

## **THE HEARTLAND INSTITUTE**

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### **Electricity Deregulation a Success in Texas**

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As of January 1, most retail prices for electricity in Texas will be completely deregulated, solidifying the state as the national leader in deregulating electricity markets.

In many areas of the state, consumers can already choose from up to 41 different plans offered by as many 18 retail electric providers. To date, more than 60 percent of residential customers have exercised choice.

Deregulation has led to a surplus of electric generation capacity, so there have been no major blackouts in Texas as there have been in more heavily regulated markets such as California and New York.

#### **Prices Stable**

Barry Smitherman, commissioner of the Texas Public Utility Commission, notes prices for electricity today in the Electric Reliability Council of Texas (ERCOT) region--the competitive portion of the Texas market--are not much different from the rates prior to deregulation.

"Competitive rates in ERCOT are not significantly different from where they were before the retail market was deregulated," said Smitherman. "That's remarkable given the over 200 percent increase in natural gas prices over the same time frame. Only the forces of competition can be credited with keeping electricity prices lower."

#### **More Capacity Proposed**

More generation is on the way as the market responds to reports of declining future capacity reserves. As many as 17 new coal-fired power plants have been proposed. The 12 that are in some stage in the permitting process would provide 11,229 megawatts of new generating capacity.

Currently, Texas has slightly more than 70,000 megawatts of capacity.

TXU, the major electric provider in north Texas, has plans to invest more than \$10 billion in 11 new power plants.

"TXU's plan will meet the urgent power needs of Texas, lower wholesale power prices, create tens of thousands of jobs, and improve air quality," said Mike McCall, CEO of TXU Wholesale.

The proposed new generation will raise the forecasted reserve margin (the safety margin above peak capacity) from around 17 percent today to more than 22 percent in 2011.

### **Critics Express Concern**

Despite those successes, critics of deregulation complain the market hasn't responded fast enough to the decline in natural gas prices from their 2005 peak.

"Since the deregulation of the electric industry, Texas electric consumers have been paying much more for electricity than it really costs to produce," said Tom Smith, director of the Texas office of Public Citizen. "While this may be legal, it isn't right."

However, Smitherman said the claim that electric prices in Texas haven't exactly tracked natural gas prices is not a fair indictment of retail competition.

"Deregulated markets are more efficient at quickly passing through changes in fuel cost, in both directions," said Smitherman. "Prices are now falling just as regulated utilities elsewhere are lumbering toward rate increases."

### **Prices Respond Rapidly**

In other words, consumers in regulated markets will be paying for the increase in natural gas prices for some time to come, while electricity prices in Texas are already falling.

The benefits of deregulation may also be seen in today's prices as they reflect the voluntary tradeoffs consumers make between cost, quality, and convenience. In this case, higher prices could reflect Texans' desires to invest in new plants that have lower emissions and provide reliable supplies.

Electricity generation in Texas is heavily dependent on expensive natural gas--72 percent of capacity in Texas versus 45 percent in the rest of the country.

Natural gas prices are much higher than they were in 1999 when deregulation began, and prices for electricity in Texas have naturally tracked upward with gas prices.

Another factor that could be impacting Texas' electricity prices is the permitting process for the new plants.

Texas Gov. Rick Perry (R) in 2005 issued an executive order shortening the process, but environmental activists and some big-city mayors have attempted to halt or significantly increase the cost of the process over concerns about air quality and global warming.

### **Positive Effect on Economy**

One issue lost in the debate over deregulation and the environment is the impact that reliable electric supplies have had on the Texas economy.

At press time, year-to-date employment growth in Texas was 2.7 percent--more than twice the national average--accounting for an increase of 177,300 jobs.

*Site Selection* magazine, which has recognized Texas for attracting the most business relocations the past two years, points out that fast growth-job markets and innovative strategies by electric providers are key components in these relocations.

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