

# Re-Verticalizing Electricity

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Presented to  
**Harvard Electricity Policy Group**  
**Thirty-Fifth Plenary Session**

**June 4, 2004**

# Re-Verticalizing Electricity

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- Is it happening?
- Is it a problem?
- What are appropriate policy responses?

# Residual Obligations

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- **Electric utilities have residual service obligations post restructuring (e.g. POLR).**
- **Originally intended as transition services, but now appear to be perpetual.**
- **Meeting residual service obligations is complicated by customer switching rights.**
  - **All of the traditional load risks (e.g. weather)**
  - **Plus asymmetric risk of customer switching**

# The Procurement Problem

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- Utilities no longer own generation, so must purchase power to meet service obligations.
- Power markets are volatile.
- There are many feasible procurement plans.
- In many cases regulators have not established clear procurement criteria.

# Challenges

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- **Utilities have a high degree of exposure to regulatory risk. (Can *always* identify a lower cost procurement plan after the fact.)**
- **Credit quality diminished by sale of generation and loss of exclusive service franchise.**
- **Many participants anxious about long-term performance/reliability of wholesale market.**

# Procurement Models

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- **Portfolio Model**: acquire/manage a portfolio of contracts to meet residual obligations, supplemented by balancing in “spot” market.
- **Transfer Model**: bid out residual service obligations to third-party suppliers.
- **Ownership Model**: retain/acquire generation assets to back residual service obligations.

# Motivation for Re-Integration

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- **Ownership of generation assets appears to be attractive as a risk management strategy.**
  - **Hedge long-term price risk**
  - **Enhance credit quality**
  - **Mitigate regulatory risk**
  - **Assure long-term reliability**

# Policy Responses

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- **Establish competitive, transparent, and standardized procurement processes.**
- **Define basis for exceptions to the rule that utility does not own generation.**
- **Anything to promote well functioning wholesale markets.**