BEFORE THE PENNSYLVANIA PUBLIC UTILITY COMMISSION

IMPLEMENTATION OF ACT 129 OF :
OCTOBER 15, 2008; DEFAULT SERVICE : Docket No. L-2009-2095604

COMMENTS OF CITIZEN POWER

I. Introduction

The Pennsylvania Public Utility Commission ("Commission") seeks comments regarding the above-captioned docket in connection with revisions to default service regulations which became effective on September 15, 2007. On October 15, 2008, Governor Edward Rendell signed House Bill 2200, Act 129, into law which has made revisions necessary so that the regulations are consistent with the Act. A Notice of Proposed Rulemaking Order was published in the May 1, 2010 Pennsylvania Bulletin regarding the above-captioned docket. In the following section, Citizen Power responds to the questions that were located under the heading "Additional Issues".

II. Responses to Additional Questions Related to the Implementation of Act 129 of October 15, 2008; Default Service at Docket No. L-2009-2095604

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

   The requirement under 66 Pa C.S. §2807(e)(3.4)(II) that the mix of contracts that a DSP enters into for generation procurement shall be designed to ensure the "least cost to customers over time" is a laudable goal. However, a DSP cannot literally ensure the least cost to customers without the help of a crystal ball given the unpredictability of energy markets. Therefore, a reasonable interpretation of the phrase "least cost to customers over time" is that a DSP, when faced with uncertain electricity markets, creates a portfolio of procurement contracts that minimizes both the cost and the risk to consumers as much as possible. Since the reduction of risk (certainty of rates) always comes at a price (risk premiums), the portfolio of contracts should strive to find the procurement options that strike a correct balance between these two competing goals. In addition, DSPs should also attempt to reduce price fluctuations to consumers, since unexpected price increases produce a very real cost for consumers on a budget.

The reality of creating a procurement plan is that there will be always be significant trade-offs. Some options may involve lower rates in the near future with significant uncertainty later on. Other options may result in certain rates that increase over time. It is difficult to determine which mix of procurement options results in the "least cost to customers over time" when they all have their advantages and disadvantages. However, customers themselves have a good indication of how to value the risks involved. Therefore, in the creation of a procurement plan that is the "least cost to customers over time", the DSP should reach out to customers to determine how they assess the costs of competing options. This information not only is valuable to the DSP in creating their plan, but would also provide evidence that the procurement plan is least cost.

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

The Commission should evaluate a DSP's procurement plan based upon a 20 year time frame, which is the length of the longest-term contract contemplated under 66 Pa. C.S. §2807(e)(3.2)(iii). For instance, if a DSP's procurement plan only includes long-term contracts for an 8 year period, the Commission should evaluate whether also including 20 year long-term contracts could produce least cost to customers over time.

3. 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?

Implicit in the requirement of DSPs to provide adequate and reliable service is the requirement that adequate generation resources exist. Theoretically, generation capacity should not be an issue in Pennsylvania because of the presence of the PJM capacity market. However, in our opinion, the presence of this market does not guarantee that sufficient generation will be developed so as to provide adequate and reliable default service. Therefore, it is possible that a situation could develop where the generation assets necessary to provide an adequate margin over peak load is not present.

We believe that if new generation is required in order to maintain adequate and reliable service, that generation should be put into service as a regulated asset and ideally owned by a public entity. Large wholesale electricity markets do not deliver electricity at the lowest price over the long-term because electricity does not act like other commodities; it is a necessity without any good substitutes evidenced by large economies of scale and the unusual physical property that the supply must match demand instantaneously. Over the long-term, the least cost solution (for consumers) is for new generation to be procured by the DSP on a cost-of-service basis from a regulated generation facility.

However, under Act 129, default supply must be obtained through a competitive procurement process. One procurement option under 66 Pa C.S. §2807(e)(3.1)(III) is the use of bilateral contracts. Long-term power purchase agreements at cost-of-service prices could be entered into by the DSP in order to stimulate generation capacity. Under 66 Pa C.S. §2807(e)(3.3), the Commission can extend these power purchase agreements beyond 20 years if necessary to incentivize the necessary generation. If it is necessary for DSPs to ensure the construction of necessary generation, we prefer long-term power purchase agreements at prices based upon cost-of-service.

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

One possible solution would be to add the following to §54.186(e)(4): "The DSP's plan includes prudent steps necessary to ensure adequate and least cost generation capacity through long-term contracts if the Commission has determined that additional generation is required to maintain adequate and reliable service."

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, in most cases, will produce the least cost to customers over time because it allows for the DSP to hedge against possible future price spikes. A full requirements approach may be considered during periods when there are relatively low power prices in order to take advantage of these low prices. However, caution should be taken with this approach because full requirements service limits the number of potential bidders which may drive the price up. One possibility that may be considered for the larger territories is to allow for full requirements service to provide a number of tranches within a managed portfolio.

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

The definition of a "prudent mix" of spot, long-term and short-term contracts is dependent upon the current environment that a DSP faces in creating their procurement plan. What is "prudent" therefore changes over time and should be determined using a reasoned analysis keeping in mind the goal of "least cost to consumers over time".

7. Does a “prudent mix” mean that the contracts are diversified and accumulated over time?

In general, contracts should be diversified and accumulated over time. However, if a DSP can take advantage of a period of over-capacity to lock in low rates for consumers, it should take advantage of that circumstance.

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, there should not be qualified parameters on the prudent mix. Although, in general, a wide variety of contracts would limit risk through hedging, there may be situations where a less balanced approach is prudent. DSPs should not be unnecessarily limited in the tools available at their disposal to obtain generation at the least cost over time.

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

No. DSPs should be allowed the flexibility to avail themselves of advantageous market situations when they present themselves. However, the Commission should review plans that are less balanced with a more critical eye to ensure that default service is being provided at the “least cost to customers over time”.

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?

Yes. 66 Pa. C.S. §2807(e)(3.2) is clear in the requirement that default service load must be served through spot market purchases, short-term contracts, and long-term contracts and the term “prudent mix” implies that all three methods must be employed.

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?

    There does not necessarily have to be a requirement that each rate class procurement group's load be served through all three methods. However, the Commission should examine procurement plans that rely on only two product categories for a rate class procurement group more closely to determine if the plan would produce the least cost to customers over time. Procurement plans that rely upon only one product category for a specific rate class procurement group should be especially scrutinized.

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?

    There should not be a requirement that the DSP hedge its positions with futures, though the DSP should investigate the option. In addition, the futures prices can be used as an additional tool in the determination of the appropriate risk premium for medium and long term contracts.

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

    The standard itself is not different for each different customer class, though what constitutes a "prudent mix" may be different. This is because each customer class may have different views regarding the values of cost and risk. What is prudent for one class of customer is not necessarily prudent for another.

14. What will the effects of bankruptcies of wholesale supplier to default service supplies on the short- and long-term contracts?

Any cost differential between the contracted cost for supply and the replacement cost for the same supply should not be passed to the default customers.

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?

66 Pa C.S. §2807(e)(3.8) is clear that costs stemming from a procurement plan may only be disallowed if the DSP is found to have not complied with the Commission approved plan or if the DSP committed fraud, market manipulation, or collusion with regard to the procurement plan contracts. An after-the-fact review of costs resulting from discretionary actions of a DSP is not possible unless the plan itself allowed for such a review or the discretionary actions involved fraud, market manipulation, or collusion. In our view, a balance must be struck between allowing DSPs the flexibility to seek out opportunities to build a portfolio that is "the least cost to customers over time" and protecting customers from decisions that may raise the cost of default service. Therefore, we do not believe that the Commission should grant the EDC substantial discretion in procurement decisions within their default service plan without the requirement of preliminary Commission approval of those procurement decisions.

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."

In our opinion, the "prudent mix" requirement is for the total DSP default service load and should not be applied selectively to alternative energy portfolio standards credits. If, for instance, long-term contracts can procure credits for the “least cost to customers over time”, a DSP should not be required to also obtain credits through short-term contracts.

Respectfully Submitted,

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