

**BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Investigation of Pennsylvania's Retail  
Electricity Market

:  
: Docket No. I-2011-2237952  
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**COMMENTS OF  
THE RETAIL ENERGY SUPPLY ASSOCIATION  
POST MARCH 21, 2012 *EN BANC* HEARING**

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Dan Clearfield, Esquire  
Attorney ID #26183  
Deanne M. O'Dell, Esquire  
Attorney ID #81064  
Carl Shultz, Esquire  
Attorney ID #70328  
Eckert Seamans Cherin & Mellott, LLC  
213 Market Street, 8th Floor  
Harrisburg, PA 17101  
(717) 237-6000 (phone)  
(717) 237-6019 (fax)

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Attorneys for Retail Energy Supply Association

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## I. INTRODUCTION

The Retail Energy Supply Association (“RESA”)<sup>1</sup> submits these comments to provide additional input following the Retail Markets Investigation *En Banc* Hearing that was held on March 21, 2012. RESA is a broad and diverse group of retail energy suppliers who share the common vision that competitive retail energy markets deliver a more efficient, customer-oriented outcome than a regulated utility structure. RESA supports the Pennsylvania Public Utility Commission’s (“Commission”) stated goal of moving default service customers into the competitive market and has been an active participant in this proceeding to provide input and suggestions on how to accomplish this goal.

During the *En Banc* Hearing, participants were invited to provide a legal analysis regarding the various “Possible End-State Default Service Models” described in the Staff Discussion Document attachment to the Commission’s March 2, 2012 Secretarial Letter. As set forth in more detail below, RESA’s preferred Model A as well as Model B either currently comply with the Electric Generation Competition and Customer Choice Act<sup>2</sup> (“Choice Act”) or can easily be structured to comply as the operational details for the selected model are developed. RESA cautions against Model C as it is a continuation of the current procurement plan process that does not result in prices that accurately track market prices and conditions and fails to produce a market outcome that produces “least cost” service for all customers accounting for their individual needs and preferences.

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<sup>1</sup> RESA’s members include: Champion Energy Services, LLC; ConEdison *Solutions*; Constellation NewEnergy, Inc.; Direct Energy Services, LLC; Energetix, Inc.; Energy Plus Holdings LLC; Exelon Energy Company; GDF SUEZ Energy Resources NA, Inc.; Green Mountain Energy Company; Hess Corporation; Integrys Energy Services, Inc.; Just Energy; Liberty Power; MC Squared Energy Services, LLC; Mint Energy, LLC; NextEra Energy Services; Noble Americas Energy Solutions LLC; PPL EnergyPlus, LLC; Reliant; TransCanada Power Marketing Ltd. and TriEagle Energy, L.P.. The comments expressed in this filing represent the position of RESA as an organization but may not represent the views of any particular member of RESA.

<sup>2</sup> 66 Pa. C.S. §§ 2801 to 2812.

A second issue participants were invited to address is statewide consumer education. Commission Staff circulated a “Proposal for a Statewide Consumer Education Campaign” dated March 13, 2012 and seeks input about messaging and potential funding sources. As set forth in more detail below, RESA supports statewide consumer education with broad messaging and significant stakeholder input. RESA also recommends that a charge be assessed on all distribution consumers to fund such campaign. Following basic cost causation principles and understanding the broad benefits to all consumers, RESA does not recommend utilizing the Purchase of Receivables (“POR”) discount rate as a funding mechanism for statewide consumer education which, among other issues, results in requiring only shopping customers to bear the cost of the statewide consumer education campaign.

## **II. END-STATE DEFAULT SERVICE MODELS**

From the beginning, RESA has recognized that there are many possible end-state default service models and implementation plans that can be adopted to better facilitate retail choice. RESA has consistently advocated for an end-state default service design that better serves the public interest by transitioning to a market model that results in default service prices that are competitive and most reflective of the market price, where there are numerous “non default service” competitive alternatives from which consumers can choose and the incumbent electric distribution company (“EDC”) is better able to focus its resources on providing reliable service to all ratepayers.

The Models set forth in the Staff Discussion Document attached to the Commission’s March 2, 2012 Secretarial Letter identify three possible transitional models in which electric generation suppliers (“EGSs”) serve in the default service provider role. Although many specific implementation details remain to be addressed, RESA can support Model A or Model B (with a

preference for Model A) as acceptable transitional steps preceding a true end-state market design. Both Models A and B would rely on EGSs to provide “default service” with the EDC providing a backstop, “provider of last resort” service. This produces several benefits including:

- Implementation of a Commission competitive process whereby a number of EGSs would provide bids to provide default service thereby resulting in competitive default service pricing
- Allowing new entrants in the market to achieve economies of scale and scope, resulting in more efficient competition and ultimately lower prices and “least cost” service for customers.
- Mitigate the “brand loyalty” and “status quo bias” effects that provides an advantage to the incumbent EDC.
- Eliminate ratepayer cross subsidization in the provision of default service.
- Eliminate the problems associated with the current automatic cost recovery reconciliation process.
- Facilitating the movement to a true “end-state” where default service becomes a back-stop /provider of last resort service available from EGSs when needed.

During the *En Banc* Hearing, interested stakeholders were asked to provide additional information analyzing how the various models would comply with the legal requirements of the Choice Act which sets forth the statutory requirements that a default service provider must meet.<sup>3</sup> As explained further below, implementation of either Model A or B can satisfy all of the statutory requirements without the need for further legislative amendments.

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<sup>3</sup> See 66 Pa. C.S. § 2807(e).

## **A. The Choice Act Requires That The Competitive Market Be The “First Stop” Generation Service**

The Choice Act mandates that customers have direct access to a competitive retail generation market.<sup>4</sup> This is based on the legislative finding that “competitive market forces are more effective than economic regulation in controlling the costs of generating electricity.”<sup>5</sup> Thus, a fundamental policy underlying the Choice Act is that competition is more effective than economic regulation in controlling the costs of generating electricity.<sup>6</sup>

Today in Pennsylvania, the generation supply offered by the EDC through its default service plan is a “first stop” product. All new and moving customers are automatically placed on default service. Customers who do nothing remain on default service. Customers who lose their EGS service for whatever reason are automatically returned to default service. While efforts have been made to educate and encourage consumers to shop, the reality is that many do not for a number of reasons including: (1) lack of knowledge about retail choice; (2) concerns about reliability of service; (3) concerns about financially harming their EDC; and, (4) the misperception that switching suppliers will be difficult.<sup>7</sup> As the Commission has recognized, the time is now to restructure the market to bring the full benefit of retail competition to Pennsylvania consumers. By removing the EDC from the default service role and ultimately from the provision of any generation service, more customers will experience the benefits of shopping choices. By making the default service product a market based and market priced product, EGSs will have the regulatory certainty of a truly sustainable retail market design. This

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<sup>4</sup> 66 Pa. C.S. § 2802(3).

<sup>5</sup> 66 Pa. C.S. § 2802(5). See *Green Mountain Energy Company, et al. v. Pa. PUC*, 812 A.2d 740, 742 (Pa. Commw. 2002)..

<sup>6</sup> 66 Pa. C.S. § 2802(5).

<sup>7</sup> See <http://www.puc.state.pa.us/electric/PDF/RetailMI/EnBanc111011-P-CE-CK.pdf> and <http://www.puc.state.pa.us/electric/PDF/RetailMI/EnBanc111011-P-CE-TG.pdf>

will ensure that EGSs will offer attractive competitive alternatives to default service which will result in customers receiving the “least cost” electricity service for the specific electricity product of their choosing that accounts for each customer’s unique needs and preferences.

All three transitional models contemplate EGSs providing a “default service” product with the EDC providing a “Provider of Last Resort (Backstop Service)” product. This is consistent with RESA’s preferred model for Pennsylvania’s transition to the end-state.<sup>8</sup> Ultimately, however, RESA recommends that the final “End-State” should be one wherein EGSs are exclusively providing “default service” and “provider of last resort” generation services. As discussed below, statutory authority currently exists to permit the EGS to provide both default and provider of last resort service.

### **1. The Choice Act Permits EGSs to Provide Default Service**

The Choice Act clearly contemplates the possibility of one or more EGS(s) providing default service. Prior to the legislative amendments implemented by Act 129, default service was defined as requiring an EDC “or commission-approved alternative supplier [to] acquire electric energy at prevailing market prices to serve the customer.”<sup>9</sup> When the Commission adopted default service regulations to implement the Choice Act, it recognized that default service could be provided by an entity other than the EDC.<sup>10</sup> The Commission also defended its decision to designate each EDC as the initial default service provider in its respective service

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<sup>8</sup> See RESA Preferred End-State Default Market Mode for Pennsylvania dated January 24, 2012 available at [http://www.puc.state.pa.us/electric/PDF/RetailMI/DD-End\\_State\\_DSM-RESA\\_012412.pdf](http://www.puc.state.pa.us/electric/PDF/RetailMI/DD-End_State_DSM-RESA_012412.pdf).

<sup>9</sup> 66 Pa.C.S. § 2807(3) deleted by 2008, Oct 15, P.L. No. 129 (“Act 129”) effective November 14, 2008.

<sup>10</sup> 52 Pa. Code § 54.183. While these regulations include “an evaluation of the incumbent EDC’s operational and financial fitness to serve retail customers, and its ability provide default service under reasonable rates and conditions,” the regulations do not require that the Commission must find that the EDC is incapable of serving the default service role to assign an alternative default service provider.

territory but also stated that identifying a process by which the default service provider could be changed is “in the public interest” and consistent with the intent of the General Assembly.<sup>11</sup>

Section 2807(e)(3.1) was added by Act 129 and replaced the previously used phrase of “EDC or commission-approved alternative supplier” with the more generic term “default service provider” in describing the default service function.<sup>12</sup> No language from the Act 129 amendments specifically requires that the default service provider be the EDC. On the contrary, the Act 129 amendments make clear that the General Assembly intended that the default service provider role could be provided by non-EDC entities. This is evidenced by the fact that the Choice Act makes clear when it is referring to “default service provider” requirements or EDC-only requirements. For example, the Act 129 amendments added the following definition for “default service provider:”

"Default service provider." --An electric distribution company within its certified service territory or an alternative supplier approved by the commission that provides generation service to retail electric customers who:

- (1) contract for electric power, including energy and capacity, and the chosen electric generation supplier does not supply the service; or
- (2) do not choose an alternative electric generation supplier.<sup>13</sup>

Furthermore, the Act 129 amendments make clear that the General Assembly did not intend to express a preference for the EDC as the default service provider nor did it merely provide for an alternative default service provider as a theoretical concept. This is evidenced by the fact that the legislature specifically assigns certain other functions to the EDC. For example,

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<sup>11</sup> *Rulemaking Re Electric Distribution Companies' Obligation to Serve Retail Customers at the Conclusion of the Transition Period Pursuant to 66 Pa.C.S. § 2807(e)(2)*, Docket No. L-00040169, Final Rulemaking Order entered May 10, 2007 at 12.

<sup>12</sup> 66 Pa.C.S. § 2807(e)(3.1).

<sup>13</sup> 66 Pa.C.S. § 2803.

the energy efficiency and smart meter requirements of Act 129 are requirements that the EDC must ensure are fulfilled. Section 2807(f) requires EDCs to file smart meter technology procurement and installation plans with the Commission. .

The definition of “default service provider” and other references in the law, on the other hand, are clear that an entity other than the EDC can fulfill the default service role. By clearly limiting certain functions to the EDC in one instance yet clearly specifying that the role of default service could be provided by another entity in another instance, the General Assembly clearly expressed its intent that the Commission was authorized to approve alternative default service providers without any need for further legislation. It also shows that if the General Assembly had intended to limit the default service role to the EDC or wanted to express a preference for this role to remain with the EDC, it would have clearly stated such intent in the statutory language. Thus, all of Staff’s proposals to utilize EGSs to provide default service are consistent with the statutory requirements for default service.

## **2. The Choice Act Defines Default Service To Include Provider Of Last Resort Functions**

All three of Staff’s proposed default service models rely on the EDC to provide “Provider of Last Resort (Backstop Service).” The statutory requirements do not specifically separate these two concepts. Rather, it defines the role of the “default service provider” to make available generation service to: (1) a customer who contracts for generation service and the chosen supplier does not provide the service; and, (2) a customer who does not choose an alternative electric generation supplier.<sup>14</sup> Scenario number one addresses true “provider of last resort” or “backstop” service. In this scenario, a customer has chosen an alternative supplier but the supplier does not or cannot provide the service likely due to financial default or other reasons. In

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<sup>14</sup> 66 Pa. C.S. § 2807(e)(3.1).

this case, there needs to be a “backstop” service available so that the customer is not without electricity for the short period of time necessary to make other arrangements. While RESA would not oppose having the EDCs provide this type of service on a transitional basis as recommended in the Staff proposal, ultimately this service should be transitioned to EGSs in the final end-state as it is economically inefficient for the EDC to remain in this role. The EDC will continue to be required to support and maintain all of their customer service and billing systems in the event they are ever called upon to provide provider of last resort service. To require the EDCs to maintain these costly systems in order to respond to sporadic events is not economically prudent and places a huge burden on ratepayers to continue supporting systems that may be used only occasionally and will require continual and costly updates and modifications that will ultimately be recovered from ratepayers..

In scenario number two, the customer has not chosen an alternative EGS. Under the current market model, these customers remain with the EDC as the default service provider. All of Staff’s proposed models recommend selecting EGSs to perform this function for both “non-shopping customers” and “returning customers.” RESA supports this approach but notes that “new customers” – who do not otherwise select an EGS – should (like returning customers) be required to take default service from the EGS default service provider. Currently, to receive electricity service, customers are required to contact the EDC to establish service and nothing in the statute requires customers who do nothing to automatically receive electricity service. Likewise, when EGSs assume the default service role, customers should be required to contact the default service EGS to get service or choose an alternative EGS consistent with the practice in place today. During the initial transition period when service is first moved from an EDC to an EGS, the Commission may consider allowing all default service customers a “one-time pass”

on being required to take any action in which case they would be transitioned to EGS provided default service through the mechanism approved by the Commission. Subsequently, however, new and moving customers would be required, as they are today, to contact the default service provider or alternative EGS to establish generation service.

Designating an EGS to fulfill any or all of these functions is consistent with the statutory requirements. As explained in the previous section, the law clearly contemplates that default service – which encompasses the concept of provider of last resort – may be the EDC or an alternative supplier approved by the Commission. Nothing in the law requires that default service or backstop service be limited to the EDC. In other words, the General Assembly could have included language stating that only EDCs could provide default service to “a customer who contracts for generation service and the chosen supplier does not provide the service” or that only EDCs could provide default service to customers who do not choose an alternative supplier. As explained above, the law is clear by its text when certain obligations are placed on the EDC rather than on the default service provider. Since the General Assembly did not choose to make such distinction in establishing responsibility for all the default service functions, there is nothing that statutorily prohibits the Commission from relying on an EGS to provide all default service functions including provider of last resort functions.

Moreover, allocating the default service role and the provider of last resort role between an EDC and an alternative default service provider when an EDC is relieved of its default service provider obligation is within the Commission’s discretion. In this scenario, the alternative default service provider would be responsible for electric supply service to retail customers who: (i) do not affirmatively select a supplier; (ii) are unable to obtain service from an alternative supplier; or, (iii) have contracted with an alternative supplier who fails to perform. And, in

comparison, the provider of last resort would: (a) act as a back-up in case the alternative default service provider goes out of business; and, (b) be obligated to provide electricity service to any customer who loses service from an alternative default service provider. Having the EDC function as the provider of last resort may be reasonable and appropriate during the transition period.

Even under the current model where the EDC is providing default service, there is – in essence – both a “default service” and a “backstop service.” Under the currently approved EDC default service plans, the EDCs are required to include a contingency plan in the event that one or more of the selected wholesale default service suppliers is unable to provide generation service for which it has contracted.<sup>15</sup> Accordingly, a mode where “backstop” service is distinguished from “default service” already exists and has been found legally valid by the Commission.

Under a future transitional model where EGSs provide default service, this requirement for contingency planning would still exist. During this transition, it is reasonable and appropriate to have a contingency plan for the failure of the alternative default service provider itself. Even with heightened technical and fitness standards for EGSs acting as the alternative default service provider, there is still a (small) risk of failure. To manage this risk, a provider of last resort should exist. Given that the EDC presently provides all of the default service obligations, the Commission could properly determine that the EDC could remain as the provider of last resort during the transition period and concurrent with the Commission assigning other default service responsibilities to an EGS. Such contingency planning would ensure the reliable provision of

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<sup>15</sup> 52 Pa. Code § 54.187(k).

service in the (unlikely) event of the failure of an alternative default service provider. In the end-state, the EGS community can provide both default service and provider of last resort service.

In the future retail market design end-state structure, distinguishing between the concept of “default service” and the concept of “provider of last resort service” is useful. As explained above, these services are not inexorably intertwined but all can be provided by an EGS consistent with the legal requirements.

## **B. Requirements of Default Service Procurement Plan**

The law does not require a specific rate design methodology for default service. Instead, it requires that the default service provider offer electric generation supply service “pursuant to a commission-approved competitive [default service] procurement plan” that must include a “prudent mix”<sup>16</sup> of resources designed: (i) to provide adequate and reliable service; (ii) to provide the least cost to customers over time; and, (iii) to achieve these results through competitive processes which shall include one or more of the following: auctions, requests for proposals and/or bilateral agreements.<sup>17</sup> Staff’s proposed Models A and B either are or can be easily structured to fulfill all of these statutory requirements.

### **1. Commission-Approved Default Service Procurement Plan**

#### **a) Competitive Default Service Procurement**

Section 2807(e)(3.1) requires a default service provider to provide electric generation supply service “pursuant to a commission-approved [default service] competitive procurement plan” that includes one or more of the following: (i) auctions, (ii) requests for proposal, or (iii) bilateral agreements.<sup>18</sup> Section 2807(e)(3.6) requires the default service provider to file its

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<sup>16</sup> 66 Pa. C.S. § 2807(e)(3.2).

<sup>17</sup> 66 Pa. C.S. §§ 2807(e)(3.1).

<sup>18</sup> 66 Pa.C.S. § 2807(e)(3.1) and (3.4)(iii).

default service procurement plan with the Commission for approval and Section 2807(e)(3.7) sets forth the findings the Commission is required to make in evaluating the default service procurement plan.<sup>19</sup> These statutory requirements can be fulfilled through an EGS provided default service model.

Consistent with the Commission’s regulations, a competitive process would be established by the Commission to select the EGS(s) that would provide default service and a methodology for transitioning current default service customers to the newly designated EGS default service providers.<sup>20</sup> This process is likely to involve a Request for Proposals, auctions or some other competitive selection process where the Commission would ultimately approve the winner(s). By using a competitive process to select the EGS default service provider, EGSs will be competing against each other to be selected and, therefore, their proposals comply with whatever pricing methodology the Commission determines is consistent with the statute. In addition to designing and ultimately approving the competitive process that will be used to select the EGS default service provider, the Commission will be designing and approving the pricing methodology that the EGS plans must be designed to achieve. For example, under Model A, the Commission would define the product on the basis of real-time/hourly PJM locational marginal price (“LMP”).<sup>21</sup> Any administrative adder could be set as a result of the bids from interested EGS default service providers, or portions of the adder could be administratively determined by the Commission, or a combination approach could be used. Then there would be a competitive process to select the EGS default service provider(s) which the Commission would ultimately

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<sup>19</sup> 66 Pa.C.S. § 3807(e)(3.6) and (3.7).

<sup>20</sup> 52 Pa Code § 54.183(c).

<sup>21</sup> PJM Interconnection is a FERC-approved regional transmission organization (“RTO”) that manages the high-voltage electric grid and the wholesale electricity market in all or parts of thirteen states and the District of Columbia, including most of Pennsylvania. Hourly prices in PJM LMP are not determined until after the applicable hour has elapsed, thus customers do not know the exact prices they will be charged until after-the-fact.

need to approve. This process as overseen and implemented by the Commission would fulfill the statutory requirement for a Commission-approved competitive procurement plan.

This proposed process is consistent with that in place today whereby EDCs submit their default service procurement plans to the Commission for approval. The Commission reviews the plans and determines whether or not they are reasonably calculated to meet the requirements of the Choice Act. In fact, the proposed new process would represent an improvement over the current process in ensuring that the default service prices that result from the process are competitive and free of ratepayer cross-subsidization. This is because the default service plans submitted by the EDCs do not compete against any other proposed default service procurement plan. Thus, EDCs have no incentive to ensure that their proposed default service procurement plan is designed in the most competitive manner. Thus, EGS provided default service not only fulfills the competitive procurement requirements of the Choice Act but, arguably, does so better than the current market model.

**b) Ensuring Adequate and Reliable Service and the Least Cost To Customers Over Time**

In addition to the competitive procurement requirements for default service procurement plans, the Choice Act requires that the default service procurement plan be designed to ensure adequate and reliable service and the least cost to customers over time.<sup>22</sup> This statutory requirement is satisfied in Models A and B because the Commission retains ultimate authority to approve the default service plan that will be offered by the EGS(s). Moreover, as explained above, the use of a competitive process to select the supplier who will provide default service is an effective tool to ensuring that the resulting product will best achieve the goals required by the statute.

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<sup>22</sup> 66 Pa.C.S. § 2807(e)(3.3).

Model A ensures that customers will receive adequate and reliable service by ensuring that the EDCs are in a position to focus all of their attention and resources on maintaining reliability of their systems. This is the case in all of the models being proposed by the Commission.

As explained above, the new process would result in default service prices derived from a competitive process which will produce the least cost over time for default service customers. In addition, this model will also produce an outcome that is more consistent with the “least cost over time” standard than what exists under the current paradigm. This is because such a default service model will produce a more sustainable competitive retail market which will deliver a wide range of products and pricing options that best suit individual customer needs and preferences. In this regard, a default service model that produces robust competition will ensure that all customers, not only default service customers, receive electric generation service at the “least cost over time” for the particular product or pricing plan that each customer desires.

## **2. Prudent Mix Of Contracts**

Section 2807(e)(3.2) requires that the electric power procured for default service include a “prudent mix” of: (i) spot market purchases; (ii) short-term contracts; and, (iii) long-term purchase contracts.<sup>23</sup> Models A and B establish a pricing methodology – or formula – and EGSs will be required to offer prices that comply with these formulas. EGSs will procure supply to achieve the pricing to which they commit and that, by the Commission’s own defined pricing methodology, satisfies the requirements of Section 2807(e)(3.2). Moreover, suppliers will be at risk for 100% of their procurement strategies, so if their defined “prudent mix” results in prices

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<sup>23</sup> 66 Pa.C.S. § 2807(e)(3.2).

that are higher than the default service price they are obligated to provide, they are at risk for 100% of the price difference.

Notably, the Choice Act does not require that each of the three types of contracts be included in the default service procurement plan. Consistent with this, the Commission has determined that what constitutes a “prudent mix” should be “interpreted in a flexible fashion” to permit default service providers “to design their own combination of products” to meet the requirements of the statute.<sup>24</sup> Thus, the Commission has declined to establish specific percentages of default service load that should be served under various types of products<sup>25</sup> and, in fact, has adopted default service procurement plans with a varying degree of contract types, some of which consist solely of spot market purchases. For example, the FirstEnergy EDCs’ large industrial and commercial customers rely on default service which is priced on an hourly spot market basis as are many other default service plans for this customer class.<sup>26</sup> The Commission has also approved a spot market only approach for default service for all customers in the Pike County Light & Power Company (“PCL&P”) service territory. The Commission first adopted this model in 2007 after a litigated proceeding.<sup>27</sup> The plan was approved for a second time for the period of June 1, 2009 through May 31, 2011 with the Commission finding that:

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<sup>24</sup> *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 at 60.

<sup>25</sup> *Id.* at 66.

<sup>26</sup> *See, e.g., Petitions of Metropolitan Edison Company and Pennsylvania Electric Company for approval of their default service programs*, Docket No. P-2009-2093053 and P-2009-2093054 (Order entered November 6, 2009)(The Companies will offer industrial class customers an Hourly Pricing Service (“HPS”) priced to the PJM real-time hourly market); *Petition of Pennsylvania Power Company for approval of its default service programs*, Docket No. P-2010-2157862 (Order adopted October 21, 2010)(same); *Petition of the West Penn Power Company d/b/a Allegheny Power for Approval of its Retail Electric Default Service Program and Competitive Procurement Plan for Service at the Conclusion of the Restructuring Transition Period*, Docket No. P-00072342(Order entered July 28, 2008) (ST 40 customers will be charged based upon hourly locational marginal price (LMP)).

<sup>27</sup> *Petition of Pike County Light & Power Company for Expedited Approval of its Default Service Implementation Plan* Docket No. P-00072245 Opinion and Order entered August 16, 2007 .

[C]ustomers can obtain competitive supply pursuant to the spot market, which represents the appropriate least cost portfolio for the few remaining customers currently taking default service. . . Temporary spot purchase, in this instance, are the optimal and prudent solution from a least cost over time perspective.<sup>28</sup>

The Commission approved continuation of the spot market approach for a third time, consistent with the agreement of the parties, for another one-year term from June 1, 2011 through May 31, 2012.<sup>29</sup>

The intent of the various proposed models is to design a market that seeks to reduce reliance on default service and increase customer participation in the competitive market. In such a market where the majority of customers and load are served by EGSs, the only "prudent" or "wise or judicious" mix of supply for those few customers who likely will remain on default service would be one that achieves market reflective pricing on a real-time basis and avoids the unnecessary incurrence of stranded costs. It would be unwise, frivolous and very expensive to procure what would effectively be long-term default service options at a fixed price for such a small number of customers.

However, even if the statute were to be strictly interpreted to require all three types of contracts in the default service procurement plan (which it should not be), the default service procurement strategies utilized by most EGSs will likely to comply. Most EGSs will have a mix of shorter term, longer term and spot market contracts in their default service procurement portfolios. Furthermore, the concepts of "short term" and "long term" need not be restricted to the term of the fixed price under the contract. The law does not specify that the default service pricing term has to be fixed for a particular period and there are a number of ways that a new

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<sup>28</sup> *Re: Petition of Pike County Light and Power Company for Expedited Approval Of Its Default Service Implementation Plan*, Docket No. P-2008-2044561 on and Order entered March 23, 2009 at 14-15.

<sup>29</sup> *Petition of Pike County Light & Power Company for Approval of its Default Service Implementation Plan*, Docket No. P-2010-2194652, Order entered February 25, 2011

default service model relying on EGSs can be designed to ensure compliance with the prudent mix requirements of the statute.

### **3. Cost Recovery**

Section 2807(e)(3.9) gives the default service provider the “right to recover on a full and current basis, pursuant to a reconcilable automatic adjustment clause. . . all reasonable costs incurred under . . . a commission-approved competitive [default service] procurement plan.”<sup>30</sup> Models A and B do not permit the default service provider to “reconcile” costs but they do not prohibit cost recovery. RESA submits that reliance on reconciliation mechanisms to recover costs is an imperfect way to permit cost recovery in a competitive market. In the new market design which relies on EGSs to provide default service, EGSs will be competing against one another for the ability to provide default service and, therefore, can and should embed all their costs of providing this service in the pricing structure that will be used to establish the default service price.

### **4. Quarterly Default Service Rate**

Section 2807(e)(7) requires the default service provider to offer residential and small business customers a generation supply service rate that changes no more frequently than on a quarterly basis.<sup>31</sup> Model A suggests a monthly price change and Model B recommends a quarterly or semi-annual price change. The “frequency” of the price change from the perspective of the customer can be quarterly even if the pricing is based on the methodology described in Model A – as is currently done in the PCL&P service territory. Also the statutory language does not specifically require that the default service product be a quarterly priced product. Rather, it states only that the “default service provider shall offer” such a quarterly fixed priced product.

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<sup>30</sup> 66 Pa.C.S. § 2807(e)(3.9).

<sup>31</sup> 66 Pa.C.S. § 2807(e)(7).

Thus, another way to satisfy this statutory requirement could be to require the chosen default service provider to offer a quarterly fixed price product to all default service customers as a condition of providing default service. The default service product could be structured to change pricing consistent with Model A and the default service provider would make available a second product that offers a price that remains fixed on a quarterly basis. Either of these approaches are consistent with the statute.

## **5. Assessments on EGSs Providing Default Service**

Currently, EGSs may not levy an “assessment” on EGSs pursuant to 66 Pa. C.S. § 510.<sup>32</sup> To the extent the Commission seeks to require EGSs to pay the assessment contained in Section 510, legislative changes would be necessary. However, the Commission appears to have already concluded that it could impose upon the EGS default service provider (or bidders) the regulatory costs incurred in selecting a default service provider as a condition of becoming an alternative default service provider.<sup>33</sup>

### **C. The Commission Should Be Cautious About Proceeding With Model C**

Under Model C, default service would be provided to non-shopping and returning customers on the basis of a Commission-approved default service procurement plan. Prices would change quarterly or semi-annually, reconcilable on a twelve-month rolling basis.

RESA cautions against Model C because the alternative default service provider must file detailed default service procurement plans similar to what is done today with the Commission. Experience has shown that these plans can be the subject of extensive litigation. As such, litigation can be expected to either remain the same as currently or increase under Model C.

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<sup>32</sup> See *Delmarva Power & Light Co. v. Commonwealth*, 870 A.2d 901, 911 (Pa. 2005)

<sup>33</sup> *Rulemaking Re Electric Distribution Companies’ Obligation to Serve Retail Customers at the Conclusion of the Transition Period Pursuant to 66 Pa.C.S. § 2807(e)(2)*, Docket No. L-00040169, Final Rulemaking Order entered May 10, 2007 at 12

Rather than continue the litigated process, RESA believes the Commission can have broad oversight of a regulatory process to define the pricing structure for the alternative default service provider and the selection process. This pricing methodology does not need to require: (a) strict adherence to a particular hedging strategy; or, (b) the filing of detailed information about hedging practices since the EGS bears the risk of nonperformance. Consistent with the Choice Act, the Commission would maintain regulatory oversight of the default service providers to ensure compliance with the law while, at the same time, lessening regulatory burdens on all stakeholders and the Commission itself which will result in consumers receiving the benefit of a better default service product.

### **III. CONSUMER EDUCATION INITIATIVES**

On March 13, 2012, Staff issued a proposal for a statewide consumer education campaign which set forth three options for consideration. The proposals include ideas related to messaging, media outlets, and funding. RESA fully supports consumer education as a critical piece of effectively transitioning to the end-state retail electricity market. Today, despite all of the consumer education undertaken to date, the number of consumers who still do not even know that they have ability to choose a competitive supplier is unacceptably high (between 8 and 15%) and, for those who may have heard about it, they have not switched for reasons that are factually incorrect or based on inadequate information. For these reasons, appropriately structured and targeted statewide consumer education is critical to ensuring the successful completion of all the efforts being undertaken in this proceeding.

#### **A. Messaging**

Staff's consumer education proposal states that the primary message of the campaign would be to promote electric shopping and drive customers to PAPowerSwitch.com. The secondary messages would be to educate consumers about changes made during this

investigation. Developing the key messaging and ensuring that all interested stakeholders are working together to create effective and reasonable marketing aimed at delivering that messaging is critical. RESA recommends that the following key messages be conveyed in any statewide consumer education effort.

**1. Pennsylvania Has A Well-Functioning Competitive Market And Shopping Is Encouraged**

Consumers need to understand that it really is OK to shop. Consumer education messaging should make clear that:

- There are strong consumer protections in place with oversight by the Commission, state legislature, utilities, and federal regulators (FERC) and the same consumer protections in place today will remain in place, even if the consumer switches to a competitive supplier.
- System reliability will be maintained for shopping customers. Customers will still call their EDC if they have an outage or other service emergency and the EDC is still responsible and will respond as quickly as possible, regardless of whether the customer has shopped.
- Consumers can enroll with a competitive supplier via a phone call, online, or in-person by providing their EDC account number. The supplier will then notify the EDC of the request to switch suppliers
- Consumers will continue to receive one bill from the EDC, who will include the suppliers' charges on the bill. Consumers will pay the EDC for monthly usage, just as they do today.

In addition to educating consumers that it is OK to shop, consumer education messaging should also provide suggestions on how to choose a plan that satisfies the consumer's needs.

One suggestion is for consumers to "Remember the 3 P's":

- Product – renewable, fossil fuel, or mix?
- Plan term and conditions – month to month, 12 month term, any early cancellation fees, any monthly service charges?
- Price fixed product, variable, introductory, guaranteed savings?

Finally, any structural changes to the market or implementation of programs intended to encourage shopping should be accompanied with focused, statewide consumer education to explain the changes and help consumers understand their intent and purpose.

## **2. Benefits Of Pennsylvania's Competitive Market**

In addition to ensuring that consumers receive accurate and correct information about the impact and process for shopping, consumers should be educated about how they can benefit from the competitive market. Some key issues that should be included:

- Better value for your energy dollar
- Choice of suppliers (approximately 30 residential suppliers active in Pennsylvania; approximately 50 business customer suppliers active in Pennsylvania)
- Innovative products and services (time of use rates, senior/veterans discounts, fixed rate offerings for those that are budget conscious; variable rates if you would like to float with the market)
- Energy efficiency and conservation
- Environment – more wind and solar available than in non-restructured energy markets
- Economic Development – competitive suppliers provide jobs and significant investments into the Commonwealth

Further, as competitive energy markets evolve, a variety store of innovative products will develop and flourish. Some examples include:

- Reward options that can be turned into free flights, hotel stays, money for college or retail bonuses.
- HVAC repair, replacement and tune-up services.
- Home energy checkups.
- Solar Leasing programs for homes as well as buy-back programs for selling electricity back to the grid.

- Rate plans, programs, apps and gadgets that empower customers to take more control over managing their energy usage resulting in conservation, efficiency and savings.
- Recharging packages for electric vehicles.
- Carbon offset programs.
- Renewable energy products that help green the regional power grid.

Therefore, consumer education should not be limited to focusing only on potential price savings as there are benefits that go beyond electricity price and savings. Thus, an important component of any statewide consumer education campaign must be to give Pennsylvanians the knowledge and tools necessary to shop for value-added competitive energy services that fit their budget, lifestyle and beliefs.

## **B. Potential Funding Mechanisms**

Comprehensive consumer education regarding electric choice has existed since the passage of the Choice Act. Initially, in 1998, a statewide education program was created to educate consumers about choice which was funded through the Competitive Transition Charge assessed on all consumers as a distribution charge. This consumer education campaign ended around 2004.

In 2007, the Commission was concerned about ensuring that consumers were informed about the pending expiration of rate caps including the anticipated electric rate increases.<sup>34</sup> To address this, the Commission directed each EDC to file a consumer education plan with the Commission for review and approval by December 31, 2007. The Commission identified specific Energy Education Standards and directed each EDC to explain how it would meet these standards. Each EDC's consumer education plan is funded through a non-bypassable surcharge

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<sup>34</sup> *Policies to Mitigate Potential Electricity Price Increases*, Docket No. M-00061957, Final Order entered February 13, 2007.

assessed on all distribution customers.<sup>35</sup> These EDC consumer education campaigns are still in place today. In addition to the EDC-specific consumer education campaigns, the Commission initiated a statewide consumer education campaign to complement and reinforce the EDC education programs that was to be funded by allocating \$5 million from the assessments paid by the EDCs to the Commission.<sup>36</sup> That funding was targeted to cover the 2008-2009 and 2009-2010 time periods.

The March 13, 2012 Staff proposal now suggests implementation of a new statewide consumer education campaign and that funding come from either: (1) requested contributions from the EGSs; or, (2) through revenue collected by the EDCs from their purchase of EGS receivables through POR. While RESA supports a Staff-led statewide consumer education effort for the reasons set forth above, funding for this initiative needs to be carefully considered and reasonably allocated. The issue here is not one simply of making “the EDC” or “the EGS” fund consumer education. As the prior funding mechanisms utilized by the Commission recognized, all ratepayers benefit from consumer education and, therefore, allocating the costs of such education among all ratepayers is reasonable. Even if a funding mechanism is adopted whereby the EGS ostensibly contributes financially, this cost is likely to be passed on to the EGS customer who: (1) has already shopped for an EGS; and, (2) is already bearing the cost of his or her EDC consumer education campaign through the consumer education surcharge assessed on all distribution customers. Of course since EGSs operate in competitive markets and have no captive customers, they have no way of assuring that they will be able to recover such costs. Moreover, since the purpose of a statewide consumer education campaign is to educate those customers who have not shopped about shopping, requiring shopping customers to bear an

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<sup>35</sup> *Id.* at 6-9.

<sup>36</sup> *Id.* at 9-12.

unreasonable portion of the costs when they are no longer benefiting from the statewide education campaign (because they have shopped) is not reasonable.

Another issue to keep in mind is that EGSs themselves also engage in marketing and consumer education. Thus, a statewide consumer education campaign does not and should not be viewed as a marketing tool for any particular EGS. In fact, since the messaging of such an initiative would be coordinated among a wide variety of stakeholders with varying interests, the ultimate messaging is unlikely to be what any specific EGS would utilize for its own marketing purposes. RESA recommends that these considerations be taken into account as the Commission considers this very important issue. Regarding potential funding mechanisms, RESA offers the following comments.

**1. The Preferred Approach: A Distribution Charge Assessed On All Customers**

As explained above, all consumer education funding to date has been a shared allocation among all ratepayers – whether through a surcharge assessed by the EDC on all customers or in the form of the assessments paid by the EDC to the Commission as required by 66 Pa. C.S. § 510. RESA prefers continuation of this approach for a number of reasons. First, all customers benefit from a vibrant and workably competitive retail market which creates a downward pressure on generation prices and leads to environmental benefits, energy efficiency, innovation, and economic development benefits. Therefore, allocating the cost of this benefit among all ratepayers is reasonable.

Second, the amount of the surcharge could be relatively minimal for each ratepayer. According to PAPowerSwitch, as of December 31, 2010, there were 4,970,057 residential

customers in Pennsylvania<sup>37</sup>. Assessing a dollar on each of these customers would result in almost \$5 million dollars available for a statewide consumer education campaign. If the costs were also allocated to the small business customers, even more funding would become available. Other states including the Commonwealth have used this approach and per customer assessments have ranged from 50 cents to over two dollars per customer.

Finally, this approach is administratively easy to implement. A new surcharge could either be created in the pending default service/competitive enhancement proceedings involving each of the major utilities or each EDC's current consumer education surcharge could be increased by a specific amount to be allocated to funding this statewide initiative.

## **2. Other Potential Alternatives: Fair Share Of Costs Allocated To EDCs And EGSs Or Equal Allocation Of All Costs To EGSs**

If the Commission is not inclined to permit a distribution charge assessed on all customers to fund a statewide consumer education campaign (which is RESA's preferred option), then other alternatives should be considered. For example, the Commission could implement a "Fair Share" approach which allocates the cost of a statewide consumer education campaign between EDCs and EGSs based on the current level of statewide migration. Based on the current migration statistics, approximately 28% of all residential customers are receiving service from an EGS.<sup>38</sup> Thus, all of the EGSs licensed to serve residential customers in Pennsylvania would equally share 28% of the costs of the consumer education campaign. The remaining 72% of the campaign would be paid by EDCs mostly likely through a bypassable surcharge (since consumers already shopping would be paying their share through the EGS

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<sup>37</sup> See Weekly PAPowerSwitch Update: Customers Switching to an Electric Generation Supplier as of march 28, 2012 available at: <http://extranet.papowerswitch.com/stats/PAPowerSwitch-Stats.pdf?/download/PAPowerSwitch-Stats.pdf>

<sup>38</sup> See Weekly PAPowerSwitch Update: Customers Switching to an Electric Generation Supplier as of march 28, 2012 available at: <http://extranet.papowerswitch.com/stats/PAPowerSwitch-Stats.pdf?/download/PAPowerSwitch-Stats.pdf>

contribution). While collection and enforcement of this allocation may be more administratively difficult to implement, the approach still reasonably allocates the cost of consumer education among all ratepayers and does so on a rational basis directly tied to the purpose of the consumer education campaign.

If the Commission concludes that EGSs should be responsible for 100% of the consumer education costs (which is not RESA's preferred option), then several issues would need to be addressed to ensure that the costs are fairly allocated among the EGSs. At the outset, a mechanism would need to be developed to determine the most fair and equitable manner by which to allocate this cost among EGSs. Not all EGSs serve all customer classes and licensed EGSs include brokers who do not take title to energy or who work as consultants for retail customers. Moreover, entities that may not yet be licensed as EGSs may decide to wait until after funding for the statewide consumer education campaign has been collected before receiving their license and operating in Pennsylvania. Determining how to fairly allocate the costs to EGSs in consideration of these factors is important. In addition, a statewide consumer education that is funded exclusively by EGSs should result in giving EGSs the primary role in the messaging and direction of the Commission delivered effort. Past statewide consumer education campaigns have included a number of other tangentially related issues which may not be appropriate to include in a statewide campaign funded exclusively by EGSs.

### **3. Increases To The POR Discount Rate Should Not Be Utilized To Fund Consumer Education**

Through a POR program, the EDC purchases the accounts receivable of the EGS, adds the supplier's charges to the customer's distribution bill, and sends the customer one bill with all his or her electricity charges. A properly structured POR program enables competitors to efficiently and reasonably reach customers and is a critical component to establishing robust

retail competition. Today in Pennsylvania, most EDCs offer a POR program. A component of the POR program is the amount by which the EDC purchases the EGS's accounts receivables. In a "no discount" POR program, the EDC purchases the accounts at 100% of their value. In a discount POR program, the EDC purchases the accounts at some percentage less than 100%. For EDCs who have utilized a discount POR program in Pennsylvania, some portion of the discount may be used to: (1) recover the administrative costs to develop and administer the POR; and, or (2) recover the uncollectible expense associated with the EDC's inability to collect 100% of the value of the accounts bought from the customer.

A proposal has been made to implement a higher discount rate (i.e. an EDC would pay an EGS in the POR program less than 100% of the value for the accounts purchased) and utilize the value of that discount to fund a statewide consumer education program. RESA does not support this approach for a number of reasons. First, it violates the principle of cost recovery following cost causation. The purpose of the POR discount, as explained above, is to recover an EDC's POR program implementation costs, administrative costs and/or the uncollectibles associated with the purchased accounts. A statewide consumer education campaign is totally unrelated to the costs that are intended to be recovered through the POR discount and, therefore, this is an inappropriate mechanism for funding a statewide consumer education campaign.

Second, utilizing POR would result in the unintended consequence of exempting those suppliers who do their own billing (through dual billing) and could encourage those utilizing POR to no longer do so because they are receiving less value for their purchased accounts. Either consequence would not be in the public interest.

Lastly, any purchase of receivables-based assessment would unfairly and disproportionately assess competitive suppliers based on market share. In other words, the more

customers an EGS has utilizing POR, the more significant the POR discount and the more the EGS will be contributing to the statewide consumer education campaign. Market share is gained in large part, by significant investments in the Commonwealth, expenditures on the part of the supplier to educate customers, increase their awareness of choice and product offerings, and to better manage their overall energy usage. Instead of receiving the benefit of these investments through the acquisition of a greater number of customers, these EGSs would be penalized in the form of being required to make a proportionally larger financial contribution to the statewide consumer education campaign.

For all these reasons, RESA strongly recommends that the Commission reject the concept of funding a statewide consumer education campaign through the POR discount and instead consider the more equitable approach of utilizing a distribution charge assessed to all customers.

#### **IV. CONCLUSION**

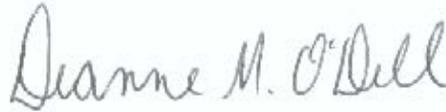
RESA believes that the changes to the default service model presented in the discussion document are just one component of an overall “end state” retail market design. While RESA can support maintaining certain services and functions with the EDC during the initial transition to an end-state model, over time, additional modifications should be considered:

- Eventually transition even the POLR service to the competitive market instead of the EDC.
- Implementation of an economically viable and operationally feasible supplier consolidated billing platform which will allow EGSs to build long lasting customer relationships through the billing and customer interfacing functions.
- Fully unbundling and removing all generation related expenses, such as billing, customer care, credit and collections, general overhead and administrative costs from distribution rates.

- Working to make all universal service funds portable so low income customers can have full access to the benefits of the competitive market.
- Legislative changes to Act 129 so energy efficiency and demand management programs can be provided through the competitive market.

RESA appreciates the Commission's efforts in this very important proceeding and looks forward to continuing to work cooperatively with all interested stakeholders in achieving the goal of moving default service customers into the competitive market.

Respectfully submitted,



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Daniel Clearfield, Esquire  
(Pa. Attorney ID No. 26183)  
Deanne O'Dell, Esquire  
(Pa. Attorney ID No. 81064)  
Carl Shultz, Esquire  
(Pa. Attorney ID 70328)  
Eckert Seamans Cherin & Mellott, LLC  
213 Market Street, 8th Fl.  
Harrisburg, PA 17108-1248  
717 237 6000

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Attorneys for the Retail Energy Supply Association