Competition in North American Electricity Markets: The Balance Sheet

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Genesis

- Geographic Rate Differentials
- Market Leverage of Large Customers
- Ideology
- Utility Risk Aversion (State of “Regulatory Compact”)
- Technology Change in Generation and Transmission
- Regulatory Environment
  - Prudence Reviews
  - Skewed Risk/Reward Symmetries
  - Perverse Incentives
  - Externality/Social Considerations
  - Capture
  - Administrative/Political – Not Customer – Focus
The Promise!

- Competition = Lower Prices
- Improved Risk Reward Symmetries
- Greater Product Diversity & Innovation
- Productivity Gains
- Improved Price Signals
- More Focused Management (i.e. On Unbundled Assets)
The Problems/Barriers

- Designing Markets, Retail and Wholesale, is Hard
- Institutional Arrangements Need Basic Change
  - Vertical Integration
  - State and Federal Jurisdictional Issues
  - Impact of Tax Laws and Securitization of Assets
- Public Tolerance of Upward Price Volatility
- Residual Market Power – Horizontal & Vertical

continued …
The Problems/Barriers (con’t)

- Interest Groups: Politics and Governance
- Stranded Assets/Benefits
- Resource Use and Public Policy – What Should Be Left to Market?
- Pricing for End Users/Eliciting Demand Response
- Network Pricing
- Lethargy of Market Participants and of Consumers
The Results

- Market Prices Go Up As Well As Down
- Risk Reward Symmetries – Mixed Signals
  - Bankruptcies in Generation Sector
  - Capacity Market Proposals
  - Changing Role of RTO’s and Planning
  - Leveraging Rate Base
- New Products – Mixed Results
  - Disappointment in Retail Market
  - Commercialization of Unbundled Transmission Services
  - Different Management of Generating Assets

continued …
The Results (con’t)

- Productivity Gains – Mixed Results
  - Perhaps in Generating Plants
  - Yes in Transmission (but RTO costs are controversial)
  - Not Much Change in Distribution – Perhaps Decline

- Improved Pricing – Perhaps in Some Areas
  - LMP in Transmission, Especially in Northeast
  - Transmission Expansion Incentives Uncertain
  - Marginal Cost Pricing for Generators
    - Has That Produced Adequate Supply?
  - Distribution – If Changed, It Is Only Marginal

continued …
The Results (con’t)

- Unbundled Focus – Yes and No
  - Transcos Are Positive Development
  - Mere Functional Separation May Be Inadequate
Dealing With The Problems

- Market Design
  - Mixed Wholesale Results (e.g. CA vs. PJM)
  - Retail Design: Entry Barriers and POLR Issues

- Institutional Arrangements
  - Continued Lack of Clarity on State/Fed Issues
  - Deverticalization Still Optional
  - Tax and Securitization Issues Still Influential

- Intolerance of Price Volatility
  - Electricity is Hard to Depoliticize

- Residual Market Power
  - Vertical Integration = Major Problem in Non-RTO Markets
  - RMR Units
  - Continuing Vigilance Needed on Horizontal Power

continued …
Dealing With The Problems (con’t)

- **Interest Groups: Politics and Governance**
  - Arbitrage Between Markets and Politics Unavoidable
  - No Decline in Politicization of Electricity

- **Resource Options**
  - Conflicting Public Policies: How Much Market Reliance?
  - Basic Tension Between Markets and Planning

- **End User (Demand) Response**
  - Poor Price Signals
  - Gap Between Talk and Action

- **Network Price Signals**
  - Major Improvements in Some Regions: More Transparency
  - Disconnect Between Pricing and Institutions (e.g. Siting)
Where Are We?

- Gone Too Far To Go Back
- Not Gone Far Enough To Know For Sure