

POWER MOVES!

Newsletter of the New York Energy Buyers Forum Summer, 2000

HUNKERING DOWN IN PHASE III

As predicted, Phase III of deregulation in the Con Edison territory has been bumpy, to say the least. All of the following is happening at one time:

1. Many customers dropped out (or were dumped) when word got out that savings would be only a 1-3 mills (tenths of a cent) due to reinstatement of taxes and marketers running scared of summer pricing. As many (or more) megawatts dropped out as joined, including several universities and the Electric Power Procurement Alliance (an aggregation group of mostly commercial real estate managers). As a result, the program has been left open to new subscribers.

2. Starting June 1, the state sales tax was replaced by a "Compensatory Use Tax" of 4% and the gross receipts tax began a phaseout over the next 4 years; go to http://www.tax.state.ny.us/PDF/memos/sales/MO_O_4s.PDF for details.

3. Due to various wholesale forces, price volatility appeared and was seen for the first time in retail bills via the Market Supply Charge (MSC). As a result of the February shutdown of Indian Point 2 (due to a radioactive steam leak), the Market Adjustment Charge (MAC, which replaced the fuel adjustment charge) reflecting the increased cost of fuel to Con Ed for its last remaining large power plant. This double whammy has caused prices for the energy portion of some commercial customers' bills to double or triple (for July) what they were last year.



Keyspan's Ravenswood plant, as seen by Forum members who visited it during May's field trip.

To blunt the impact of wholesale price volatility, the NY ISO petitioned FERC for (and was granted) \$1,000/MWh (that's \$1/kWh) price caps on the prices that suppliers will get paid for power and ancillary services. Further to that end, at least one vendor (SmartEnergy.com) offered fixed rates for energy just above 8 cents/kWh (\$80/MWh). While limiting the impact of high summer pricing, such a plan also holds that price steady for a year through the winter when wholesale prices should drop back down below 4 cents. But it could have been worse. Fortunately, most of the summer (with the exception of an early May roasting) has been much cooler than normal, sparing us the ongoing price meltdown seen on the West Coast.

Many customers are waiting until all of Con Ed's load opens to competition on November 1 (just after the end of the commercial cooling season) to see how vendors retool their offerings at that time. It is likely, however, that the summer of

2001 may also prove challenging since most of the planned increases in generation in New York State will not be ready for startup until at least a year thereafter.

Such generation expansions are moving ahead, with Keyspan announcing a 250 MW increase at Ravenswood, Enron adding 80 MW at its Linden, NJ facility, and various new power plants being approved (such as the PG&E 1,000 MW Athens plant). No real answers have appeared, however, to address the load pocket restrictions built into Con Ed's constricted transmission system into New York City. Until more capacity is seen in the 5 boroughs, high local summer pricing will likely continue for some time.

A few changes are on the horizon that may slightly reduce local transmission and distribution (T&D) charges. Beyond the 2% per year rate reduction mandated by the 1997 settlement, there may be other T&D reductions if excess revenue received by Con Ed (due to the booming economy) is used for that purpose. See the article on the global settlement for more details.

STEAM SETTLEMENT YIELDS MAJOR IMPROVEMENTS

Many Forum members use Con Ed steam instead of running boilers, and electric deregulation has also impacted steam prices. Several of Con Ed's steam plants generate power, and for years the electric side of the utility had been subsidizing the steam side (by as much as 25% of the steam bill). For a while, it looked like steam rates might jump when that subsidy was removed. After a great deal of artful negotiation by the Forum and its allies, rate increases were limited, improvements were obtained in how Con Ed's revenues will be allocated, and new steam supply options were created.

For those not versed in the intricacies of the utility steam system, it serves about 2,000 customers, all in Manhattan below 96th St. By providing steam for cooling as well as heating, that system serves to limit the peak electric

demand that would be seen if all chillers were instead run by electricity. Its continued vitality is thus of importance to all Con Ed power customers, as well.

Concerns were raised regarding the impact of these issues on future steam rates. Last November, Con Ed applied for a significant steam rate increase, resulting in an extensive proceeding in which the Forum and others were active participants. In a parallel proceeding, new ways to maintain and expand the use of the utility's steam were being examined. Those deliberations have now resulted in settlements that ensure steam rates remain reasonable, and provide steam customers with new opportunities for controlling their costs.

Forum members received a detailed memo on the new steam tariff by e-mail in mid-July. Below is a synopsis of that memo.

- The revised tariff covers the 4-year period from 10/1/00 through 9/30/04.
- The base rate (i.e., no fuel adjustment) will increase by about 5% in the first year, followed by a 3-year base rate freeze. Even that increase will be mitigated by an expected \$26M in net fuel savings over the 4-year term, so the actual rate increase (including fuel adjustment) will be about 3.4% in the first year, just under 1% in the second year, about .3% in the third year, and no increase in the fourth year.
- Revenue from the sale of Con Ed's First Avenue properties related to the steam system will be used to net out existing depreciation expenses not yet recovered (thus limiting future rate hikes).
- The East River power plant will be significantly upgraded ("repowered"), yielding net efficiency benefits to be used to reduce the steam fuel adjustment charge.
- Subsidy of steam rates by electric rates will cease at the end of the 5-year electric deregulation settlement (i.e., 2002). Any increase in steam rates will be reflected in the fuel

adjustment charge, as mitigated by savings from sale of First Avenue properties and savings from repowering the East River plant.

- To reduce the volatility of steam fuel costs, Con Edison will develop a strategy for hedging fuel price variations through use of gas and/or oil futures contracts and advance purchases (i.e., "forward contracts").

- Three new tariff options were created:

1. a new Back-Up/Supplementary Service rate - customers having (or installing) their own boilers serving the same loads as Con Ed steam may now use utility steam as a back-up or additional energy source

2. a pilot Transportation Service rate - steam from a "Third-party supplier" (not Con Ed and not the customer) may be injected into Con Ed's pipes and retrieved through the existing steam connections in other buildings

3. an option to seek a Special Contract - steam service contracts may be privately negotiated with Con Ed to retain and attract customers with viable competitive alternatives to Con Edison's steam service (e.g., a cogen plant or a new boiler plant).

These options are the first of their kind in any utility steam system in the U.S.

A parallel steam proceeding resulted in a new Steam Air Conditioning Discount Rate Program. Starting next October, customers replacing or installing steam-driven A/C equipment for summer cooling receive a \$2.00/Mlb (roughly 20%) discount on such summer steam during the 2-year term of this program. When combined with subsidies presently available from NYSERDA for new steam A/C systems, such discounts merit serious consideration by those looking to replace or expand existing chiller plants.

A slight change in City water/sewer rates will also affect steam rates. Water rates are to go up 1% over last year and since sewer rates remain equal to 159% of the water rate, they will also go

up 1% over last year's rate. Those higher rates will impact steam customers because, for the first time, they will see separate charges on their steam bills for the condensate they discharge into the sewer system, ranging from 67% to 90% of the amount of steam measured by their meter.

For details on the water rate change, go to:

<http://www.ci.nyc.ny.us/html/dep/html/press/print/wboard9pn.html>

GLOBAL SETTLEMENT ON THE HORIZON

Due to a variety of factors, Con Ed is willing to re-open the last 2 years (4/1/00 to 3/31/02) of the 1997 settlement that brought retail access. Con Ed would like to extend it to 3/31/05. In return, it has entered into discussions with the Forum and its allies on the following issues.

Overearnings - Due to the booming economy, Con Ed is earning more than its allowed rate-of-return, reportedly by more than \$100 million. Some (or all) of that excess could be farmed back to T&D rate reductions over the next several years.

Divestiture proceeds - there is a big difference between what Con Ed says it earned on the sale of its non-nuclear plants and what PSC staff claims was earned.

Savings from Con Ed's pending merger with Northeast Utilities - in its filings to the PSC, Con Ed promoted this merger as resulting in \$1.3 billion of net cost savings over 10 years, some of which is related to electrical operations. How much of those savings will customers see on their bills?

Sale of the First Avenue properties - the Waterside electric/steam plant and adjacent parking and other properties constitute prime real estate on the east side of Manhattan. Developers have been salivating over this unique opportunity, and (according to the NY Times) offers as high as \$630M have been made. Just how much of that money would be seen by

stockholders or electric customers is at issue. In a separate steam settlement (see Steam article), a process for allocating some of those proceeds has been established.

Other issues - a variety of items may also be part of such a settlement, including the further general unbundling of retail rates.

In total, this action (according to press reports) could involve the distribution of up to \$1B in customer benefits. Other issues (such as the "bottom up" unbundling of retail rates) could have far-reaching impact on electric rates under deregulation, possibly creating competition in portions of the 75% of electric bills that are still Con Ed's monopoly control. The Forum plans to be active in these proceedings, which could set

the pattern for electric rates and utility competition for the next 5 years.

September's Meeting Topic

"Playing the Weather Card: How to Manage Temperature Uncertainty" features a panel moderated by Scott Mathews, marketing director of United Weather Corp., on how to employ weather derivatives to control energy costs related to heating and cooling. Such financial instruments are now being used extensively by utilities and large energy users to hedge their exposure to variations in degree-days (up or down). See the attached flyer for further details. Come to the Forum's Sept. 20 meeting to learn how commercial end users are now taking advantage of this new option!