

# Electric industry deregulation

On the Mainland, states are debating the deregulation of the electric utility business. Lower costs for customers is the overall goal behind deregulation. But low supply and/or high demand can also cause costs to escalate. For example, customers in parts of California, one of the first states to deregulate, have been hit with power shortages and skyrocketing prices in the wake of deregulation.

After these experiences and the lessons from deregulation of the airlines and telecommunications industries, it's clear that restructuring a highly regulated industry is a complex undertaking that requires careful planning. In Hawaii, the Public Utilities Commission (PUC) is taking just such a thorough approach, with a docket to consider what makes sense for our island state.

Some of the key issues for Hawaii include:

## No interconnections

On the Mainland, a vast network of transmission lines across the continent makes it possible to send electricity from one state to another. Hawaii's island utility systems are not connected to each other, and we're not connected to any other state.

## Reliability standards

Because Hawaii can't get back-up power from neighboring utilities, it's much more critical that our electric service is reliable. There must be clear responsibility and accountability for daily operation of the electric system and long-term planning to ensure facilities are available to meet future demand.

## Small markets

Hawaii does not have as many large commercial and industrial power users compared to the Mainland. In a small market, if a large user of electricity leaves the utility grid, remaining customers will have to carry more of the electric system's operating costs. Breaking up the utility system could result in a loss of economies of scale and scope and higher costs to customers.

## No low-cost alternative fuels

Many Mainland suppliers are able to offer customers lower electricity costs because they can use lower-cost natural gas instead of other fossil fuels. There is no source for natural gas in Hawaii and it is not feasible to transport it to the islands.

## Customers can benefit without full-scale deregulation

Hawaiian Electric Company and its subsidiaries, Hawaii Electric Light Company and Maui Electric Company, are proposing changes to the PUC that can provide many of the benefits of competition without exposing customers to the risks and high costs.

## Performance-based ratemaking

Performance-based ratemaking provides incentives to continue to improve efficiency. When the utility does well financially, it shares some of that benefit with its customers. That means if it earns over a certain rate of return, it **shares those earnings** with customers in the form of a rate decrease. If its return drops below a certain threshold, there's an option to increase rates. There would also be a middle range where no sharing is triggered.

**Performance incentives** help ensure reliability and customer service remain top priority. If customer satisfaction or reliability target goals are achieved, the company gets a "bonus" from customers. If it doesn't meet these goals, it pays a "penalty."

## Price caps

Price caps help limit the amount rates can go up. The cap would be indexed for inflation and other factors.

## Innovative pricing

To provide more flexible pricing for customers in different situations, HECO, HELCO and MECO are also proposing to expand the menu of rate options.

Some examples:

- **Time-of-use rates** for residential and small business customers, which reward off-peak energy use with a lower rate. Right now, this alternative is available only to big customers.
- **Two-part rates** that encourage economic development for businesses. Any additional load as the business expands would be charged a lower rate.
- **Exit fees** to make sure the "little guys," primarily residential and small business customers, don't get stuck holding the bag if large customers leave the system by producing their power on site. Large customers would also pay "stand by" charges if they leave the system but want to use it for back-up insurance.

The risks of full competition for an island utility system like Hawaii's are high. Rather than leaping to adopt costly Mainland solutions, let's make changes that are right—for Hawaii.

