

## I. Procedural History

In December 1996, the Advisory Staff issued a white paper pointing out the escalating debate over a radically different electricity market being proposed in the United States.<sup>1</sup> The white paper led the Alabama Public Service Commission (Commission) to establish a Staff Electric Industry Restructuring Task Force (Staff, Task Force) to explore the potential results of deregulating the electric industry for Alabama's ratepayers and the States economy. In particular, the Commission asked that the Task Force explore and ascertain whether, when and in what shape congressional action might prevail, what affect the Federal Energy Regulatory Commission's (FERC) Order 888 wholesale electric policies would have on Alabama, how Alabama should approach retail competition, and "all other deregulatory-initiated influences which may affect the future economy and consumer rates for Alabama."<sup>2</sup>

In October 1997, the Task Force issued its *Report and Policy Development Plan* which made the recommendation that a phased study of restructuring should be instituted by the Commission, with the ultimate goal of determining to what extent the public interest in Alabama would be affected by restructuring and competition in this state.<sup>3</sup> As a result of the *Report*, the Commission, in April 1998, established the instant docket, APSC Docket 26427, *In re: Restructuring in the Electric Utility Industry*. In June 1998, the Commission issued a Scheduling Order under this docket in which they posed a number of questions grouped under 12 Issue Areas. The Commission received and analyzed hundreds of pages of comments and reply comments from interested parties. As a result of the comments received and the analysis by the Staff, *Interim Report No.1* of the Staff Electric Industry Restructuring Task Force made recommendations concerning the issues and for the next phase of the investigation.<sup>4</sup>

The Staff *Interim Report No.1* recommended that the threshold matters of the Public Interest and the Jurisdiction and Role of Regulation by this Commission should be

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<sup>1</sup> Eugene G. Hanes, Federal Affairs Advisor, Advisory Staff, Alabama Public Service Commission, White Paper: *The Electricity Industry and Restructuring*. Internal Commission Communication, December 1996.

<sup>2</sup> Memorandum from Commissioners Sullivan, Cook, and Martin of December 13, 1996, "SUBJECT: The Deregulation of the Electric Industry."

<sup>3</sup> *Report and Policy Development Plan*, Staff Electric Industry Restructuring Task Force, October 10, 1997, p. ii.

<sup>4</sup> *Interim Report No. 1*, of the Staff Electric Industry Restructuring Task Force, September 8, 1999.

set for inquiry under the instant docket, and that other areas previously identified should be held in abeyance pending resolution of these two matters. On November 1, 1999, the Commission accepted the Staff *Interim Report No. 1*, and ordered that the matters of the Public Interest and the Jurisdiction and Role of Regulation by the Commission be set for Inquiry.<sup>5</sup> By order issued February 9, 2000, the Inquiry was set for the week of April 17, 2000.<sup>6</sup> At the conclusion of the Inquiry, the parties were afforded a total of 40 days to file supplemental written comments.<sup>7</sup>

The Staff Task Force has analyzed and researched the thousand plus pages of transcript, exhibits and supplemental comments generated from the Inquiry, and with this *Report on the Public Interest and Role of Commission* makes recommendations and observations concerning the issues at hand.

## II. Discussion of Issues

The issues of the public interest and the role and jurisdiction of the Commission relative to electric industry restructuring are interrelated. If the restructuring of the electric utility industry is found to be in the public interest, does the Commission have the current statutory authority to accomplish the task? The reverse is that if the Commission does have the authority, is the restructuring in the public interest in Alabama at this time? As was noted by Alabama Power Company in their post-Inquiry comments, quite unsurprisingly the positions advocated by the parties at this stage in the investigation are the same fundamental positions previously expressed.<sup>8</sup> The Staff has relied heavily on these initial comments of first impression relating to Regulation, since most information provided since that time has been a repeat of the initial responses, or an attempt to discredit other parties replies. Broadly speaking, the commentators in this docket can be classified in four categories: consumers (industrial, commercial and residential), competitive suppliers, utilities (investor owned, municipal, cooperative and public

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<sup>5</sup> Docket 26427, Adoption of Report and Scheduling Order, November 1, 1999.

<sup>6</sup> Docket 26427, Scheduling and Procedural Order, February 9, 2000.

<sup>7</sup> Docket 26427, Procedural Order, April 5, 2000; Order, May 15, 2000.

<sup>8</sup> Alabama Power Company, *Supplemental Comments of Alabama Power Company: Docket 26427*, May 30, 2000, p. 2.

power), and other interested parties with special areas of concern. Their responses and concerns are similar by category.

The Staff will first discuss the role and jurisdiction of the Commission, and then examine the matter of the public interest.

#### **A. Jurisdiction and Role of the Commission**

The following are the questions concerning Regulation put forward for comment in the Commission's order of June 15, 1998:<sup>9</sup>

1. What is this Commission's authority to institute retail electric competition? Discuss jurisdictional conflicts between the State and the Federal Energy Regulatory Commission (FERC) and any enabling state and federal legislation you foresee to be necessary to allow the PSC to authorize and implement retail competition in Alabama.
2. Define the role of the PSC under the retail competition process.
3. How can the PSC ensure a smooth transition while avoiding any adverse impacts of restructuring?
4. Why would competition in Alabama be preferable to maintaining our current low cost status under a regulated environment? What will we achieve through competition? Since Alabama is a low cost state, discuss any improvements likely to be made to the current system by restructuring of the electric industry. What positive attributes of the current structure should be retained in a restructured industry?
5. Would there be net benefits in the long and short run for **each** customer class in Alabama under a restructured industry? Describe and provide evidence of these benefits.
6. What are the positive and negative effects on the Alabama economy associated with a move to a restructured industry and associated with maintaining the *status quo*?

After examining these questions and answers, only questions one through three are relevant to the topic of Regulation, while questions four through six more properly address the issue of the Public Interest. The Staff will treat the responses accordingly.

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<sup>9</sup> Scheduling Order, APSC Docket 26427, June 15, 1998, p. 3.

The first question that must be answered is what authority the Commission has to implement changes in the manner that electric utilities are regulated in Alabama. The answers of the parties are fairly unanimous regarding the Commission's authority to order a shift from cost-based regulation of a monopoly to some form of market controlled retail competition.

In general, the parties that responded to the question related to this Commission's authority to institute retail electric competition do not believe that the Commission has the unilateral authority to implement retail competition without statutory change and policy guidance from the Legislature.<sup>10</sup> The Attorney General (AG) says that at the outset the Legislature must set forth, through enabling legislation, the state policy objectives that will be accomplished. In addition, they say that certain amendments to state statutes and policies will be needed.<sup>11</sup> The Alabama Industrial Energy Consumers (AIEC) say that in all probability the Alabama Legislature will be called on in conjunction with any restructuring.<sup>12</sup> Alabama Power Company (APCO) states that the Commission does not presently have authority to institute retail competition. Their opinion is that the Legislature long ago made the policy decision to replace competition in the electric power industry with comprehensive legislation, and only the Legislature can change this fundamental policy determination.<sup>13</sup> The Alabama Rural Electric Association of Cooperatives (AREAC) believes that absent a mandate by the Legislature, or all encompassing Federal legislation, the Commission does not have the authority to institute electric competition.<sup>14</sup>

The Alabama Municipal Electric Authority/Electric Cities (AMEA) does not comment on the Commission's authority to institute direct access, but they do remind all participants that the Commission has statutory limitations as to its authority over electric systems owned and operated by municipal corporations. In addition, they believe the Legislature would have to amend certain statutes concerning the certificate of

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<sup>10</sup> See *Interim Report No. 1, op. cit.*, Attachment B: Regulation, for a Staff summary of the Initial and Reply comments of the parties to the questions posed by Staff.

<sup>11</sup> AG Initial Comments, p. 10.

<sup>12</sup> AIEC transmittal letter accompanying Initial Comments, p. 2.

<sup>13</sup> APCO Initial Comments, p. 8.

<sup>14</sup> AREAC Initial Comments, p.22.

convenience and necessity process.<sup>15</sup> The North Alabama Public Power Association/Tennessee Valley Public Power Association (NAPPA/TVPPA) has no comments on the Commission's general authority over utilities it regulates, but remind the Commission that Federal law would preclude effectively including their members in retail restructuring at this time.<sup>16</sup>

Two differing opinions were offered by the Alabama Retail Association (ARA) and Dynegy, Inc. (Dynegy). ARA puts forth the proposition that the Commission can allow a customer to be served by another power distributor if the current power distributor is not providing satisfactory service. By declaring that any distributor that does not allow for competitive supplies is providing unsatisfactory service, the Commission could then authorize other distributors to provide service.<sup>17</sup> Dynegy states that it has not researched the specific Alabama statutory authority of the Commission, but believes that the debate centers on a commission's legal authority to "mandate" retail access. While the Commission may not be able to mandate restructuring, Dynegy believes a commission could "permit" retail access by developing incentives that encourage utilities to open their systems to competition.<sup>18</sup>

As to the matter of jurisdictional conflicts between the State and the Federal Energy Regulatory Commission (FERC), or enabling federal legislation required, the parties answers are varied. The one FERC/State jurisdictional problem mentioned by the most parties was the conflict between FERC Order 888 and State jurisdiction over transmission facilities.<sup>19</sup> FERC has stated that if a state has unbundled retail service, then FERC will assume exclusive jurisdiction over the transmission function. This would leave the Commission with authority over local distribution facilities, defined by FERC in a seven part test, on a case-by-case basis. FERC has said that they will defer to states' recommendations to where the jurisdictional lines should be drawn, as long as the seven

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<sup>15</sup> AMEA Initial Comments, p. 10, citing §37-1-34, *Code of Alabama*, 1975: "Nothing contained in...(Title 37) shall...confer upon the commission the power...to regulate and supervise any utility owned and operated by any municipal corporation..." Also see p. 12.

<sup>16</sup> NAPPA/TVPPA Initial Comments, p. 10.

<sup>17</sup> ARA Initial Comments, p. 3.

<sup>18</sup> Dynegy Initial Comments, p. 6.

<sup>19</sup> In general, see the Initial Comments of ARA, p.3; ALAGASCO, p. 2; AMEA, p. 11; APCO, p. 9; and, AREAC, pp. 22-23. FERC Order 888, *Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, Appendix G, 61 Federal Register 2725.

factors are complied with. While all parties cited represent this as a potential jurisdictional problem, ARA asserts that FERC has set reasonable and appropriate guidelines for dividing jurisdiction between federal and state regulators and this has not proven to be a source of significant conflict in other states.

Regarding the need for Federal enabling legislation, the parties that responded did not feel that Federal enabling legislation is necessary to implement retail competition in Alabama. Several areas of concern were pointed out by the parties that they felt would require some Federal action to help clarify positions and level the playing field among competing players in the market. The areas of concern are related to the Public Utility Holding Company Act (PUHCA), the Public Utilities Regulatory Policies Act (PURPA), existing and future public power financing and regulatory schemes, and control of and access to the transmission system.<sup>20</sup>

The commentor's positions on the role of the Commission under the retail competition process and during the transition to a competitive process are also fairly unanimous. Most parties felt that the exact role of the Commission could not be stated without knowing how the utilities and industry will be structured.<sup>21</sup> In spite of this caveat, as a general proposition the parties went on to enumerate many matters that the Commission could become involved with during a transition and after a transition to competitive markets. The topics mentioned were: consumer education about the new regime, as well as consumer protections<sup>22</sup>, certification of new suppliers<sup>23</sup>, ensuring open and equal access to the transmission network and encouraging the formation of ISO's<sup>24</sup>, and addressing horizontal and vertical market power issues, while retaining traditional regulation over the distribution function<sup>25</sup>. Several parties stated that the Commission should take a slow and deliberate approach to restructuring, while studying actions in other jurisdictions to avoid adverse or unintended consequences of restructuring.<sup>26</sup> ARA

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<sup>20</sup> In general see the Initial Comments of AG p.12; AIEC, p. ii; ALAGASCO, p.2; AMEA, p. 11; APCO, p. 9; ARA, p.3; and, AREAC, pp. 12, 22-23.

<sup>21</sup> In general, see Initial Comments of Dynegy, p. 7; APCO, p. 10; AREAC, p. 24; and, TVPPA, p. 11.

<sup>22</sup> In general, see Initial comments of AG, pp. 12-13; AIEC, p. 6; DYNEGY, p. 9; ALAGASCO, p. 3; APCO, p. 10; and, EPSA, Initial Comments, p. 4.

<sup>23</sup> In general, see Initial comments of AG, p. 12; AIEC, p. 6; ALAGASCO, p. 3; and, APCO, p. 9.

<sup>24</sup> In general, see Initial comments of AIEC, p. 6; ALAGASCO, p. 3; AREAC p. 22; and, Bruno's, p. 3.

<sup>25</sup> In general, see Initial comments of AIEC, p. 6; AIM, p. 7; ALAGASCO, p. 3; AMEA, p. 12; AREAC p. 24; and, EPSA, p. 3.

<sup>26</sup> In general, see Initial comments of ALAGASCO, p. 3; AMEA, p. 13; APCO, p. 10; and, TVPPA, P. 12.

says that the Commission should develop the appropriate and necessary framework in which the market should be free to act, with only the minimum and most necessary regulation, because anything more impedes the market. They continue that the state needs a complete transition to competitive markets, because a free market and competition cannot coexist with a command and control monopoly.<sup>27</sup> Dynegy says that to accomplish this task, the Commission needs an adequate staff with the right skills, knowledge and experience, while taking an active role in the collaborative process.<sup>28</sup> AIM states that this should be done in a short transition.<sup>29</sup>

**It is the opinion of the Staff that the Commission can not mandate or otherwise allow retail competition or electric industry restructuring without state enabling legislation.** The policy of the Legislature was to put the Public Service Commission in place of competition in the electric utility industry beginning in 1915.<sup>30</sup> That was the mandate then, and that is the Commission's mandate now. In addition, the Territorial Franchise Act, §37-14, *Code of Alabama* 1975, and the Consumer Protection Act, §37-4, *Code of Alabama* 1975, are both testaments to the policy and will of the Legislature that the Commission continue the regulation of electric utilities under its jurisdiction in the manner originally proscribed. The Staff does not mean to indicate that these are the only Legislative changes that would be necessary, for a great deal of Title 37 would need revision, in addition to changes in other state statutory areas (such as taxes) that could be impacted by a change in Commission regulation. In addition, if it were the will of the Legislature that some change in the manner that municipals and cooperatives are currently treated should be made to include them in restructuring by the Commission, this would also require Legislative attention.

**In the matter of Federal conflicts and the need for Federal enabling legislation, it is the Staff opinion that Federal enabling legislation is not required to implement restructuring.** This is a matter that is currently reserved for the states. There are other matters that will require further Federal action to help eliminate inequities

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<sup>27</sup> See Initial Comments, ARA, p.4.

<sup>28</sup> See Initial Comments, DYNEGY, pp. 7, 9.

<sup>29</sup> See Initial Comments, AIM, p. 8.

<sup>30</sup> See *Staff Report and Policy Development Plan, op. cit.*, pp. 1 – 8.

and smooth the transition to competitive markets. Such issues as PUHCA and PURPA repeal or revision, ISO formation and operation, and the manner in which public power is treated will all require Federal resolution. The Staff believes that restructuring does not have to wait for Federal resolution of these matters to proceed with state efforts, but resolution of these matters will make for a smoother transition for all concerned. There are numerous Congressional bills pending that would address these matters, as well as pending resolution of some of these matters before FERC. The Staff should stay abreast of these situations and continue to provide input from the State perspective as necessary, and be prepared to incorporate any such changes into any plan proposed in Alabama.

**The Staff feels that role of the Commission both during and after any transition will be shaped by what form restructuring ultimately will take in Alabama.** There are new emphasis areas that will be required of Commission staff, regardless of the form, and these are areas that the Commission should be prepared to transition to along with the transition of the industry. There are many legitimate areas that the Commission will have to deal with during and after any transition.

## **B. Public Interest**

The following are the questions concerning the Public Interest put forward for comment in the Commission's order of June 15, 1998:<sup>31</sup>

1. Is electric retail competition in the public interest in Alabama?
2. Will electric retail competition be ready for resolution in Alabama over the next two to five years?
3. Which electric services should be open to competition?
4. If electric competition is found to be in the public interest in Alabama when should it be introduced? Should retail access be phased in over time, or should there be a flash-cut to retail access for all customers? Would it be in the public interest for one customer class to have direct retail access before another customer class? If a phase-in program is adopted, what would be accomplished during the phase-in?
5. If retail competition is found to be in the public interest in Alabama, and customers are permitted to choose whether to avail themselves of retail access, are some ratepayers naturally captive? Please identify the likely attributes of

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<sup>31</sup> *Op.cit.*, Scheduling Order, p. 2.

such ratepayers. Without any special requirements, what is the likely effect of retail competition on such customers? Should load aggregation be allowed, or required, to allow such customers to take advantage of retail Competition? Should retail marketing areas be set up and administered to bring direct retail access to captive customers?

In addition, Questions four through six under Regulation should be considered in this discussion.<sup>32</sup> Those questions were:

4. Why would competition in Alabama be preferable to maintaining our current low cost status under a regulated environment? What will we achieve through competition? Since Alabama is a low cost state, discuss any improvements likely to be made to the current system by restructuring of the electric industry. What positive attributes of the current structure should be retained in a restructured industry?
5. Would there be net benefits in the long and short run for **each** customer class in Alabama under a restructured industry? Describe and provide evidence of these benefits.
6. What are the positive and negative effects on the Alabama economy associated with a move to a restructured industry and associated with maintaining the *status quo*?

From the beginning of this investigation, the Staff has made certain preliminary remarks concerning the reasons for this investigation and the point from which we began. In addition, the Staff has made certain statements about the nature of the analysis and comparison they would make during this investigation. Those remarks need to be restated, prior to the discussion of the Public Interest.

In the Staff *Report and Policy Development Plan*, October 10, 1997, (*Plan*) the Staff observed in its Recommendations that “(t)he utility industry is in upheaval today as the last remaining monopolies are being deregulated. While some question the necessity for this, the driving forces appear too strong to be stopped. State and federal actions are moving toward the inevitable restructuring...”<sup>33</sup> That statement was true in 1997, and it is closer to reality today than ever before. Current actions before Congress and other Federal agencies lend substance to this statement and will add substance to the analysis of the necessity for Alabama actions concerning restructuring, both now and in the future.

The Staff also stated in its *Report* that “(t)he variety of electric industry restructuring activities in the states is not happenstance. It indicates in a very real way

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<sup>32</sup> *Op.cit.*, Scheduling Order , p. 3.

<sup>33</sup> *Op.cit.*, *Report and Policy Development Plan*, p.42.

that we in the south, and other low cost areas of the country, are protecting our ratepayers by refusing to rush to judgement because other states have chosen to do so. Our regulatory agencies have provided our region with low cost power. It would be a shame if years of hard work to keep power rates in check are negated...”<sup>34</sup> The Staff went on to say that “(a)bout the only thing everyone can agree on concerning this topic is that there will be winners and losers. Alabama is currently a winner under traditional regulation, with industrial, commercial and residential rates well below the national average.”<sup>35</sup> These statements were true when they were made, and nothing the Staff has seen or heard changes the fundamental truth behind those opening statements.

In the Staff *Interim Report No. 1*, the Staff said that any proposals to restructure the electric utility industry in Alabama would be weighed against an overarching principal that stated:

Consumers should have access to adequate, safe, reliable and efficient energy services at fair and reasonable prices at the lowest long-term cost to society. Structural changes in the industry should be encouraged only if they result in economic efficiency and serve the broader public interest.<sup>36</sup>

This is the criteria against which the Staff has weighed the Public Interest in restructuring Alabama’s electric utility industry at this time. In its Scheduling Order in this docket, the Commission also stated that “...properly documented empirical evidence is desirable and will be afforded deference by the Commission.”<sup>37</sup> In order to change the manner in which we now regulate to a more competitive market, and still retain our stated goal, it must be a move that will result in greater economic efficiency, and serve the broader public interest more than it is currently served. This is the crux of the debate, and is the point where the parties diverge in their opinions of what will serve the public interest, and what will lead to greater economic efficiency. As might be expected, the directions of the parties, after assuming all consumers must benefit, are in direct relation to their generally recognized economic interests.

The consumer parties that have filed comments or made presentations during our investigation have all been adamant: restructuring will greatly benefit the public interest

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<sup>34</sup> *Op. cit.*, *Report and Policy Development Plan*, p.42.

<sup>35</sup> *Op. cit.*, *Report and Policy Development Plan*, p.42.

<sup>36</sup> *Op. cit.*, *Interim Report No. 1*, p. 3.

by lowering prices and improving services for all Alabama consumers (if not in the short run, at least in the long run).<sup>38</sup> In order to convince the Commission that this is the correct path, these parties generally cite theoretical economic arguments<sup>39</sup> or historical/suggestive evidence from other previously regulated markets.<sup>40</sup> The only consumer party that strays very far from this position is the American Association of Retired Persons (AARP), who stated that “(u)nless there can be assurances that residential rates will drop or guarantees that the financial benefits of restructuring will be shared by all...not just the state’s largest customers, we do not see why residential customers should support restructuring the market at this time.”<sup>41</sup> As to what should be unbundled and when this process should start, the majority of consumer parties generally felt that the immediate opening of all services, with the exception of transmission and distribution, would be preferred, and five years would be more than adequate.

The parties to this investigation that would be considered utility interest were equally unanimous in their opinions of the public interest in this matter. First, they all agreed that all classes of ratepayers must benefit in the long and short run, and the benefits must exceed the direct and indirect costs to transition and restructure the electric industry in Alabama. Second, they state that there is no compelling reason or pressure at this time to rush into restructuring, given Alabama’s adequate, reliable and relative low cost electric services. They recommend that the Commission should take a slow approach and learn from the mistakes and successes of other states and federal programs, while allowing the wholesale market to mature. They suggest that non-partisan empirical studies should be performed, and that a two to five year study period would be adequate. A phase-in of restructuring was slightly favored over a flash cut. All agreed that generation would be competitive, while transmission and distribution would remain

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<sup>37</sup> *Op. cit.*, *Scheduling Order*, p. 2.

<sup>38</sup> In general, see: AARP, Tr. 17 – 20, 25; AF&PA Initial Comments, pp. 2 – 3; AG Initial Comments, pp. 2-7, Replies, pp. 1 – 20, Tr. 363 – 374; AIEC Initial Comments, pp. 1 – 5, Replies 1 – 3, Tr. 32 – 48; AIM Initial Comments, pp. 1 – 7, Tr. 484 – 518, Replies, pp. 2 – 20; ARA Initial Comments pp. 1 – 3, Replies, pp. 1 – 3; Bruno’s Initial Comments, pp. 1 – 3; FTC Initial Comment, pp. 4 – 9. (“Tr.” refers to the Transcript of the Inquiry held April 17 and 18, 2000 in this docket).

<sup>39</sup> AG Initial Comments, p. 6: Maloney, McCormick and Sauer; AIEC Initial Comments, p. 1: Resource Data International, Energy Information Administration.

<sup>40</sup> AG Initial Comments, p. 4: Crandall and Ellig; AIEC Initial Comments, p. 2: Crandall and Ellig; AIM Initial Comments, p. 2: Crandall and Ellig, p. 9: Moorhouse, p. 9: Thierer.

<sup>41</sup> AARP, Tr. 15.

regulated.<sup>42</sup> As with the consumer parties, theoretical economic arguments were put forth. These studies purportedly show an increase in costs for Alabama ratepayers and economy from a move to a competitive electric market in Alabama.<sup>43</sup>

The two competitive providers that made comments in this area believe competition is in the public interest, if the restructuring program is implemented properly. Dynegy feels that there must be a liquid wholesale market before retail markets are workable, and the key to workable wholesale markets is open access transmission. In fact, mitigation of market power is a condition precedent before any service can be considered workably competitive. Both parties believe that now is the time to restructure, while one believes a flash-cut is appropriate and the other believes that a phase-in approach is correct.<sup>44</sup> Dynegy offers a theoretical economic study that purports to show that the impact of restructuring on low cost states will be positive.<sup>45</sup>

**It is the opinion of the Staff that restructuring of the electric industry in Alabama is not in the public interest *at this time*.** The presumption of proof must lie on those who wish to see the electric industry in Alabama restructured at this time. While Staff believes in the free market and the theoretical concepts that support that movement as it applies to the electric utility industry, the Staff does not believe that it has been demonstrated that all consumers in Alabama would continue to receive adequate, safe, reliable and efficient energy services at fair and reasonable prices under a restructured retail market, at this time. This finding does not mean that Alabama should not restructure, but that the time is not right.

While historical data may show that other industries have seen savings under deregulation, it does not necessarily follow that these same savings will accrue in the retail electric market in Alabama. In addition, the theoretical economic studies that purport to show net savings or losses to the Alabama ratepayer as a result of restructuring

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<sup>42</sup> In general see: AMEA Initial Comments, pp. 3 – 9, Tr. 145 – 153, Replies, pp. 2- 14; APCO Initial Comments, pp. 4 – 7, Replies, pp. 3 – 8, Tr. 204 – 213, Replies, pp. 3 – 10; AREAC Initial Comments, pp. 10 – 19, Replies, pp. 4 – 11, Tr. 259 – 269, Replies, pp. 2 – 10; NAPPA/TVPPA Initial Comments, pp. 4 – 8, Tr. 318 – 326.

<sup>43</sup> AREAC Initial Reply Comments, p.8: AU/UA Study, p.8: USDA; NAPPA/TVPPA Initial Comments, p.13: DOE, p. 13: Consumers Union and Consumer Federation of America.

<sup>44</sup> In general see Dynegy Initial Comments, pp. 1 – 1-, Tr. 617 – 633; EPSA Initial Comments, pp. 1 – 6.

<sup>45</sup> See Dynegy Initial Comments, p. 10: INGAA.

do so in direct correlation to the stated positions of the parties that offer these studies. For this reason, the Staff puts little faith or credence in the results of the theoretical economic studies offered, pro or con. The Staff believes that in light of current circumstances in the market place, any previous national or regional economic studies should be re-evaluated using current known and projected inputs.

The current state of activity in jurisdictions where competition is being pursued provides evidence that the slow, cautious and deliberate approach to competition by this Commission is the appropriate path to follow. It is not because the concept of competition is flawed that Alabama should proceed slowly, but because the implementation can be extremely costly and initially unworkable. Markets will work, but there must be a properly functioning infrastructure to support the market. The transitional problems currently being experienced in California, the northeast, and other jurisdictions attest to the need for monitoring and studying the actions and plans of these jurisdictions in order to learn from their experiences. In this instance, haste can lead to very expensive mistakes for ratepayers and utilities alike. The fact that Alabama is a relatively low cost state lends further to the argument against haste in this matter. There is no distinct immediate advantage to being at the forefront of this grand experiment. Delaying competition in Alabama for the sake of protecting turf is not in the public interest, but waiting for solutions to market power, transmission problems and proper program design is prudent.

The creation of a viable wholesale market is a cornerstone of a workably competitive retail market. The current wholesale markets have serious economic and engineering problems. The lack of such a workable market in generation has been one of the main reasons cited for the aberrations in prices this summer for the markets that are restructuring. Lack of equal access to the transmission grid is another roadblock to the opening of competitive wholesale and retail markets. These issues will require time to resolve and are being dealt with. The addition of new generating facilities and the FERC resolution of comparable access to the transmission grid will make the move to retail competition more seamless and less costly.

The Staff believes that the reliability of the transmission grid must be insured prior to a move to open markets. Undeniably the grid is strained and constrained.

Congressional and FERC action is necessary to insure that an efficient and reliable transmission grid is in place. Currently there are proposals under FERC Order 2000 to establish Regional Transmission Organizations (RTO's) to help ensure fair access to the transmission grid, and as a result, support for the competitive wholesale markets. The Staff feels that the Commission should continue to evaluate the effectiveness of RTO's to ensure that they maintain reliability and promote cost efficient development of the transmission system for retail customers.

All of the actions required of restructuring come with a price. The transition costs at this time have proven to be highly volatile and costly. The Staff believes that the markets will eventually respond in terms of balancing supply and demand, but in the interim, the cost to transition is proving to be significant and volatile to ratepayers and utilities. It should be noted that the Commission has already taken steps to obtain benefits for retail customers from the wholesale market. The recent solicitation of competitive bids for generation suppliers by Alabama Power Company under guidelines developed at the Commission's request will select the most competitive long-term power supplies for future retail electric needs. In this respect, Alabama retail customers will realize the benefits of wholesale competition without being subjected to the substantial volatility and risks of the short-term wholesale market. This competitive bidding procedure will capture many of the current benefits of competition, while allowing the Commission time and opportunity to study and evaluate restructuring schemes adopted in other states.

Based on the Staff recommendations, the Commission has several avenues available for it to take on a going forward basis. Those would include:

1. Suspend Docket 26427, while monitoring activity in other states and at the federal level;
2. Convene collaborative workshops around the identified issue areas to achieve consensus where possible and try to resolve problem areas. This could lead to the development of a strawman restructuring proposal and requisite legislative changes;
3. Remodel previous pro and con economic studies, replacing forward looking estimates with current known information, and conduct net benefit

economic analysis to assess the costs and benefits relative to our low cost status;

4. Study the unbundling of generation, transmission and distribution rates for informational purposes.

This list is not exhaustive and the Staff welcomes further suggestion.