

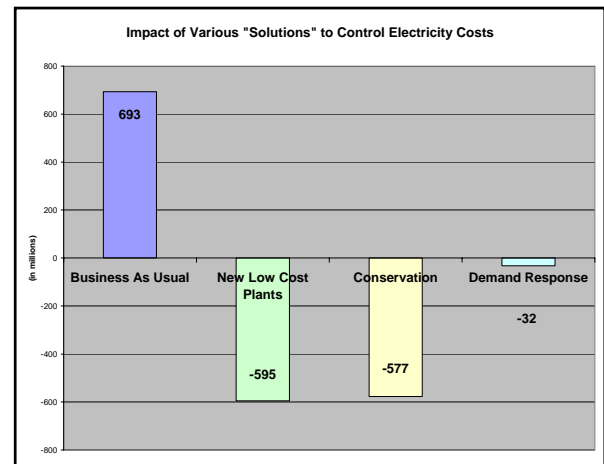
Controlling Electricity Costs

Wholesale electricity prices in New England are directly linked to the cost of the fuel to produce electricity and the amount of electricity used by consumers at peak times during the summer season. Since the majority of the region's power plants are fueled by natural gas and set the wholesale electricity price, the volatility of natural gas prices this past fall and winter has been reflected in electricity prices. Consequently, as natural gas prices have begun to stabilize, wholesale electric prices have decreased. In turn, New England's utility companies have begun to reduce retail electricity rates. Power consumption on the hottest summer days has been growing at a rate of 2% each year, which is higher than growth in overall consumption. This consumption trend drives the requirement to build additional resources, adds to the capacity costs of the region, and is creating an inefficient power system where resources are built to satisfy demand for only a few days of the year.

ISO New England conducted an analysis to identify such factors that drive electricity prices and quantify the corresponding solutions for controlling electricity costs.

Highlights of Analysis

- Fuel costs, primarily natural gas, drive electricity costs in both regulated and restructured environments.
- The addition of low cost power plants and conservation are the most effective ways to control costs.
- Adding 1,000 MW of supply produced by low cost plants will save consumers \$595 million a year.
- Reducing electricity use by 5% through conservation will save consumers \$577 million a year.
- A 500 MW increase in Demand Response participation will cut costs by \$32 million a year.
- "Business As Usual" will cause electricity costs to remain high. A 5% increase in electricity use will increase costs by \$693 million.



Components of Electricity Rates

- Consumer electricity costs are comprised of three primary components: power, transmission, and distribution
- The ISO estimates that power costs, which reflect the cost of producing electricity and vary with the global fuel markets, will make up approximately half of the average consumer's electric bill in 2006. Of this, fuel and capacity costs account for 95% of the total.
- Transmission and distribution costs, which make up the remaining 50% of the bill, are regulated and reflect the cost to build, maintain, and operate the regional transmission system and the local transmission (distribution) networks.
- Over the next ten years, power costs are expected to track natural gas prices and capacity cost trends unless targeted action is taken to control these costs. Capacity costs are expected to increase by 75% as the region implements a new capacity market to ensure supply keeps up with growing demand. Transmission costs, while a small component of total costs, will rise by 77% as new lines are built and paid for. Distribution costs are assumed to remain fairly stable.

Action Plan for Managing Electricity Costs in New England

- Consumer conservation to reduce electricity use at peak times will lessen the need to add new plants.
- Development of power plants using low cost fuels, such as wind, nuclear, and clean coal, can lower power costs by displacing the operation of higher cost power plants.
- State officials and New England consumers can take more control of electricity prices in the region by:
 - Taking a leadership role to encourage conservation, especially during peak periods;
 - Adopting retail rate policies that provide incentives to businesses and residential consumers to manage their electricity use in real-time during peak use and high price periods; and
 - Siting new supply resources that use wind, clean coal, nuclear, and other alternative energy sources.