HARVARD ELECTRIC POLICY GROUP
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MUNICIPALIZATION - AN IOU PERSPECTIVE

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THE UPSURGE IN MUNICIPALIZATION INTEREST

SOME QUESTIONS:

What is it?

Why is it happening?

What are the forms?

Is it a good Idea for the customer and community? as public policy?

What's the alternative?
MUNICIPALIZATION - WHAT IS IT?

- Displacement of a privately or investor-owned utility with a
  Publicly or government owned utility

- Classic form - local ownership of poles and wires through acquisition or condemnation

  * provides bundled service to retail customers
  * wholesale purchase of electric supply and transmission service

- Many other forms possible (more on this later)
MUNICIPALIZATION - WHY NOW?

In the 1980's, little movement one way or the other

In the 1990's

- Transmission access provisions of NEPAct

- In some regions, retail rates depart dramatically from market prices
MUNICIPALIZATION - WHY NOW?

Retail rates out of line with market prices.

Major Causes Of The Problem: (Varies by region)

(We Say)  Administration of PURPA

(Others Say)  High cost additions to IOU capacity

(But We Reply)  Excess capacity may be the real problem

- Slow economic growth
- PURPA-driven over-investment in supply
- DSM?
ECONOMICS OF NIAGARA MOHAWK GENERATION

(Based on April 7, 1994 Competition" Report)

- Some of our generation is higher cost
  - i.e. Nine Mile Two 9.7¢/kwhr

- But this is offset by capacity of very low cost
  - NM hydro 2.6¢/kwhr
  - Coal: Dunkirk 3 & 4 2.7¢/kwhr

- Total average cost of NM-owned units in 1993
  - at actual 1993 load factors 5.5¢/kwhr
  - at system load factor of 67.9% 5.1¢/kwhr
NIAGARA MOHAWK GENERATION
(Continued)

(Based on April 7, 1994 Competition" Report)

- Estimated cost of new generation

  - New combined cycle
    @ 67.9% c.f.  
    5.1¢/kwhr

  - New coal
    (500mw @ 80%c.f.)  
    5.5¢/kwhr
MUNICIPALIZATION - WHY NOW?

Retail Rates out of line with Market Prices

Other Factors

- Taxation

- Obligation to serve (e.g. rural vs urban)

- Environmental requirements

- Public Policy "incumbent burdens"
MUNICIPALIZATION - THE FORMS
(A Sampling)

• Traditional - Eminent Domain
  - New York
  - Maine

• As intermediary for inter-IOU competition
  - Las Cruces, NM

• Buyer Leverage
  - Ford and Brook Park, Ohio

• "Muni Lite"
  - Falls Church, VA

• Build Your Own
  - Clyde, OH

• Annexation
  - Niagara Mohawk

• "Paper" Municipal
  - Suffolk County, NY
MUNICIPALIZATION - A GOOD IDEA?
(For Customer & Community)

- A major gamble
  - Stranded costs (FERC NOPR)
  - Extensive litigation over proper compensation
  - Cost and risks in securing bulk power
  - Operational risks
    - Storm emergencies
    - Health and safety, etc.
  - Regulatory requirements
MUNICIPALIZATION - A GOOD IDEA?
(For Customer & Community)

- Potential reliability and quality deterioration

- Success possible but far from guaranteed

- Retail access comes anyway
  - Municipalization was unnecessary
  - Competitive risks are inherited
MUNICIPALIZATION - A GOOD IDEA? (As Public Policy)

Economic Efficiency

- Distribution
  - Public vs private ownership
  - Scale economies

- Transmission
  - Loss of T&D vertical economies

- Generation
  - Pitfalls to partial opening of markets
MUNICIPALIZATION - A GOOD IDEA? (As Public Policy)

Fragmentation

- Health and safety
- Consumer Protection
- Fair and equitable ratemaking
- Environmental compliance

Transaction costs

- Legal and engineering
- System reconfiguration
- Protracted litigation
MUNICIPALIZATION
WHAT'S THE ALTERNATIVE?

- Dissatisfaction with prices remains

- Niagara Mohawk view: Competition is best way to improve economic efficiency

- But, real efficiency benefits are long run

- In short run, prices can only be reduced (in a major way) by shifting costs to others

- So

  - Deal equitably and fairly with transition costs

  - Can then expand competition more quickly and effectively