

# Restructuring Today

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## National customer aggregation sought by NEMA

### QUOTE OF THE DAY:

I want Nora [Brownell] to hear this. Demand aggregation at the national level is critical to problems of scale. When marketers can have millions of customers instead of the local 10,000 or 100,000 that's when you're talking about national scale... We've got thousands of McDonalds out there each paying a retail, single-meter rate. There has to be a way to aggregate demand on a national level so that someone like [he names NEMA members at the table] can literally aggregate and service and offer a discount coast-to-coast for a McDonalds who wants to buy from one supplier coast-to-coast

and get one bill and that's totally impossible now but that's where we need to be.

*NEMA President Craig Goodman at the group's closing session.*

### 2d QUOTE OF THE

**DAY:** I think that that [above] would be a great issue for Stan Wise to undertake as chairman of NARUC [laughter].

*FERC Commissioner Nora Brownell responding to Goodman (above) in the presence of Wise who was a speaker and who is to take over as the next NARUC president. Wise is a member of the Georgia PSC. Brownell had been NARUC president when she was named to FERC.*

## Arizona chairman for markets at NEMA convention

Arizona Corporate Commission (ACC) Chairman Marc Spitzer does not favor electricity and gas prices "set by state regulators."

He favors prices "set by supply and demand," he told NEMA last week in Washington.

He does not count himself among the "large contingent of state regulators and their constituencies that want to return to the discredited price-setting mechanism of command and control.

"Opponents of competition are doomed to failure by the simple forces of economics," he added.

The ACC is an elected body and running successfully as a Republican required Spitzer to overcome the political stereotype that his party was in bed with utilities and would always vote to raise rates.

Now Spitzer sees politics making for "strange bedfellows" as opponents of competition muster their forces.

"We've got the left coast in league with southern monopolists," Spitzer observed, along with those Wall St investors who "feel singed by competition."

"I've had analysts bluntly tell me they don't like competition anymore because

under competition, God forbid, you can lose money."

Wall St in 1999 wanted every utility to become an Enron-type trader, Spitzer reminded, but now is "demanding vertically integrated monopolies."

Spitzer contended that FERC's SMD does not promote competition and "may have created a backlash that induces more uncertainty."

As a former tax lawyer, Spitzer sees FERC's NOPR as "running into a text that will rival the Internal Revenue code.

"We don't want to live by laws that are incomprehensible."

Spitzer agrees that utilities ought to have the option of protecting their native load.

"I have 5 million ratepayers that paid for the wires and paid for the poles and those folks ought to have some consideration as well."

Federal jurisdiction over public power, Spitzer said, is "a uniquely western issue."

Generations of Arizona politicians have negotiated contracts and some have been codified in federal law, Spitzer noted, and he would be upset if "a bureaucrat on the Potomac simply overrides 100 years of state history."

## Wise cites what regulators like to do

"Regulators regulate," said Stan Wise. "They love that piece of what they do even in a deregulated market" like gas in Georgia.

"We love to tinker and manipulate and solve problems or at least try to solve problems... in something that should be market-driven."

What you don't see in a regulated market is technology developments, he added, since technology is driven by an open market.

He's looking for ways as a regulator where "markets can drive the equation."

The best solutions, Wise said, may be the one that gets him and Commissioner Judy Jones of Ohio (also on the panel) "out of the way." NEMA Chief Craig Goodman reported hearing from members fears of price caps in Georgia, a move Goodman described as only appropriate for "an absolute emergency."

Wise is against price caps, he replied, and he knows of no reason why the Georgia commission would do that.

Wise was bullish on the Georgia gas market now that price competition has broken forth. Some people are now saving 50% on their gas, he noted.

Some are paying a fixed commodity rate of 51-55¢/therm compared with variable rates of \$1.10-1.14.

Shell's variable rate is actually about \$1.27.

April prices? We checked on the fifth of the month but since it was a weekend the month's prices were posted on the PUC website.

"There's no fuel cost recovery docket," Wise said with pride.

The RTO framework provides certainty, Spitzer acknowledged, but regional differences must be recognized.

The ACC has "never failed to site a transmission line," Spitzer added.

Spitzer sees irony in some of his "more liberal left-coast colleagues" raising the

## 3 stories in 0.8 minutes

### Sorting out Enron

**debris costly:** Enron has hired 48 law and accounting firms and legal fees exceed \$318 million, more than it cost to build the ballpark that was called Enron Field. Its primary bankruptcy firm of Weil, Gotshal & Manges has billed Enron \$60 million over the 17 months, not counting invoices it has yet to submit. Bankruptcy Judge Arthur Gonzales last week approved Enron's hiring of another firm to avoid mounting conflicts of interest among attorneys representing the many interests in the case. The total fees could exceed half a billion dollars, the most expensive bankruptcy ever.

### Ont keeping plan

**to curtail use:** The Ontario market was able to get through a record-breaking summer without calling on customers who had signed up for curtailments. Prices spiked and that led many to cut power use and thus allowed the Independent Electricity Market Operator (IMO) to get through a tough challenge. OK, what happens next summer when retail prices for half the market can't spike? The IMO last week extended its emergency demand response program for another year citing the price caps that may have a negative effect on demand response. The program was to expire this month. More generation will be online this summer and the IMO is looking at signing up customers for an hour-ahead dispatchable load program.

### NYC parks to get

**free web access:** The Alliance for Downtown New York (ADNY) intends hooking up free high-speed wireless internet access in six parks and public spaces in Lower Manhattan next month for use by anyone with a laptop or personal digital assistant (PDA). The system is being created by Emenity, a for-profit company formerly known as Cloud Networks, that is affiliated with NYC Wireless. The project will be one of the largest free wireless networks in the nation, said Anthony Townsend, Emenity COO.

states' rights issue.

"I've had great fun reminding them that the last Democrat to argue states rights was [former Georgia governor] Lester Maddox."

Spitzer expressed the hope that "there are federalists inside the Republican party who have the ability to recognize the concerns of individual states.

"The rejection of competition is futile. The proponents of competition will win," Spitzer predicted.

But his views have evolved.

"Arizona's transition to a restructured electricity market has already achieved notable success," he wrote (RT, 7/22) of the market that had been let's-pretend open for 18 months.

He listed benefits as investment in new generating capacity along with "viable and vibrant local utilities and most importantly Arizona consumers continue to enjoy reliable and affordable electricity."

### S&P sees \$50/mwh over 12 months

History is not likely to repeat itself when it comes to gas prices this year, Standard & Poor's said in its report on energy commodities.

Gas prices spiked to \$10/mmbtu in January 2001, S&P reminded, but reduced demand, increased supply and competition from coal and nuclear power brought the price back down to \$3/mmbtu.

The biggest difference between now and two years ago is the pace of drilling, S&P said, because that remains "well below levels achieved during the natural gas bull market of 2001."

The Mid-Atlantic cost of forward power rose with higher gas prices and cold weather, S&P found, and they forecast an average over the next 12 months of \$50/mwh.

The Midwest is trading at \$37/mwh, the South about \$40/mwh and Texas about \$45. Less efficient units and limited grid capacity have led to an \$80/mwh price in New York City and \$60/mwh in Boston.

The forward curve shows a gross margin for a 7,100 btu/kwh gas unit in the Midwest remaining "dismal" but better than in the East.

The more efficient units saw better

### Perlman forecasts Texas won't give up markets

The message in Texas has been "choice and innovation," said PUC Commissioner Brett Perlman, thus establishing a broader base of support for competition.

It takes a "leap of faith" to come to the conclusion that competitive markets are better than old-style monopolies, Perlman told NEMA. "In Texas we made a commitment," he said, and "there's no going back."

He was disappointed that the public doesn't shop.

Spitzer decried "the failure of retail electric competition, the failure of IPPs to invest in solutions to Arizona's transmission-constrained areas — the same areas in which they proclaim a desire to serve — and the failure of the parties to reach agreement on competitive solicitation in Arizona's wholesale electricity market during a period of historically low wholesale prices."

Spitzer found that with "zero residential customers taking competitive service in Arizona," the captive-customer argument "for a delay in implementing the transfer and separation of assets is particularly compelling."

In how many states have the regulators created markets where sellers wouldn't think of coming in then the regulators step back and accuse the market of not working?

We've lost count.

spark spreads, especially in New York City where the implied gross margin rose by \$40/kw year to \$175.

Boston is up \$20 to \$70/kw year while overall the Mid-Atlantic has risen \$15/kw year to \$44 and the South is up \$10 at \$31.

Heavy rainfall in the Northwest has mitigated drought concerns, S&P said, and forward prices have "tumbled."

The 12-month strip fell to \$38/mwh from a high of \$58 in late February.

The average break-even heat rate for the next 12-months is 7,400 btu/kwh down from 9,800/btu/kwh, dropping the net revenue for a 7,100 btu/kwh gas unit to \$13.40/kw year from a month ago.

Hydropower had a smaller effect on prices in other western regions, S&P reported.

The 12-month forward strip rose \$5/mwh for Southern California (\$56), Northern California (\$54) and Arizona (\$50).

The implied net revenue for 7,100 btu/kwh gas plants improved to \$80/kw year in Southern California, \$72/kw-year in Northern California and \$51/kw-year in Arizona.

While everyone is watching Texas to see whether competition can succeed, Ohio has the highest electricity switching statistics anywhere in the US with 13.5% of its residential and small commercial customers buying from competitive suppliers.

Only 7.3% have switched in Texas, noted Ohio Commissioner Judy Jones. That success has come largely from

municipal aggregation programs in 150 cities, villages, counties and towns that have taken 700,000 customers off full utility service.

Local voters have to OK aggregation but considering that fewer than half of eligible adults vote and no more than a majority of one is required to pass municipal aggregation, many still are taken by surprise when they begin getting bills from a supplier other than their utility, Jones noted.

Even with opt-out aggregation, educational efforts are important and Ohio used an ad agency and public relations firm to make sure the public knew what was going on.

Ohio's biggest dilemma isn't choice, it's seams, a problem Jones pointed out on a multi-colored map that showed Ohio's bifurcated RTO map where some utilities belong to MISO and others are going into PJM.

Almost 8,500 mw of generation — mostly gas-fired peakers — have been built in Ohio's market since price spikes in the late 1990s, bringing "home the

## Centrica official decries price expectations

Ontario's retreat back to price caps last fall shows the dangers of overselling consumer savings as the single benefit of competitive markets, a Centrica official told NEMA's meeting last week.

A hot summer in Ontario and shutting down a couple of generation plants sent prices skyward and brought a "huge outcry" from disappointed consumers, explained Nick Fulford, senior vice president of business development at the international mega-marketing firm.

Service and innovation are just as important, he explained, and Centrica spends a lot of time trying to "create real glue between" the commodity and services.

"It's not just about cents per kwh."

The danger of overstating the savings without selling the services is "you can have sudden and substantial churn [customer loss] without that glue," Fulford warned.

Centrica's business model in the UK is to sell a lot of people a lot of different things.

The 20 million households that are its

## California sets time-of-use pilot

The PUC and California Energy Commission (CEC) picked Charles River Associates to run a pilot program to estimate the impact of time-of-use pricing and assess the benefits of advanced metering technology statewide.

importance of a strong, competitive wholesale market," Jones noted.

The threat of future spikes has made Jones, along with other Midwest regulators supporters of SMD but Ohio and other states are hedging their bets by working together on transmission-siting issues.

Ohio law doesn't force utilities to sell their generation but it does require them to turn their grids over to an RTO, she noted.

Two years into "competitive markets" most Ohioans like choice, particularly affluent city dwellers 45 or younger, Jones reported.

Most distrustful are older people who worry service will deteriorate if they leave their utility.

As successful as the programs have been there's that temptation to return to the comfort of the old ways.

"We've been regulators so long" and PUC staffs are so used to the old ways, "it's hard to turn the ship around and look at things in new ways."

But, she added, "Ohio made a commitment" to competitive electricity and gas markets.

customers buy on average two Centrica products that might be power, natural gas, credit card or membership in the auto club.

The company's philosophy is to offer choice, a "suite" of competitive services and provide outstanding customer service.

So far Centrica has invested \$1.6 billion in North American acquisitions and \$100 million in organic growth to build a customer base expected to hit 5.5 million this summer.

All will come under the Direct Energy Essential Home Services banner due for continent-wide rollout soon.

Advances in technology and metering will create the next wave in competitive markets as consumers look for providers who can supply electricity, natural gas, energy management, home security and home entertainment in one convenient package.

A large part of the value of competitive markets will come from customer demand for new services, Fulford noted.

The test group is to have 2,600 residential and small business customers.

The 18-month program begins in July. They call it a "large-scale social experiment" to be applied in other areas.

## NewEnergy leader calls for market tuning

After more than a year of bad press over Enron and California, how can the industry get everyone to focus on the good stuff competitive markets have provided, Clem Palevich asked the NEMA marketers last week.

Markets need fine-tuning to get over the crises of the past couple of years, he said.

We're "a nation of bandwagon jumpers," the president of Constellation NewEnergy said.

The firm may be the USA's largest retail marketer.

The fundamentals of markets are there, he noted, with a glut of capacity and some 100,000 mw of C&I customers eligible to choose.

But just 40,000 mw have switched.

The key is going to be crafting "value-added products" to get customers to switch.

Rational credit and risk management policies and practices are evolving and the marketplace is coming up with financial products to ease risk but "we need physical" products as well, he noted — structured products that fit customers' load profiles.

Constellation is active in 13 states and provinces — everywhere that has a "viable" market design, said Palevich — but better retail design is critical.

"PJM is a great wholesale market," he said, but Pennsylvania retail is "a bust of a market."

Palevich urged better and more standardized data exchange, evoking nods and smiles throughout the room, as well as stable regulation and structure.

One of the biggest risk-management problems now is regulatory uncertainty, he noted.

Regulators need to provide strong enforcement but mustn't "inhibit innovation in the market."

The light at the end of the tunnel is faintly visible. A recent *Los Angeles Times* article lauded Texas' market as succeeding where California's failed.

"If California is willing to concede that to Texas, then anything is possible," Palevich quipped.

## CFTC seeks energy regulatory balance

The CFTC doesn't want to stifle innovation by regulating markets too closely but those who violate the rules will feel the commission's teeth, Chairman James Newsome told NEMA's conference in Washington last week.

More charges may be filed as the regulator continues its probes of electricity and gas markets during the California crisis, Newsome warned.

"The temptation to resort to static rules is hard to resist," Newsome said, but that would "stifle legitimate business activity."

Risk management is "critically important to the US economy" and it's time to "identify the wrongdoers" and exonerate the innocent so they can get back to business.

Working with FERC and other federal agencies is making the CFTC "keenly aware" of the special challenges for energy companies trying to manage their risk.

The agency has been working as well with NYMEX, the Intercontinental

Exchange and EnergyClear — providers of clearing services and trading platforms — to develop new rules.

The agency has been looking too at changes in the bankruptcy laws that protect those who use trading platforms.

It's important, Newsome said, "to act quickly and clearly on all fronts so the market can get quickly back on its feet."

Industry efforts to come up with best practices are commendable, Newsome noted.

Using derivatives to manage risk "contributes to greater flexibility, resiliency and efficiency in our economy," Newsome added.

Warren Buffet's attack on derivatives as "weapons of financial mass destruction" points out the importance of spreading the message that derivatives are important to the economy.

"I continue to believe that one-size-fits-all regulations and prohibitions that ignore unique risk-management needs are effective neither in maximizing the efficiency of our various markets nor in

minimizing the risk to participants," Newsome stressed.

Rather, oversight boundaries should be "clearly defined and focused on real risk" to allow "real innovation in risk management while maintaining and enhancing workable safeguards."

That's "not only the best protection against systemic problems but also a good provider of legal and regulatory certainty for business decision makers."

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