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**MIDWEST ENERGY OUTLOOK
THE ROLE OF COMPETITIVE POWER
SUPPLIERS**

ENERGY MARKETS IN TURMOIL
May 17, 2001

Freddi L. Greenberg



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MIDWEST INDEPENDENT POWER SUPPLIERS COORDINATION GROUP (MWIPS)

**1603 Orrington Avenue, Suite 1050
Evanston, Illinois 60201
Telephone: (847) 864-4010
Facsimile: (847) 864-4037**

**Freddi L. Greenberg
Executive Director and General Counsel**



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MWIPS Members

- **Aquila**
- **Calpine Corporation**
- **Chevron Energy Solutions**
- **Coral Energy**
- **Dominion Energy, Inc.**
- **Dynegy, Inc.**
- **Enron Corporation**
- **Indeck Energy Services**
- **Midwest Generation**
- **Mirant Corporation**
- **NRG Energy, Inc.**
- **Peoples Energy Resources Corporation**
- **PG&E National Energy Group**
- **Tenaska, Inc.**
- **WPS Power Development, Inc.**



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National Trend Toward Competition

- **Customer-driven phenomenon**
- **Competition replaces regulation**
- **Wholesale electricity business becomes a commodity sales business**
- **Wholesale competition offers benefits even in the absence of retail competition**

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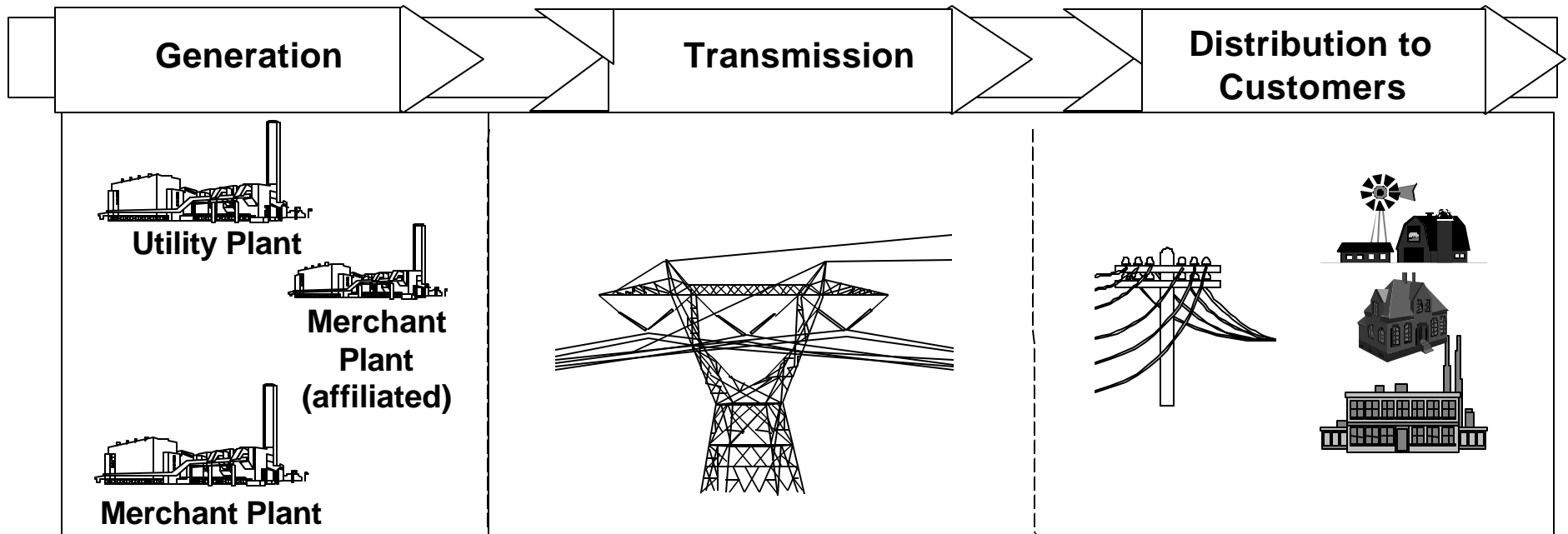
Regulation v. Competition

- **Regulated Environment**
 - focus on regulating profits of the monopoly provider
 - the way to increase profits is to increase ratebase
 - regulated cost-of-service rates
 - over 80 years, the cost structure has risen

- **Competitive Environment**
 - profits regulated by competitive pressures
 - the way to be profitable is to be the lowest cost producer and to offer products that meet customer needs
 - market-based rates
 - shift in risk from customers to suppliers

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Electricity Competition: The Basics



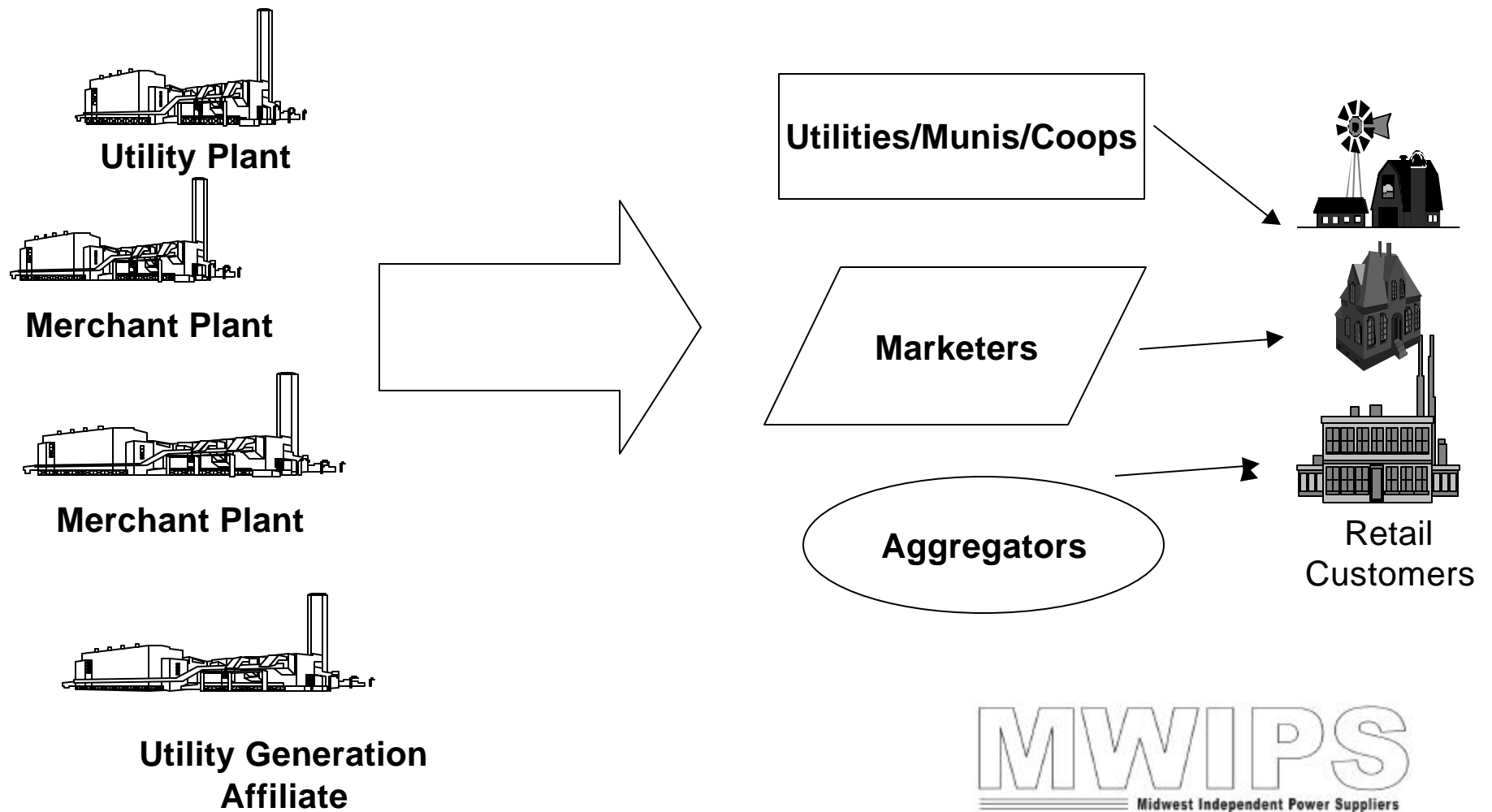
Merchant plants compete to supply electricity

Non-discriminatory access to transmission system

Monopoly utility continues to own and operate local delivery system

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Evolution of Wholesale Competition



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Features Of A Competitive Market

- **Wholesale competition shifts risks from customers to suppliers**
- **Competitive generation equals bid-based generation - generators bid to supply power**
- **Wholesale competition includes forward markets, day-ahead markets, real-time markets and power purchase contracts**

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Competitive Market Shifts Risks From Customers to Suppliers

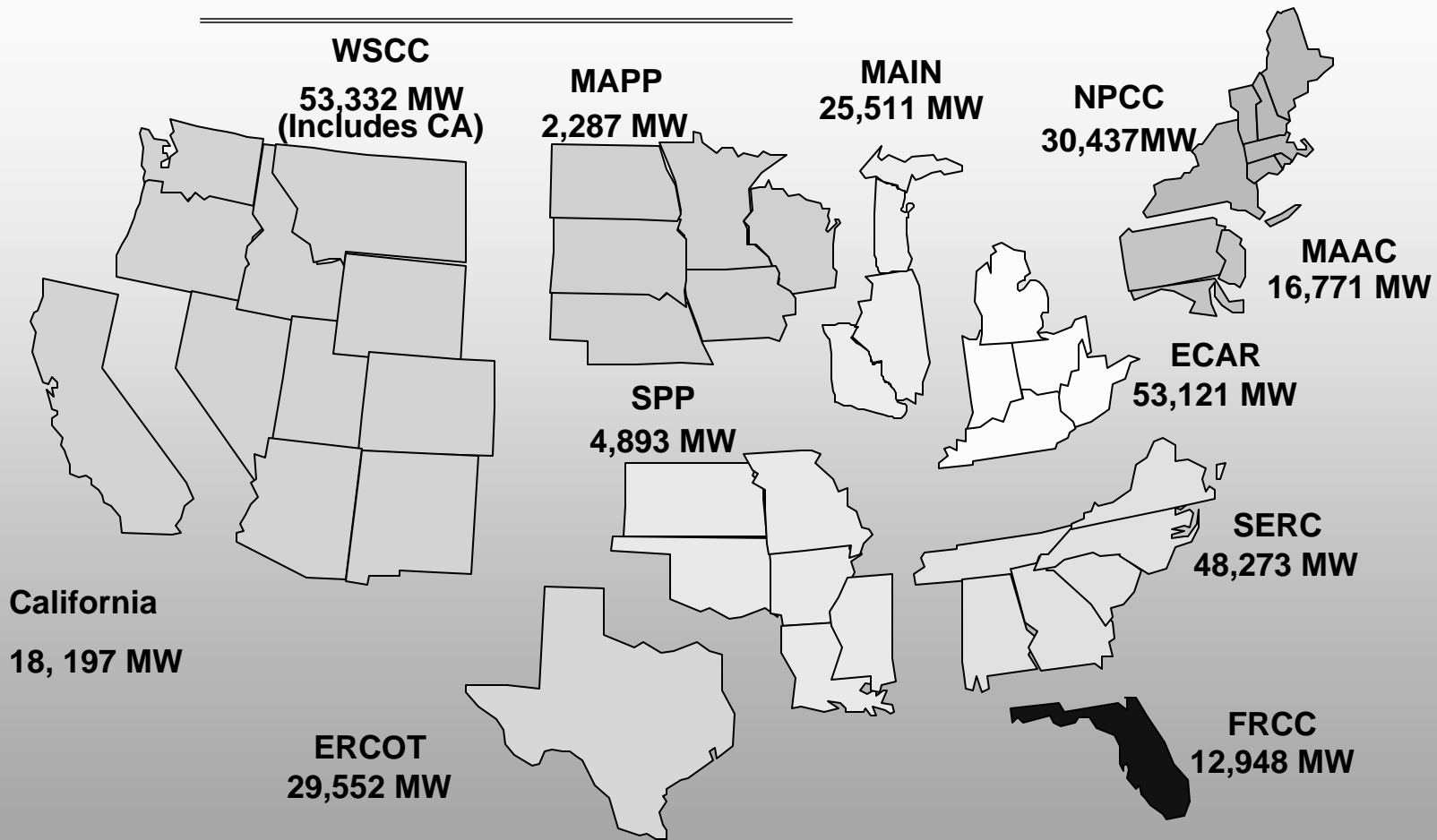
- **Price Risk**
- **Delivery Risk**
- **Volume Risk**
- **Performance Risk**
- **Credit/Counterparty Risk**
- **Currency Risk**
- **Regulatory Risk**
- **Operating Risk**
- **Technology Risk**
- **Labor Risk**
- **Interest Rate Risk**

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What is a Merchant Plant?

An electric power plant that sells into a competitive wholesale market on a commodity basis without the benefit of a captive customer base or a regulated utility ratebase

Announced Merchant Plant Additions



Source: Electric Power Supply Association, February 2001

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The Market will Benefit from the Addition of Competitive Generation

- **Investment risk shifts from captive ratepayers to merchant plant shareholders**
- **New lower cost plants and multiple suppliers put downward pressure on wholesale prices -- leading to lower retail prices**
- **New technology is cleaner and more efficient**
- **New products will respond to market demand**
- **Reliability of the electricity system is enhanced through the addition of new resources**
- **Electricity becomes a commodity traded on a weekly, daily, hourly basis**

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HOW CAN STATES ENCOURAGE COMPETITIVE ELECTRIC SUPPLIERS TO ENTER THE STATE?

Streamline permitting process for generation

- **Eliminate need analysis**
- **Eliminate multi-site alternatives**
- **Objective and defined criteria for approval**
- **Strict and short deadlines for agency action**
- **Regulatory certainty is important**

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HOW CAN STATES ENCOURAGE COMPETITIVE ELECTRIC SUPPLIERS TO ENTER THE STATE?

Access to transmission

- **Standardized interconnect agreement**
- **System upgrades to accommodate new bulk power market**
- **Streamline permitting for transmission**
- **FERC jurisdiction, but states can have impact**

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HOW CAN STATES ENCOURAGE COMPETITIVE ELECTRIC SUPPLIERS TO ENTER THE STATE?

Tax equity

- **Fuel Tax**
- **Sales/Gross Receipts Tax**
- **Revenue sharing to encourage local support**

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COMMON MISCONCEPTIONS ABOUT COMPETITIVE POWER SUPPLIERS

- They will build only peakers
- They will build only gas-fired plants
- They will not supply in-state needs, but plan largely to sell to other states
- They will not commit to contracts to supply power to utilities
- They will not consider brownfield sites
- They are “out of state” companies with no vested interest in our state

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REALITIES ABOUT COMPETITIVE POWER SUPPLIERS (I)

- They will respond to market signals as to fuel
 - Competitors do invest in coal plants
 - Level playing field needed here
- They will respond to market signals as to plant type
- Plants are generally sited where capacity is needed
 - Transmission access can be uncertain and comes at a cost
 - Power markets are increasingly regional
 - Utilities have always bought and sold power from one another
 - Local system benefits even when power is exported

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REALITIES ABOUT COMPETITIVE POWER SUPPLIERS (II)

- **Merchant plant developers will contract for all or a portion of plant output**
 - They do not need contracts for financing
 - Merchant developers will contract for all or a portion of plant output
 - Merchant plant developed in response to concern about long term contracts
- **They are sensitive to concerns about greenfield sites**
- **An out-of-state company that invests millions of dollars in a state becomes an in-state “citizen” with a vested interest in the state’s economy**

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HOW CAN STATES ENCOURAGE COMPETITIVE ELECTRIC SUPPLIERS TO ENTER THE STATE?

Let the market work – “If you open it, they will build !”