Senate Energy and Technology Committee

PA 286 of 2008

Prepared Testimony of

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Who is Energy Choice NOW?

Energy Choice Now is a coalition of more than 100 Michigan businesses, consumers, suppliers, trade associations, and other interested stakeholders that are committed to passing legislation that will raise the current cap on Michigan's electric suppliers, increase competition, and lower energy costs. Since our launch in August, 2010, our Coalition continues to grow each month. We pledge to work hand-in-hand with every member of the Michigan Legislature who recognizes that the current 10 percent cap on electric competition harms Michigan businesses and families.

Michigan's Successful Choice Market 2000-2008

Following the identification of energy costs as a barrier to Michigan's competitiveness in the late 1990s, Governor John Engler embarked upon the task of opening up Michigan's electric market to competition. The Michigan legislature passed the "Customer Choice and Electric Reliability Act" of 2000.

In return for supporting a competitive market, Michigan's major publicly-owned utilities successfully bargained for two compensating devices. First, the utilities were allowed the full recovery of "net stranded costs" and "implementation costs." This compensated utilities for any financial losses due to their generation costs being above the competitive market. After the utilities received over $163 million in net stranded costs awards ($63 million for Consumers[1] and over $100 million for DTE[2]), it was determined by the MPSC in 2006 that DTE and Consumers Energy had fully recovered all stranded costs.[3]

Second, the utilities were allowed to "securitize" certain assets through a 15-year bond issue.[4] Consumers Energy was allowed to securitize up to $468.8 million[5] and DTE up to $1.74 billion[6]. This guaranteed the recovery of costs for generation facilities that likely could never compete in the marketplace. Costs for the securitization bonds will continue to be charged all customers – including Electric Choice customers – on their monthly utility bills through 2015.

Between 2000 and 2008, electric customers were able to choose their own electric supplier, and Michigan businesses saved over $400 million in energy costs through participation in the electric choice program.

During the period of full Electric Choice, 2000-2008, over 4,000 megawatts of new generating capacity was built by independent suppliers in our state and Michigan began to significantly close the gap on energy rates with neighboring and competing states.

- Plants in Dearborn, Zeeland, Covert, Carson City and Jackson built at shareholder expense and risk
- Increased reliability in Michigan
- Proof that new generation can be built under competition – without mandates that customers pay for utility mistakes

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1 MPSC Case # U-13720/U-14098
2 MPSC Case # U-13808
3 MPSC Case # U-14526/U-13808-R
4 PA 142 of 2000
5 MPSC Case # U-12505
6 MPSC Case # U-12478

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After receiving over $163 million in stranded costs and implementation costs and having over $2.2 billion of their assets securitized by the State of Michigan (for which customers will pay until 2015), in 2007 the major utilities began a concerted effort to eliminate or restrict competition.

PA 286 Enacted

The current cap on electricity supply in Michigan was mandated on October 16, 2008, after the Michigan Legislature passed and former Governor Granholm signed PA 286 into law. The major provisions of the "energy reform" package:

- Limited competition to just 10 percent of load
- Instituted renewable mandate – but limited ability for companies to buy from others
- Reduced rate regulation on the Utilities
  - MPSC has to approve almost all rate hikes
  - MPSC has only 180 days to approve a hike, or utility can "self-implement"
- Called for deskewing -- aimed at reducing manufacturer rates – and increasing residential
- New provisions for financing new power plants under the Certificate of Necessity process

What happened?

- Utilities hailed passage
  - Said cleared way for new plants
  - Said would lower rates for factories
  - Said would provide greater "predictability"
- Reality
  - No new plants – none needed!
  - Industrial rates increase despite demand reduction
  - Twice a year, predictably, they raise their rates.
  - Cap hit in a year.

The Impact of Killing Competition: Skyrocketing Rate Hikes

At the time PA 286 was under consideration, proponents asserted that the 10% cap on electric choice was needed in order to build new power plants and that in any event it would not be reached for a very long time. However, the cap was reached in the Consumers Energy service territory in August, 2009 and in the DTE service territory in December, 2009— approximately one year from the effective date of PA 286. Since then,

- Gap between Michigan and other states grows
  - Especially Illinois and Ohio, who have used competition to lower rates
- Michigan rates now above national average
- Utilities decide they don't need additional power, drop plans for new plants
- Government is picking winners – those who were lucky enough to leave utilities – and losers – those forced to stay

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Michigan is now in a situation where a significant portion of its commercial and industrial customer base is "locked out" from the benefits and savings from competitively priced power. Today, over 5,500 customers of Detroit Edison and Consumers Energy are in the Electric Choice "queue" – unable to take competitive electric supply because of the Cap. Although prevailing market prices are dropping, Michigan's electric rates are increasing rapidly.

It's no surprise that Michigan consumers are frustrated. According to data from the Michigan Public Service Commission, DTE has raised residential rates by 10 percent annually since 2008, a whopping 29.9 percent increase. From 2000 to 2008, when DTE faced competition under state law, DTE raised rates for customers by about 3 percent a year. Consumer Energy (CMS) rates have increased, on average, by 25%, with commercial rates at 26%-31% and industrial rates soaring at 34%-38%.

These significant electric rate increases are occurring while the rest of the nation benefitted from a roughly 50 percent drop in wholesale electricity prices. Due to the cap on retail competition, 90 percent of Michigan consumers are being deprived of those dramatic electric price reductions.

Competitive Retail Electric Markets Needed Time To Become Fully Functional

Most major markets passed legislation to allow for electricity competition between 1998-1999. The purpose was to bring the benefits of the competitive wholesale markets to the retail customer. In Michigan, while the legislation passed in 2000, final MPSC orders and tariffs to allow full retail competition were not complete and full competition for all customers allowed until January 2002[7]. From 2001-2005 there were still necessary aspects of the retail markets that needed to mature to allow customers the ability to fully realize the benefits of retail competition. 1) utility system changes to allow customers to switch 2)full development of Regional Transmission Organizations and 3) customer education.

While many laws were passed to open the markets early on it took two years or more across all states for utilities to create systems which would allow customer switching to occur. Then and still today the utility remains the entity that not only reads the meter but also maintains the lines. For a supplier to serve a customer both the suppliers systems and the utility must sync together. This is necessary for access to customer data, but also for a supplier to provide data on electricity delivery to the utility to ensure system integrity. This first essential process had to be in place before even a single customer could be served.

The second critical item was a fully functional Regional Transmission Organization or RTO to allow power to flow from outside the utility service territory. The whole purpose of a RTO is to allow power to flow from a generator across many transmission service territories at a single price. In other words postage stamp rates as long as the power remains within the RTO. From 2004-2005 the Midwest Independent System Operator or MISO region became fully operational and what were referred to as seams within MISO were eliminated[8]. Although fully functional the development within each RTO has been dramatically different. MISO currently covers only three competitive states with the rest of the states remaining traditional monopolies. Therefore the development of MISO has tended to follow a socialization of

[7] MPSC Case # U-11290
[8] *Midwest Independent Transmission System Operator, Inc.*, 109 FERC ¶ 61,168 (2004) (November 18 Order), *reh'g pending Docket# ER05-6*

costs and not necessarily competitive approach to costs. PJM however covers the mid-atlantic states which are competitive. The PJM approach tends to move faster than MISO and be market based. In the PJM states retail competition has increased at a much greater pace than those states within MISO and effective January 2012 all of Ohio will be within PJM leaving Michigan and a very small portion of Illinois as the remaining competitive states within MISO.

The third piece was and continues to be customer education. Electric competition while not complicated was a major change to a customer culture that had never before had choice. Therefore the first movers were the larger commercial and industrial customers. From a supplier perspective it is easier to work with one entity that has the load of 5,000 residential customers than to educate 5,000 residential customers. At the beginning of 2007 (5 years after the market fully opened) as RTO's and markets matured the focus in many states turned to residential customers. It was at this time that Michigan moved to cap competition. As markets tend to do there comes the tipping point where the education and market forces collide to move a market forward. For electricity competition this started in late 2008-2009. Referring to figures 1 and 2 attached the PJM markets saw large upswings of residential competition of 14% or more with commercial switching over 50%. Just as Michigan capped customer choice to 10% other markets experienced downward pressure on prices through effective competition. Today Illinois, Ohio, and Pennsylvania have prices significantly lower than Michigan. Not only is the default Illinois utility price for customers who do not choose an alternative supplier lower than DTE and Consumers but, alternative supplier offers in the Illinois MISO service territory range from 10-18% savings off that already lower utility rate.[9]

Functioning Competitive Markets In Other States

Not only has switching increased now that markets have matured but the amount and types of products available in competitive states have increased. For residential customers there are pre-paid products that allow customers to pre-load an amount on their electricity account each month. In return the customer receives regular text messages alerting them to a decline in their balance. The customer can then change their usage pattern immediately – not 45 days later after they receive their utility bill. For commercial customers the products are endless. There remain the standard fixed budget offerings allowing an energy manager to come in under budget year after year. In addition, commercial customers have a variety of online tools that allow manufacturers to adjust production to times of the day where they can actually make money through demand response. Competitive offers can not only offer savings but can help turn a company's energy use into a revenue stream – a competitive advantage in today's economy.

While Michigan remains under a cap, the Public Utilities Commission of Ohio has issued orders which move the procurement of utility power out from under the utility into auctions from wholesale power providers resulting in much lower prices across the northern tier of the state[10]. In addition, two other Ohio utilities including AEP have filed to move to wholesale auctions for their default service. Illinois utilities no longer procure the power for their default service but instead this has been done through wholesale request for proposals for several years[11]. In fact, for commercial customers in Illinois there is no fixed default price they must choose a supplier or receive hourly market prices. Pennsylvania uses wholesale procurements for power and recently issued a tentative order including several items to

[9] www.pluginillinois.org Ameren residential offers as of October 30, 2011
[10] PUCO Case # 10-1284-EL-UNC
[11] PUCO Case # 11-0346-EL-SSO and 11-3549-EL-SSO

move customers into choosing a retail supplier[12]. As the states around Michigan focus on competition their energy prices continue to decline.

Michigan Residents Favor Competition; Competition is Healthy for the Economy

In statewide polls taken in both the fall of 2010 and summer of 2011, 79 and 75 percent, respectively, of Michigan residents said homeowners and businesses should be able to select their electric company, just as they choose their telecommunications and natural gas providers and current state law should change.

Because competitive electric markets are the best way to keep prices as low as possible, such markets also provide the greatest opportunity for economic growth and job creation.

When electric choice is offered, business response is immediate and robust. Competitive electricity markets lower costs overall and give consumers the flexibility to choose an electricity supplier to attain the lowest costs possible. Increasing the cap on competition with allow consumers to have access to numerous retail power suppliers who offer pricing options that vary with respect to contract term, price, risk, and other factors. Consumers can choose renewable and alternative energy products or choose energy efficiency, demand response, or other unique products and services.

Unequal access to retail competition makes some Michigan businesses more competitive against other Michigan businesses. Michigan's political leaders should not be in the position of picking winners and losers based on which businesses were lucky enough to get competitive electricity under the current 10% cap.

A broad range of customers will benefit from raising the cap on competition. Raising the cap will provide a greater number of businesses, consumers and local units of government with a choice in their electric supplier and the opportunity to enjoy lower costs for electricity.

Finally, increasing the cap on electric competition will ultimately improve utility efficiencies, accountability and customer service, just as competition does for every other Michigan business.

Michigan Electric Consumers Demonstrating A Desire To Obtain Competitive Service

As part of the process to implement the cap, the PSC was charged with developing a process and procedure to handle the situation where the cap gets reached and there are customers that wish to take advantage of customer choice and competition in the event that space became available under the cap. In a collaborative fashion with the AESs, the PSC Staff, and the utilities, a detailed queuing process was developed and approved by the PSC.

In order for a customer to put themselves in the queue, they must acknowledge via Affidavit that they have entered into a contract with an AES to take service. As of October 31st, 5587 customers have put themselves in the queue. Due to the numerous steps required under the PSC's rules to place a customer in the queue, including the requirement to enter into a legal contract, the number of customers that are likely interested in customer choice and competition is undoubtedly much, much higher.

[12] PA PUC Case# I-2011-2237952

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The reason for customer interest is not just about having a choice but also an economic one as customers understand what type of savings propositions are available in the competitive market compared to the rates of DTE and Consumers. While potential savings opportunities depend upon individual customer usage and the offers that an AES may provide, there exists today upwards of 20% savings for customers.

These savings opportunities are not limited to just individual customers as our experience is that in competitive markets, a number of business and trade associations have gotten directly involved in the competitive market by offering Affinity programs for the members of groups. One model is that these organizations aggregate the load of their membership and seek a "preferred supplier" relationship that can take many different forms and structures. In Illinois, the Illinois Manufacturers Association has held a highly successful program and relationship with my company Constellation Energy that has been mutually beneficial to both organizations. In Ohio, organizations like the Ohio Manufacturers Association, Ohio Hotel and Lodging Association, and Building Owners and Managers Association of Cleveland are just an example of a few organizations that have successfully implemented such programs. Here in Michigan, a number of schools have organized and developed such different programs to achieve savings opportunities for the members of such groups or organizations.

What Will You Hear Today From the Utilities and Their Allies?

I am sure that you will hear many things from the Utilities today as their arguments continue to change. No longer do you hear them promising to build power plants. No longer do you hear them assuring you that the cap would never be hit and if so it would take years. We all know that those promises made to this body back in 2008 simply were not true. There are no plans to build power plants and the Utilities have told the PSC so. The cap was hit in 9 and 12 months respectively. Please be very mindful of what assertions you will hear today as their past promises that were made to this Committee (and the entire Legislature) never materialized.

One of the new arguments that the Utilities have conjured up include calling companies like Constellation, Direct Energy, GDF Suez, Integrys Energy, Exelon, Glacial, FirstEnergy Solutions, Noble Americas, and other AESs carpet baggers. Out of state businesses that will just cherry pick customers. This is really a laughable proposition. We have local offices, employ Michiganders with high quality jobs, and pay taxes to the State. We are major corporations, Fortune 200 and 500 companies, serving millions of customers nationwide. In Michigan, we serving thousands of customers, many of us since the advent of competition and restructuring. We are extremely interested in providing Michigan customers of all sizes with competitive options and the opportunity to save money on their electric bills. DTE does not get greeted with such hostility and opposition from utilities in the various other States like Illinois, Ohio, Pennsylvania, and others when it chooses to compete there. Can you imagine if Michigan had policies that deterred other major automakers from establishing Michigan as a place to do business?

Another new argument is that lifting or expanding the cap on competition will cause rates to rise for full service utility customers. While we have not seen any facts from the Utilities and their allies to back up this scare tactic, the experience in competitive markets demonstrates the exact opposite. Competition and customer choice results in substantial cost savings of fuel, purchased power, and transmission for utilities, and these savings would offset any purported increase in costs to other customers. Further, sales transferring to retail competition are no more harmful than reduced sales due to energy conservation programs that the utilities have so highly praised in these Senate hearings.

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What Should be Done?

Michigan is again at the same point it was back when Governor Engler examined Michigan's competiveness during the 1990s. And once again energy costs are among the major disincentives to locating and growing a business in Michigan. In addition to businesses, local units of government and educational institutions are facing increasing needs in an environment of limited resources. Money spent on energy rate increases reduces funds available for police, fire protection and critical infrastructure.

Michigan business coalitions, such as Energy Choice Now, the Customer Choice Coalition and many other Michigan businesses believes that the *fundamental solution* to the problem of getting lower electric prices for Michigan businesses is to *eliminate the cap on Electric Choice*.

We believe that the 10% cap on electric competition and customer choice severely impedes Michigan's competitiveness and should be eliminated. Raising the cap on competition will make Michigan more competitive among the states. The creation and preservation of jobs and retention of businesses within the state, obviously a top priority, can only be accomplished with non-discriminatory access to competitively priced electricity.

Electric Choice results in substantial costs savings of fuel, purchased power, and transmission for utilities, and these savings virtually offset any increase in costs to other customers. Further, sales transferring to Electric Choice are no more harmful than reduced sales due to energy conservation programs that the utilities have so highly praised in these Senate hearings.

Competition drives innovation, efficiencies, and lower prices. Michigan policy makers need to unleash the power of competition by eliminating or raising the cap on Electric Choice.

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Figure 1. Percentage of Non-Residential Customers Taking Competitive Supply

(2003-Current Year) and Current Market Size (TWh) for the Top Non-residential Markets (>10 TWh)

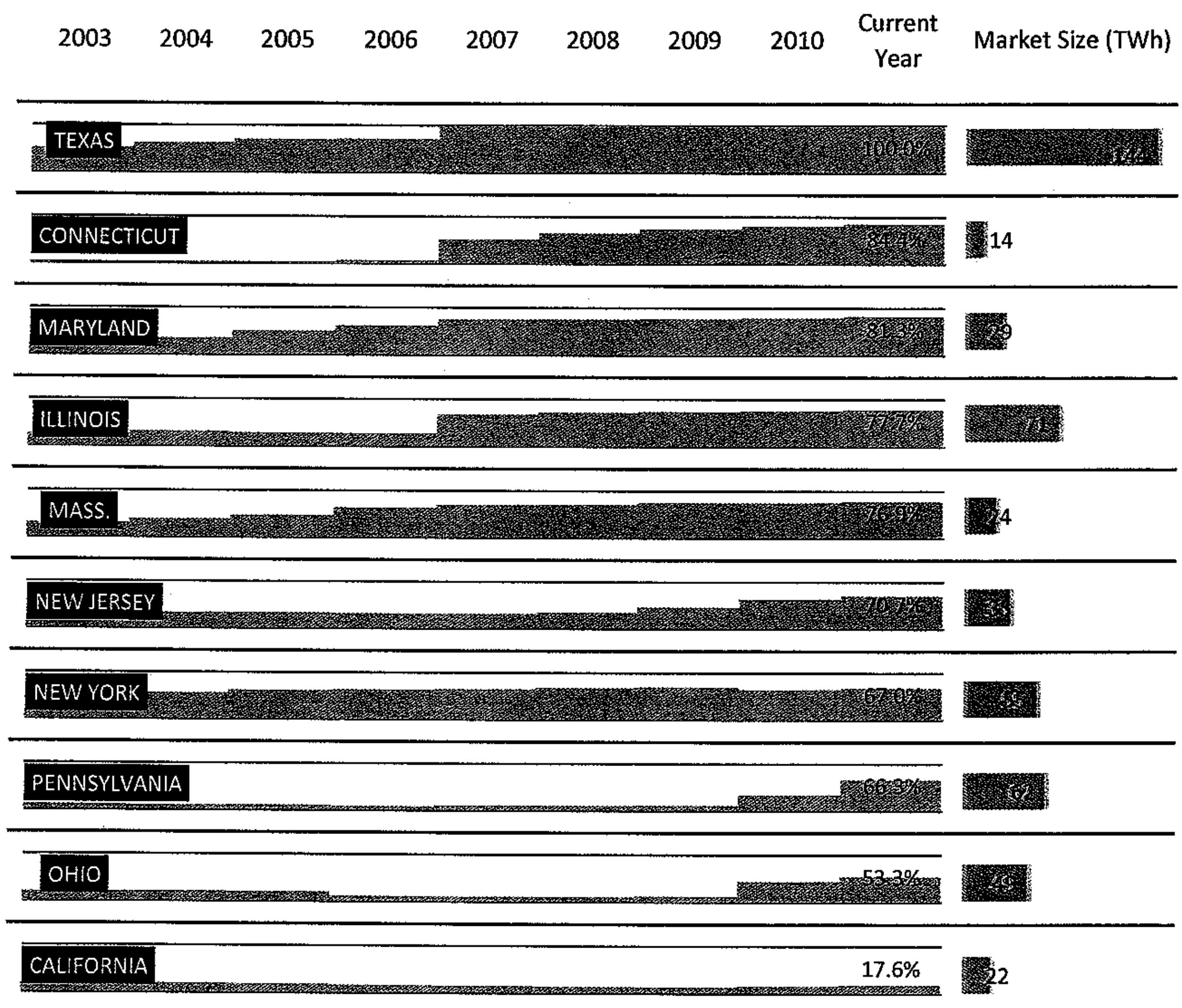

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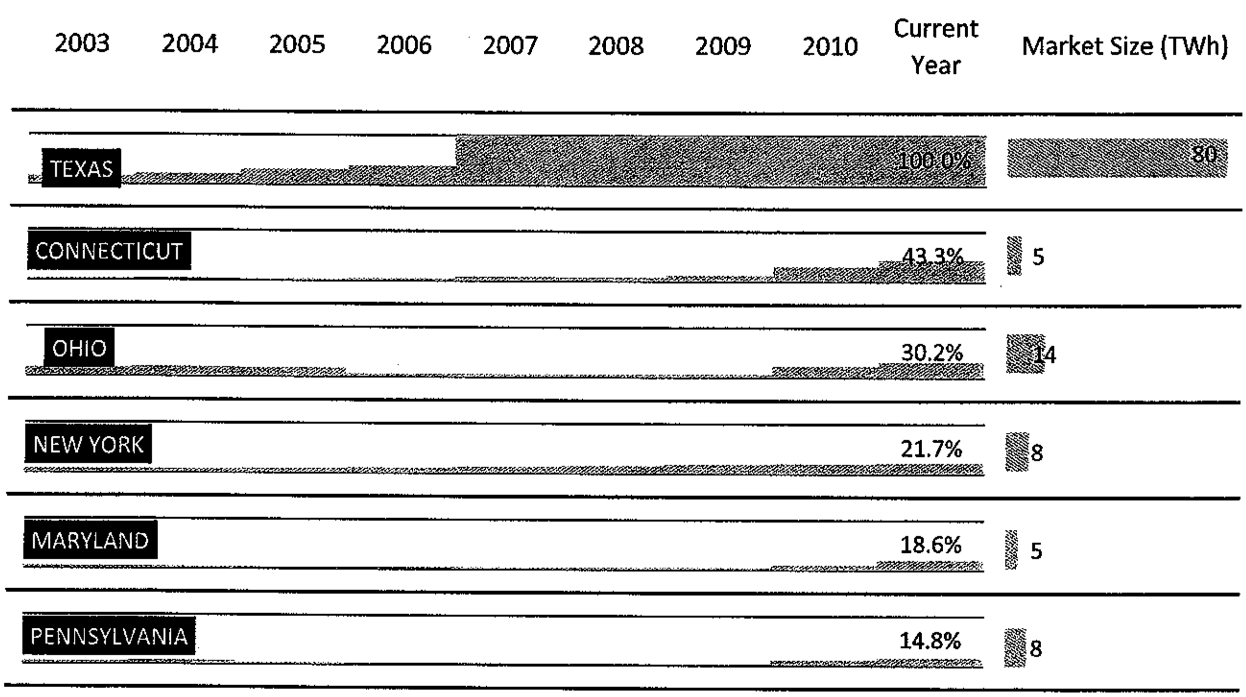
Figure 2. Percentage of Non-Residential Customers Taking Competitive Supply

(2003-Current Year) and Current Market Size (TWh) for the Top Residential Markets (>5 TWh)



Myths and Facts

1. **Isn't the 10% Cap needed to allow utilities to get financing for new generating plants?**

- No. It is the grant of a "certificate of necessity" by the MPSC under PA286 that guarantees utility recovery of new project costs through rate making and thereby provides the necessary assurance to those financing the investment----not the 10% cap.
- The "certificate of necessity" provision is not being changed.
- A utility should match its future generating supply requirements to the customers it expects to serve and should not attempt to lock in a customer base to the generation it wants to build.
- Because of the capacity requirement instituted by the Midwest ISO in 2009 (see #2 below) any supplier – utility or competitive supplier – need provide generating capacity only for the customers it expects to serve.

2. **Utilities argue that a low Cap is needed to protect utilities from too many customers leaving and then returning to utility service if competitive prices are too high. Utilities claim they must have generation available to serve these returning customers.**

The utility arguments no longer make sense.

- The "returning customer" argument may have been plausible when PA286 was enacted in October of 2008, but it is now obsolete.
- Since June of 2009, the Midwest ISO requires <u>all</u> suppliers – both utility and competitive – to provide capacity including reserves to serve their loads. If a customer leaves one supplier to take service from another, that *frees up* the former's capacity, which becomes available on the market to be purchased by the new supplier. We are all part of a large "pool" of power available to all customers in the Midwest ISO.
- Consequently, if customers change suppliers, whether utility or competitive suppliers, it has no effect on regional reliability or on the market cost of capacity to serve those customers.
- Rules have been in place for several years requiring customers returning to utility service to give adequate notice and requiring them to remain for at least a year so that the utility is not financially harmed. A customer who fails these requirements is charged a market rate, which is financially neutral to the utility. These rules have worked well to protect the utility, and therefore no additional restrictions on a customer's choice of supplier are needed.

3. **Some assert that customers who leave the utility for Electric Choice are not paying their fair share for the generation plants built to serve them.**

Under the provisions of PA 141, utilities have already received ample compensation for opening up full Electric Choice.

- Under PA 141 of 2000, the legislature provided generous support for utilities to transition to a competitive market. This included securitizing over $2 billion in utility assets through a 15 year bond issue paid by rate payers and the award of more than $100 million in stranded costs.
- The MPSC determined in 2007 that Consumers and DTE had fully recovered all stranded costs.

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- All customers – both utility and Electric Choice – continue to pay a monthly securitization charge on their utility bill to pay for the $2B in securitization bonds (through 2015) for Consumers and DTE, but the Electric Choice program is now limited to only 10% under PA 286. That's what is not "fair."

- Further, although Electric Choice customers pay securitization charges for utility generating plants, they receive no benefit from these plants, either capacity or low-cost energy. Consequently, Electric Choice customers are subsidizing full-service utility customers.

4. **Another argument is that a cap is needed because if customers leave the utility for Electric Choice, the utility will have excess generation but not be able to collect for it.**

- Neither Consumers Energy nor Detroit Edison has any excess generation. Both buy expensive capacity in the summer months. Customers leaving for Electric Choice actually *reduce* the amount of summer capacity that the utilities must purchase—thereby reducing utility costs and resulting in a lower PSCR for existing customers.
- Any excess capacity can be sold into the marketplace.
- Testimony in both Detroit Edison and Consumers Energy cases has demonstrated that when customers move to Electric Choice, the utility reaps savings that are approximately equal to, and in some instances exceed, the utility's reduced revenue.[13] Thus, remaining utility customers are not harmed by Electric Choice.

5. **What about the future? Does not Michigan need to build new in-state generation to meet its future power requirements, replace aging plants and generate new jobs? Is not the 10% Cap needed so that utilities can build new generation for reliability in Michigan?**

A cap on Electric Choice is not needed to facilitate new supplies of electric power. Consider the following:

- Whether a new power plant is necessary or prudent is determined by the MPSC under the *"certificate of necessity"* process under PA 286. It has nothing to do with the 10% cap.
- Michigan's electric power demand is shrinking, not expanding, due to lower demand and energy efficiency measures.
- As the result of the pending enactment of PA 286, a major 750 MW independent power plant project (LS Power) was cancelled in 2008.
- With the Governor's Executive Directive (E.D. #2009-2) on new coal-fired plants and under the terms of the proposed MDNRE air permit, Consumers Energy would be required to shut down over 900 MW of existing plant capacity in order to build 850 MW of new capacity—a net loss in base load capacity. This will result in higher costs for new plants, shuttering low cost plants before the end of their useful life, higher depreciation costs for rate payers, and the layoff of workers at Consumers' facilities----not to mention the loss of significant local tax revenue for cities in which the facilities will be closed (e.g. Muskegon).
- Between the enactment of PA 141 in 2000 and PA 286 in 2008 – a period of uncapped Electric Choice – over 4,000 MW of new generation was built in Michigan. None of this was built by a regulated utility. This demonstrates that a cap on Electric Choice is not required for generation to be built in Michigan.

[13] Detroit Edison general rate case U-16472, testimony on behalf of Energy Michigan and Exhibits EM-2, EM-3, and EM-4. Consumers Energy Revenue Decoupling Mechanism case U-16566, testimony on behalf of Energy Michigan and Exhibits EM-2 and EM-3.

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