

**BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

<b>Investigation of Pennsylvania’s</b>	)	
<b>Retail Electricity Market:</b>	)	<b>Docket No. I-2011-2237952</b>
<b>Intermediate Work Plan</b>	)	

**Comments of Spark Energy**

Spark Energy, L.P. (“Spark Energy”) hereby respectfully submits its comments to the Tentative Order issued by the Commission on December 15, 2011 concerning the intermediate work plan being developed in support of the Commission’s Investigation of Pennsylvania’s Retail Electricity Market. Spark Energy’s comments address the “Retail Opt-In Auction Programs” discussed at pages 22-41 of the Tentative Order. Spark Energy supports the Commission’s adoption of opt-in auction programs and appreciates this opportunity to comment on the opt-in initiative.

Spark Energy is a licensed Electric Generation Supplier (EGS) in Pennsylvania that sells electricity to customers in the PECO and PPL service territories. Spark Energy Gas, LP (“Spark Energy Gas”) is an affiliate of Spark Energy and a licensed Natural Gas Supplier (NGS) in Pennsylvania. Collectively, Spark Energy and Spark Energy Gas serve retail customers in seventeen states across the country.

Spark Energy believes the Commission’s opt-in policy needs to strike the appropriate balance between (1) encouraging Customer Choice through the opt-in experience and (2) inadvertently *discouraging* Customer Choice through opt-in features which motivate individual customers to abandon shopping, or alternatively, diminish supplier interest in the auction and ultimately in the Pennsylvania market. In support of finding that appropriate balance, our comments are limited to 3 issues: 1) restrictions that should be in place during the enrollment

period; 2) restrictions on bonus payouts under the fixed price product option; and 3) the opt-in auction structure.

### **Opt-In Auctions - The Enrollment Period**

The Commission noted in the Tentative Order that customers should know the exact price they will be expected to pay before deciding to enroll in an opt-in auction. To make this feasible, the Commission acknowledged that the enrollment period should be short (no longer than a month), and should occur as closely as possible to the actual service start date. We suggest one additional clarification and one more significant caveat: the enrollment period should start immediately upon successful closure of the auction, and mechanisms that shield suppliers from unanticipated wholesale market price change during the enrollment period should be built into the auction and enrollment window.

Suppliers will bid in the auction based on (among other things) then-current forward wholesale market prices, profit expectations, and anticipated customer enrollment over the life of the term. The longer the enrollment period, the greater the risk to a supplier of adverse, unanticipated price changes in the wholesale market. A month may be a short time to conduct customer outreach and enrollment but it is a long time for suppliers to carry an unknown exposure. The Commission correctly noted that suppliers can approximate customer enrollment but they cannot anticipate major adverse wholesale price change during the enrollment period.

A simple example illustrates the point. If the enrollment period were 30 days and a price shock occurred at day 15 (say, for example, wholesale prices jump 20%), default customers who were otherwise not interested in enrolling, or customers who have shopped but have variable prices or are near the end of a fixed price term, could be motivated to enroll and take advantage of this “free option”. While the 50% cap on participation puts an upper bound on the problem, a

prudent supplier could be exposed to significant unanticipated volume risk at a fixed price which had just become well under market, or alternatively, would have to purchase financial instruments to protect from such risk and thus inflate the price that could otherwise be offered.

To avoid this problem, we suggest that bidders be allowed to submit bids that cap tranche size if a pre-defined adverse market change occurs during the enrollment period. For example, if the market price moves more than 5% above the day-of-auction level for more than 33% of the enrollment period, a supplier would have the opportunity to cap its tranche at “x” number of customers rather receive the standard anticipated tranche size (for example, 10% of total customer enrollment). A supplier would specify “x” as part of the bid and could only exercise this option if the 5/33% threshold conditions were met. If the threshold conditions were met and one or more winning bidders requested a reduced tranche size, other suppliers which had specified higher “x’s” (or no limit) would have the opportunity to receive larger tranches.

Spark Energy recognizes that further discussion would be needed to appropriately define the measure of market price and whether different numerical values were more appropriate for the threshold conditions. These details could be worked out in OCMO discussion groups.

### **Opt-In Auctions – Bonus Payouts**

The Tentative Order would allow all residential customers, even those already with a supplier, to participate in an auction. Our concern is that existing Choice contracts not be undermined by the opt-in initiative. The Commission stated its intent to target education efforts to non-shopping customers but we suggest that the Commission also alter the proposed product structure so as to not unduly undermine existing Choice contracts.

The Tentative Order envisioned a fixed rate product with a bonus (\$50-\$100) and percent-off default rate with no bonus as the two possible opt-in product structures. We believe

the motivation behind offering a bonus is to deliver a message to non-shopping customers of “here’s an incentive to try something new, you might like it”. However, the same bonus offer to a customer who has shopped and is currently with a supplier in a fixed term contract delivers this message: “here’s a state-sanctioned payout to help you renege on your existing contract”. The first message supports Choice, the second does not.

Spark Energy suggests two alternatives to avoid this problem. Preferably, the Commission could require that opt-in education and marketing materials specify that any bonus offer is only available to first-time Choice participants (and not available to customers who are or have previously received service from a supplier). Alternatively, allow an existing supplier to be reimbursed for an early termination fee if a customer departed an existing contract in favor of an opt-in auction and did not pay an applicable early termination fee. In effect, the latter option allows the existing supplier to place a lien on the bonus before it is paid out at the end of the third month. The opportunity for the existing supplier to claim the bonus otherwise due to a customer would be communicated in education and marketing materials.

If the Commission allows bonus payouts to customers who have already chosen a supplier, one possible market development is that suppliers could adopt more and larger early termination fees in advance of opt-in auctions. In the telecommunications industry, suppliers have adopted – and rigorously enforced – large early termination fees for cell phone plans as a means to fend off the constant barrage of free phone and other service offerings from competitors. The looming threat of opt-in auctions could trigger a similar practice in Pennsylvania’s retail electric market. Spark Energy does not believe such an outcome would be beneficial, particularly at this early stage of market development.

#### **Opt-In Auctions – Auction Structure**

Spark Energy favors the sealed bid approach over descending clock for conducting opt-in auctions. While descending clock has been successfully employed for reoccurring large scale default service auctions, in our view the sealed bid is more applicable to a one-time opt-in auction meant to replicate a customer-initiated request-for-proposal (RFP) process. Sealed bid would be less complex and expensive to conduct. Given the array of bidding strategies available with either structure, there is no reason or evidence to suggest that one approach would produce a lower price than the other.

Here is how we envision the sealed bid to work for an auction with 10 tranches, with each tranche representing 10% of the customers who enroll, and presuming that the Commission accepts Spark Energy's earlier suggestion to allow a bidder to cap its tranche size if the wholesale market price increases by 5% or more from the day-of-auction price for at least 33% of the enrollment period (the "threshold condition"):

1. Sealed bids are submitted on a date-certain in a format consistent with the chosen product structure (either fixed price or percent off default price, as determined by the utility with the approval of the Commission). Bids may contain, but would not be required to contain, a maximum tranche size the supplier could invoke if the threshold condition is met.
2. A single supplier (including any affiliates) could submit bids for up to 5 tranches. The tranches are bid individually; no 2 need be the same but all 5 could be the same.
3. Bids are stacked from most favorable to least favorable (from the perspective of the customer). The 10<sup>th</sup> most favorable is the highest accepted bid and it along with all 9 more favorable bids are accepted. The winning bidders are paid the clearing price (the 10<sup>th</sup> most favorable bid) and all enrolling customers receive the clearing price.

4. If 2 or more bids are tied for 10<sup>th</sup> place, the 10<sup>th</sup> tranche would be split equally into the number of shares that are tied for 10<sup>th</sup> place. For example, if 3 identical bids are tied for 10<sup>th</sup> place, one-third of the 10<sup>th</sup> tranche would be awarded to each of the 3 tied bidders.
5. Bids would be opened on their due date, winners selected, and the Commission would approve the results within one business day. The enrollment period would commence the next business day following Commission approval.
6. Enrollments would be conducted during the (presumably 30-day) enrollment period.
7. APPLICABLE ONLY IF THE THRESHOLD CONDITION IS MET (the wholesale market price exceeded the day-of-bid price by 5% or more for 10 or more days). Suppliers who won tranches but specified a maximum number of customers less than the size of a tranche would be allowed to invoke that maximum. The remaining customers (tranche size minus supplier maximum) would be offered to suppliers whose bid did not contain a maximum or whose maximum was greater than the actual tranche size. Priority would be given in the order of bids in the stack (first priority to best bid, etc.). In the extremely unlikely event that some customers who had enrolled are left unchosen by all suppliers, then the last enrollees would be placed on a waiting list (or alternatively, denied enrollment).

Example: 10 tranches of 100,000 customers each are awarded to winning suppliers “1” through “10”, numbered in the order of the ranked bids. Supplier 3’s bid contains an 80,000 customer maximum, invocable only if the threshold condition occurs, which it does. Supplier 3 chooses to accept only the 80,000 maximum, leaving the remainder of tranche 3 (20,000) to be allocated to other suppliers. Supplier 1 is offered the remaining 20,000 and accepts 10,000. Supplier 2 is offered the remaining 10,000 and accepts all 10,000. Process is concluded.

Spark Energy thanks the Commission for its consideration of these comments.

Sincerely,

A handwritten signature in black ink, appearing to read "Harry Kingerski". The signature is fluid and cursive, with a small mark above the "i" in "Kingerski".

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