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NEWSLETTER

Fall 1998, Issue 14

In This Issue

- Update on the Centres
- Peter Nicholson Luncheon
November 5, 1998
- Electricity Deregulation Forum
October 6, 1998
- New Corporate Members
- New Board Members
- Speech Available

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CENTRE FOR REGULATORY AFFAIRS AND CENTRE FOR TRANSPORTATION

ALEXANDER BLACK, *Executive Director*

The Van Horne Institute has been established to address important **transportation** and related **regulatory** issues confronting industry and government, in North America and internationally, through research and education.

The Institute was incorporated federally in 1991 as a not-for-profit organization,

UPDATE ON THE CENTRES

The Van Horne Institute is pleased to announce the appointment of **Alexander Black** as Executive Director of both the Centre for Transportation and the Centre for Regulatory Affairs. Prior to his appointment in August, Mr. Black was Legal Counsel for TransCanada PipeLines Limited in the Litigation and Regulatory Department. From 1988 to 1996, he was a Lecturer-in-Commercial Law for the School of Law, at the University of Glasgow, Scotland. His education includes: Master of Laws, University of British Columbia (1988); Diploma in Petroleum Law, University of Dundee, Scotland (1985); Bachelor of Laws, University of Dundee, Scotland (1984) and Honours Bachelor of Arts, Lakehead University, Thunder Bay, Ontario (1982).

Mr. Black's duties as Executive Director of the Centres will be to work with the Academic Directors to develop and implement a core educational and research program. The Centres were created by the Institute to fill the void of opportunities for relevant education in transportation and regulatory affairs in Canada. Over the coming months, Mr. Black will be contacting industry and government representatives to determine educational and research priorities.

The Institute is also pleased to announce the appointment of **Dr. Jeffrey Church**, Associate Professor of Economics, at the University of Calgary to act as Academic Director for the Centre for Regulatory Affairs. As well, **Dr. Nigel Waters**, Professor of Geography at the University of Calgary, has been appointed as the Academic Director for the Centre for Transportation. The Academic Directors of the Centres will develop program offerings and work closely with the Executive Director to ensure that such offerings are timely and practical to users. In addition to these appointments, the Institute has established a Committee for each Centre that will govern the activities of the Centres. These Committees consist of Institute representatives from industry and the academic community, (both the University of Calgary and the University of Alberta).

Both Centres have begun their work. The Centre for Regulatory Affairs kicked-off its program with a very successful event, the *Electricity Deregulation Forum*, which was held on October 6th. (The program is described in more detail on the next page). A course in *Regulatory Economics* is also being developed for early 1999 and targeted towards employees without formal training in regulatory economics, but who would benefit from a general introduction to the main concepts, theories, and practice of economic regulation.

As well, the Centre for Transportation has teamed up with the Canadian Institute of Traffic and Transportation (CITT) to offer one core course towards its transportation designation. The course, *Physical Distribution & Logistics*, began for the fall term in September, and will be offered again in January for the winter term. Additional CITT course offerings are under consideration. Anyone interested in the

PETER NICHOLSON LUNCHEON

course, and the CITT designation, please call the Institute. *Executive Strategies for Transportation Projects* is another course under development for executives and managers for January 1999. Participants will work in groups determining the best transportation practices using the case study method.

ELECTRICITY DEREGULATION FORUM

If you are interested in finding out more about the work of the Centres, and its program offerings, please call Mr. Black at the Institute's offices.

Peter Nicholson, Executive Vice-President, of BCE Inc., will be speaking at a luncheon at the Calgary Chamber of Commerce on Thursday, November 5, 1998. The subject of his speech is *"What's Revolutionary about this Communications Revolution?"* For information on tickets, please call the Institute. About 100 participants attended the Electricity Deregulation Forum on October 6, 1998 in Calgary. Panels featured speakers on transmission issues, retail competition, and strategies and opportunities in the new deregulated environment. The day's session began with an overview provided by **Richard Woodward**, Director, Deloitte & Touche Consulting Group.

Dick Frey, President of Alberta Power Limited, described the new world of electricity supply under deregulation. The Power Pool now buys from generators, and retailers/customers will buy from the Pool. No one company has specific responsibility for planning/buying reserve power. He asked the audience to consider some questions that will affect future market development, such as investment and capacity issues. For example, who will buy capacity, now and in the longer term, as the Pool only buys and sells energy?

Kevin Wellenius, a Consultant with London Economics, spoke about mitigating market power with Auctioned Biddable Contracts (ABCs). Traditional utility regulation has been based on creating local monopolies in certain geographic areas. Therefore, any move towards competitive generation markets must address the inherited monopoly structure. ABCs transfer bidding/dispatch control of individual units to the purchaser for duration of a contract (e.g. 20 years). The operation, maintenance and ownership of physical assets remain with the current owner. ABCs are plant or unit contracts, so they can be sold to different contract holders, fostering competition. The price paid for an ABC at an auction allows a 'market valuation' of assets for resolution of stranded cost/residual benefit issues. In this way, ABCs avoid many distortions of alternative methods for mitigating market power. It also allows fundamental changes in market structure without the need for divestiture of assets.

Richard Kline is President and CEO of Mercury Electric Corporation, an independent power producer, which provides small-scale on-site energy solutions. In 1997, installed power capacity in the province was 7,719 megawatts (MW). The load factor increased in 1996 to 76%, and the reserve margin declined to only 7% in 1998. It is predicted that between 200-300 MW will be

needed each year for the next 10 years to keep up with increased demand. He outlined some solutions to the looming energy supply shortage, such as can be supplied by his company.

Ann Scully is the President & CEO of ESBI Alberta Ltd., the transmission administrator (TA) for Alberta. Its mission is to provide fair access to secure transmission at economic rates. The transmission administrator has been legislated to provide open access to the transmission system including: setting policies for transmission system operation; responsibility for access arrangements for ancillary service exchange on inter-ties; contracting with transmission owners and support service providers for facilities and services; paying for transmission losses; paying incremental generation costs arising from transmission constraints, and preparing tariffs to recover costs.

James Bushnell, Research Associate with the University of California Energy Institute, talked about market power and transmission rights (TRs). He then reported on TRs in California and the Independent System Operator (ISO) Market Surveillance Committee's concerns, namely the potential for using rights to withhold transmission capacity. Transmission pricing may then shift completely to secondary markets with less transparent prices, more difficulty in monitoring abuses and more reliance on the ISO real-time energy market. The Committee then recommended to limit capacity of TRs issued this year to 1/3 of system 'capacity,' and to monitor the impact of TRs on the ISO transmission market.

Murray Nelson, Executive Vice President, Transmission and Distribution for TransAlta, indicated that TransAlta was very supportive of deregulation of the industry, as it gave up control of the transmission system in 1996 when an independent transmission administrator was appointed. The costs of the new structure must be considered, such as the three new monopolies (transmission administrator, system controller and power pool administrator), new metering, and the more complex regulation that will result. Customers must see a net saving. He concluded by asking the following questions: Is transmission a natural monopoly? Should there be one owner/operator? Is Alberta too small for the current structure?

Guy Bridgeman, is Director of Regulatory Affairs for EPCOR Utilities, which owns Aqualta (a water company), Edmonton Power (regulated generation, transmission and distribution) and Eltec (electrical services). His comments focused on the Stable Rate Option (SRO), the guaranteed stable rate for a 5 year period starting in 2001 for small and residential customers. He identified some issues such as eligibility of the customers, the delivery agent, the method of regulation, the definition of 'stable,' the level of costs and the management of commodity cost risk. In his concluding comments, he indicated that SRO implications must be considered as the Power Purchase

Agreements (PPAs) and the auction process are designed.

Mark Ronayne, Commerce Office, Civil Branch of the Competition Bureau, outlined the elements for effective retail competition: effective generation competition; non-discriminatory access to distribution, information and consumers; structural separation, knowledgeable consumers; and control of anti-competitive behaviour. In the transition period, consumer protection is key through consumer education, regulated or industry-led marketing codes of conduct, and avoidance of unnecessary competition restraints.

James Fitzowich, Vice President Marketing of TransCanada Power, outlined the key elements for retail competition: liquidity in supply (many sellers); efficient whole market mechanism (Px or Hub); fair and non-discriminatory transmission access and liquidity in the market (many buyers and customer choice). There are two types of retail markets: corporation/industrials with large loads and individuals/commercial with small loads. Large customers are the markets of choice for suppliers; small customers are the least desirable markets. TransCanada plans to concentrate on the wholesale side of the market - fuels, transport and large loads. Efforts will focus on building and purchasing new generation and supply. There are no plans to sell to individuals or the small retail market.

NEW MEMBERS

NEW BOARD MEMBERS

Karen Shea, Project Manager with Pacific Gas and Electric Company, gave an update on the deregulated market in California. The new market started April 1, 1998. The Power Exchange (PX) handles the day-ahead market and the one hour-ahead market. The Independent System Operator (ISO) balances energy demands in a real-time market, and the ancillary services markets (capacity and reserves). She reported that the day-ahead market is operating well, the hour-ahead market is just beginning, customer choice in switching and billing is functioning, and the ancillary services market is functioning, but not as well. However, throughout the changes, reliability has been maintained.

Darwin Gillies, Director of Business Development for Encore Energy Solutions, spoke about what is on the horizon for Alberta's electricity industry. Direct access (partial customer choice) will begin next year with a stable rate option for non-choice customers. There will be distribution access and auction of power purchase agreements by the year 2001. The meter and CIS monopoly will continue as the "Wires Services Provider." He predicted that in this market there would be increased customer choice, new technologies, products and services, convergence and retail service mergers, and outsourcing of energy management (also risk, portfolio and asset management).

Ron Munkley, Vice Chairman and Head of the Power & Utilities Group at CIBC Wood Gundy, talked about strategies and opportunities in the industry. He indicated that deregulation is leading core changes in many industries and there are many parallels between them. The natural gas industry was deregulated in 1995 and now virtually all industrial and com-

SPEECH AVAILABLE

mercial customers buy 'direct', with prices that have fallen significantly. The new energy value chain has moved to one of low margins and high risks from a relatively stable environment. He sees strategic opportunities in infrastructure, independent power production, energy trading, and retail markets. New competencies will be required for partnerships, alliances, mergers, acquisitions and privatizations. The market will now move to customer choice versus the 'one size fits all' market of the past.

The Luncheon Keynote Speech was given by the **Honourable Stephen West**, Alberta Minister of Energy. He spoke about the evolution of the new framework for deregulation of the electricity industry. He acknowledged that there were a number of transitional issues to deal with, in particular, power generation capacity reserves, which are lower than they have been

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