

Some Natural Gas Issues

Western Conference of
Public Service Commissioners

Remarks of Ron Binz, Competition Policy Institute

June 14, 2000

Competition Policy Institute

CPI is an independent, non-profit organization that advocates state and federal policies to bring competition to energy and telecommunications markets in ways that benefit consumers.

- Founded in 1996 by Debra Berlyn and Ron Binz
- Advised by a committee of leading consumer advocates from across the country
- Funded by grants from a variety of energy and telecommunications companies and associations
- Complete information at <www.cpi.org>

The questions...

- What do consumers want from natural gas restructuring?
- Will gas marketers serve small customers?
- Which outcomes of the monopoly system should we attempt to retain?
- What policy strategies should regulators consider to protect consumers?

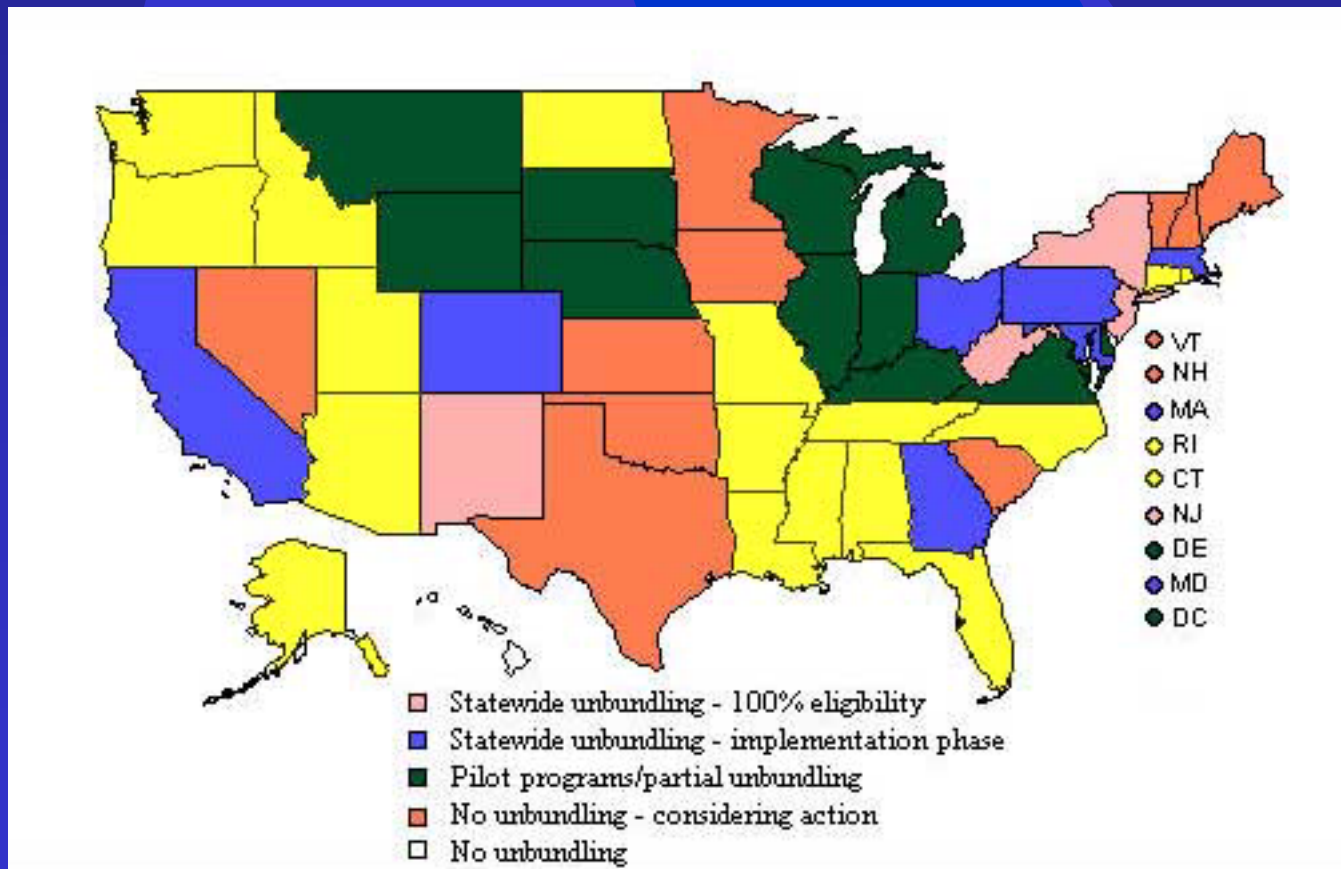
What do consumers want?

- There is a spectrum of consumer demand (and it is probably widening).
- Most consumers want a choice of suppliers.
- Almost paradoxically, consumers want simplicity.
- No compromise on quality and reliability.
- Consumers expect fair prices and predictability.

Caveat: Consumer demand is not immutable.

State of the States

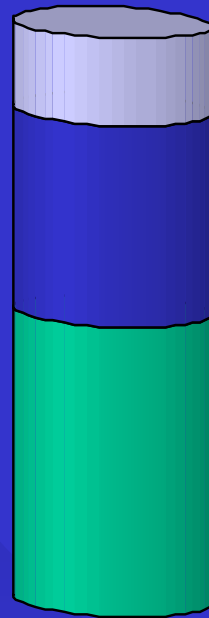
Residential Natural Gas Choice in March 2000



Will marketers serve small customers? And will consumers switch?

- The early evidence is mixed.
- Margin for competition is mainly customer costs (acquisition, metering, billing, customer care).
- Marketing skill will produce early advantages.
- Scale and customer targeting will be key.
- Attractiveness of small customer market is linked to status and role of LDC and to the provider of last resort issue.

The Competitive Margin



Customer Costs

Distribution Costs

Gas Costs

Mechanics that must be worked out

- Gas system balancing
- Allocation of upstream capacity
- Allocation of capacity behind citygate
- Storage
- Metering
- Reliability

Desirable features of the current monopoly system

- Customer understanding and acceptance
- Obligation to serve/default provider
- Universal service funding/bad debt handling
- Customer service practices
- Single bill

Advantages of a marketer-provided merchant function

- Customers have a choice for retail service
- Subjects gas customer-related functions and gas supply activities to competitive pressure
- Eliminates some costly regulation (e.g., prudence reviews of gas supply portfolios)
- Enables rebundling of gas service with other consumer services
- Likely to spur innovations in pricing and character of service

Potential disadvantages of a marketer-provided merchant function

- Loss of scale economies and operating economies for some functions of LDC.
- At least during a transition period, some consumers may be surprised by price volatility.
- Increased discrimination in pricing.
- New consumer issues will arise; slamming comes to natural gas.

Predictions

- Consumer savings will be relatively small.
- Consumers will generally accept retail natural gas competition, but not across all customer groups.
- Zero-sum price volatility will make more headlines.
- LDCs' continued presence as commodity supplier will retard entry by marketers.
- There will be relatively few marketers in a state or region serving small customers.
- Unbundling will spur rebundling natural gas with other consumer services, beginning with electricity.

Strategies for regulators

- Refine your vision of a competitive market.
- Give consumers the ability to protect themselves.
 - Information
 - Multiple providers
 - Ease of switching
- Keep marketers entry barriers low.
- Tailor protections narrowly to abuses.
- Analogize to non-utility industries.
- Help LDCs develop an exit strategy.