

EXECUTIVE SUMMARY

The Office of Inspector General of the City of New Orleans (OIG) retained TBG Consulting (TBG) to perform a detailed assessment of utilities regulation in New Orleans.¹ New Orleans is the only city in the United States to regulate an investor-owned energy utility when there is a state-level agency in place. The Home Rule Charter empowers the New Orleans City Council (Council) with the authority to grant franchises, set rates, and exercise regulatory control over utilities operating in Orleans Parish. Regulatory decisions made by the Council not only affect the utilities but every resident, business, and governmental entity in New Orleans. These entities' competing interests makes measuring the effectiveness of regulation by any single metric (e.g., residential customer rates) inappropriate. Ultimately, the goal of utility regulation is to advance the overall public interest in both the short and long term.

During the course of this project, new members were elected to the Council and the composition of the Council's Utilities Committee changed and expanded. However, the core regulatory framework analyzed in this report did not change.

The purpose of this review was to answer several questions:

- Are utility customers in New Orleans best served by the city's unique regulatory authority? Or, would the Louisiana Public Service Commission (LPSC) be a more appropriate regulator for the city's energy utilities?
- How does the Council deploy its regulatory resources?
- Are the Council's regulatory processes designed to maximize effectiveness and transparency?

TBG/OIG found that despite the potential for lower regulatory costs by a shift to LPSC regulation, the interests of the city's utility customers would likely be underrepresented. Ongoing changes to the Entergy system (i.e., dissolution of the System Agreement and shift to a regional transmission organization) could have significant consequences for the city's utility

¹ TBG's President is a nationally renowned expert with over four decades of experience helping regulatory agencies improve their effectiveness.

customers.² In addition, a previous attempt to shift regulatory authority to the LPSC resulted in the LPSC allocating more shared costs to the city's utility customers than the Council recommended prior to the regulatory transfer. For these reasons, the report concluded that it is in the public interest for the Council to continue as the regulator of the city's investor-owned energy utilities until there is further clarity on how the changes to the Entergy system will impact the city's utility customers.

The report identified several areas of concern in terms of how the city's energy utilities are regulated. TBG/OIG found that the Council carried out its regulatory responsibilities by relying almost exclusively on outside consultants. The issue is not whether the Council should use outside consultants; the issue is whether the Council should use outside consultants for everything. Regulatory commissions across the country use a mix of internal and external resources. However, 96 percent of the Council's \$7.2 million regulatory budget for 2013 was allocated to a group of outside consultants.

The Council's wholly outsourced approach resulted in higher than necessary regulatory costs because many activities could have been performed by a well-trained in-house staff at a lower cost. For example, four attorneys retained by the Council billed approximately \$2.4 million per year between 2011 and 2013 and four technical consultants billed approximately \$1.4 million per year during the same period indicating that a significant volume of work was being performed on an ongoing basis. Although many of the consultants' activities focused on highly specialized regulatory issues, several tasks were routine and are typically handled by in-house staff at other regulatory commissions. Ultimately, these costs were paid by the city's utility customers. Beyond cost, the Council's overreliance on outside consultants prevented the development of in-house expertise and institutional knowledge regarding critical regulatory matters.

The regulatory process in New Orleans relied on a limited number of participants and was largely driven by the efforts of outside consultants on behalf of the Council. Participation by non-Council entities is important as it adds independence to the regulatory process and provides checks and balances to the regulatory framework. The interests of residential and small business customers were not represented by a publicly-funded public advocate with adequate resources.

² The System Agreement is contract that governs the operation of the individual Entergy companies as a single power pool to capture the economic efficiencies of a larger system.

Further, the Executive Branch did not fulfill its regulatory responsibilities (i.e., recommending rates and performing investigations of utilities): the City eliminated the Department of Utilities in 2002. In the absence of participation by the Executive Branch, the nonexistence of a publicly-funded public advocate, and the lack of in-house Council regulatory staff, outside consultants fulfilled both roles in the regulatory process (i.e., trial and advisory). This dual role meant that the findings and recommendations made by the outside consultants went mostly unchecked.

TBG/OIG found that the Council's regulatory approach and practices lacked basic controls to ensure transparency, prevent misconduct, and promote effective decision-making. For example, Councilmembers were permitted to engage in verbal ex parte communications with the utility and other intervenors. This practice had the potential to introduce bias and errors into the regulatory process because these off-the-record conversations go unchallenged and can have a disproportionate impact on regulatory decisions. The lack of transparency was further exacerbated by the Council's use of settlements to resolve nearly all regulatory matters and the resulting lack of publicly available documentation to understand how and why decisions were made.

The recommendations presented in the report are intended to provide the Council and the City's Executive Branch with ways to improve local utilities regulation, including increasing the number of participants with defined roles in the regulatory process, building in-house capacity while reducing the reliance on outside consultants, and implementing safeguards to protect the integrity of the regulatory process and promote effective decision-making. Specifically, TBG/OIG recommended the following:

- The Council should improve how it uses its resources by building in-house capacity to carry out routine regulatory functions and use outside consultants as needed for specialized activities. Some of the contracts with the outside consultants should be reduced and some of the contracts should be eliminated. The Council can fund an expansion of its in-house staff by using various assessments and cost recovery mechanisms outlined in the City Code.
- The number of participants should be increased to add checks and balances by separating the various duties fulfilled by each party. This could be accomplished by expanding the Council's internal resources and the Executive Branch fulfilling its regulatory responsibilities related to recommending rates and performing investigations of the utilities. In addition, the Executive Branch could fulfill some of its regulatory

- responsibilities by creating a publicly-funded public advocate function to represent residential and small business utility customers.
- The Council should improve the safeguards in place to protect the integrity of the regulatory process. This includes strengthening ex parte rules to prevent off-the-record conversations between stakeholders and decision-makers, separating the roles fulfilled by the outside consultants (i.e., trial and advisory), and empowering an administrative law judge (ALJ) to make recommendations on disputed matters within the Council's regulatory jurisdiction. In addition, the Council should develop and implement an electronic filing system and post documents and information related to regulatory matters on an enhanced website.

Increasing the number of participants with clearly defined roles and imposing meaningful ex parte restrictions would add balance and independence to the City's regulatory process. Improvements to the Council's use of regulatory resources would lower regulatory costs and provide an opportunity for in-house personnel to gain institutional knowledge regarding critical regulatory matters. These modifications would increase the likelihood that regulatory decisions made by the Council effectively align the overall public interest and private interests.