Model State Legislation

Bill Summary and Handbook

Electric Utility

Restructuring

by

National Consumer Law Center

for

AARP

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About AARP

AARP is the nation’s leading organization for people age 50 and over. It serves their needs and interests through legislative advocacy, research, informative programs, and community services provided by a network of local chapters and experienced volunteers throughout the country. The organization also offers members a wide range of special membership benefits, including Modern Maturity magazine and the monthly Bulletin.

The AARP State Legislation Department provides assistance and resources to the Association’s volunteers and staff to expand their capacities for influencing state policy-making. The department’s goal is the adoption of state public policy that addresses the broad needs of older persons within an intergenerational context that promotes the well-being of all.

The Utility Issues Team of the State Legislation Department seeks, through legislative and regulatory advocacy, to protect the rights of residential utility consumers to reliable utility services, fair rates, privacy, fair marketing of services by utilities, adequate information on available services, and proper representation before state utility commissions.
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AARP Model State Legislation on Electric Utility Restructuring: Bill Summary and Handbook

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This model state statute on electric industry restructuring reflects the policy recommendations of AARP on retail electricity competition. As volunteers or friends of AARP, you can take this language to your state representatives, assemblymen, or senators and ask that this bill be used as the basis for electric industry restructuring in your state. You also can use specific sections of this model to strengthen existing bills, or restructuring legislation, in your state.

The policy recommendations of the Association reflect the input and views of AARP’s members across the country, through their state, regional, and national development of policy positions. These are the principles that have guided the development of this model statute.

AARP stands at the forefront of consumer organizations, presenting the perspective of the older person, the individual resi-
dential consumer. Small consumers face uncertainty with the onset of retail electricity competition. They require protection from higher rates, consumer scams, deteriorating customer service, and other risks of so-called "industry restructuring." This model state statute includes provisions to meet the risks that AARP has identified for the senior household, the small consumer, and the individual consumer at risk in a newly competitive market.

The model statute takes strong pro-consumer or pro-market positions on all the major issues that arise in the typical restructuring debate, such as (a) immediate rate reductions, (b) 50/50 sharing between customers and utilities of uneconomic costs ("stranded costs"), (c) mandatory divestiture of generation assets, (d) limits on the extent of sales a utility's marketing affiliate may make in the utility's service area, (e) required warrants for utility stock in exchange for any stranded cost recovery, and (f) strong consumer protections and protections against abuse of market power.

In some cases, the position reflected in the model language is stronger than language that has been included to date in statutes passed by the 13 states with restructuring legislation. Taken together, they present the strongest responsible pro-consumer positions. In legislation to date, a strong pro-consumer provision in a restructuring statute may be traded-off for a more pro-utility or pro-industry position. It will require judgment and an assessment of the situation in your state to determine where, if at all, to compromise these positions.

To Restructure or Not?

This bill is written as if your state has basically decided to introduce retail competition into the sale of electricity. The fundamental model is that the poles and wires would still be owned by one company, which would thus have a monopoly over the transmission and distribution of power in a certain geographic region (a "service area" or "service territory"). However, the actual electricity running through the poles and wires and being sold to the consumer would be sold by one of a number of competitive firms, probably separate from the utility owning the poles and wires. When policy makers talk about "restructuring" the electric industry, they usually mean introducing this retail competition into the sale of the electricity.
This model statute differs from most that have been passed to date in that it does not assume absolutely that the state will adopt retail competition. Like the Nevada statute, it sets up a list of conditions for whether the state regulatory agency will open up the power market to retail competition.

The reason for making the introduction of competition conditional is that there is a concern among many consumer advocates over the impact of retail electric competition. For example, competition exposes small consumers to the effects of "market segmentation," under which larger customers are the first to reap the rewards of the market.

The introduction of competition makes the most sense in states with high prices. Most of the states with utilities with very high electricity prices, relative to the national or regional averages, have already declared that competition should be introduced. The remaining states are starting to take a wait-and-see attitude. If prices are relatively low in your state, you may well question the wisdom of changing the industry structure that has achieved this result.

Your state regulatory agency or local utility should be able to provide comparative price information, so you can see where your state and your local utility rank in terms of electricity prices for various classes of customers. The U.S. Department of Energy's Energy Information Administration (DOE EIA) has a web site—www.eia.doe.gov—where a detailed summary of utility financial statistics is posted. You can get a sense of the relative rates of your state's utilities and others' from this web site.

If your state is on the path to implementing retail competition, this model statute provides a way to cooperate with that movement, while putting the burden on the pro-competition forces to demonstrate that their approach will benefit all consumers. It also tries to capture the needed protections for consumers against the risks of the market, and the risks that no real market will develop.

**Consumer Protection**

Many older persons must live on low and limited incomes, and AARP's policies reflect this reality by including provisions to protect those of low or fixed incomes. Older persons, along with other residential consumers, can find the chore of comparison shopping
a daunting task. Hard-sell marketers, and even scam artists, can prey on the unwary in any market, especially the market for a necessity like electricity. Supplier license requirements, consumer protections, anti-slamming, and anti-cramming provisions are among the protections reflected in the model statute.

Lower Rates—True Competition

The promise of lower rates for small consumers may not be delivered if some companies can corner the market for electric power and use their market dominance to keep out competitors. Thus, the model statute contains strong language to prevent any company, including today’s monopoly utilities, from having undue market power in a competitive electric industry.

Total electricity prices for many years will be dominated by the so-called “stranded costs” of today’s utilities. These uneconomic costs were rung up by the utilities to build power plants or contract for power at prices higher than the cost of new facilities today. The model statute does not assume that utilities will be fully paid for 100 percent of these uneconomic costs. Rather, the statute provides for a sharing of costs. In addition, in exchange for ratepayers funding half of the utilities’ stranded investments, the statute provides for a sharing of the company’s prospects for future profits. Much as the federal government received stock warrants from Chrysler as a condition of that bail-out, the model statute provides for shares in the utility’s future good fortune, in exchange for customer payment of the uneconomic costs of the past.

The statute contains a number of other provisions designed to protect consumers from the risks of electric industry restructuring. While you may not be able to see every provision enacted, the model language should help in strengthening the protections enjoyed by the consumer.
This handbook should help you to understand how the model state statute was put together. It will also explain some of the choices that were made in selecting these particular provisions.

Most of the language for the statute has been drawn from statutes passed by the 13 state legislatures that have enacted electric industry restructuring as of the summer of 1998. The fundamental organization of the statute, and many of the specific provisions, are modeled on the Maine restructuring statute. Footnotes for each provision will help you locate the closest language for that section from an actual statute that has been passed into law. Some provisions have been offered in various states, but not yet enacted. Other provisions were drafted by the authors to deal with issues important to older persons. In these cases, the provisions try to present “state-of-the-art” protections for the small and vulnerable consumer.
The handbook goes through the model state statute section by section. Sometimes it will not be clear why a certain provision is included. Other times, the statutory language is so technical that its meaning is not instantly apparent. The handbook will discuss these clauses and explain the more arcane provisions. Ideally, once you have read through the statute and this handbook, you should have a pretty good idea what the various sections are intended to accomplish.

There are three appendices to the model bill. Appendix I provides model language for the “retail marketing area” (RMA) concept championed by some consumer advocates in Ohio. The RMA concept is a way of introducing new electricity suppliers to consumers at the beginning of competition, while ensuring that consumers do not face higher bills. Appendix II sets out an alternative to Section XXX-19, the stranded cost recovery section. The stranded cost provisions in Appendix II are modeled on the Connecticut statute.

Appendix III is a list of the citations for state unfair and deceptive acts and practices (UDAP) statutes. In any electric restructuring legislation, advocates need to ensure that the UDAP statutes will apply to all electricity suppliers in the state.

Each state has its own way of writing bills, as well as a slightly different way of regulating public utility electric companies. The language used for different regulatory concepts or agencies in each state is a bit different, so the language used in the model statute is the most commonly used around the country. Also, the most common forms of industry regulation in place today and the most common forms of industry organization found around the country are assumed. But, of course, you will have to take this model and lay it next to your state’s public utility code (or compilation of statutes on the regulation of the electric industry) to locate the minor differences in language and conform this model to your state’s specific details of regulation.

The supplement at the end of this handbook examines the issue of competitive billing and metering. This model statute does not include language to make either of these services competitive.
Sec. 1. Findings

It is customary in a major piece of legislation to include findings of "legislative fact." In these findings, the legislature sets out its assumptions about the situation facing it that provide the context in which it is proposing the new policies of the statute. These are useful for those trying to understand why the legislature is taking the step of proposing new policies. Legislative findings are used by courts when they interpret the statute.

The findings proposed in this model statute are drawn from the New Hampshire statute. That state was facing a situation in which rates were among the highest in the country. A state with relatively lower electricity prices would have to determine what other factors exist that prompt the state to introduce retail competition.

- The findings proposed here do not include the strong language included in some existing restructuring statutes declaring retail
competition to be the best way to organize the electricity industry. It should not be necessary to make such a declaration in order to justify moving to a system of retail competition. Further, the proposed statute contains standards for determining whether to open certain aspects of the market to competition. The existence of these standards is a recognition by the drafters that policy makers cannot be certain of the future—the introduction of retail competition may not bring the benefits the legislature expects for it. For this reason, the findings do not declare that competition will definitely work to lower rates and improve services.

Sec. 2. [TITLE and CHAPTER OF CODE]

Sec. XXX-1. Purpose

Sec. XXX-2. Statement of Principles

Section 2 begins the restructuring statute proper. The material in this section will be transferred to the code of legislation when it is passed, and become part of the general laws of the state. Thus, a numbering system within a numbering system is required. The provisions that will become part of the code of the state are indicated here in the form “Sec. XXX-.” The first sections are the purpose of the legislation and the statement of principles.

No piece of legislation can cover every situation that will come up when the statute is implemented. It is important to spell out the principles the legislature wants the regulatory commission, the courts, and other agencies of government to follow when giving life to the specifics of the Act. This will help ensure that the will of the people is carried out when other branches of government interpret the general terms of the bill.

Principles to Protect Consumers, Not Abstract Principles

Most restructuring statutes passed to date have something like a statement of principles. Most of the principles set out in the model statute appear in some form in existing restructuring legislation. However, there are important differences between the principles suggested here and the average restructuring bill.

For example, most existing restructuring statutes take for granted that opening up the electricity generation market to retail com-
petition will produce tremendous benefits for consumers. They also appear to assume that competition for retail purchases of electricity will not produce greater risks than the present structure of regulated monopolies. That is, they take the benefits of any market called “competitive” on faith. And they assume, in effect, that what is good for the competitive marketers is good for the customers. Get it right for the competitors and the rest will take care of itself, is the message.

By contrast, the statement of principles here stresses issues of concern to consumers. It does not look at restructuring from the point of view of potential competitive electricity sellers, or even the large industrial consumer. Rather, it looks at restructuring from the point of view of the small consumer.

The principles hold up a standard of performance for the newly regulated industry. Affordable service, universally available, consumer protection from unfair practices, lower rates and true competition, reliable and high quality service—these are what consumers want from an electricity industry. Put together, these principles constitute a set of conditions that any organization of the electricity industry (monopoly regulation, wholesale competition, public power, retail competition, etc.) must meet.

“Burden of Proof” on Market Proponents

The model statute’s principles set out a test for whether a new industry structure will be beneficial to consumers. In effect, the model statute puts the burden on proponents of change to demonstrate that their new model will achieve the conditions required by customers.

These conditions, set out in the fifth principle in proposed code Section 2, must be met before the commission can declare that any part of the electricity business should be opened up to competition, and price regulation removed. The model statute does take a favorable view towards the prospect of retail competition for generation sales. There are a number of references in the findings, principles, and statement of purpose to this view. On the other hand, some aspects of the industry, like metering and billing, are not treated as presumptively competitive, and proponents must prove their case before the commission can open the door to retail metering and billing competition.
However, even retail generation competition does not get a free ride. Proponents of this new approach will have to prove to the commission that the conditions for competition are met before regulation of generation sales prices is eliminated in favor of market forces. This is essentially the approach being taken in Nevada, and the conditions for competition are largely drawn from that statute.

**Sec. XXX3. Definitions**

Every major statute like this—changing how a whole aspect of industry and government will function—requires a definitions section.

The model statute has a number of new terms that are used frequently in the Act. The definitions section will need to distinguish the various types of providers in the marketplace, since some requirements and opportunities apply to less than all the different providers.

*New Market Needs a Scorecard to Identify the Players*

This issue of distinguishing the players also applies to distinctions the definitions draw between existing (vertically integrated) electric utilities, and their successor companies that provide only transmission or distribution service. The statute also provides a basis for distinguishing transmission and distribution monopolies from affiliates who wish to provide competitive supplies of electricity after restructuring, to the extent this will be permitted, if at all. This is necessary in order to discuss and resolve the question of whether existing utilities may continue to sell power in the restructured world, and if so, whether they must set up a separate affiliate.

Issues of market power and the different obligations and opportunities that apply to affiliated competitors versus regulated monopoly poles and wires companies will be important in the new structure. For this reason, the definitions go to some lengths to separate out these different types of entities. This model statute assumes that utilities will be severely limited in continuing to perform both the monopoly transmission and distribution functions, and the competitive supply functions.¹

¹Model Section XXX-15 requires most generation-related assets to be sold, and forbids monopoly transmission and distribution utilities from owning such generation assets. Model Section XXX-16 severely limits the extent to which a large electricity utility that provides transmission and distribution service can provide

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As a result of the interrelated restrictions of the statute, a company that today owns generators, transmission lines and a distribution network (and sells power it generates to its customers) will in the future be permitted to retain the transmission and distribution network, own only a severely limited amount of local generation for restricted uses, and sell power it buys at wholesale to only a small portion of the retail customers in the area where it has its monopoly distribution network. Even those sales will have to be made by a completely separate affiliate with a strict code of conduct preventing the monopoly poles and wires company (and its customers) from cross-subsidizing the competitive marketing firm to the detriment of the distribution utility customers and the competitive electricity providers against whom the affiliate will compete.

Aggregation—Definition Limited to Value-driven or Customer-driven Entities

Some statutes distinguish various types of players in the new competitive markets, for example, including definitions for brokers, marketers, aggregators, generation suppliers, and the like. Aggregators are defined in the statute because the regulatory commission and the utilities are given specific responsibility under the Act to help consumers voluntarily aggregate their loads to buy electricity in the competitive market (Section XXX-4(C)).

All others who are in the various businesses relating to selling power to retail customers are gathered together under the definition “competitive electricity supplier.” There is no need to break these suppliers out into separate groups in this model statute. The obligations placed on competitive suppliers in the statute do not turn on the distinctions between brokers (who would not ordinarily own the power they are arranging to sell to customers), marketers (who similarly might not take title to the power), and generation suppliers who actually have title to power they resell, and so forth.

marketing services within its service territory. Model Section XXX-16 also limits the proportion of the region’s generation a firm or its affiliates can control and still market power in the state. And Section XXX-16 provides that to the extent the corporation is permitted to continue selling electricity, instead of just delivering it for others, it must do so via a separate subsidiary.
Under this model, the obligations of a competitive electricity supplier attach when an entity is in the business of selling power to retail customers. If the firm is a broker, it may be selling someone else’s power. Nonetheless, brokers, and all others who sell at retail, must be licensed (Section XXX-9) and must observe the consumer protection requirements of the statute (Sections XXX-10 through XXX-14).

Sec. XXX-4. Retail Access; Deregulation of Prices

Section XXX-4 is the core statement of the terms for introducing retail competition in electricity sales. It provides that customers will have the right to buy energy from competitive electricity suppliers, and utilities must deliver that power to the customers over their poles and wires, if the regulatory commission finds the conditions for competition have been met.

The conditions for competition are essential as a check to prevent jumping into competition without thinking through the pros and cons for the state, and making sure that competition will actually function in the relevant market to deliver the benefits intended:

Sec. 2(E) Conditions for Competition. Regulation of prices is necessary where competitive forces will not adequately discipline a market, where competition will jeopardize the safe and reliable operation of the integrated electricity network, and where segmentation of the market by providers will result in unfair discrimination in prices to different classes of customers. Accordingly, the commission shall determine that an electric service is a potentially competitive service only if it finds, after a public hearing, that provision of the service by alternative sellers:

(1) will not harm any class of customers;

(2) will decrease the cost of providing the service to residential and small commercial customers in this state and also increase the quality or innovation of the service to customers in this state;

(3) is a service for which effective competition in the market is certain to develop;
(4) will advance the competitive position of this state relative to surrounding states; and

(5) will not otherwise jeopardize the safety and reliability of the electric service in this state.

This formulation requires the regulator to be willing to express more certainty about the future market conditions than the Nevada statute language from which it is drawn. In principle, it is impossible to know the future. However, if the language merely requires a finding of "likelihood" of producing the benefits claimed, then there is no rigor to the standard. Thus, the effort here is to force some hard thinking about claims for the new market structure.

The process set out in the statute for evaluating whether the conditions are met requires the regulator to answer a series of questions about the structure of the competitive market and the likely impact of that structure on the extent of true competition and the resulting prices for services in that market.

Transition Dates and Transition Periods—Short or Long?

The statute provides for a target date for competition to begin, a few years after passage of the statute, so long as the regulatory commission has found that the conditions of competition are met. As of the transition date, most aspects of pricing would no longer be controlled by regulators.3

The transition period is intended to give time to set up the new market mechanisms that do not exist today. This includes the

3Because it is important in creating a working market, most statutes, and this model statute, provide that regulators will continue to have some measure of control over the terms and conditions of selling electricity, which includes not only consumer protections such as advance notice of termination and limits on the grounds for termination, but also limits on fees for switching, limits on late fees and unfair deposits, limits on the price that a designated default supplier can charge, and licensing limits on who may enter the business. The model statute, like other restructuring statutes, also requires clear apples-to-apples information for consumers about electricity price, among other things. But in a retail competition market, other than in the few situations explicitly set out, retailers will be free to ask what price they want for their power, and customers will be free to decide whether to buy it at that price, with no regulator to dictate what the price will be.
divestiture of a utility’s generation assets from its monopoly poles and wires (transmission and distribution) business, as provided later in the model statute.³

A transition period is also useful to existing utilities that benefit from having more time under the current monopoly regulation regime to write down their uneconomic assets and otherwise prepare for competition. For this reason, a long transition period is generally understood to be favorable to the utility, and worth something to them in the ultimate negotiation over the shape of the bill. On the other hand, customers who do not want to move quickly to a retail market may also see a benefit in a longer transition period. In such a case, of course, the question of whether the bill provides for rapid rate reductions becomes more important.

To summarize, utilities will want to keep current rates in place for as long as possible, and so will favor a longer transition period and a small or non-existent obligation to reduce rates.⁴ They may be willing to make concessions on eventual market power controls (such as mandatory divestiture of the generation business from the transmission and distribution business) in order to protect themselves from having to cut rates sharply, or open their systems to retail competition soon.

³If your state decides not to require divestiture, this reason for an extended transition period falls away. There may be other reasons—particularly if your state does not expect competition to come of its own accord to small customers, and the model chosen is thus one where everyone has the right to competition soon—but small customers will, in practice, take their power from the incumbent utility or the winner of the bid to provide standard offer power, at regulated standard offer rates.

⁴Be on the lookout for what appears to be a rate reduction, but actually is only a cost deferral. Some utilities may willingly agree to drop rates today by 10 or 15 percent, but only if they can defer any losses that causes them out to the future. This approach, unfortunately, has a great deal of appeal to some politicians, because they can claim to be getting a rate reduction for their constituents, and bank on the hope that no one will trace back later rate increases (or later inability to reduce rates to levels they should have reached) to the restructuring statute’s plan for loss deferrals. There are a couple of ways that such schemes are structured. For further information, contact Jerrold Oppenheim, National Consumer Law Center, Boston, Massachusetts.
Big customers and competitive marketers will be eager for a short transition period, so that they can quickly begin doing business with one another. Small customers will differ on whether they see retail competition as more of a promise than a threat. Those who think they will do as well as the big customers will agree that quick movement to competition is more important than near-term rate reductions. The majority of small customers, who see the risks as larger than the rewards, will want a long transition period with guaranteed and substantial rate reductions beginning as soon as possible. Both big and small customers will want to have strong protections against the incumbent utility keeping unfair control over the market, and preventing true competition from arising in the new world without price regulation.

In some states, the transition period to competition is separated from the stranded cost recovery period. And, conceivably, both may be separated from the period during which the present utility (or a supplier chosen by competitive bid) must offer a “standard offer” package of service to customers who do not wish to shop in the competitive market. However your state handles this question, the statute needs to be clear. And you need to understand the implication of the different periods for these various functions.

Aggregation
Section XXX-4 places considerable importance on what has come to be known as “aggregation.” Aggregation is a term that does not have a single, clear meaning across the country and among electricity restructuring experts. Generally, it means grouping customers together and supplying electricity to them (as opposed to each individual customer making a one-on-one contract with an electricity-generating plant to provide electricity to that customer).

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5 It can be argued that big customers do not care who they do business with, and would just as soon keep buying supply from the incumbent utilities, but they want to have the threat of competitive supply alternatives alive so that they can bargain their prices down.

6 Because of the way that electricity is delivered, if a customer is plugged into the grid, the customer gets power from the pool of all the output of all generators operating at the moment the customer turns on an electricity appliance.
The proposed model statute defines aggregation as follows:

B. Aggregate. "Aggregate" means to organize individual electricity consumers with common characteristics, such as geography, affiliation, or some other characteristics in common, into an entity for the purpose of purchasing electricity on a group basis.

C. Aggregator. "Aggregator" means an entity that aggregates individual customers for the purpose of purchasing electricity.

This model statute, then, uses the aggregation concept to refer to a grouping of customers around a common characteristic. An example might be a municipality that gathers together residents and businesses in the town and arranges purchases of electricity for those who live or do business in the town. Another example would be an automobile club that adds electricity purchasing services to its list of member benefits, and buys electricity for group members who choose to participate, or gets a discount from a chosen supplier who then contracts directly with participating members.

The model statute goes beyond permitting aggregation and includes a requirement that the regulatory commission and the regulated distribution utilities encourage and facilitate aggregation of retail customers. This provision is included to respond to a growing sense that for-profit electricity suppliers are not likely to find it profitable to market to small customers (residential and small commercial accounts). Aggregating customers around common characteristics, by affinity groups, municipal aggregation, or otherwise, is one option for enabling small customers to combine their purchasing power even where mass market suppliers do not see an opportunity to sign up individuals from the group on a retail basis.

In addition to the municipal aggregation and voluntary customer aggregation noted in this model statute, there are other forms of aggregation that have been suggested around the country. For example, the Connecticut statute provides that the state purchasing office will obtain electricity from competitive suppliers not only for the state’s uses, but also for low-income customers receiving home energy assistance.

There are a number of ways that aggregation can be accomplished. In effect, the competitive electricity suppliers, the default
suppliers, the municipal aggregation suppliers, those who offer the standard offer, and indeed anyone who sells at retail, all “aggregate” the loads of their various customers. The special push mandated by the statute is for consumer-initiated aggregation, particularly aggregations of small consumers. This is because there are greater barriers to consumer-initiated aggregation than to the grouping together of customers by other means.

In the case of standard offer, default, or municipal aggregation service, there is a ready-made group of customers that a supplier can make sales to, which lowers marketing costs and makes it more likely that competitors will come into the market to sell. In the case of marketers selling to individual customers, they are motivated to gather such customers together and take responsibility to supply them because the marketers will earn their revenues in that fashion. Consumer-initiated aggregators that need assistance in organizing themselves are likely to be made up of small consumers. Much as in the case of food cooperatives, such entities will require large investments of time and commitment to overcome the lack of funding and capital.

Sec. XXX-5. Reduction in Residential Rates; Standard Offer

Section XXX-5 is in some ways the heart of the model statute. This section provides that residential customers will get a 15 percent rate reduction within nine months of passage of the statute, and eventually a further 10 percent reduction, for a total rate reduction of 25 percent, whether they shop for power in the competitive market.

A number of states have imposed rate reductions (California—10 to 20 percent; Massachusetts—15 percent after divestiture; Illinois—10 to 20 percent, depending on the utility, by 2006). The reduction proposed in the model statute is steep and quick: 15 percent shortly after the statute takes effect, moving to a 25 percent reduction within a few years. It is likely that the amount of any near-term rate reduction will be a hotly contested issue in negotiations.

Steep Rate Cuts—Evaluating the Possibilities

You will want to know whether the scale of rate reduction proposed here is within the boundaries of reasonable expectations, considering the situation of the utilities in your state. The lower
your rates are today—relative to a regional average, for example—the more difficult it would be to achieve rate reductions along the lines proposed in this model bill (although even in the highest-cost states steep rate reductions may threaten the financial integrity of the utility). It will be helpful to have an idea of how these reductions compare to the proposals the utilities and others are willing to live with. Be on the lookout for proposals that would reduce rates today but have the effect of requiring ratepayers tomorrow to make the utility whole for any losses the near-term rate reductions cause it to experience.

To get a sense of these parameters, you may want to tap into the analysis being done in your state by the utility consumer advocate (if any), a utility watchdog group, the commission staff, or the major industrial customers regarding the financial situation of the utility, and the impact of various rate reductions. These will help put into perspective the likely claims of the utilities that they cannot withstand the level of rate reductions being proposed. It is also possible to trade an easing of the rate reduction demand for other concessions that may be more palatable to the utilities.

Note also that if the utility loses money in order to provide a rate reduction, it is similar in effect to a disallowance of so-called stranded costs—the uneconomic costs of power plants owned by the utility. Consumers care about rates, but they are mobilized by concerns about “bailing out” the utilities. On the other hand, utilities need to show Wall Street that they are recovering their capital costs, but might be able to agree to rate reductions, gambling that they can make up the shortfalls later.

Because the future is uncertain, there are many forecasts that are plausible. This in turn leaves room for bargaining about what will be fixed as policy into the future, and all sides may come away betting that their vision of the likely future will prove true and benefit them.

In the case of the model statute, the required bill reductions come off the total bill, not just the energy portion of the bill. Be careful when reading the language of statutes proposed in your state that the percentage reductions are stated in apples-to-apples terms. Utility bills historically are made up of base rates, and fuel or energy charges, and sometimes other surcharges or adjustments. If the statute talks in terms of reductions to base rates, this
is not as good a deal for the consumer—base rates can make up as little as one third of the bill, depending on the circumstances.

**Standard-offer Bid Process**

The model statute provides for a competitive bid process to select an alternate supplier to provide the energy portion of the bill. It is unlikely that such a bid process will result in a supplier willing to sell energy at a sufficient discount that the total bill will be reduced by the target percentage. For example, if energy is one third of the bill, to get a 10 percent reduction on the total bill, the energy portion would have to be reduced by 30 percent.

The model statute provides that the distribution utility shall continue to provide generation services under the standard offer if no competitive seller comes forward to offer service at a price low enough to produce the required rate reductions. The distribution utility need not own the generation supplies it uses to provide this power. Alternate stranded cost recovery language should be used in case the bids come in too high (see Appendix II).

**Financial Integrity—Warrants against a Brighter Future**

Such large rate reductions could in some cases jeopardize the financial integrity of the distribution utility. To provide for this risk, the model statute first permits the utility to petition the regu-

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7 The Massachusetts statute has utilities providing the electricity themselves unless they run into problems financially; the Maine statute bids it out and sees what happens. The choice to make here is competition or lower rates. Maine opted for certain competition in the hopes that over the long run it would produce lower rates. Massachusetts went for certain lower rates, with the expectation that competition would emerge eventually.

8 It is conceivable that a middle ground could be provided for in the statute, whereby if a competitive supplier bid to provide at least part of the standard-offer reduction, that supplier could win the bid, and the distribution utility would make up the balance of the rate reduction off the monopoly transmission and distribution rates.

*It could buy power on the wholesale market, through a mix of short-term and long-term contracts, and some reliance on the spot market, to make up its supply portfolio for the standard-offer sales. Utilities will resist being forced to divest their generation yet retain an obligation to serve. Remember, however, that if utilities hold on to their generation supplies, they may have undue market power. Also, a divestiture sale is one way of putting a market value on generation, for use in determining the amount of any stranded costs.*
latory commission for authority to take steps to mitigate the risk of such financial danger. If there is no way to mitigate this risk sufficiently, and still provide the required rate reduction, the statute allows the utility to petition the commission for funding from a Ratepayer Equity Trust Fund, established in the state treasury. This fund is made up of tax revenues from the sale of utility plant, statutory penalties, and income from investment of fund assets.

As in the case of the Chrysler bailout in the 1970s, if a utility must tap into the fund, the taxpayers who made the fund possible receive a legal interest in the future success of the utility. This legal interest comes in the form of stock warrants. They can only be exercised if the price of the stock goes up comfortably above the (presumably depressed) level at the time the warrants were issued. And the state would not actually hold any stock, but rather would exercise its right to buy the stock at the earlier (lower) price, and this would trigger an obligation on the part of the utility to buy it back at the present (higher) price, less a 5 percent grace amount.

By virtue of the mandatory price reductions, the financial integrity backstop of the fund, and the warrants to taxpayers against future recovery and success, ratepayers get immediate relief from high rates, utilities' financial integrity is guaranteed, and the taxpayers who guarantee that integrity obtain a claim on the future good fortune of a recovered utility.

Deciding if the standard offer is only transitional, and the terms of ending it, require careful thought. Competitive suppliers will demand a short term for the standard offer, arguing that the standard offer is anti-competitive and prevents them from getting into the market. In effect, they demand that prices be raised so that they can compete and, hopefully, lower prices in the future. Utilities would argue for a longer standard-offer position if the standard-offer price was high enough to let them earn a good return, and if they were permitted to provide the power themselves. This would, in effect, leave them in place as the vertically integrated supplier for most of the customers. The model statute undercuts this incentive by allowing for the standard-offer energy component to be bid out.

The model statute has two alternate versions of language to create such a fund.
Sec. XXX-6. Limit on Spread between Residential and Other Rates: “Cap the Gap”

Another cornerstone of the model statute is the section limiting the spread between residential rates and both industrial rates and average rates for the region. Rates for small customers have been rising faster than those for larger customers. The model statute, patterned after a similar provision in the Connecticut legislation, caps this gap in rates. It also puts a check on the spread between residential rates and the average price in the region as a whole.

The commission is also required by this section to examine the impact of restructuring on residential rates, and on the affordability of electricity to low-income consumers. The results of this ongoing review are to be forwarded to the legislature annually, under Section XXX-27.

Sec. XXX-7. Municipal Aggregation

Section XXX-7 is an adaptation of the municipal competitive franchise statute passed in the Massachusetts restructuring bill. It paves the way for a municipality (or group of local governments) to conduct a bid process and select a competitive electricity supplier for their town or city. The supplier so selected would not only supply the governmental offices but would be the presumptive supplier for the electricity customers in the municipality. Consumers would have an opt-out right.

The particular version of the legislation offered here places great emphasis on the leadership of local government in energy efficiency and renewable power. It also permits the aggregation of natural gas customers, not just electricity customers. It could theoretically be extended to telephone service, just as well.

It is important when considering local government aggregation that the procedure for adopting this tool not be made onerous. If the procedural requirements for selecting the municipal aggregation model are made too cumbersome, this approach to aggregating loads and achieving public goals will not succeed. Municipal aggregation can combine the best of local control and competitive markets, while allowing small customers to band together for greater purchasing muscle.
An opt-out (or automatic enrollment with open enrollment options or windows) is essential to preserve the right sought by some customers and key stakeholders for individual customers to be able to choose their own supplier. Note that if the municipality does not have an automatic enrollment status for customers who do not opt out, it may be prohibitively expensive to run a viable municipal aggregation process. The assumption made here, then, is that the democratic decision of the representatives of the community sufficiently reflects the will of the community that requiring those not in agreement to opt out is fair.

Sec. XXX-8. Licensing Competitive Providers; Consumer Protections; Enforcement

One of the major questions facing legislatures in restructuring the electric industry is the extent to which competitive electricity suppliers will be subject to government controls on their business practices. It is well understood that prices for sales of power will be deregulated. However, most states have decided that competitive electricity suppliers must be licensed. That is, they must meet minimum standards in order to do business selling electricity in the state, they must agree to observe requirements set out by the state, and they risk losing their right to sell electricity if they violate these requirements.

The model statute follows the typical path in charging the public utilities commission with the responsibility to vet applicants and issue licenses. It is possible to give this responsibility to the attorney general’s office, an existing consumer protection agency, or a new electricity supplier licensing agency. However, it makes sense to give the job to the commission, which in most states has licensing authority for other types of utility providers (e.g., telephone companies), and is knowledgeable about the industry.

The model statute reflects the understanding that licensure is an important tool in protecting consumers. Information that the applicant must provide the commission includes:

- evidence of its ability to provide reliable service;
- evidence of its record in other states regarding consumer protection complaints;
• evidence of its compliance with specific requirements of the state;\textsuperscript{11}

• evidence of the applicant's technical and managerial capacity to provide the services proposed in compliance with all applicable laws and policies of the state;\textsuperscript{12}

• a description of the areas where the applicant intends to offer service and the types of services it intends to offer, and, if the applicant intends to serve residential or small business customers in an area smaller than the entire service area of an existing electric utility, evidence demonstrating that so doing will not result in unlawful redlining; and

• disclosure of the names and corporate addresses of all affiliates\textsuperscript{13} of the applicant.

Together, these provisions give the commission information about the applicant's fitness and ability to provide reliable service, on a non-discriminatory basis, with adequate consumer protections.

The statute permits the commission to require applicants to post a bond. This would provide a fund from which consumers could be compensated if the company fails to provide service (or to provide service in accordance with its rate schedules), or harms a consumer by violation of the consumer protection requirements of the statute.

Section XXX-8 also contains a provision intended to prevent so-called "bottom-feeders" from entering the state and targeting vulnerable customers with high-pressure sales tactics, poor service, and high prices. Acting in low-income and minority neighborhoods where many perceive they have few alternatives, such firms follow in the tracks of loan sharks and "phone sharks." The model statute empowers the commission to weed out such predatory

\textsuperscript{11}(such as the minimum level of renewable power resources in the supplier's portfolio)

\textsuperscript{12}(with the ability to argue that it is serving customers with large demands, and a resulting sophistication and market power, and thus need not have fully developed retail customer service branches, for example)

\textsuperscript{13}Affiliates include holding companies owning the stock of the applicant.
suppliers before they set up a business in the state. The statute permits the license to be revoked for price-gouging practices, and a bottom-feeder that does not get a license is doing business unlawfully and may be put out of business.

Another protection against consumer scams is the prohibition of misleading names, such as "Don’t Know." A telephone competitor is actually getting people to switch to its service in some states by having telemarketers ask "which telephone company do you prefer," and when they get the predictable answer from many customers, "don’t know," taking that as authorization to switch to their service.

The general licensure section also provides for limited duration licenses, conditional licenses, and the like. It empowers the commission to adopt rules to govern the licensure process.

Sec. XXX-9. Consumer Protections; Obligations of Competitive Electricity Providers

The model statute sets out in considerable detail consumer protections that all suppliers must observe. The statute provides that these protections apply to both electric and gas services.

Existing Protections as the Floor

As in the case of the Pennsylvania and Massachusetts statutes, the model statute provides that existing protections14 must continue at a minimum. State commissions have sometimes interpreted such a principle to mean that consumers are protected so long as one supplier observes all the existing consumer protections, and consumers can take service from this last-resort supplier if they run into trouble with their competitive supplier.

Some states (notably Connecticut) go further and recite that all suppliers must observe all current consumer protections. Where a statute simply says that existing consumer protection obligations apply to competitive suppliers, a commission can undermine the legislative intent by lax enforcement, or even inconsistent commission regulations. The model statute puts key consumer protections in the statute itself, leaving no doubt about what rights consumers

14 The model statute contains the "continue existing protections" statement, but does not stop there.
have. The model statute also makes it plain that violation of these protections is grounds for a supplier to lose its license.

**Spelling Out Consumers' Rights**

The model statute spells out consumer rights in a number of key areas: no disconnection from the distribution network for non-payment of a competitive supply, no prepayment or other unfair requirements, a prohibition on selling credit life or credit disability for residential bills,¹⁵ a right to return to the standard offer, a limitation on the charges for switching service, and prohibitions on redlining and other unfair discrimination.

These are specific consumer protections that experience in other industries has proven are necessary when moving to a competitive market. The statute also covers the timing of disconnections and contract terminations, extreme weather hardship protections from disconnection or contract termination, limitations on back-billing in the case of erroneous underbilling, notice and receivership protections in the event a landlord defaults on a bill, and other specific consumer protections.

If your state has statutory or regulatory language that sets out other protections for electricity consumers today, or protections that are stronger or more detailed than those in the model statute, it would be beneficial to include them in the restructuring statute in your state. Connecticut, a state with a long tradition of enacting utility consumer protections in statute, rewrote all of its many detailed provisions to make it clear that they now will apply to protect consumers of competitive electricity supply. The benefits for consumers of having such explicit language in the statute are well worth the cost in terms of getting some help in identifying the rules and drafting them in legislative format.

The model includes these protections in the Connecticut statute:

- inaccurate billing, rebilling;
- termination of service for non-payment, when prohibited;
- notice of termination of residential service or contract, process;

¹⁵In other contexts, credit insurance has proven to be routinely overpriced and too often sold using hard-sell or misleading tactics.
• notice furnished tenants by utility regarding intended termination;
• petition for receiver of rents, hearing, appointment, duties;
• non-payment by absent spouse; and
• refusal of residential utility service.

The commission is empowered to define additional specific protections that are a condition of licensure, if circumstances dictate. Also, the commission is given some leeway to adopt its own procedural rules on dealing with license issuance or revocation. This makes sense, rather than trying to anticipate all the possible situations in a statute. In any event, any statutory rules on these procedures would have to track the specific Mini-APA\(^1\) or other due process norms of the state for analogous situations. (It is beyond the scope of this model statute, and unnecessary for the purpose, to catalog all the different varieties of procedures used for such licensing issues in the 50 states.)

Some states distinguish between rights of small consumers (e.g., those with a demand of 100 kilowatts or less)\(^2\) and larger consumers, who are presumably able to negotiate the package of specific rights they wish. You may find it necessary and acceptable to agree to a similar limitation.

**Sec. XXX-10. Consumer Protection: Recourse and Enforcement**

The model statute gathers together the primary tools for consumer redress in Section XXX-10. These include dispute resolution, ordering restitution, instituting enforcement actions, private rights of action, penalties, and cease and desist orders.

With regard to dispute resolution, the proposal here is to empower the commission to hear consumer complaints against

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\(^1\) Administrative Procedures Act at the state level, analogous to the APA at the federal level, setting out procedural requirements for promulgating regulations and rules, as well as conducting contested hearings in individual cases.

\(^2\) One hundred kilowatts is the instantaneous draw of electricity by a modest-sized commercial business.