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August 30, 2016

**Via Electronic Filing**

Rosemary Chiavetta, Secretary  
PA Public Utility Commission  
P.O. Box 3265  
Harrisburg, PA 17105-3265

Re: Proceeding to Evaluate Transition to Corrected Non-Solar Tier I Calculation  
Methodology, Docket No. M-2009-2093383

Dear Secretary Chiavetta:

Enclosed for electronic filing please find the Comments to the Tentative Order dated August 15, 2016 of the Retail Energy Supply Association ("RESA") with regard to the above-referenced matter.

Sincerely,



Deanne M. O'Dell

DMO/lww  
Enclosure

cc: Scott Gebhardt, TUS, w/enc. (via email only)  
Kriss Brown, Law Bureau, w/enc. (via email only)

**BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Proceeding to Evaluate Transition to :  
Corrected Non-Solar Tier I Calculation : Docket No. M-2009-2093383  
Methodology :

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**COMMENTS OF  
THE RETAIL ENERGY SUPPLY ASSOCIATION  
TO TENTATIVE ORDER ENTERED AUGUST 15, 2016**

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Date: August 30, 2016

**TABLE OF CONTENTS**

- I. INTRODUCTION ..... 1**
- II. COMMENTS ..... 3**
  - A. Impact Of The Quarterly Adjustment Obligation Increase On EGSs ..... 3**
    - 1. Likelihood Of Cost Recovery From Former Customers Or Existing Customers Is Low ..... 5
    - 2. Embedding The Costs Of This Increase In Current Contracts Will Skew Market Prices And Create A Competitive Disadvantage For EGSs ..... 7
  - B. Recommended Solution 1: AEC Procurement & Non-Bypassable Cost Recovery by the EDC ..... 8**
    - 1. AEC Procurement And Non-Bypassable Cost Recovery By The EDC Is The Preferred Option Because It Fairly And Equitably Recovers The Unanticipated Costs From All Customers ..... 8
    - 2. Implementation Suggestions ..... 9
  - C. Recommended Solution 2: Delay True-Up Period ..... 10**
- III. CONCLUSION ..... 10**

## I. INTRODUCTION

Pursuant to its Tentative Order entered August 15, 2016, the Commission seeks comments on remedial actions that can be taken to minimize the effect on the market of requiring all electric distribution companies (“EDCs”) and electric generation suppliers (“EGS”) to determine how to recover the costs of an unexpected seven percent increase in a portion of the non-solar Tier I obligations. The compliance obligations are required by the Alternative Energy Portfolio Standards (“AEPS”) Act<sup>1</sup> and the Electricity Generation Customer Choice and Competition Act,<sup>2</sup> but the unanticipated seven percent increase is the result of correcting an error in how the obligations have been calculated. Recognizing the potential adverse impact to the market of this unanticipated increase if no remedial action is taken, the Commission’s Tentative Order recommends two possible solutions and invites comments from interested stakeholders. The first recommended solution would require the EDC to procure the AEC credits, transfer them to all load serving entities (“LSEs”) and then recover the costs through a preexisting non-bypassable charge. The second recommended solution would delay the compliance true-up period. Both of these solutions are narrowly focused on the portion of the non-solar Tier I obligations resulting from the flawed calculations and not the “base” AEPS obligations related to solar Tier I and Tier II requirements.

The Retail Energy Supply Association (“RESA”)<sup>3</sup> is a trade association of competitive suppliers many of which are licensed in Pennsylvania and will be directly impacted by the

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<sup>1</sup> 73 P.S. § 1648.3.

<sup>2</sup> 66 Pa. C.S. § 2814(c).

<sup>3</sup> The comments expressed in this filing represent the position of the Retail Energy Supply Association (RESA) as an organization but may not represent the views of any particular member of the Association. Founded in 1990, RESA is a broad and diverse group of more than twenty retail energy suppliers dedicated to promoting efficient, sustainable and customer-oriented competitive retail energy markets. RESA members operate throughout the United States delivering value-added electricity and natural gas service at

unanticipated increase in a portion of their non-solar Tier I AEPS compliance obligations for 2016. RESA fully supports the Commission's recognition that remedial action is necessary, and the Commission's decision to narrow such remedial action to just the portion of non-solar Tier I AEPS compliance obligations impacted by the flawed calculation is reasonable. As explained below, EGSs had no reason to anticipate that the increased costs of AEPS compliance resulting from correcting a mathematical error and, therefore, did not factor these costs into retail pricing. Without remedial action, the only option available to EGSs is to embed the costs in new contracts going forward which will skew market prices and create a competitive disadvantage for EGSs.

Upon consideration of the two solutions set forth in the Tentative Order, RESA supports AEC procurement and non-bypassable cost recovery by the EDC as the optimal way to fairly and equitably recover the unanticipated costs of correcting the flawed calculation of AEPS requirements from all customers and recommends that it be implemented for the 2017 and 2018 compliance years as well as the 2016 compliance year. If, however, the Commission elects to delay the true-up period, then RESA recommends that the delay would need to extend until at least the 2018 AEPS compliance year to provide any meaningful relief.

RESA commends the Commission for taking proactive steps to recognize the potential negative market impacts of correcting the erred calculations and offering viable solutions intended to mitigate the resulting harm. RESA appreciates the opportunity to provide comments on these issues.

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retail to residential, commercial and industrial energy customers. More information on RESA can be found at [www.resausa.org](http://www.resausa.org).

## II. COMMENTS

### A. Impact Of The Quarterly Adjustment Obligation Increase On EGSs

In its Tentative Order, the Commission requests comments on how best to mitigate the potential negative market impacts of correcting the flawed calculations related to AEPS compliance obligations as required by Act 129.<sup>4</sup> As set forth in its August 9, 2016 Secretarial Letter, the Commission has appropriately narrowed this proceeding to addressing the unanticipated seven percent increase in the non-solar Tier I requirement. Unlike the “base” AEPS compliance requirements that EGSs would have been able to reasonably anticipate, the error amount could not have been reasonably anticipated. If the Commission does not implement one of the proposed solutions set forth in its Tentative Order, addressing the impact of this unanticipated increase in AEPS obligations presents significant issues due to the manner in which EGSs recover the costs of AEPS compliance.

Ideally, the costs of a specific AEPS compliance year are recovered from all the EGS’ customers who received power from that EGS during that specific AEPS compliance year. In order for an EGS to accomplish this, prior to entering into a contract with a retail customer, the EGS will calculate (at least within a reasonable margin of error) the expected cost of AEPS compliance for a particular period and then factor the estimated cost into the contract price that aligns with the AEPS compliance period. The EGS will rely upon the information provided by the AEPS Administrator in making these pricing decisions. Further, EGS retail contracts have varying start dates and varying terms that do not always align with AEPS compliance years,

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<sup>4</sup> Tentative Order at 1. The “Act 129” adjustments are set forth in 66 Pa C.S. § 2814(c) which was adopted as part of amendments to the Electricity Generation Customer Choice and Competition Act commonly referred to as “Act 129.”

which also makes transparent and timely information about AEPS compliance obligations critical.

Prior to the 2016 AEPS compliance year, the impact of the Act 129 adjustments on total Tier I requirements was available on a quarterly basis and, since the inception of AEPS, the final requirements for the compliance year as established during the true-up period has not varied significantly from projections. As a result, EGSs were in a position to reasonably estimate the costs of AEPS compliance and these estimates were accordingly priced into retail contracts. Any variances between estimated and actuals, due to their insignificance over the years, were easily managed through the nominal purchase of additional AECs, banked AECs or alternative compliance payments. As such, the base AEPS compliance requirements have been anticipated by EGSs and factored into EGS retail contracts that were in place during the applicable compliance period. Therefore, and consistent with the Commission's approach here, limiting the remedial actions under discussion here to the portion of the non-solar Tier I obligations that were not calculated properly is reasonable.

Determining how to address the costs of the seven percent increase resulting from the flawed calculations and similar increases for all subsequent compliance years imposes a significant and unexpected cost obligation for EGSs. EGSs pricing contracts for power flow starting with the 2016 compliance year had no reason to anticipate such a significant increase in obligations. As such, they would not have incorporated these calculations into retail contracts for supply terms inclusive of compliance period 2016 and beyond. As discussed further below, the likelihood of EGSs recovering the unanticipated AEPS compliance costs from customers who received power during 2016 and future compliance period is low. Without Commission adoption of a solution, the only other option available to EGSs – to embed the costs in new

contracts going forward – will skew market prices and create a competitive disadvantage for EGSs.

**1. Likelihood Of Cost Recovery From Former Customers Or Existing Customers Is Low**

As discussed above, EGSs normally recover the costs of AEPS compliance by including all anticipated AEPS compliance costs applicable to the contract supply term in the pricing to customers. These pricing determinations are made by EGSs in advance of entering into a contract based on the reasonably expected AEPS compliance costs. For the 2016 compliance year, however, EGSs could not have reasonably anticipated the increased costs resulting from the flawed calculations. Since the AEPS 2016 compliance year runs from June 1, 2015 through May 31, 2016, there are several difficulties regarding the ability of the EGS to recover the unanticipated AEPS costs from those customers who were with the EGS during the 2016 compliance year.

First, many of the customers who received power from an EGS during the 2016 compliance year may not be current customers of the EGS. EGSs enter into contracts with customers of varying lengths. EGSs also lose customers who elect to cancel their contracts. An EGS has no ability to recover the unanticipated 2016 compliance costs from former customers.

Second, for a subset of mass market customers who entered into contracts with the EGS for supply terms including 2016 and beyond and happen to still remain customers of the EGS, the *Fixed Price Label Order* places practical constraints on the ability of EGSs to recover the unanticipated increased costs of AEPS compliance.<sup>5</sup> This is because an EGS offering a fixed

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<sup>5</sup> *Guidelines for Use of Fixed Price Labels for Products With a Pass-through Clause*, Docket No. M-2011-2362961, Final Order entered November 14, 2013 (“*Fixed Price Label Order*”).

price product cannot adjust the contract during the term to recover costs such as those here – regardless of whether or not such right is reserved in the contract.<sup>6</sup> EGSs also cannot rely on a “regulatory out” clause in the contract to recover the cost from the fixed price customer because the *Fixed Price Label Order* requires an EGS dealing with an unpredicted increase in costs (that it did not already factor into the fixed price product) to provide the customer prior notice of the EGS’s intent to pass on the charge to the customer. If the customer does not affirmatively agree to the price increase, then the EGS must cancel the contract. The likely outcome of this action is for the EGS to lose the customer. For all these reasons, the practical impact of the *Fixed Price Label Order* for the competitive market is that it limits the ability of EGSs to recover the costs of the unanticipated 2016 AEPS compliance from existing mass market customers.

Third, EGSs that have acquired customers through the various standard offer customer referral (“SOP”) programs of the utilities are required to offer a price that is 7% off the then-effective price-to-compare (“PTC”) and they must maintain that price during the twelve-month term of the SOP contract. Thus, EGSs cannot pass on the unanticipated increased AEPS costs to existing SOP customers. Also important is that EGSs consider a number of factors in deciding whether or not to participate in an EDC’s SOP program. These decisions include the overall financial impact of doing so which necessarily includes factoring in the costs of compliance with the AEPS Act. In part because SOP requires a 7% discount off the PTC, the margins are already slim-to-none for EGSs to participate in SOP. As a result, if EGSs are required to recover the unanticipated costs regarding the 2016 AEPS compliance year, this will have to be factored into their decision about whether or not to participate in SOP going forward. The greater the costs

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<sup>6</sup> *Fixed Price Label Order* at 24 (“a ‘fixed price’ product must not change in price during the term of the agreement”).

imposed on EGSs to meet this obligation, the less likely they will be able to participate in SOP. Moreover, since the cost of an individual EGSs' AEPS compliance is based on the amount of electric energy sold by the EGS,<sup>7</sup> adding new customers to the EGS through SOP increases the amount of the compliance obligation which is another factor that EGSs will have to consider as they contemplate future participation in SOP.

For all these reasons, EGSs are significantly limited in their ability to recover the costs of the unanticipated AEPS compliance from the customers that were under contract with the EGS during the compliance period. Moreover, the increased costs of compliance may negatively impact the ability of some EGSs to participate in the SOP programs of the EDCs.

**2. Embedding The Costs Of This Increase In Current Contracts Will Skew Market Prices And Create A Competitive Disadvantage For EGSs**

If the Commission were to take no remedial action, EGSs would have no choice but to embed into new contracts the costs of unanticipated AEPS compliance obligation. This is true regardless of whether an EGS uses banked AECs, elects to pay an alternative compliance payment or purchases AECs to meet its obligations. All of these actions have costs which the EGSs will seek to recover from customers. Given the difficulties discussed above, embedding these costs in new contracts will misalign the time period in which the obligation occurred and the time period in which EGS provided power to the customer. Thus, the competitive price of energy for tomorrow's contracts will be higher because they are factoring in an obligation from a prior period. Moreover, EDCs will recover the costs of this unanticipated compliance obligation through various reconciliation mechanisms in their PTC. Given the timing of these changes, it is likely that EDCs and EGSs will not be factoring in these costs at the same time. EGSs will need

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<sup>7</sup> 73 P.S. § 1648.3.

to factor in the costs immediately in their new contracts. If the EDC reconciliation mechanisms result in a lag before the costs are included in the PTC, then the EGS pricing is at a competitive disadvantage based on a comparison with the prevailing PTC.<sup>8</sup>

Moreover, as Pennsylvania's competitive market evolves, it is important to remember that not all EGSs operating in the marketplace today provided competitive supply to customers during the AEPS 2016 compliance year. Some of these EGSs may not have even been licensed yet to provide service during that time period. Requiring these EGSs to pay increased costs now for load that they did not serve would unreasonably increase the costs to these EGSs of providing service in Pennsylvania which could negatively impact the business plans of these companies and their ability to provide future service to customers.

**B. Recommended Solution 1: AEC Procurement & Non-Bypassable Cost Recovery by the EDC**

**1. AEC Procurement And Non-Bypassable Cost Recovery By The EDC Is The Preferred Option Because It Fairly And Equitably Recovers The Unanticipated Costs From All Customers**

In its Tentative Order, the first remedial option offered by the Commission is to require the EDCs to procure the needed AECs for their service territory to cover the unanticipated increased requirements and then recover the costs of this procurement through a preexisting non-bypassable charge.<sup>9</sup> The additional AEPS compliance obligations recovered in the non-bypassable charge would be for the incremental requirement resulting from the flawed calculation and applicable to all LSEs – including both EGSs and EDCs. RESA supports this approach as the optimal solution for a number of reasons.

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<sup>8</sup> While RESA does not support comparison of EGS pricing to the PTC as an appropriate measure of the market price of energy, the reality in Pennsylvania today is that consumers do make those comparisons.

<sup>9</sup> Tentative Order at 5.

First, this approach equitably distributes the costs of the unanticipated AEPS compliance requirement among all customers – regardless of whether they are currently shopping or not. This addresses the issues discussed in the prior section regarding the inability of EGSs to recover these costs from customers they were serving during the 2016 compliance period.

Second, this approach maintains consistency in the underlying cost obligations between competitive supply service and default service. It addresses concerns about distorted price signals that would result from disparate timing between when EDCs reflect this cost in the default service rate and when EGSs reflect this cost in contract pricing. The Commission has already acknowledged the negative impacts on the competitive retail market when the default service product does not reflect current market conditions.<sup>10</sup> Further exacerbation of this issue can be avoided by implementing this proposed solution.

## **2. Implementation Suggestions**

In its Tentative Order, the Commission appears to focus on remediating the impacts of the flawed calculation for the 2016 compliance year only. Importantly, though, prior to the announced AEPS calculation error, EGSs had already entered into contracts for power flow dates well beyond the 2016 AEPS compliance year (which ended on May 31, 2016). Thus, EGSs are still at financial risk for forward contracts signed prior to the announced AEPS calculation error and many of these contracts extend into 2017, 2018, and beyond. Price distortions, too, between EGS prices and the PTC will likely extend into 2017 and 2018. Therefore, RESA supports requiring the EDCs to procure the needed AECs for their service territory to cover the

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<sup>10</sup> *Investigation of Pennsylvania's Retail Electricity Market: End State of Default Service*, Docket No. I-2011-2237952, Final Order entered February 14, 2013 at 13-14 (Commission discusses how PTC artificially drives EGS decisions and the “boom-bust” cycle.)

unanticipated increased requirements and then recover the costs of this procurement through a preexisting non-bypassable charge for the 2017 and 2018 compliance years as well as the 2016 compliance year. This would address any issues the unanticipated seven percent increase would have on an EGS that entered into a three-year contract based on incorrect pricing that did not reflect the unexpected AEPS compliance adjustment.

For all the reasons discussed above, AEC procurement and non-bypassable cost recovery by the EDC is the optimal way to fairly and equitably recover the unanticipated costs of correcting the flawed calculation of AEPS requirements from all customers.

### **C. Recommended Solution 2: Delay True-Up Period**

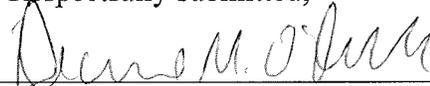
Pursuant to this recommendation, the Commission proposes that EGSs would be allowed a number of additional years to procure and retire the AECs needed to comply with the incremental seven percent increase in the AEPS obligation for the 2016 compliance period. This would allow EGSs the time necessary to collect the increased costs associated with the 2016 compliance year from future EGS customers. While the Tentative Order notes that the appropriate time period can include compliance by the presently set November 30, 2016 deadline, to be effective, the period of delay would need to be longer to give EGSs time to factor in the increased costs in future contracts. As noted above, EGSs currently have contracts with customers that extend into 2017, 2018 and beyond. Thus, the delay in true-up period would at a minimum need to extend until at least the 2018 AEPS compliance year to provide any meaningful relief.

## **III. CONCLUSION**

While the error in calculating AEPS obligations is unfortunate and imposes unanticipated cost obligations on EGSs that cannot easily be recovered from customers, RESA appreciates the Commission's efforts in the Tentative Order to open a discussion about potential remedies to

mitigate the impact of the error. Without adoption of a solution such as one of the ones described in the Tentative Order, EGSs will have no other option but to embed the unanticipated increased AEPS compliance costs in new customer contracts going forward which will skew the market prices and create a competitive disadvantage for EGSs. Upon consideration of the two recommended solutions, RESA supports AEC procurement and non-bypassable cost recovery by the EDC as the optimal way to fairly and equitably recover the unanticipated costs from all customers and recommends that it be implemented for the 2017 and 2018 compliance years as well as the 2016 compliance year. If, however, the Commission elects to delay the true-up period, then RESA recommends that the delay extend until at least the 2018 AEPS compliance year to provide meaningful relief. Importantly, though, implementing either of the Commission's recommended solutions is necessary to address the potential negative impacts to the market of requiring EGSs to embed the costs of this error into future contracts.

Respectfully submitted,



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