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June 15, 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 the Reply Comments 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 Reply Comments, and kindly return them to our messenger for our filing purposes.

Very truly yours,

McNEES WALLACE & NURICK LLC

By 

Pamela C. Polacek

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

PCP/km

Enclosures

c: Elizabeth Barnes, Assistant Counsel, Law Bureau (via E-mail)

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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. On June 1, 2010, Citizens' Electric Company of Lewisburg, PA ("Citizens") and Wellsboro Electric Company ("Wellsboro") (collectively, "the Companies"), among others, submitted Comments in order to present their preliminary position and to address their concerns regarding the Commission's proposed regulations.

Pursuant to the established schedule in this proceeding, the Companies hereby submit these Reply Comments to address specific areas of concern with respect to other stakeholders' Comments submitted in response to the Commission's Proposed Rulemaking Order.

I. REPLY COMMENTS

Unlike the Companies' Comments that generally addressed preliminary concerns regarding the PUC's Proposed Rulemaking Order, these Reply Comments focus on various stakeholders' positions, as set forth in the Comments submitted on June 1, 2010.¹ The Companies also reserve the opportunity to address additional issues in subsequent phases of this proceeding, as necessary.

¹ The Companies' failure to address a specific proposal raised by any party does not represent the Companies' support for, or acquiescence to, such proposal. The Companies addressed the primary areas of concern in their Comments and submit these Reply Comments only on areas that necessitate an additional response.

A. A "Market-Reflective and Market-Responsive" Procurement Approach is Not Required Under Act 129 and is Merely a Restatement of the "Prevailing Market Price" Approach, Which Act 129 Eliminated and Replaced With the "Least Cost Procurement" Standard Using a "Prudent Mix of Contracts."

In its Comments, the Retail Energy Supply Association ("RESA") asserts that the "least cost procurement" standard, as set forth in Act 129, "is satisfied when [Default Service Provider's ("DSP")] proposed default service plan produces rates that are *market-reflective and market-responsive*, include all the costs of providing default service into the service rate and, therefore, result in a sustainable retail market." RESA Comments, pp. 12, 15-19 (emphasis added). Although RESA attempts to justify its interpretation of the "least cost procurement" standard as a measure that complies with the Electricity Generation Customer Choice and Competition Act ("Competition Act") and encourages competitive alternatives, a market-reflective and market-responsive procurement approach is merely a restatement of the "prevailing market price procurement" standard that Act 129 expressly eliminated. As such, the PUC must reject RESA's recommendation to evaluate default service plans based primarily on whether default service rates reflect and are responsive to market prices.

In support of its recommendation, RESA also suggests that, "[b]ecause default service, as mandated by the Competition Act, is a 'one-size only' product, it alone cannot ensure 'least cost' service." *Id.* at 16. Despite RESA's doubts about whether a default service product can produce least cost service, the General Assembly mandated that default service plans be designed and implemented in accordance with a least cost procurement strategy. The Commission must implement the General Assembly's determination that the "least cost procurement" standard should be pursued rather than the prevailing market price approach endorsed by RESA. RESA's recommendation should therefore be rejected by the Commission.

B. A Default Service Procurement Process Where Multiple Wholesale Generation Suppliers are Solicited Meets the "Competitive Procurement" Requirement Set Forth in Act 129.

RESA has proposed to add language to Proposed Section 54.186(e) to ensure that a "DSP's plan includes prudent steps necessary to negotiate favorable generation supply contracts *through a competitive procurement process.*" *Id.* at 40-41 (emphasis added); *see also* Proposed 52 Pa. Code § 54.186(e). While Citizens' and Wellsboro do not necessarily oppose the addition of such language to Proposed Section 54.186(e), the Companies wish to make clear that their current procurement process is competitive. Specifically, under the procurement approach currently employed by Citizens' and Wellsboro and approved by the Commission, the Companies work with multiple bidders in the wholesale market to competitively procure default service at the least cost to customers over time. *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").

Because the PUC has already found the Companies' default service procurement process to be consistent with the requirements of Act 129, Citizens' and Wellsboro submit that their procurement approach is competitive and consistent with RESA's recommended addition to Proposed Section 54.186(e). As a result, if RESA's change is accepted, then this new language should not be used to object to the Companies' procurement process in future default service proceedings.

C. A Managed Portfolio Approach, Rather Than a Full Requirements Approach, is More Likely to Produce the Least Cost to Customers Over Time.

In their Comments, Constellation NewEnergy, Inc. and Constellation Energy Commodities Group, Inc. ("Constellation"), as well as the PJM Power Providers Group ("P3

Group") argue that a full requirements approach is superior to a managed portfolio approach for acquiring default service supply. *See generally* Constellation Comments, pp. 22-30; P3 Group Comments, pp. 5-6. Both Constellation and P3 Group assert that a full requirements contract approach is preferable because it shifts risk from ratepayers to market participants and, thus, insulates ratepayers from construction cost overruns, commodity volatility, weather, and other risks of generation business. *Id.* The Companies disagree with this assessment.

A managed portfolio may expose customers to some risks of price volatility but, in exchange, the customer's rates do not reflect the mark-up that the full requirements suppliers include in their bids for bearing these risks and do not reflect the profit that Constellation and the P3 Group members make on full requirements contracts. As recognized in the Office of Small Business Advocate's ("OSBA") Comments, in the future the PUC will have actual rates produced by each approach to determine the cost of the "insurance policy" reflected in full requirements contracts and whether that cost provides adequate customer benefits in comparison to a managed portfolio approach. Both approaches appear to be permitted under the statute if designed to produce the least cost to customer over time.

To lend support for its defense of full requirements contracts, Constellation argues that the congestion event experienced in Wellsboro's service territory in 2008 proves that ratepayers are benefited, in all respects, by the "insurance" provided by a full requirements supplier. Constellation Comments, pp. 22-23. The Companies believe that the congestion event illustrates one of the benefits of a managed portfolio approach. Although the congestion event that Wellsboro experienced was beyond its control, because Wellsboro operated under a managed portfolio approach rather than a full requirements contracts approach, the event was quickly detected by Wellsboro and the underlying cause was remedied. Importantly, if Wellsboro had

been operating under a full requirements approach, then Wellsboro would not have had the knowledge or motivation to actively investigate the cause of the congestion event. Instead, the underlying cause would not have been addressed and the risk of future volatility would have been monetized in future full requirements bids, thereby increasing rates imposed on and paid by default service customers.

Constellation also argues that, because of its vast number of employees in various areas of expertise, Constellation is "able to drive down a wholesale supplier's costs of meeting load requirements and provide the most reliable, up-to-the minute improvements and adjustments to a portfolio of resources, from which all of the supplier's customers will benefit." *Id.* at 26. Under a full requirements approach, however, the retail customers do not see the benefit of those adjustments because they pay a fixed price. In making this argument, Constellation also fails to address the core issue – whether Constellation's full requirements bids, including their profit, result in less costs for customers than the Companies' managed portfolio approach. Constellation is providing wholesale default service supply to make a profit for its shareholders. Citizens' and Wellsboro are using a managed portfolio approach because the Companies believe it will produce the best rates for their customers. Moreover, as discussed in the Companies' Comments, because the potential exists with a full requirements approach for wholesale suppliers to "front load" power prior to the auction date and then inflate bids based on their market position, such an approach is problematic. *See* Citizens' and Wellsboro Comments, p. 6.

In addition, Constellation describes the full-time meteorologists that it employs to continually monitor and predict weather patterns and asserts that, "[w]ithout such professionals, . . . no evidence exists to suggest that an EDC as a portfolio manager will be able to predict the weather." Constellation Comments, p. 26. Constellation then concludes that "[t]he EDC's

consumers will bear the burden of the costs of this inability to accurately predict and plan for the weather in real-time." *Id.* at 27. While utilizing the expertise of meteorologists may be necessary to implement Constellation's business model, it is certainly not required under the Companies' managed portfolio strategy. Specifically, due to the manner in which the Companies' managed portfolio approach is structured, Citizens' and Wellsboro do not require minute-by-minute weather forecasts. Rather, Citizens' and Wellsboro must pre-purchase blocks of power and do not have the discretion to make "minute by minute" changes to the number of blocks. Moreover, it isn't clear that the added value of having a team of meteorologists outweighs the costs in comparison to relying on publicly-available weather forecasts and information.

Finally, the Companies also note that a full requirements contracts approach, even when not affected by "front loading" during the bidding, is not foolproof and can produce undesirable results. For example, PPL Electric Utilities Corporation's ("PPL") 2010 default service rates, which are based on a full requirements approach, are over 10 cents per kWh. Meanwhile, Citizens' pricing, based on a managed portfolio approach, in the same territory has been 8.2687 cents per kWh (1st Quarter), 9.0550 cents per kWh (2nd Quarter) and 6.9464 cents per kWh (3rd Quarter). As such, the recommendation that a full requirements approach is clearly superior – and will produce the least cost to customers over time, as required by Act 129 – should be rejected.

D. Act 129 Does Not Allow for an After-The-Fact Review of the "Cost Reasonableness Standard."

In its Comments, the OSBA recommends that the PUC determine that the Commission has the authority, under Act 129, to review the reasonableness of default service costs after the Commission has approved a DSP's default service plan. *See OSBA Comments, pp. 31-33.*

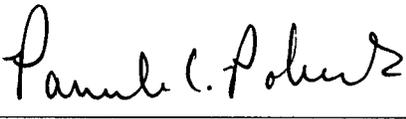
Specifically, the OSBA suggests that, "although Act 129 does not set out a detailed process for an after-the-fact review of a DSP's decisions under a managed portfolio, the statute also does not explicitly preclude such review." *Id.* at 33. Act 129 does specifically state when costs can be disallowed and the Commission has explicitly rejected post facto review. *See Citizens' and Wellsboro Comments*, p. 8; *see also 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). As such, once the PUC approves a level of discretion in a default service plan, the Commission should not be permitted to subsequently review the reasonableness of the costs incurred under the plan, as long as the DSP follows the plan approved by the Commission and does not engage in fraud, market manipulation or collusion.

III. CONCLUSION

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

Respectfully submitted,

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