

CONSUMER OWNERSHIP OF VERMONT UTILITIES

*A Concept Paper in Response to the
Report of the Working Group on Vermont's Electricity Future*

Washington Electric Cooperative

December 21, 1998

Washington Electric Co-op (WEC) offers this concept paper for public discussion in response to the Working Group's recommendation that a comprehensive solution to Vermont's above-market electric energy costs should include a merger of the state's investor-owned utilities. The report further suggests that the state's cooperative and municipally owned utilities should also consider complete merger of their poles and wires functions, and further, that these consumer-owned utilities might benefit by opting in to the merger of the investor owned utilities.

These suggestions are very seriously flawed. Due to the weight given to the report in general and because several of Vermont's opinion leaders and editorial writers have so quickly and uncritically endorsed this concept, WEC is obliged to put forth an alternative concept, that of consumer ownership. This is a concept paper. It is not a fully formulated proposal, although such concepts have been under consideration by WEC and others for some time.

As shall be discussed in further detail, a system of consumer-owned energy companies truly offers Vermonters the greatest chance for preserving Vermont ownership and control of its utilities, whereas the Working Group's proposal actually increases the risk that Vermont will lose this control. Consumer-owned utility systems can offer Vermont consumers the greatest likelihood for:

- ▶ controlling costs
- ▶ maintaining and improving quality of service
- ▶ operating in an environmentally and socially responsible manner and promoting energy efficiency
- ▶ democratic governance
- ▶ economic benefit for consumers

WEC proposes consideration of the concept of consumer ownership. *We believe the concept has merit whether Vermont's utility industry is opened up to retail competition or not.* For this reason we are not proposing one particular form or structure at this time.

WHAT'S WRONG WITH THE WORKING GROUP'S PROPOSAL?

- ▶ The proposal to merge the three investor-owned utilities appears to be driven primarily by the current financial situation of these companies only. Other options for achieving similar economies of scale or preserving Vermont control of the distribution system were apparently not considered.
- ▶ The idea that such a merger would help our distribution system remain a Vermont-based industry is surprisingly naive, given what is going on in the industry, especially given recent developments in the industry. Consolidating these three utilities in the manner proposed merely makes for a more attractive takeover target by large corporate entities with no connection or concern for Vermont. Contrary to the Working Group's opinion, WEC finds that economy of scale savings achieved through today's mega-mergers are primarily touted as benefiting shareholders, not the average consumer. In the past two weeks, major utilities in Massachusetts and California have been bought by foreign companies.
- ▶ The Working Group's rationale is entirely cost-based. No consideration whatsoever is given to other values such as quality of service, responsiveness, local control, relationship with the consumer, direct equity ownership by consumers, and other issues which Vermonters care about. The fact that the Working Group suggests that existing consumer-owned utilities should be subsumed into this merger without regard to these values is troubling, especially when this only further increases the odds of subsequent buyout by interests far from Vermont.

WHAT IS CONSUMER-OWNERSHIP?

Vermont has a long tradition of consumer-ownership in the electric utility industry. Vermonters are also very familiar with consumer co-op businesses, as evidenced by the very significant market penetration of credit unions, and the growing memberships in food and other types of co-ops. There are two types of consumer-owned utilities:

- ▶ Cooperatives, which are businesses owned by the consumers they serve.
- ▶ Municipal utilities, which are departments of local government.

Although in this paper, WEC primarily discusses the advantages of cooperatives, we also recognize that we have a great deal in common with municipal utilities. Within a cooperative structure, there is clearly opportunity for coordination, alliance or consolidation between co-ops and municipals. Such alliances exist to some extent today.

Our point is that the direction suggested by the Working Group is not the direction Vermont should head. The state's investor-owned utilities (not presently owned primarily by Vermonters to begin with) should not be consolidated and then possibly further absorbed. Rather, in this time of uncertainty in the industry, consumer ownership of Vermont's poles and wires is the best way to assure continuing Vermont control, and to lessen the likelihood that our system will be acquired (and probably re-sold again) by outside corporate interests motivated only by maximizing profits quickly.

HOW DOES A CO-OP UTILITY BENEFIT ITS CONSUMER/MEMBERS?

- ▶ Each consumer is a member. A cooperative is the only type of utility where the consumers directly elect the governing board. All consumers have a vote, whether they are residents, businesses, institutions and organizations or seasonal residents.
- ▶ In a cooperative, consumers actually build ownership (equity, or capital credits) in the company by paying their bills. Capital credits remain with a member whether they continue on the system or not. A financially healthy cooperative returns equity by making distributions. (In 1998, WEC returned approximately \$200,000 to members and former members.)
- ▶ Cooperatives generally benefit from high member loyalty due to their reputation for responsiveness, honesty and consumer education.
- ▶ While co-ops are democratically governed, they are not government. They are businesses that can respond to changing consumer needs. Members have close contact with their board, staff and as well as senior management of the company.
- ▶ Electric co-ops today cover many communities, and by definition serve the most rural, rugged and difficult to serve territory in Vermont. They have a very high percentage of residential members. They are more likely to remain committed to their members and the communities they serve than companies owned and run from afar.
- ▶ A consumer owned utility does not have an inherent conflict between the shareholders interests and the consumers . It is no accident that the two utilities that have done the most to reduce their members bills through efficiency services are consumer-owned (WEC and BED).
- ▶ Consumer-owned utilities are more likely to be environmentally and socially responsible, to promote renewable energy and technologies such as new dispersed generation (home and business based) generation.

CAN CO-OPS SUCCEED IN AN INDUSTRY INCREASINGLY DOMINATED BY A HANDFUL OF GIANTS?

- ▶ As mergers and consolidations accelerate in sectors such as banking, consumer services for household and small business accounts have decreased and become more expensive. Cooperative financial institutions (credit unions) continue to provide competitive, consumer-oriented services targeting ordinary consumers who do not benefit from mega-mergers designed to benefit large customers and shareholders.
- ▶ In other industry sectors such as agriculture and food processing, cooperatives have long been among the dominant players, while working on behalf of their member producers.
- ▶ Market research done by electric and other cooperatives show significantly higher customer loyalty than for other types of businesses.
- ▶ The fastest growing types of cooperatives are co-ops made up of small businesses aggregating themselves to compete in the modern economy. (For example, locally owned hardware stores are increasingly joining cooperatives such as Ace, TrueValue and ServiStar in order to compete.)

- ▶ Local electric cooperatives throughout most of the country have long achieved the economies of scale recommended by the Working Group, through cooperative alliances for purposes of generating, purchasing and transmitting wholesale energy, power planning, financing, computer and billing systems, equipment purchase, consumer education, and management. It is a recognized cooperative principle that co-ops work with co-ops. They form service co-ops (cooperatives whose members are co-op businesses). In the northeast, where there are relatively few electric co-ops, a new service co-operative is presently being formed that include energy co-ops, credit unions, food co-ops, and the housing cooperatives of New York City (which represent potentially more households than there are meters in Vermont). WEC has played a leadership role in formation of this service co-op.

HOW WOULD CONSUMER OWNERSHIP BE STRUCTURED IN VERMONT?

- ▶ There are a number of potential structures possible. They range from simple acquisition of existing utilities into a single large co-op, to formation of more locally based co-ops that would achieve economies of scale through cooperative management, operational and administrative structures. There are a number of co-op structures throughout the country that can be instructive.
- ▶ Municipal utilities can readily be included in a cooperative structure or alliance in Vermont.
- ▶ WEC recognizes that our suggestions could result in structural change for our cooperative. We have not at this point analyzed the specific impact of any new cooperative structure either on WEC or on any other entity.
- ▶ The concept is applicable both in the current regulated monopoly environment, as well as in a retail competition environment, should Vermont go in that direction. It can be structured independently, or in combination with proposals by others to refinance or buydown above market power contracts.

IS CONSUMER OWNERSHIP ACHIEVABLE?

- ▶ WEC is a member of the National Rural Utilities Cooperative Finance Corporation (CFC), headquartered in Herndon, VA. CFC is an AA-rated lender with a \$12 billion portfolio, which raises private capital for the operational needs of existing and new co-ops, to assist them in developing new services, and to bring cooperative opportunities to new consumers.
- ▶ CFC has a track record in helping electric cooperatives acquire investor-owned electric and gas utilities, in financing new cooperatives, and in enabling rural telephone systems to acquire assets from the Baby Bells and from GTE.
- ▶ CFC is willing and able to work with WEC and others in Vermont to bring consumer-ownership to all or portions of Vermont's utility system, and to do so in a way that supports other efforts to reduce above market power costs outlined in the Working Group's report.

IN SUMMARY

WEC is proposing a concept for public discussion. We felt that it was necessary to respond quickly to the Working Group's proposal, because Vermonters deserve a more thoughtful discussion, and because we know there is significant interest in consumer-ownership. WEC does not agree that a merger of Vermont's investor-owned utilities is in Vermont's best interest, and we believe there is a better idea.

Contact:

Avram Patt, General Manager
Washington Electric Cooperative
PO Box 8
East Montpelier, VT 05651
802/223-5245
avram@washingtonco-op.com