FINANCIAL RISKS FOR OWNERS AND RATEPAYERS OF REGULATED UTILITIES:

A PRACTITIONER'S VIEW

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WHAT DO REGULATED UTILITIES* WANT?

“Constructive regulatory environment,” *i.e.,* compliant PUC

“Regulatory certainty”

Opportunities for large capital investments

Assurance of cost recovery

Timely cost recovery

***caveat: observations from experience with vertically integrated utilities in fully regulated jurisdictions with no RTO/ISO**

WHAT DO REGULATED UTILITIES FEAR?

Delayed (or worse, denied) recovery of costs

Angry customers

Aggressive regulators (PUCs, environmental agencies, FERC)

Bad publicity (disasters, scandals, rate hikes, outages)

Disruptive technologies & declines in load growth

Competition! (Deregulation; RTOs/ISOs; FERC jurisdiction; third-party electricity sales)

CATEGORIES OF RISK

Environmental risk

Risk of regulatory disallowance

Fuel price risk (usually a pass-though to customers, but statutory obligation to minimize costs)

Risk to credit rating

Cost overruns at large capital projects

RISKS TO SHAREHOLDERS

Inability to recover costs—especially for huge capital investments

Commission-approved rate of return lower than target

Revenue erosion—from efficiency, distributed generation, weather

Downgrade of credit rating and inability to attract financing on favorable terms

Criminal penalties (*e.g.*, Duke Energy coal ash)

RISKS TO RATEPAYERS

Capital cost overruns

Construction work in progress

Cost recovery for abandoned plants (*e.g.*, Crystal River)

Fuel costs—volatility, price spikes

Risks incurred at other subsidiaries of parent company

Unknowns (both known and unknown)

ALLOCATION OF RISK

Imbalance in allocation of risk—risks to shareholders will often affect ratepayers, but the converse often not true

Risk-shifting justified by utilities, regulators, even consumer advocates as a cost savings for customers (*e.g.*, cost recovery for CWIP—before plant is used and useful)

OPPORTUNITIES TO RAISE THE ISSUE OF RISK

Mergers

New plant certifications (but is RE a new profit center?)

Rate cases

Avoided cost rate dockets

Fuel cost recovery riders

Integrated resource plans

Briefings

CHALLENGES

Law in regulated jurisdiction is probably utility-friendly

"We know best" attitude: utilities understand their business and the financial risks, and you don't

"Regulatory capture"?

Consumer advocate agencies may be focused on details and not on the big picture

Environmental/clean energy advocates may not be a credible voice for consumer protection

COMMUNICATING RISK TO COMMISSIONS AND THE PUBLIC

Is the utility telling Wall Street a different story from the story it is telling the PUC?

Example:

“[I]t would have been *imprudent* to include large capital costs for compliance” in their IRPs. **(Duke Energy Response to Comments by SACE, CCL and Upstate Forever on 2013 Integrated Resource Plan, SC PSC Docket No. 2013-8-E and 2013-10-E (March 12, 2014) (“SC Response to Comments”) p. 2. (emphasis added).**

Duke Energy CEO Lynn Good: the company estimated $3 billion in environmental compliance expenditures (or “investments”) in the Carolinas; touted the “good history of environmental recovery” in the Carolinas. **(Transcript of Q4 2013 Duke Energy Corporation Earnings Conference call (February 18, 2014), pp. 18-19.)**

LESSONS LEARNED

Utilities will go to great lengths to remove "stakeholder" opposition to getting what they want from regulators

Commissioners and consumer advocate agencies care about financial stability of utility–often because law requires it

Victories are seldom, hard-won and usually incremental—with rare exceptions

Scandals/disasters may create opportunities for change

Protecting shareholder earnings is utilities' paramount concern

QUESTIONS? FEEL FREE TO CONTACT ME:

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