Will Regulatory Changes Alter How Suppliers Structure Electricity Pricing?

Regulatory costs are completely out of the control of third-party electricity suppliers. That is why EVERY third-party supplier has language in their contracts that state if there are changes in regulation or changes in law the supplier reserves the right to pass through increased costs to the customer.

There are 3 major cost components that make up electricity rates.

- **Commodity (Electricity)-** The generation and use of electric power over a period, expressed in kilowatt-hours (kWh)
- **Capacity (ICAP)-**Capacity rates – measured in $/megawatt/day – are published 3 years in advance and apply to all customers on the grid. Each individual customer has a unique capacity tag that is based on actual usage during the 5 peak days experienced by the entire grid from June to September of each year.
- **Network Integration Transmission Service (NITS)-**Allows the grid to integrate, plan, economically dispatch and regulate grid resources to serve and ensure the long-distance transportation of electricity to local utilities and end load customers.

Demand charges (ICAP and NITS) typically make up at least 25-30 percent of a commercial electricity bill. When these costs are increased by regulatory bodies, suppliers will pass these increases through to the customer as a separate line item on a utility consolidated bill or a direct bill from the supplier.

Demand charges are hard to predict.

When a supplier calculates a customer's rate for a firm fixed contract, especially a multi-year contract, they estimate the cost of demand charges based on current published demand rates. For example, ICAP costs are published for 3-year increments. If a contract is signed to run beyond the known 3-year period, there is a greater risk that capacity costs will be adjusted for future terms, hence a greater likelihood that the supplier will pass through additional charges for the remainder of the contract.

Unlike capacity costs which are published for 3-year increments, NITS charges are much more volatile, as we have seen over the last several years. Utilities nationwide are raising NITS charges to recover the costs of maintaining aging grid infrastructures, to ensure grid reliability. For example, throughout Pennsylvania and New Jersey regulatory bodies have increased NITS charges by upwards of 30-40%. Because NITS is considered a regulatory component, even if a customer has a firm fixed contract, these increased costs are now being passed through, resulting in higher than anticipated energy costs.

Obviously, any regulatory changes significantly affect the customer due to unanticipated increases in energy costs. But third-party suppliers are also affected as well. With the recent increases in NITS throughout PA and NJ, suppliers have worked diligently to inform their customers;

however, the unexpected changes have added significant administrative stress on supplier resources while they work to respond to increased customer correspondence while ensuring all increases have been calculated correctly for each end-user.

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The answer is clearly yes, as we have already seen one of the largest third- party suppliers in the U.S change its pricing models and fixed contracts. Now, instead of locking in all energy components, this specific supplier will now only lock in Energy, Line Losses, Ancillaries and Fees, while passing through Demand Charges such as Capacity and Nits.

By passing through Demand Charges as a separate line item, the supplier creates a better customer experience by providing greater transparency and reducing the frequency of regulatory communication.

This evolution in contracting will not adversely affect the end-user. The customer has to pay regulatory charges and if those charges increase, they will be passed through regardless. What this shift in contracting will provide is greater billing transparency and an effective end to the term “firm fixed” contracts.