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June 1, 2010

Rosemary Chiavetta, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street, 2nd Floor
Harrisburg, PA 17120

VIA HAND DELIVERY

RE: Implementation of Act 129 of October 15, 2008; Default Service; Docket No. L-2009-2095604

Dear Secretary Chiavetta:

Please find enclosed for filing with the Pennsylvania Public Utility Commission ("PUC" or "Commission") an original and fifteen (15) copies of Citizens' Electric Company of Lewisburg, PA ("Citizens'), and Wellsboro Electric Company ("Wellsboro") (collectively, Companies") in the above-referenced proceeding.

Please date stamp the extra copy of this transmittal letter and Comments, and kindly return them to our messenger for our filing purposes.

Very truly yours,

McNEES WALLACE & NURICK LLC

By
Carl J. Zwick

Counsel to Citizens' Electric Company of
Lewisburg, PA, and Wellsboro Electric Company

CJZ/sds
Enclosures
c: Elizabeth Barnes, Assistant Counsel, Law Bureau (via E-mail)

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Implementation of Act 129 of	:	
October 15, 2008; Default Service	:	Docket No. L-2009-2095604

COMMENTS OF CITIZENS' ELECTRIC COMPANY OF LEWISBURG, PA, AND WELLSBORO ELECTRIC COMPANY

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Dated: June 1, 2010

I. INTRODUCTION

On January 19, 2010, in accordance with Act 129 of 2008 ("Act 129"), the Pennsylvania Public Utility Commission ("PUC" or "Commission") issued its Proposed Rulemaking Order to recommend changes in the Commission's regulations to reflect the default procurement provisions of Act 129. *See Implementation of Act 129 of October 15, 2008; Default Service*, Docket No. L-2009-2095604 (Order entered Jan. 19, 2010) ("Proposed Rulemaking Order"). The Proposed Rulemaking Order was published in the *Pennsylvania Bulletin* on May 1, 2010, with Comments and Reply Comments due 30 days and 45 days from publication, respectively.

Citizens' Electric Company of Lewisburg, PA ("Citizens'"), and Wellsboro Electric Company ("Wellsboro") (collectively, "Companies") submit these Comments to address their preliminary position and concerns regarding the Commission's proposed changes to its default service regulations.[1]

Citizens' and Wellsboro recognize that the PUC's implementation of the changes that Act 129 imposes on the Commission's default service regulations requires a balance of all stakeholders' interests. The Commission recently approved a default service plan for Citizens' and Wellsboro for the period from June 1, 2010, through May 31, 2013, that was filed to comply with the default service procurement provisions of Act 129. *See Joint Default Service Plan for Citizens' Electric Company of Lewisburg, PA and Wellsboro Electric Company for the Period of June 1, 2010 through May 31, 2010*, Docket Nos. P-2009-2110798 and P-2009-2110780 (Order entered Feb. 26, 2010) ("Citizens' and Wellsboro Default Service Order"). Citizens' and Wellsboro submit these Comments to ensure that the Commission understands and considers the recently-approved plan in fashioning its final regulations. In addition, the Companies respond to

[1] The Companies' failure to address a specific proposed regulation does not represent the Companies' support for, or acquiescence to, such proposal. The Companies are on addressing only primary areas of concern in these Comments.

the sixteen questions posed by the Commission in its Proposed Rulemaking Order. Because many of the proposed changes to the default service regulations mirror the statutory language of Act 129, the Companies do not object to such changes and will not address them in their Comments. Rather, the Companies' Comments focus on the specific regulations that may be inconsistent with Act 129 or the Companies recently-approved plan, as well as the sixteen questions raised by the Commission.

II. COMMENTS

A. Proposed 52 Pa. Code § 54.182 – The Definition of "Bilateral Contract" Should Include Financial Products.

Pursuant to Act 129, the Commission intends to add the term "bilateral contract" to the definitional section of its final regulations. *See* Proposed 52 Pa. Code § 54.182. Although the Companies do not object to the inclusion of this term within the PUC's regulations, the Companies are concerned that, to the extent the definition limits the use of bilateral contracts to physical products, the definition is overly restrictive. The Companies' recently-approved default service plan includes the use of cleared financial products, and provides the Companies with the opportunity to seek approval for non-cleared products that would be memorialized through a bilateral contract. *See generally* Citizens' and Wellsboro Default Service Plan. Although the definition in Act 129 recognizes in the final sentence that a "standard industry template" may include "the ISDA Master Agreement for financial energy purchases," the definition also references buying "a quantity of electric energy at a specified price for a specified period of time," which could be construed as only a physical purchase. 66 Pa. C.S. § 2803. The Commission should take the opportunity to resolve any ambiguity by specifically confirming in the final regulations that a bilateral contract may be used for physical or financial transactions.

B. Proposed 52 Pa. Code § 54.184 – A Competitive Procurement Process Should Include the Purchase of Products In Markets Operated By Applicable Regional Transmission Organizations ("RTOs").

The PUC is revising its regulations to reflect the Default Service Provider's ("DSP") obligation to serve, as set forth in Act 129. In doing so, the Commission recommends, among other things, that a DSP procure default supply through a competitive procurement process. As currently proposed, a competitive procurement process would include one or more of the following: (1) auctions; (2) requests for proposals; and/or (3) bilateral agreements. *See* Proposed 52 Pa. Code § 54.184. While Citizens' and Wellsboro do not object to this change, the Companies suggest that the final regulations recognize an additional type of competitive procurement process – purchases of products in the markets and auctions operated by the applicable RTO. When a DSP is not using a full-requirements procurement approach, the DSP needs to purchase products such as spot purchases, capacity, ancillary services, transmission, auction revenue rights ("ARRs"), and financial transmission rights ("FTRs"), in the PJM Interconnection, LLC ("PJM") markets and auctions. The final regulations should confirm that purchases in the PJM (or applicable RTO) markets and auctions are permissible.

C. Proposed 52 Pa. Code § 54.186 – The Definition of "Long-Term Contract" Should Include a Contract of At Least Four Years In Length.

In accordance with the requirements of Act 129, the Commission proposes to redefine the term "long-term contract" as a contract "of more than 4 and not more than 20 years." Proposed 52 Pa. Code § 54.186. There seems to be ambiguity in Act 129 as to whether a long-term

contract includes a contract of four years.[2] Specifically, Act 129 defines a long-term contract as a contract "*of more than four* and not more than 20 years." Under this definition, a 4-year contract would not be characterized as a long-term contract. Because the Companies believe that the General Assembly intended a 4-year contract to be a "long-term contract," the Commission should clearly define the term in its final regulations to include a contract "*of at least four years* but not longer than 20 years."

Moreover, through its Proposed Rulemaking Order, the Commission recognized, among other things, the General Assembly's mandated shift from "prevailing market price procurement" to "least cost procurement" for default service using a "prudent mix" of contracts. *See* 66 Pa. C.S. § 2807(e)(3.7); *see also* Proposed 52 Pa. Code § 54.186. To the extent that this change is consistent with Act 129, Citizens' and Wellsboro do not object.

D. Proposed 52 Pa. Code § 54.186 – The Provision Allowing a DSP To Offer a Negotiated Rate To Large Customers May Be Better Situated in Proposed 52 Pa. Code § 54.187.

The Companies note that in Proposed Section 54.186(b)(1)(iii)(A), the Commission intends to include a provision that would allow a DSP, in its sole discretion, to offer a negotiated rate for service to a customer with a peak demand of 15 MW or greater at one meter location within the DSP's service territory. Although this provision is required by House Bill 1530 of 2007 ("H.B. 1530"), the provision may be better situated in Proposed Section 54.187, which sets forth the rate design for default service products. Because Proposed Section 54.187 addresses issues of rate design and cost recovery, while Proposed Section 54.186 deals with default service

[2] In addition, there seems to be inconsistency between the Commission's Proposed Rulemaking Order and Proposed Policy Statement regarding this issue. *See Proposed Policy Statement Regarding Default Service and Retail Electric Markets*, Docket No. M-2009-2140580 (Order entered Jan. 19, 2010) ("Proposed Policy Statement"). For example, in the PUC's Proposed Rulemaking Order, the Commission defines a long-term contract as a contract "of more than 4 and not more than 20 years." Proposed 52 Pa. Code § 54.186. Under this definition, a 4-year contract is not a long-term contract. On the other hand, in Proposed Section 69.1805, a long-term contract is defined as a "contract neither less than 4 years nor greater than 20 years in length." This definition indicates that a 4-year contract is a long-term contract.

procurement and implementation, the provision may more appropriately relate to Proposed Section 54.187.

E. Directed Questions Regarding the Interpretation of Act 129's Procurement Requirements

To further resolve certain ambiguities that exist with regard to the statutory interpretation of Act 129's procurement requirements, the Companies submit the following responses to the sixteen questions that the Commission included within its Proposed Rulemaking Order. Citizens' and Wellsboro limit their responses to issues that are relevant to the Companies.

(1) What is meant by "least cost to customers over time?"

The phrase "least cost to customers over time" must reflect a balance of rate levels and rate stability over an appropriate period of time to determine whether a given procurement approach is effective in relation to other approaches. For example, relying solely on spot market purchases may result in the least cost, but it may also result in an unacceptable level of retail rate volatility for default service customers. Conversely, relying on multiple-year full requirements contracts may result in rate stability, but not in the least cost for customers. In addition, the Commission must recognize that a forward-purchasing procurement approach can have different results depending on whether the market is rising (i.e., prices are increasing) or falling (i.e., prices are decreasing). As a result, the effectiveness of a given procurement approach should not be analyzed on a year-by-year basis; rather, such an analysis should encompass multiple years.

(2) What time frame should the Commission use when evaluating whether a DSP's procurement plan produces least cost to customers over time?

To ensure that the Commission fully considers the effectiveness of a given procurement plan, the Commission should evaluate a plan over no less than a 5-year period.

(3) In order to comply with the requirement that the Commission ensure that default service is adequate and reliable, should the Commission's default service regulations incorporate provisions to ensure the construction of needed generation capacity in Pennsylvania?

No position.

(4) If the Commission should adopt a provision to ensure the construction of needed generation capacity, how should the default service regulations be revised?

No position.

(5) Which approach to supply procurement – a managed portfolio approach or a full requirements approach – is more likely to produce the least cost to customers over time?

A managed portfolio approach is more likely to produce the least cost to customers over time, especially for DSPs serving a small territory. In fact, because the potential exists with a full requirements approach for wholesale suppliers to pre-buy large blocks of power prior to the auction date and then inflate bids based on their market position, such an approach may be ineffective, even for larger DSPs. This practice is commonly referred to as "front loading."

(6) What is a "prudent mix" of spot, long-term, and short-term contracts?

A "prudent mix" of spot, long-term, and short-term contracts requires a DSP to maintain an appropriate balance between rate levels, rate stability, and market responsiveness of rates. In other words, a "prudent mix" of contracts is one that achieves a reasonable level of risk vis-à-vis price.

(7) Does a "prudent mix" mean that the contracts are diversified and accumulated over time?

A "prudent mix" could mean that the contracts in a DSP's portfolio are diversified and accumulated over time; however, it does not have to. For example, it may be prudent for a DSP to enter into a 5-year contract at a low price, rather than multiple contracts at various prices.

(8) Should there be qualified parameters on the prudent mix? For instance, should the regulations preclude a DSP from entering into all of its long-term contracts in one year?

No, the PUC should not be prescriptive for all plans, as a "one-size-fits-all" approach is inappropriate. Rather, the Commission should review plans on an individual basis. For electric distribution companies ("EDCs") with smaller default service loads, it may be possible and prudent to have only one "long-term" contract (or no "long-term" contracts). Furthermore, the Commission must be able to prospectively modify the parameters of the "prudent mix" standard to accommodate changing market conditions.

(9) Should the DSP be restricted to entering into a certain percentage of contracts per year?

No, for the same reasons as stated in Questions 7 and 8, a DSP should not be restricted in such a manner.

(10) Should there be a requirement that on a total-DSP basis, the "prudent mix" means that some quantity of the total-DSP default service load must be served through spot market purchases, some quantity must be served through short-term contracts, and some quantity must be served through long-term contracts?

The Companies believe that the statute provides the PUC with the discretion to find that the "prudent mix" can be achieved through reliance on only two of the three potential product lengths in some circumstances. As a result, there should not be a requirement to include all three.

(11) Should there be a requirement that some quantity of each rate class procurement group's load be served by spot market purchases, some quantity through short-term contracts, and some quantity through long-term contracts? In contrast, should a DSP be permitted to rely on only one or two of those product categories with the choice depending on what would be the prudent mix and would yield the least cost to customers over time for that specific DSP?

To be considered a prudent mix, a DSP must maintain a combination of more than one type of contract, but not necessarily all three types of contracts. In other words, a prudent mix means at least two types of contracts.

(12) Should the DSP be required to hedge its positions with futures including natural gas futures because of the link between prices of natural gas and the prices of electricity?

The DSP should be permitted, but not required, to hedge its positions with futures. Hedges, however, should not be limited to futures, because swaps, options, and other products could be just as prudent. Also, hedges should not be limited to natural gas because there may be other cost drivers that can be hedged financially (e.g., energy hedged with financial products or congestion hedged with FTRs).

(13) Is the "prudent mix" standard a different standard for each different customer class?

No position.

(14) What will be the effects of bankruptcies of wholesale suppliers to default service suppliers on the short and long term contracts?

It is difficult to generalize about impact of a wholesale supplier's bankruptcy. Specifically, the effect of a wholesale supplier's bankruptcy on a DSP's contracts will depend on the state of the market (i.e., whether the market is rising or falling) at the time the bankruptcy occurs and whether the underlying contract requires a non-defaulting party to pay damages to a defaulting party. The impact may also depend on mitigation strategies pursued by the DSP.

(15) Does Act 129 allow for an after-the-fact review of the "cost reasonableness standard" in those cases where the approved default service plan gives the EDC substantial discretion regarding when to make purchases and how much electricity to buy in each purchase?

No. Act 129 does not permit an after-the-fact review of the "cost reasonableness standard." Once the PUC approves a level of discretion in a default service plan, the Commission cannot subsequently review the reasonableness of the costs incurred under the plan,

as long as the DSP follows the conditions approved by the Commission. The Commission's recent decision in the Companies' default service proceeding confirms this. See Citizens' and Wellsboro Default Service Plan, p. 32 (ruling that "there is clearly no statutory mandate for an after-the-fact prudency review" of procurement-related costs).

(16) How should the requirement that "this section shall apply" to the purchase of AECs be implemented. Section 2807(e)(3.5) states that "the provisions of this section shall apply to any type of energy purchased by a default service provider to provide electric generation supply service, including energy or alternative energy portfolio standards credits required to be purchased, etc."

Section 2807(e)(3.5) requires that AEC purchases include a prudent mix of purchases, which could include long-term purchases. As explained above, the prudent mix does not necessarily require the use of a long-term contract.

III. CONCLUSION

WHEREFORE, the Citizens' Electric Company of Lewisburg, PA, and the Wellsboro Electric Company respectfully request that the Pennsylvania Public Utility Commission consider and adopt, as appropriate, the foregoing Comments.

Respectfully submitted,

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