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Deregulation in Maine: The Why and How

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I. HIGH RATES

Maine's retail electricity rates - although (on average) the lowest in New England - were in 1997 (the year Maine passed its restructuring legislation) nearly 40 percent higher than the national average. Industrial customers paid rates 40.4 percent above the U.S. average; commercial 36.9 percent more, and residents (i.e., voters) a whopping 51.3 percent more than residential consumers across the country.

Place the risks of investment decisions in the market, where they belong. Technological developments (paralleled by changes in national regulatory policy) have erased the natural monopoly nature of the general portion of the electricity industry. Since regulators are not uniquely qualified to make the best decision on generation investment, why not let the private sector do it? Ratepayers will no longer have to pay for the risk of inefficient decisions. Let investors take the risk - and reap the rewards, if done properly (or if they're lucky).

II. BUILDING BLOCKS - Preparing the Field.

A. Understand your goals - Your approach will vary based on your goals.

Do you want to:

1. Lower electric rates immediately? If so, the legislature or the PUC might mandate an artificially low (i.e., below market rate) default rate, or require utilities to lower their by a specified fixed percent. This begs the question of how the utilities achieve their revenue requirement. Such an arrangement is not sustainable long term.

2. Lower electric rates in the long run? Today, Maine is paying high prices because of state and Federal policy coupled with aggressive regulator action. We believe that, in the long run, retail competition will move Maine's electric rates closer to lower national-average prices. Moving toward national-average prices is clearly beneficial if your prices are currently above the national average. If you are below the national average, will opening to competition result in lower prices?

3. Place decision-making and risk in the market? Facilitate markets and be on guard to protect consumers - business and residential - from market-power or consumer abuses. Work to allow the energy market to settle at an economically efficient price, while still regulating the T&D company as the monopoly company it still is. We believe this approach offers the greatest benefits for consumers - residential or business - over the long run.

B. Level the playing field for market participants.

1. Full divestiture of generating assets. Maine is the only state which, by statute, required full divestiture. Maine's competition law required utilities to divest themselves of their generating assets to ensure that the remaining utility - a transmission and distribution (T&D) utility, a "wireless company" - had no incentive to favor any one seller of electricity supply over any other. We believe that divestiture is critical to ensuring a

"level playing field."

2. Strict affiliate transaction rules. If affiliates of T&D companies are permitted to sell generation, clear, fair, and strict rules should be designed to ensure that T&D utilities cannot unfairly favor their marketing affiliate. In a field where margins are likely to be thin, these restrictions may discourage utilities from marketing electric supply.

3. Let the market determine the price of default service. The dilemma: highly priced default service promotes competition (through a "price umbrella" which exacts above-market prices from non-choosing [i.e., default] consumers); prices administratively (or legislatively) set too low preclude competitors from entering the market, effectively preserving a monopoly. Maine's answer: bid out the opportunity to be the default (we call it "Standard Offer") provider. While Maine's initial effort did not go fully as expected, we continue to believe bidding out default service is the best approach.

C. Educate customers - Proactively inform, don't wait for them to ask.

Use stakeholder input and hire an experienced, professional firm. Be prepared that consumers won't listen until the last minute, but then be prepared to inform them through a variety of media. Keep print and broadcast journalists fully informed; based on Maine's experience, they serve two valuable functions - disseminating information and dispelling mistrust.

D. Details! Details! Pay attention to details! - Get the infrastructure in place.

You ignore this at your peril. Market players - utilities are competitive suppliers - abhor uncertainty; they want to know what the rules are. Give utilities the time and the tools (and prod them constantly!). Give yourselves the time to think out your rules carefully.

1. Get your rules in place. Do it in time for all market participants to do what's necessary to support competition. Make your rules compatible with those of nearby states; this creates larger markets, attracts competitors, and facilitates their entry into your market. The Maine Commission had 2 3/4 years to implement Maine's competition law. [In fact, we had even more time, if you consider that the bill the Legislature passes was the basic design and 90 percent of the details of a plan developed by the Commission over 18 months (mid-1995 through its presentation to the Legislature in December 1996).

2. Redesign utility billing systems. Anyone who has worked with these systems knows that everything is harder than you might think.

3. Set up utility procedures to enroll customer and interact with providers. Most states are using EDI transactions to exchange data. Competitors will expect it, but it takes players time to implement the procedures.

E. Recruit competitors.

This was difficult in Maine. We spoke to provider groups, regularly informed the trade press, hired a consultant to advise us and reach out to suppliers, developed a useable webpage dedicated to providers, offered supplier training monthly, and asked them to help us write the rules and procedures.

F. Monitor and work to improve markets and eliminate market-power abuses.

Markets are not fully developed when they start. They require fine-tuning at the least and sometimes major revisions. Companies used to competing in wholesale markets are unlikely to be savvy retailers.

III. PROBLEMS AND PITFALLS

A. Wholesale market rules.

In New England, an immature regional market has been a big problem. Because rules are not fully developed, the future is uncertain. This risk is reflected in provider's higher prices and reduced participation in Maine's standard offer bidding.

B. Competing activity in other states.

Providers are scrambling to keep informed of the newest development. Many are small operations and cannot be active in all states. When we requested default-service bids, some providers were concentrating on Pennsylvania and Connecticut and had few resources left to bid in Maine.
Renewable resource portfolio requirement - Might be a problem; we're not sure. Some states (not all) have a renewable requirement. Early experience indicates that there is a price premium (maybe ½ cent, but that is very, very uncertain) to cover the requirement. But equally important, the requirement is a hassle, which may discourage competitors from entering the market at all.

C. Consumer protections.

The law protects small businesses and residential consumers. Some suppliers have said that Maine's five-day rescission period is a barrier. Default-service bidders were concerned about the ability of residential customers to opt out of default service at will.

IV. WILL CUSTOMER CHOICE TAKE OFF?

Yes! Definitely for businesses, even relatively small businesses. Within six weeks of the start of competition in Maine, competitive suppliers had won a quarter of Maine's load, perhaps 1,500 customers (out of 650,000). Anecdotal comments from suppliers lead us to believe that "medium-sized" businesses will soon be served. Residential will take a while longer.

This is a marathon, not a sprint. Short-term price drops, or high market participation immediately, are not goals for us. Long-term price drops to the national average and efficient adequate supply will spell success here.

Be careful of your measures of success - especially since this may be linked to political judgements of how well competition is working (and how well the SCC has done its job). Don't make the presence or absence of competitors the determinant of success. Having educated consumers able to benefit from competition, we found some critical when competition did not appear on opening day - even though their prices dropped by an average of 10 percent.

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[*]William M. Nugent, Commissioner. Now in his ninth year as a Commissioner on the Maine Public Utilities Commission, Mr. Nugent has been working for more than five years to bring full retail electricity competition to Maine. It began on March 1, 2000. Prior to joining the Commission in 1991, Nugent was Executive Vice President and Chief Operating Officer of a Portland environmental consulting firm and subsequently President and CEO of Maine's largest Chamber of Commerce. A former president of the New England Conference of Public Utility Commissioners, Nugent currently serves as Second Vice President of the National Association of Regulatory Utility Commissioners. He also chairs NARUC's Regulatory Strategies Committee, is a member of the Executive Committee of the World Forum on Energy Regulation and director of National Regulatory Research Institute. The Senior Commissioner on NARUC's Committee on International Relations, Nugent has presented at and participated in training/conferences/missions to Cairo, Riga, Warsaw, and Budapest. He has visited more than two dozen counties in Europe, African, and the Americas. Previously, Nugent was Deputy Director of Management and Budget for the State Michigan, Commissioner of the Michigan Lottery, and a staff member of the White House Council, the Office of the Secretary of Defense, and in the State Department. Commissioner Nugent attended the U.S. Military Academy at West Point, is a Phi Beta Kappa graduate of Fordham University, and studied public administration as a Heinz Fellow at the University of Pittsburgh.

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