

2009-10 Energy Policy for Montana

Prepared by Sonja Nowakowski

November 2009

Part VI of IX "Reducing regulations that increase ratepayers costs"

Governor Schweitzer's Energy Policy statement related to energy costs:

"Montana has suffered from the effects of electricity deregulation in the past decade. If that market can't be policed adequately and provide affordable energy for Montanans, we will consider creative ways to re-integrate Montana's electrical energy generation, transmission and distribution and the possible re-regulating of prices. We need to seek ways to ensure that adequate amounts of the electric energy produced at the lowest cost in this state are reserved for Montana's businesses, industries and families."

ETIC Energy Policy statement: (This is a DRAFT statement that has not received ETIC approval. It is meant ONLY as a starting point for ETIC discussion)

Findings

The Montana Public Service Commission (PSC) ensures that public utilities in Montana provide adequate service at reasonable rates. The PSC strives to balance the interests of ratepayers with a utilities' need to earn a fair rate of return on their investment. The Montana Consumer Counsel represents Montana consumers in utility proceedings before the PSC and in appropriate proceedings before the Federal Energy Regulatory Commission, and appropriate state and federal court proceedings.

In 1997 the Montana Legislature deregulated the electric utility industry. The change was to bring competitive markets to Montana and provide Montana electricity consumers with cheaper prices over the long term. For the most part, competitive markets developed to serve large industrial electricity customers, and most of those customers selected alternative electricity suppliers. Market volatility and the lack of significant small-customer retail competition, however, forced the 2007 Montana Legislature to effectively put an end to full customer choice. The "reregulation" bill approved by the Legislature in 2007 allows NorthWestern Energy to more effectively pursue long-term, low-cost contracts for its customers and/or to build its own generation facilities.

The cost of electricity changed dramatically following 2000. Rising demand, prolonged drought, and a lack of new supply, pushed energy prices higher and higher. Montana's current residential electricity rates are, on average, lower than national averages. In the West, Montana's rates are currently comparable to neighboring states. However, concerns remain that Montana's largest utility must purchase significant amounts of electricity in a volatile market to supply Montana customers.

ETIC recommendations: ?

Recommendations (Examples from other state energy policies):

Idaho (During the 2006 session, the Idaho Legislature passed House Concurrent Resolution No. 62, directing the Legislative Council Interim Committee on Energy, Environment and Technology to develop an integrated state energy plan. Idaho's rank among the fifty states for average electricity prices in 2005 was the second lowest. Idaho's rank among the fifty states for residential natural gas prices in 2005 was the sixth lowest. Idaho has not deregulated

natural gas or electricity. In June 2009, the average retail price of electricity for residential customers was 8.31 cents per kilowatt hour.¹)

Idaho recommendations and policies:

- Idaho's existing energy resource base has resulted in some of the lowest electricity and natural gas prices in the country, providing enormous benefit to Idaho consumers. However, new energy resources are becoming increasingly costly, and Idaho's position as an importer of more than 80 percent of our energy needs leaves Idaho consumers vulnerable to issues that are outside of our control.
- Conservation and renewables diversify the state's resource base, reducing its dependence on imported fossil fuels and providing insurance against increasing fuel prices. Idaho relies on imported fossil fuels for approximately 80 percent of its energy needs. This exposes consumers to geopolitical events such as instability in the Middle East that drive up the price of crude oil. It also means that most of the \$3 billion dollars that Idahoans spend each year on energy are sent outside the state, providing little secondary economic benefit.
- A growing demand in the Northwest and new pipeline capacity between the Rocky Mountains and lucrative markets in the Northeast are likely to erode Idaho's locational price advantage over the next several years. This Energy Plan recommends that Idaho support responsible exploration and production of natural gas and expansion of the natural gas infrastructure that serves Idaho customers.
- The state should maintain Idaho's low cost energy supply and ensure access to affordable energy for all Idahoans. The Idaho Public Utilities Commission (PUC) should support market transformation programs that provide cost-effective energy savings to Idaho citizens.
- The Idaho PUC and Idaho utilities should consider adopting rate designs that encourage more efficient use of energy. Idaho citizens and businesses have benefitted from a stable, reliable and low-cost electricity supply, and this Energy Plan does not recommend major changes to the structure of Idaho's electricity industry.

Texas (The "2008 Texas State Energy Plan" was produced by Governor's Competitiveness Council in July 2008. The plan was produced by an executive agency and was reviewed by public and private leaders, appointed by the Governor. In 2002, Texas deregulated its natural gas and electricity markets. In June 2009, the average retail price of electricity for residential customers was 12.93 cents per kilowatt hour.)

Texas recommendations and policies:

- Texas should resist attempts to re-regulate the market and instead focus on removing barriers to lower-cost generation resources. Retail competition has brought new competitors, products, and services to the market and promises to bring forward technology that will give residential customers the real-time ability to monitor their electricity usage with the goal of reducing consumption or moving it off-peak. However, rising natural gas and energy prices have led some to conclude that restructuring has failed to deliver its promised benefits to customers. As a result, proposals to re-regulate the industry are introduced every legislative session. Such proposals cause legal and

¹ Energy Information Administration, "Average Retail Price of Electricity to Ultimate Customers by End-use Sector, by State, June 2009 and 2008, Table 6.6.A.)

regulatory uncertainty, making it more difficult for energy companies to gain access to capital markets and, ultimately, to deploy the new technologies and products that could enable electricity customers to save money.

- With such a large amount of natural gas generation meeting the electricity needs of Texas customers, the impact of high and volatile natural gas prices has significantly increased the cost of electricity since the market opened and made it more difficult for customers to manage and plan for their electricity usage. The Public Utilities Commission (PUC) should revisit its certification requirements for retail electric providers and evaluate whether current standards are adequate given the significant change in natural gas and wholesale electricity market conditions since market opening.
- The events of May and June 2008 will undoubtedly cause some to call for a re-regulation of the electricity market. However in order to reduce electricity prices in Texas, natural gas must be moved off the margin by the addition of a large amount of non-natural gas baseload generation. While significant amounts of nuclear and coal generation are under development, uncertainty about the potential for costly regulation of CO₂ emissions is preventing these lower cost resources, especially coal, from being developed in the quantities sufficient to lower electricity prices. Also, uncertainty about long-term storage of spent nuclear fuel is having the same effect on nuclear generation.
- The power generation and retail electric sectors are, at this point, generally unregulated, with prices and investment decisions determined by the forces of competition. The transmission and distribution sector remains fully regulated by the PUC, with rates set on a cost-of-service basis and open access guaranteed to all buyers and sellers of electricity.
- In 2006, in response to a request from the Legislature, the PUC performed an analysis of the rates that would have been charged had regulation been in effect, the rates charged by the affiliated retail electric providers, and the prices offered by the competitive market through 2005. The PUC concluded that even customers who had remained with the affiliated retail electric providers paid lower prices than they would have under continued regulation. Customers also had competitive options that resulted in an estimated savings of \$800 to \$1,440 between January 2002 and December 2005.
- Even with this continued rise in natural gas prices, Texas's competitive retail market is continuing to provide options for customers that mitigate these severe price increases. While natural gas prices have risen almost 300 percent since market opening (as of June 3, 2008), competitive offerings include prices that are less than a 40 percent increase from the regulated rates that existed at the end of 2001, even though Texas' heavy reliance on natural gas sets the price of all fuel used to generate electricity.

Background

Customer of a Montana public utility, such as NorthWestern Energy or Montana-Dakota Utilities Co., look to the PSC as the state statutory agency that is charged with ensuring that Montana public utilities provide adequate service at reasonable rates. The Montana Consumer Counsel is the constitutional entity that is responsible for representing residential and small business interests in matters before the PSC.

The PSC has very broad regulatory, supervisory, and investigative powers over public utilities. The PSC is charged with encouraging efficient utility operations, effective use of utility services, and efficient rates. It ensures that every public utility furnishes reasonably adequate electricity services and facilities and reasonable and just prices. When the PSC sets electricity rates, it must provide public notice of the proposed changes and conduct a hearing on those proposed changes. Electricity customers affected by the proposed change in rates may formally

intervene and participate in the rate case proceeding or participate more informally by submitting comments to the PSC either in writing or in person at the public hearing.

Customers of a Montana electric cooperative are considered a part owner of that cooperative. Electric cooperatives are not-for-profit entities that are democratically controlled by the members of the cooperative. Electric cooperatives are not regulated by the PSC. The electric cooperatives are self-regulated by their members. Cooperative members democratically elect a board of directors that sets customer protection policies and establishes the rates for electricity distribution and supply. There are 25 not-for-profit distribution electric cooperatives in Montana with about 216,846 meters served.

A municipal electric utility has the power and authority to regulate, establish, and change, as it considers proper, rates, charges, and classifications imposed for electricity services to its citizens. Rates and charges must be reasonable and just. If a municipality proposes a change in electricity rates, it must hold a public hearing. A municipal electric utility is required to adopt rules with the concurrence of the governing body of the municipality for the operation of the utility that protects municipal customers. The city of Troy is Montana's only municipal electric utility.

In January 1997, the Montana Power Company and a number of Montana's large customers brought forward a legislative proposal (Senate Bill No. 390) to deregulate retail electricity supply. Montana's electricity laws and policies have received significant public attention and scrutiny since that time, when Montana decided to deregulate electricity supply and opted to allow some Montana consumers to choose, given a competitive market, their own electricity supplier. At the time, it was a fundamental policy shift for the state from regulating the price of electricity supply to allowing competitive markets to set the price of electricity supply.

Competitive choice, however, did not develop for small residential and commercial customers in the state, and in 2007, the Montana Legislature undid portions of the Electric Utility Industry Restructuring and Customer Choice Act. The "re-regulation" bill, as it was often called, allows NorthWestern Energy to own electric power plants again and to dedicate the power it produces to Montana customers. It significantly tailored customer choice, limiting the ability of retail customers with a monthly demand of less than 5,000 kilowatts to migrate to other electricity suppliers if those customers were receiving electricity from a public utility prior to October 2007.

Prior to the 2007 law, a NorthWestern customer could choose an electricity supplier. For members of a cooperative that did not open up to competition or Montana-Dakota Utilities Co. customers, the price of retail electricity supply

Average Retail Price of Electricity to Ultimate Customers by End-Use Sector, by State June 2009 (Cents per kilowatt hour)		
State	Residential	All Sectors
California	15.01	14.38
Nevada	12.02	10.11
Arizona	11.27	10.09
New Mexico	10.37	8.37
Colorado	9.97	8.25
Montana	9.36	7.32
Wyoming	9.16	6.06
Utah	9.12	7.56
Oregon	9.04	7.54
Idaho	8.31	6.93
Washington	7.94	6.79
Pacific Average	12.78	12.06
Mountain Average	10.61	8.72

Source: EIA

remains set by either the cooperative board or the PSC, respectively. The original Montana electricity restructuring law set up a transition period for all NorthWestern customers to choose an electricity supplier by July 1, 2002. Market volatility and the lack of significant small-customer retail competition forced the 2001 Montana Legislature to delay full customer choice until July 1, 2007. Subsequent changes made by the 2003 Montana Legislature further extended the date for full customer choice until July 1, 2027, and with the approval of the "Electric Utility Industry Generation Reintegration Act" by the 2007 Legislature, the transition to customer choice ultimately ended for NorthWestern

The 2009 Legislature continued to take steps to allow for utility integration. In approving House Bill No. 294, the Legislature allowed a natural gas utility that had restructured to acquire natural gas production and gathering resources and include them in rate base. The revisions to the law also establish procedures for a utility to apply to the PSC for approval to rate-base prior to the acquisition.

In 2008 and 2009, NorthWestern Energy's 320,000 customers saw a 2 percent increase, but the company offset that amount through future actions based on a negotiated agreement. NorthWestern recently filed a motion with the PSC to delay the filing of an anticipated general rate case while the company reviews the implications of a recent Internal Revenue Service decision.

In 2008 Montana-Dakota Utilities, which last increased rates in 1987 and serves about 24,000 customers, also increased residential customer rates. The PSC allowed a 7.1 percent increase experienced by residential electricity customers to become permanent and allowed an additional 1.4 percent increase for January 2009.

In July 2008 NorthWestern Energy customers were paying 10.2 cents per kilowatt-hour for electricity. (An average household uses about 750 kwh a month). The NorthWestern rate was 20 percent higher than the second-highest major utility electric rate in the region, according to an analysis by the Billings Gazette State Bureau.² NorthWestern Energy must buy electricity on the open market, making it vulnerable to market prices for electricity.

When compared to other Mountain states, however, Montana's rates are comparable and even low in some areas. In June 2009, the average retail price of electricity for residential

Average retail price of electricity to ultimate customers: Total by End-use Sector, 1995-June 2009 (Cents per Kilowatt hour)		
Period	Residential	All Sectors
1995	8.4	6.89
1996	8.36	6.86
1997	8.43	6.85
1998	8.26	6.74
1999	8.16	6.64
2000	8.24	6.81
2001	8.58	7.29
2002	8.44	7.2
2003	8.72	7.44
2004	8.95	7.61
2005	9.45	8.14
2006	10.4	8.9
2007	10.65	9.13
2008	11.36	9.82
Through June 2009	11.47	9.86

Source: EIA

² "NWE's electric rates highest among region's big utilities", Billings Gazette, Mike Dennison, July 13, 2008.

customers in Montana was 9.36 cents per kilowatt hour³. The numbers in 2009 show changes in the economy, and a reduction in electric costs. In July 2009, NorthWestern Energy residential customers were paying an average of \$70.46 a month or 8.78 cents per kilowatt-hour for electricity. In July 2009, MDU's Montana residential customers were paying an average of \$68.25 a month or 9.1 cents per kilowatt-hour.

In July 2009, for the 24 retail electric distribution cooperatives that are members of the Montana Electric Cooperatives' Association, cooperative residential customers paid an average of \$84.63 a month or 9.8 cents per kWh for electricity. For all classes of customers, the average cost was 8.5 cents per kWh that same month. (All but one electric distribution cooperative is a member of the association.)

In 2008 the PSC allowed NorthWestern Energy to purchase the Colstrip 4 power plant and include it in rate base. The Montana Consumer Counsel argued the plant was too expensive, and NorthWestern's parent corporation was charging the utility subsidiary too much for the Colstrip 4 power plant. The monthly bill impact on an average customer (750 kWhs per month) is estimated to be less than \$3 for the next 10 years, when customers are projected to begin to see bill savings because Colstrip 4 costs are lower than the market, according to NorthWestern. The PSC found that the rates that would result from adding Colstrip to the supply portfolio would be just and reasonable. The Consumer Counsel disputed NorthWestern's estimated monthly bill impact and predicted increases of at least \$7 per month for all non-choice customers. "The PSC is fully aware that approving NorthWestern Energy's rate-basing proposal means customers' rates will be somewhat higher for several years, but the PSC finds the initial cost is justified by the benefit to customers from the relative rate stability that rate-basing contributes to the supply portfolio, as well as the benefit to customers from lower rates in the long term."⁴

Total U.S. electricity consumption fell by 4.4 percent during the first half of 2009 compared with the same period in 2008, primarily because of the economic downturn reducing industrial electricity sales. The expected year-over-year decline in total consumption during the second half of 2009 is a 2.3-percent decline, as residential sales begin to recover, according to the Energy Information Administration (EIA). The EIA expects electricity retail prices to show year-over-year declines next year for the first time since early 2003 because of lower fossil fuel costs for generation. The projected annual average 2010 residential electricity price of 11.4 cents per kilowatt hour is about 2 percent lower than the 2009 average.

Statutes related to electric rates

69-2-101, MCA PSC rates

Grants the PSC rulemaking authority for tracking and monitoring the rates charged by public utilities.

Title 69, chapter 3, MCA PSC regulation of utilities

The PSC has broad regulatory, supervisory, and investigative powers over investor-owned public utilities. The PSC can investigate the management of the business of all public utilities. PSC jurisdiction includes customer service and reliability standards and rates charged to retail electricity customers. Ratemaking procedures are outlined in part 3.

³ Energy Information Administration, "Average Retail Price of Electricity to Ultimate Customers by End-use Sector, by State, June 2009 and 2008, Table 6.6.A.)

⁴ Montana Public Service Commission, Final Order, Docket NO. D2008.6.69 ORDER NO. 6925f, November 13, 2008.

69-3-308, MCA Tracking of taxes and fees, rate adjustment

A public utility may separately disclose in a customer's bill the amount of state and local taxes and fees assessed against the public utility that the customer is paying. The PSC must allow a public utility to file rate schedules containing provisions for the automatic adjustment and tracking of Montana state and local taxes and fees, except state income tax, paid by the public utility.

69-2-216, MCA Customer fiscal impact analysis

After receiving notification of a proposed electrical generation facility or transmission facility or upgrade, the office of Consumer Counsel must complete an analysis outlining the fiscal impacts of the project on electricity customers in Montana. The analysis must include an estimation of how customers' rates may be impacted. Projects proposed by utilities and affiliates are exempt.

69-5-107, MCA Customer-owned facilities

Customers may construct, own, or operate electric service facilities for the customer's own use, and construction, ownership, or use may not cause the customer to be considered a utility. A customer may not duplicate existing electric service facilities.

69-8-201, MCA Customer choice -- limitations

"Undoes" portions of the 1997 utility deregulation act. It limits customer choice for small customers, but still allows larger customers to choose a new supplier under certain circumstances. The utility also must apply to the PSC for approval of an electricity supply resource.

69-8-215, MCA Ratepayer and shareholder protection

Provides protection for ratepayers and for the shareholders of innocent third-party purchasers for the errors or omissions of a predecessor utility.

Title 69, chapter 8, MCA Net metering

Public utilities must allow net metering if a customer chooses to generate his or her own energy using solar, wind, or hydropower to offset customer requirements for electricity. Its generating capacity can't be greater than 50 kilowatts. Cooperatives also offer net metering.

Title 69, chapter 3, part 20, RPS

"The Montana Renewable Power Production and Rural Economic Development Act" requires that public utilities and competitive electricity suppliers procure a minimum of 5 percent of their retail sales from eligible renewable resources through 2009, 10 percent between 2010 and 2014, and 15 percent starting January 1, 2015. Contracts to meet the requirements are eligible for advanced approval by the PSC. Upon advanced approval by the commission, the contracts are eligible for cost recovery from ratepayers. There are also three different cost caps established in meeting the standards.

69-3-712, Conservation in rate base

Authorizes utilities to purchase conservation or directly engage in conservation investments that have been approved by the PSC, with the cost-effective conservation measures to be at the customer's discretion, installed by either a private firm, the customer, or the utility. The statutes also authorize the PSC to make onsite audits to ensure compliance with the criteria set out in Title 69, chapter 3, part 7, MCA, and prohibit a utility that has placed the conservation in its rate base from claiming a conservation tax credit.

Title 69, chapter 3, part 6, MCA Qualifying Facilities

Federal law requires all state-regulated utilities to purchase qualifying facility power at either a freely-negotiated rate, or at a rate set by the state PSC.

69-8-426, MCA, Generation assets

Generation assets acquired by a public utility must be used by the public utility to serve and benefit customers within the public utility's Montana service territory and may not be

removed from the rate base unless the commission finds that customers of the public utility will not be adversely affected.

Article XIII, section 2, Montana Constitution. and Title 69, chapter 2, part 2, MCA, Montana Consumer Counsel

Represents Montana consumers in electric utility proceedings before the PSC.

69-3-1201 through 69-3-1206 and 69-8-419, and 69-8-420, MCA

NorthWestern and MDU submit their long-range plans for acquiring electricity supply resources to the PSC for review and comment every 2 years. If either utility is planning to construct a generation facility, the utility must undertake a planning process that looks at low-cost alternatives to the proposed generation facility.

CI0429 9299slec.