

## **INVESTIGATION INTO ELECTRIC POWER COMPETITION**

**Docket No: I-940032**

*"Permitting competition to benefit only a small group of customers leaves everyone else worse off. Consequently, it is imperative that a fair and orderly transition that gives all customers choice be started as soon as possible. Only when all customers have the power of choice can competition benefit all ratepayers."*

*Commissioner, John Hanger, September 26, 1995.*

At issue is not competitiveness in the electric industry but deregulation and market access. So far the arrangement of a government monitored oligopoly has contained costs, induced alternative electrical sources and ensured reliable service. There is no need to tamper with a system which has benefited consumers and allowed companies to profit. Deregulation of the gas industry was beneficial to industrial customers, but was of no practical value to small businesses and residential consumers. The Office of Consumer Advocate (OCA) correctly recognized inequities implicit in the deregulation of electricity:

As the electric industry becomes subject to greater competitive pressure and as the bargaining power of some large customers grows even stronger, the OCA submits that the Commission must be vigilant in ensuring that the costs of these developments not simply be foisted upon those customers who lack any semblance of market power. [Office of Consumer Advocate, Public Utility Commission (PUC) v. Pennsylvania Power & Light (PP&L), October 25, 1995.]

The electric industry has never been competitive and further corporate consolidation and realignment makes "competition" nothing more than a cruel joke for residential customers. Left to its own devices, the industry will seek the least cost fuel option with no incentive to contain rates or minimize environmental pollution. This would run counter to the Ridge Administration's priority of inducing business to the state. (1)

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1 Rate structure and maintaining and creating a favorable business climate was the crux of the PPL Industrial Customer Alliance recent intervention in PP&L's \$261.6 million rate request.

Retail wheeling is the vogue fixture of Federal Regulatory Commission (FERC) deregulation:

The growing influence of market-based pricing is evidenced by the increasing number of proposals that have come before the [Federal Energy Regulatory] Commission for the sale of power where market-based pricing considerations are reflected and by the Commission's efforts to examine significant issues...[of] market-based rates and...services." [Cf. Richard D. Cudhay, "Retail Wheeling: Is this Revolution Necessary?," 15 Energy L.J. 351 (1994.)

Ironically, FERC's retail push comes at a time when many electric utilities have finally stabilized. "Now, with the major interest rate shock abated and with the threat of deregulation and competition even less immediate, electric utility stocks have slowly begun to come back, helping their mutual funds rebound, too." ("Newsday," Money and Investing, February 5, 1995, page 7.) Retail wheeling could undermine utility bond ratings, increase stranded investments and facilitate rate shock transference; whereby, hostage residential customers would be forced to pay for uneconomical investments in other regions. (2) However, we can not ignore the rapidly changing nature of electrical generation and distribution, corporate forays into non-regulated investments, governmental mandates and hostile and "friendly" mergers.

Electrical demand has been reduced by two consecutive recessions in the 1980s, energy efficiency, conservation and demand side management (DSM.) Technologies have vastly changed since the 1970s when economics of scale encouraged centralized generating station. Smaller more efficient facilities have supplanted the economic boondoggles of the 1970s. Deregulation, under the guise of competition, will inevitably roll back gains in efficiency and environmental programs. Pennsylvania utilities have substantially reduced labor costs through attrition, "downsizing" and volunteer retirement programs. Obviously, the next programs to be sliced as a result of cost-cutting initiatives will be renewables and energy efficiency.

This would only further skew an unbalanced playing field. The most economical plants are the oldest and dirtiest and deregulation would militate against DSM and energy efficiency since power suppliers would be enticed to sell bulk electricity on the retail market.

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Pennsylvania consumers are currently burdened with servicing debt for large, centralized nuclear generating stations: Limerick 2 - \$3.8 billion and the Susquehanna Steam Electric Station: \$4.1 billion.

Environmental logic is a fact of life and not a marginal compliance factor. The Federal Clean Air Amendments of 1990 forced Pennsylvania utilities to deal with toxic air emissions through a market-driven approach that utilizes transfer emission credits. PP&L reported to shareholders: "Collectively, these costs represent a potential capital exposure of up to \$1.0 billion beyond 1997, as well as additional operating costs in amounts which are not now determinable but could be material." (Annual Report 1994, page, 16.) The fact of the matter is that, "The Act is aimed at reducing sulfur dioxide emissions in the most efficient manner, and like the 1970 Act, allows generating plants to meet emission standards in the cheapest way possible." (44 F. 3d 591, \*597; 1995 US App., Lexis 460, \*\*19; 39 ERC (BNA) 2025.) The general public, irrespective of race, gender or political party, has consistently supported rate relief for cleaner burning fuels. According to a Times/Mirror Polls conducted in April and September 1994: 82% of Americans want stricter laws to protect the environment; 67% would pay higher prices for environmental protections; and, 66% believe that environmental protections and economic growth go hand-in-hand.

Deregulation is based on short term economic gains ignoring long term fiscal and environmental benefits. Retail wheeling would strangle energy efficiency and renewables just at the time when they have become economically feasible. "Fossil fuels remain apparently less expensive than renewable sources - despite remarkable cost reductions in wind and solar technologies over the past ten years - because the energy market doesn't account for the costs of pollution or resource depletion, or for the benefits of developing local resources. " Donald Aitken, Union of Concerned Scientists, Nucleus, Volume 17, Number 2, Summer 1995.)

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Electricity rates do not take into account all the costs of the harmful effects of electricity production. In meeting environmental requirement, utilities incur costs - for pollution control equipment, for example - that are considered internalized environmental costs because they are included

in electricity rates. However, other costs - those for residual pollution emission, which are not controlled - are not reflected in electricity rates. (Government Accounting Office, "Electricity Supply: Consideration of Environmental Costs in Selecting Fuel Sources," May 19, 1995.)

The Pennsylvania electric industry's solvency is ensured through massive governmental subsidies and relies on an energy mix which is not now, or for the foreseeable future, competitive in a free and open market. According to the Congressional Research Service, nuclear power received 60% of all federal research and development monies from 1948-1994 or \$97 billion since 1950. (Komanoff Energy Associates, 1992.) Luther J. Carter found:

These industry actors, for the most part, find themselves nicely insulated from the cost of waste management. The Price-Anderson Act, for example limits industry liability, and nuclear waste policy act allows utilities to pass waste management costs through to ratepayers. Thus nuclear waste management costs, like nuclear wastes, are a residue of the 1950s nuclear promotion policy. Moreover, a portion of nuclear wastes and their management costs are the result of improperly underpricing nuclear electricity and creating an over-investment in nuclear plants and equipment. (Luther J. Carter, "Jurimetrics Journal," Fall, 1988. 29 JURIM J 97.)

This translates into expensive nuclear generated electricity, of which Pennsylvania is dependent.

On average, electricity from non-federal utilities with nuclear reactors costs residential rate payers 9.38 cents per kilowatt hour - more than 20% higher than electricity from similar utilities without nuclear generating capacity (7.25 cents per kilowatt hour)...Between 1968 to 1990, nuclear generating electricity cost an average of 8.8 cents per kWh, or nearly twice the cost of electricity from coal, oil or gas during the same period ...Assuming an average household's electricity consumption rate of 788 kWh per month [based on assumptions from the Department of Energy's Energy Information Administration], the cost to rate payers is \$57.13 per month for the non-nuclear versus \$73.91 per month for the nuclear dependent consumer." (Safe Energy Communication Council, September 19, 1995.)

Pennsylvania utilities have disproportionately higher rates based on their percentage of nuclear assets (%/kWh):

- **Philadelphia Electric Company (PECO) 58%/13.2 cents per kWh.**
- **Dusquesne Light Company 30%/12.8 cents per kWh.**
- **General Public Utilities (GPU) 23%/9.7 cents/kWh.**
- **Pennsylvania Power & Light (PP&L) 31%/8.3 kWh.** (3)

In contrast, Potomac Electric Power Company with 0% nuclear assets has rates of 7.0 cents per kWh. Clearly, nuclear power production in our region is uncompetitive and any further consolidation of nuclear assets would adversely impact all classes of electric customers. (4)

Hazel R. O'Leary stated during her confirmation hearing before the Senate Energy and Natural Resources Committee in 1993. "As a utility executive, I can state from experience that it is a difficult time for nuclear power. The costs of nuclear power, if you include new construction, are not competitive." This trend is not likely to change. A ten year study published in 1992 by the Utility Data Institute found: "On the average, nuclear non-fuel O&M costs per installed kilowatt increased 165% over the last decade, while comparable costs for fossil plants rose only 38%" ("Power Engineering," July 1992, Page 15.) GPU admitted: "Costs associated with then replacement electricity according to the Company.

operation and maintenance (O&M) costs at nuclear plants have continued to increase and become less predictable, in large part due to changing regulatory requirements and safety standards and experience gained in the construction and operation of nuclear facilities."

(General Public Utilities, Annual Report 1992, page 31.)

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3 "Public Utilities Fortnightly," October , 1993 and the "The Electricity Journal," MSB Energy Associates and the Conservation Law Foundation.

4 The cost of purchasing replacement electricity during extended plant shut downs is premium. For example, Three Mile Island 1, shut down by order of the Nuclear Regulatory Commission (NRC) from 1979 to 1985, spent approximately \$1 billion on market priced power. Peach Bottom 2 and 3, shut down by the NRC from 1985 to 1987, spent \$168 million o

Coal remains king in Pennsylvania and throughout the rest of America. Regional economies in coal producing states have a vested interest in maintaining generating stations and utilizing local sources of fuel. However, the Commerce Clause precludes the consideration of local economics as a hardship or recognized externality. (Wyoming, 112 S. Ct. at 800.)

Pennsylvania's electrical production is generated by coal and nuclear fuel: Coal accounts +59.51% of the state net generation, while +34.81% is supplied by nuclear sources. The remainder of the energy mix is as follows: oil = +3.24%; gas = +2.74%; and , = -0.3%. ("Electric Utility Operational Report," PUC, August 1995.) Coal accounts for 56% of all electricity generated in 1992. Electric utilities, the primary consumers of domestic coal, burned 78% of the 998 millions of coal produced in the United States in 1992. Coal is produced in over half the states and is sold in a highly competitive national market.. Yet the competition of coal is skewed in favor of regional producers and low-sulfur states. With the transfer of emission "allowances" and possible weakening of the Clean Air Act, increased coal production may come at the price of accelerated environmental degradation.

The essential problem facing Pennsylvania electrical generators is diversification. If we are to countenance corporate consolidations and realignments, we should be encouraging a diverse mix of sources. For example, Baltimore Gas and Electric (BG&E) and the Potomac Electric Power Company's (Pepco) proposed merger combines utilities with eclectic energy assets. Pepco has no nuclear plants and gets most of its power from coal, gas and hydroelectric sources. Baltimore Gas on the other hand, gets 40% of its power from nuclear plants and has had problems with its Calvert Cliffs plant..." ("The New York Times," September 26, 1995.)

Regardless of a company's energy mix, well intentioned mandates have encouraged utilities to purchase electric at higher than market rates. Under the Public Utilities Regulatory Policy Act (PURPA) of 1978, utilities were required to purchase electricity from small power producers referred as "qualifying facilities." But,

PURPA's effort to introduce competition, and thereby lower power generation costs, has had the ironic effect of forcing Pennsylvania electric utilities to pay more for QF-generated electricity than if they had purchased power at today's market prices from another source...The forces unleashed by PURPA and EPAct [Energy Policy Act 1992] in the wholesale power market have encouraged many large industrial customers to demand open access competition at a retail level. (PUC, Capitol Communications, Volume 1 No.2, August 1995.)

GPU Chairman, President and Chief Executive Officer James Leva echoed this view:

Another outdated law is the Public Utility Regulatory Policies Act that was adopted in 1978 to foster co-generation and savings. Because of that legislation utilities must purchase power from qualifying facilities, sometimes at higher-than-market- prices, and charge its customers accordingly. We can't afford to do that in a competitive electric utility world...As this letter is being mailed to you, we're negotiating to buy out contracts for uneconomical, unbuilt non utility facilities. If successful, it will save nearly \$1 billion in excess costs to ratepayers. ("Letter to Shareholders," August 16, 1995.)

While there were some counter-productive results to PURPA/EPAct, we should continue to encourage the industry to acquire new power sources through wholesale competition and amend existing flaws accompanying this initiative.

Retail wheeling has also been roundly criticized by the industry. PECO stated:

The Company responded [to the PUC] that access by retail customers to alternate electricity suppliers (retail access) is not in the public interest and should not be implemented unless there is reasonable expectation that the total benefits created will exceed the total cost of the changes...The Company believes that retail access should not be adopted if it represents a mere shifting of costs from one class of customers to another. The Company believes that retail access does not currently provide a net benefit. Regulatory changes permitting retail access may also create "stranded investment," investment by a regulated utility in assets currently included in rates that are not recoverable if its customers are served by another energy supplier. (PECO Energy Company, 1994 Annual Report, "Competition," page 15.)

In the interim, it would be instructive to: 1) Monitor the behavior of Pennsylvania electric utilities in non-regulated economic activity. PP&L has already cautioned shareholders about the uncertainty involved in non-regulated corporate adventures:

### **Unregulated Business Activity May Involve More Risk.**

Following consummation of the Restructuring, the Company will be able to pursue business opportunities through unregulated operating subsidiaries without obtaining the prior approval of the PUC. The Restructuring therefore will enable the Company to pursue certain business opportunities that might involve more risk than would be permitted to be pursued by PP&L as a regulated electric utility. Pursuit of business opportunities with greater risk could, in turn, have either a positive or adverse effect of a Shareowners' investment, depending upon the return realized from such opportunities. (PP&L, "Notice of Annual Meeting of Shareowners," April 26, 1995, page 12).

2) Analyze electric companies' ability to balance economic growth with environmental behavior in the soft regulatory playing fields of the Third World. For example, GPU's unregulated subsidiary, General Portfolios Corporation, owns 50% of a generating station in Bolivia and plans to expand into Central America. PP&L's progeny, Power Markets Development Company recently invested in a gas-fired combustion turbine project in Bolivia. Bear in mind, "Many funds have invested in Latin American utilities, including Telefonos de Mexico, which were badly hurt by the pesos devaluation." ("Newsday," Money and Investing, February 5, 1995.page 7.) 3)Conduct periodic prudence reviews of generating projects. 4) Engage in a constructive and collaborative efforts involving all stake holders based on the model implemented by the Northwest Power System. (See enclosure.)

Three Mile Island Alert (TMIA) strongly supports the PUC's staff recommendation against deregulation. Removing proven and effective operating rules for electrical generation and transmission is not free enterprise nor is it in the best interests of residential customers. Competition is not a realistic option for electrical production until there is a federal initiative to dissolve the substantial subsidies the industry enjoys. The guidance of the Public Utility Commission has realized competition as one of its objectives. Regulation is a surrogate for competition. "One of the goals of public utility regulation is to create the same results within the regulated industry as would occur in a competitive market. In a competitive market, if a firm does not use the efficient alternatives, it must either exit the market or receive a lower than normal return." (Expert Witness Sturgeon, *Re Wolf Creek Nuclear Generating Facility*, 70 PUR 4th 475 (1985), Page 528.)"