Jesse A. Dillon
Senior Counsel

PPL
Two North Ninth Street
Allentown, PA 18101-1179
Tel. 610.774.5013 Fax 610.774.6726
jadillon@pplweb.com

June 1, 2010

VIA HAND DELIVERY

Rosemary Chiavetta
Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street, 2nd Floor North
P.O. Box 3265
Harrisburg, PA 17105-3265

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

Dear Secretary Chiavetta:

Enclosed, for filing, please find an original and fifteen (15) copies of the Comments of PPL EnergyPlus, LLC to the Proposed Rulemaking Order in the above-referenced proceeding.

Respectfully Submitted,

Jesse A. Dillon

Enclosures

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

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

COMMENTS OF
PPL ENERGYPLUS, LLC
TO THE PROPOSED RULEMAKING ORDER

TO THE PENNSYLVANIA PUBLIC UTILITY COMMISSION:

I. INTRODUCTION

On January 14, 2010, the Public Utility Commission ("PUC" or the "Commission") issued an Order requesting comments on the proposed amendments to the Commission's default service regulations, 52 Pa. Code §§ 54.181-54.188, as required by the enactment of Act 129. Therein, Commission indicated that the purposes of the Proposed Rulemaking is to implement the provisions of Act 129. The Commission also requested responses to sixteen Additional Questions set forth in the Proposed Rulemaking Order. The Proposed Regulations and Additional Questions were published in the *Pennsylvania Bulletin* on May 1, 2010, with a 30-day comment period.

PPL EnergyPlus, LLC ("PPL EnergyPlus") is the energy marketing and trading subsidiary of PPL Corporation. PPL EnergyPlus buys and sells energy commodities and structured products in the competitive wholesale markets. PPL EnergyPlus is also active in deregulated retail markets, and offers electricity supply, natural gas supply, and renewable

energy products to commercial, industrial, and institutional customers. PPL EnergyPlus believes that its familiarity and experience in the competitive wholesale markets will benefit the Commission and parties in this proceeding.

The proposed regulations generally adopt Act 129 procurement requirements verbatim, and PPL EnergyPlus has no basis to disagree with that language. However, to assist in the interpretation and implementation of Act 129, the Commission posed sixteen (16) Additional Questions for comment. PPL EnergyPlus hereby submits the following responses to these Additional Questions posed by the Commission:

II. RESPONSES TO ADDITIONAL QUESTIONS

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

The phrase "least cost to consumers over time" implies lowest cost to consumers as reasonably possible. In order to achieve least cost over time, while understanding the risks associated with too heavily relying on the spot market and the exposure related to long term contracts (*e.g.*, stranded costs), a diverse portfolio made up of short term contracts (six months and one year), intermediate term contracts (between two and five years) and spot market purchases is recommended.

However, an alternative to a diverse portfolio of supply contracts for the EDC would be allowing retail suppliers to provide consumers with supply, demand response, alternative energy and efficiency choices. A diverse portfolio of shorter term contracts, less than one year, would result in consumers working with retail suppliers on more efficiently utilizing their energy spend in a marketplace that will provide more choices, more products and more use of technology.

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

No time frame for the Commission's evaluation of DSP procurement plans should be prescribed. A DSP submits a procurement plan that includes a mixture of contracts that meets the requirements of Section 2807(e)(3.4). The Commission reviews the procurement plan and determines if the plan will produce the least cost to customers over time. The plan is then approved based on this review and meeting the requirements set forth in Section 2807(e)(3.4). Thus, the Commission evaluates whether a DSP's procurement plan produces least cost to customers over time through the regulatory review process when the procurement plan is submitted. The relevant evaluation is whether each procurement that a DSP conducts is competitive and whether the results are the "least cost to customers" based on compliance with the approved procurement plan.

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, the market will provide for new generation as it has in the past and continues to do today.

Pennsylvania Act 129 requires Electric Distribution Companies (EDCs) to procure default service supply for customers who do not select alternative suppliers at rates that are the least cost over time. The Commission has agreed that EDCs should satisfy this requirement through a prudent mixture of spot, short-term and long-term power supplies purchased in the competitive market. We believe there are risks and cost exposures related to long term contracts and such risks and exposures are best left to the markets.

As a matter of fact, a provision by which the PUC would ensure construction of generation is contrary to the "least cost over time" requirement of Act 129. The design of Pennsylvania's competitive electricity market removes the financial risk inherent in the decision to build generating capacity from EDC captive ratepayers. This change has been a major factor in moving Pennsylvania electricity prices from well above the national average to below the national average. A provision that authorized the PUC to direct EDCs to build generation would remove the protection ratepayers currently enjoy, and could subject them to higher rates in the long-term due to uneconomical investment in new generation or cost overruns from construction or inefficient operation of generating facilities.

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

The default service regulations should not be revised to adopt any provision to ensure construction of generation capacity. The market will provide for new capacity just as it has in the past. More importantly, market participants, along with a well defined and properly regulated market structure, will identify other resources that provide "capacity like" capabilities such as demand response, energy efficiency and other types of conventional and renewable generation resources.

A provision by which the Commission can direct EDCs to build new generation is contrary to the intent of the "least cost over time" provision of Act 129, and could subject EDC ratepayers to higher prices and new stranded costs. In any case, while the Commission has the authority to approve a wide range of different DSP's proposed by EDC's, it is not clear that the Commission has the authority to adopt a provision requiring construction of new generation.

Lastly, if for some unfortunate reason such a provision were to occur, it should be a demand charge on all customer invoices. The requirement of the new resource would serve everyone and all customers should pay for such resource.

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 full requirements product is more likely to produce the least cost to customers over time when compared to a managed portfolio product.

A full requirements product requires the supplier to bear most, if not all, of the risk related to the uncertainty of commodity prices, uncertainty of consumer usage, uncertainty of economic conditions and uncertainty of market and policy rulemaking. These risks are best managed by commodity and energy market participants than an EDC. The management of these risks by the market mitigates the customer from taking unforeseen risks.

For an EDC to provide this service effectively, the EDC would have to actively manage a portfolio of power supply products and consistently demonstrate that it could do so at a lower cost than the market. In addition, the EDC would have to manage the portfolio risks related to full requirements service more efficiently – holding less risk - than the market. A managed portfolio approach may result in commodity positions being held by the EDC which are not serving customers due to changes in customer shopping, the economy or other market conditions unforeseen by the EDC or regulators. These positions create a volumetric and a price exposure for customers which may result in higher prices and stranded costs.

For example, if the EDC were to rely solely on a portfolio of block products, intermediate and long-term contracts instead of full-requirement load-following products, it would need considerable specialized expertise in commodity prices, trading, forecasting and contracting.

These skills are outside of EDC's core business. However, these skills are critical to wholesale suppliers' core business. The addition of necessary personnel to undertake these activities within the EDC would create an additional default service cost.

Moreover, to deliver default service supply and risk management services at least cost, the EDC would be required to implement these commodity, trading, forecasting and contracting skills better than wholesale suppliers to deliver default service supply consistently at a lower price. Absent evidence that the EDC could manage these risks better than the marketplace while providing customers with the same rate stability that can be achieved under load following contracts.

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

A prudent mix would be comprised of short term contracts (six months and one year), intermediate term contracts (between two and five years) and spot market purchases. A "prudent mix" will be separately established through the regulatory review of the procurement plans filed by each DSP as required by Act 129. There is no one set formula or schedule of what constitutes a "prudent mix," and there can be infinite variety of procurement plans that can be considered a "prudent mix." The regulatory process will permit all interested parties the opportunity to express their opinions on the specifics of a "prudent mix".

As described earlier, an alternative to a prudent mix of supply contracts for the EDC would be allowing retail suppliers to provide consumers with supply, demand response, alternative energy and efficiency choices. A diverse portfolio of shorter term contracts, less than one year, would result in consumers working with retail suppliers on more efficiently utilizing their energy spend in a marketplace that will provide more choices, more products and more use of technology.

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

Yes. Procurement plans should use a laddering approach which utilizes varying procurement periods and differing contract durations to ensure the maximum benefit of cost averaging.

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?

Yes, any procurement terms beyond short term contracts should not be completed at any one time or within one year. Given the recommendation of the laddering approach described in response to question 7 above, regulations should be implemented to restrict default service providers from entering into all these contract types within a year.

However, some situations may exist for it to be prudent to enter into these contracts types in one year. For example, the DSP is procuring only a small percentage of its load requirements during a procurement process and due to the size of the procurement it would not be prudent to spread the volume of the procurements over multiple periods

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

Procurement plans should use a laddering approach which utilizes varying procurement periods and differing contract durations to ensure the maximum benefit to customers.

The prudent mix for a DSP will be established through the regulatory proceeding of the Default Service Procurement Plan filed as required by Act 129. There can be infinite number of procurement plans and the regulatory process allows parties to express their opinions on a

prudent mix. However, the Commission should not prescribe to the DSPs the percentages of contracts per year.

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?

Again, a laddering approach of procurement with varying terms and durations of short term and intermediate term contracts is the most effective way to manage exposure to customers.

Long-term contracts place significant risk on the customers of the EDC and should not be required. Long-term capital investments and long-term market risks should remain with the market.

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?

No, there should not be a mandate that some quantity of each rate class procurement group's load be served by spot market purchases, short term and long term contracts. The requirement should be not to rely too heavily on spot market purchases or long term contracts as these present greater risk to customers with respect to price volatility and stranded costs. However, an exception may be for large commercial and industrial customers who should primarily be offered service utilizing the spot market.

Further, a DSP should be permitted to rely on only one or two of these 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. Utilizing a ladder approach of full requirement products may better result in an appropriate prudent mix and provide least costs to customers over time.

In addition, an alternative to a prudent mix of supply contracts for the EDC would be allowing retail suppliers to provide consumers with supply, demand response, alternative energy and efficiency choices. A diverse portfolio of shorter term contracts, less than one year, would result in consumers working with retail suppliers on more efficiently utilizing their energy spend in a marketplace that will provide more choices, more products and more use of technology.

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?

No. The power markets provide ample liquidity to procure the full requirements approach and the managed portfolio approach discussed here. The use of cross commodity hedging, natural gas and electricity, should not be considered prudent. Several reasons for not utilizing natural gas as an electricity hedge besides the inherent commodity risk are (1) correlations between the two commodities break down at delivery, (2) DSPs do not have the resources and skills to manage cross commodity correlations and (3) energy and regulatory policies have the potential to change present correlations thus creating risk to customers.

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

Yes, EDCs should develop a prudent mix standard through the regulatory proceeding process that is different for each customer class. For example, residential and small commercial

customers should have a different standard than large C&I customers, who are more sophisticated and have the capability to manage commodity risks.

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

DSPs and their customers have counterparty credit risk as a result of the default procurement(s). More importantly, the longer the term of the supply contract, the greater the counterparty credit risk. A valuable lesson that has been learned in the energy and financial markets, is that counterparty credit is extremely important and the risk to customers can be significant.

If a wholesale supplier were to default, the DSP would have to replace the energy within the portfolio with a new procurement. The amount of the exposure would depend on market prices at the time of the default as well as whatever credit protection was provided by the counterparty by means of a parental guaranty, letter of credit or cash.

The overall cost to customers can be either positive (lower new price) or negative (higher new price), however, counterparty credit risk is important and must be managed properly from both a wholesale and retail supplier standpoint.

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. There is no such authority under Act 129. Rather,Section 2807(e) (3.8) provides the Commission with authority to conduct an after-the-fact-review to disallow costs only for non-compliance with the approved default service plan, or the commission of fraud, collusion, or market manipulation. Any other after-the-fact review to disallow of costs incurred by a DSP to

obtain supply to meet its default service obligations would be contrary with Act 129 and other provisions of law.

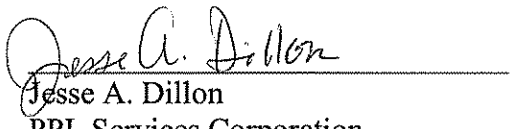
16. How should the requirement that "this section shall apply" to the purchase of AECs be implemented. Section 2807(e)(3.5) states that "the provisions of this section shall apply to any type of energy purchased by a default service provider to provide electric generation supply service, including energy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

A DSP must obtain any other products required to provide default service, including, but not limited to, capacity, ancillaries, congestions, and etc. A DSP must also obtain AECs to comply with the AEPS Act. The Commission's regulations should address all of these products as essential components of DSP supply.

III. CONCLUSION

For the reasons set forth above, PPL EnergyPlus respectfully requests that the Commission modify its Proposed Regulations consistent with the above-stated responses to the sixteen Additional Questions posed by the Commission.

Respectfully submitted,



Jesse A. Dillon
PPL Services Corporation
Two North Ninth Street
Allentown, PA 18101-1179

Attorney for PPL Energy Plus, LLC

Date: June 1, 2010