ELECTRIC UTILITY Deregulation
1997 Warren M. Anderson Legislative Breakfast Seminar Series

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Ford Motor Company

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NYS Senate Energy & Telecommunications Committee

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Hon. Paul Tonko
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WARREN M. ANDERSON

Warren M. Anderson is a distinguished alumnus of Albany Law School and an active member of the Government Law Center Advisory Board. Having served in the New York State Senate for thirty-five years, he is perhaps best known for his leadership during his tenure as President Pro Tem and Majority Leader from 1973 to 1988.

Warren Anderson began his legal career as an Assistant County Attorney in Broome. He then joined the law firm of Hinman, Howard & Kattell where he is currently practicing law. Throughout his career he has received numerous honors and awards.

PROGRAM DESCRIPTION

In furtherance of its mission to serve as a resource to all levels of government in the resolution of specific problems, the Government Law Center is pleased to present the seventh annual Warren M. Anderson Breakfast Seminar Series. Monthly breakfast programs feature experts addressing the legal aspects of a variety of policy issues pending before the Legislature. The seminars are designed to provide access to current legal information on a given topic. The Government Law Center welcomes your suggestions for future programs.
1997 HONORARY CO-HOSTS

The Government Law Center is grateful to the Leadership of the New York State Senate and Assembly for serving as honorary co-hosts of the 1997 Series:

Honorable Joseph L. Bruno  
*Senate Majority Leader*

Honorable Sheldon Silver  
*Speaker of the NYS Assembly*

Honorable Martin Connor  
*Senate Minority Leader*

Honorable Thomas M. Reynolds  
*Assembly Minority Leader*
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PATRICIA E. SALKIN, ESQ.
Director
Government Law Center

The Government Law Center was established at Albany Law School in 1978 with a three-fold mission: to allow disciplinary studies and research in government and the problems facing government, to introduce law students to the government policy analysis and to public service, and to serve as a resource for government of all levels in the resolutions of specific problems. It is this last objective that inspired us to create The Warren M. Anderson Legislative Breakfast Seminar Series. The program is named in honor of the distinguished alumnus of the New York State Senate and a special member of the Albany Law School community.

Albany Law School and Senator Anderson are honored that this year the legislative leadership agreed to serve as honorary co-hosts for the Series. We wish to thank Senator Bruno, Speaker Silver, Senator Connor, and Assemblyman Reynolds for lending their names to this non-partisan educational effort. I also want to thank the program sponsors. Without their continued support and assistance, the program would not be possible. They are: the Civil Service Employees Association; The Energy Association of New York State; Gibney, Anthony & Flaherty; Hinman, Straub, Pigors & Manning; MCI Telecommunications; The New York State Association of Architects; the New York Stock Exchange; Niagara Mohawk Power Corporation; Philip Morris Management Corporation; and Wilson, Eiser, Moskowitz, Edelman & Dicker. Our appreciation also to each of the outstanding panelists who participated in the Series.

We are pleased to make the 1997 Anderson Series available through this publication. The seminars address the following issues which legislators and other policymakers are currently facing in New York State and around the country: cameras in the courtroom, electric utility deregulation, real property tax reform, and the right to die.
To reach an even wider audience, the final program on physician-assisted suicide was professionally videotaped for broadcast to legislators through New York Network's "The Capital Channel" and to the community via local cable stations across the State.

The Government Law Center plans to once again host the Series during the 1998 Legislative Session for the benefit of policymakers and the citizens of New York State. We hope you will join us.
ELECTRIC UTILITY Deregulation
February 26, 1997

Panelists

John Bozzella
Northeast Regional Manager
Ford Motor Company

It is certainly an honor and a privilege to meet with several important policy makers, legislators, regulators, and other experts on this topic.

I'm an industrial customer. I hope to be the voice of the customers, at least the large industrial customers today. The primary issue for us is competitive prices—prices that are competitive with utilities supplying our plants across the country and our competitors' plants.

What does it mean to compete? I want to talk about competition the way we understand it at Ford Motor Company. We compete on several different levels. On the most obvious level, our products compete against other products—locally, nationally and around the world. We're a global company and must compete with other global car manufacturers. Anyone here who has purchased a car recently knows that we, in the domestic industry, have learned a lot about competition in the last twenty or twenty-five years. Simply put, as large customers of electricity and the manufacturing process, we need a reliable supply of electricity at the lowest possible cost. That's pretty basic.

We also compete internally. This may not be as apparent to people outside the auto industry. Our plants compete with outside suppliers and with each other for work. We have a large stamping plant in Buffalo. (A stamping plant is were huge rolls of sheet metal are made into panels, body panels and other car parts.) It's a main and basically, final, supplier of assembly plants. Everything that
leaves the Buffalo stamping plant goes to a final stamping plant. When the Buffalo stamping plant competes, they've got to actually bid for work against other plants. For example, there's another stamping plant--Woodhaven Stamping--in Michigan which is very similar to the Buffalo Stamping Plant. They both have roughly 2.5 million square feet under one roof and employ about 2,300-2,400 people. They represent two of the best stamping plants in our fleet. Interestingly, the Woodhaven stamping plant pays about 35% less for their electricity than the Buffalo Stamping plant. Every time the plant manager at Buffalo bids on a part, he is competing with Woodhaven. When you look at what that will cost in terms of electricity, it is 2.2 million dollars a year. There is, therefore, a 2.2 million dollar a year cost penalty on the Buffalo Stamping Plant solely attributable to the price of electricity.

There aren't really any major differences between the plants. Labor is controlled nationally by a national contract. While the Woodhaven stamping plant is much closer to some of the assembly plants (making shipping costs more expensive for Buffalo), Buffalo is a much more efficient plant in many other ways. Thus, the comparison is an appropriate one. We must keep the focus on the fact that there is an enormous cost penalty for doing business because of energy.

The Chicago Stamping plant is another example. They have five huge, very technically-automated and expensive presses. We have one of those presses in Buffalo. The only way to get another press is to get new work.

How do we get to competitive prices? The only way is through retail competition. Frankly, I'm not optimistic about New York's ability to move to a more competitive environment quickly enough to stem any job losses. Keep in mind that we are losing jobs in New York this very minute. During the national recession, between July of 1990 and March of 1991, we lost 272,000 jobs in that period alone. We continue to lose jobs. In manufacturing, in the late eighties and early nineties, we were losing 35,000 jobs a year.

We're doing much better now. In 1996, we only lost 18,000 jobs in the manufacturing sector. These are good jobs. The jobs that left, incidentally, were held by residential rate payers. We are talking about significant impact here in terms of jobs. We all recognize that it is a huge problem for our economy.
I'm concerned that we're not going to move to competition quickly enough. The Public Service Commission has ordered retail competition by 1998, but the utilities have sued and appealed and, frankly, that makes me very pessimistic. I am also concerned that even interim measures to keep manufacturing viable will be difficult to achieve. A bill to provide low-cost economic development power has languished in the State legislature. Companies like Ford Motor Company are looking every day at what's happening in New York and frankly we're not impressed with the State's ability to get to retail competition in a timely manner.

I look forward to hearing the other presentations today. Thank you for the opportunity to participate in this program.
RICHARD KING, ESQ.
Managing Attorney
Public Service Commission

My remarks this morning will address three matters. First, I will summarize the Public Service Commission's vision in the competitive opportunities case. I will then discuss how that vision is being translated into action today. Finally, I will briefly outline the major outstanding issues that are confronting the Commission.

The Commission's competitive opportunities decision of last May was the culmination of a broad-based inquiry into potential competitive benefits in the electric sector. The participants included all interested stakeholders, consumer groups, environmental groups, large industry, small commercial representatives, state and federal agencies, and legislators, etc. The opinion sets forth the Commission's architecture for the future. The Commission basically believes, as do many people, and this has been confirmed in many studies: that competition will lower electric rates. It will lead to increased customer choice, and spur innovation and new products and services. The Commission hopes to see vigorous wholesale competition in 1997 and retail competition beginning in 1998.

There is a pilot program under way with Orange and Rockland Utilities that's been under way since last year. The Commission expressed a preference for divestiture of utility generation assets to further competition in the generation sector and it identified further competitive opportunities that might be provided by energy service companies. The order rejected the public utilities' argument that they have a legal right to recover 100% of stranded costs; that is, costs that might not be recoverable in the competitive arena. As was noted, the utilities did appeal this case in court and the Supreme Court decision did affirm the Commission's decision. The opinion also stressed a need for continued maintenance of system reliability and customer service protections. The Commission directive also required five of the seven utilities (the two that were excluded were Long Island Lighting and Niagara Mohawk) to file rate and restructuring plans to address the Commission's vision.
In varying degrees, the utilities' submissions of October 1, 1996 respond to the Commission's concerns. All of these filings have been the subject of intensive settlement negotiations by interesting parties. Although the schedule for submitting settlements has been extended several times, we expect these discussions to be concluded in the coming days.

Concurrently, initiatives at the Federal Energy Regulatory Commission have resulted in additional competitive measures, including the open access tariffs for transmission services pursuant to the Order 888 decision of last April. Moreover the utilities and the New York Power Authority recently filed a proposal to establish an independent system operator which would basically operate the power pool system, the transmission grid, in a different way than it has been in the past. These measures should increase competition at the wholesale level.

Finally, there are numerous hurdles in our path toward total retail access competition. You undoubtedly heard the arguments about stranded costs. I'm sure that they will be discussed further today. Clearly we want these costs mitigated as much as possible and then ground rules established for recovery of authorized stranded costs.

Retail access itself poses many problems. How are the low target, load pocket and market power issues resolved? What pilot programs should be initiated first to debug the systems? How will new entrants be encouraged to participate and what standards should govern their participation? How do we ensure the benefits of competition are shared by all? These are complex technical issues and they will certainly be addressed in the coming days.

Finally, some regulatory reform is probably needed because the current apparatus was designed for a monopoly-type system, decades ago, and existing requirements may prove to be anachronisms in the near future.

Thank you.
The Public Utility Law Project represents low and fixed income residential customers on electric utility issues. Five minutes is a very short amount of time and as Dick’s talk indicated, the scope of this subject is enormous. This morning, I've decided to focus on one issue that you do not hear a great deal about in the electric debate and one that I would like everyone to focus on some more. It has to do with a law that has been on the books since 1981: the Home Energy Fair Practices Act. It is model legislation for the entire country. It is legislation that protects residential customers—that sets out most of the rights of the utility company and the obligations of the utility consumers. It deals with the right to obtain gas and electric service. It deals with protections against gas and electric shut-offs. It has provisions limiting the security deposits, provides the right to an affordable deferred payment plan and creates an emergency utility payment program that requires the state to pay when the family's only alternative is freezing in the dark.

The Home Energy Fair Practices Act has served us well. The occasional tragic death and frequent tales of suffering are no longer seasonal news stories that shamed us all as they did before the passage of the Act. If we have any sense of justice, the Home Energy Fair Practices Act need not become a victim of the introduction of competition in the electric industry. Today, more aware than ever of the imperfections of regulation, the regulators have become the loudest proponents of the power and the economic efficiency of the marketplace.

Regulators greet every criticism of electric power competition With the cry “the marketplace will take care of it.” In the name of competition, the Public Service Commission is ready to abandon the protections of the Home Energy Fair Practices Act. The Public Service Commission has become mesmerized by the theory of a competitive market and in the course of that has lost its sense of justice. More than that, in the pursuit of its mission to introduce competition to the electric industry, the Commission is allowing new entrants into the utility business to ignore the requirements of the Home Energy Fair Practices Act: the
law the legislature passed to protect residential customers.

This is what I consider to be the dark side of the competition:

- Competition as an excuse for the erosion of protections that were important to us all; competition as an excuse for eliminating consumer protections. The marketplace will not take care of that.

- Competition as an excuse for dismantling environmentally sensitive decisions on electric generation. The marketplace cannot take care of that.

- Competition as an excuse for eroding historic levels of privacy protection when the competitors share consumer credit information. Again, the marketplace itself will not take care of that.

- And competition as an excuse for allowing volatility in the marketplace to do harm to New Yorkers who are too poor to suffer the ups and downs of that marketplace. No, the marketplace cannot take care of that either.

In my opinion, the debate about restructuring the electric industry will end in the passage of a bill by this Legislature. If we look at California, Pennsylvania, and a number of other jurisdictions, I think the obvious lesson is that aggressive regulatory activity on utility restructuring and on competition, will inevitably lead to legislative reform and legislative action. Furthermore, the adoption of that legislation can, and hopefully will, ensure the continuation of environmental sensitivity, consumer protections, affordable rates for the poor, and the continuation of high service quality and system reliability. Thank you.
HON. JAMES L. SEWARD  
Chair  
NYS Senate Energy  
& Telecommunications Committee

I'm very pleased to be here this morning, particularly to participate in a breakfast seminar that is named for Senator Warren Anderson, because I recall very vividly January of 1987, as a freshman senator, being called to Senator Anderson's office, then Majority Leader Anderson, to discuss my committee assignment. And I'll never forget, he said "Jim, I've got a committee chairmanship for you that you can really sink your teeth into", and that was the Energy Committee. And my response was, "Andy, I can sink my teeth into it, but I can easily get my teeth knocked out as well." It has been a great ride during these last 11 sessions and it has become a very rapidly changing world, and increasingly so.

We've heard this morning already in terms of the economic climate in New York, what we need to do to improve our economic business climate in this state and the necessity for the improvements. We've made great strides, it seems to me, these last two years under the leadership of Governor Pataki, and like-minded legislators in both houses and both parties. Here in the Legislature, we've made great strides: tax cuts, regulatory reforms, workers' compensation reforms—the list goes on. But there is no question that there is a big nut that needs to be cracked here, and that is high electric rates and their negative impact on our economy and job creation in this state. That is why we are all here this morning, and I am sure our goal, shared by everyone on this panel regardless of other differences, is lower electric rates, and how do we get there.

I believe that ushering in an era of competition in the electric utility industry of this state is an important first step toward lower electric rates. It is insufficient alone. Competition alone will not do the job, but I think it is an important first step coupled with other measures as well: such as the renegotiation of the independent power contracts that the utilities had signed in the years prior to 1992, the "six-cent" law, and other changes. Those contracts are continuing to contribute to high electric rates in this state. They need to be
renegotiated, and there are a number of talks under way to do just that. We also need tax reform as it relates to our utilities. When you stop to think that approximately 20 cents of every dollar that we pay in our utility bill is taxes, we need to make changes there to get at the lower monthly rates. But the PSC Competitive Opportunities proceeding is, I believe, an important proceeding. The PSC is on what I call a fast track with wholesale competition expected this year and retail competition next year. Obviously there are a number of issues yet to be resolved at the PSC and I'm sure they will be, but this proceeding is ushering in a very dynamic new era in the State of New York and it is very important that we allow that to proceed. There are a number of things that I believe we should appropriately do in the Legislature to spur a transition to competition. I remain convinced that the real action should remain at the PSC because of the slowness of the legislative process to react to a rapidly changing world in the electric utility industry; I believe that the flexibility and the ability to handle particular situations exist at the PSC and that they should be taking the lead as they are. But there are a number of things we can do in the Legislature to help spur this whole process. For example, in the Senate, we have the Power for Prosperity legislation to form a partnership with the utilities and the State Power Authority to provide low cost power for businesses in our State over the next few years as we undergo the transition to competition.

There is the Electric Ratepayer Relief Act, the so called securitization bill, which will be the subject of a hearing one week from today in the Senate. We are going to be looking at the experiences in other states which have already done this and how we can have this concept relate here to New York State and provide lower electric rates for all classes of rate payers. But the bottom line from my point of view, and the Senate's point of view, is that with the combination of competition, and the renegotiation of the independent power contracts and tax reforms, we will achieve lower electric rates in the State.
HOWARD SHAPIRO
President
The Energy Association of New York State

Some might say here I am again representing the electric utility industry between a rock and a hard place, Assemblyman Tonko and Senator Seward. I prefer to think of myself as fortunate to deal with two very thoughtful and intelligent energy committee chairmen who have a very difficult issue to address --as do we all. Five minutes is hardly enough time to introduce this subject and I realized as I was focusing on my remarks late last night that 2 1/2 minutes of my comments were just preliminary, so I'll just wipe them away.

I want to start with a quote that I am taken with that comes from an article in December announcing the selection of the new president of the Enron Corporation, represented in this room here today and a major player in the energy business in the United States. Enron is a very, very large corporation with a lot of money, spending 25 million dollars on a national campaign to promote itself and competition and deregulation in the electric utility industry. The article reports that the new president of Enron has on his bulletin board the following quote from Machiavelli: "there is nothing more difficult to plan, more doubtful of success more dangerous to manage than the creation of a new system." Here we are talking about the world's most complicated system, the electric utility system, that has been heavily regulated, as Richard King and others will tell you, for the better part of this century. And the trick is to move this heavily regulated industry to a competitive marketplace.

We aspire, in many ways, to be positioned similarly to the Ford Motor Company, where we could set our prices and pick our customers as we choose. That is certainly not the electric utility industry of 1997. So the overriding issue involves the transition from a heavily regulated to a more competitive industry and I want you to know at the outset that the companies I represent, the 8 major electric and gas utility companies in the state, support and endorse competition and we are enthusiastic about it and looking forward to moving towards it, but as we deal with an industry that is probably the most complex that you can imagine, an industry that is very unique, an industry that probably affects every
man, woman, and child and most domestic animals in New York State, more than any other industry on a constant and continuous basis, we have to be careful. We have to treat this transition to competition very carefully. As Bob pointed out, there are certain things about competition that people have to focus on. I was impressed by an article in the January 26, 1997 Times Union newspaper, that was entitled "Free Market Reform Brings Higher Phone Rates to the Public: Only Beneficiaries Appear to be Big Businesses with Negotiating Clout."

An issue that I think is very important to focus on is the issue of reliability. When I think of the electric utility industry, I think of not just prices and the economic side of it, but also the issue of reliability. Our electric system in New York is unsurpassed, anywhere in the world. It is so good that people tend to take it for granted and focus on the economic side of the business. High energy prices are a problem. Without a doubt electric utility prices in New York State are too high and there is a reason for that. The prices are too high in New York because our costs are too high. And I think it is irrefutable that the costs in New York State that are driving the prices to levels that are too high are primarily caused by government policies--past and present. When you look at a Niagara Mohawk bill and realize that 50% of each customer's bill is attributable to state and local taxes and utility payments made pursuant to State legislation which subsidizes independent power producers, you realize that these are the costs that must be addressed and must come down.

Competition does not mean, nor does it translate into, automatically lower prices. It means that market forces control and it means supply and demand rules, without government tampering, without manipulation. Competition must not mean regulated competition. As I said, our industry supports competition, but it has to be fair, it has to be economically efficient, it can't be government regulated competition, and most importantly, the public cannot be misled. Competition should not be oversold, nor customers given unreasonable expectations, or there will be hell to pay. The thought I would like to leave you with today is this: competition in the electric utility industry is not coming, it's here. We support it, but we have to be very careful so we don't look back in the year 2007 and say: what did we do in 1997 and why in the world did we do that? Thank you.
HON. PAUL TONKO
Chair
NYS Assembly Energy Committee

There is no doubt in anyone's mind that we are in the midst of an energy price crisis. Just like the crisis of several decades ago that was a supply-based crisis, we need to resolve the energy cost situation in this State. On average, we are approximately 50% above the national average. There is no way anyone can grow and sustain an economy without addressing energy rates. I listened to John Bozzella talking about the exit of manufacturing jobs just a few moments ago. While the picture may have improved, we could also suggest, cynically, that not many manufacturing jobs are left to exit. Thus, the base from which we're calculating that exit from has diminished considerably. An estimated 19,000 jobs leaving the state is still a significant number. I would suggest that the manufacturing sector of our economy is still a strong and vital piece of our jobs equation. We need to revamp and modernize it, but undoubtedly energy will still be a significant cost of the operational situation. There is no hope to grow or retain jobs without addressing the energy side of the formula.

With that in mind, the Assembly has for the last several years been promoting the reduction of energy costs and bringing benefits to the consumers. In January 1996, we introduced Competition Plus/Energy 2000: our bill package that spoke to the energy price crisis of this State. There were three major dynamics associated with that proposal: 1) an immediate freeze on rates in the State; 2) second, the introduction of competition over a reasonable time frame with safety nets for consumers; and 3) an overall reduction approaching 25% whereby we could bring into reasonable view the relationship of New York as an energy state to those in the rest of the country. We then waited for a response from the Governor and the Senate because we do believe there should be a consensus between the two houses of the Legislature and the Governor, to provide the vision that would then be applied to various agencies to carry forth with the overall goal. That did not happen in the interim between January and mid-March, so we introduced, in bill form, that same package. We carried forth with bipartisan hearings across the State, travelling to all regions of the State to fine tune the Legislation. We then waited until the near end of session to go
forward and pass legislation because there was still no response.

I really believe our State is lacking the energy vision we desperately need to put together a blue print. It is now, more then ever, essential that we develop one.

To hear that the Public Service Commission expresses the vision of the administration is frightening. I believe that the regulator in this case should be the agent of change after the policy has been established by the Legislature and the Governor. Consumer protections, reliability, working with the workforce, and transforming it into a modern new competitive arena are all part of our legislation. We want to provide assistance for both large and small businesses. We also require that the pool of power to be shared for that program be competitively bid for. We believe those dynamics need to be introduced in the interim as we move forward with the final package.

Regarding the securitization bill that has been mentioned here this morning, we need to reduce costs, not cover those costs and hold people harmless. Bailing out an industry would be as dangerous as doing nothing. Perhaps a limited application of that concept as they have in other states would be fine. States like New Hampshire, California, and Pennsylvania have passed us by in energy reform. We had a chance last year to be a leader in this nation, and we failed miserably on behalf of the consumers. Thank you.