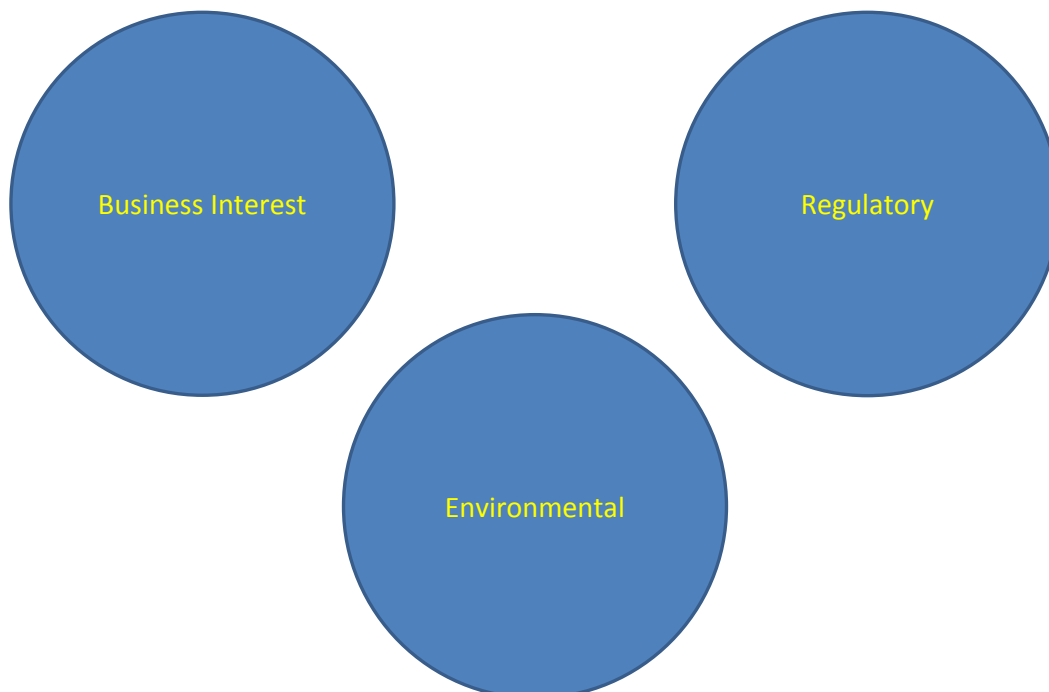


The 32nd Annual National Conference of Regulatory Attorneys

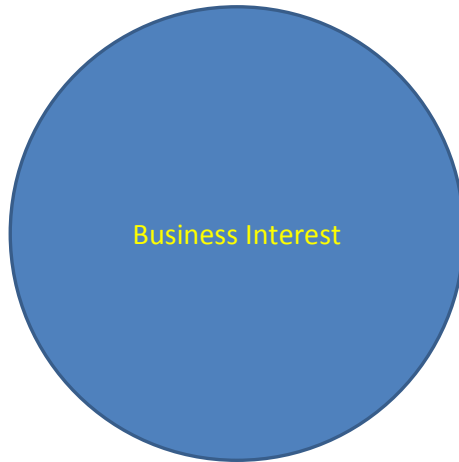
Why Regulation Does Not Fail Us (Unless We Fail Regulation)

Kenneth Rose
Independent Consultant and
Senior Fellow, Institute of Public Utilities
at Michigan State University
June 1, 2009
Las Vegas, Nevada

Three Spheres of Influence



Sphere of Influence – Business



Who

- Utilities
- IPPs/merchant gen.
- Equipment vendors

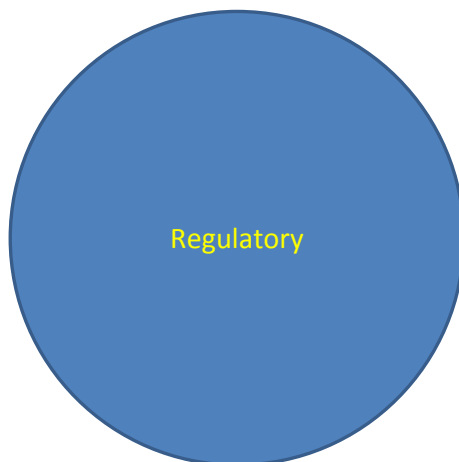
Characteristics

- Profit motive
- Oldest of the three “spheres”

Watchwords

- “Choice”
- “Markets always know better than bureaucrats”
- “Greed is Good”

Sphere of Influence – Economic Regulation



Who

- State PUCs
- Federal regulators
- Antitrust regulators

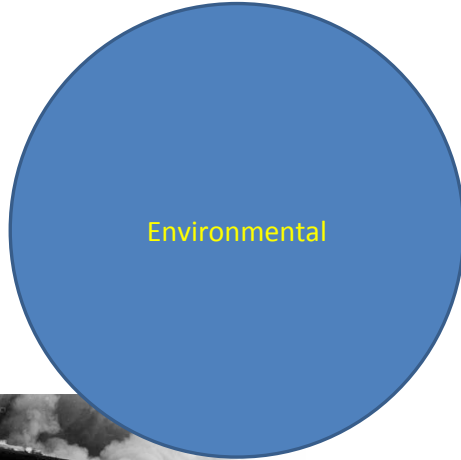
Characteristics

- Developed from progressive era politics
- Price control of franchised “natural monopolies”

Watchwords

- “Affordability”
- “Just and reasonable rates”
- “Public interest is Good”

Sphere of Influence – Environmental



Who

- Environmental regulators
- Environmental advocacy groups

Characteristics

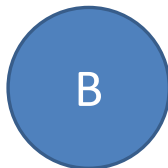
- Newest of the three “spheres”
- Modern-era version born in 1969 when the Cuyahoga River caught fire (wasn’t the first time!)

Watchwords

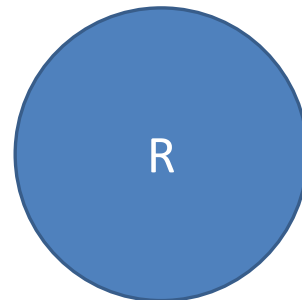
“Green is Good”

1979

“The Government is the Solution”

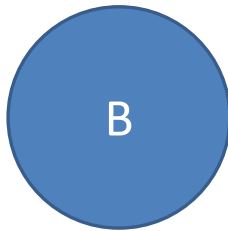


- ✓ Post Golden-Age
- ✓ Fuel prices increasing
- ✓ Capital cost increasing
- ✓ Rates increasing
- ✓ Unhappy customers and regulators

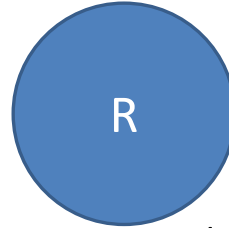


1989

“Government is the Problem”

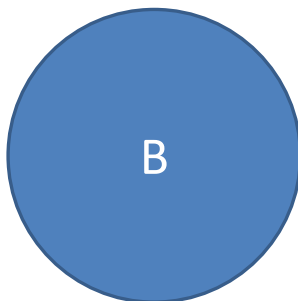


- ✓ Deregulation in many industries
- ✓ Growing support for environmental regulation
- ✓ Doubts about the effectiveness of regulation was growing

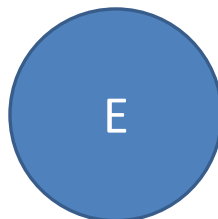
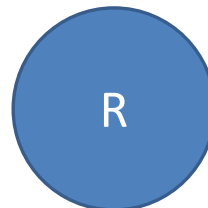


1999

“Government is Still a Problem”

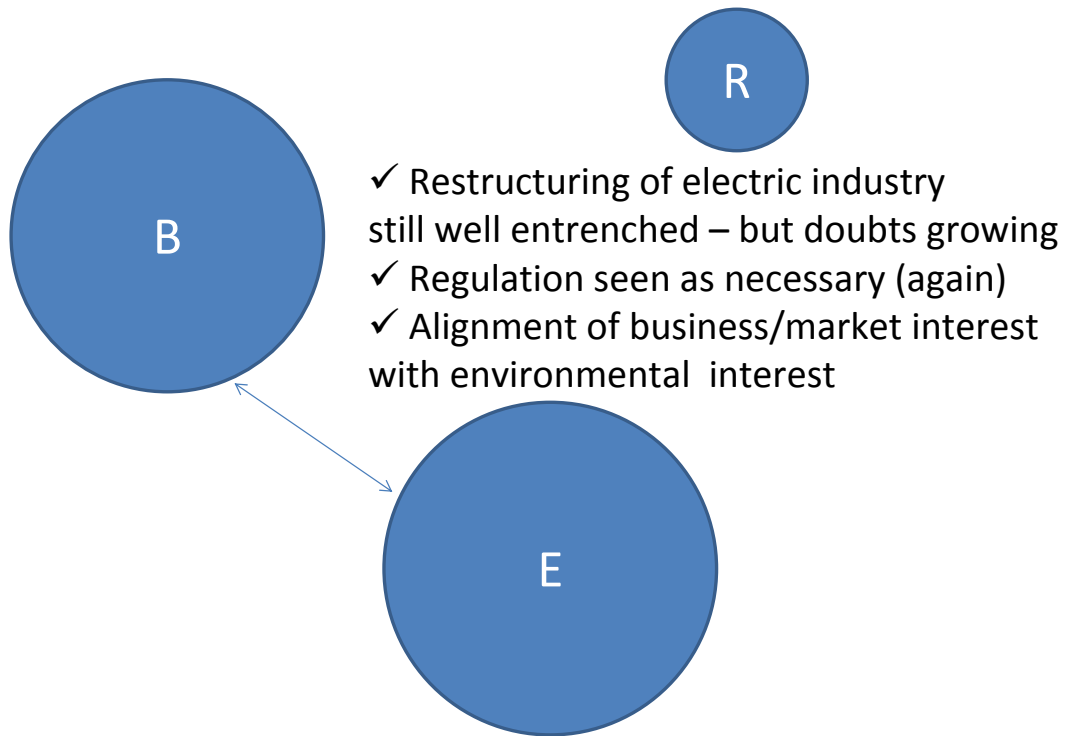


- ✓ Restructuring of electric industry well entrenched
- ✓ Regulation seen as an obstacle to be overcome



2009

“OMG! Where’s the Government!”



Where are we today, and how do we fix it

- Business and environmental interests changed over the years to fit the changing economic and political conditions
 - business changed by becoming more politically astute
 - environmental interest changed by becoming more business and market friendly
- In contrast, regulation changed little in how it has operated

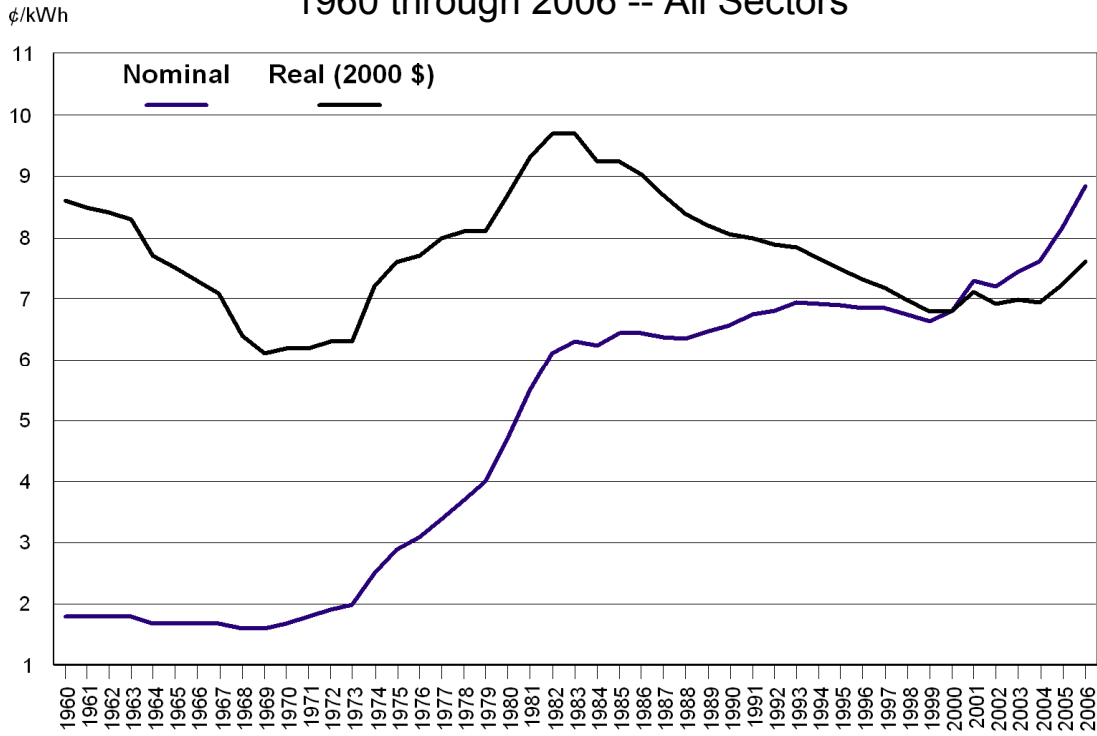
Where are we today, and how do we fix it (*continued*)

- Regulation cannot align itself with business interest – or any particular interest
- Must be independent
 - otherwise we end up with the Wall Street Bankster/Political/Regulatory alignment, and will get the same result
- Have to convince legislators that regulation is necessary, effective, and in the long term interests of the voters ah, public

Where are we today, and how do we fix it (*continued*)

- The Wall Street parallels are striking
 - political alignment between DC and financial interest
 - “watchdogs” take a long nap – including credit rating agencies and regulators not regulating
- End result is something even capitalists don't like

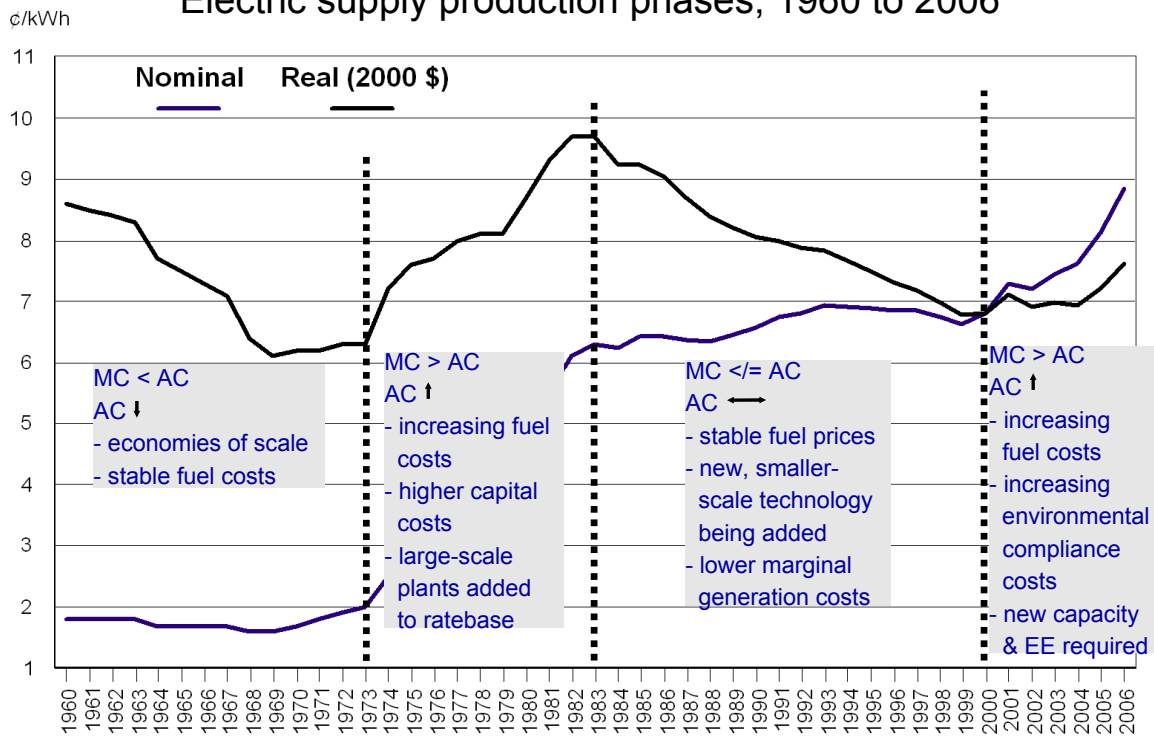
US Average Retail Price 1960 through 2006 -- All Sectors



Data source: DOE/EIA.

What's Ahead?

Electric supply production phases, 1960 to 2006



Data source: DOE/EIA.

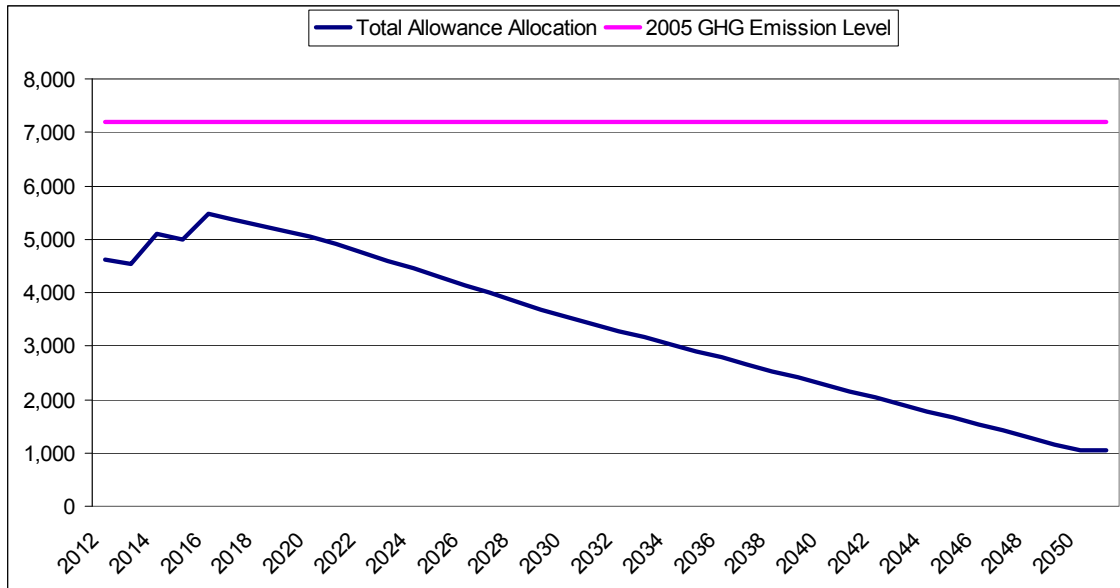
The “American Clean Energy and Security Act of 2009”

- The U.S. House of Representatives, Committee on Energy and Commerce concluded markup of H.R. 2454 on May 20, 2009
- “The legislation will create millions of new clean energy jobs, save consumers hundreds of billions of dollars in energy costs, promote America's energy independence and security, and cut global warming pollution.” -- Chairman Waxman
- There are some significant challenges for state PUCs and FERC

SEC. 703. -- Reduction targets for specified sources

- Goal is to cap and reduce annual greenhouse gas emissions for each calendar year beginning in 2012, so that
 - in 2012, the quantity of greenhouse gas emissions from capped sources does not exceed 97 percent of the quantity of greenhouse gas emissions from such sources in 2005;
 - in 2020, the quantity of greenhouse gas emissions from capped sources does not exceed 83 percent of 2005;
 - in 2030, the quantity of greenhouse gas emissions from capped sources does not exceed 58 percent of 2005; and
 - in 2050, the quantity of greenhouse gas emissions from capped sources does not exceed 17 percent of 2005.

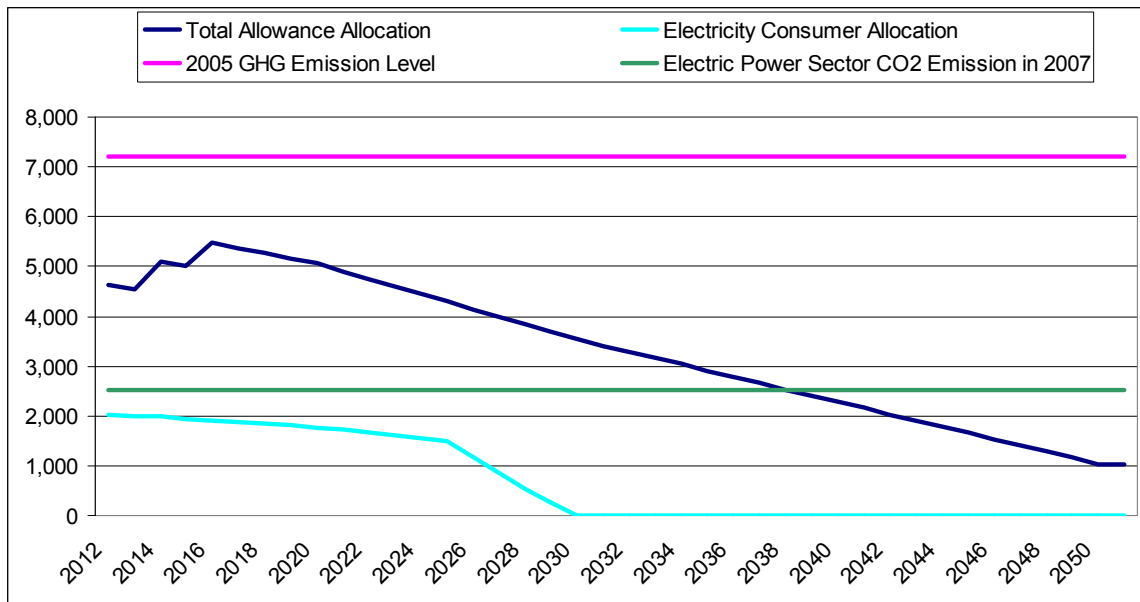
Emission allowances (millions) by year (sec. 721(e)(1))



Sec. 782(a) – Allocation of Allowances for Electricity Consumers

- For years 2012 and 2013, 43.75 percent of the emission allowances established for each year under section 721(a)
- years 2014 and 2015, 38.89 percent
- years 2016 through 2025, 35.00 percent
- year 2026, 28 percent
- year 2027, 21 percent
- year 2028, 14 percent
- year 2029, 7 percent

Emission allowances (millions) by year (sec. 721(e)(1))



Allowance allocation for electricity consumers

- The allowances allocated to electricity consumers in the graph do not include all possible allowances to be allocated
- Other allocations are included for:
 - low income consumers
 - deployment of carbon capture and sequestration
 - energy efficiency and renewable energy
 - QFs, IPPs, & merchant coal generators
- Also are compensatory allowances and offset credits

Who gets the allowances?

- EPA would distribute these allowances to the electricity sector *to local distribution companies* – but first subtracting allowances for merchant coal generators and for “long-term contract generators”
- Different from the way SO₂ allowances were allocated under the 1990 Clean Air Act

Basis of the allocation

- 50 percent of the emission allowances allocated to electricity local distribution companies are to be based on the annual average carbon dioxide emissions attributable to generation of electricity sold at retail by each such company during—
 - calendar years 2006 through 2008; or
 - any 3 consecutive calendar years between 1999 and 2008
- The other 50 percent of the allowances are to be based on each electricity local distribution company’s annual average retail electricity deliveries for 2006 through 2008 – unless the owner or operator of the company selects 3 other consecutive years between 1999 and 2008

Who will determine this?

- “(A) RATEPAYER BENEFIT.—Emission allowances distributed to an electricity local distribution company under this subsection *shall be used exclusively for the benefit of retail rate payers of such electricity local distribution company*. Emission allowances received by an electricity local distribution company under this subsection may not be used to support electricity sales to entities or persons other than the retail ratepayers of such electricity local distribution company.
- “(B) RATEPAYER CLASSES.—In using emission allowances distributed under this section for the benefit of ratepayers, an electricity local distribution company shall ensure that ratepayer benefits are distributed—
 - “(i) among ratepayer classes ratably based on electricity deliveries to each class; and
 - “(ii) equitably among individual rate payers within each ratepayer class . . .”

. . . and this?

- “(C) LIMITATION.—No electricity local distribution company may use emission allowances to provide to any ratepayer a *rebate* that is based solely on the quantity of electricity delivered to such ratepayer. To the extent an electricity local distribution company uses the value of emission allowances distributed under this subsection to provide rebates, it shall, to the maximum extent practicable, provide such rebates with regard to the fixed portion of ratepayers’ bills.”

Here's some work for you . . .

- “(B) PLANS.—Not later than April 30 of 2011 and every 5 years thereafter through 2026, each electricity local distribution company shall submit to the Administrator a plan, *approved by the State regulatory authority* or other entity charged with regulating the retail rates of such company, describing such company’s plans for the disposition of the value of emission allowances to be received pursuant to this subsection, in accord with the requirements of this subsection.”

And this too . . .

- “(C) REPORTS.—Not later than June 30 of 2013 and each calendar year thereafter through 2031, each electricity local distribution company that received emission allowances under this subsection in the preceding calendar year shall submit a report to the Administrator, *and to the relevant State regulatory authority* or the entity with authority to regulate retail electricity rates in the case of an electricity local distribution company not regulated by a State regulatory authority, describing the disposition of the value of any emission allowances received by the company in the prior calendar year pursuant to this subsection, including—
 - “(i) a description of sales, transfer, exchange, or use by the company for compliance with obligations under this title, of any such emission allowances;
 - “(ii) the monetary value received by the company, whether in money or in some other form, from the sale, transfer, or exchange of emission allowances received by the company under this section;
 - “(iii) the manner in which the company’s disposition of emission allowances received under this subsection complies with the requirements of this subsection, including each of the requirements of paragraph (3); and
 - “(iv) such other information as the Administrator may require pursuant to subparagraph (A).”

State Allowance Programs

- Can exchange greenhouse gas emission allowances issued before December 31, 2011, by the State of California or for the Regional Greenhouse Gas Initiative, or the Western Climate Initiative (“state allowances”) for federal emission allowances

What is not allocated will be auctioned

- For years 2012 through 2025, allowances not designated for distribution or auction are to be auctioned by EPA and the proceeds deposited into the treasury
- For years 2026 through 2050, EPA is to have an auction for allowances not designated for distribution or auction, with the proceeds from the sale placed in the “Climate Change Dividend Fund”

What PUCs Need to Know

- Allocation of allowances for your electric and gas distribution companies
- This would be applied to a significantly changed electric supply industry -- than when the 1990 law was passed
- Be aware of the “unholy alliance” (Harry) and how it will affect customers