

Department of Legislative Services
Maryland General Assembly
2006 Session

FISCAL AND POLICY NOTE

Senate Bill 1099

(Senator Pipkin)

Finance

Economic Matters

**Constellation Energy Group, Inc., and Baltimore Gas and Electric Company -
Return of Transition Costs**

This bill requires that until Constellation Energy Group, Inc. returns to Baltimore Gas & Electric Company (BGE) \$528 million in transition costs recovered during electricity deregulation, that a merger between FPL Group, Inc. and Constellation Group may not occur and BGE may not increase electricity rates for residential customers in its service area.

BGE must use the return of the transition costs to reduce any increase in electricity rates for residential customers that may occur after the electricity rate caps expire. If Constellation Group does not return the transition costs, it must reimburse BGE for any losses incurred by BGE directly attributable to the rate increase prohibition.

The bill takes effect June 1, 2006.

Fiscal Summary

State Effect: None. The bill pertains exclusively to private sector activities.

Local Effect: None.

Small Business Effect: None.

Analysis

Current Law: As of July 1, 2000, all customers of electric companies have the opportunity for choice of electric suppliers. However, a customer has the option to remain with the supplier of the electric utility under standard offer service (SOS). Any obligation of the electric company to continue to offer SOS expired on July 1, 2003 unless the Public Service Commission (PSC) found that the market was not competitive. Then PSC could extend the requirement to provide SOS to residential and small commercial customers at a market price that permits recovery of the verifiable, prudently incurred costs to procure or produce the electricity plus a reasonable return. PSC is to reexamine whether the market is competitive annually. An electric company may procure the electricity needed to meet its SOS from any electricity supplier, including an affiliate of the electric company.

In settlement agreements with each of the State's investor-owned utilities, PSC has extended the obligation to provide SOS. The Electric Customer Choice and Competition Act of 1999 required price caps with statewide rate reductions for four years which could be extended by a settlement agreement. Under the final settlement agreements, the price caps required under the Electric Utility Restructuring Act of 1999 expired in the PEPCO and Delmarva service territories on July 1, 2004, and are scheduled to expire in the BGE service territory on July 1, 2006, and in the Allegheny service territory on January 1, 2009. Because there continues to be little competition in residential electric service in the State, PSC has extended the obligation to provide SOS in the PEPCO, Delmarva, and BGE service territories by four years after the expiration of the price caps.

Background:

Transition Cost Recovery

One of the more complex issues in enacting electric utility industry restructuring was the treatment of transition costs or benefits, the difference between the book value and market value of an electric company's generation assets, subject to adjustments for reasons of public policy. Deregulation allowed an electric company to recover certain prudently incurred transition costs but those costs had to be under a PSC-approved transition plan, developed in accordance with fact-finding and evidentiary proceedings, and subject to full mitigation. An electric company with verified recoverable transition costs could institute a competitive transition charge that applied generally to customers located in the electric company's service territory. An electric company was able to transfer its generation facilities or generation assets to an affiliate, but the transfer could not affect or restrict the PSC's determination of the value of a generation asset for purposes of transition costs or benefits.

As part of the transition cost determination, PSC was required to consider, the following factors in determining transition cost relating to investment in a generation asset: (1) the prudence and verifiability of the investment; (2) whether the investment is used and useful; (3) whether the loss is one of which investors can be said to have reasonably borne the risk; and (4) whether investors have already been compensated for the risk.

The settlement agreement with PSC provided BGE with after-tax transition costs to be recovered from customers of \$528 million. The cost recovery began (per kilowatt charge) July 1, 2000 and ends June 30, 2006.

It is anticipated that energy costs are going to increase substantially this summer, the same time that the BGE rate freeze is set to expire on July 1, 2006. Based on the recent bidding process for the market priced SOS, BGE residential rates will increase by an average of 72% beginning in July 2006. The average bill will increase by 39% for PEPCO residential customers and by 35% for Delmarva Power and Light residential customers. As a proactive measure, on January 10, 2006, PSC initiated a proceeding to investigate and take actions it may find appropriate to deal with the anticipated price increases. PSC staff developed a mitigation plan for BGE's generation price increase which was adopted on March 6, 2006. The mitigation plan contains the following features:

- BGE Rate Stabilization Plan (the plan) begins in July 2006 and ends May 2008 for most residential customers. This two-year rate mitigation plan allows customers the option of more gradually adjusting to market rates over an extended period of time.
- Low-income customers participating in the Electric Universal Service Program will receive an option of a three-year rate mitigation plan.
- As part of the plan the initial increases will be limited to 21% and customers will receive credits to the distribution portion of their bill from July 2006 to February 2007. For the remaining period of the plan customers will receive a charge to the distribution portion of their bill to recover the credited amount. At the conclusion of the program, a final true-up will occur for program participants.
- The plan will serve as the default option for residential customers. Customers who wish to pay the full price of electricity beginning July 1, 2006 will have that opportunity.
- BGE will pay the full market price of the electric generation even though customers will only be paying the mitigated amount. PSC has determined that the appropriate interest rate for recovering this short-term deferred balance is 5.0%.

BGE is required to work with PSC and other interested parties to develop a consumer education plan and enrollment details which must be submitted to PSC by March 31, 2006.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Public Service Commission, Office of People's Counsel,
Department of Legislative Services

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ncs/jr

Analysis by: Karen S. Benton

Direct Inquiries to:
(410) 946-5510
(301) 970-5510