

Checklist for Choosing a Winning Retail Energy Services Provider

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As of late 2003, 24 states have opened their energy markets to some form of electric utility deregulation. Commercial and industrial users of electric power in virtually all business sectors in the United States stand to benefit the most from the choices now available through deregulation. According to the *Retail Market Status Report* issued by KEMA in June 2003, the total non-residential market amounts to 355,835 megawatts; the eligible non-residential market is 144,874 megawatts; and current migration to competitive suppliers is 40,804 megawatts. KEMA also predicts that non-residential energy provider markets are likely to experience 15 to 30 percent load migration growth over the next two years.

The Upside and Downside of Deregulation for Customers

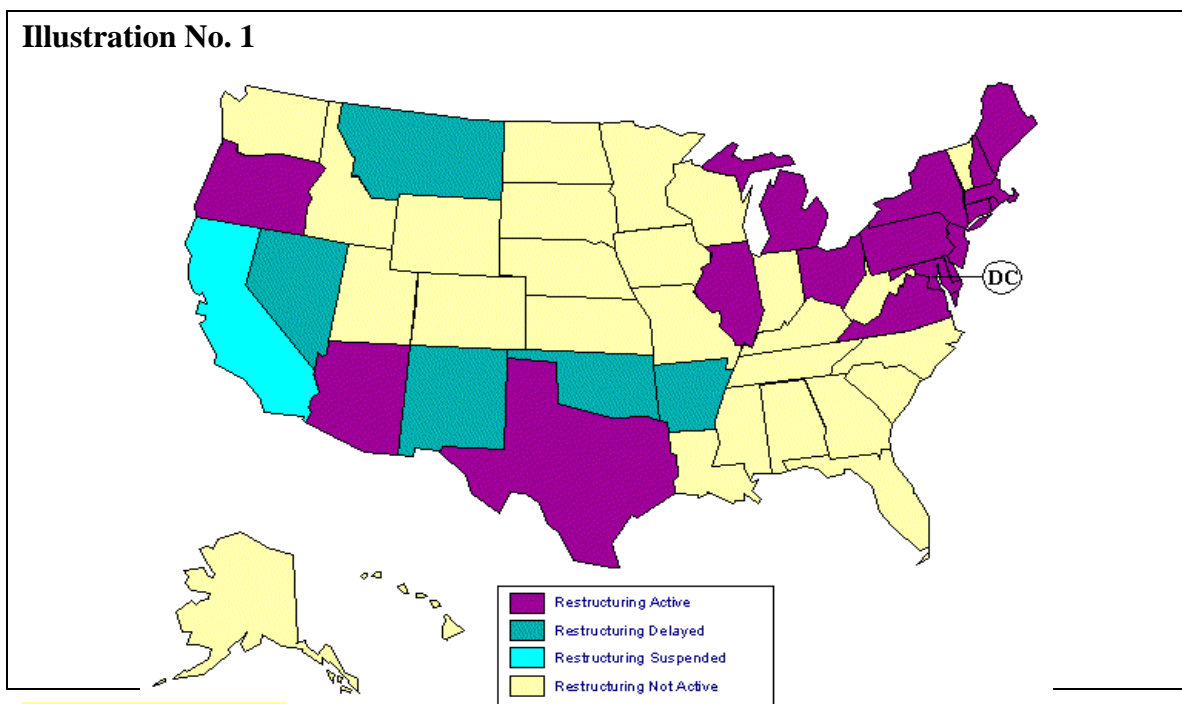
Typically, commercial and industrial customers consume one megawatt or more of power and have utility bills ranging from \$275,000 to \$30 million per year. By evaluating their alternatives, they can potentially save between 5 and 15 percent annually on their electric utility costs, and manage the volatility inherent in the utility bill. They can assume more responsibility for truly managing their energy needs and costs while maintaining a sharper focus on their core business (manufacturing, retailing, real estate management, etc.). They can access new products and services that their incumbent utility may have never offered them. And they can actually demand and get better customer service and more accurate, timely billing.

Yet, if choice is supposed to be so good for customers, then why is the process of choosing a retail energy services provider so time-consuming, confusing, stressful and, in short, daunting and discouraging? While there are many reasons, some of the most common include:

- The large number of US non-residential energy service providers from which to choose (the number has skyrocketed to more than 200 in 18 states)
- Affiliates of incumbent local utilities account for at least one-fourth of the total number of providers
- Uncertainty of suppliers relative to industry experience, geographic reach or financial staying power (Only a small percentage of suppliers are considered national and less than 20 percent operate in multiple states.)
- Increased price volatility and lack of experience in predicting or addressing price relative to usage
- Shifting risk to the customer

The challenge for customers is that many of them either don't *really* know the supplier they are dealing with **OR** they aren't deeply engaged in contract negotiations with their supplier. For their own benefit, that should change. What may look too good to be true usually IS too good to be true. Buyers should beware of signing up with a high-risk provider and risk being placed on provider of last resort.

The illustration below shows the competitive landscape in the United States. Overlay your company's footprint and search for value propositions.



Source: eia.doe.gov

Positive Factors of Deregulation for Customers

- Increased choice of service providers
- Increased innovation
- Increased customer focus
- Unleashed market forces
- Potential savings

Negative Factors of Deregulation for Customers

- Uncertainty of suppliers
- Increased complexity

- ❑ Increased price volatility
- ❑ Shift of risk to the customer

Checklist for Choosing an Energy Services Provider

Non-residential customers do have the opportunity to “empower themselves” to make the best choice in electric power providers. The following checklist provides a framework for procurement managers at commercial and industrial companies to use when they are evaluating options among many electric service providers. It is wise to gather information on as many as 5 to 8 providers. Then, even before seeking competitive bids, evaluate each one using the Scorecard provided in Illustration No. 2.

1. The provider should be **Registered or Approved** by the state public utility commission in each jurisdiction.

To maintain Uniform Business Practices, each state utility commission approves legitimate and credit-worthy competitors. Each supplier must prove that it meets certain Credit, Systems, and Legal minimum standards.

2. The provider offers **Refined Risk Management Capabilities**.

As a legitimate supplier, a company should be able to describe each and every component of its offering and the level of risk passed on or mitigated for the customer. Suppliers must always be able to assure their customers that they procure an adequate quantity of supply to meet their customer’s needs. Suppliers are in the business of managing risk for their customers.

3. The provider should offer **Innovative and Simple Products**.

At a minimum, the supplier should be able to show Fixed or Index commodity solutions. These two products represent each end of the risk spectrum. Additionally, the supplier should be willing and able to offer product solutions between those two ends. Examples include Stipulated Quantities, Block Prices, and Cross Commodity Swaps. Additionally, the supplier should be able to demonstrate how its products create value for the customer. Customers should ask for and get a simple explanation of terms and conditions (a one-page summary is very convenient for customers). Beware of “leaving” optionality on the table. A supplier may be asking you to give up what seems like a very simple option in the future. Every option has a value, it is imperative that all optionality is evaluated and measured by both parties.

4. The provider has a **Fair and Balanced Contract**.

The contract serves as the suppliers method by which they lay out the general terms and conditions, transaction specifics, and risk sharing techniques (i.e. product specifications) A fair and balanced contract is one that handles exceptions equitably and expeditiously. A contract should follow a standard form.

5. The provider should offer a **Competitive Price.**

Get at least three bids. Evaluate each bid for product specification and risk tolerance. The lowest bidder may not be the best solution. It is often said that the devil is in the details. Some suppliers purposely bid low prior to execution of the contract. Low bids usually indicate the potential of hidden costs, hidden risks, and hidden price volatility.

For each of the customer's accounts or groups of accounts, the supplier should be willing and able to explain how its offer is better than the customer's second best alternative, whether it is from an incumbent utility or another competitor. At times a utility offering may be more beneficial to a customer and, if so, a good supplier would be willing to tell you that. Long-term customer value is not generated by signing the next contract, rather from servicing the customer efficiently and honestly.

6. The supplier offers **Reliable, Timely** and **Accurate billing.**

The bill is an important way for suppliers to stay in front of their customers. Customers should ask to see samples of a customer bill and understand how the supplier resolves billing disputes.

At a minimum, customers should get their bill at the same time every month. The bill should be clear and concise. Means to resolving billing disputes should be clearly stated. Common ones include discussion to reach agreement, going to court or arbitration steps, or negotiating a new agreement. The best thing a customer can do is to pay the undisputed amount of the bill first, then come to an agreement on the disputed amount within five to 10 business days.

7. The supplier should be **Financially Stable.**

Suppliers perform a credit check on customers, so customers should do the same of their current or prospective supplier. During the current industry shake up, customers are smart to “hitch their wagons” to a long-term player.

A good question to ask is whether or not the supplier’s credit had ever been denied by an ISO (independent system operator), which means that no power can be released from the grid to that supplier for customers. It seriously curtails the supplier's ability to schedule delivery of power and therefore availability of power for its customers.

Additionally, a supplier should have a BBB- or better credit rating (investment grade). If a company is unrated, then the company should have strong financials, which reflect a conservative debt to equity ratio, significant cash reserves and its ability to generate profits and cash flows. Further, it is important for one to receive the notes to the financials. The aforementioned will allow one to see if the prospective supplier has adequate capacity on its line of credit, explain off-balance contingencies, etc. Ask for a copy of your prospective suppliers financials.

Other appropriate questions to ask to establish financial viability are:

- Credit triggers: Try to determine what the supplier's outcome would be if the credit rating agencies downgraded its ratings. Specifically, what is its ability to weather collateral calls in the event of a downgrade.
- Stability of operating cash flows
- Timing of bank and bond debt maturities
- Significant regulatory hurdles: rate cases, contract disputes
- Things to monitor: widening of spreads (i.e. bond spreads, credit default swap pricing spreads, equity based default spreads)

Other credit considerations beyond reading the supplier's financials:

- Listen to earnings calls
- Monitor news releases
- Review rating agency analysis and methodologies
- Build a relationship with key management
- Analyze industry and economic trends
- Leverage peer and banking relationships
- Confirm that the supplier has a credit policy – it is a safeguard from the supplier taking undue credit risk
- Ask whether the supplier has credit insurance
- Try to get a sense of the supplier's business reputation
- Confirm that the supplier has a Risk Committee that allows for independent oversight in the company's business
- Make sure the supplier has a proven track record
- Find out if the supplier has a diverse group of customers
- Have them provide you with both customer and supplier references
- Make sure you clearly understand your rights and obligations within the contract, specifically credit mechanisms

8. The supplier should have significant Industry Experience.

Longevity in the electric power industry is key. Customers should look for a company with a long, robust industry heritage and assess the overall experience of the company and team members that are providing electric power services. Other important factors to consider include commitment to customer service, responsiveness, industry knowledge and experience.

9. The supplier should have solid customer or strategic partner References.

Customers should ask for three to five references. References can be past or current customers, strategic partners or creditors.

10. Most of all suppliers should maintain a customer centric view with Efficient and Effective Customer Service.

Post contract execution, the operational aspect of a supplier gets put to the test. The best supplier should deliver a very efficient enrollment plan, describe the complaint resolution plan, include accurate contact information, and measure customer satisfaction with published metrics.

Additional Resources

There is no national clearinghouse for electric suppliers, however the following resources are available to all customers.

1. State Public Utility Commissions
 - a. Texas - <http://www.puc.state.tx.us/>
 - b. New York - <http://www.dps.state.ny.us/>
 - c. New Jersey - <http://www.bpu.state.nj.us/home/home.shtml>
 - d. California - <http://www.cpuc.ca.gov/>
 - e. Maryland - <http://www.psc.state.md.us/psc/>
 - f. Ohio - <http://www.puc.state.oh.us/>
 - g. Pennsylvania - <http://puc.paonline.com/>
 - h. Illinois - <http://www.icc.state.il.us/home.aspx>
 - i. Massachusetts - <http://www.state.ma.us/dpu/>
 - j. Maine - <http://www.state.me.us/mpuc/>
2. Independent System Operators
 - a. Texas - <http://www.ercot.com>
 - b. New York - <http://www.nyiso.com>
 - c. New Jersey - <http://www.pjm.com>
 - d. California - <http://www.caiso.com>
 - e. Maryland - <http://www.pjm.com>
 - f. Ohio - <http://www.pjm.com>
 - g. Pennsylvania - <http://www.pjm.com>
 - h. Illinois - <http://www.midwestiso.org>
 - i. Massachusetts - <http://www.iso-ne.com>
 - j. Maine - <http://www.iso-ne.com>
3. States on Deregulation:
 - a. <http://www.utilityconnection.com/page2d.asp#state>

Illustration No. 2 Retail Energy Service Provider Scorecard

Score each of the prospective bidders, rank each bidder according to total.

For each criteria score between 0 and 100.

<i>Criteria</i>	<i>Supplier 1</i>	<i>Supplier 2</i>	<i>Supplier 3</i>
Registered By State Utility Commission			
Offers Risk Management Capabilities			
Provides Innovative and Simple Products			
Fair and Balanced Contract			
Offers Competitive Price			
Provides Reliable and Accurate Billing			
Demonstrates Financial Stability			
Demonstrates Industry experience			
Provides References (3 to 5)			
High level of Customer Service			
Total Score			

Narrowing the Field

Once the homework is done and the scores are calculated, it's time to get down to the business of selecting the right electric services provider. The following are three simple steps to help get customers closer to the contract and sealing the deal:

1. Issue a Request for Proposal (RFP).
 - ❑ Develop risk tolerance and product specifications.
 - ❑ Assign enough time prior to enrollment to acquire data from UDC, Price, Negotiate, and Execute
2. Sign Letters of Authorization.
 - ❑ Sign LOA to allow prospective suppliers to secure usage history and develop a price.
3. Rank competitive bids.
 - ❑ Rank the bids based on Evaluation Criteria provided in the Scorecard.
4. Select provider and negotiate win/win contract.

About the Author

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