

N on-private Power Aggregation: New Markets for Public-private Partnerships

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The emergence of privately sponsored customer aggregation firms aimed principally at the private market in response to electric power deregulation was an obvious development, following the pattern set first in natural gas. Aggregators—whether independent, or associated with power marketers or ESCOs—bring with them not only the capability to enhance composite purchase power muscle, but to provide to aggregation customers valuable system planning intermediary services to structure lower overall costs, by, for example, better matching usage requirements.

The emergence of “non-private” aggregators in the public and the not-for-profit sector has not received as much attention, because those fields generally have been viewed as additional markets for the private sector rather than themselves entrepreneurial initiators of change. That viewpoint overlooks a salient fact: deregulation threatens these sectors themselves with privatization unless they respond proactively themselves.

This response is now beginning to emerge—in self defense. It presents the private sector with an opportunity novel in the domestic power arena, but increasingly common in other formerly public service fields: the creation of forms of “public-private partnerships” able to justify their existence to consumer citizens in the marketplace, on both an economic and a social basis, and backed by strong political muscle.

It is useful to recognize—and to analyze the ramifications of the fact—that the non-private sector currently is not unitary. It is comprised of three different types of responses to deregulation:

- (1) bottom up “municipalization,” whereby local public jurisdictions seek to seize for their political constituents deregulation economic benefits that may go outside of their communities to the large business sectors;
- (2) “top down” public power and coop efforts to transform themselves and thereby preserve their institutional role in the changing marketplace; and
- (3) “clustering” efforts by institutions historically serving not-for-profits in other fields (and concerned with the competitive viability of their not-for-profit customers in a privatizing society).

By focusing on the common and then the special aspects of each of these non-private submarkets—regulatory and institutional—private entrepreneurs can identify a number of concrete possibilities for useful collaboration. Examples of each type of collaboration now can be identified.

The common concern of each of the non-private constituencies has its generic foundation in the fact that FERC Order No. 888 fundamentally focused on two goals: (1) opening competitive markets on the blanket theory that all would be benefited, both pricewise and in terms of product differentiation and (2) providing electric power firms which had been developed in the pre-deregulation environment with transitional reimbursement for prior investments rendered non-competitive. There has necessarily been some breakage of other interests affected by this approach, notably in the nonprivate sector.

As a general matter, as a consequence of utility exit fee requirements, the economic rate reduction benefits of wholesale deregulation by FERC have been primarily limited to existing wholesale customers. Many existing public power firms furthermore have found their prospects for competition with imported power not encouraging and now are facing Federal legislative efforts to circumscribe their ability to compete in power export markets, even where they are competitive.

Bundling of disaggregated electric services and packaging of electric services with related end use consumer, convergent non-power services has proved to be slow in its implementation. ISOs now being established at the regional and state level are homogenizing the delivery of unbundled electric services.

Overall, as a result of utility stranded cost recapture, except to the extent of specially contrived securitization arrangements, the benefits to residential retail customers—certainly at least pending the introduction of vigorous effective real retail competition—remains to be seen.

In response to these common related regulatory developments, different groups in the non-private sector have responded differently.

BOTTOM UP MUNICIPALIZATION

One response to emerging disillusionment by consumers to the perceived limited impact of deregulation has been the emergence of “bottoms up” support for community franchising and energy development—notably in upstate New York and New England. In part, these initiatives are linked to the extent of surviving local franchise in the electric power arena, relative to state-regulated monopoly investor owned utility franchising.

The same legal stratagem which virtually ended dispersed industrial cogeneration relative to franchised investor owned companies effectively cut back local franchise authority as well. The concern of local franchise deregulation critics is clear: blind efforts to wipe out local community authority and forms of community choice in the name of clearing “market barriers” potentially in the absence of public involvement could open the way to predatory market practices by power marketers and in consumer related fields.

Private developers, like Energy Choice in New York, have begun to collaborate with municipalities seeking to address this issue, encouraging municipal use of powers of condemnation of existing investor owned assets; construction of parallel facilities; annexation and “muni-lite” (provision for a minimal level of municipal control as a grounds for wholesale purchase rights). FERC has directed the utility to provide transmission in two such cases and derived one “muni-like” case. The majority of cases are still in process or on hold.

It is an on-going battle which the advent of retail competition may or may not obscure.

In New York, one effort seeking to go forward is relying on legal interpretation of Order No. 888 to the effect that if service from multiple alternative private users was available pre-deregulation, then municipalization is available post-deregulation without requirement of the payment of exit fees. Its proposal is the subject of a local referendum, which, if passed, will entitle the municipality to act pursuant to the State's "quick take" eminent domain law, subject however to FERC action.

The key argument underpinning community energy developer claims of substantial future savings is that for individual consumers, only the energy part of their bills—roughly 25% of the whole—will be subjected by competition to deregulation. The balance of such bills will continue to be paid for basic utility services which will still be performed by the original provider, on a non-competitive basis.

If community energy municipalization becomes a more successful trend over time, other forms of private collaboration with public entrepreneurs besides aggregation would become possible—notably public finance of new facilities and securitization.

MUNICIPAL POWER/COOPERATIVES

Whether that will be the case, however, will be a function, in part, of whether existing municipal utilities and cooperatives, as a class, will continue to be viable players on the electric power scene. There is a growing school of thought that public power could only survive in the past in its non-entrepreneurial form because privately owned utilities were themselves so heavily regulated as not to be competitively as aggressive as they might have been.

In effect, to a significant extent, IOUs and munis each operated in a monopoly service territory. In particular, in the new era, while public power agencies which essentially are distribution systems are not necessarily threatened, those systems which own high cost generation and those that are diverse, diffusely governed joint action agencies (particularly if not very competitive) face considerable difficulties. There are certainly states like Nebraska (10% publicly owned power) where there are low prices, high reliability and community

sensitivity all embodied in the power system, as its legislator's commissioned reports have noted.

But many municipal agencies feel compelled to seek, in effect, types of product differentiation from the investor-owned competitors springing up all around them, if they are to stay in business. One key such public power strategy is load aggregation— of all or some of municipal services—both as a revenue source and a basis to enhance competitiveness of assets.

The Energy Authority created by Jacksonville, MEAG and South Carolina Public Service as a public power ISO is an example. Some major public power firms have taken this further and have entered the power marketing field. This has been more feasible for those public utilities and coops which have voluntarily undertaken the type of functional restructuring which IOUs have undertaken more extensively. Oglethorpe's arrangements which enabled it to collaborate with power marketers are an example.

Nevertheless, it does not seem prudent, as a general matter, for municipals to assume that they can fight their way out of their potential problems simply by combining the utilization of aggregation techniques with a better service package, unless that package is able to be price competitive. It also remains a problematic issue as well whether bundling of electric services with consumer services such as home security, telecommunications, HVAC and energy services, will—in what is already a privately driven service aggregating marketplace—produce the desired results.

Consequently, it is appropriate for municipal power to be exploring how, through a variety of private sector strategic alliances, it can relate its obvious potential central role as aggregator, to market position strengthening elements which it can gain from the private sector.

These public-private alliances can either be focused on finances, operation (including outsourcing) or diversification. The possibility of reworking the capital structure of municipal power through IOU contract buy down (in effect, the reverse of IPP stranded cost buy down by IOUs); through use of power marketing; and through long term purchases of future capacity delivery, have only begun to be explored.

While many munis are still thinking they can prepay their existing contracts and hence their way out of their problems by raising rates, this could prove to be a politically unwise strategy. There is

room, in short, for public/private strategic alliances related to finance, without reference to power sales contract restructuring and risk management.

The extent of muni financial flexibility may be further enhanced through strategic alliances with the energy marketing firms that complement the munis' core strengths (e.g., customer presence and relationships; distribution/maintenance services) with their own in areas such as the development of innovative customized products and services; multi-commodity and risk management skills, wholesale trading capabilities, and financial flexibility in structuring asset outsourcing. The essential point for munis is that existing assets may have to be used in new ways in the lower cost, more competitive deregulated market. Introduction of skilled private parties not only may provide new ideas in this regard, but new mechanisms to effect restructuring consistent with the special legal requirements governing public power financing, using, for example, derivatives.

Diversification into other services (or exploitation of the franchise available extending even to telecom uses of rights-of-way to provide such services) very likely also can be effected better with a private partner.

Not-for-Profits

The logic impelling government to acquire the benefits of aggregation in order to continue to serve their constituencies, applies as well to non-profits in fields such as health and education. Privatization impinges on them and their service institutions in different ways.

As social services are deregulated, these non-profits stand to be driven from the marketplaces they serve by for-profit entities. Health care, training and welfare/social service administration are concrete examples. The pressure of privatization moves them in the same way the pressure of competition moves private firms to control energy costs. In turn, that pressure moves the institutions which serve the non-public sector.

Institutions servicing the large market which non-profits represent sometimes are in a more flexible position than governments to extract special benefits from private providers of aggregation and other energy services. A good example of the exercise of this potential is the Massachusetts Health and Education Financing Administra-

tion (“HEFA”), which branched into aggregation, and sought a panopoly of useful services for its members—thus enhancing the value of its aggregation package. These included:

- (1) Supply Service—firm, with delivery assured to one or more points of service location; on two and five year contract bases (including time of use, fixed price and indexed offer);
- (2) Green portfolio supply option, with commitments to expand the source;
- (3) Special tailored enhancements to meet the requirement of individual participants; and
- (4) Program for employees as well as for institutions.

The HEFA procurement package provides, in effect, for institutional consumer protection assurance. HEFA’s goals include expansion into prepurchase of electricity and expansion into natural gas, heating oil, propane and perhaps even telecommunications.

Non-profits are not generally captive to long term energy purchase use arrangements designed to facilitate financing, like municipals; dependent on the operation of public laws governing procurement and partnering, like municipalizers; or committed to the use of taxable finance, like private aggregators or outsources.

They are well situated to link aggregation to consumer social preferences (e.g. “green” power) or special economic needs (e.g. dispersed energy for high tech applications.)

Overall, then, they possess strategic advantages which make them natural aggregators and partners for private firms.

Conclusions

In sum, motivated by needs to survive the twin thrusts of deregulation and privatization, the “non-private” sector is beginning to take the initiative in the energy aggregation field. Success in establishing public-private partnerships with it requires appreciation of the legal and also the institutional survival issues with which they are dealing. The results can be creative uses of municipal franchises, a renaissance of non profit power firms, and the continuing financial

vitality of the seriously threatened and socially valuable not-for-profit public sector.

From the perspective of private firms, aggregation by non-private firms can be a portal to response to the electric power deregulation revolution.

ABOUT THE AUTHOR

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