BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Investigation of Pennsylvania's Retail Electricity Market	: :	Docket No. I-2011-2237952

COMMENTS OF
FIRSTENERGY SOLUTIONS CORP.

I. INTRODUCTION

FirstEnergy Solutions Corp. ("FES" or "Company") respectfully submits these Comments addressing issues relating to testimony presented during the Pennsylvania Public Utility Commission's ("Commission") *en banc* hearing held in Harrisburg, Pennsylvania on March 21, 2012 in the above-referenced proceeding (hereafter, the "Retail Markets Investigation" or "RMI"). The March 21 *en banc* hearing focused on matters relevant to the Commission's impending proposal in the RMI of a Long-Range Work Plan concerning the future design of electric default service and retail supply programs in the Commonwealth. By Secretarial Letter dated March 2, 2012, interested parties were invited to submit comments following the *en banc* hearing for the Commission's consideration in the development of a Tentative Order on the Long-Range Work Plan.

FES, a subsidiary of FirstEnergy Corp., provides wholesale and retail energy and related products to customers located throughout the Mid-Atlantic and Midwest regions. In addition to being a licensed Electric Generation Supplier (EGS)[1] authorized to serve all categories of retail customers throughout the Commonwealth, FES also participates in the default service supply procurements of all of the largest electric distribution companies ("EDCs") in Pennsylvania. FES has many years of experience serving the Pennsylvania retail and wholesale electricity markets, and offers a variety of products and services in those markets. FES has actively

[1] Docket No. A-110078 (1998)

participated in all phases of the RMI by filing Comments, presenting testimony by Tony C. Banks, FES' Vice President of Competitive Market Policies, at the Commission's three *en banc* hearings,[2] and by participating in working groups, sub-groups and technical conferences.

Since the inception of the RMI in April 2011, FES has fully supported the Commission's goals of ensuring a properly functioning and workably competitive retail market, including the appropriate design of end-state default service in the Commonwealth. FES respectfully submits these Comments for the Commission's consideration when developing its Tentative Order on the RMI Long-Range Work Plan.

II. COMMENTS

<u>A. Introduction</u>

FES appreciates that the Commission has been receptive to the constructive and informative input of all stakeholders throughout the RMI process. Such widespread participation indicates that the Commission's initiatives in the RMI have attracted the interest not only of electric industry participants, but of customers and consumer protection advocates as well. The stakeholders' varied input in this process has been invaluable, and in FES' opinion has confirmed the correctness and importance of FES' overarching principle in designing customer programs, expressed many times during this proceeding, of giving customers what they want, i.e., the lowest available pricing.

With that principle in mind, FES will comment on the following issues addressed at the March 21, 2012 en banc hearing, and under consideration in connection with the Commission's RMI Long-Range Work Plan:

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[2] June 8, 2011, November 10, 2011 and March 21, 2012

1) FES believes that Model A of the Staff's recommended alternative models for end-state default service will best benefit all customers since it properly reflects market pricing which enhances supplier participation and promotes customer shopping in a competitively neutral manner.

2) FES fully supports the importance of consumer education in connection with the programs the Commission will implement through the RMI; however, FES has concerns about certain cost recovery mechanisms that were discussed for such programs.

3) FES supports expanded opportunities for small and medium business customers to more fully participate and share in the benefits available from the retail marketplace.

FES respectfully offers its Comments on these issues below.

B. End-State Default Service Models

1) Introduction

FES' witness Mr. Banks participated in the EGS End-State Default Service Models panel during the March 21, 2012 *en banc* hearing and testified regarding the three alternative end-state default service models proposed by Commission Staff for consideration during the hearing. The March 2, 2012 Secretarial Letter described the three alternative models as follows:

> Under Model A in the Staff Discussion Document, default service would be provided to non-shopping and returning customers on the basis of real-time/hourly locational marginal prices and an administrative adder. Prices would change monthly (or more frequently) and not be reconciled.
>
> Model B would involve default service being provided to non-shopping and returning customers on the basis of prevailing market prices, as established through an index, auction, or other acceptable method. Prices would change quarterly or semi-annually and not be reconciled.
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> Model C would mirror the existing framework of providing default service to non-shopping and returning customers at a price that is compliant with 66 Pa. C.S.

§2807(e)(3.1)-(3.4). Prices would change quarterly or semi-annually, reconcilable on a twelve-month rolling basis.

In general, FES believes that the appropriate primary focus of an end-state default service program should be the product, not the provider of the service. FES sees no impediment to an EGS serving in the role of default service provider ("DSP"). Mr. Banks testified with respect to the differences among, concerns with, and challenges of each of the three alternative models, as well as other issues that need to be considered in order to implement a workable, appropriately-designed end-state default service program, and those comments are reiterated and further explained here.

As stated at the beginning of these Comments, the overarching principle FES focuses on when designing its retail products is being responsive to customers' preferences. Based on its years of experience as a retail service provider, including customer surveys, focus groups, and actual enrollment data, FES believes that at this point in time, customers' primary motivating factor in making shopping decisions is to receive the lowest price possible. Act 129, with its "least cost over time" procurement obligation, might appear to reflect that interest. However, Act 129 does not assure that the lowest possible price is obtained for default service over the entire time period covered by a default service plan, nor that prices achieved under the Act 129 principles compare favorably with offers that are available in the retail competitive marketplace, as Mr. Banks testified (Tr. 466). Further, EGS' procurement processes may arguably satisfy the "least cost over time" Act 129 standards at least as well as EDC default service procurement portfolios, since experience over the past couple of years has shown that EGSs regularly offer prices lower than EDCs' default service prices (Tr. 465-466). Commissioner James H. Cawley indicated his agreement with Mr. Banks' assessment that "alternative suppliers are providing a better price than what [Act 129] provides from the default supplier" (Tr. 467), and therefore EGSs' methods of obtaining supply may well satisfy Act 129's requirement that suppliers' procurement portfolios provide customers with generation that is the "least cost over time."

2) The Three Alternative Models

a) Model A is the Best Choice Among the Models Proposed by Staff for End-State Default Service

Having carefully evaluated the three models proposed by Commission Staff, FES strongly believes that Model A is the key to a successful end-state default service program in which the great majority of customers receive generation service from competitive suppliers, and few customers remain on default service. As explained below, of the three alternatives models, Model A is the most likely to encourage substantial retail supplier participation, which will lead to more competition and more varied alternatives for customers, including innovative products and services that offer value propositions in addition to price.

There are a couple of reasons FES believes Model A would result in the best end-state default service product. Since the Model A default service product includes real-time LMP pricing and does not contemplate any price reconciliations, customers would see the true cost of default service for the first time. Customers would then be able to accurately compare default service with the benefits of products that can only be offered by retail suppliers. Customers who value price certainty and predictability will have ready access to a variety of products that meet those needs from retail suppliers as opposed to default service.

Default service under Model A should be provided by one or more EGSs in each EDC service territory. Under Staff's proposal, Model A pricing will include an "administrative adder" on top of real-time LMP. In order to determine which EGS(s) provide default service in any given service territory, this administrative adder should be competitively bid, with the winning

EGS(s) being selected based on the lowest bid(s). In addition to the LMP plus the bid administrative adder, the final default service price could also include a Commission-determined component to offset costs the Commission determines should be borne by those customers choosing to remain on default service.

Of the three alternative models, Model A is most unlike the current default service construct. Most customers would probably not like the considerable price volatility resulting from Model A's real-time LMP pricing. Therefore, Model A should only be implemented after as many customers as possible have moved from default service to competitive suppliers. FES continues to believe that the quickest way to achieve this customer migration would be to conduct Commission-sponsored opt-out auctions prior to the projected June 1, 2015 start date of the End-State Default Service model. The use of auctions to move customers to a fixed price opt-out auction product would minimize the number of customers remaining on default service. The retail opt-out auction product should cover an initial two-year term, from June 1, 2015 to May 31, 2017, to match the term of the default service period, and all qualified suppliers should be permitted to participate.

In addition to the benefits customers would see in moving to retail suppliers compared with the variable cost of Model A default service, the smaller default service load should result in a relatively low financial assurance requirement from potential DSPs (compared with that which would be required to serve current default service loads). The likelihood of the lower financial assurance requirement will entice more competitive suppliers to consider the possibility of acting as DSPs, and result in more suppliers qualifying to provide that service.

b) Potential Legal Issues with Model A

During the March 21 *en banc* hearing, Commissioner Pamela A. Witmer asked that parties discuss in their Comments whether or not their End-State Default Service proposals will require statutory or regulatory changes to implement (Tr. 472). FES appreciates the Commission's concerns, as the models proposed (particularly Model A) would represent substantial revisions to the current default service construct. FES believes the retail opt-out auction is essential in order for the Model A construct to work, because it would be the most expeditious way of moving current default service customers to retail service. The circumstances surrounding the transition to end-state default service justify the Commission in exercising its wide discretion and flexibility under the Competition Act and Act 129 to employ an opt-out auction mechanism as part of the overall End-State Default Service program. The combined Model A end-state default service program and a long-term fixed price auction product will, FES submits, provide the dual benefit of serving the public interest and furthering the Commission's goal of a robust, competitive retail supply market in the Commonwealth by moving large blocks of customers to EGSs. FES recognizes that Model A may require an amendment to Act 129's requirement that the DSP offer residential and small business customers a generation supply service rate that changes no more frequently than quarterly.[3]

In addition, FES expects that some parties may argue Model A's LMP-based pricing does not satisfy the "prudent mix" portfolio requirement of Act 129[4]. FES respectfully disagrees with this argument. While no appellate court has decided the issue, the Commission has indicated its belief that Act 129 does not require a DSP's supply portfolio to include a minimum of two types

[3] 66 Pa.C.S. § 2807(e)(7).
[4] 66 Pa.C.S. §2807(e)

of products (long-term, short-term and spot market).[5] The Commission's interpretation of Act 129 will be entitled to substantial deference unless clearly erroneous. Of course, if the Commission determines that the Model A end-state for default service does not satisfy the "prudent mix" requirement of Act 129, then a statutory amendment would be required before it could be implemented.

c) Models B and C Are Not Good Choices for End-State Default Service

FES will briefly discuss why it does not believe Models B or C are appropriate for End-State Default Service. First, Model B goes back to the pre-Act 129 standard of establishing default service prices based on "prevailing market price". However, similar to the "least cost over time" or "prudent mix" provisions of Act 129, there is no clear definition of "prevailing market price." Second, both Models B and C include quarterly or semi-annual price changes or reconciliations of over and under-collections, which continues the current problem of sending false price signals to customers. As evidenced by testimony during the March 21 *en banc* hearing, customers like longer-term, fixed price products[6]. However, quarterly or semi-annual price changes or reconciliations of default service prices make it difficult for suppliers to design long-term fixed price products that they can be confident will beat the default service price. Finally, Model C is very similar to the currently effective EDC default service model but just removes the EDC as the DSP; as stated above, FES believes the appropriate focus of the End-State Default Service model should be the right product to spur competition, not which entity provides the default service. Model C does not address any of the underlying problems with the current default service construct. The problems that exist with current default service products

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[5] *Implementation of Act 129 of October 15, 2008; Default Service And Retail Electric Markets*, Docket No. L-2009-2095604 (Final Rulemaking Order entered October 4, 2011), slip op. at 60.

[6] See Section D, infra.

and pricing versus retail supply will continue to exist. Additionally, as discussed below, an extra and unnecessary layer of EDC-provided POLR service will also continue to exist.

3) Issues Common to All Three Alternative Models

Certain issues are common to all of the alternative models. First, under each scenario service would begin on June 1, 2015 and would be in effect for two years. FES agrees with these recommendations.

Second, EDCs would remain in the role of provider of last resort ("POLR") or back-stop service in the event of default by the default service provider. FES respectfully recommends against this approach. As described above, under FES' preferred Model A the majority of customers will have transitioned to the retail market, and the remaining default service load will be relatively small, which means that the risk of a DSP defaulting is minimized. In the unlikely event a DSP defaults, another qualified EGS will be capable of taking on the DSP role since there is very little price risk in the market-based price proposed in Model A. It is neither prudent nor cost-effective to require that EDCs maintain resources and infrastructure necessary to provide traditional back-stop service when this type of service will be such a small portion of load under the End-State Default Service Plan FES and other suppliers prefer.

Third, the appropriate maintenance of customer information and data needs to be addressed. Maintaining the integrity of customer information and data management is of utmost importance under all three model scenarios. If an EGS is serving as both the DSP and a retail supplier in the same service territory, care must be taken to assure that the retail supplier as DSP does not have any advantage over other retail suppliers through its access to customer information and data. FES believes the best way to prevent an advantage to the EGS DSP is to keep the EDC in the role of data manager. The EDC's continued data management responsibilities would include metering, billing, settlements, service terminations, POR programs, and universal service programs. As the distribution provider, the EDC may be the only entity that has a connection with 100% of the customers in its service territory, and EDCs have the existing infrastructure in place to perform these functions effectively. Further, requiring that EGS DSPs be responsible for customer data management would require unnecessary and duplicative costs that would have to be absorbed by the marketplace, particularly if multiple EGSs are serving as DSPs in a single utility's territory. However, if EDCs are to continue providing customer data management services to DSPs and to retail suppliers active in their service territories, they would need to maintain and update their systems so they can provide flexible billing services necessary to allow suppliers to offer a variety of products and services. To the extent that EDC system limitations do not support the various data management needs of EGSs as either DSPs or retail suppliers, such limitations should be addressed prior to the implementation of the End-State Default Service model.

C. Statewide Consumer Education

The primary purpose of education programs established by the Commission in this proceeding should be to present consumers with an unbiased message explaining the benefits of shopping for their generation supply through the retail enhancements enacted by the Commission in the RMI proceeding. Statewide, general education campaigns should focus on instructing all Pennsylvania customers about choices they will have as a result of the RMI initiatives. The programs proposed by the RMI Customer Education subgroup are designed to address issues raised at the November 2011 *en banc* hearing and to increase all Pennsylvania customers' awareness of shopping and to advise them how they go about changing their electric supplier. Since these statewide education programs benefit all electric customers, such programs should be funded through traditional EDC universal cost recovery mechanisms, meaning that EDCs should recover the cost of Commission-sponsored consumer education programs through a non-bypassable charge. Beyond the general statewide programs, marketing and consumer education aimed at particular customer classes or at customers in individual EDC service territories should be left to the discretion of, and funded by, individual suppliers as part of their competitive strategies.

Testimony presented by Ron Cerniglia of Direct Energy, LLC during the March 21 *en banc* hearing addressed the subject of cost recovery for consumer education programs (TR. 415-416). Mr. Cerniglia describes several funding options available for consumer education programs. The options he presented were: (1) a one-time non-bypassable EDC charge; (2) a "fair-share" approach where costs are allocated between utilities and competitive suppliers based on current levels of statewide migration; and (3) cost-sharing equally among suppliers. Any of these options can be considered a fair sharing of costs to fund consumer education. However, FES strongly disagrees with proposals that EDCs' "purchase of receivables" (POR) programs are the appropriate mechanism to collect the costs of Commission-sponsored consumer education or other retail enhancements. FES agrees with Mr. Cerniglia that the imposition of such costs on EGSs through a discount on POR is not appropriate since: (1) it violates the principle that cost recovery should follow cost causation; (2) suppliers that secure customers through the RMI retail enhancements but who do their own billing do not participate in POR programs and would therefore not pay their fair share (or any share) of such costs; and (3) cost recovery through a POR discount unfairly and disproportionately allocates costs based on EGSs' market shares, with no connection to the benefit EGSs may receive from the programs. A discount on POR should be used only for reasons that have a logical connection to the purposes of the POR program, not as a mechanism for funding cost recovery from EGSs for programs totally unrelated to the purpose of the POR programs. Such unrelated cost imposition will simply encourage EGSs to discontinue their participation in POR programs, and possibly to discontinue participating as retail suppliers in the EDC territories where such costs are imposed. Since POR programs were implemented for the purpose of attracting increased EGS activity in EDC service territories where they might otherwise not participate, it makes no sense for the Commission to now make these programs unattractive to EGSs.

D. Shopping Experiences of Small and Medium Business Customers

The Commission's Final Order on the Intermediate Work Plan (IWP) entered March 2, 2012 included increased education and outreach efforts, and to enhance the retail shopping experience for small commercial customers on PAPowerSwitch.com.[7] The testimony offered by Mssrs. Dallas Smith and Thomas W. Schneider during the March 21 *en banc* hearing made clear that commercial customers want to see the benefits of shopping, but do not want the experience to be time-consuming or confusing. Mr. Smith and Mr. Schneider both expressed a preference for supply contracts that provide a guaranteed fixed price for 24 months with a supplier who offers EDC consolidated billing (Tr. 375 and 380-381). In response to a question from Commissioner Witmer, Mr. Smith stated that his two most important considerations were price and contract length (Tr. 390). FES supports the programs initiated through the IWP to increase the small business group's awareness of retail shopping, and believes the Commission's decision to place comparative pricing data from multiple suppliers on PaPowerSwitch.com will provide valuable information to these customers.

[7] Final Order on Intermediate Work Plan at pp. 9 and 12.

FES submits the following recommendations so that commercial customers can obtain readily available information they need to make their shopping decisions. First, offers available to commercial customers on PaPowerSwitch.com should not be limited to one offer per supplier; suppliers should be able to list multiple product offerings for commercial customers, specifying contract length, product type and price. While it may be appropriate to limit residential offers to one offer per supplier per EDC, commercial customers are more likely to weigh a variety of factors in making their shopping decisions. On the current "Shop For Your Home" section of PAPowerSwitch.com, residential customers are able to see the supplier, product type (fixed or variable) and price information. FES strongly believes that in addition to these items, contract length should also be displayed in the "Shop For Your Business" listing for commercial customers.

Second, while the shopping statistics for small and medium commercial customers are difficult to quantify due to the current reporting methodology, John Bodine of OnDemand Energy Solutions testified at the March 21 *en banc* hearing that the number of suppliers offering products to this category of customers has increased since the expiration of rate caps (Tr. 366-367). Thus, it appears that current marketing efforts are increasing this customer class's awareness of shopping benefits, and the initiatives begun in the RMI IWP Order should further help to improve the shopping statistics for this group. In the event that additional standardized programs for small commercial customers are developed or expanded, FES urges the Commission to remember the testimony from the commercial customers during the *en banc* hearing, particularly that they want fixed price, long term contracts. That being the case, any further changes to the PAPowerSwitch.com website should take these desires of consumers into account.

III. CONCLUSION

FES commends the work done to date in the RMI including the recommendation of several retail enhancements and a statewide consumer education campaign. The combination of the right default service product, concise, simple consumer education, and an equitable sharing of program costs will establish Pennsylvania as the leader among all electric choice states because the design of the programs that are part of this initiative will be based on what is best for the Commonwealth's customers taking into consideration input from all interested stakeholders. FES appreciates the opportunity to submit these Comments, thanks the Commission for its efforts and support for robust retail electric competition, and looks forward to continuing to engage with the Commission, Staff and other stakeholders as we transition to the next phase of default service in the Commonwealth.