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Electric Utility Consumer Protection at a Crossroads

Since the inception of electric deregulation, complaints have risen and prices have only dropped due to lower fuel costs and pre-restructuring mandates. Consumer protections passed in 1999 need to be strengthened.

Deregulation promised consumers lower prices and improved service quality. At the one-year anniversary mark, it was clear the new electric market had failed to deliver either.

The sober reality is that consumer complaints regarding electric service have increased over 250% in the past year. This dramatic jump resembles the wave of dissatisfaction that has plagued local phone deregulation since 1996, and it is especially troubling because electricity is indispensable.

Historically, Texas utility regulators established minimum consumer protection standards, including the protection of vulnerable customers, acceptable credit terms, and disconnection practices.

Unfortunately, with a new market, there are new opportunities to take advantage of people. Some of the tactics foisted on consumers in the first year include high-pressure door-to-door sales tactics and the use of credit scoring to avoid serving certain customer segments.

Deregulation has taken the regulatory cop off the beat. But it is clear that the market alone is insufficient to police anticonsumer practices. Experience has shown that with deregulation even stronger customer protections are called for.

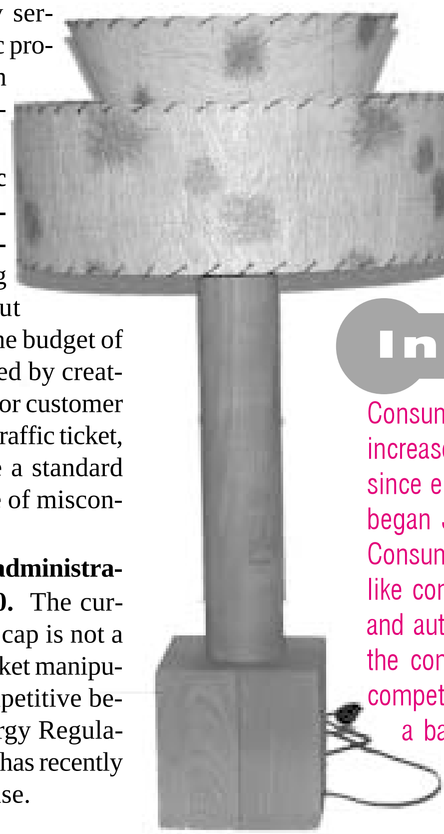
In addition to protecting consumers, tough consumer protection rules can improve market efficiency by reducing the total costs. For example, standardized terms of service agreements foster competition by encouraging informed comparison shopping. Further, if consumers become suspicious of utility service providers because of the actions of a few unscrupulous companies, they will be more inclined to shun new players and lose any potential benefit from competition.

Deregulation does not mean "no regulation". In 1999, the Legislature took an important step to improve consumer protections in utility markets by passing Senate Bill 86. However, the permissive language has resulted in rules that favor the companies' interest over consumers.

Recommendations

There is a need for stronger legislative direction in utility customer protections.

- **Create a consumer complaint report card.** By having user-friendly complaint data sorted by service area and retail electric provider, consumers can choose companies that excel in service.
- **Assess automatic fines payable to the consumer for customer service violations.** Improving customer service without significantly increasing the budget of the PUC could be achieved by creating a system of penalties for customer service violations. Like a traffic ticket, the victim would receive a standard amount based on the type of misconduct.
- **Increase the cap on administrative penalties to $25,000.** The current $5,000 per violation cap is not a sufficient deterrent to market manipulation and other anti-competitive behavior. The Federal Energy Regulatory Commission (FERC) has recently requested a similar increase.



In Short

Consumer complaints have increased over 250 percent since electric deregulation began January 1, 2002. Consumer protection rules--like complaint report cards and automatic fines paid to the consumer-- encourage competition by giving buyers a baseline for comparison and confidence in the basic services.

Electric Deregulation's Rocky Road

Although wholesale prices dropped after launch of the new electricity market, consumer prices actually rose. Only if the "price-to-beat" is linked to the real cost of power will consumers see the savings they were promised.

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Proponents of electricity deregulation tout Texas as the model market. If Texas is the best, it is the best of a bad idea. With inherently volatile prices and unstable supply, the risks simply outweigh the benefits—especially to residential customers.

Most observers agree that Texas' first year foray into electric deregulation has been a rocky road. Consumers Union disagrees with those who dismiss the many problems as "just part of the transition."

While the Public Utility Commission has worked to address some of the problem areas, we believe reforms are necessary to ensure Texas consumers continue to receive reliable, affordable electric service.

To find out if residential and other small-user consumers are getting what they were promised, CU SWRO asked a series of questions: Are Texas consumers better off under restructuring? Are they saving much money? Is the system as reliable? Is service as good as before? Is the market healthy? In each case, the answer is no.

Allegations of customer savings rely mostly on smoke and mirrors. Press releases tout $900 million in residential price to beat savings. The price to beat is the regulated rate offered by incumbents like TXU and Reliant Resources that still applies to 94% of residential consumers in Houston and Dallas/Fort Worth. We found that the alleged $900 million savings reflects mandated price reductions and lower fuels costs, both which were likely to occur without deregulation.

In Short

The California experience should remind us that adequate reserves are a critically important backup in the event of severe weather, forecasting errors, fuel shortages or other unforseen problems. As many Texas companies cancel power plant construction or take plants out of service, reserves may dip as low as 9 percent.

Comparing the savings consumers could achieve by moving to a competitor, versus the price to beat, the PUC estimates only $7 million savings for residential customers who chose a competitive retailer.

Deregulation was supposed to result in lower wholesale prices. And those lower wholesale prices were supposed to be passed through to consumers in the form of lower retail prices. However, the opposite has occurred in Texas—wholesale prices did drop, but at the same time the small customers on the price to beat have seen their rates increase.

The old system ensured adequate generation reserves and sufficient transmission, key to reliability and price stability. Today, as many companies put on hold or cancel new power plant construction, and others take plants out of service, the once sizeable reserve margin is projected to dip as low as 9 percent by 2007. The California experience should remind us that adequate reserves are a critically important backup in the event of severe weather, forecasting errors, fuel shortages or other unforeseen problems.

The market itself stumbled soon after it opened. After just one year, there are already allegations and admissions of market "gaming"—undeserved extra payments that boosted profits during the hottest months while consumers saw their bills skyrocket. In addition, formerly rock solid utilities TXU and Reliant have had their credit ratings downgraded to junk status due to declining investor confidence.

Recommendations

Given the fact that we are already traveling this road, consumers need certain protections to survive in the market.

- Ensure price to beat customers are getting the best deal possible. Link price to beat adjustments to the cost of providing power, not simply natural gas futures that have little correlation to the actual cost of providing power. Allow the PUC or Office of Public Utility Counsel to request a lower fuel factor when the cost of providing power decreases.
- Establish a long-term reserve margin, a public load forecasting process and reporting requirements to project future energy needs and ensure reliable service.
- Establish a mandatory code of conduct with enforcement mechanisms for the wholesale market.