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Retail Choice Will Not Bring Down Puerto Rico's High Electricity Rates

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Summary

In the wake of the devastation Hurricane Maria caused Puerto Rico's electrical system, a plethora of policy and regulatory changes have been proposed to rebuild and provide resiliency for the electrical grid. Among the more recent proposals is the suggestion that Puerto Rico move to a model of "retail choice," where individual electricity customers select their providers. Puerto Ricans currently get their electricity from a monopoly utility, the Puerto Rico Electric Power Authority (PREPA).

The impetus for this proposal seems to be that it would reduce the high price of electricity in Puerto Rico, where residential customers paid an average of 20.2 cents per kilowatt hour in 2017, well above the average price for the United States of 12.90 cents per kilowatt hour.[1, 2]

José Ortiz, the new executive director of PREPA, is a proponent of retail choice. In an August 20 interview with *El Nuevo Dia*,[3] he referred to it as a "second step" in plans to transform the electricity system where "retailers would come on the scene to negotiate kilowatt sales packages" which customers would purchase.

About one-third of U.S. states have adopted some version of retail choice over the past two decades, and their experience indicates how retail choice would affect electricity rates in Puerto Rico. Rather than proving to be a boon for customers, retail choice has instead cost residential customers billions in excess charges in several states, and some providers have harmed customers by using predatory and deceptive sales practices.

With the turmoil in Puerto Rico's physical electrical system as well as the many regulatory, ownership, and policy changes coming or likely to be coming, we are highly skeptical that Puerto Rico can avoid the missteps that have befallen other states that implemented retail choice. Indeed, we think it is highly unlikely that retail choice, even if implemented perfectly, would do much to address high residential rates.

What is Retail Choice?

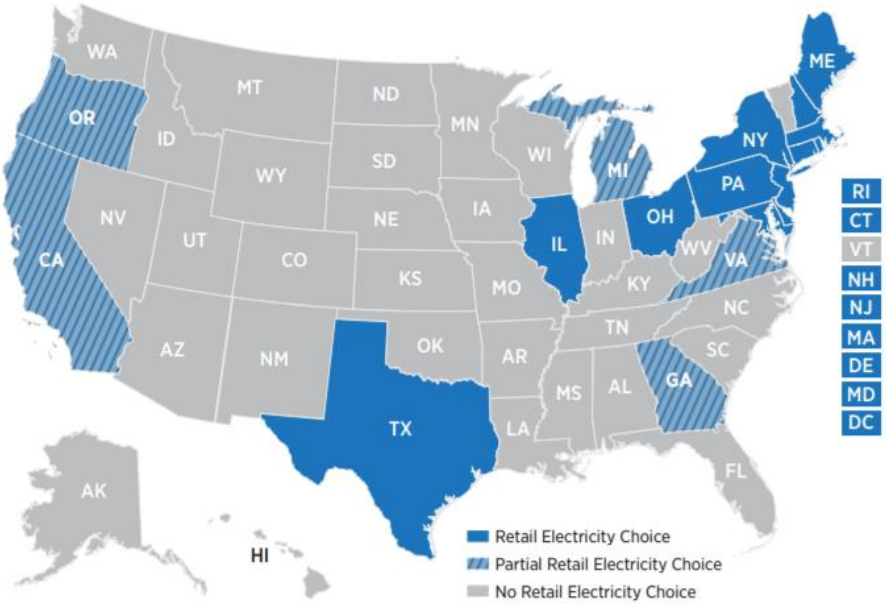
In the 1990s, a number of states adopted an alternative to the traditional electricity utility model, in which one utility owns and operates all aspects of the system from the power plants that generate electricity to the wires and poles that make up the transmission and distribution system used to deliver electricity to consumers and thus has a monopoly on the provision of electric service to customers in its service territory. The alternative to this model, known as "restructuring," mandates that these "vertically integrated" utilities sell off their generation assets, so that generation and distribution assets were held by different companies (though, in practice, many were simply spun off to affiliates of the same holding company.) Generation

[1] June 2017 Puerto Rico Electric Power Authority Operations Report. August 18, 2017. See fiscal year 2017 rate, p. 8.
[2] U.S. Energy Information Administration (EIA). EIA electricity sales data for Puerto Rico show rate of recovery since hurricanes. August 6, 2018.
[3] *El Nuevo Dia*. Los clientes de la AEE no podrán escoger el proveedor de servicio eléctrico. August 20, 2018.

owners would then sell electricity into a wholesale market facilitated by the introduction of regional transmission organizations (RTOs) and independent system operators (ISOs).

This opened the door for the introducing retail choice for customers in the states that decided to pursue restructuring. Retail choice allows customers to decide if they want to purchase electricity from the electricity utility that had previously provided service in their area (also known as the default service provider), or from a different retail supplier. Figure 1 shows which states have chosen to implement retail electric choice.[4]

Figure 1: States with Retail Electricity Choice



Source: State public utility commissions (2017).

The retail choice itself refers in most cases to the source of generation. Customers who choose to purchase from a competitive supplier pay whatever that supplier's rate for electricity might be. The remainder of the bill, typically known as the distribution charge, is not subject to retail choice and remains the same for all residential customers. All customers, regardless of whether they purchase electricity from the utility or an alternative supplier, will still be charged a cost for using the distribution system to deliver electricity to their household. Typically, in states with retail electricity choice, ownership of the distribution system has remained with the legacy electric utility.

Proponents of retail choice have argued that it would achieve the following goals: lowering electricity prices through access to competitive wholesale markets where competition is based on price and performance; improving service and options for customers; creating innovative product and service offerings for customers (such as green power products)[5] and making environmental improvements through the displacement of power plants that generate more pollution.[6]

Despite these goals, residential customers in a number of the states that have chosen to adopt retail choice have not seen lower electricity prices.[7] and thousands of customers have been victims of abusive

[4] Taken from Zhou, S. (2017). *An Introduction to Retail Electricity Choice in the United States* (No. NREL/BR-6A50-68993). National Renewable Energy Lab.(NREL), Golden, CO (United States). Retrieved here.
[5] Green power products offer a bundling of renewable electricity and renewable electricity credits (RECs).
[6] Federal Energy Regulatory Commission. (2006). Report to Congress on competition in the wholesale and retail markets for electric energy. *The Electric Energy Market Competition Task Force. Washington, DC*.
[7] NCSL Energy Policy Forum. Electricity Market Restructuring: Where Are We Now? Presentation by Johannes Pfeifenberger. December 6, 2016.

and predatory marketing practices.

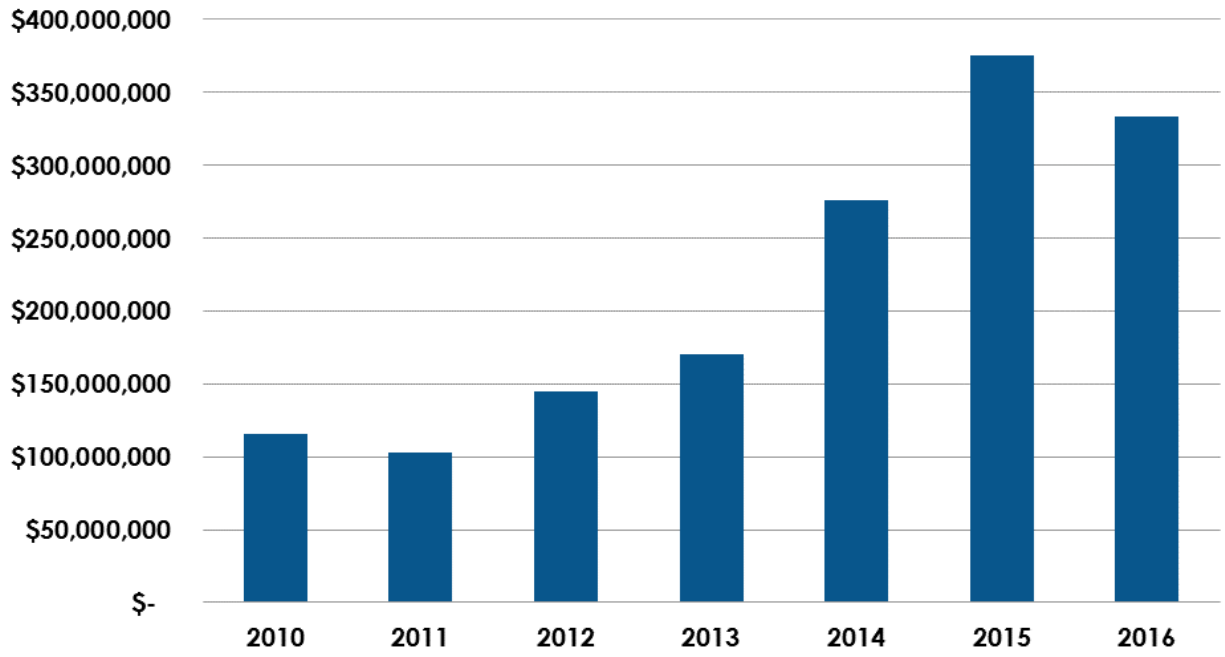
Retail Choice in New York State Has Cost Customers Over $1 Billion

Implementation of retail choice in New York State has harmed rather than helped consumers and has sparked thousands of complaints to the state's Public Service Commission.

An audit into charges by energy service companies, known in New York as ESCOs, found that low-income residents in New York paid $96 million more to these companies in just the thirty months ending June 30, 2016 than they would have paid to a utility for electricity and gas charges.[8] In July 2016, New York Governor Andrew Cuomo announced a moratorium on ESCOs selling electricity and natural gas to low-income customers, in part because some ESCOS confirmed "they were not likely to provide a guaranteed savings to low-income customers."[9]

More recently, the Public Utility Law Project of New York (PULP) analyzed Energy Information Administration (EIA) data[10] from 2000 to 2016 to determine how much more customers of ESCO service providers paid versus those served by the default provider. PULP found that between 2000 and 2016 ESCO overcharged residential ratepayers $1.8 billion, with $1.5 billion of these overcharges occurring between 2010 and 2016. Figure 2 shows the annual excess charges to residential customers served by ESCOs between 2010 and 2016.[11]

Figure 2: ESCO Electricity Extra Cost to Residential Customers in New York

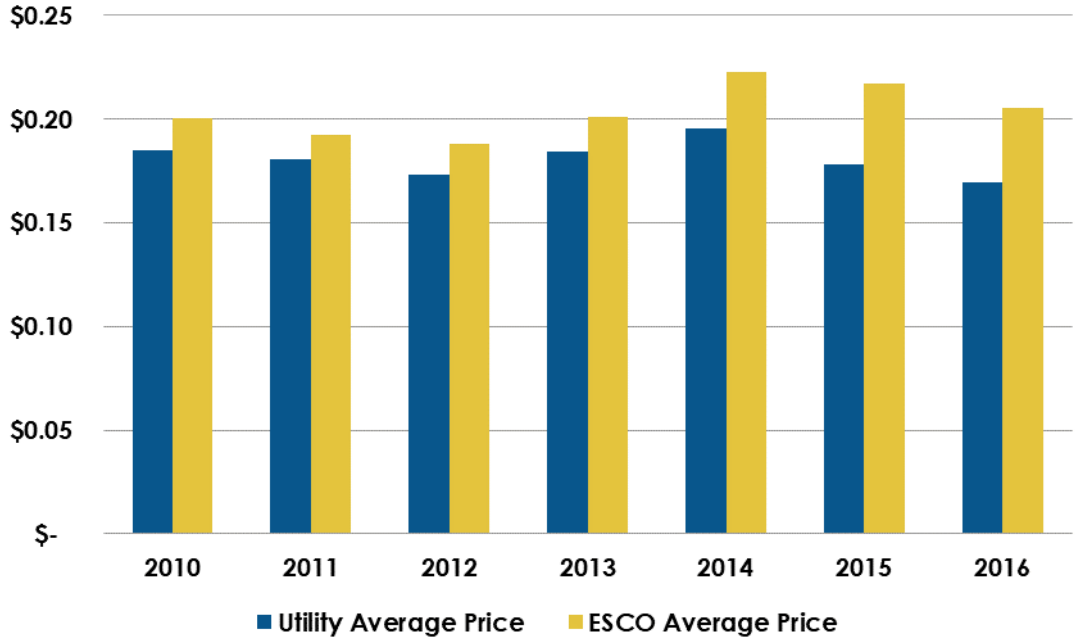


Source: U.S. Energy Information Administration (EIA).

[8] New York Public Service Commission Press Release. ESCOs Banned From Selling to Low-Income Customers in New York, December 15, 2016.
[9] New York State Office of the Governor Press Release. Governor Cuomo Announces Moratorium on Competitive Energy Service Company Sales to Low-Income Customers. July 15, 2016.
[10] U.S. Energy Information Administration (EIA). Average price of residential electricity supplied by ESCOs versus incumbent utilities for 2000 to 2016 derived from EIA dataset Average Price (Cents/kilowatt hour) by State by Provider. Extra cost (overcharges) to New York State residential electric customers supplied by ESCOS versus what they would have been charged if they received their electric supply from their utility from EIA-861 Sales to Ultimate Customers (MWh).
[11] Testimony of William Yates in New York Public Service Commission Case No. 15-M-0127, filed October 13, 2017, with 2016 data added on.

Figure 3 shows the difference between the average prices charged to residential customers by electric utilities and those charged by ESCOs. Every year, ESCOs had a higher average price than the default provider.

Figure 3: Average Price[12] of Electricity for Utility vs. ESCOs in New York



Source: U.S. Energy Information Administration (EIA).

Retail Choice Led to Higher Rates and Deceptive Marketing Practices in Several Other States

In addition to the well-documented problems in New York, investigations in several other states show that customers have been harmed by the practices of companies in retail choice markets. These include:

Customers Paid Well Over Market Price for Electricity in Massachusetts, Connecticut, and Illinois

Following an influx of complaints received about energy supply companies, the Massachusetts Attorney General's Office commissioned a report to investigate whether residential customers benefit from purchasing their electricity from an energy supply company versus the default electric service provider. Susan Baldwin, the report's author, found that between July 2015 and June 2017, customers participating in the competitive supply market paid $176.8 million more[13] than they would have paid if they had purchased from their default provider. Additionally, Baldwin found that low-income households in Massachusetts participated in the competitive supply market at twice the rate as non-low-income households, amounting to an average annual loss of $252 for low-income households.

Data analyzed by the Office of Consumer Counsel in Connecticut found that for June 2016 through May 2017, residential customers in Connecticut who purchased electricity from competitive energy suppliers paid $66,736,598 more than they would have paid if they purchased from their default service provider.[14]

[12] The average price for the utility is derived by taking the total of the full service, which includes delivery and the supply price of electricity for the utility. The ESCO average price represents the total of the utility delivery price and the ESCO supply price of electricity.

[13] Baldwin, S. Are Consumers Benefiting from Competition? An Analysis of the Individual Residential Electric Supply Market in Massachusetts. March 2018.

[14] Bosco, J. Competing to Overcharge Consumers: The Competitive Electric Supplier Market in Massachusetts. National Consumer Law Center. April 2018.

The Illinois Commerce Commission found similar results— residential customers purchasing from competitive energy suppliers spent $115,204,320 more from June 2014 to May 2015; $73,439,971 more between June 2015 and May 2016; and $152,108,081 from June 2016 to May 2017.[15]

Deceptive Marketing Practices Have Harmed Customers

Enforcement agencies in New Jersey, Pennsylvania, Illinois, and Massachusetts have levied fines against retail choice service providers for deceptive and misleading behavior.[16, 17, 18, 19]

These states found that some energy service companies used deceptive door-to-door and telemarking strategies to persuade customers to switch to their service, including misleading customers about contract terms, (offering a low introductory price that quickly spikes with a high variable rate) and trapping customers in contracts through high cancellation fees. Consumers also complained about energy service companies engaging in an illegal practice known as "slamming," whereby they switch customers to the energy service company without their knowledge. Many of these malicious practices employed by energy service companies have targeted low-income households, minorities and those who do not speak English. In Massachusetts, complaints against energy service companies included members of a sales team misrepresenting themselves as National Grid employees in order to access a locked apartment building and then convincing a customer to switch to their gas service, while also switching her electrical service without her knowledge.[20]

Retail Choice is the Wrong Model for Puerto Rico

Based on these experiences, there is significant reason to believe that retail choice will harm rather than help residential electricity customers in Puerto Rico. Low-income residents on the island, where the poverty rate is 43.5%,[21] may be particularly vulnerable to the misleading and predatory tactics some energy service companies have used elsewhere.

The introduction of retail choice would further burden a weakened electric regulator and allow predatory suppliers to take advantage of Puerto Ricans seeking relief from high electric prices.

Puerto Rico recently enacted a new law consolidating the Puerto Rico Energy Commission under the umbrella of the Public Service Regulation Board, while cutting the commission's budget. In addition, Puerto Rico appears to be[22] moving toward a sale of all, or many, of PREPA's assets to third parties, a system that could cause further chaos.

Retail choice does nothing to address the fundamental challenges that have caused Puerto Rico's electricity prices to rise to unsustainable levels, including: PREPA's high level of debt; disinvestment in transmission, generation and distribution infrastructure; and extreme reliance on oil-fired generation. These problems have only been exacerbated by the utility's high level of unpaid customer bills, management corruption, and need to rebuild its system following Hurricane Maria. Retail choice would offer no escape from these realities: indeed, it would likely raise the very high rates that already burden PREPA's residential customers.

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[15] *Ibid*.
[16] *Ibid*. Just Energy entered into an Assurance of Discontinuance and restitution for consumers in the amount of $3.8 million for misleading marketing practices and customer overcharges.
[17] Retail Energy Providers in New Jersey settled for $2.1 million for malicious marketing.
[18] Respond Power settled a case in Pennsylvania where they paid $5.2 million for deceptive marketing.
[19] A case against Major Energy was filed in Illinois for their deceptive sales pitches.
[20] *Ibid*.
[21] United States Census Bureau. Population Estimates, July 1, 2017, Puerto Rico.
[22] *Associated Press*. Puerto Rico gov. signs bill to privatize PREPA utility assets. June 21, 2018.

About IEEFA

The Institute for Energy Economics and Financial Analysis (IEEFA) conducts research and analyses on financial and economic issues related to energy and the environment. IEEFA's mission is to accelerate the transition to a diverse, sustainable and profitable energy economy. www.ieefa.org

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