

**BEFORE THE
PENNSYLVANIA
PUBLIC UTILITY COMMISSION**

**Policies to Mitigate Potential Electricity)
Price Increases)**

Docket No. M-00061957

**COMMENTS OF THE
NATIONAL ENERGY MARKETERS ASSOCIATION**

The Commission instituted this proceeding to examine measures to mitigate potential electricity price increases upon the expiration of utility rate caps in 2009/2010. NEM¹ commends the Commission for proactively addressing this issue. By providing timely information pertaining to the existence of below market rate freezes and the subsequent impact of bringing market forces to bear on rates, improved pricing signals and energy technologies that increase efficiency and enable meaningful demand response, consumer rate “shock” could largely be prevented. Moreover, NEM urges the Commission to consider that the ultimate form of price mitigation is competition. Existing rate caps have heretofore prevented the development of meaningful competition. In fact, one of the clearest ways to mitigate prices is to create a competitive retail market that supports the ability of competitive suppliers to make offerings tailored to meet consumers’ needs.

¹ NEM is a non-profit trade association representing wholesale and retail marketers of natural gas, electricity, as well as energy and financial related products, services, information and advanced technologies throughout the United States, Canada and the European Union. NEM's membership includes independent power producers, suppliers of distributed generation, energy brokers, power traders, electronic trading exchanges and price reporting services, advanced metering, demand side management and load management firms, billing, back office, customer service and related information technology providers. NEM members are global leaders in the development of enterprise solution software for energy, advanced metering, telecom, information services, finance, risk management and the trading of commodities and financial instruments.

NEM members also include inventors, patent holders, systems integrators, and developers of solar, thin-film, building-integrated photovoltaics, fuel cells, advanced Broadband over Power Line (BPL) as well as new and innovative electrical encoding, applications or decoding known as Smart Electricity.TM NEM and its members are committed to a consumer-focused, value-driven transition to a reliable, price and technology competitive market for energy and related products, services, information and technologies.

Accordingly, NEM suggests that the Commission consider instituting market structures and reforms that support the competitive retail electric market.

I. The Commission Should Encourage Energy Competition to Mitigate Energy Prices

NEM urges the Commission to utilize competition itself (energy price, service, technology and other value-added services and products) to mitigate prices and/or provide enhanced consumer value. To accomplish this objective NEM recommends that the Commission implement as many low-cost, high-impact structural and information technology enhancements as soon as possible to permit competitive providers to help Pennsylvanians mitigate rate shock. Basically, the lowest cost, highest impact structural elements of any price mitigation program should minimize costs and encourage the acceleration of the transition by consumers into a competitively priced market. NEM recommends that the Commission eliminate duplication of infrastructure and other transition costs associated with billing and back-office business processes and minimize the costs related to ratepayer-funded utility bad debt expenses.

NEM suggests that the Commission: a) institute embedded cost based unbundled utility rates and market-based commodity pricing signals; b) encourage the non-recourse, purchase of receivables by the utility at the utility's bad debt rate; and c) institute marketer referral programs. These improvements represent best practices that minimize consumer migration costs, minimize duplication of infrastructure and permit alternative providers to aggregate sufficient numbers of customers to build economies of scale and scope.

1. Embedded Cost-Based Rates and Market-Based Commodity Pricing

The current, transitional retail market structures, whereby utilities provide default service at artificially low, capped rates has inhibited the development of the retail energy market. In the long term, the efficiency of the retail market could be improved if commodity pricing signals followed the market more closely and if utilities implemented embedded cost-based unbundled rates.² Utility pricing of commodity to large commercial and industrial customers who can be billed hourly should be based on an hourly, time of day rate. Additionally, as long as a utility is providing commodity-related services to small commercial and residential customers, the commodity component of the "price to beat" should start with a monthly-adjusted, market-based rate to which should be added a utility's fully allocated embedded and projected stranded costs associated with providing all of the otherwise competitive commodity related products, services, information and technologies currently bundled in full service rates. By reflecting a utility's embedded and stranded costs of providing competitive services, consumers will quickly find that it is no longer in their interest to purchase competitive products and services from a utility that is designed to connect, maintain and reliably deliver. Additionally, marketers who cannot beat a "full cost" "price to beat" are not likely to be competitive.

² The New York Public Service Commission determined that, "one prerequisite to fostering market development is the conduct of cost studies, the ensuing assignment of costs to the utilities' various functions and services, and the establishment of fully unbundled, cost based rates for electric and gas service." (New York Public Service Commission, Case 00-M-0504, Order Directing Expedited Consideration of Rate Unbundling, issued March 20, 2001, page 1). The Commission further found that embedded cost based rates were required. (New York Public Service Commission, Case 00-M-0504, Order Directing Filing of Embedded Cost Studies, issued November 9, 2001). *See also* NYPSC Staff "Report on the State of Competitive Energy Markets: Progress to Date and Future Opportunities," March 2, 2006, p. 4 (recommending that, "Utility bills should continue to fully and separately identify energy supply costs and energy delivery costs, to provide the level of price transparency customers need to compare offers when selecting an energy supplier.")

Utilities should remove all costs related to commodity sales from delivery service charges and place them in their commodity price. Costs should follow causation, e.g., all costs associated with SOS service should be in the commodity component of SOS rates. These costs include:

transmission charges, scheduling and control area services, distribution line losses, a share of pool operating expenses, risk management premiums, load shape costs, commodity acquisition and portfolio management, working capital, taxes, administrative and general expenses, metering, billing, collections, bad debt, information exchange, regulatory compliance, and customer care.

These same costs are also included in utility pricing and, thus, result in a double payment of these costs by consumers if such costs remain in utility delivery service pricing. By properly assigning costs and unbundling competitive services from monopoly services, the Commission will encourage true competition on the basis of pricing, quality of service, and provision of value-added services.

2. The Payment Allocation Order Should Not Unfairly Favor Utility Distribution Service (Purchase of Receivables)

As a general matter, payments on a consolidated bill should be applied first to the consumables portion of the bill, then to the non-consumables portion. Payment for a consumed commodity should have priority over payments for depreciable physical assets like pipes and wires. Such a methodology recognizes that the utility pipes and wires are assets that can still be called into use, irrespective of a customer's non-payment. By comparison, energy that is consumed by a customer without subsequent payment cannot be recovered and resold to another customer. Simple fairness dictates that the consumables portion of an energy bill receive payment priority. This payment allocation order is warranted until the utility billing function is competitively outsourced or

unbundled from utility rates, with the unbundling based on the utility's fully allocated embedded costs of providing billing and collection services.

Additionally, as long as utilities are permitted to incur and recover costs associated with billing and customer care, they should be required to offer to purchase the receivables associated with a utility's consolidated bill without recourse at a reasonable discount that is reflective of actual costs. Utility purchase of receivables avoids the duplication of costs at the front end of the transition to a fully competitive market. As consumers migrate to the competitive market, more infrastructure costs such as billing and customer care can be borne by the marketplace and utility resources can be redeployed into critical infrastructure investments.

3. Marketer Referral Program

A successful program first implemented in New York by Orange and Rockland and now being implemented by other utilities in the state is the Power Switch marketer referral program.³ Marketers participating in the O&R program offer enrolling customers a seven percent introductory discount from the utility commodity rate for a period of two billing cycles. Customers are enrolled in the program when they contact Orange and Rockland directly about it or they can be referred to the program after the having been informed about it by the utility's customer representative from an inbound call transaction (i.e., new service call, bill inquiry, etc.). O&R has promoted the program through advertising, bill inserts, and special events. Customers can request a specific marketer or be assigned

³ New York Public Service Commission, Case 05-M-0858, Order Adopting ESCO Referral Program Guidelines and Approving an ESCO Referral Program Subject to Modifications, issued December 22, 2005; Order Adopting Orange and Rockland Utilities, Inc.'s Plan for an ESCO Referral Program, issued April 19, 2006; Order Adopting Consolidated Edison Company of New York, Inc.'s Plan for an ESCO Referral Program, issued April 19, 2006; Order Adopting Niagara Mohawk Power Corporation's Plan for an ESCO Referral Program, issued April 19, 2006.

to marketers on a random basis. The customer also has the option to return to utility service at any time. Orange and Rockland purchases the receivables of marketers participating in this program. The residential migration rate in O&R exceeds thirty percent. The program provides benefits for all involved – consumers benefit from an introductory discount and risk free introduction to choice; marketers benefit from reduced customer acquisition costs and reduced bad debt exposure; and the utility benefits from a streamlined program that facilitates the migration process.

Providing market-based pricing signals coincident with the implementation of appropriate competitive supplier and choice rules and business practices, as recommended by NEM, fully supports a measured and smooth transition to market-based rates and choice for Pennsylvania consumers, and, thus, is in their best interest. Proper supplier choice rules and business practices coupled with proper market-based price signals are the only way to truly ease the transition to market prices. NEM's recommendations would enhance the impact of the other policies being considered by the Commission in the instant proceeding and, if implemented, would further mitigate the impact of increasing energy prices on consumers.

II. The Policies Suggested by the Commission Would Mitigate Potential Price Spikes in a Competitively Neutral Fashion that Supports the Development of the Competitive Retail Market

The Commission raised a number of additional potential measures for consideration. NEM will address these measures in the sequence in which they appeared in the Commission's Order for ease of reference.

1. Educate Consumers

The Commission suggests that initiating a consumer education program well in advance of the expiration of rate caps would facilitate consumers ability to adjust their budgets and usage. NEM agrees that consumer education is a critical component of the movement toward market-based rates.

NEM recommends that the consumer education related to the expiration of rate caps should not be used to confer an unfair competitive advantage to advertise utility service. Likewise, the education materials should not mislead consumers about the nature and causes of the price increases, and there should be no implications that price increases are in any way caused by the restructuring of the retail energy market in Pennsylvania.

Well-educated consumers are critical to the achievement of successful competitive energy markets. The better-educated consumers are, the better shoppers they will become. Upon the expiration of the prolonged rate freeze, customers will have the opportunity to see market-based pricing signals. It is vital that consumers understand the transition and the choices that will be made available to them. The choices must be conveyed in a competitively neutral fashion. Consumers must understand that commodity markets as a general rule are inherently volatile. They should also know their choice among products can include such things as fixed price offerings, “green” offerings, risk management services and other value-added products and services.

NEM strongly suggests that all stakeholders be permitted to review and offer input on consumer education materials to better ensure a competitively neutral message. NEM would be pleased to participate in such an effort.

2. Encourage Conservation

In order to encourage consumers to engage in meaningful conservation efforts, they should be exposed to improved pricing signals. The historical approach of providing consumers with averaged rates fails to provide the necessary price signals, and incentive, to respond with modifications in demand.

See Response to 3 Below for further recommendations in this regard.

3. Reduce Peak Demand for Electricity

a. Strategies for Encouraging Demand Response

As an initial matter, NEM notes that EPC Act Section 1252(f) sets forth a national policy in support of demand response. It provides that,

It is the policy of the United States that time-based pricing and other forms of demand response, whereby electricity customers are provided with electricity price signals and the ability to benefit by responding to them, shall be encouraged, the deployment of such technology and devices that enable electricity customers to participate in such pricing and demand response systems shall be facilitated, and unnecessary barriers to demand response participation in energy, capacity and ancillary service markets shall be eliminated.

In support of this national policy, Section 1252(a) of EPC Act requires electric utilities to offer “time-based rate schedules” and supporting “time-based meters.” A non-exhaustive list of time-based rate schedules for possible implementation set forth in EPC Act include time-of-use pricing, critical peak pricing, real-time pricing, and consumer credits for peak load reduction agreements. Furthermore, choice customers are to be provided with, “the same time-based metering and communications device and service as a retail electric consumer of the electric utility.” Section 1252(a). EPC Act explicitly defines an

investigation requirement for state regulatory authorities with respect to utility implementation of time based rates and meters.⁴ Section 1252(b) provides that,

Each State regulatory authority shall conduct an investigation and issue a decision whether or not it is appropriate for electric utilities to provide and install time-based meters and communications devices for each of their customers which enable such customers to participate in time-based pricing rate schedules and other demand response programs.

The Commission's consideration of this issue beginning in this proceeding could be in satisfaction of this requirement.

The Commission identified a number of strategies for encouraging demand response including "adopting hourly pricing as the default service rate for large customers; establishing default service rates for customers that vary from season-to-season, month-to-month, or even time-of-day; and encouraging or requiring installation of technologies such as thermostats that automatically reduce a customer's usage during peak periods." (Order at 5). However, Commissioner Shane expressed doubts about hourly pricing suggesting that it would merely result in "manipulated competition" and questioned whether it produces "meaningful shifts in energy consumption." (Commissioner Shane Statement at 3).

⁴ However, EPAct carved out exceptions to the requirement of utility implementation of time-based rates and meters in certain instances. These include:

- (1) the State has implemented for such utility the standard concerned (or a comparable standard);
- (2) the State regulatory authority for such State or relevant nonregulated electric utility has conducted a proceeding to consider implementation of the standard concerned (or a comparable standard) for such utility within the previous 3 years; or
- (3) the State legislature has voted on the implementation of such standard (or a comparable standard) for such utility within the previous 3 years.

NEM submits that the U.S. Department of Energy's recent report on demand response is an important resource for highlighting the benefits of demand response and how to achieve them. DOE explains that,

The most important benefit of demand response is improved resource-efficiency of electricity production due to closer alignment between customers' electricity prices and the value they place on electricity. This increased efficiency creates a variety of benefits, which fall into four groups:

- *Participant financial benefits* are the bill savings and incentive payments earned by customers that adjust their electricity demand in response to time-varying electricity rates or incentive-based programs.
- *Market-wide financial benefits* are the lower wholesale market prices that result because demand response averts the need to use the most costly-to-run power plants during periods of otherwise high demand, driving production costs and prices down for all wholesale electricity purchasers. Over the longer term, sustained demand response lowers aggregate system capacity requirements, allowing load-serving entities (utilities and other retail suppliers) to purchase or build less new capacity. Eventually these savings may be passed onto most retail customers as bill savings.
- *Reliability benefits* are the operational security and adequacy savings that result because demand response lowers the likelihood and consequences of forced outages that impose financial costs and inconvenience on customers.
- *Market performance benefits* refer to demand response's value in mitigating suppliers' ability to exercise market power by raising power prices significantly above production costs.⁵

Accordingly, it is NEM's recommendation that residential and small commercial customers should receive monthly adjusted, market-based pricing. Other jurisdictions have instituted monthly-adjusted rates. Orange and Rockland customers in New York pay a monthly-determined Market Supply Charge.⁶ The Public Utilities Commission of Ohio determined that the Gas Cost Recovery Mechanism could be adjusted on a monthly

⁵ U.S. Department of Energy, Benefits of Demand Response and Recommendations, February 2006, at vi.

⁶ See P.S.C. No. 2 Elec., 11th Rev. Leaf No. 22V at:

<http://www.oru.com/documents/tariffsandregulatorydocuments/ny/electrictariff/electricG114.pdf>

basis finding that “the frequent calculation of GCR rates can be beneficial during periods of market/price volatility.”⁷

NEM agrees with the Commission that large commercial and industrial customers should receive hourly pricing. The U.S. Department of Energy recommended in its recent report that state Commissions consider adopting real time pricing as the default service for large customers.⁸ It concluded that, “Default service RFP tariffs that index hourly prices to day-ahead markets support demand response and retail market development by giving customers more notice and certainty of the financial consequences of their response.”⁹

Other retail choice jurisdictions have arrived at the same conclusion. The New Jersey Board of Public Utilities expanded the class of customers on hourly PJM real time pricing to all customers above 1000 kW effective June 1, 2007.¹⁰ Additionally, the New York Public Service Commission (NYPSC) recently required utilities to implement hourly, real time pricing (RTP) for their large customers.¹¹ The NYPSC found that,

As price signals for the highest peak hours are transmitted to customers, those large customers can be expected to respond, as the experience of National Grid and Central Hudson demonstrates. Since large customers

⁷ Public Utilities Commission of Ohio, Case No. 03-1384-GA-ORD, Finding and Order issued March 11, 2004, page 3. See also Ohio Administrative Code 4901:1-14-04.

⁸ U.S. Department of Energy, Benefits of Demand Response and Recommendations, February 2006, at page 53.

⁹ Id. at 52.

¹⁰ NJBPU Docket No. EO05040317, Decision and Order, December 8, 2005, pages 15-16.

¹¹ ConEd and O&R implemented hourly pricing for their mandatory time of use customers, those with peak demands greater than 1.5 MW and 1 MW respectively, as of May 1, 2006. National Grid will implement hourly pricing for its SC3 customers at 500kw and above as of September 1, 2006. NYSEG and RG&E must implement mandatory hourly pricing as of January 1, 2007, for their time of use customers at 1000kw or above. NYSEG and RG&E must file plans for converting the remainder of their mandatory time of use customers to hourly pricing. Central Hudson implemented an hourly pricing program in 2005 for its customers with peak demands greater than 1 MW. See New York Public Service Commission, Case 03-E-0641, ORDER DENYING PETITIONS FOR REHEARING AND CLARIFICATION IN PART AND ADOPTING MANDATORY HOURLY PRICING REQUIREMENTS, issued April 24, 2006.

use amounts of electricity disproportionate to their number, that response could have a significant impact on peak period prices.

More accurate price signals are also known to promote economic efficiency in general. Moreover, as demand-side load reduction and load control measures are implemented in response to these price signals, the potential for the exercise of wholesale market power is mitigated. Gaining and taking advantage of market power is more difficult, particularly during peak periods, when efforts to increase the price of supply meet resistance in the form of reductions to demand. As a result, moving from a policy of voluntary RTP to a policy of mandatory hourly pricing for large customers is fully justified at this time.¹²

NEM submits that the rationale of the NYPSC is instructive in the instant proceeding and supports the extension of hourly pricing to Pennsylvania's large commercial and industrial customers.

b. Advanced Meter Technologies

The Commission noted that in order to support demand response that advanced meter technologies¹³ may need to be implemented that permit "more concurrent measurement

¹² *Id.* at 14-15.

¹³ NEM recommends that the Commission consider separating the definitions, and resultant cost recovery incentives, between "enhanced" and "advanced" metering and information technology investments. Much of the law, regulation and public policy governing incentives for research and technology development support such a distinction.

For example, "Enhanced Metering Technology" (EMT) could be defined to include technology that is far superior than the decades old meters currently in place and yet currently available. Truly "Advanced Metering Technology" (AMT) on the other hand may require more rapid cost recovery provisions to offset the higher technology risks to make it a competitive use of capital in the shortest timeframe possible. Advanced metering and information technology could include bi-directional, remotely addressable and configurable and easily upgradeable, independent and parallel-processing nodes that may already be technically achievable.

NEM recommends that any Advanced Metering and Information Technology approved for social funding should at least be capable of remotely reducing demand (or dispatching sufficient supplies) in near real time to avoid congestion and/or new generation additions. Deployment of such Advanced Metering and Information Technology in environmentally sensitive and/or congestion-constrained areas should yield even more significant social benefits.

Moreover, until and unless public policy is competitively neutral between utility and non-utility investments in advanced information technologies, NEM recommends that the information obtained with captive ratepayer funds either with Enhanced or Advanced Metering Technology be a public good available

of electricity usage, and the ability of consumers, utilities and other market participants to access this time-of-use information.” (Order at 6). Currently, consumers lack the market-based rates and time-differentiated usage information that are prerequisites to permitting them to make educated cost-benefit decisions on their energy usage. Without these tools, consumers cannot be expected to engage in conservation or demand shifting in a significant way. Most of the effort in restructuring has been to correctly price supply, yet the truly efficient market must also properly price demand as well.

NEM urges that the metering infrastructure be upgraded to permit dissemination of real-time energy usage information. The availability of this information will permit competitive suppliers to more accurately match supplies to meet demand and avoid imbalance and standby costs. In this way, suppliers can significantly reduce costs and can pass along these savings on energy bills.

Likewise, consumers can also reap substantial benefits and cost savings through the integration of telecommunications, Internet and enhanced/advanced metering technology. This state-of-the-art combination of technologies will enable small and medium size consumers and businesses to closely monitor their energy consumption to reduce costs, create energy efficiencies and create the conservation incentives necessary to meet our current and future energy needs. Indeed, metering advances for large customers have added considerably to increases in productivity, efficiency and significant savings.

One means in which real-time prices could be communicated to consumers is through in-premise displays and interactive controls that provide real-time cost, consumption and

to the public at large for a nominal cost so that the use of the information may serve the consumers that funded it.

rate and accumulated cost per period time information and feedback. The devices would work in conjunction with the power kWh meter using some type of bi-directional communications. Additionally, behind-the-meter products exist that respond to pricing signals in the areas of home automation and control that permit consumers to monitor and adjust energy consumption by appliance, thereby promoting energy efficiency and conservation.

4. Energy Price Phase In Alternatives

The Commission discusses two different time frames for a phase-in of energy price increases. In one scenario, higher energy prices would be phased in after the rate caps expire with a deferral of energy costs. In the other scenario, utilities could begin to move rates to market levels prior to the expiration of the rate caps. Additional money collected through the early phase in, as well as interest, could be used to mitigate the size of retail rate increases when rate caps do expire.

With respect to a phase in program to be implemented after the expiration of rate caps, NEM strongly recommends that any discount be implemented in a competitively neutral manner through the nonbypassable distribution charge.¹⁴ This would permit a mitigation

¹⁴ As noted by the Commission price mitigation measures have been considered in Maryland. The decision of the Maryland Public Service Commission pertaining to BGE's residential rate mitigation plan provides valuable guidance in this regard. In this case, the Maryland Commission determined at the outset that,

In order to prevent distortion in the competitive retail market, the Commission prefers to consider a transition plan that would reflect market-based price signals for electric supply, while mitigating the effects of rate shock on the non-bypassable portion of customers' bills. Maryland Public Service Commission, Case No. 9052, Order Initiating Proceeding, issued January 10, 2006, at page 2.

The plan accepted by the Commission did, in fact, implement the discount as part of the non-bypassable delivery charge, not the commodity charge. As a result, it served the twin goals of "significantly reducing [customers] initial liability for increased rates upon the expiration of the rate cap, while providing full price

of price increases but at the same time ensure that consumers receive improved commodity pricing signals. The development of the competitive retail market and the corresponding development of consumer benefits is inextricably linked to the provision of improved pricing signals. Additionally, as noted above, consumers cannot be expected to engage in meaningful demand responsive behavior if they do not have access to timely price signals.

A phase-in to market based rates prior to the expiration rate caps also merits consideration. By gradually exposing consumers to price signals, it should increase awareness of the pending transition, and depending on prevailing market conditions and the magnitude of the utility price increase, could possibly facilitate competitive offerings. The Commission suggested that monies collected from the price phase-in could be used to offset price increases realized when the rate caps expire. NEM would suggest that any such offset be applied to the nonbypassable delivery portion of customers bill to promote competitive neutrality and preserve the market-based commodity pricing signal necessary for a competitive retail market.

5. Programs to Assist Low Income Customers

The Commission requested information to form an evaluation of the adequacy of universal service and energy conservation programs that could form the basis of recommendations to the legislature regarding assistance for low-income customers.

signals to such customers regarding their actual energy use which will promote competition.” Maryland Public Service Commission, Case No. 9052, Order 80638, issued March 6, 2006, at page 33. As of this writing, the Maryland legislature passed a rate stabilization measure incorporating the concept as well.

In order to facilitate the provision of services to low-income customers in Pennsylvania, barriers to providing service to low-income customers should be removed. Low-income customers should have the ability to apply all energy assistance payments to a competitive supplier offering. By excluding the application of such payments to competitive supplier charges it hinders the competitive market's ability to serve low-income customers.

NEM also recommends that market-based solutions such as aggregation should be utilized to address the needs of low-income consumers and to allow low-income customers access to lower prices in the competitive market. For example, the state could experiment with pilot programs that bid out aggregated low-income groups either as part of the POLR service or a separate service.

6. Review Interplay with Wholesale Energy Markets

The Commission suggested that a review of the relationship between wholesale and retail energy markets is necessary because of the strong linkage between the two. As discussed in an FTC Staff Report on Retail Competition,

wholesale market demand at any given time is derived from retail customers' demand at that same time. Thus, it is important for states to adopt policies that will facilitate retail pricing that reflects real time pricing that reflects wholesale price changes. As a result, there would be less need for the consideration of price caps on wholesale sales of electricity, because market participants will be able to adjust their consumption according to the prices for wholesale power.¹⁵

The FTC Report went on to explain that,

[p]rices are likely to be lower and reliability is likely to improve if more customers have time-sensitive rates and timely and accurate price information. With these things, customers can make better consumption

¹⁵ FTC Staff Report on Retail Competition, issued September 2001, at page 34.

and investment decisions that determine an efficient market equilibrium for electricity services. Increasing the price sensitivity of demand also will help to constrain existing or potential market power in generation. This is true because a price increase will be less profitable for generators if it is passed through and retail buyers respond by reducing their consumption by a significant amount.¹⁶

NEM urges the Commission to continue to work toward the development of a robust competitive retail market, including providing consumers with access to pricing information and time-sensitive rates as a concurrent measure to complement the development of the wholesale market.

7. Multiyear Contracts for Default Energy Service Supplies

Commissioner Shane asked commenters to discuss the approach of using multiyear contracts for default energy service supplies, as is utilized in New Jersey, as a means of protecting consumers for volatile energy prices. NEM submits that the three-year duration of the wholesale Basic Generation Service (BGS) supply contracts in New Jersey has retarded the development of a competitive retail market in the state. This structure is likely to lead to higher supply prices due to the lack of liquidity to hedge supply in the last half of the contract as well as increased counterparty credit requirements. The three-year duration also insulates a retail "Fixed Price" from market movements inasmuch as 2/3 of supply will always be locked in. As a result, a retail boom is created when the forward market drops below the "locked in" BGS rate and a retail bust is created when the forward market increases above the "locked in" BGS rate. This contributes to the general lack of mass market customer switching in New Jersey. By

¹⁶ FTC Staff Report on Retail Competition, issued September 2001, at page 41.

comparison, the large commercial and industrial customers that are exposed to market-based, hourly pricing on BGS have migrated in sizable numbers to competitive suppliers.

III. Conclusion

NEM appreciates this opportunity to offer its comments on policies to mitigate potential price increases that also support the development of the competitive retail market.

Sincerely,

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