Consumers Energy
Testimony by David G. Mengebier
Michigan House Energy and Technology Committee
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Good morning Chairman Nesbitt, Vice Chairman Glenn, Vice Chairman LaVoy, and members of the committee.

My name is David Mengebier. I'm the Senior Vice President of Governmental and Public Affairs for Consumers Energy and its Chief Compliance Officer. With me this morning is Tim Sparks, our Vice President of Energy Supply who testified before this committee on February 25 regarding expected energy supply shortfall and Consumers Energy's plans to meet future energy needs of our customers.

Thank you for this opportunity to testify in support of House Bill 4298.

At Consumers Energy, we recognize that the whole issue of Michigan's electric market design, whether it's a regulated, deregulated or hybrid model, is complex and in some quarters politically charged. If I could put myself in the shoes of our retail open access customers, I'd understand why they do not want Michigan to return to a fully regulated market. They have obligations to their owners, customers and employees. Many are multinational companies and sophisticated energy buyers that compete on the global stage. Not surprisingly, they want unfettered access to the cheapest power available, whether it's by buying it through an out-of-state energy marketer when market prices are low or returning to their Michigan utility when market prices rise. If I were in their shoes, I'd want to preserve the ability they have today in Michigan to jump back and forth depending on whose prices are lower.

But I would submit to you that when it comes to energy policy for the state of Michigan, the utilities, by virtue of our statutory obligation to serve as the provider of last resort, and you as law makers, have a broader responsibility. It extends not just to a single company or a select group of customers, nor is it limited to a particular geographic region.

Our collective responsibility extends to all parts of Michigan, all communities and all types of customers, whether they are large, multi-national corporations, medium or small size businesses, or homeowners. This is appropriate, not only because of our shared responsibility to ensure the safe delivery of affordable and reliable power to ALL of the people of Michigan, but because of the interconnected and integrated nature of our electric grid. Because Michigan's grid is a system that all customers rely on, we believe the energy policy choices you make as lawmakers must take into account the interests of all customers.

While there are some interests and some policymakers who would prefer that Michigan completely deregulate its electric market, this is a model, when subject to scrutiny, that is seriously flawed, and often driven more by ideology and in some cases, short-term profit-making, than it is by economic fundamentals and the physical characteristics of electricity.

The unique characteristics of electricity make it a commodity that is entirely unsuited to a deregulated market. Electricity can't be stored, it travels at the speed of light and it must be consumed instantaneously. As a result, electricity is the most volatile commodity in the world - 300 times more volatile than commodities such as oil, corn or wheat or natural gas.

In order to minimize price volatility in electricity markets, energy providers make long-term investments in power plants sufficient to meet demand, plus provide a reserve margin to cover periods when demand for electricity spikes. The utility industry is the most capital intensive in the world - power plant investments range from tens of millions, into the billions of dollars. In order to make these investments affordable for customers, the costs of these plants are recovered over 30 or 40 years or more.

In fact, the primary driver for the regulated model used by 36 states today is that it provides the certainty of cost recovery energy providers need to finance and construct new generating plants. The regulated system may not always lead to the lowest prices, but it keeps prices stable and predictable. Based on our daily interactions with customers, as well as extensive customer satisfaction research, this is what the vast majority of our customers are looking for. No state has passed deregulation legislation in the past 15 years. Instead, states are taking actions to move back toward a fully regulated model.

For certain customers that use a lot of power, the cost of electricity can be a major driver for their competitiveness. Consumers Energy is taking steps to make our rates more competitive for business customers while continuing to keep residential bills below the national average. We have in effect frozen base rates for all customers for the last two years. In addition, our PA 169 case pending before the MPSC would result in business customer rates that are 5-15% lower, depending on their energy usage. Enactment of House Bill 4298 would lead to rates that are even lower - on average 3 to 4% lower for existing utility customers across the board.

In sharp contrast, deregulated markets provide strong disincentives for long term investments in power plants necessary to ensure sufficient supplies to cover the wide swings in electricity demand. States that have deregulated their markets continue to experience great difficulties attracting new generation investment because of the uncertainty their energy providers face in recovering their investments as customers come and go. Not only is this presenting major reliability challenges for these states, it is contributing to very high electricity prices - on average 25% higher than in regulated states.

During periods when there is a surplus of generating capacity in the market, there is no need for the type of certainty I'm talking about and the price volatility problems found in deregulated markets are muffled. This has been true in the Midwest where low natural gas prices and excess capacity have depressed market prices for electricity.

But as Bob Dylan would say, "times are a-changin'." This committee already has heard extensive testimony on the power shortages the Lower Peninsula could be facing as early as next year so I won't belabor the point other than to say this is an urgent and serious challenge for our state, and one that is exacerbated by Michigan's one-of-a-kind hybrid market.

Consumers and DTE have both made filings with the MPSC indicating that we have sufficient supply and demand response programs in place to meet our bundled utility customers' needs for the next five years.

What we are concerned about is the prospect of 2,000 MW of ROA load returning to the utilities with as little as two months' notice if their alternative energy marketers cannot perform. This circumstance could occur if the marketer cannot secure firm, physical capacity or if they decline to meet their contractual obligations because the cost to the marketer to acquire the power becomes too high.

This is not theoretical speculation on our part nor is it a short-term problem. With the closure of more than 60 plants in MISO, the market will move quickly from a surplus to a shortage of capacity which we expect will drive up market prices for power. In states that have deregulated, we've seen instances where alternative suppliers were abruptly forced to stop providing service when prices get too high and customers are "turned over" to their incumbent utilities on short notice. The capacity shortfall is not going away. According to a statement made just last week by the president of the North American Electric Reliability Council, proposed EPA rules governing carbon emissions from power plants will lead to even more coal plant retirements, creating additional generation shortages in the Midwest and other regions of the country.

To put the prospect of the return of the 800MW of ROA load on our system in perspective, this would represent 10 years of growth in demand in less than one year. This would present both significant reliability and price problems for our customers. If Consumers Energy were required to make short-term purchases from the market to serve returning ROA customers, under MISO's rules, we would pay premium "Cost of New Entry" pricing which is about 15 times higher than today's market prices. The very short notice provisions for ROA customers to return to bundled service also pose reliability challenges. 800MW of load is equivalent to one large, combined cycle natural gas plant. The time it takes to site, permit and construct a plant of this size, even on an accelerated basis, is 3-5 years. The pressure the returning ROA load would put on our reserve margin raises reliability challenges, not just for these ROA customers, but for all customers.

Someone might ask, "Why don't we begin building new power plants today to make up for the capacity shortfall MISO is projecting?" This would make sense in a fully regulated market where the customer base and supply and demand projections are much more predictable. But under Michigan's hybrid market, where 99% of our customers already subsidize - to the tune of $150 million annually - the power supply costs of the 1% that are on ROA, it doesn't make economic sense for our supply customers to invest hundreds of millions in a new power plant with the uncertain prospect the ROA customers will return.

Someone might ask, "Why can't we just import electricity from other states?" There are physical limitations as to how much capacity can be imported into Michigan. Several of those limitations don't even reside in the MISO transmission system. Siting and building appreciable new transmission can take several years - approaching 10 or more years is not out of the question, which is more than twice as long as building a new gas fueled power plant. Therefore, transmission is not a viable answer for the foreseeable future to fix this quickly approaching need.

The chairman's legislation to re-regulate Michigan's energy market is, in our view, the best policy choice for our state and for our customers. It restores fairness, eliminating the subsidy 99% of utility customers provide to the less than 1% on ROA. It ensures Michigan has a regulatory framework that will stimulate new generation investment, assuring reliability of supply and creating Michigan jobs at a time when power plants are being retired at a rapid rate. And it ensures Michigan, not Washington DC is in control of our state's energy future, today and well into the future. One only need look to the Upper Peninsula's ongoing energy crisis to appreciate why we don't want the feds in charge of Michigan's energy future.