

**TO: California Public Utilities Commission (Commission) – California Customer Choice Staff**

**FROM: The Direct Access Customer Coalition (DACC) and Alliance for Retail Energy Markets (AReM)**

**RE: Response to October 19 Ruling Regarding Customer Choice Workshop**

DACC and AReM respond herein to the questions attached to the October 19, 2017, Ruling of Administrative Law Judge Jeanne M. McKinney.

### **White Paper Scoping Questions**

**1) The California Customer Choice project has three principles and eight key questions when considering customer choice (see below) in California and other markets. Are there any additional questions that the project should be considering? Why?**

Principles (in alphabetical order):

- **Affordability:** Design Rates and Charges So That Bills Are Affordable
- **Decarbonization:** Meet California’s Environmental and Climate Goals
- **Reliability:** Maintain Safety, Reliability, and Resiliency of Electricity Services

Key Questions in Considering Customer Choice

**Question 1:** How does this choice model ensure consumer protections?

**Question 2:** How does this choice model support development and incorporation of innovations driven by customer demand?

**Question 3:** Does this choice model ensure universal electric service?

**Question 4:** How does the choice model leverage investment necessary to finance the evolution of the electric grid?

**Question 5:** How does this choice model consider the transition of utility obligations?

**Question 6:** Does this choice model have competitively neutral rules among market participants?

**Question 7:** Can customers determine their level of participation and are they informed to participate at their desired level?

**Question 8:** How does this choice model impact and benefit local communities?

**Response:** DACC and AReM endorse the stated eight questions as foundational to the consideration of retail choice. In addition to these, there are additional threshold questions that should be incorporated into the California Customer Choice Project (“Project”) deliberations to ensure that the Project team’s planned White Paper evaluates and develops a comprehensive framework for retail choice in California to assist the Commission in implementing *market* structures that provide a platform for all load-serving entities (“LSEs”) to meet California’s three goals of Affordability, Decarbonization, and Reliability. These additional questions include:

**Question 9:** What are the modifications that state regulatory agencies, including the Commission, need to make to their current rules and regulations to support competitive retail choice?

**Question 10:** What is the right balance of regulatory oversight that promotes the supply procurement flexibility necessary for retail choice to thrive while complying with reliability and environmental mandates?

**Questions 11:** How does the Commission ensure compliance with reliability and environmental requirements when it no longer has investment authority over load-serving entities?

**Questions 12:** What new market structures must be put in place for competition to work?

**Questions 13:** What role should the CAISO have in helping to implement those new market structures?

**Question 14:** How can the utilities be transitioned out of commodity and other competitive businesses?

Adding these questions to the scope of this proceeding will ensure that a robust and challenging discussion occurs regarding the Commission's historical degree of authority over supply procurement, and how those historical practices must change in order to encourage and facilitate the successful expansion of customer choice.

As the Commission has already recognized, load migration to community choice aggregation ("CCA") and the possible reopening of direct access ("DA") market participation, coupled with expected further declines in cost thresholds for residential, commercial and industrial self-generation and storage options, signals an unequivocal and possibly irreversible departure from traditional utility supply procurement practices and ratemaking. Attempts to contain the strong forces of competition by mandating certain types of investments that all must pay for or otherwise impose command and control oversight of competitive procurement practices will lead to market inefficiencies. Investment, like electricity, flows in the path of least resistance.

Therefore, the fundamental role of the Commission and Staff should be to act as change agents that (a) facilitate and encourage competition, customer choice and innovation in energy products and services; and (b) implement market structures that allow such competition to flourish and send the right price signals to incent generation builds to sustain reliability. Increasing choice and competitive options invariably leads to greater investments, which in turn spawn creative innovation.

**2) The California Customer Choice Project is reviewing several markets as key examples of how customer choice operates under different regulatory frameworks. These markets include:**

- **New York**
- **Texas**
- **Illinois**

- **United Kingdom**

**Are there other markets, either domestic or international, that you think would be an important model for California to consider as a regulatory framework option? Why?**

**Response:** While the functioning retail choice markets found throughout PJM (including Illinois), New England, New York and the United Kingdom all have varying degrees of success, AReM and DACC believe the Texas market to be the most vibrant and dynamic, as demonstrated in this year’s report to the 85th Texas Legislature on the *Scope of Competition in Electric Markets in Texas*, issued by the Public Utility Commission of Texas in January 2017.<sup>1</sup> A sample of its findings include:

This year marks 15 years since the opening of the Texas retail electric market in 2002, brought about by the passage of Senate Bill 7 by the Texas Legislature, which began the project of restructuring the Texas electricity market. In the 15 years since the market opening, the Public Utility Commission of Texas (Commission) has overseen the transformation of the Texas electric landscape from one of incumbent utilities to a thriving electric market in the Electric Reliability Council of Texas (ERCOT) region...

Under the Commission’s oversight, the Texas retail market remains the national leader in competitive residential, commercial, and industrial offerings, with the highest number of competitors and product variety in the country. As of March 2016, in the portion of the state that is open to customer choice, 92% of all customers had exercised their ability to switch providers.

On average, residential retail rates in the competitive areas of Texas have declined since 2014, to prices as low as 4.5 cents per kilowatt-hour (kWh), compared to a nationwide average of 13.45 cents per kWh in 2016. In addition, wholesale market prices in Texas have fallen 21% since 2013.

This is evidence that customers can and will exercise choice on their own without the intervention of regulators. Every customer in competitive areas in Texas, as testified by Darrin Pfannenstiel of the Retail Energy Supply Association (“RESA”) at the workshop, have many renewable products at their disposal – with no regulatory dictate to offer those products.

Affordability is one of the Project’s three bedrock principles. In that regard, it is notable that the Electric Power Monthly report by the U.S. Energy Information Administration (“EIA”), issued October 24, 2017, shows the Average Price of Electricity to Ultimate Customers, across all sectors, to be twice as high in California as in Texas (17.15 cents/kWh in California and 8.56 cents/kWh in Texas for August 2017).<sup>2</sup> While investments in energy efficiency and demand response have indeed reduced the demand for electricity, the Commission must take care to ensure that Affordability is not accorded lower status than Decarbonization and Reliability. Rather, all three attributes deserve equal stature and equal attention from the Commission as it facilitates market structures that allow competition to deliver all on all three commitments.

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<sup>1</sup> [https://www.puc.texas.gov/industry/electric/reports/scope/2017/2017scope\\_elec.pdf](https://www.puc.texas.gov/industry/electric/reports/scope/2017/2017scope_elec.pdf).

<sup>2</sup> See, EIA Electric Power Monthly with Data for August 2017, at Table 5.6.A.

### 3) What published resources do you recommend the California Customer Choice team review in addressing key questions for evaluated markets?

**Response:** As an example of how a state commission can help foster and encourage competition, the team should first go to Power to Choose, a website maintained by the Public Utility Commission of Texas that is available to all electric providers to list their offers for free.<sup>3</sup> The website contains a link, *About Shopping*, that provides access to information on (a) the Shopping Process; (b) Questions to Ask; (c) Business (Non-residential); (d) Plan Options; and (e) Buying Renewable Power. The latter topic covers both finding green suppliers as well as how residential and commercial/industrial customers that choose to install power-generating sources, such as solar panels or wind turbines, can sell their excess generation.<sup>4</sup>

Next, the team should review the July 2017, paper entitled “Restructuring Recharged - The Superior Performance of Competitive Electricity Markets 2008-2016,” authored by Dr. Philip R. O’Connor, the former chair of the Illinois Commerce Commission. Sponsored by RESA, the paper’s conclusions include:

- Electricity prices in states with competitive retail markets have trended downward while prices have risen in states with monopoly regulation.
- Power plant investment in competitive markets is tempered by market forces, while in monopoly states new plant investments are made by captive ratepayers who are on the hook financially if the investment proves to be a poor economic decision.
- The power plants in competitive markets tend to operate more efficiently, because they are dependent on returns from the marketplace. In contrast, power plants under monopoly regulation receive their investment plus a rate of return regardless of the performance of the power plant. The efficiencies gained by power plants in competitive markets therefore produced not only economic but environmental gains.

Another important source, published in 2017, is a study from Rice University’s Baker Institute for Public Policy entitled, “Electricity Reform and Retail Pricing in Texas.”<sup>5</sup> Its author, Dr. Ken Medlock, analyzed whether retail prices were tracking underlying wholesale prices. The study, which analyzed data from 2000 to 2016, showed that both residential and commercial rates were closely tracking wholesale energy prices in competitive areas, and that the correlation grew closer over time, a strong indicator that competitive forces were working for the benefit of consumers. In stark contrast, the study showed that retail prices in the areas of Texas that did not move to retail choice (municipal utilities and cooperatives) continued to rise even as wholesale prices declined.

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<sup>3</sup> See: <http://www.powertochoose.org>.

<sup>4</sup> See: <http://www.powertochoose.org/en-us/Content/Resource/About-Shopping>.

<sup>5</sup> See: [https://www.bakerinstitute.org/media/files/research\\_document/7d32313b/CES-pub-TXElectricity-060717.pdf](https://www.bakerinstitute.org/media/files/research_document/7d32313b/CES-pub-TXElectricity-060717.pdf)

The team should also review *Evolution of the Revolution: The Sustained Success of Retail Electricity Competition* (July 2015) by Dr. O'Connor, and Erin O'Connell-Diaz, formerly a member of the Illinois Commerce Commission. The report highlights that retail electricity choice has been and continues to be a success for consumers, businesses and electricity stakeholders across the country in all retail choice models, based on nearly two decades of evidence in the 13 states and the District of Columbia that have access to retail choice. Their study reached the following conclusions:

- Customer Choice is thriving in 13 states and the District of Columbia, which have full access (“Customer Choice Jurisdictions”).
- From 2003 to 2013, in the 14 Customer Choice Jurisdictions, accounts served with supply from competitive suppliers rather than with power supply from local delivery utilities, **grew by 524% for Commercial and Industrial (“C&I”) customers and 636% for residential**, totaling 19 million customer accounts by year-end 2013.
- From 2003-2014, in the 14 Customer Choice Jurisdictions **electrical load served by competitive suppliers grew dramatically even in an era of overall flat growth in electricity consumption: 181% for C&I and 673% for residential** – accounting for 20 of every 100 kilowatt hours sold in the contiguous United States.
- Competition era price trends in the Customer Choice Jurisdictions have been more favorable to customers than price trends in the 35 traditional monopoly regulation jurisdictions (“Monopoly States”), with **average electricity prices falling against inflation in Customer Choice Jurisdictions, but far exceeding inflation in Monopoly States**.
- Customer Choice Jurisdictions, as a group, have outperformed Monopoly States in generation, attracting billions of dollars of investment in new, more efficient generation, **resulting in higher capacity factors than in Monopoly States** and parity in resource adequacy to meet load.
- The five states of the Industrial Upper Midwest offer a compelling intra-regional example of the success of Customer Choice, with the competitive states Illinois and Ohio outperforming the Monopoly States of Indiana, Michigan and Wisconsin with lower price trends and greater generation efficiency.

A further valuable source of information for the team would be the article *Electricity Customer Choice Out-Performs Traditional Monopoly* located at the Utility Dive website.<sup>6</sup> Written by Wayne Kuipers, director of Energy Choice Now, and Laura Chappelle, the former Chair of the Michigan Public Service Commission, the article observes that “evidence continues to accumulate that the performance of electricity customer choice is superior to that of traditional vertically integrated monopoly. Since the recession of 2008-9, electricity customer choice has been routinely outperforming traditional monopolies in terms of price.” It further notes that, “The big question facing policy makers in states served by unreformed incumbent monopoly utilities is how much longer customers should be forced to pay higher prices to compensate for

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<sup>6</sup> <https://www.utilitydive.com/news/electricity-customer-choice-out-performs-traditional-monopoly-1/424986/>.

anemic demand for electricity. How much longer should customers in Monopoly states be required to bear the fuel, technology and market risks that in Choice states are borne by investors in competitive states?”

In addition to the studies cited here, Attachment A contains a list of additional papers that the Project Team should find informative. Published resources such as these can be reviewed by the team to gain a comprehensive perspective of how competitive markets can be made to work to the benefit of ratepayers as they grapple with the best ways to implement retail choice in California.

**4) What specific statutes should the California Customer Choice team review when considering customer choice as discussed during the workshop?**

**Response:** Since retail competition was implemented in California in 1998 (through DA) and 2010 (through CCA), numerous laws have impacted customer choice and made significant changes to utility procurement practices since the 2000-2001 energy crisis. These laws and the policies put in place to implement them must be reviewed, discussed and analyzed to determine whether and how to modify them and the regulations that have implemented them, in order to move forward with expanding the benefits of retail choice in California. The following is a list of what AReM and DACC consider to be the most prominent:

1. AB 57, which put the utilities back into the asset building and procurement business and halted divestitures.
2. AB 380, which required the Commission, in consultation with the CAISO, to establish Resource Adequacy Requirements (RAR) for all the LSEs under Commission jurisdiction.
3. California’s long list of RPS legislation that have advanced the state’s environmental goals, which in turn have led to many forms of mandated investments by the utilities have created a large overhang of stranded costs that do not reflect the steep cost reductions that have occurred for renewable resources.
4. SB 695, which (a) provided for a limited expansion of DA that has been consistently over-subscribed in the annual lotteries, but left to the legislature any further expansion; and (b) included cost allocation mechanism (“CAM”) language on reliability that has since been implemented in a way that led to excessive imposition of utility investment costs on competitive suppliers and their customers, and impeded their ability to manage their supply portfolios.
5. Other special purpose legislation, such as the energy storage mandate in AB 2514 that directed the Commission to determine appropriate targets, if any, for each LSE to procure viable and cost-effective energy storage systems and set dates for any targets deemed appropriate to achieve.

Even as these new laws and investment mandates were being implemented, one tenet of the original restructuring legislation has remained intact. Public Utilities Code Article 12, Consumer Protection, Section 394(f), explicitly limits the jurisdiction of the CPUC regarding DA providers, as it provides, “(f) Registration with the commission is an exercise of the licensing function of the commission, and does not constitute regulation of the rates or terms and conditions of service offered by electric service providers. Nothing in this part authorizes the commission to regulate the rates or terms and conditions of service offered by electric service providers.” This restriction on the jurisdiction of the Commission over ESPs was an explicit recognition that retail choice is predicated upon the ability of customers and suppliers to negotiate the product and services they want at prices they are willing to pay. This provision should serve as a fundamental premise against which further policy changes to improve retail choice are considered; that is, for any new policy or policy reform that is suggested, the Commission should evaluate such reforms against a metric of whether that policy will enhance or compromise the ability of customers and suppliers to negotiate the terms and conditions for the services that customers want.

Given this legislative background, DACC and AReM believe the key market structures that the Commission must focus on for retail choice to thrive are:

1. The use of reliability market structures to replace CAM, such as a capacity market constructs;
2. Energy price formation to limit the need for capacity pricing;
3. Provider of Last Resort service for those customers who do not elect a competitive supplier; and
4. Elimination of the cap on DA.

### **Panel Follow-up Questions – Market Perspectives**

1) What are the most compelling examples of successful implementation of customer choice that you heard during the Market Perspectives panel?

**Response:** For all the reasons highlighted above, and as was noted by Chris Hendrix during this part of the workshop, Texas has clearly achieved the most comprehensive implementation of customer choice. Nevertheless, for the reasons explained in the O’Connor/O’Connell-Diaz and Kuipers/Chappelle papers cited above, retail choice has benefited customers across the country in the states that have adopted different retail choice models as well. It is noteworthy that the aggregate of all 14 of the competitive jurisdictions are significantly out-performing the aggregate of the 36 monopoly states with regard to pricing, power plant investment being tempered by market forces and the efficiency of generation operations, to mention a few of the dozens of data points and statistical measures outlined above in the response to Question 3.

2) Given some of the pitfalls illustrated by the panelists, how might California best avoid or mitigate these issues?

**Response:** As was noted by Chris Hendrix, full retail choice has allowed his company to further their efficiency and renewable goals while holding the line on energy prices, all to the benefit of their customers in the many geographic areas where they do business. They would prefer all their California locations be on DA, but the existing cap prevents that. Avoiding the pitfall of allowing only limited retail choice is, here in California, a legislative problem as discussed above in the response to Question 4.

Mr. Hendrix also spoke to the need for clear market price signals, not only to ensure cost effective energy purchases, but also to facilitate decisions on when and where to invest in renewable self-generation. In California, the key pitfall in this area that will require significant attention from the Commission is how to move away from its current hybrid market model that has resulted in utility ownership and/or control of most supply side resources (generation and demand response resources) under rate regulations that contain no incentives for cost risk management. A hybrid model that includes utility rate base and/or cost of service ratemaking to recover the costs of long term PPAs will never be an investor-friendly market for retail choice customers or suppliers, as the economic underpinning for such investments is constantly threatened with devaluation when new rate based and cost of service backed assets enter the market.

For retail choice to work, the Commission should back away entirely from such mechanisms, except perhaps in the most extreme examples associated with emergency reliability issues, and instead let market price signals inform market participants – customers and their suppliers – to determine when and where to efficiently deploy new assets, and what type of assets to deploy.

AReM and DACC recognize the important role that the Commission has in ensuring compliance with reliability and environmental requirements. However, in moving to a market structure where customers are free to choose their supplier and their technologies, it will be important that the Commission not seek to mandate specific forms of investment or direct the utilities to procure on behalf of load they do not serve, as such actions will, by definition, impact the level of service that competitive suppliers can provide. In short, as the California retail energy choice market expands, the Commission must remain mindful of the conclusion that it reached in Decision (“D.”) 05-11-025 that:

This Commission has less overall control over how ESPs and CCAs operate than we do over how utilities operate. Also, to the extent we consider ESP and CCA operations, our concerns about their operations differ somewhat from our concerns about the operations of the investor-owned utilities. In the context of the RPS program, our primary concern is to ensure that ESPs and CCAs do in fact reach the goal of 20% renewable energy by 2010. We are, however, somewhat less concerned about the details of how they get there.

3) What are the motivations and entities driving customer choice in California? How are they similar or different from the other markets?

**Response:** As to a fundamental motivation for customer choice: Choice is pervasive. We choose where to buy groceries, where to buy clothes. We choose what brand of gas to buy for our cars, and where to go for entertainment. Our choices for telephone, internet and cable TV services are varied, diverse and we can shop to our heart’s delight. With all these choices available to Californians, the question is simply why do we treat electricity any differently and restrict customer choice, especially now as the types of products and services available down to the residential level in the form of distributed generation are becoming so pervasive? The question has no logical response and so the quest for choice continues unabated. This is the same quest that occurred in each state that has customer choice – it begins always with customers wanting the ability to manage their costs in line with their product preferences. All Californians should have the right to elect from whom they wish to purchase electricity, and what products and services they want. From the smallest studio apartment resident to the largest commercial or industrial customer, choice should be a fundamental right (and, parenthetically, the right *not* to choose should also be a right, and those customers provided with quality default or provider of last resort service). Some consumers like to research their purchases thoroughly in advance while for others convenience and ease of purchase is all-important. Some value price, others value service and many value the combination of both. What matters is that each consumer should have the same freedom of choice regarding electricity as she or he has regarding all other goods and services.

Beyond these fundamentals, as Chris Hendrix pointed out during this portion of the workshop, choice has benefited his company and his customers by allowing Walmart to deploy renewables to a level that has achieved 26% renewable worldwide, and to deliver on its promise to help its customers save money on the things they buy so they can live better. That rationale for choice is undoubtedly shared across the spectrum of entities that favor more retail choice. The rationale in opposition to customer choice instead subscribes to a viewpoint that residents and businesses will be more harmed than helped by competition in the energy sector because reliability will be compromised, or environmental improvements will not occur. Indeed, achieving reliability and environmental improvements in a retail choice market will not occur as it would under rate regulation – it will be more customized and more decentralized, which will require different forms of regulatory oversight – but the rewards in terms of supporting innovation and cost reductions are well supported by the record in competitive states, and should be allowed to take hold here in California.

**Panel Follow-up Questions: Shark Tank**

1) After reviewing the “shark tank” presentations, what are the “must haves” as California considers regulatory framework options to manage the transition associated with customer choice? What is the most compelling vision of customer choice as presented in the shark tank?

**Response:** It should first be noted that DA customer choice has existed in California since 1998, and the first CCA, Marin Energy Authority (now Marin Clean Energy) began service in 2010. Therefore, we are not in a “transition” to retail choice; rather we are confronting the issue of how

to end the limits on retail choice. The Shark Tank section of the workshop did not address this issue. Instead, the participants were asked for their market views and how those views hold up to scrutiny – they essentially were asked to defend their market views, and so that is what they did: SCE argued for full cost recovery, the solar and energy storage representatives want their industries to receive continued preferential treatment and IEP continued to advocate for utility-based long-term contracts. In short, a vision for an expanded retail choice market was hardly explored as the participants engaged more in defending the status quo. This is not meant as a criticism of those remarks; they were asked to defend the status quo and therefore spent their time doing so.

DACC and AReM, however, believe that the time for defending the status quo is over. Instead, the Commission needs to engage more deeply with market participants to directly address what it perceives to be the thorniest problems associated with increasing retail choice. In response to Question 1, we listed additional questions that should be addressed as the Commission explores the expansion of retail choice. Then, in response to Question 4, we have outlined the legislative and policy considerations that must be addressed. We look forward to engaging on these issues as the Customer Choice Project continues, and hope to have a chance to directly engage with the Commission on these topics in future workshops.

2) As California considers potential updates to its regulatory framework on customer choice, it is possible that certain existing rules or statutes may need to be reconciled. Are there any “must change” and/or “must not change” statutes? What are these rules and statutes and why?

**Response:** See the response to Question 4 above.

**Attachment A**  
**Publications for the California Public Utilities Commission**  
**Electricity Choice Inquiry**

Imperfect Markets Versus Imperfect Regulation in U.S. Electricity Generation, Steve Cicala  
<http://www.nber.org/papers/w23053.pdf>

Ohio NOPEC White Paper  
<https://marketing.nopecinfo.org/acton/attachment/18528/f-014f/1/-/-/-/-/Customer%20Choice%20White%20Paper.pdf>

Pennsylvania Case Study  
[http://kleinmanenergy.upenn.edu/sites/default/files/A%20Case%20Study%20of%20Electric%20Competition%20Results%20in%20Pennsylvania\\_0.pdf](http://kleinmanenergy.upenn.edu/sites/default/files/A%20Case%20Study%20of%20Electric%20Competition%20Results%20in%20Pennsylvania_0.pdf)

Electricity & Natural Gas Customer Choice in Illinois  
[http://media.mlive.com/business\\_impact/other/Illinois%20Energy%20Reform%20Feb%202014%20final.pdf](http://media.mlive.com/business_impact/other/Illinois%20Energy%20Reform%20Feb%202014%20final.pdf)

Econometric Assessment by Agustin Ros, NERA  
[http://www.nera.com/content/dam/nera/publications/2015/PUB\\_Econometric\\_Assessment\\_Elec\\_Demand\\_US\\_0615.pdf](http://www.nera.com/content/dam/nera/publications/2015/PUB_Econometric_Assessment_Elec_Demand_US_0615.pdf)

Five-Point Plan Next Wave of Restructuring, Public Utilities Fortnightly  
<https://www.fortnightly.com/fortnightly/2016/05/five-point-plan-next-wave-electricity-restructuring>

Competition at Work, J. Lesser  
<http://continentalecon.com/publications/cebp/2011.09.pdf>

Right Question – ElectricityPolicy.Com, Shelk & Thomas  
<http://www.electricitypolicy.com/images/2013/03/Sheik/Sheik-3-10-13-final-1.pdf>

Conjectures & Refutations - Electricity Journal, Lesser & O'Connor  
<http://www.sciencedirect.com/science/article/pii/S1040619014001511>

Regulation & Relevancy: Assessing the Impact of Electricity Customer Choice – ElectricityPolicy.Com January 2013 – link not available.