

THE IMPLICATIONS FOR COAL MARKETS OF UTILITY DEREGULATION AND RESTRUCTURING NOVEMBER 1995

PURPOSE

The National Coal Council has been asked to consider the effects of possible changes in the electric utility industry on domestic coal markets in the next decade. This study evaluated the effect on coal markets of such changes as FERC's proposed mandatory access to the transmission systems by all wholesale electric customers, the possibility of deregulation of certain parts of the electricity market currently regulated, and the entry of new entities into the electricity supply sector. The possible changes to be considered are to be based on these and other regulatory/legislative events of the last decade.

FINDINGS

The National Coal Council recognizes the high degree of uncertainty about the future of the electric utility sector and even greater uncertainty about its effect on coal use by the electric industry. The Council evaluated the direction of the impact on coal use in each of the following major implications for the industry:

- Increased competition.
- More customer choice.
- Less protection by regulatory oversight.
- Generation/transmission/distribution unbundling.
- Decreased cost of alternative technologies.
- Partnering

After evaluation on domestic coal use, the National Coal Council believes that:

- In the short term (two to five years), there may be a significant increase in coal demand, stemming from higher utilization of existing facilities with access to low-cost coal but offset by the closing of older non-competitive plants.
- Over the next five years, most of the increasing demand for electricity will be met by other fuels.
- In the mid-term (five to ten years), and continuing into the longer term, there is a potential for coal use to grow if one or more of several events occur:
 - a) The price of alternate fuels, primarily natural gas, rises or is perceived as likely to rise very substantially relative to the price of coal.
 - b) New organizational partnering among coal suppliers, transporters, and users is developed to reduce coal's cost relative to other fuels.
 - c) Either existing or new coal technologies decline sharply in cost and in the time required to construct such projects.

The National Coal Council believes that these changes may affect the rate at which clean coal technologies are being developed. Increased competition among electric utilities will encourage a focus on reducing costs. It will also reduce their willingness to make capital investments in new technologies because regulatory protection of these investments through a guaranteed return is unlikely. Combined, these changes are likely to delay development and deployment of clean coal technologies. This, in turn, will reduce coal's competitive ability, fuel new generation facilities, and delay the expected improvements in the environment available through employment of clean coal technology.

RECOMMENDATIONS

- The federal government, together with the private sector, should participate actively in the formulation of the transition strategy and the final institutional design decisions regarding electric utility deregulation with the objective of assuring that:
 - a) Existing coal facilities are not put at an unfair disadvantage compared to other sources of electricity.
 - b) New coal-based electric generating facilities can compete fairly with other new facilities generating business.
- The Department of Energy has championed the next generation of coal-based generating facilities, particularly through the Clean Coal Technology Program. The National Coal Council encourages DOE to help catalyze the commercialization of clean coal technologies by the private sector and to focus on lowering the capital cost of the lead time of such facilities.
- The National Coal Council is concerned that unnecessary environmental regulations may reduce coal's competitive position. Therefore, the Council urges DOE and other federal and state agencies involved in setting environmental regulations to ensure that sound science and appropriate cost/benefit analysis are applied to environmental decision making.
- The National Coal Council believes that the several industry sectors involved in the coal chain and others, such as technology developers and regional development groups, can reduce costs by coordinating their individual interests. Therefore, the Council encourages industry to develop such strategic alliances and urges regulators, to the extent they have oversight, to permit such institutional arrangements.