SUBJECT: Restructuring the electric utility industry

COMMITTEE: State Affairs — committee substitute recommended

VOTE: 13 ayes — Wolens, S. Turner, Alvarado, Bailey, Brimer, Counts, Craddick, Danburg, Hunter, Longoria, Marchant, McCall, Merritt

2 nays — D. Jones, Hilbert

SENATE VOTE: On final passage, March 17 — voice vote (Barrientos, Nixon, Truan recorded nay)

WITNESSES: *(On original committee substitute:)*
For — Julie Blunden, Green Mountain Energy; Gordon Forward, TXI and Chaparral Steel; Stan Johnson and John Osgood, Jr., Texas Air Conditioning Contractors Association; Robert J. King, Texas Energy Services Coalition; Jim Marston, Environmental Defense Fund; Ray Palmer, New Energy Ventures; Garrett Stone, NUCOR Steel; James A. Tramuto, Competitive Power Advocates; Klip Weaver, Control Systems International; Mike Williams, Texas Electric Cooperatives

Against — Carol Biedrzycki, Texas Ratepayers Organization to Save Energy; Janee Briesemeister, Consumers Union, Southwest Regional Office; Burl Buchanan, City of Spearman; Randall Chapman, Texas Legal Services Center; Stephen Fenoglio, Apache Corp., Texas Independent Producers and Royalty Owners Association, Texas Cattle Feeders Association, and Texas Cotton Ginners Association; Claudia Gooch, EOAC; Jerruld Oppenheim, National Consumer Law Center; Tom “Smitty” Smith, Public Citizen; Glenn Summers, EOAC of Waco

On — Jim Darling, City of McAllen and CP&L Cities’ Steering Committee; Randy Eminger, The Center for Energy and Economic Development; Robert King, Texas Renewable Power Coalition; Rick Levy, Texas AFL-CIO; Suzi McClellan, Office of Public Utility Counsel; George Smith, Sierra Club, Lone Star Chapter, Air Quality Committee; Pat Wood, Public Utility Commission of Texas

BACKGROUND: The state began regulating the electric utility industry in 1975 when

lawmakers created the Public Utility Commission (PUC) to set standards and rates for both electric and local telephone service. Before 1975, cities had the primary responsibility for regulating electric rates.

The electric utility industry is a $20-billion-a-year industry in Texas, with three general types of utilities:

- Investor-owned utilities, private companies owned by shareholders and regulated by the PUC, sell electricity to about 70 percent of all customers in Texas. Utility investments are reviewed by the PUC. If investments are deemed prudent, they are figured into electric rates and paid for by customers.
- Rural electric cooperatives are owned by the communities they serve. The owners of co-ops are the customers. Rates for the 73 Texas co-ops are not set by the PUC. Investments are approved by the co-ops with support of the customers.
- Municipal utilities are owned by cities. A municipal utility board is either elected or appointed by elected officials to set rates and make investments in infrastructure. Texas has 75 municipally owned utilities.

In 1995, the Legislature deregulated the wholesale electric market. Competitors now may sell power in the wholesale market to all three types of electric utilities.

In general, a utility has the right to serve a specific geographic area in Texas. In exchange for a guaranteed customer base, utilities agree to provide reliable, safe, and reasonably priced electric service to all customers in that area.

The U.S. electric network is divided into three grids: the Western Interconnection, the Eastern Interconnection, and the Electric Reliability Council of Texas (ERCOT). While most of Texas is in the ERCOT power region, portions of the Panhandle, northeast Texas, and southeast Texas are in the other adjacent power regions.

As of April 1, 1999, 20 states had overhauled their electric utility systems through legislation or regulatory orders, and legislation on restructuring was pending in four other states. Twenty-four other states, including Texas, were debating the issue. Meanwhile, federal lawmakers are working on plans to restructure the industry nationally, with legislation expected within the next

two years. See also House Research Organization Focus Report 76-12, *Retail Competition in Electric Generation: Experience in California and Pennsylvania*, April 30, 1999.

POINT BY POINT ANALYSIS:

RETAIL COMPETITION

DIGEST: CSSB 7 would restructure the electric utility industry in Texas to provide retail competition and customer choice beginning January 1, 2002, for all customers now served by investor-owned utilities. Transmission and distribution of electricity would remain regulated by the PUC. Customers of investor-owned utilities could choose their retail electricity provider beginning on January 1, 2002. The PUC would have the authority to delay competition if it found that a power region could not offer fair competition and reliable service to all customers.

The bill, which would take effect September 1, 1999, would provide a rate freeze from January 1, 1999, through December 31, 2001. After that, customers would receive a rate cut of 6 percent. The bill includes provisions that would:

- allow utility companies to add a competitive transition charge to electric bills to recover costs of investments previously authorized by the PUC that might not be recoverable from customers in a competitive market;
- allow utilities to refinance debt by issuing bonds to be paid by utility customers;
- allow municipally owned utilities, cooperative utilities, and river authorities to choose when to enter the competitive market;
- prevent domination of the electricity market by any one utility;
- require that all electric customers pay a systems benefit fee to make up lost revenues to school districts resulting from restructuring and to finance low-income and customer education programs;
- provide consumer protections for customers;
- ensure reliability in the state electric power network;
- provide mechanisms to protect workers displaced by restructuring;

- set goals for generation of electricity from renewable sources of energy;
- require older power plants to reduce air pollution;

- allow the General Land Office to sell electricity to state agencies and other public entities; and
- reduce taxes to natural gas producers by $130 million over the next two years.

Supporters say: A competitive market would lead to lower electric rates for all customers in Texas, better response to customers, increased business efficiency, and a more attractive business environment. Many new electric generation providers want to compete in Texas and potentially could offer electricity at a lower price than is currently available in a monopoly market. Competition always is a better mechanism for setting rates than government regulation. All customers would benefit from being able to choose among electric providers. Furthermore, it would be better for Texas to develop its own plan than to wait for a less appropriate plan from the federal government. CSSB 7 also would reduce air pollution and preserve electric service reliability. The bill would provide consumer protections to prevent abuses from the new market system.

Opponents say: Electric utility restructuring is still an experiment and so far has not lowered electric bills for residential customers over the long term. In other states that have restructured the electric utility industry, only large industrial customers truly have benefitted.

This is not a good time to restructure in Texas. Texas consumers already are on the verge of receiving lower rates under today's regulated monopoly system. Utility fixed costs are declining as the major companies have been paying off the high cost of nuclear plants, and other costs are going down as well. Freezing rates at their current level would mean that customers would have to pay more money than they would pay under the current system.

There also are serious questions about how reliable the electric generation system would be if it were not regulated and monitored by the PUC. There have been many problems and few real benefits from long-distance telephone market deregulation. There has been a huge increase in nuisance calls from telemarketers selling phone services.

Other opponents say: CSSB 7 should do more to ensure that all customers benefit from restructuring. This bill would add costs to customers' electric bills not currently included under the regulated system. At the same time,

CSSB 7 would give residential and small business customers only a 6 percent rate cut, when rates might well be reduced even further under continued regulation. Provisions in the bill that would encourage electric providers to offer service to all customer classes and to prevent rate increases for small energy users would last only through the first five years of competition. After 2007, residential customers would have no guarantee that benefits from competition would continue for them.

TRANSITION TO RETAIL COMPETITION

Rate freeze. CSSB 7 would require electric utilities to freeze their retail electric rates at the level in effect on January 1, 1999, until January 1, 2002, the start of competition. A utility could not raise base rates above the frozen rate unless the company suffered significant losses from a major disaster or from new state or federal regulatory requirements.

During the rate-freeze period, no one could file a complaint, request a hearing, or make any type of determination as to the reasonableness of the retail base rates, overall utility revenues, return on invested capital, and net income. A customer would have the right to complain to the PUC regarding the quality of electric service or the applicability of the particular rate charged to the customer.

Pilot projects. The PUC would have the authority to use customer-choice pilot projects to evaluate the ability of each power region and each electric utility to implement customer choice. It could delay competition based on negative results from the pilot projects. Beginning June 1, 2001, each electric utility would have to offer customer choice to customers representing 5 percent of its combined energy load (the total amount of energy sold to customers). Each utility operating a pilot project would have to charge residential and small business customers the frozen utility rate.

Supporters say: CSSB 7 would allow utilities to freeze existing rates to pay off debt on generation plants more quickly. This mechanism would save customers money in the long run. At the start of competition, all residential and small business customers would get a mandatory 6 percent rate decrease if they remained with their old utility's affiliated retail electricity provider.

Customers who chose alternative providers likely would see savings of up to 15 percent, according to some estimates.

Opponents say: CSSB 7 would freeze existing high rates for the next three years, then give consumers only a 6 percent rate cut. Consumers have paid higher than market-price rates to pay off debt on generating plants. Electric rates should be falling because of lower prices for energy and depreciation of debt.

STRANDED COSTS

BACKGROUND: A key issue in restructuring legislation is how to pay for long-term investments that utilities might not be able to recover in a competitive market. Such "stranded costs" include debt still owed for high-cost power plants and long-term contracts negotiated at unfavorable rates. For example, stranded costs for nuclear power plants reflect the difference between the book value of the plants under state regulation and what those plants would be worth if a utility tried to sell them on the open market. Utilities also have generating plants that might be worth more in a competitive market than they are worth on the books today. The cost of building those plants also was built into today's electric rates.

Competitive transition charge. CSSB 7 would allow utilities to recover 100 percent of their net stranded costs incurred in purchasing power and providing electric generation service, as long as those costs could be verified and could not be reduced through mitigation. Recovery would be authorized through a competitive transition charge (CTC) on all existing or future retail customers within the utility's geographical certificated service area as of May 1, 1999. At the end of the rate-freeze period, any costs associated with nuclear decommissioning obligations also would be included as a charge to retail customers.

Each utility would have to file detailed annual financial reports with the PUC. Among other things, the reports would have to describe the determination of annual costs, any positive differences between annual revenues and costs, and the determination of any invested capital. The PUC would use these reports to determine the CTC for each utility.

Allocation of stranded costs. CSSB 7 would require utilities to allocate stranded costs among all customer classes based on:

- the type of generation plant that caused the stranded costs to exist;
- whether the plant provided power constantly (base load) or was used mainly to provide power at times of peak demand (peak load); and
- the average demand from each customer class throughout the year for the output of that particular plant.

After the rate-freeze period ended, the allocation of stranded costs could not be shifted from one customer group to another.

Retail stranded costs not directly related to a generation plant would have to be allocated to retail customer classes based on the kilowatt-hour usage of each class. With certain exceptions, including ownership of an on-site generation facility, no customer or customer class could avoid paying the amount of stranded costs allocated to that customer or class.

Mitigation of stranded costs. CSSB 7 would require utilities to pursue commercially reasonable means to reduce their potential stranded costs before the start of competition. This would include good-faith attempts to renegotiate high-cost fuel and purchased power contracts, as well as accelerating depreciation on certain facilities. The PUC would have to consider the utility's mitigation efforts when determining the final amount of the utility's stranded costs that could be charged to customers. The PUC could not substitute its judgment for a market valuation of generation assets.

CSSB 7 would require that any positive difference between annual revenues and annual costs be applied toward paying down stranded costs of generating assets. During the rate-freeze period, an electric utility that did not have stranded costs could use any positive difference to improve or expand transmission and distribution facilities or could use it toward efforts to improve air quality. An electric utility with additional positive differences would have to return the amount to its customers.

Ensuring accuracy of stranded cost estimates. CSSB 7 would prohibit a utility from collecting too much money to pay off stranded costs. It would require affiliated power-generation companies to quantify stranded costs that they could recover from customers. Before 2002, regulated utilities would

make initial estimates of their stranded costs using computer modeling, and the PUC would use these estimates to set the CTC. When competition began in 2002, the utilities would use their actual market values to quantify their actual stranded costs. Market valuation could be based on sale of generating plants and other methods involving whole or partial spin-offs or exchanges of assets.

Stranded cost review. CSSB 7 would require the affiliates of former monopoly utility companies to join together to make final determinations of stranded costs that would be reconciled with the estimates used to develop the CTC. This would occur after January 10, 2004. The PUC would review each utility's estimate and make adjustments to the CTC in a "true-up" proceeding. Changes in electric rates caused by rate cases remanded from the courts to the PUC during the rate-freeze period would be dealt with in the stranded cost review.

Supporters say: The benefits that competition would bring in terms of lower rates far outweigh any temporary charges included on electric bills to cover the costs of making the transition to the new competitive market. That includes the costs to customers for utility investments that might not be recoverable under competition. Utilities have a right to be paid for these investments. These investments were reviewed on behalf of the state by the PUC in lengthy rate-case hearings with plenty of opportunity for argument. The PUC approved these costs as prudent.

CSSB 7 would provide a fair allocation of stranded costs among all electric customer classes. Currently, the cost of debt for nuclear plants is built into the electric rates. Because residential and small business customers pay a higher rate for electricity than do industrial customers, they pay a greater share of the debt. Under the current allocation method, industrial customers as a class pay about 20 percent of stranded costs, small business customers pay about 34 percent, and residential customers pay about 46 percent.

Under CSSB 7, the allocation of stranded costs among customers would be based on energy usage, the type of energy, and what kind of plant produced the energy. Under this new allocation method, industrial customers would pay 34 percent of stranded costs, small businesses would pay 32 percent, and residential customers would pay 34 percent. This provision would save residential and small business customers about $45 million annually,

according to the PUC.

Utility companies predict that industrial customers would see an average increase of 3.5 percent on their bills, but this is before calculating the benefits of competition such as lower rates and better service. Average industrial rates in Texas would be about 4.14 cents per kilowatt-hour (kWh), compared to the national average of 4.93 cents per kWh reported by the Edison Electric Institute.

Utilities that sell generating facilities that would be worth more in a competitive market should get to keep the profits. Utilities should benefit from having made wise decisions in the past.

Opponents say: Stranded costs for unprofitable generating plants, mostly nuclear plants, are estimated at about $4.9 billion at the start of competition. CSSB 7 also would force customers to pay an additional $600 million to clean up old generating plants, according to the PUC. Only the costs for generating plants currently are figured into customers' regulated rates. Residential ratepayers would see little savings from competition because of the additional costs on their electric bills.

The new allocation of stranded costs in CSSB 7 would shift tremendous costs onto Texas businesses and employers. This bill would force industrial customers to pay an additional $61 million annually for stranded costs. This would mean a huge increase in electric rates for industrial customers. While residential customers would see only about $2 in savings per month, the increase for large business customers could be thousands of dollars a month. Businesses use much more electricity, and there are fewer of them over which to spread out the costs.

No other state that has adopted electric restructuring has included a similar stranded cost allocation. Texas could lose its economic advantage to other states as businesses look for friendlier places in which to build and expand.

Other opponents say: CSSB 7 also would allow industrial companies to build their own generating plants, escape paying their share of stranded costs, and shift those costs to residential customers. This could shift one-sixth of the bill for stranded costs to residential ratepayers in Texas, based on the estimate of cogeneration plants that were built by 1991.

Stranded costs should be a two-way street. If utilities are allowed to pass along costs of expensive nuclear plants, customers should get the benefit from efficient plants that are worth more. It is not fair to force customers to pay billions of dollars worth of debt for unprofitable plants and not get any benefits for plants that were paid for through regulated rates.

CUSTOMER CHOICE AND PRICING

CSSB 7 would provide that all electric utility customers now served by investor-owned utilities could choose their retail electricity providers beginning January 1, 2002. The affiliated retail electricity providers of former monopoly utility companies would continue to serve customers who did not choose an alternative provider. Retail providers would have to demonstrate to the PUC that they had the financial, managerial, and technical resources needed to provide reliable electric service and that they could comply with customer protection requirements.

Price to beat. CSSB 7 would require retail electric providers affiliated with former monopoly utilities to give residential and small business customers a 6 percent rate reduction from their frozen rates at the start of competition. This reduced rate would be the "price to beat." Customers that did not choose another retail electricity provider would be served by the affiliated retail electricity provider at the price-to-beat rate.

CSSB 7 would authorize the PUC to adjust an affiliated retail electricity provider's price to beat if it threatened the provider's financial integrity or the provider demonstrated that its existing fuel factor was inadequate to reflect significant changes in the market price of natural gas and purchased energy.

Affiliated retail electricity providers could not compete in their affiliated transmission and distribution service areas until 40 percent of residential and small business customers were being served by alternative providers, or until 36 months after competition, whichever came earlier. Following the true-up review of stranded cost totals, the PUC would have the authority to adjust the price to beat.

Five-year rate cap. The affiliated retail electricity provider could not charge rates higher than its price to beat for five years, except to reflect major fuel

price fluctuations.

Energy rebate. Two years after competition began, CSSB 7 would require affiliated retail electricity providers to calculate the difference between the fixed price to beat and the market price of electricity after competition. This rebate would be credited to customers remaining with each utility-affiliated retail electricity provider. The rebate cap would be set at $150 per customer, applied to the number of customers remaining with the utility, less the number of new customers the utility's affiliated retail electricity provider served outside its home territory.

Choices for residential customers. A retail electric provider serving an aggregate load of more than 300 megawatts would have to sell at least 5 percent of total energy load to residential consumers for 36 months after retail competition began. A provider not complying with this requirement would have to pay a certain amount into the system benefit fund. The amount would be calculated using a formula comparing the amount of power actually sold to residential customers and the amount the utility should have sold to residential customers, based on the requirement.

Aggregation. CSSB 7 would allow customers to aggregate or join together to negotiate lower rates for electricity from a retail electricity provider, a municipally owned utility, or an electric cooperative.

Prepaid electric service. CSSB 7 would prohibit electricity providers from selling prepaid electric service to residential customers at a price that was higher than the price charged by the provider of last resort, the company designated by the PUC to offer a basic rate package to serve customers that other utilities did not want to serve.

Transmission and distribution rates. CSSB 7 would require the PUC to establish reasonable and comparable rates for open access to distribution facilities for retail electricity providers on or before January 1, 2002.

Supporters say: A critical issue in restructuring the electric utility industry is creating effective customer choice and providing that all customer classes benefit from rate reductions. Individuals and small businesses may not have the same power as large industrial customers when it comes to negotiating

favorable electric rates. Rural customers also could be at a disadvantage because the cost of delivering energy over long distances to them is higher.

CSSB 7 would guarantee that residential and small business customers benefit from restructuring with lower rates and the ability to choose from alternative electricity providers. The bill also would ensure that electric rates would not go up for five years.

The price-to-beat mechanism would ensure that existing utilities could not use predatory pricing to undercut competitors. This mechanism would stay in place for three years or until the affiliated electric provider lost 40 percent of its residential customer base to competitors. Requiring affiliated providers to charge a higher rate for electricity would give consumers the incentive to shop for an alternative provider. This approach has been very successful in encouraging competition in Pennsylvania.

CSSB 7 also would guarantee that residential customers would have alternative electricity providers from which to choose during the first three years of competition. All retail providers who chose to sell electricity in Texas would have to sell at least 5 percent of their energy to residential customers or pay a penalty. An electricity provider that served an aggregate load of 300 megawatts would have to serve about 20,000 residential customers. This would prevent electricity providers from “cherry-picking” more profitable business customers and ignoring residential customers.

Electricity providers would pay the penalty on the difference between the required 5 percent and the actual percentage of residential customers they served. For example, if only 4 percent of a utility’s load was residential, that utility would be penalized for the 1 percent difference. This would ensure that utilities were not hit with penalties that would be too high.

CSSB 7 would benefit all Texans, whether they live in urban or rural areas. All customers would receive the opportunity to reap the rewards of electric competition, such as better prices, more choices, and new service options.

The bill would limit the amount that residential customers could be charged for prepaid electric service. The current trend for many services is to charge lower-income people more for service and require them to pay in advance. These customers should not be required to pay higher rates when they pay for

service in advance.

Opponents say: Provisions in CSSB 7 actually could decrease competition in Texas. The price to beat would prevent a retail electricity provider that was affiliated with an investor-owned utility from offering a competitive price to residential and small business customers in that utility's service area for five years, or until the provider had lost 40 percent of its residential and small business customer energy load. The price-to-beat concept would deny residential and small business customers lower prices and innovative pricing plans from an affiliated retail electricity provider, because the provider could charge only the price to beat.

Requiring retail electricity providers to ensure that at least 5 percent of their energy load was supplied to residential customers would discourage new electricity providers from doing business in Texas at all.

A competitive market should be designed to give customers choices, not to protect specific competitors by restraining others in ways that work to the detriment of consumers. Customer satisfaction based upon price and service options will determine the success of electric industry restructuring.

AIR POLLUTION CLEAN-UP COSTS

BACKGROUND: "Grandfathered" facilities are exempt from most state air permitting requirements because they predate the 1971 Texas Clean Air Act and have not changed significantly since then. Grandfathered facilities may remain exempt from major permitting requirements so long as they do not undergo modifications that would result in a significant increase in air contaminants. All grandfathered facilities, however, must comply with state emission-reporting requirements and must pay fees for pollutants they emit, currently set at $26 per ton with an annual cap of 4,000 tons.

CSSB 7 would allow utilities to include costs of improvements to air quality incurred before January 1, 2002, in the total for the utility's stranded costs. Capital costs incurred by an electric utility or power generating company to improve air quality after January 1, 2002, and before May 1, 2003, would be eligible for inclusion in the determination of stranded costs in the true-up review proceeding in 2004.

These costs could be included in stranded costs only to the extent that the cost was applied to offset or reduce air-pollution emissions from electric utility plants. The Texas Natural Resource Conservation Commission (TNRCC) also would have to determine that the reduction was essential to achieving compliance with federal Clean Air Act standards, or necessary for an unpermitted electric generating facility to obtain a permit.

Emissions reductions of grandfathered facilities. CSSB 7 would require all owners or operators of power plants to apply to TNRCC for an air-contaminant emissions permit by September 1, 2000, or be shut down by May 1, 2003, unless TNRCC found good cause for an extension. The permit would require the facilities to eliminate 50 percent of their 1997 emissions of nitrous oxides and 25 percent of their 1997 emissions of sulphur dioxide. A municipal utility, electric cooperative, or river authority could exclude any power plant of 25 megawatts or less from these requirements and would have to inform TNRCC by January 1, 2000, of its intent to do so.

CSSB 7 would require TNRCC to develop a permitting program that would allocate emissions allowances of sulphur dioxides and nitrogen oxides among power plants. It would allow facilities to trade emissions allowances for those air pollutants within three geographic regions.

An electric utility company would have to consider whether retrofitting a generating plant with air-pollution equipment would be more cost-effective than closing the facility. If retirement were the most cost-effective alternative, the net book value of the facility could be included in the utility's stranded costs.

Supporters say: In a competitive utility market where there is pressure to keep prices low, there also will be pressure to produce electricity from facilities that are cheap to operate. This favors fossil fuel plants over renewable resources. Using more of these cheaper, dirtier plants could increase emissions that cause ground-level ozone, an air pollutant. CSSB 7 would put a firm cap on emissions in place so that utilities could not increase emissions from older plants.

CSSB 7 would help mitigate ozone smog problems in Texas by giving a date certain to end the emissions loophole for grandfathered facilities. The bill also would provide a firm cap on total emissions in each region, preventing units from using averages to skirt the bill's intent. A firm cap plus a trading

credits program for emissions reductions would make the environmental provisions more efficient and less costly.

A trading credits program for emissions reductions would give utilities full flexibility to determine which facilities and with what technology they would achieve the required emissions reductions. This would provide the most economically efficient manner to achieve reductions, lowering the cost to ratepayers.

The entire state would benefit from the cleaner air that would result. The emissions reduction requirements in CSSB 7 are significant, and additional reductions requirements under a Best Available Control Technology (BACT) standard would overburden utilities and increase costs for ratepayers. Under CSSB 7, residential customers would pay an average of 38 cents per month more to cover the cost of upgrading these plants. Reduced costs from the emissions trading program likely would reduce the impact on customers' electric bills.

Opponents say: This provision of CSSB 7 would add $600 million to the stranded cost bill, according to the PUC. Including the cost of cleaning up air pollution in utilities' estimate of stranded costs would force ratepayers to foot the bill for costs that should be borne by utilities themselves. The utilities have escaped laws to require them to comply with clean air standards for nearly 30 years, and they should be required to pay to upgrade outdated plants themselves.

Other opponents say: CSSB 7 should require all power plants to upgrade so that they meet the most current clean air standard, the BACT standard. This would require power plants to reduce nitrogen oxide emissions by up to 75 percent and reduce sulphur dioxide emissions by up to 60 percent.

SELLING UTILITY DEBT

BACKGROUND: Securitization allows utilities to sell their debt to a third party. The utility receives a lump-sum payment, equaling the amount of debt sold, from investors. Investors then issue securities. Utility customers pay the principal and interest payments on the securitized debt instead of paying the cost on their electric bills over time. This mechanism allows debt to be

refinanced at potentially lower interest rates, cutting total cost of the debt. Once bonds are issued, however, ratepayers must continue to pay for them.

CSSB 7 would allow a utility, any time after the rate-freeze period, to securitize up to 100 percent of its regulatory assets and up to 75 percent of the initial estimate of its stranded costs. Alternatively, utilities either could securitize those debts and recover the cost through a CTC, recover up to 100 percent of stranded costs only through a CTC, or use a combination of the two methods. CSSB 7 would require the PUC to review transition charges that would be used to recover securitized costs and to adjust them at least annually to correct any overcollections or undercollections during the preceding 12 months.

Supporters say: Securitization refinances the debt at a lower interest rate, the same way that homeowners might refinance their mortgages. CSSB 7 would require the PUC to analyze actual stranded costs using market-based methods and to make adjustments in regulated transmission and distribution rates. This would ensure that companies do not over- or undercollect these costs from customers.

Opponents say: Utilities should not be allowed to securitize their stranded costs. Once securitized bonds are issued, they are irrevocable. Utilities will have recovered their stranded costs up front, rather than over time. Adjusting this if stranded cost estimates are not accurate could be difficult. Also, securitization would provide a large lump sum of windfall cash for the utility at the start of competition. This would be a special advantage given to the incumbent utility that could be used for anticompetitive purposes.

PREVENTING ABUSE OF MARKET POWER

BACKGROUND: Market power means the power of one company to dominate the market. Traditional utilities were authorized by law to own and operate all aspects of the electric industry in a single market, including generation, transmission, distribution, and retail customer service. Because traditional utilities have an incumbent advantage in all of the aspects of the utility industry, they potentially could play a dominant role in each aspect of the business.

Limitation of ownership of installed capacity. On the date competition began, a power generating company could not own and control more than 20 percent of the "installed capacity" located in or capable of delivering to a power region. The PUC could waive or modify the requirement for good cause in a power region not located entirely within the state. The PUC would have to monitor market shares of installed capacity to ensure that the limits were not exceeded. Electric providers found in violation would have to file a market power mitigation plan with the PUC.

Capacity auction. At least 60 days before competition began, each affiliated power generating company would have to sell at least 15 percent of its installed generating capacity at auction. Installed generating capacity would mean all potentially marketable generating capacity, including facilities already connected with a transmission or distribution system and facilities that would be connected within 12 months.

This requirement would continue until 40 percent or more of the affiliated provider's small business and residential load was being served by alternative electricity providers, or 60 months after competition started, whichever came earlier. An electric utility could choose to auction more than the required amount or to continue to auction that load for longer than the required time period. Any utility that owned less than 400 megawatts of installed generating capacity would be exempt.

Monitoring for market power abuse. The PUC would have to monitor for market power abuses, including actions restricting competition, such as discrimination in providing services or products, linking unregulated products or services to regulated ones, predatory pricing, preventing market entry, or collusion. The commission's remedies for market power abuses would include:

- seeking an injunction or civil penalties of between $1,000 and $5,000 for each day of each violation, as authorized by Utilities Code, chapter 15;
- imposing an administrative penalty as authorized by chapter 15; or
- suspending, revoking, or amending a certificate or registration.

Separating utility activities. By the start of competition on January 1, 2002, each electric utility would have to separate each of its business activities into individual units — a power generating company, a retail electricity provider,

and a transmission and distribution utility — so that personnel, information flow, functions, and operations were separated. Utilities could do this by:

- selling generating assets to completely independent companies;
- creating different affiliates, allowing ownership to remain with the parent company;
- creating separate, non-affiliated companies; or
- creating separate transmission and distribution utilities.

Market power mitigation plan. An electric utility or power generating company owning and controlling more than 20 percent of the generating capacity in a power region would have to file a market power mitigation plan with the PUC by December 1, 2000. This would be a written proposal for reducing ownership and control of installed generating capacity through such means as auction, sale, exchange of assets, or other means. The PUC would have to consider the impact of the plan on stranded costs, competition, the public interest, the company's federal income taxes, and whether the company was likely to receive the reasonable value for selling the assets. If the PUC had not approved a company's plan before January 1 of the year it was to take effect, the PUC could order the company to auction entitlements.

Affiliate code of conduct. CSSB 7 would require the PUC to adopt rules governing transactions between a transmission and distribution utility and its affiliates to avoid market power abuse. Affiliated companies would be prohibited from transferring confidential information, creating opportunity for preferential treatment or other unfair competitive advantages, creating customer confusion, or creating significant opportunities for cross-subsidization of affiliates. The PUC also would have to establish a code of conduct for electric cooperatives and municipally owned utilities on anticompetitive practices.

The PUC would not have authority to review or approve transactions between or among municipally owned utilities, river authorities, special districts created by law, or other political subdivisions.

Supporters say: Restructuring would not produce a competitive market automatically. Electric monopolies have major built-in advantages over newcomers, including customer loyalty, name recognition, and inertia of customers when it comes to changing brands. Existing electric power

monopolies will start the competitive race with an overwhelming advantage in markets where they have long been the only supplier of power.

CSSB 7 would provide tools to limit market power so that competition would benefit all participants. The bill would ensure that no single electricity provider had more than 20 percent of the generating capacity in a power region. CSSB 7 also would include a strong code of conduct to reduce the chance of affiliated electric businesses sharing information and preventing other companies from competing for customers.

The bill would ensure fair competition by requiring utilities to divide their business activities into separate entities, and it would give utilities flexibility in meeting this requirement.

Opponents say: CSSB 7 would place an arbitrary and unnecessary 20 percent cap on the amount of generating capacity that any one company could own and control in Texas. Consumers would be hurt by this cap because efficient competitors would be punished. Every owner of generating facilities would be prohibited from growing beyond the 20 percent cap. Relatively inefficient competitors would be rewarded because they would retain customers they otherwise would lose to more efficient competitors.

Analysis of many competitive markets clearly indicates that robust competition can exist even where some competitors have much more than a 20 percent market share. Many companies, such as Federal Express, Gillette, and Coca-Cola all have significantly higher market shares than 20 percent, yet those industries' markets are highly competitive.

Utilities oppose any requirement that they sell off assets because this could result in heavy federal income tax bills. Allowing holding companies for separate affiliates would be difficult for regulators because it would require oversight of the interactions between affiliate companies.

CSSB 7 would not adequately protect against market power abuses, and the bill's provisions would be in place only through 2007. After that, electricity providers would have no regulation to prevent them from dominating the market.

CSSB 7 would allow utilities to meet the requirement that they separate business functions by allowing them to set up affiliates that would remain under the same holding company. The process to monitor for abuses and remedy them would be time-consuming and expensive for regulators. The bill should require utilities to set up completely separate companies.

The two largest utilities in Texas, which control 68 percent of the generating capacity needed to meet demand on the hottest days of the year, could control prices. While CSSB 7 would try to limit market power to 20 percent of generation, the bill would allow cogeneration units and units that were not operational to be included in capacity calculations. That gives them an unfair advantage, because this generating capacity is not part of the retail market.

The big utilities could dominate the market through name recognition, and while the bill would require that they separate functions, they still could operate under the same brand name. This would give them enormous competitive advantages over new, lesser-known electricity providers. The bill would not allow the PUC to deduct this value of incumbency from a utility's stranded cost recovery amount.

COMPETITIVE MARKET STRUCTURE

Independent system operator. Each power region would have to establish at least one independent system operator (ISO), approved by the PUC, that would be independent of any electricity producer or seller. The ISO would ensure:

- access to the transmission and distribution systems for all buyers and sellers of electricity on an equal basis;
- reliability and adequacy of the regional electrical network;
- that information relating to a customer's choice of retail electricity provider was conveyed in a timely manner to persons who needed it; and
- that electricity production and delivery were accounted for accurately among the generators and wholesale buyers and sellers in the region.

The Federal Energy Regulatory Commission would have to approve a regional transmission organization for a power region outside of ERCOT.

All market participants would have to comply with ISO rules and procedures. The PUC could revoke, suspend, or amend a certificate of registration or impose an administrative penalty not to exceed $5,000 for each day a violation continued or occurred.

Metering and billing. When competition began, the transmission and distribution company affiliated with the former monopoly utility would have to continue to provide metering and billing services. Metering and billing services for residential customers would not be open to competition until at least 40 percent of the company's customers were being served by alternative electricity providers, or until September 1, 2005, whichever came later.

Beginning on January 4, 2004, metering services provided to commercial and industrial customers would be open to competition.

Transmission and distribution. The transmission and distribution company affiliated with a former monopoly utility company would remain regulated by the PUC. All retail electricity providers would have to pay a non-bypassable charge to use the transmission and distribution system.

Supporters say: CSSB 7 would create a structure that would allow a smooth transition to a competitive market and would allow that market to flourish. The ISO would ensure fair and open access to the system. The PUC's role would evolve from a regulatory agency to an oversight agency.

Competition in metering and billing for residential customers should be delayed until the 40 percent threshold had been met. This would ensure that residential consumers would have both competitive metering and billing at the same time they had competitive choice of electric provider, eliminating confusion.

Opponents say: Competition in the metering and billing business for residential customers should not be delayed. Retail electricity providers should be able to provide competitive metering services to all customer classes at the same time to eliminate confusion.

UNIVERSAL SERVICE AND LOW-INCOME PROGRAMS

System benefit fund. CSSB 7 would create a system benefit fund to subsidize lower electric rates for low-income people, to establish customer education programs, and to make up property tax losses to school districts. The fund would be financed by a non-bypassable fee not to exceed 50 cents per megawatt-hour. Municipal utility and electric co-op customers would not have to pay the fee unless they opted into the competitive system.

CSSB 7 would provide assistance to low-income electric customers that would include reduced electric rates and targeted energy efficiency programs in coordination with existing weatherization programs. Retail electricity providers could not charge customers a fee for participating in the low-income program.

School funding loss mechanism. CSSB 7 would require part of the systems benefit fund to compensate school districts for their losses in property taxes through August 31, 2007. The Texas Education Agency would have to determine the amount necessary to compensate school districts for lost revenue resulting from the loss in value of electric generating assets due to the onset of a competitive market. The PUC would have to transfer that amount from the system benefit fund to the foundation school fund for distribution to school districts that incurred such losses.

Provider of last resort. The PUC would have to designate a provider of last resort by June 1, 2001, for areas of the state in which customer choice would be in effect. The provider of last resort would have to provide a basic retail service package at a fixed rate that could not be discounted to any customer requesting it. The provider of last resort would be responsible for ensuring that customers could receive the basic package, with no interruption in service, in the event that a provider failed to provide such service.

The PUC could solicit bids from utility companies seeking to be designated the provider of last resort. If no retail electricity provider applied for the designation, the PUC could require a retail electricity provider to become a provider of last resort as a condition of receiving a certificate to serve that particular service territory. The PUC also could redesignate the provider of last resort according to a schedule it deemed appropriate.

Supporters say: Even though they use less electricity than other residential

customers, poor Texans with incomes at or below 125 percent of the federal poverty level spend from 13 percent to 44 percent of their total incomes on utility payments. CSSB 7 would ensure that low-income Texans would get electricity at affordable rates.

The provider of last resort would ensure that customers who did not choose an alternative electricity provider still could buy electricity at fair prices. The provider of last resort would ensure that if an electricity provider no longer could serve its customers, those customers would be transferred to the provider of last resort without an interruption in service.

CSSB 7 would give the PUC the authority to allow retail electricity providers to compete for designation as the provider of last resort. This would give competitors the chance to bid to serve these customers if they wanted to.

Opponents say: The system benefit fund would cost more than $100 million per year to subsidize rates. Electric rates in Texas already are lower than the national average. Subsidizing rates for some people would increase the cost for everybody else.

Customers who did not affirmatively choose an alternative provider at the start of competition should not be doled out arbitrarily to competitive providers. This would amount to “state-sponsored slamming” and would disregard customers’ choice to remain with their affiliated retail electricity provider.

Other opponents say: The low-income provisions of CSSB 7 are not strong enough. Vulnerable elderly people and families have an especially difficult time paying electric bills during the summer, when the heat increases usage. Lower rates and energy efficiency would minimize bills so that customers with limited incomes could afford to pay electric bills.

Rural electric customers could be subject to higher rates because it costs more to provide them with electricity. Rural Texans now served by investor-owned utilities should not have to pay higher electric rates because of restructuring. The system benefit fund could be used to offset the higher cost of providing people in rural areas with affordable electricity.

The provision requiring retail electricity providers to make sure 5 percent of

their energy load served residential customers should include a requirement to serve a minimum percentage of rural customers as well. It also could require that rural customers be served at comparable rates to urban customers. The goal of restructuring the electric utility industry is to benefit all customers, yet rural Texans could be left out.

CSSB 7 should require the provider of last resort to be chosen on the basis of competitive bidding. If the affiliated retail electricity provider were granted this designation, that provider would be granted a large customer base at the start of competition. This would save the company millions of dollars that it otherwise would have had to spend to lure that many customers on its own. If regulators designated that company as the provider of last resort without competitive bidding, the value of that designation should be recognized. That company should have to offset its estimated stranded costs by the value of the customers it got by being the provider of last resort.

RELIABILITY

CSSB 7 would charge the independent system operator (ISO) with establishing and enforcing procedures to ensure the reliability of the regional network. The ISO would have to account for the production and delivery of electricity among generators and all other market participants. ISO procedures would be subject to PUC oversight and review.

The PUC would have to establish reliability standards and take appropriate enforcement action as needed. Utilities would have to maintain adequately trained personnel and could not neglect rural areas, small communities, or low-income areas. Reliability standards would have to take into account the frequency and duration of service interruptions and the average response time to customer service requests.

Supporters say: CSSB 7 would maintain the reliability of Texas' current electricity system by continuing the regulation of transmission and distribution. The bill also would set new guidelines for the PUC to use as it developed reliability standards to manage a retail electric market. Immediate action is needed so that progress can be made to develop infrastructure needs, such as new generating, transmission, and distribution facilities. Uncertainty about the future of electric regulation in Texas is impeding the construction

of new generating facilities. Without clear public policy like CSSB 7, Texas could face energy shortages.

The bill also would establish an ISO to manage the region's electricity system. The ISO would be accountable for the reliability of the regional network and would ensure that generating businesses would coordinate successfully with transmission and distribution companies.

Opponents say: Planning to ensure reliability in the generation, transmission, and distribution of electric power is much easier when regulators have to deal with only a few monopolies. Mechanisms for managing physical transactions along the network of electric wires are complex and become even more so when the number of different companies using the network, or power grid, increases.

The existing transmission system is not designed for retail competition. With more players in the market, regulators would find it harder to monitor companies to make sure they met reliability standards.

Capacity also is an issue. Regulation protects monopolies from losing money when they build excess capacity that is needed to deal with fluctuating demand. For example, they can build plants that sit idle for months until demand for air conditioning goes up in the hot summer months and still make a profit because regulators allow them to build these costs into rates. The increased number of market participants competing to provide low-cost service could make it difficult to ensure sufficient reserves of generating capacity to meet customer needs.

Planning for transmission facilities needed under retail competition should be done more carefully. From planning to completion, providing major transmission lines takes from five to ten years. Under CSSB 7, retail competition would begin in less than three years.

CUSTOMER PROTECTIONS

CSSB 7 would require the PUC to provide protections for retail customers before competition began on January 1, 2002, including the right to:

- safe, reliable, and reasonably priced electricity;
- protection against service disconnections in extreme weather or in cases of medical emergency or nonpayment of bills for unrelated services;
- privacy of customer consumption and credit information;
- bills presented in a clear format and in understandable language;
- the option to have all electric services on a single bill, except for instances where multiple bills were allowed for customers of municipally owned utilities and electric cooperatives;
- information in a standard format allowing customers to compare prices and services offered;
- protection from discrimination;
- accuracy of metering and billing;
- information in English and Spanish and other languages as necessary concerning rates, terms, and conditions of service and the environmental impact of certain generating facilities;
- information in those languages concerning low-income assistance programs and deferred payment plans;
- protection from unfair, misleading, or deceptive practices;
- protection against billing for services not authorized or provided;
- impartial and prompt resolution of disputes with companies; and
- the same quality of service after restructuring that was provided as of December 31, 1999.

The PUC would have to maintain a “no-call” list for utility customers who did not want to be contacted by telephone solicitors about electric service. The PUC would have to determine the fee for customers who wanted to be on the list, but it could be no more than $5.

Customer education. CSSB 7 would require the PUC to develop and implement an educational program by January 1, 2002, to inform customers about customer choice of electricity providers, low-income programs, and the pilot program. The education program could not be targeted toward areas served by municipally owned utilities and electric co-ops that had not adopted customer choice. As part of ongoing customer education, the PUC could provide information about specific retail electricity providers, including instances of complaints against them and records relating to quality of customer service.

Supporters say: CSSB 7 would give the PUC ample authority to establish

consumer safeguards, including protections against "slamming," the unauthorized switching of a consumer's electricity provider, and "cramming," adding unauthorized charges to a consumer's electric bill. The bill also would ensure that customers got all the information they needed to choose their electric provider in language they could understand, and assurance that customer consumption and credit information would be kept private.

Customers would benefit by being allowed to sign up for a statewide "do not call" list. This would protect those customers from telemarketing solicitations urging them to switch electricity providers.

For competition in the retail electric market to be successful, consumers must be aware of their choices and the benefits of shopping for an alternative electricity provider. CSSB 7 would allocate funds from the system benefit fee collected on customers' bills to implement a statewide customer education campaign.

Opponents say: No apparent opposition.

RENEWABLE ENERGY AND ENERGY EFFICIENCY

CSSB 7 would set a goal of phasing in an additional 2,000 megawatts of generating capacity to come from renewable technologies by January 1, 2009. Renewable energy sources would include energy derived from the sun, wind, geothermal, hydroelectric, wave or tidal energy, or biomass products.

Renewable energy would not include energy resources derived from fossil fuels or waste products from inorganic sources. Retail electricity providers, municipally owned utilities, and electric co-ops that did not meet these requirements would have to buy renewable energy credits instead of directly owning or purchasing renewable energy capacity.

CSSB 7 would require transmission and distribution utilities to offer energy efficiency incentives. The PUC also would have to make sure that all customers had a choice of energy efficiency alternatives. The PUC would have to allow electric utilities to offer loans at below-market interest rates for energy efficiency investments. CSSB 7 would require retail electricity providers to include an "environmental impact" statement for generating

facilities on electric bills.

CSSB 7 also would set a goal that 50 percent of the generating capacity in the state after January 1, 2000, be produced using natural gas, in addition to the renewable energy requirement. The PUC would have to set up an energy credits program to meet this goal. The PUC would have the authority to enforce these provisions.

Supporters say: In a competitive market, utilities may have little incentive to invest in energy efficiency programs, which enable consumers to lower their overall costs by reducing their consumption. CSSB 7 would require electricity providers to get a specific amount of energy from renewable sources. The bill would require this amount to increase every two years so that by 2009, 2,880 megawatts of electricity would come from renewable sources. Today, about 880 megawatts come from these sources.

An overwhelming percentage of electric customers in Texas want more of their electricity to come from renewable sources. A poll conducted by TU Electric in

1998 found that 96 percent of the participants wanted the utility to invest in renewable technology.

Wind power is a $2 billion industry worldwide and is the fastest growing energy industry in the world. Texas has the best wind resources in the nation. Encouraging the use of renewable energy would attract investment firms that develop and operate wind power projects and that manufacture components to go into those projects.

The renewable energy requirement in CSSB 7 would enable Texas in the most efficient and effective manner possible to take advantage of its exceptional resource base and to respond to the popular support for renewable energy.

Opponents say: All electricity generation should be based on the market. Renewable energy is more expensive and therefore is not a cost-effective way to produce energy. Requiring utilities to use this more expensive energy would increase electric rates for customers. Wind and solar plants cannot produce the same amount of energy as more traditional types of generating

plants.

Building wind farms or solar energy generating facilities requires a source of backup energy from a traditional source. This duplicates generation and further increases costs. The environmental impact statement required by CSSB 7 is intended to depict generation from fossil fuels, coal and natural gas, as dirty and unhealthy. This statement could include listing emissions information and "health" effects as well. Such language would mislead customers into thinking that fossil fuel plants are not operating under safe environmental guidelines and controls.

Tracking the environmental impact of a particular facility on a customer is an impossible task. Electricity moves at the speed of light, so it is impossible accurately to trace electrons from power plants to a residence or business. Trying to list the source of the emissions and their environmental impact would only confuse and mislead customers.

Other opponents say: CSSB 7 would set as a goal that 50 percent of the state's generating capacity be fueled by natural gas beginning in 2000. This could violate federal law. The Federal Trade Commission Act regulates so-called proper consumer claims. The law says that a product cannot be called something it is not to make it sound better. Natural gas is not considered a renewable or "green energy" by any standard. This provision of the bill could be considered an unqualified claim.

This provision also could violate the international General Agreement on Tariffs and Trade, which prohibits favoring a domestic product over a foreign product. This provision specifically would require Texas natural gas to be used.

RIVER AUTHORITIES AND MUNICIPALLY-OWNED UTILITIES

Customer choice. CSSB 7 would exempt municipally owned utilities and river authorities operating a steam generating plant on or before January 1, 1999, from competition in the electric utility industry, unless the governing body decided to opt into the competitive market. Municipally owned utilities would not be allowed to reverse a decision to enter the market.

A utility that did not opt into competition could not compete in areas outside its service territory. The utility would not have to provide access over its transmission facilities for service to retail customers in its service area.

CSSB 7 would require a municipal utility that opted into competition to designate itself or another entity as the provider of last resort for customers in its service area. The provider of last resort would have to provide a standard package to any customer unable to obtain service from a retail electric provider. A utility that decided to offer customer choice could choose to continue to control metering and billing within its service area.

Municipally owned utilities that opted into competition would not have to separate services or functions of the utility. However, the utility would have to maintain separate books and records of its operations from those of the operations of any affiliate.

A municipally owned utility that owned or operated transmission and distribution facilities would have to set rates that complied with PUC open-access rules. The utility would have to file those rates with the PUC before the 90th day competition began for its service area.

If the PUC received a complaint by a retail electricity provider and found that a municipal rule, order, or action was anticompetitive or did not allow for nondiscriminatory access to distribution facilities or customers, the PUC would have to notify the utility. The utility then would have three months to remedy the anticompetitive behavior.

Municipally owned utilities could establish their own rules for consumer protections and safeguards that accomplished the same goals as the PUC's rules for investor-owned utilities.

Securitization. Municipally owned utilities and river authorities could securitize up to 100 percent of their stranded costs, as determined by the governing body. Municipal utilities would have to operate under rules and procedures established by the governing body, and the PUC would not have authority to regulate their recovery of stranded costs. River authorities would have to operate under PUC rules and procedures.

PUC jurisdiction. The PUC would have jurisdiction over municipally owned

utilities only in the following cases:

- to regulate wholesale transmission rates and service;
- to regulate certification;
- to regulate rates on appeal;
- to establish a code of conduct;
- to establish terms and conditions for open access to transmission and distribution facilities for utilities opting in to competition;
- to require collection of the system benefit fee and to administer the renewable energy credits trading program; and
- to require reports necessary for the PUC to maintain reliability of the system or to monitor market power.

Municipal power agencies' recovery of stranded costs. Cities that had participated in creating a municipal power agency under Utilities Code, chapter 163, on or before August 1, 1975, could recover stranded costs if they decided to opt in to competition. The member city's governing body would have to set the non-bypassable charge to recover the stranded costs over no more than 16 years.

CSSB 7 would require a municipal power agency to sell its electric facility to pay off its debt.

Supporters say: Municipally owned utilities generally are governed by city councils or citizens' boards. Some cities use revenue from their utilities to subsidize other municipal programs. Competition would end these subsidies, possibly leading to increases in local taxes. CSSB 7 would preserve local control for the 75 municipally owned utilities in Texas.

Suburban cities should not be allowed to opt into competition on their own if they are served by a municipally owned utility now. Citizens of a suburban city can petition the city council to vote to opt into competition. Allowing suburban cities to opt out on their own also could allow them to escape paying their fair share of stranded costs the municipally owned utility may have.

Opponents say: All customers should have the opportunity to choose their electricity provider at the same time. Customers living in areas served by a municipally owned utility would miss the opportunities and savings brought

by competition.

Cities being served by another city's municipal utility should be allowed to opt into competition on their own. Suburban cities should have the same rights as a city that owns a utility to opt into competition.

Residents of cities surrounding a city with a municipally owned utility cannot vote for members of the city council that would make the decision to opt into competition in the electric utility industry. CSSB 7 would prevent these citizens from receiving any of the benefits of restructuring.

ELECTRIC COOPERATIVES

Customer choice. CSSB 7 would exempt the 73 Texas rural electric cooperatives from competition in the electric utility industry unless the governing body decided to provide customer choice. A subsidiary of an electric co-op could not provide energy outside of its service area unless the co-op offered customer choice inside its service area.

If an electric co-op decided to provide customer choice, the PUC would have jurisdiction to establish terms and conditions for access by other electric providers to the co-op's distribution facilities. The PUC could not prohibit co-ops or related entities from sharing officers, directors, or employees.

The PUC could not regulate the recovery of stranded costs. Electric co-ops could securitize up to 100 percent of their stranded costs, as determined by the board of directors.

CSSB 7 would require an electric co-op that opted into competition to designate itself or another entity as the provider of last resort for customers in its service area. A co-op that decided to offer customer choice could choose to continue to control metering and billing within its service area.

Electric co-ops that opted into competition would not have to separate functions. However, the utility would have to maintain separate books and records of its operations from those of the operations of any subsidiary and would have to ensure that the rates charged for electric service did not include any costs of its subsidiary.

An electric co-op that owned or operated transmission and distribution facilities would have to set rates that complied with PUC open-access rules. The utility then would have to file those rates with the PUC before the 90th day competition began for its service area.

A utility that did not opt into competition would be prohibited from competing in areas outside its service territory.

PUC jurisdiction. The PUC would have jurisdiction over electric co-ops only in the following cases:

- to regulate wholesale transmission rates and service;
- to regulate certification;
- to establish a code of conduct;
- to establish terms and conditions for open access to distribution facilities for utilities that provided customer choice; and
- to require reports necessary for the PUC to ensure public safety and to maintain reliability of the system or to monitor market power.

If the PUC received a complaint from a retail electricity provider and found that an electric co-op providing customer choice had engaged in anticompetitive behavior, the PUC would have to notify the co-op. The utility then would have three months to remedy the anticompetitive behavior.

Supporters say: Rural areas, the typical market for co-ops, can be more expensive to serve because more equipment is needed to reach a smaller population per square mile. Because costs of service are higher, rural residents fear that for-profit companies could “cherry-pick” larger business customers, ignoring residential consumers and leaving farm and ranch families with even higher bills. Electric cooperatives should be exempt from electric utility restructuring.

Opponents say: The customer protections required by CSSB 7 would not apply to customers in areas served by electric co-ops, even if they opted into competition. CSSB 7 would require co-ops to develop their own customer protections, but the bill would not require co-ops to provide the same level of customer protections as for customers of other electric providers.

MISCELLANEOUS PROVISIONS

Natural gas tax exemptions. CSSB 7 would exempt natural gas from the severance (production) tax and the well-servicing tax if the gas were produced from wells drilled after January 1, 2000, and used by power plants to make electricity.

Supporters say: This provision would promote development of the state's natural gas resources, create jobs, and provide an inexpensive fuel for power plants. It would be good for Texas industry and would promote use of a safe, clean fuel that is good for the environment.

Opponents say: This provision would give preferential treatment to one particular type of generating plant and energy source. Competition should rely on market forces to determine use of electric generating fuels. This also would give one particular industry a windfall while costing taxpayers an estimated $130 million in fiscal 2000-01, including $97 million from general revenue and

$32 million from the foundation school program. The losses to the state would increase each year after that.

General Land Office. CSSB 7 would allow the General Land Office to sell electricity to state agencies, institutions of higher education, public school districts, or political subdivisions of the state. The state could compete with utilities during the rate-freeze period and with retail electricity providers upon the start of competition. In a municipal or co-op service area not offering choice, the state could not sell electricity to more than 2.5 percent of the incumbent utility's total retail energy load.

Displaced workers. CSSB 7 would allow utilities to include in their stranded cost estimates reasonable employee-related transition costs incurred and projected for severance, retraining, early retirement, outplacement, and related expenses for the employees. The PUC would have to require that a generating facility that was sold or transferred to a new owner be operated by the same operating personnel for at least two years.

Other. CSSB 7 would provide that all utility services, including transmission and distribution services, provided to the state would have to include applicable stranded costs and system benefit fees.

CSSB 7 would establish a legislative oversight committee composed of six legislators to monitor the effectiveness of electric utility restructuring, review PUC legislative recommendations, and make comments on proposed PUC rules relating to restructuring.

NOTES:

The Senate of SB 7 would restructure the electric utility industry in essentially the same way as CSSB 7. However, the two versions contain substantial differences.

Allocation of stranded costs. Under the Senate version, the allocation of stranded costs would be based on the rate per kWh each customer class paid. This would mean that residential and small business customers would pay a greater percentage of stranded costs.

Rate cut. The Senate version would give all customers a 5 percent rate cut at the start of competition instead of the 6 percent cut in CSSB 7. In both versions, the affiliated electricity provider would have to charge the discounted rate as its price to beat for three years and could not charge rates higher than this for five years.

Customer choice. CSSB 7 would include more provisions to guarantee that residential and small business customers had choices of alternative electric providers. The Senate version would not require retail electricity providers to serve 5 percent of their energy load to residential customers, as in CSSB 7.

Market power. The Senate version would not require utilities to "unbundle" their generation, transmission/distribution, and retail service businesses, as CSSB 7 would require. However, the Senate version would grant the PUC broader authority to address market power, including the authority to adopt rules to govern transactions or activities between a transmission and distribution utility and its affiliates.

Grandfathered emissions. The Senate version would allow utilities to include capital costs to reduce or offset air pollution from an electric power plant in their stranded cost determination. The improvements would have to be an essential component in either achieving compliance with federal clean air standards or obtaining a permit from TNRCC. The Senate version would not require any specific reductions for nitrogen oxides or sulphur dioxide nor place a cap on total regional emissions, as in CSSB 7.

Renewable energy. The Senate engrossed version would set different goals for renewable energy in Texas. Each retail provider would have to obtain 3 percent of its annual capacity requirements from renewable energy by January 1, 2009, instead of a set amount of 2,880 megawatts by that date, as in CSSB 7.