part. These high costs have come from utilities who have engaged in the construction of expensive nuclear plants as well as those utilities who have significantly overbuilt capacity. As a result, the part of the industry where consumers are most likely to find cost-savings resulting from competition involves the part of the industry involving generation.

Second, the place where advanced combined cycle combustion technology has created opportunities for new companies to enter the electric industry has been the generation part. These new types of power plants have not allowed companies to deliver energy more efficiently or less expensively. Nor have they allowed electric utilities to significantly reduce costs related to billing, collecting or other forms of customer service.

Given that the historic problems with high electric prices have involved generation, and that new technological advances have allowed new companies to reduce the cost of power generation, proponents of wholesale competition urge that it would make sense to allow for competition at the wholesale level while leaving the rest of the utility industry structure intact.

The Push for Retail Competition

Some people reason that wholesale power competition cannot work over the long-term. The push for retail competition, they say, is not strictly an economic, but rather a political, phenomenon. Large user customers that have the political and market power to obtain a better deal through reduced prices will push for those reduced prices. If prices below the local electric

utility's rates are available at the competitive wholesale level, therefore, it could be expected that renewed pressure will arise to permit large user direct access to that power. And, given the political and economic power of the customers who would seek such direct access, it could be expected that the industry will move in that direction.

Summary

In sum, two different types of competition are being discussed for the electric utility industry. The first type involves retail competition, where each individual consumer --including everyone from the biggest businesses to individual persons-- shops for electricity in the same way they shop for telephone service, or for automobiles, or for insurance.

In contrast, under the competitive wholesale industry structure, the local utility would shop for electricity. Rather than producing its own power as is done today, the local electric company would decide which power company offers the best deal and then buy power from that company. The savings generated from being able to purchase in a competitive market would then be passed along to consumers.

Roger Colton is an attorney and economist in Belmont, Massachusetts. Colton has been hired to analyze electric restructuring issues by clients ranging from the U.S. Department of Energy (DOE), to the National Association of Regulatory Utility Commissioners (NARUC), to the Edison Electric Institute, the national electric utility industry association. Colton has also worked for numerous state agencies and local community-based organizations on restructuring issues.

Roger D. Colton
Fisher, Sheehan & Colton
Public Finance and General Economics
34 Warwick Road, Belmont, MA 02178
617-484-0597 *** 617-484-0594 (FAX)
rcolton101@aol.com (E-MAIL)
