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WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

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August 14, 1995

Re: Examining Regulation of Electric Utilities in the Face  
of Change in the Electric Industry  
Docket No. UE-940932

Status of the Notice of Inquiry and Policy Statement Establishing  
Interim Principles for Regulation of Electric Utilities

To All Parties and Interested Persons:

SUMMARY

By this letter, the Commission informs interested persons of the status of its Inquiry on the regulation of electric utilities in the face of change in the electric industry. The pace of change and activities which profoundly affect the environment of the electricity industry in Washington has accelerated in recent months. These circumstances have lead the Commission to conclude that it does not yet have sufficient information to refine existing, or to develop new, regulatory tools to address resource planning, resource bidding, and prudence determination. Decisions concerning these tools will be deferred until a clearer picture has emerged of the structure of the industry, and the domain over which Washington state regulation will have authority. The Commission's immediate focus will be on external factors and processes, particularly the Federal Energy Regulatory Commission (FERC) notice of proposed rulemaking (NOPR) (RM95-8-000 and RM94-7-001) on transmission access and stranded investment, and developments affecting the future role and structure of the Bonneville Power Administration (BPA). In the meantime, Commission staff will evaluate studies of market conditions in the electric industry, and undertake a survey of customer views concerning electricity competition and service.

The Commission anticipates that challenging regulatory issues will arise as the electricity industry adapts to a greater degree of competition and to changes in both customer expectations and the national and regional industry environment. Accordingly, the Commission issues an interim policy statement pursuant to RCW 34.05.230 and WAC 480.09.200 and invites comments on this draft statement from interested parties. The draft policy statement consists of a set of principles and objectives to help guide the transition to a more competitive electricity industry.

The Commission intends to use this set of principles to guide decisions about specific filings made by regulated companies in response to competitive circumstances.

#### STATUS OF THE INQUIRY PROCESS

On December, 16, 1994, the Commission undertook an Inquiry into changes in the electric industry and consequences that such changes might have for current regulatory tools, such as least cost planning, competitive bidding, and prudence review of utility electricity resource decisions.

Two rounds of written comment have been completed. A total of 41 parties have submitted 506 pages of comments. The interested party list now contains more than 300 names. The Commission thanks all parties for their time, attention, and thoughts. Copies of all sets of comments have been published, and continue to be available on request from the Commission's Records Center.

The Commission and its staff have reviewed the comments, and found them constructive statements of views and positions held by the diverse range of electric industry stakeholders. Two themes emerged from the initial rounds of comments. The Commission concludes that these key themes should form the basis for interim principles to guide utility policy as the industry evolves.

The first theme is the broadening of the array of choices made available to customers to meet their electricity service needs. Broadening the choices available to customers may involve expanding the array of service products offered by utilities, or broadening opportunities to choose the provider of unbundled products, or both.

The second theme is the preservation, under changing competitive circumstances, of the benefits of the existing electricity supply system. Among these benefits are: equity among customers, long-term reliability and efficiency, universal access, affordable service, environmental stewardship, and public involvement in electricity resource planning and development.

The few months since the Inquiry began have seen substantial and accelerating change in the electricity industry.

1. Low natural gas prices, increased transmission access, the rise of power marketers, and enhanced electricity price transparency have led to the development of a substantial surplus of bulk power in the West. This, in turn, has led to a vigorous market of attractively priced wholesale power products.

2. The FERC issued its NOPR on restructuring the wholesale power market to ensure healthy competition in the generation market. The NOPR raises a number of questions concerning state/federal jurisdiction. While the FERC makes no direct assertion of authority over retail service, the transmission system through and over which supply competition takes place is ambiguously partitioned into state and federal jurisdiction.

3. The BPA is faced with significant price competition from the wholesale surplus (see #1, above) and may undergo substantial restructuring through federal legislation. In particular, the access that investor-owned utility (IOU) residential customers have to federal power system benefits, primarily through the residential exchange program, has been proposed by BPA in its 1996 rate case to undergo significant change. In addition, BPA has recently proposed significant changes in transmission services and pricing.

4. Industrial customers, reacting to the declining price of wholesale power, are pressuring some utilities for rate concessions. The Commission recently approved a special contract between Puget Power and ARCO in Whatcom County. Some utilities are adding new retail industrial loads through attractively priced power deals. Washington Water Power has negotiated a contract to serve an industrial customer formerly served exclusively by BPA as a direct service industry. Puget Power has filed an exit fee tariff, WWP has indicated interest in filing a "competitive service" tariff, and some industrial customers have expressed interest in unbundled local distribution services.

Since the Inquiry was initiated in December, the electricity industry has seen an expansion in the available supply of wholesale electricity, an expansion in the number of participants and the roles they play in the wholesale electricity market, and greatly enhanced market price transparency. The 20 to 30 mill prices now available in the wholesale market are below many of the new resource cost estimates made over the last few years. For the near term, at least, supply is up and prices are low.

The initial Inquiry was primarily focused on issues surrounding regulatory tools which affect planning for new resources and new resource acquisition and the application of these tools for centrally provided, monopoly, retail electricity service.

The developments in the wholesale power market have changed the environment for the Inquiry by shifting emphasis from development of new resources to the accommodation of greater competition. Consequently, the focus of the Inquiry must change, at least for the near-term.

At this point, the Commission has yet to form an opinion on the nature or extent of competition that would be beneficial and fair in the retail market, or what actions, if any, it can or should take to facilitate such competition. A comprehensive approach to the retail service and regulatory process must await greater clarity on the circumstances and need for regulation that grows out of the FERC's actions, and any restructuring affecting BPA.

The tools for facilitating retail service competition (for example, unbundled service tariffs) cannot be effectively developed without resolution of the structural and jurisdictional issues raised in the NOPR. Moreover, proposals to restructure BPA and its transmission system could significantly affect the basic framework for competition in Washington. Similarly, questions about resource planning, bidding, and prudence review cannot be resolved until it can be determined for whom -- for which customers -- such regulatory oversight is needed and appropriate.

We anticipate the FERC process yielding results by spring 1996. For the time being, existing Washington regulatory rules governing least-cost planning, and resource bidding will remain in place, and prudence of utility expenditures will be handled in general rate cases.

Comments submitted by Inquiry participants will help inform the Commission in its response to FERC and BPA/regional issues. In addition, to address the call for greater analysis made by some commentors, Commission staff will collect and evaluate research on the nature of the evolving electricity market and conduct a survey of consumer views about electricity service and competition. Analyzing market characteristics and consumer viewpoints will prepare the Commission to address both benefits and implications of expanding the service choices available to retail customers once FERC and BPA playing fields are better understood.

Given the uncertain institutional context, the Commission believes that fair and efficient competition would benefit from common rules and principles guiding the competitive relationships between and among Washington's various retail service utilities, regardless of history or ownership form. For those utilities under its jurisdiction, the Commission anticipates that regulatory issues prompted by adaptation to changing competitive circumstances and situations are likely to arise in the near term. We expect that the special contract rule (WAC 480-80-335),

banded rate tariff authority (RCW 80.28.075), and the Commission's general authority to regulate in the public interest (RCW 80.01.040) will provide sufficient flexibility to address many of these situations. In addition, the Commission will use a set of general principles to provide guidance in the consideration of specific regulatory issues as they arise.

The following set of principles comprise an interim policy statement made pursuant to WAC 480-09-200. The Commission invites comments on these interim principles and will make appropriate revisions to the principles subsequent to the review and analysis of comments received.

Parties wishing to comment should submit comments bearing the caption Guiding Principles for an Evolving Electricity Industry and reference Docket No. UE-940932 to Steve McLellan, Commission Secretary, no later than September 18, 1995.

The Commission requests that commentors file an original and ten (10) copies of their written reply comments. The Commission also requests that an electronic version of your comments be provided on a 3 1/2 inch, high density diskette, with the format identified, or in ASCII text format.

INTERIM POLICY STATEMENT: GUIDING PRINCIPLES FOR AN EVOLVING ELECTRICITY INDUSTRY

1. The Commission's fundamental responsibility is to ensure that the electricity service needs of customers are met at a cost that is fair, just, reasonable, and not unduly or unjustly discriminatory. Where competition can serve to accomplish results that are fair and efficient for all customers, it should be accommodated and encouraged.
2. Non-economic bypass and the inappropriate shifting of the fixed cost of the electrical system between or among customers are not fair and efficient competition, are contrary to the public interest, and should be avoided. Customers of continuing monopoly service should benefit, or at least not be harmed, by choices made by customers with competitive options.
3. The long-term integrity, safety, reliability, and quality of the bulk electric system and retail electricity service should not be jeopardized.
4. Consumers should be afforded the broadest possible range of choice in electricity service and pricing options. Customer service and pricing options should reflect customer needs, as

well as differences among electricity providers. All classes of customers should have access to a basic level of reasonably priced and reliable service.

5. Competitive markets should not undermine public policies favoring environmental protection, energy efficiency, resource diversity, and technological innovation. If these policies are to be realized, the utilities, new market entrants, and electricity customers, as well as institutions not directly a part of the electricity industry, will all have important roles to play. Approaches that encourage development of markets for energy efficient equipment (e.g. market transformation), or which are otherwise market-based and competitively neutral should be emphasized.

6. Transitional regulatory decisions concerning specific situations and responses to competitive circumstances should be made carefully in a manner that does not advantage or disadvantage any group of competitors or the "natural" evolution of efficient markets.

7. The opportunity for members of the public to voice their views in the planning, choice of resources, siting, and impacts of the electricity system should be preserved and enhanced.

8. Regulation serves its responsibility for protecting customer interests by acting as a surrogate for competition. Regulation cannot and should not ensure that utilities are, in all circumstances, made entirely whole for generation or other costs that are determined through actual and fair competition to be stranded or uneconomic.

Signed at Olympia, Washington, this 14th day of August 1995.



Sharon L. Nelson  
Chairman



Richard Hemstad  
Commissioner



William R. Gillis  
Commissioner