Preparation for Electricity Deregulation Needs to Include Risk Management Strategy

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On July 1, 2002, more than 500 of the area's largest commercial and industrial energy users will no longer be able to buy their energy the 'old fashioned way'. Instead, they will enter the unchartered waters of electricity deregulation where they will be on their own to select, negotiate with and rely on an alternative energy service provider.

While these 500 organizations will officially be the first to experience the frontier of electricity deregulation, they will quickly be followed by the other remaining commercial and industrial users in the coming year. In fact, a recent article in *The Wall Street Journal* reported that the Pennsylvania, New Jersey and Maryland region is the most developed deregulated market in the country.

How does an organization prepare itself to make new and unfamiliar decisions around such critical issues as how to approach the alternative energy market, how to select a supplier, is fixed pricing the right way or does a variable pricing approach make the most sense? How should the contract be structured?

In addition, because 'energy procurement' has meant that utility costs have been handled by accounts payable like other routine business expenses, companies now need to determine who on their staff should tackle these decisions. Should it be the CFO? Operations? Purchasing?

The complexity of these decisions and the looming deadline is further intensified by an extremely volatile electricity market.

New Market Situation Requires New Approach

The days of stable, consistent energy costs are over and as such, organizations who want to prepare themselves for deregulation in the best and smartest ways possible, are viewing their energy procurement decisions in the same way as they view other key business decisions: as a risk management issue.

Developing an overall energy strategy and then incorporating it into the business plan is an excellent way to begin this process. Annual energy expenses should then become a part of the annual operating budget. Developing a workable and smart energy strategy should be based in part on how great a portion the energy expenses represent in the budget.

Comparable Costs=Comparable Management

Once the magnitude of energy expenses is determined relative to the overall operating budget, it can then be viewed from a risk management perspective to help answer key questions such as how are other costs of this size managed. Are these costs actively managed or is a more passive procurement approach used?

Electricity risk management requires consideration of a variety of issues including an understanding of current energy loads, anticipating future market expansion and contraction, determining if energy procurement should be handled internally or outsourced like other professional services.

Electricity deregulation has forever changed utility costs from a fixed to a variable expense that will now require that it be managed with the same attention to detail and accountability as other areas of the organization are managed.

Developing an overall energy procurement strategy that is based on a risk management perspective is the critical and logical first step to successfully preparing for deregulation.