

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE COMMISSION S) CASE NO. GNR-E-96-1
INVESTIGATION INTO CHANGES)
OCCURRING IN THE ELECTRIC INDUSTRY.) ORDER NO. 26555
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BACKGROUND

On January 30, 1996, this Commission issued a Notice of Inquiry and Order No. 26312 initiating an investigation into changes occurring in the electric industry. Subsequent to the issuance of the Notice/Order, a series of workshops was conducted by the Commission Staff involving numerous groups having a stake in the future of Idaho s electric industry, including this state s three investor-owned utilities as well as non-regulated electric suppliers such as municipal corporations, cooperatives, independent power producers and out of state, investor-owned utilities. Other participants included representatives from various customer classes, large industrial customers and a low income/conservation group.

The purpose of the workshops was to identify issues facing Idaho s electric utilities and their customers related to the nationwide transformation of the electric industry to a more competitive environment. The workshops were further intended to assist the Commission in defining its own role relative to the changing industry and to provide it with information critical in its continued effort to ensure that all of Idaho s electric consumers continue to receive quality service at reasonable rates.

Pursuant to the Commission s directive, a voluntary working group consisting of interested stakeholders was formed to draft a position paper outlining the issues facing the industry and providing a summary of the various stakeholders perspectives on those issues with specific recommendations for the Commission regarding the future regulation of electric utilities in Idaho. That position paper, titled Report on Changes Affecting the Electric Utility Industry, was filed with the Commission on May 28, 1996 and is attached to this Order as Appendix A. The paper is a nonbinding document that reflects the perspectives and efforts of many different groups and individuals. The Commission has reviewed the position paper and, after due consideration of the matter, issues the following findings.

FINDINGS

We wish to commend the working group and all those who participated in this proceeding for the exemplary work performed. The position paper reflects considerable initiative and effort and has provided this Commission with valuable insight into the landmark evolution occurring within the industry.

Because of the speed at which change is taking place, any attempt to summarize the state of the industry is, at best, a snapshot in time. Moreover, the forces that are creating that change are many and varied, from policy decisions made by the Federal Energy Regulatory Commission (FERC) to the choices of individual consumers. Suffice it to say that change within the industry is occurring and will continue to occur regardless of the will or desire of any individual or organization. Nonetheless, it is the duty of this Commission to exercise its statutory authority in an effort to shape the future of the industry so that all customers of Idaho's regulated electric utilities continue to receive high quality service at reasonable rates. In this regard, the efforts of the working group and the deliberation resulting from this proceeding will prove valuable in our decision making as the future unfolds.

In the meantime, we have made some general observations and conclusions regarding the state of the industry and the course this Commission must take in response to the changes occurring. First, we expect that the electric industry as a whole will continue to experience a transformation toward free market principles. Recent developments that helped to bring about this paradigm shift include improved thermal generation technologies, low natural gas prices and actions taken by the FERC. In addition, regulatory agencies in other states such as California have addressed problems related to high-cost utilities and the demands of large customers who believe they can obtain more favorable rates from suppliers other than their current utilities.

Although terms such as competition and retail wheeling are generally used to describe the evolution taking place in the industry, it is not always clear what they mean. For the purpose of our analysis, we presume that the deregulation or opening up of Idaho's distribution system is not feasible or desirable at this time. When we use the term competition or any of its mutations, therefore, we are referring to the possibility that customers of Idaho's regulated electric utilities may, in some form or another, have the option of selecting an energy supplier other than their current utility, but not a new supplier of distribution lines.

As discussed below, we have concerns regarding the effect that competition, regardless of how it is defined, will have on the majority of Idaho's ratepayers. Notwithstanding those concerns, this Commission has demonstrated time and again that it is not opposed to change so long as it is in the best interest of Idaho's citizens. For instance, in Case No. IPC-E-95-11, the Commission adopted a new regulatory regime for Idaho Power in which the Company would be allowed to accelerate the amortization of deferred income tax credits in years of poor financial performance but would share earnings with customers in highly profitable years. This constituted a departure from traditional ratemaking and is an example of our willingness to explore alternative forms of regulation that serve the needs of both utilities and their customers.

We are convinced that we should be cautious, however, with respect to an outright deregulation of Idaho's electric markets for several reasons. First, customers of Idaho's regulated

electric utilities, on the average, currently pay some of the lowest electric rates in the nation. While some of Idaho's larger customers may be able to obtain lower rates through contract sales with other energy suppliers due to their size and buying power, we find that there is evidence suggesting that the majority of Idaho's ratepayers may experience an increase in rates over the long term. This is simply because, region-wide, and on the average, rates for comparable services outside Idaho are higher. Thus, in a completely free market, Idaho's regulated utilities could find customers in other states who are willing to pay rates that are considerably higher than those currently paid by Idaho consumers. Without adequate oversight, Idaho customers could be required to compete with others for low cost hydroelectricity produced now for the benefit of Idaho customers. Under such a scenario, smaller customers could see their electric rates increase as a result of competition.

Another matter of concern to this Commission is the possibility that a full or partial deregulation of the electric utility industry may result in the diminution of the quality of service Idaho's ratepayers currently enjoy. In addition, the recent power outages experienced throughout the western United States serve as a reminder of our dependence on electricity and the importance of maintaining reliability in the delivery of electric service to customers. As the industry transforms, we are keenly interested in exploring possible mechanisms that will ensure that reliability.

There is also the concern that deregulation may advantage a select few customers at the expense of the majority. That is, larger customers who make desirable targets for outside suppliers may be able to obtain advantageous rates. Smaller residential customers, however, clearly do not possess the buying power of a large industrial user and may ultimately pay relatively higher rates. This result may be exacerbated by the fact that once larger customers leave the host system for their source of supply, the fixed, generation-related costs of that host supplier may be required to be spread over fewer customers thereby increasing their rates.

In light of the foregoing, it is the conclusion of this Commission that the deregulation of Idaho's electric utilities, without some form of Commission oversight, is not in the best interests of the general body of Idaho's electric utility ratepayers. This declaration should not discourage our regulated utilities from making innovative proposals that are free-market based and in the best interests of all ratepayers. We believe, however, that it would be unwise at this time to simply let unrestrained market forces dictate price and terms.

It is neither the desire nor intent of this Commission to act as an impediment to the transformation to competitive ideals. Considering Idaho's unique position in the industry and taking into consideration the best interests of all Idaho ratepayers, we do not believe that it is our role to actively attempt to bring about the deregulation of the electric industry in this state. Rather, we believe that the interests of Idaho's ratepayers would best be served if this Commission serves as a facilitator and resource of information in the policy debates that industry transformation has or will engender at all

levels including the legislature of this state. We do encourage utilities and other interested groups to continue making innovative proposals, however, as the industry continues to transform so that the needs of all of Idaho's ratepayers are addressed.

We note that there is currently pending before this Commission Case No. WWP-E-96-2, in which the Washington Water Power Company has proposed an experimental tariff that gives Water Power's Schedule 25 (larger) customers the option of obtaining service from a third party supplier to serve a small portion of their loads over a limited term. Regardless of how we ultimately rule on Water Power's application, this is an example of the case by case manner in which this Commission will be presented with and expects to resolve specific, restructuring related issues.

The Position Paper presented by the working group in this proceeding contains eleven specific recommendations regarding action that could be taken by this Commission, its Staff or some combination of entities. We will now respond to each of those recommendations.

Recommendation No. 1: Examine restructuring from a regional perspective.

The Position Paper proposes that the Commission Staff review and report on restructuring activities in the region and that the Commission develop policies that will allow Idaho the opportunity to remain a full participant in the regional energy market.

We note that Staff has been monitoring restructuring developments in other states and this Commission has and will continue to be involved in the regional review process. While our jurisdiction lies solely within the boundaries of this state, the electric grids to which our utilities are connected go beyond state boundaries. A regional awareness and cooperation is ultimately in the best interests of Idaho's electric customers. Policies that allow this state's utilities to remain competitive and take advantage of opportunities within the region will, ultimately, inure to the benefit of citizens.

Recommendation No. 2: Examine adoption of service quality standards.

The Paper proposes that the Commission direct a study on current customer service standards and actual results and suggests state legislation clarifying the Commission's ability to monitor and enforce performance standards.

We note that Title 61 of the Idaho Code already vests this Commission with considerable latitude to establish and enforce service quality standards. We are concerned, however, that as the industry becomes more competitive, utilities may place less emphasis on service quality. The temptation to improve short-term financial results through personnel reductions, thereby reducing service quality, has been observed in other industries. Without regulatory oversight, this is a distinct possibility in the electric industry. While we do not believe it is necessary at this time to develop service quality standards or to seek legislation clarifying Commission authority, we want to make it clear that customer service is of the utmost importance and we are prepared to take action if utilities' performance in this area begins to deteriorate.

Recommendation No. 3: Examine customer relations policies.

The Paper suggests that current policies and rules be revised in light of the transition toward competition and that there be possible legislation strengthening customer protection.

We believe that issues relevant to customer relations are integrated with those related to service quality. The degree to which service quality and customer relations will be affected by competition depends, of course, on the extent and manner in which deregulation occurs within the industry. As the industry evolves, so too must this Commission's role in ensuring that customers receive the highest overall quality of service possible and that customers are treated fairly and without discrimination.

Recommendation No. 4: Consider legislation for consumer protection in a deregulated environment.

The Paper proposes that legislation could be introduced in the upcoming session emphasizing the Commission's role as mediator/arbitrator of consumer-utility disputes with the authority to impose sanctions where necessary and to establish standards for the public safety, convenience and necessity.

There is some degree of overlap between this recommendation and the several preceding it. The Commission is already vested with the authority to resolve disputes between public utilities and their customers. In fact, this is one of Staff's daily functions. Furthermore, the current statutory regime provides the Commission with the power to do all things necessary to ensure the public safety, convenience and necessity with respect to the operation of utilities. Whether any additional legislation or changes to the existing statutory structure are needed depends entirely upon how the industry evolves and whether legislation is proposed which would affect the Commission's jurisdiction or the manner in which it regulates public utilities. Regardless of what changes ultimately befall the industry, this Commission will staunchly advocate its continued role as a protector of the interests of public utility consumers.

As a further matter, we believe that even in the event that Idaho's electric customers are ultimately given the option of choosing between competing suppliers, this Commission should continue to be vested with the authority to ensure that those suppliers meet certain threshold criteria regarding their ability to provide safe and reliable electric service.

Recommendation No. 5: Seek agreement on DSM, previous commitments to PURPA, etc.

The Paper suggests that alternative funding mechanisms could be established for new DSM programs and the costs recovered through transition rates where appropriate.

As the industry moves toward open market principles, the manner in which conservation and PURPA related projects will be initiated and treated for cost recovery will need to change. This will require innovation on the part of utilities, this Commission and other interested parties. We believe

thatThe policy decision of funding for public purposes such as DSM, environmental protection, etc, is one that should be debated. The resolution of this issue may require legislative action.

Recommendation No. 6: Examine stranded cost magnitude and treatment.

The Paper suggests that the Commission identify each utility s relative exposure with utility by utility filings including a proposal for recovering those assets that are stranded.

We do not intend, at this time, to initiate a generic examination of stranded costs. If and when this becomes of sufficient concern to each of the regulated utilities, they may seek specific action from this Commission.

Recommendation No. 7: Consider expansion of service options to customers.

This is the very definition of the benefits that many believe competition will bring to the electric industry. Although we have previously expressed concern over some of the consequences also attendant to competition we fully expect Idaho s regulated electric utilities to remain innovative in offering their customers meaningful choices with regard to service and to bring proposals such as a read your own meter rate, as suggested by one utility, before the Commission to give customers better service and reduce costs.

Recommendation No. 8: Pursue pricing flexibility.

To the extent this recommendation relates to the specific needs of individual customers or customer classes, our position is set forth in response to Recommendation No. 7. Regarding alternative ratemaking, we strongly encourage the utilities to offer proposals in lieu of general rate increases, such as the recent Idaho Power proposal to accelerate the amortization of deferred tax credits, and to look for opportunities to use reductions in other expenses to offset the write-down of regulatory assets.

In a somewhat related matter, we note that if Idaho s investor-owned utilities are to be deregulated, it will be necessary for them to itemize their billings, segregating the costs of their various functions such as generation, transmission, distribution, etc.

Recommendation No. 9: Explore provision of competitive service.

The Paper proposes that the Commission continue to allow special contracts for larger customers and that it explore the use of alternative tariffs for others.

We can see no reason to discontinue our policy of allowing special contracts for larger customers due to their size and the unusual characteristics of their respective loads. We are supportive of any type of pricing that is responsive to customer needs so long as the net revenues collected from those customers are fair and do not place an undue burden on other customers. Again, we encourage the utilities to be creative in this regard.

Recommendation No. 10: Develop market-based mechanisms that will ensure all customers have the opportunity to participate in greater levels of competition if they so choose.

The point of this recommendation seems to be that to the extent some aspect of the industry

is deregulated, that all customers have the opportunity to compete for favorable rates and/or service.

We agree wholeheartedly. Large customers must not be allowed opportunities that are not available to small customers, under the guise of competition. Restructuring should be accomplished in a manner that allows the economic efficiencies of a competitive market to benefit all customers and not just a select few.

Recommendation No. 11: Re-examine the Electric Supplier Stabilization Act.

This Act consists of the operative statutes which provide public utilities with their monopoly status. Thus, in all practicality, the Act must be re-examined before any form of deregulation can take place. First, the Act should be clarified to provide exclusivity only in the provision of distribution lines, not the supply of energy.

It is also our opinion that the Act should be revised to vest this Commission with the explicit authority to determine if, when and how deregulation of investor owned electric utilities occurs. Without such authority, it may be very difficult for us to respond to a rapidly changing industry requiring flexibility and innovation. Further, we believe that the Act should be revised to outline a process for consideration of this issue with respect to the service territories of non-public utility suppliers, such as municipal corporations and cooperatives.

We know that disputes between regulated utilities and municipals or cooperatives involving the provision of distribution services to customers have been litigated under this Act. As the industry is restructured, the method of resolving those disputes should be examined to determine if the current process is optimal. Another alternative could be to revise the Act to vest this Commission with authority to establish geographical boundaries between the respective service territories of distribution providers. This would require the Commission issue certificates to municipals and cooperatives for the limited purpose of defining their exclusive distribution areas.

In proposing the foregoing changes to the Act we do not suggest that the existing authority of municipals to annex areas and acquire service territory or customers be altered. Furthermore, we are not suggesting that this Commission be given the authority to set rates for or regulate the operations of municipals or cooperatives.

ORDER

IT IS HEREBY ORDERED THAT the Commission's investigation in this matter having been completed, this proceeding is hereby closed consistent with the terms and conditions set forth herein.

THIS IS A FINAL ORDER. Any person interested in this Order (or in issues finally decided by this Order) or in interlocutory Orders previously issued in this Case No. GNR-E-96-1 may petition for reconsideration within twenty-one (21) days of the service date of this Order with

regard to any matter decided in this Order or in interlocutory Orders previously issued in this Case No. GNR-E-96-1 . Within seven (7) days after any person has petitioned for reconsideration, any other person may cross-petition for reconsideration. See *Idaho Code* 61-626.

DONE by Order of the Idaho Public Utilities Commission at Boise, Idaho this day of August 1996.

RALPH NELSON, PRESIDENT

MARSHA H. SMITH, COMMISSIONER

DENNIS S. HANSEN, COMMISSIONER

ATTEST:

Myrna J. Walters
Commission Secretary

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