

Statement on Behalf of AReM

Senate Committee on Energy, Utilities, and Communications

February 28, 2003

Chairwoman Bowen and Members of the Committee, I thank you for this opportunity to address you on how California Public Utility Commission decisions affect electric rates in California. My name is Steven McClary, and I am speaking today on behalf of the Alliance for Retail Energy Markets or AReM. AReM is the industry association of energy service providers. AReM members provide direct access services to large and small electric customers across the state, in all three utilities' service areas.

You will have heard many views, favorable and otherwise, on the impact of recent CPUC decisions on the rates paid by California consumers. Our customers - the businesses, schools, public agencies and residential consumers who have exercised their right to choose alternative power providers - are also California consumers. Let me add three important points to what you will hear today:

Fairness:

AReM members recognize that their customers, along with all other electric customers who weathered the crises of 2000 and 2001, must pay a fair share of the resulting costs. They are doing at least that. The Public Utilities Commission under then-President Lynch spent much of 2001 and virtually all of 2002 addressing the question of how best to allocate direct access customers their share of the lingering Department of Water Resources (DWR) costs. The Commission heard many hours of testimony and read thousands of pages of briefs and testimony before issuing an order concerning direct access customer cost responsibilities. An overriding goal of that proceeding was to fairly allocate the costs of the crisis between bundled service customers and direct access customers. Their chosen mechanism is the non-bypassable "Cost Responsibility Surcharge," or exit fee, that direct access customers must pay. The CPUC's decisions seek to implement that goal of fair cost allocation, and if anything, the Commission has leaned in the direction of protecting bundled service customers at the expense of direct access. Indeed, many of our customers continue to question why they are paying for power purchased in 2001 and 2002 when they received none of that power.

The Exit Fee:

There are no loopholes in the exit fee, sometimes referred to as the CRS: if a customer was on bundled service during the crisis, even for one day, that customer is liable for the Cost Responsibility Surcharge. The cutoff date for direct access customers to be exempted from a portion of the surcharge was moved up by ~~three~~ five months from July 1, 2001 to the beginning of February 2001. This means that only a small fraction of direct access customers - those who never relied on the DWR for power purchases - are exempted from some (though not all) of the exit fee.

Direct access customers are not escaping payment of the costs of the energy crisis at the expense of other ratepayers.

Lets look at what direct access customers are paying through the Cost Responsibility Surcharge:

- First, direct access customers are paying for DWR power they consumed during the crisis. They are paying this through the DWR bond charge, and they are paying the very same Bond Charge rate as that paid by bundled customers. It doesn't matter if they only used DWR power for a single day, the exit fee includes the full DWR Bond Charge.
- Second, through the CRS direct access customers are paying for the ongoing DWR contracts. This is in spite of the fact that they're not receiving any power delivered under those contracts — not a single kWh.
- Third, direct access customers are continuing to pay for utility stranded costs, again, even though they're not receiving a single kWh from them. This is true of even the direct access customers who remained on direct access service throughout the crisis, never buying a single kWh from either the utility or the DWR.
- Here in Southern California, direct access customers are also paying off Edison's costs recorded in the "PROACT" account, and in fact will continue to do so long after bundled customers are off the hook.

The total amount to be paid by direct access customers through the CRS has yet to be determined. In fact, it cannot be absolutely determined, because it depends on such factors as the ongoing market price of power, the outcome of DWR's contract negotiations, and litigation winding through the court system and through FERC. The Commission has set the policy on the elements of the exit fee, but final numbers have yet to be determined. The numbers for the upcoming year will come out of ongoing Commission-sponsored workshops and proceedings. Estimates of the amount to be paid by direct access customers will be revisited every year, and if the Commission mis-estimates it this year, it can—and will—be revised the following. Anyone saying that the total amount owed is X, Y, or Z dollars is only proffering their estimate of the actual costs to be recovered.

Furthermore, the current 2.7 cent per kilowatt-hour cap on the exit fee is also subject to adjustment. The Commission is currently examining the level of the cap and will adjust the cap if it there's a problem.

The Balancing Account:

Balancing accounts, such as the one that will collect costs related to the cap on exit fees, are a standard ratemaking tool in California and elsewhere. The balancing account is conventional ratemaking practice and is used to reduce the volatility of rates, easing the rate shock of sudden changes in rates and tracking costs that can not be known in advance. Any shortfall resulting from the CRS cap will be paid off, with interest, by direct access customers—bundled customers will be made whole. Such balancing accounts are an established, tried and true aspect of utility accounting. There are numerous such accounts in use today, without controversy. Their purpose is to make sure an obligation is paid with interest, without creating undue rate volatility. That is

exactly what this balancing account will accomplish. This is an established and fair way to address exactly this kind of issue.

While we don't know today how the exit fee responsibility will develop, the impact on bundled service customer rates of any short-term undercollection resulting from the CRS cap is likely to be small compared to other factors, such as DWR bond charges, ongoing DWR charges, or even general rate increases. Estimates of how much might be needed to be held in the balancing account are on the order of a few hundred million dollars for Edison and PG&E and will be paid down in roughly a decade. For SDG&E, current estimates are that there may be no undercollection resulting from the CRS cap. The Edison and PG&E numbers may sound like a lot, and they are, but put them in context:

- the DWR bonds are covering a shortfall of \$10 billion—the amount of the debt obligation, and is being financed through 2020. Direct access customers are paying the same as the bundled customers on this.
- The ongoing DWR contracts are obligations of tens of billions of dollars until beyond 2010. Again, direct access customers are paying for part of this power, even though they're not receiving any of those kWhs.
- In its ongoing General Rate Case, Southern California Edison is asking for an additional \$286 million per year in base rates. PG&E is proposing a similar increase, and SDG&E is likely to, too. Unlike debt accrued in the DA CRS balancing account, these charges will be a permanent burden to ratepayers, bundled and direct access alike.

In short:

- Direct access customers, like other ratepayers, are paying their fair share, if not more, of the costs run up during the power crisis,
- The mechanism devised by the Commission to receive direct access customer's contributions is a standard and appropriate ratemaking tool that does not create a true burden on non-direct access customers,
- The scale of any possible undercollection resulting from the implementation of a cap on the DA CRS---remember we don't and cannot know exactly what that is-- likely pales in comparison to the other huge costs run up in ratepayers' names by the DWR and utilities.

Finally, let me add one additional point: the California companies and residents currently taking direct access service made that decision in order to manage their energy costs in a time of crisis. After-the-fact rate increases such as the exit fee make it harder for California companies to compete with operations elsewhere, where rates are lower and the regulatory climate more stable. In the face of those high costs companies are faced with laying off employees, or even going out of business. When considering electricity rates in this state, both for direct access and bundled service customers, AReM urges the committee to bear in mind the larger economic issues facing the state and seek solutions that help get the economy get back on track and keep jobs in California.

Thank you.