BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Rulemaking Re Electric Distribution Companies' Obligation to Serve retail Customers at the Conclusion of the Transition Period Pursuant to 66 Pa.C.S. § 2807(e)(2)	:	Docket No. L-00040169
Default Service and Retail Electric Markets	:	Docket No. M-00072009

REPLY COMMENTS OF THE
OFFICE OF CONSUMER ADVOCATE

Tanya J. McCloskey
Senior Assistant Consumer Advocate
PA Attorney I.D. # 50044
E-Mail: TMcCloskey@paoca.org

Counsel for:
Irwin A. Popowsky
Consumer Advocate

Office of Consumer Advocate
555 Walnut Street
5th Floor, Forum Place
Harrisburg, PA 17101-1923
Phone: (717) 783-5048
Fax: (717) 783-7152

Dated: March 23, 2007

TABLE OF CONTENTS

I. INTRODUCTION

On March 2, 2007, the Office of Consumer Advocate (OCA) and many other interested parties filed Comments regarding the Commission's Advance Notice of Final Rulemaking (ANOFR) regarding its default service regulations and its proposed Policy Statement (Policy Statement Order) intended to provide guidelines for the procurement of default service supply under the regulations. In its Comments, the OCA supported the Commission's direction of encouraging the default service provider to acquire a portfolio of resources designed to provide the lowest reasonable long-term cost for default service. It is clear to the OCA that, for residential customers, default service will remain the primary means by which essential electric service is made available on reasonable terms and conditions. A least cost procurement standard for resources acquired from the wholesale markets, similar to that for the procurement of natural gas supply, will allow these customers to share in the benefits of the competitive wholesale generation market, even if they are unable to choose a retail supplier. It is the OCA's view that residential customers should not be forced to switch to other competitive retail suppliers in order to obtain the benefits of the competitive wholesale generation markets that were made available to them through the Electricity Generation Customer Choice and Competition Act (Act).

The Comments of the interested stakeholders reveal that both customers of this essential default service and those providing the service, the electric distribution companies (EDCs), express the same overall goal – using the competitive wholesale generation markets to provide customers with service at reasonable rates. Differences exist as to the best method for procuring this supply in those markets, and concern has been expressed as to the application of the standard for assessing the result of the procurements. It is the OCA's view that these differences and concerns are not insurmountable.

As to the concern regarding the Commission's proposed regulation that the portfolio of procured resources be designed to provide the lowest reasonable long-term cost to customers, the OCA submits that this standard is consistent with both the language of and the goals of the Act. The OCA agrees with those commenters who caution against applying this standard through after-the-fact prudence reviews or comparisons of the portfolio price to short term or spot market price. A procurement plan that has been approved and purchases that have been made in implementing that approved plan should not be second guessed. Additionally, those purchases should not be compared to short term or spot changes in market prices. Nevertheless, it must be recognized that the goal of the default service plan is to provide long-term, stable and reasonable prices for reliable electric service. There is nothing inconsistent, though, in the goal of achieving the lowest long term costs for consumers while acquiring the portfolio of resources to achieve that goal at prevailing market prices for the products acquired in the competitive wholesale markets.

The Commission's approach to requiring the development of a default service procurement plan will also allow for a variety of methods to be utilized as the competitive wholesale markets continue to develop. The OCA strongly supports the use of a portfolio approach, and experience with this approach by Pennsylvania's natural gas companies in purchasing natural gas supply, and by Duquesne Light Company and UGI-Electric Company in purchasing default electric service supply, speak to the benefits of such an approach. The portfolio approach will allow a variety of procurement methods to be utilized, and as we gain experience with these methods, and as the wholesale markets develop, the most effective and efficient procurement methods within the portfolio will evolve.

The commenters have made a number of suggestions or provided clarifications with which the OCA agrees. As an initial matter, the OCA agrees that the effective date of the proposed regulations and proposed policy statement should be established for default service beginning on and after January 1, 2011 so that existing default service plans, and purchases made to support default service, can be provided the necessary certainty, and so that all settlements, including restructuring settlements, can be fully honored. With a certain effective date, EDCs can begin to plan to meet their obligation in accordance with the regulations beginning with that date.

Some commenters have also echoed the OCA's concerns regarding rapid changes in rate design. See, *e.g.*, PECO Comments at 10-12. Changes in rate design can compound the effect of what may already be significant rate increases for various customer classes. The recent experience in Illinois, where electric heating customers saw increases of 100% or more, as compared to the average increase of 40% to 55%, because of rate design changes urges caution in this approach. See, *Electric Bills Jolt Many In Illinois*, Chicago Tribune of February 27, 2007. Moving to a flat, uniform cents/kwh rate for all customers under all circumstances also may not properly reflect the cost to serve the customers within the class. As PECO notes, "rate classes, no matter how carefully drawn, invariably include customers with markedly different usage characteristics." PECO Comments at 10-11. Rate designs other than a flat, uniform cents/kwh should continue to be permitted when cost justified. Additionally, if existing rate designs are eliminated, they should be phased out over time to avoid significant disruptions, particularly for customers that have invested significantly in systems and equipment based on the rate offerings of the utility.

The electric distribution company (EDC) commenters and the consumer commenters, including the Office of Small Business Advocate (OSBA) and Industrial Energy Consumers of Pennsylvania (IECPA), also identified concerns with the Commission's proposal that certain costs be unbundled from distribution rates and included in the default service rates. See, *e.g.*, UGI-E Comments at M-00072009 at 2-3; Citizens/Wellsboro Comments at 4-5; OSBA Comments at 9-10; IECPA Comments at M-00070183 at 16-17. As noted by the OCA and these other commenters, the only costs that should be assigned to default service are those costs that are avoidable when a customer purchases supply from an alternative supplier. See, *e.g.*, OSBA Comments at 9-10; Citizens/Wellsboro Comments in M-00070183 at 4-5. Additionally, as noted by some commenters, many of the costs identified by the Commission may not need to be included in the default service rate because similar costs are already included in the wholesale prices bid by the supplier (and used as the basis of the retail rate). Since the wholesale bidder must include all costs associated with providing service in their bids in order to recover those costs, the bid price already reflects these cost elements. Citizens/Wellsboro Comments in M-00070183 at 4. For example, each bidder will incur administrative costs in preparing the bid and will reflect these costs as part of its bid price to recover those costs. At this time, particularly before the end of the rate cap period for many EDCs, there seems to be little reason, or justification, for mandating a further unbundling of costs from distribution rates.

Finally, many of the electric generation supply (EGS) commenters continue to call for changes in default service that would, in the OCA's view, make that service more volatile and expensive. RESA Comments at 7-13; Direct Energy Comments at 3-5; Dominion

Retail Comments at 4-5; Reliant Energy Comments at 5, 11-12; NEM Comments in M-00072009 at 4-9. The proposals for volatile and expensive default service do not reflect Pennsylvania law, nor do they reflect the fact that electric service is an essential service necessary for the health, well-being of the residents of this Commonwealth and for the economic vitality of the Commonwealth. Proposals to move toward such volatile and expensive models for electric service should be rejected outright by the Commission so that there is no further waste of resources on these types of proposals.

The OCA has provided a thorough discussion of its position in its Comments filed on March 2, 2007, and in its prior Comments filed in this rulemaking. The OCA will highlight a few key areas in these Reply Comments, but will not repeat its comments on the many areas addressed by the proposed regulations and proposed Policy Statement. The OCA will focus its Reply Comments on the propriety of the lowest reasonable long-term cost standard, the use of a portfolio of resources, the need for bilateral contracts in securing a reasonable portfolio, the need for stable pricing, and the inadvisability of adopting proposals for volatile and expensive default service.

II. REPLY COMMENTS

A. The Lowest Reasonable Long Term Cost Standard Is Consistent With Statutory Requirements.

In its proposed regulations, the Commission has established that the default service procurement plan should be designed to acquire electric generation supply to meet the DSP's default service obligation at the lowest reasonable long-term cost. Proposed Regulation §54.186(b)(1). The OCA strongly supports this least cost procurement standard. Several commenters have raised concerns, however, that this proposed regulation introduces a new standard not contained in the Act or that the proposed regulation is inconsistent with the prevailing market prices standard in the Act. PECO Comments at 6; FirstEnergy Comments at 3, 7; PPL Comments at 11. Of particular concern to some of the EDC commenters is the possibility for after-the-fact prudence reviews of purchasing decisions or contract prices. The major concern expressed is that the default service prices that result from the acquisitions under the default service plan in prior periods would be considered imprudent if current market prices are lower.

The OCA agrees that the reasonableness of the default service price should not be based on any after-the-fact comparison to short term market prices or changes in market price after the conclusion of the procurement process. The OCA also agrees with the need for certainty in the default service rates if the EDC is acting in accordance with its approved default service plan. That does not mean, however, that the goal of the default service provider should not be to provide service at the lowest reasonable long-term cost.

The OCA submits that the requirement in the Act that a DSP acquire energy at prevailing market prices is not inconsistent with a standard that such acquisitions be designed to provide default service at the lowest reasonable long-term cost. As the OCA and many other commenters note, there are many products and services in the wholesale competitive market that can be used to provide reasonably priced, stable and reliable default service. It is the portfolio of these products and services and the prevailing market prices for acquiring them that go into making up the cost of default service. The Commission regulation sets the standard for determining what products and what services should be acquired at the prevailing market prices. Given the plural nature of the term "prevailing market prices" used in the Act, the OCA submits that the Commission's proposed regulations and proposed Policy Statement properly set forth the standard for the acquisitions. In other words, as the Default Service Provider assembles its portfolio by purchasing products at their respective prevailing market prices, the provider should do this with the overall goal of securing the portfolio that produces the lowest long-term cost. There is no conflict between acquiring resources at their respective prevailing market prices and the overall goal of assembling the lowest cost long-term portfolio.

Several EDC commenters also expressed concern with after-the-fact prudence reviews under the Commission regulations. The OCA recognizes the concern with the potential for looking back, or second guessing, decisions. The OCA agrees that it would not be an appropriate application of the Commission's standard to make an after-the fact review of procurements made in accordance with an approved plan by comparing the price of the contract with the current short-term wholesale market price. The OCA also agrees that it is not proper to assess the reasonableness of the price of default service based on current, or short-term market prices, particularly since the nature of this service – a reliable, stable service that must be provided to all requesting customers – is very different than service based on short term or spot prices.[1]

As noted, the goal of default service is to procure the lowest reasonable long-term cost for the service being provided – reliable, stable default service. Under the Commission's proposal, it will approve an EDC's default service procurement plan, and the EDC will be expected to implement its acquisitions in accordance with the plan. It is the OCA's understanding of the proposal that unless there are significant changes in circumstances, EDCs will follow the pre-approved plan and Commission review would be minimal. The OCA also anticipates that EDCs may ask the Commission to approve certain procurements, such as long-term contracts, at the time the EDC enters into these agreements.

The OCA agrees in this regard with UGI-Electric (UGI-E), which provided an important clarification for any review process when it stated:

> While UGI believes the Commission should appropriately retain its right to investigate violations of laws or regulations, it should clarify that it will not re-review the reasonableness of purchases accurately disclosed to and approved by the Commission. This will ensure power purchases can be made with reasonable confidence that cost recovery will not subsequently be denied.

UGI-E Comments at 10.

The OCA agrees that the focus of the Commission's efforts should be on ensuring that the default service portfolio and procurement plan is designed to meet the standards established for default service, and that the procurement methods are designed to provide the lowest long-term prices which in turn will reflect the combination of the prevailing market prices

[1] That is not to say that a DSP should be so locked into a procurement plan that it cannot make a prospective adjustment to respond to external events. If, for example, the plan called for a major solicitation on the day following a national or international event that would disrupt market prices or cause short term aberrations in market price, the EDC would not be expected to proceed with the procurement knowing of these impacts. In that situation, the EDC may need to delay the solicitation or consider and propose a change in the procurement plan.

for the products and services that are acquired in the markets. Second guessing based on short term changes in market prices should not be permitted and it is the OCA's understanding that this is not what the Commission proposed in its regulations.

B. The Portfolio Approach Provides A Reasonable Means Of Managing The Default Service Obligation.

Through its proposed Policy Statement and proposed Regulations, the Commission has encouraged the use of a portfolio approach to managing the default service obligation in a manner that will provide the lowest reasonable long-term cost for default service. The OCA supports the use of a portfolio approach for acquiring resources needed to meet the default service obligation. The portfolio approach allows the DSP to hedge against a number of risks by acquiring its supply through a variety of methodologies, over reasonable periods of time, and through the use of diverse resources and diverse contract terms and lengths.

While many of the EDC commenters recognized the importance of procuring supply across differing time periods, some of the EDCs recommended the use of statewide, or limited resource, auction processes rather than the use of a broader portfolio approach. See, *e.g.*, PPL Comments at 8; PECO Comments at 4. Smaller EDCs, while not disagreeing with the benefits of a portfolio, expressed concern about their ability to cost-effectively manage a portfolio for their very small loads. Citizens/Wellsboro Comments in L-00040169 at 2-3. Other EDCs, particularly UGI-Electric and Duquesne Light Company, supported the use of a portfolio approach, providing comments on their success with such an approach as their rate caps expired. UGI-E Comments at 1-3; Duquesne Comments at 1-3. The OCA submits that a portfolio approach can accommodate these differences while providing many benefits for customers.

UGI-Electric, an EDC with a natural gas company affiliate that provides retail natural gas service, most appropriately recognized the important lessons to be gained from the natural gas industry. As UGI noted:

> Since 2002, when UGI terminated its recovery of Competitive Transition Costs and exited out from under the statutory rate caps established under 66 Pa.C.S. §2804(4), UGI has successfully procured default service power supplies for its customers by constructing a portfolio of energy supplies in a manner that enables it to respond to changes in market conditions and to mitigate both short-term price volatility and supplier default risks. This successful approach was based, in part, on UGI's long experience in procuring natural gas supplies through a portfolio approach in wholesale markets for the customers of its gas division.

UGI-E Comments at 1-2.

By using a portfolio of purchases, there are many options available to address the various risks of providing default service, including the risks of rapidly changing markets. UGI-E further explained the many options that are available to a DSP when constructing a portfolio:

> In constructing a portfolio of supplies under a portfolio approach a DSP may elect to purchase blocks of power to meet loads that are certain, and may consider a number of different options to meet potential loads that are not known in advance and may depend on customer switching rates, weather or other factors. Alternatives may include purchasing blocks of power with the expectation of selling into the wholesale market during low-load periods, purchasing options (thereby minimizing the risk of market losses if power is not needed and wholesale prices are low), other financial products that may minimize the price risk of spot market purchases or the purchase of load following service.

UGI-E Comments at 5-6. There are many factors to be addressed in procuring supply for default service customers. A portfolio approach allows the DSP to manage these risks and respond to changes in the markets. Combined with the reconcilable cost recovery mechanism, as is used in the natural gas industry, the risk is able to be managed at a reasonable cost.[2]

The OCA remains concerned with an approach that prescribes sole reliance upon mechanistic auctions or RFPs that procure full requirements, load following supply on specified dates. See, *e.g.*, PPL Comments at 8; PECO Comments at 4-5. While such procurement processes may be appropriate for use in acquiring *portions* of any portfolio, the sole reliance on only this form of procurement method, and one form of contract, is not likely to provide default service at the lowest reasonable long-term cost. Supporters of this approach look mainly to New Jersey's laddered contracts with a descending clock auction approach. But New Jersey, after several years experience with this approach, is now reconsidering this model. By Order entered December 22, 2006, the New Jersey BPU directed its staff to convene a working group to consider the use of a portfolio approach for meeting the Basic Generation Service requirements for the fixed price service (BGS-FP). The Board indicated that the working group should consider the use of long term contracts for greater price stability, and the use of demand side resources and renewable energy to provide a positive impact for all customers. In the Matter of the Provision of Basic Generation Service for the Period Beginning June 1, 2007, Dkt. No. EO06020119 (Order entered Dec. 22, 2006)(New Jersey Order). In considering a proposal to use a portfolio approach, the Board stated that:

> [A] working group should be created to study how a portfolio of resources could be created for the BGS-FP service that could provide greater price stability for BGS-FP customers. If other longer-term resources are available, and if it is feasible and economic to do so, longer term resources could be added to the BGS-FP supply mix. Further, the Board agrees that the working

---

[2] West Penn Power raised the issue of including a return in the default service rate due to the risks inherent in this service. If an EDC uses a reconcilable recovery mechanism for the recovery of costs associated with providing the service, there is no basis to include a return component in the rate. With a fully reconcilable recovery mechanism, all risk is transferred to the customers.

> group should consider a portfolio approach that includes the use of demand side resources as part of the BGS-FP supply mix with the goal of reducing suppliers' peak resource needs thereby having a positive impact for all consumers.

New Jersey Order at 7. It appears that New Jersey may now be considering a move toward the portfolio approach for the small customer classes, such as the residential class, that is being utilized in other states such as Delaware, Rhode Island, and Maine. See, OCA Comments at 59. The OCA does not think that Pennsylvania should now rely wholly on a mechanistic auction approach that is being reconsidered in some of the states that have tried it.

One issue raised by the smaller EDCs with the portfolio approach is the possible difficulty of a very small utility implementing a portfolio approach in a cost-effective manner. The OCA recognizes that some small utilities, such as Citizens and Wellsboro, may not have sufficient load to assemble a full "portfolio" of resources as a larger utility might be able to do. See, *e.g.*, Citizens/Wellsboro Comments in L-00040169 at 2-3. Citizens and Wellsboro, however, have been able to procure necessary supply to meet their obligations through the use of Requests for Proposals that they issue when market conditions warrant. While not the same type of full portfolio that a larger utility may be able to secure, the OCA agrees that it is this type of individualized planning and flexibility in procurement process that should be permitted as the Commission implements its regulations. As the OCA has stated, a one size fits all approach may not be appropriate for the Commonwealth with the diversity of EDCs and EDC service territories.

The OCA would also note that through a portfolio approach, EDCs can utilize demand side resources as one means of providing service at the lowest reasonable long-term cost. PennFuture explained the benefits of a "true portfolio approach" that includes renewable resources, energy efficiency, demand-side and generation sources to hedge against volatile fossil fuel prices. As to the role of energy efficiency in the portfolio, PennFuture added:

> Including an energy efficiency requirement will not only lower costs to electric consumers, but will also reduce the strain placed on our electric transmission and distribution system, mitigating the need for costly repairs and increasing overall reliability.

PennFuture Comments at L-00040169 at 1.

The OCA continues to support the Commission approach of encouraging the use of a broad portfolio of resources that may include both long-term and short-term contracts, both renewable and non-renewable generation, and both supply side and demand side resources. The OCA agrees that auctions and contracts for load-following supply can be part of the portfolio of resources and procurement processes. But for those EDCs with larger loads, the OCA submits that sole reliance on such processes is not the best way to achieve reasonably priced default service over the long-term.

C. A Variety of Procurement Methods Should Be Allowed

In its Comments, the OCA supported an approach that provides the DSP with a variety of procurement methods to secure the resources needed to meet the default service obligation. In the OCA's view, included among these procurement methods should be the use of bilateral contracts negotiated at arms-length with non-affiliated generation owners as one means of procuring supply to meet the default service obligation. Several other commenters also discussed the benefits of bilateral contracts in meeting the obligation to provide default service at the lowest reasonable long-term cost. Duquesne Comments at 8-14; IECPA Comments at 4. The OCA continues to support the use of bilateral contracts as one method of securing supply. Bilateral contracts are a significant part of the competitive wholesale markets, and are a useful tool in acquiring supply to meet the default service obligation.

Duquesne's Comments clearly identified the concern with relying solely on bidding processes to secure supply:

> Wholesale solicitations do not necessarily provide the same level of price certainty to retail customers nor have wholesale solicitations proven to result in higher levels of shopping than currently experienced in Duquesne's service area. In fact, Duquesne currently has significantly higher residential shopping levels than other jurisdictions that have relied on solicitations to establish default service prices. Duquesne also is concerned that repeated attempts to conduct RFPs limited to its service area have not produced a sufficient pool of bidders to establish a viable competitive wholesale market. While a solicitation process is *one* reasonable way to procure power, it is not necessarily the *most* reasonable method for all utilities under all market conditions.

Duquesne Comments at 6 (emphasis in original). Duquesne also explained that sole reliance on solicitation processes can unnecessarily add cost to the default service price. As Duquesne noted:

> A solicitation process is generally a more structured approach than a bilateral agreement, and the development of a solicitation typically involves settling upon a standard format for the terms, conditions and bid procedures of the supply contracts before the contract is put out to bid. The contract terms, conditions, and bid procedures can have a significant impact on the success or failure of the solicitation. They can affect the number of suppliers willing to participate, the resulting price levels, and the risks allocated to retail customers and winning bidders. A solicitation requires time and funds to implement, and customers are exposed to market price movements during the regulatory proceedings and implementation period leading up to the solicitation.

Duquesne Comments at 10-11.

By way of contrast, Duquesne identified benefits of a bilateral agreement approach:

> The bilateral agreement may allow an EDC and retail customers to "know the price" and customer rate impacts in advance of a lengthy regulatory review period rather than require the Commission to approve a solicitation process with an uncertain

> future price outcome with only one business day to assess the reasonableness of the results.

Duquesne Comments at 11.

The OCA continues to support the use of bilateral contracts as one means of securing supply. As the OCA noted in its Comments, bilateral agreements with non-affiliated generation owners do not raise the types of anti-competitive concerns that gave rise to the Commission's concern with the use of such arrangements.[3] As some commenters also noted, affiliate arrangements require Commission review and approval, and must meet the standards of the Federal Energy Regulatory Commission (FERC) for such arrangements.[4] Duquesne Comments at 14; IECPA Comments at 4-5. Unduly restricting the procurement methods that an EDC may use to secure default supply can result in unnecessary costs and the loss of important flexibility in addressing market conditions.

D. Frequent Price Changes For Residential Customers Should Not Be Used.

Frequent price changes for residential customers can compromise a household's ability to budget for, and afford, essential utility service, while providing no discernable benefit to the stimulation of retail competition. As Duquesne correctly notes in its Comments, the model in Pennsylvania that has provided the greatest amount of retail switching by residential customers is the Duquesne model that provides a fixed rate over a multi-year period. Duquesne Comments at 1-3. The OCA submits that the Commission's direction toward the use of quarterly, or more frequent, price changes for residential customers is misplaced.

---

[3] It is important to note that there is a distinction between affiliated generation owners and affiliates that may serve a procurement function, but also do not have access to affiliated generation supply.

[4] In its Comments, the OCA had suggested the use of bid processes to enter into supply arrangements with affiliated generation owners. OCA Comments at 12. But, as other commenters point out, other methods may be available to ensure the reasonableness of affiliated agreements, including review under Chapter 21 of the Public Utility Code and review by FERC. Duquesne Comments at 14; IECPA Comments at 4-5.

PECO, in its Comments, highlighted one of the key problems with frequent price changes for residential customers:

> Moreover, multiple procurements and quarterly (or more frequent) rate adjustments (§54.187(h) and (i)) are unlikely to send consumers meaningful price signals unless a DSP is willing to commit a substantial portion of its default service supply to spot market purchases. While this may be a reasonable strategy for larger, more sophisticated customers with the expertise to manage their consumption through the use of financial or physical products, PECO questions the wisdom of such an approach for smaller ones, particularly residential and small commercial customers, who generally prefer price stability and who depend on their DSP to mitigate their exposure to wide price swings.

PECO Comments at 9.

Moreover, monthly price swings can be wide in PJM. As PPL notes in its Comments, monthly electricity pricing in the PPL zone within PJM between 2002 and 2005 increased as much as 52% in a month or decreased by 32%. Over the course of a year, monthly prices have varied by as much as 200%. PPL Comments at 12. Information from other jurisdictions that have more volatile pricing does not support the notion that frequent price change equates to increased competition. See, Duquesne Comments, Att. B.

The OCA submits that default service pricing for residential customers should adjust no more than annually, and that even these changes should only reflect changes related to the incremental purchases made during the course of the year in implementing the multi-year default service plan. Default service rates for residential customers should not be required to track short term price changes or volatile spot market prices.

E. The EGS Proposals For Volatile And Expensive Default Service Should Not Be Adopted.

In general, the comments of the electric generation suppliers (EGS) reflect their position that default service should reflect short term current prices so that customers will not want to remain on the default service for very long. NEM has suggested that the EDC exit the function of serving as the default service provider altogether. NEM Comments at 6-7. Because of this vision of default service, the EGSs generally oppose the Commission's proposed regulations and proposed policy statement that call for portfolio management, laddered procurements, long term contracts, and fixed, stable prices. While perhaps grounded in preferred business models of the EGSs, these proposals are not grounded in Pennsylvania law, nor are they grounded in the reality of the essential role that electric service plays in safeguarding the health and welfare of the residents of the Commonwealth and in the future economic development of the Commonwealth.

The proposals put forward by the EGSs have been rejected in almost every state that has considered them. Even where adopted in part, there is no evidence that these proposals lead to vibrant retail competition or, more importantly, lower prices to consumers or better products and services for consumers. These proposals should be dismissed so that Pennsylvania can proceed with a reasonable default service model without any further delay.

Pennsylvania law is clear that electric service is essential, and must be available to all customers on reasonable terms and conditions. Section 2802(9) provides:

> (9) Electric service is essential to the health and well-being of residents, to public safety and to orderly economic development, and electric service should be available to all customers on reasonable terms and conditions.

66 Pa.C.S. § 2802(9).

The provision of electricity is an essential service for residential customers and, for most residential customers, electric service remains a major household expense. The OCA submits that default services must be designed to ensure that the service remains affordable for customers. Default service for residential customers must be characterized by the lowest reasonable level of rates, stability in rates, and a diversified portfolio of power supply arrangements as a means to facilitate rate stability and mitigate risk. Rate stability through a reasonable POLR plan is important to residential customers for reasons of affordability, budgeting, planning, and making decisions about appliance and equipment purchases. Calls for volatile, expensive service simply fail to acknowledge this reality.[5]

Moreover, the statutory requirement that default service supplies be acquired at prevailing market prices does not support the call for short term, spot market pricing as the EGSs argue. The use of the plural "prevailing market prices" in the Act is telling. At any given time, there exists a wide array of prevailing market prices based on the particular characteristics of the electric product to be purchased. The wholesale market provides extensive options with respect to product type, including day-ahead products, month-ahead, multi-month, year-ahead, multi-year products, block products (on-peak, off-peak, all-hours), and requirements contracts. Each such product will entail its own prevailing market price at the time the purchase is transacted. To limit the definition of "prevailing market price" as applicable to only one or a small subset of short-term products, as some EGS commenters argue, is inconsistent with the market reality and serves no valid public purpose.

The OCA would also note that models based on frequent, volatile price changes for residential POLR service raise significant issues of affordability of service for residential customers without any demonstrated benefit. Changing POLR prices every month can be particularly harmful to customers with modest or fixed incomes. This type of pricing proposal for the generation portion of the bill can also prevent the EDC from offering budget payment

---

[5] The OCA submits that there is absolutely no basis to support the departure of the EDCs from serving as the default service provider. At this time, the EDCs remain the entity best positioned to provide this service. The Commission, in its proposed regulations, has provided standards and processes for the replacement of an EDC as the default service provider if circumstances warrant, but those circumstances are appropriately narrow in scope.

plans because of the unknown and unpredictable nature of future POLR prices during a 12-month period. Another adverse impact of such an approach would be to threaten the affordability of basic electricity service for those residential customers on payment plans where the underlying bill must be stable and predictable to assure regular monthly payment. With additional restrictions imposed on payment agreements by Chapter 14, such models raise significant issues regarding the continued availability of essential utility service.

The model of frequent, volatile price changes has recently been rejected by regulators in Maryland and Delaware. See, In the Matter of the Competitive Selection of Electricity Supplier/Standard Offer or Default Service for Investor-Owned Utility Small Commercial Customers; and for The Potomac Edison Company D/B/A Allegheny Power's, Delmarva Power and Light Company's and Potomac Electric Power Company's Residential Customers, Case 9064, Order 81102, *slip op.* at 40-41 (October 31, 2006) and In the Matter of the Provision of Standard Offer Supply to Retail Consumers in the Service Territory of Delmarva Power & Light Company after May 1, 2005 (Opened October 19, 2004), Docket 04-391, Order No. 7053, *slip op.* at 21 (October 3, 2006). The OCA submits that there is nothing to support such a dramatic change in electric service for residential customers in Pennsylvania.

In addition to its other proposals, Reliant has recommended mandatory time-of-use pricing. The OCA submits that for residential customers, time-of-use options, and other alternative rate designs should remain as ***voluntary*** offerings. To the extent that rates can be designed to provide benefit to the system and to the participating customers, these rates should be offered. Mandatory time-of-use pricing, however, is likely to have widespread and adverse impacts on customers' bills, particularly low use customers, low income customers, and customers on fixed incomes. The use of mandatory time-of-use rate designs for residential customers should be rejected.

Finally, the EGSs have supported the Commission's suggestions regarding purchase of receivables, further unbundling of distribution rates and supplier referral programs. The OCA's Comments have discussed these issues at pages 70 to 73. As the OCA cautioned in its Comments, such initiatives must be undertaken in a manner that provides appropriate protections to consumers. Of critical importance, none of these initiatives should be undertaken in a manner that jeopardizes customers' access to essential utility service or adds cost to customers' service. In addition, any customer referral programs that might be considered should not be of the type that offer an initial, short term discount with an unspecified rate thereafter. These types of programs are of little value to consumers and can result in customers paying more than they had been paying to their default service provider.

III. CONCLUSION

The OCA appreciates this opportunity to provide a reply to some of the key issues raised regarding the Commission's proposed Regulations and proposed Policy Statement. These issues remain of the utmost importance to customers and to the Commonwealth. The OCA looks forward to continuing to work to ensure essential electric service is available to all customers on reasonable terms and conditions.

Respectfully Submitted,

____

Tanya J. McCloskey
Senior Assistant Consumer Advocate
PA Attorney I.D. # 50044
E-Mail: TMcCloskey@paoca.org

Counsel for:
Irwin A. Popowsky
Consumer Advocate

Office of Consumer Advocate
555 Walnut Street
5th Floor, Forum Place
Harrisburg, PA 17101-1923
Phone: (717) 783-5048
Fax: (717) 783-7152

DATED: March 23, 2007

00093118.DOC