The State of State-by-State Deregulation

Despite colossal failures, states push slowly ahead

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Although the early momentum for utility deregulation has waned, the restructuring process continues, somewhat behind the scenes. A recap of activities is timely.

HISTORY

The Federal Energy Regulatory Commission (FERC) initiated the deregulation of utility prices in the 1980s when it relaxed its regulation of prices in wholesale markets. The resulting competition produced markedly lower prices in most wholesale power and natural gas markets. Deregulation of retail utility prices at the state level was launched to take advantage of prevailing lower prices in wholesale markets in states where retail electricity prices were persistently high.

However, low priced states stayed on the sidelines. As is well known, California led the way and suffered a dramatic failure. The California failure tainted electricity markets in all of the surrounding western states, all of which reviewed their own deregulation plans. Other states followed suit. Now that the dust has settled, only one or two states have abandoned plans to deregulate, although several states have delayed the onset. Notably, Texas, Virginia, and Oregon are all proceeding with some form of retail access this year. In summary, state-level action to deregulate retail electric (and natural gas) markets has slowed, but not stopped. Delays are concentrated in states that currently enjoy low power rates and have little to gain from retail competition.

PRICE VOLATILITY

As some states are slowing the pace of deregulation, the FERC is stepping up its efforts. The FERC is pushing electric utilities to form multi-state trading zones and open access to low-cost power providers within those zones. It is also urging electric and natural gas traders to adopt similar rules and procedures to make it easier to trade energy instead of just power and gas commodities. FERC is also actively advocating the construction of new power transmission lines to facilitate the further development of competitive electricity markets. One of the consequences of FERC's efforts to create regional power markets is increased power price volatility. Although price volatility is one of the hallmarks of commodity markets, it is not a welcome feature of retail power rates for state regulators. As a result, it is inevitable that

Illustration by Mark Harvey

there will be collisions between FERC actions and state efforts to hold power rates down and keep them from wild fluctuations. These have appeared in several western states, where retail rates held constant during the California crisis, but were increased 50 percent or more the following year. Consumers are asking, "Why is it that my rates have gone up, when wholesale prices are going down?" This kind of lag in retail rates is inevitable, until wholesale and retail rates are more closely tied together. In fact, closer links between wholesale and retail rates will continue to drive retail deregulation forward.

THE FUTURE: TEMPERED DEREGULATION

What does this mean for property and facility managers? Retail deregulation will continue. States that have deregulated will stay the course and new ones will join them, but probably not soon. Regulators will be leery of price volatility in wholesale markets infecting retail rates and will probably require retail power suppliers to offer products with price guarantees. Oregon has adopted a modified form of deregulation that may provide a model. It allows larger customers to shop for power, but provides a safe-haven regulated rate as well. Smaller customers can choose either fixed rate or floating price options, but both are subject to cost-of-service review. It won't protect against price increases, but provides some protection against price gouging. Utilities and regulators in all states are exploring new rate design options to address this issue. Most utilities and regulatory commissions have useful Web sites. Go to the sites of your local utility to learn more.

Preparing for the future should continue along the same path as if deregulation were imminent, namely:

- Understand when, where, and how much energy you use.
- Control all these variables as best you can.
- Increase your control over the timing and amount of energy use, especially at peak-load.

Potential inefficiencies in gas and electric markets and between wholesale and retail markets may justify dual-fuel equipment and on-site generation of some sort, especially co-generation applications of small to medium scale. Access to power from renewable resources will increase and price premiums should decrease. Committing to purchases of renewable or "green" power for a fixed price premium today may provide an economic hedge against future price volatility.

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