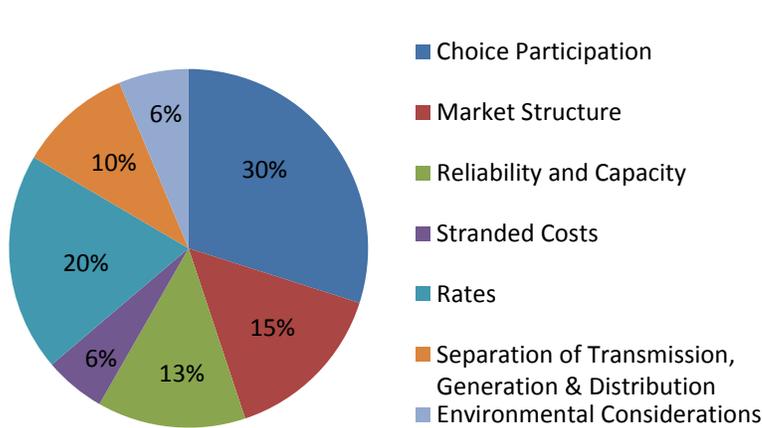


# Readying Michigan to Make Good Energy Decisions – Electric Choice

## Executive Summary

The 26 electric choice questions posted on the Ensuring Michigan’s Energy Future website garnered 114 responses. The comment summary pie chart presents an overview of comments received at the website.

*\*Please note, the number of responses used for the pie chart is slightly higher than 114 as some of the responses related to more than one section.*



**Where Michigan Is Today:** PA 286 of 2008 provides that “no more than 10% of an electric utility’s average weather-adjusted retail sales for the preceding calendar year may take service from an alternative electric supplier at any time.” There is a single exception in the law that

allows an iron ore mining or processing facility to elect an alternative supplier of electricity. As a result of legislation (PA 141 of 2000 and PA 286 of 2008), Michigan currently exhibits characteristics of both a regulated and deregulated market and is commonly referred to as a hybrid structure. Transmission and distribution of electricity is not normally impacted by a customer’s choice of electric supplier; what the current Michigan system does is allow a minority of customers to select an alternative generation supplier.

### Choice Participation

- From 2001 to 2008 choice participation was not limited (often referred to as a “full customer choice” system) as provided by 2000 PA 141 (PA 141). During this time, the level of choice participation ranged from three percent to 20 percent of utility load.
- Presently, five utilities experience active choice participation. With the exception of one of these five utilities, all are at the 10 percent choice participation cap implemented with 2008 PA 286 (PA 286).
- Although most states throughout the country operate under full regulation, the utilities cite a historically high level of customer choice participation at 12 percent of U.S customers and 22 percent of electric load, attributed to recent low wholesale power market prices. Additionally, they report that an increase in the choice cap would reduce the financial stability of utilities and therefore investors’ willingness to make long-term investments, including investments in new generation.

- Energy Choice Now comments that the actual record of utility financial solidity in restructured, competitive states stands in stark contrast to the Joint Utilities Response of allegations of financial challenges.

### Upper Peninsula Developments

- Choice development in the Upper Peninsula was slow to develop, but has recently ramped up. The current choice law, (MCL 460.10a(1)(d)), provides that any customer operating an iron ore mining facility, iron ore processing facility, or both, located in the Upper Peninsula of this state shall be permitted to purchase all or any portion of its electricity from an alternative electric supplier, regardless of whether the sales exceed 10% of the serving electric utility's average weather-adjusted retail sales.
- As a result of a combination of customers including the iron ore mines selecting an alternative supplier in the summer of 2013, WEPCo immediately lost approximately 85% of its Michigan load.
- WEPCo recently requested to suspend operations at the Presque Isle Power Plant in Marquette in 2014. MISO analyzed the removal of the plant from the electric grid and reports that the plant must continue operating to maintain reliability of the power system on Michigan's Upper Peninsula. MISO and stakeholders will consider alternatives to the plant, and WEPCo is currently in discussions with MISO regarding compensation to keep the plant operating.

### Market Structure

- Regardless of whether electric generation is regulated or deregulated, regulation continues for transmission and distribution services. For instance, transmission and distribution services remain monopolies, and the public risk involved in having a limited number of electricity providers typically leads states to continue to require oversight of the utility sector. For instance, PA 141 requires all alternative electric suppliers (AES) to be licensed by the Michigan Public Service Commission (MPSC).
- Broadly speaking, there is agreement that while there are a number of market forces that could impact the current market dynamic toward selection of incumbent or alternative energy providers (such as EPA regulations, renewables, shale gas production and high prices), regulatory policy is one of the main factors that could change the market dynamic for choice.
- In order to ensure that no one is "cut off" from service due to the inability to find a company that will take them as a customer, all states have a way of effectively forcing companies to serve. In regulated states or in Michigan's hybrid system, that role is served by the monopoly (or in Michigan's case, the incumbent) utilities. In states with fully deregulated generation, they have statutes requiring a provider of last resort, or a default supplier, or both. These alternatives vary in their operation.

- Similarly, all states have continued programs to assist low-income customers in some fashion. The utilities report that issues related to uncollectibles and low-income customers are present under both regulated and deregulated structures with additional challenges in serving low-income customers in a deregulated market. Some commenters suggest a purchase of receivables program in addressing uncollectibles and state that low-income customers should have equal opportunity to experience savings through a restructured electricity market.
- General comments suggest taking a look into markets where introducing competition has been successful.

### Rates

- The utilities report that even in today's low natural gas price environment, electric rates are 30% higher on average in deregulated states than in regulated states. Because most of those states were higher-cost prior to selecting a deregulated structure, however, causation should not be inferred.
- Historically, Michigan's rates are usually at the national average or above it. The only time in recent history that Michigan's rates have been noticeably below the national average occurred from 2000-2008; that approximately matches the time Michigan's statute provided for 100% choice. However, for five years (2000-2005), there was a legislatively-mandated rate cap, and in the remaining years of that time (2005-2009), the rates rose sharply every year, a trend that continued after the 2008 energy package was passed that created the current system.
- Some commenters suggest that market mechanisms are the most efficient at addressing change in prices and that market systems, such as wholesale auctions, can help mitigate rate volatility. Other commenters suggest that a deregulated market results in increased price volatility. Because of the large number of factors that can affect utility rates and markets, and the limited universe of "experiments" (i.e. states), it is difficult to determine a causal relationship.
- The utilities report that a survey of residential and small-business customers in Michigan and other states indicate that they place the most value on price stability and predictability. Severstal North America (Severstal) points out that large industrial customers place a higher value on lower power costs.
- Additionally, the utilities report that the free option to switch to choice costs remaining utility customers approximately \$300 million per year. Other commenters report that it's impossible to comprehend the full extent to which a customer in Michigan has been economically burdened because of the 10 percent cap due to the fact that there are very few policies to ensure pricing visibility in Michigan, and that Michigan electric bills have become unduly complex.
- Some commenters report that fully competitive retail markets create lower electric bills that decrease the cost of doing business and cost of living, which eventually attracts new

businesses to Michigan, while the utilities report that new long-term supply investments will bring new jobs and expand the tax base in Michigan.

### Reliability and Capacity

- As described in the “additional areas” report, sufficient generation is necessary to assure system reliability (keep the lights on for everyone).
- Some commenters argue that reliability is not negatively impacted by electric choice and electric choice suppliers may be better suited to respond to ever changing market conditions. Other commenters argue that regulated systems are more reliable because regulation is more conducive to new generation investment.
- MISO and utilities are jointly responsible for maintaining electric reliability and do this by establishing, following, and enforcing rules and procedures. Each utility and electric choice supplier must make a showing to MISO each year that it has sufficient supply to meet the peak demand for the upcoming year in order to comply with MISO’s tariff.

### Stranded Costs

- In general, “stranded cost” refers to the decline in the value of an asset as a result of a change, such as a regulatory change or a market change. When there are fewer customers or no customers “guaranteed” to an incumbent utility, they may have stranded costs due to a now-“oversized” system that they were required to maintain.
- A change in electric choice policy may or may not result in stranded costs. Stranded cost considerations become greater as Michigan moves towards full deregulation and lessen as Michigan maintains current policy or moves toward full regulation.
- All states that transitioned from a regulated to a deregulated structure have varying methods used to estimate and recover stranded costs. The issues have proven to be highly contentious and have been aggressively litigated.
- In Michigan, stranded cost and securitization surcharges are assessed to full service and choice customers. Some commenters report that these costs have been substantial for choice customers representing up to 10% of a large choice customer’s total electric bill.
- These same commenters report that utility recovery of stranded costs has allowed utilities to compete in the electric market and therefore there is no need for a cap on choice participation, and also state that shifting ratepayer risk related to new generation to competitive suppliers would support the financial stability of utilities. The utilities report that the remaining customers are facing a much higher cost due to the 10% choice option (\$300M).

### Separation of Transmission, Generation and Distribution

- For the most part, the electric industry remains fully integrated and regulated. Even deregulated states only required or encouraged the utility to divest or separate their

generation assets (leaving the regulated transmission and distribution assets with the utility).

- Michigan’s structure is unique in that distribution assets are owned by utilities and fully regulated by the MPSC. Transmission assets are owned by stand-alone companies (for example, ITC, METC and ATC). Generation assets are a mix of utility and independently owned facilities, with the latter being less common.
- The utilities report that once generation is divested it is extremely difficult to re-create a fully regulated, integrated model.
- An MPSC report found that “the implementation of structural separation of generation and distribution would lead to higher customer costs.” The MPSC further stated that it “did not receive any evidence that further separation of generation and distribution is necessary or desirable.”
- Some commenters report that separation of transmission and distribution in Michigan has had little impact and that the greatest impact would be to separate generation assets from the distribution business. Additionally, they report that through a properly administered transition, the regulated function of Michigan’s utilities can remain financially stable while the generation function transitions to market with a fair opportunity to compete with other providers of generation services.
- ITC Holdings reports that structural separation has improved overall transmission reliability, transmission efficiency, service restoration and regulatory compliance. The separation has made transmission planning independent from both local and regional perspectives and not influenced by market participants.
- COMPETE Coalition states that while complete divestiture of assets provides the preferred and cleanest separation of wires and supply, it is not required for a successful retail choice program.

#### Environmental Considerations

- Some commenters report that while there are a vast number of future events that could affect affordability, reliability, and environmental protection, a fully competitive market is the best system to effectively and efficiently handle the myriad of potential catalysts.
- The utilities report that the 10% cap reduced the uncertainty of unlimited switching and supports Michigan utility investment in reliable, clean energy for the future that includes the benefit of environmental protection.