# WASHINGTON GAS TESTIMONY TO THE STRUCTURE AND TRANSITION TASKFORCE OF THE ELECTRIC RESTRUCTURING SUBCOMMITTEE
**June 15, 1998**

## I. Determination of services to be offered on a competitive basis.

While it is clear that the generation of electricity is the focus of the restructuring debate, it is equally clear that other services both customer related and/or services ancillary to generation could be offered on a competitive basis. All or some subset of these services could be rebundled to suit the consumers' energy needs. In fact, these electricity services could be packaged with others related to natural gas, propane, and/or fuel oil to create a total energy portfolio. Energy suppliers will offer products and services such as, retail real-time pricing, weatherproof bills, and design build as part of a tailored package.

Washington Gas suggests the following to be considered for competitive services:

A. Customer related services

1. Customer billing and marketing related activities

B. Services ancillary to the Generation of electricity
*These services are further out on the horizon as competitive services and could be offered to or within the ISO.*

1. Operating Reserves – Reserve power utilized to deal with fluctuations in demand not sufficient enough to bring up a new generator.
2. Spinning Reserves – Energy required to maintain idling status of reserve generators that would be brought up in case there is sufficient need for additional generation.
3. Energy Imbalance – Energy required by the ISO in the event of a failure of a supplier to deliver adequate power to the power pool.

The incumbent utility should continue to be responsible for the construction, maintenance, and reliability of the distribution system.

## II. Market Power

Market Power exists when one or more dominant entities control the market through advantages gained in the non-competitive environment.

Market Power is typically segmented into two broad categories: *vertical* and *horizontal.* Each of these presents a unique set of concerns and could be mitigated utilizing distinctly different techniques.

The first step in dealing with the market power issue is a complete study that discloses the actual percentage of existing market dominance, strategic location of “must run” plants, and level of transmission constraints. The product of this analysis should be a clear set of open access rules along with policies that guide the transition to and ultimate formation of a truly competitive market.

### A. Vertical Market Power

Vertical market power refers to the ability of existing electric utilities to generate, transmit, and distribute electricity to customers. Regulators, customers and competitors are concerned that the presence of vertical market power could result in existing electric utilities erecting barriers to market entry or shifting costs and revenues among regulated monopoly services and competitive services in ways that distort efficient market operation in a restructured electric industry.

*Possible solutions include:*

a. Divestiture of generation assets (required or voluntary).
b. Structural separation of generation operations from other utility services.
c. Affiliated transaction rules and codes of conduct.

### B. Horizontal Market Power

Horizontal Market Power refers to the possibility that a dominant firm (or firms) could control production levels and manipulate market prices in an anti-competitive manner within a market region. *This type of market power tends to increase as a firm’s market share of generation increases in relation to the size of the relevant market.*

An initial concern is the existing concentration of generating assets by just a few owners. These owners control an inordinate percentage of the native generation with very limited transmission import capability thus limiting a new supplier's ability to enter the market.

Below are two specific actions by dominant generators that are destructive to efficient market operation:

1. Strategic withholding of capacity, and
2. Bidding generation into the power pool above actual variable cost.

Withholding generation at certain times, under certain market conditions could cause artificially high prices in a regional market. If the withholding operator has significant energy sales from other generating sources in the market, it could benefit significantly from artificially enhanced market price. This raises problems not only for market power abuses but also for reliability issues. Another market strategy is bidding generation into the market at prices significantly above marginal costs, particularly if it is by the largest supplier.

Other factors affecting the possibility of horizontal market power include:

1. Legislation mandating artificially lowered utility rates prior to the onset of competition
2. Incumbency itself could favor existing generators if customers are not given adequate information and assurances about new entrants.

*Potential solutions include:*

a. Promote a power pool operator that is independent (ISO/RPX) from the market participants and has the ability to oversee market operations and mitigate certain market power abuses.
b. Place a ceiling on ownership of generation capacity or the required divestiture of generation assets.
c. Development of additional transmission connections within and between regional power pools.
d. Consumer information disclosing the minimum requirements and rules of the road for new entrants.

## III. Provider of Last Resort/Default Provider or Supplier:

When addressing the issues related to subsidized services, load balancing and the provision of emergency utility services, the program requirements should be clearly defined and communicated to providers and customers, alike. These programs should exist only until full competition is in place when market forces should act to enhance reliability.

A. Provider of Last Resort - entity that provides a customer's power supply if a contracted supplier fails to deliver service as scheduled. This program should include the universal service activity to provide power to consumers in special need categories.

   1. The incumbent utility should act as the provider of last resort with the opportunity to charge a non-bypassable wires charge to cover its costs which include maintaining reasonable reserves for such a possibility.

   2. Suppliers that fail to fulfill their obligation to serve customers should pay a penalty or premium to the provider of last resort to cover their costs. This in combination with the wires charge should not exceed the incremental cost of providing this service.

B. Default Provider - the electric retail supplier that serves a customer that does not make a pro-active choice in selecting their energy provider.

   1. During the transition, which includes pilot programs, the utility should provide this service.

   2. Upon the onset of a fully competitive market, the default provider or supplier should be determined through a competitive bid process and would include appropriate requirements ensuring the ability of the default provider or supplier to serve (i.e., have the capability of supplying "firm" energy capacity).