

Why Are Electricity Prices Increasing?

■ Electricity Price Caps Are Expiring In Many States

Electricity prices—like the prices of all other energy sources—are rising across the United States. One of the factors contributing to the rising price of electricity is the expiration of price caps set in some states during industry restructuring. As these price caps are lifted, customers will see adjustments in their electric rates to reflect the *real* cost of electricity—which they have not seen for many years.

Restructuring of the Electric Utility Industry

A major shift in the utility landscape began in the mid-1990s, as a number of states, especially those in the Northeast, Mid-Atlantic region, and the Midwest, along with California, moved to restructure portions of the retail electricity industry. Aiming to lower costs by stimulating competitive markets for the generation portion of customers' bills, these states moved away from the traditional model in which state regulators set the retail prices for power.

Today, 19 states and the District of Columbia have adopted programs for retail electric competition. One prominent hallmark of nearly every state that adopted such markets was this—as part of the gradual transition to competition, state policymakers decreed that customers' bills would be frozen, and in many cases reduced, typically for a period ranging from two to ten years.

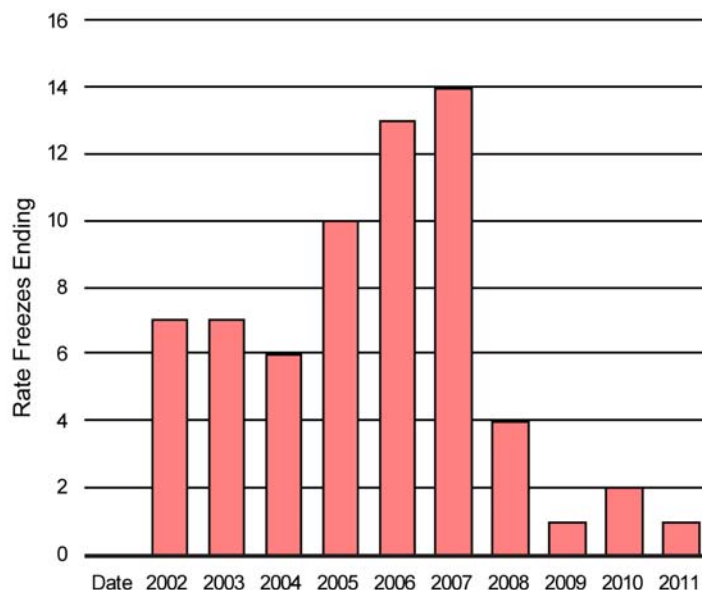
The first rate caps were put in place in 1997, and the last are set to expire in 2011. Beginning in 2004, many of those rate freezes and reductions began to be phased out. The result is that many customers now perceive that their rates are being “increased,” when in fact they are gradually reflecting the costs already incurred by utilities.

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Operating in a Rising Cost Environment

At the same time that the rate caps are expiring, the entire electric utility industry nationwide is facing a rising cost environment—and customers in both regulated and deregulated states are facing the challenge of rising electricity bills. Customers in many regulated states, for example, are paying higher electricity bills today because of higher fuel costs.

Price Caps Set During Industry Restructuring Are Expiring



As regulators and utilities revisit electricity rates that have been frozen for years, it is important to remember that these rate proceedings will help to fund the infrastructure investments that utilities must make to ensure reliable, affordable, and increasingly clean electricity. Utilities are committed to making the necessary investments to provide quality service at a reasonable cost. Adequate rate treatment is an important step in this process.

Unless otherwise noted, the information and data herein are derived from Why Are Electricity Prices Increasing? An Industry-Wide Perspective, a June 2006 study prepared for the Edison Foundation by The Brattle Group, a leading energy and economic consulting firm. The full report is posted on EEI's Web site, www.eei.org.

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