

MAINE STATE LEGISLATURE

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Annual Report on Electric Utility Efficiency

Report to the Utilities and Energy Committee On Actions Taken by the Commission Pursuant to 35-A M.R.S.A. § 3195

I. Background

35-A M.R.S.A. § 3195 authorizes the Public Utilities Commission (Commission) to adopt rate mechanisms that promote electric utility efficiency. Subsection 5 states:

Annual Report. The commission shall submit to the joint standing committee of the Legislature having jurisdiction over utilities matters an annual report detailing any actions taken or proposed to be taken by the commission under this section, including actions or proposed actions on mechanisms for protecting ratepayers from the transfer of risks associated with rate-adjustment mechanisms. The report must be submitted by December 31st of each year.

Since 1995, one or more of the utilities in Maine have operated under an alternative rate plan. These plans replace traditional rate of return regulation with a multi-year price cap approach that places an upper limit on the utility's rate increases, while allowing the utility to retain savings it accomplishes through improved efficiencies. In addition, the plans typically contain pricing flexibility provisions that allow the utility to offer reduced or re-designed rates to customers who would otherwise replace electricity with another fuel or leave the service territory. Pricing flexibility allows the utility to obtain a contribution to its fixed costs that it would otherwise lose, thereby avoiding a shift of those fixed costs to remaining customers. We have found that the alternative rate plans create rate predictability and stability, reduce regulatory costs, and provide stronger incentives for utilities to minimize their costs. The plans maintain a comprehensible and predictable regulatory approach.

All alternative rate plans expired shortly before, or coincidentally with, the onset of electric restructuring on March 1, 2000. However, many special rate contracts extended beyond March 1, 2000. As part of the restructuring process, these contracts were unbundled in a way that reflected existing market prices for generation and required customers to acquire generation at the lowest possible price.

During 2000, the Commission approved a new 7-year Alternative Rate Plan (ARP 2000) for Central Maine Power Company (CMP) that applied to only distribution delivery activities. With generation open to market competition, transmission service was subject to Federal Energy Regulatory Commission (FERC) jurisdiction, and stranded costs are periodically adjusted in accordance with Maine law. In comparison with CMP's previous ARP, the ARP 2000 contained significantly stronger productivity incentives, allowed only low-end earnings sharing, and

increased the number of service and reliability indices that CMP must maintain. These changes responded to CMP's merger with Energy East, during which we recognized that the rate conditions imposed in connection with the merger approval (ensuring that ratepayers receive a reasonable portion of the efficiency savings while allowing Energy East an opportunity to recover its acquisition premium) could best be accomplished through an incentive rate plan.

This report describes Commission actions taken during 2001 to promote electric efficiency through incentive rate plans or special rate contracts.

II. Central Maine Power Company's Alternative Rate Plan

CMP's ARP 2000 provides for annual rate changes on July 1st of each year. Rate changes are based on a well-established formula of inflation minus a productivity offset, adjusted for mandated costs, earnings sharing and service quality index (SQI) penalties. On March 15, 2001, CMP made its annual rate change compliance filing. As required by the terms of the ARP 2000, the productivity offset in 2001 was equal to inflation, so these two factors had no influence on rates.¹ Earnings sharing and SQI penalties were not applicable to the 2001 price change, and CMP asserted that all other factors fell below the threshold that would result in a rate change under the ARP 2000. However, an earlier Commission decision² allowed deferral and subsequent recovery of lost distribution revenues that occurred when CMP decreased its distribution rates for a three-month period to offset a transmission price increase, and CMP's filing included a rate increase under the ARP 2000 to recover those costs.

On June 25, the Commission approved a stipulation, signed by the Office of the Public Advocate and CMP, which reflected the price change discussed above and would increase CMP's average T&D rate by less than 0.5%. IECG objected to the stipulation on the grounds that the underlying ARP 2000 plan unlawfully allows CMP to implement rates that have not been found to be just and reasonable. However, the Commission found that the stipulation properly carried out the ARP 2000 directives and was consistent with all legislative mandates and in the public interest. Under the terms of the ARP 2000, the increase became effective on July 1. In response to an appeal by the IECG to the Maine Supreme Court, the Court affirmed the Commission's order.

CMP's rates also include a component that recovers transmission service costs. This transmission component falls under FERC jurisdiction and is revised annually through a proceeding before the FERC. During 2001, the FERC ordered a change in CMP's transmission rate component that would increase CMP's average

¹ Under the terms of the ARP 2000, the productivity offset will increase in future years, necessitating that CMP attain increased savings or lower rates.

² Investigation of Retail Electric Services and Jurisdictional Issues, Docket No. 99-185, *Order Approving Stipulation* (August 28, 2000).

T&D rate by approximately 2%. Both rate changes became effective on July 1, 2001, increasing CMP's average T&D delivery rate by approximately 2.2%. Rates for customers receiving service at distribution level voltages increased between 1% and 3%. However, because the transmission component comprises a higher portion of the delivery rate for those customers receiving service at a transmission level voltage, the T&D delivery rates to these customers increased approximately 15%.

III. Bangor Hydro-Electric Company's Alternative Rate Plan

In July 2001, Bangor Hydro-Electric Company (BHE) filed a proposal to implement an "all-in ARP" that would allow BHE to sell both T&D delivery and standard offer service and to earn a return on the sale of those combined sales. The Commission rejected the proposal to allow BHE to sell standard offer service, stating that it was inconsistent with the Legislature's decision to open Maine's retail generation market to competition and prohibiting T&D utilities from selling generation to retail consumers.³ We further stated that BHE's proposal went beyond the currently-existing arrangement in which BHE acts as the Commission's agent in procuring wholesale standard offer service in the absence of acceptable retail bids. Finally, we stated that it was premature to judge at that time whether the bids for standard offer service in BHE's territory would be less acceptable than BHE's proposal.

BHE subsequently filed proposals for an ARP (including a proposed change to BHE's distribution rates) and for a base rate case. We are currently considering the course of action we will take in response to these two proposals.

IV. Events of September 11, 2001

On September 12, 2001, to ensure that CMP was in a position to respond to requests for aid from authorities in the areas impacted by the September 11 terrorist attacks, the Commission issued an order suspending the use of SQI penalty mechanisms in the determination of rate increases under the ARP 2000. On October 17, after CMP informed the Commission that it did not expect significant further disruptions of its operations as a result of the attack, we lifted the suspension.

V. Special Rates and Contracts

A. Unbundling Activity

Alternative rate plans in effect before Maine's electric industry was restructured on March 1, 2000 allowed utilities flexibility to offer reduced or special rates to individual customers or to groups of customers. When restructuring

³ Bangor Hydro-Electric Company Request for Approval of Alternative Rate Plan, Docket No. 2001-410, *Order Rejecting Standard Offer Proposal* (September 5, 2001).

occurred, it was necessary to “unbundle” each contract and targeted rate into two portions -- a T&D portion that would be provided by the T&D utility and a generation portion that would be provided by a competitive electricity provider.

During 2000, under the provisions of 35-A M.R.S.A. 3204(10), the Commission approved the unbundling of approximately 100 contracts and 20 target rates. During 2001, we continued this process. A portion of the contract customers obtained new sources of generation, necessitating a revision to the unbundling of their contracts. It became apparent that unbundling could result in a negative distribution rate, when the price of a new generation contract is greater than a customer's original special rate contract. The Commission determined that a special rate contract that varies year by year in the amount of its contribution is not inappropriate, even if the contribution is negative for some time period, as long as the contribution is positive over the long term. The Commission thus approved such contracts.⁴ Several existing contracts expired, necessitating that the T&D utility determine the appropriate treatment of the customer's rate under current circumstances. Finally, new contracts were considered when appropriate.

B. Price Mitigation

In March, 2001, in order to mitigate the impact of significant increases in generation prices that some standard offer customers would pay effective March 1, the Commission ordered a 0.8 cent/kWh reduction in CMP's T&D rates to customers in the medium and large non-residential standard offer classes. We also ordered a 0.8 cent reduction for customers in the large non-residential standard offer class in BHE's territory. We ordered that this mitigation be accomplished by modifying the amortization schedules of each utility's Asset Sale Gain Account (ASGA), which resulted from utility generation asset divestiture.

We did not extend the 0.8 cent mitigation to customers on special rate contracts. Pricing for customers on “bundled rate” contracts were already mitigated because the customer paid the same bundled rate regardless of the cost of generation, and other customers had the benefit of lower T&D rates through their special rate contractual commitments.

Subsequent to this decision, the Industrial Energy Consumers Group (IECG) petitioned us to reconsider our decision, and the issue of mitigation for special rate customers was discussed before the Utilities and Energy Committee of Maine's Legislature. In May, we granted a portion of the IECG's request, and ordered that the 0.8 cent mitigation be granted to customers on special rate contracts, subject to

⁴ Central Maine Power Company Petition to Resolve Dispute Regarding Special Rate Contract with the Chinnet Company, Docket 2001-166, *Decision and Order* (October 2, 2001).

certain parameters.⁵ Mitigation would not be extended to customers who pay the same total rate regardless of the generation price or to customers whose special rates are tied to core rates and had thus already received the mitigation. In addition, no distribution rate element would go below zero.

In our order, we also noted that not all classes of customer received the same level of benefit from the ASGA amortization used to accomplish this mitigation. We will consider this fact when setting rates in future proceedings.

The mitigation granted under this decision became effective on April 15 and is scheduled to remain in effect until no later than February 28, 2002. However, on December 21, 2001 we approved a stipulation in CMP's stranded cost proceeding that will continue mitigation of 0.45 cents per kWh to customers eligible to receive service under CMP's transmission level rates.⁶ In addition, we are currently considering a proposal that would continue some amount of mitigation to customers in BHE's territory.

⁵ Public Utilities Commission Investigation of Central Maine Power Company's Stranded Costs, Transmission and Distribution Utility Revenue Requirements, and Rate Design, Docket No. 97-580, *Order on Reconsideration*, (May 3, 2001) and Maine Public Utilities Commission Investigation of Stranded Costs, Transmission and Distribution Utility Revenue Requirements, and Rate Design of Bangor Hydro-Electric Company, Docket No. 97-596, *Order on Reconsideration*, (May 7, 2001).

⁶ Maine Public Utilities Commission Investigation of Central Maine Power Company's Stranded Costs Revenue Requirement and Rate Design, Docket No. 2001-232.