

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

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

**Comments of
PPL Electric Utilities Corporation
to Final Rulemaking Order**

TO THE PENNSYLVANIA PUBLIC UTILITY COMMISSION:

1. Introduction

In February 2007, the Pennsylvania Public Utility Commission (“PUC” or the “Commission”) entered the following three orders addressing Provider of Last Resort (“POLR”) issues in Pennsylvania:

- 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; Advance Notice of Final Rulemaking Order entered February 9, 2007 (“Rulemaking”);

- Default Service and Retail Electric Markets; Docket No. M-00072009; Proposed Policy Statement entered February 9, 2007 (“Policy Statement”); and
- Policies to Mitigate Potential Electricity Price Increases; Docket No. M-00061957; Tentative Order entered February 13, 2007 (“Mitigation Order”).

Comments to the Rulemaking and the Policy Statement are due March 2; comments to the Mitigation Order are due March 5, 2007.

In the Policy Statement (at 2), the Commission explains that the three orders constitute a comprehensive strategy and should be reviewed together.

“This policy statement, coupled with the default service regulations, and the order on electricity price mitigation, represents a comprehensive strategy for addressing retail rates in the context of expiring rate caps. We recommend that interested parties review all three documents in formulating their comments.”

The Rulemaking and the Policy Statement generally address the same issues, but from different perspectives. In the Policy Statement (at 2), the Commission explained the nature of each and the relationship between them as follows:

“Accordingly, the Commission determined that some elements of the default service regulatory framework would be best addressed in the context of a policy statement that provides guidance to the industry as opposed to strict rules. A policy statement is more readily subject to change, and can provide needed flexibility to the Commission and market participants in the context of default service as energy markets continue to develop.”

Although related, these orders were entered in different dockets. Accordingly, PPL Electric Utilities Corporation (“PPL” or the “Company”) will file separate comments to each order.

The background of each of these proceedings is lengthy and complex. The Commission sets forth a comprehensive summary of that background in each of its orders. PPL Electric will not reiterate that summary here. However, the Company will note that it has fully participated in all aspects of these proceedings and looks forward to continued involvement as they move toward final resolution.

In this filing, PPL Electric provides its comments to the Rulemaking. The Company commends the Commission for initiating this difficult and complex proceeding and for carefully evaluating the input of all stakeholders as it moves toward promulgation of final regulations. At the outset, it is important to note that PPL Electric agrees with the majority of the Commission’s proposals in this proceeding. However, the Company believes that several modifications or clarifications would be appropriate and directs its comments to those issues. To facilitate review by the Commission and other stakeholders, the following comments track the organization of the Commission’s Rulemaking.

2. Comments

§ 54.181. Purpose.

PPL Electric agrees with the Commission’s statement of purpose, noting that some differences of opinion may remain regarding the proper interpretation of the term “prevailing market prices.”

§ 54.182. Definitions.

PPL Electric believes it is critical to future implementation of the Rulemaking and the Policy Statement that the definitions in each document are identical. To that end, PPL Electric recommends in this docket, and in its comments to the Policy Statement, that the Commission modify the definitions of:

(1) competitive bid solicitation process, (2) default service, (3) default service provider, and (4) prevailing market prices.

Competitive Bid Solicitation Process – In the definition of this term, the Policy Statement adds “lowest” before bids at the end of the definition. This adjective does not appear in the definition set forth in the Rulemaking. PPL Electric believes that specifying that a Default Service Provider (“DSP”) will award contracts to the “lowest” bidder removes uncertainty regarding future implementation of the Policy Statement and the Rulemaking. Such a statement makes clear, that after bidders have met all applicable qualification criteria, price will be the sole determinative basis on which contracts for electric generation supply will be awarded. Accordingly, the Company recommends that the Commission modify the definition of this term in the Rulemaking to be consistent with the definition in the Policy Statement.

Default Service – As written, this definition appears to set forth two separate independent definitions of default service. This is not correct because default service must meet both criteria set forth in the definition. Accordingly, PPL Electric recommends that the two subparagraphs of this definition be combined into a single definition.

Default Service Provider – The definition in the Rulemaking uses the phrase “Commission approved alternative supplier of electric generation service” to define the DSP if it is not the incumbent Electric Distribution Company (“EDC”). The definition in the Policy Statement defines this entity as a “Commission approved alternative default service provider.” PPL Electric believes that the definition in the Policy Statement is somewhat circular. That is, it defines default service provider using the term default service provider. The definition in the Rulemaking avoids this problem and more closely tracks the language used in Section 2807(e)(3) of the Electricity Generation Customer Choice and Competition Act (“Competition Act”), i.e., “Commission-approved alternative supplier.” Accordingly, PPL Electric recommends that the Commission modify the definition in the Policy Statement to be consistent with the definition in the Rulemaking.

Prevailing Market Prices – This definition should be expanded to recognize that, at any point in time, the wholesale market includes many electric generation supply products (e.g., capacity, block energy, load shaped energy, load following energy, full requirements service) available over many time periods (e.g., short-term, medium-term and long-term). The price for each of these different products over the agreed-upon term is a prevailing market price at the time the generation supply is purchased.

§ 54.183. Default Service Provider

PPL Electric strongly supports the Commission’s identification of the incumbent EDC as the DSP. The Company believes that this designation is appropriate for at least the following four reasons. First, this approach will minimize

customer confusion and disruption. Second, as a practical matter, the incumbent EDC will remain the “last resort” DSP if an alternative DSP defaults on its obligations. Third, the administrative burdens associated with approving another entity as the DSP are substantial. Fourth, and finally, approving a non-EDC as the DSP risks “stranding” the EDC’s investment and personnel in its various metering, billing and customer care functions.

PPL Electric also agrees that the Commission should have the option to reassign the default service obligation to an alternative DSP “if it finds it to be necessary for the accommodation, safety and convenience of the public.” Such reassignment of the default service obligation may be necessary to protect the interests of default service customers. However, it is important to recognize that reassignment of the default service obligation is an extremely significant matter. Such reassignment has the potential to disrupt default service to customers throughout the EDC’s certificated service territory and the potential to put the EDC at risk in the event the assigned supplier fails to perform. The Commission should require that a very high standard be met before it will take such action.

§ 54.184. Default Service Provider Obligations.

PPL Electric generally agrees with this enumeration of the DSP’s legal and regulatory obligations. The Company believes that it is critically important to hold all DSPs to these standards, both incumbent EDCs and Commission-approved alternative DSPs, if any.

In addition, this section states that the Commission will determine the allocation of universal service and energy conservation responsibilities between an

EDC and an alternative DSP when an EDC is relieved of its DSP obligation. PPL Electric believes that, under such circumstances, very few, if any, of those responsibilities should remain with the incumbent EDC. If an incumbent EDC has been relieved of its DSP obligation, it must have serious performance problems and probably cannot adequately provide universal service or energy conservation programs. Moreover, the entity stepping into the role of DSP should be capable of assuming those responsibilities and should be willing to do so.

§ 54.185. Default Service Programs and Periods of Service.

The Commission has changed paragraph (a) to require the DSP to file a “default service program” instead of an implementation plan. The default service program must be filed no later than fifteen months prior to the conclusion of the Commission-approved generation rate cap for the EDC’s service territory. Under this approach, each DSP in Pennsylvania would submit a default service program to the Commission every two years. After Commission review and approval of the program, each DSP would go into the wholesale competitive market to pursue its default service procurement plan.

PPL Electric has several concerns with this approach. First, it could place a significant administrative burden on the Commission and other stakeholders involved in the review of default service programs. PPL Electric estimates that there are approximately 12 DSPs in Pennsylvania. Reviewing that many default service programs on a two-year cycle will require a significant commitment of time and resources by the Commission and customer advocates. Second, this approach could disrupt the wholesale competitive market. Depending on the nature and timing of

each default service procurement plan, DSPs could be seeking to obtain a variety of generation supply products on different, and perhaps conflicting, procurement schedules. Third, reliance on individual default service programs could raise the possibility of inconsistent regulatory treatment between DSPs and would increase the likelihood of after-the-fact disallowances. If the Commission adopts this approach, PPL Electric believes that it is essential that the PUC approve each DSP's default service program in advance with no possibility of an after-the-fact review of that program. PPL Electric believes that a statewide descending clock auction would eliminate these concerns and, accordingly, would be a better approach for obtaining default supply. However, if the Commission proceeds with use of individual default service programs for each DSP, some of the issues discussed above could be addressed by a coordination among DSPs as contemplated by § 54.185(e) of the Rulemaking and § 69.1807(5) of the Policy Statement.

Paragraph (c) indicates that the initial default service plan should be for a period of two to three years or for a period necessary to comply with § 54.185(d)(4). The cited section provides that the default service procurement plan's period of service "shall align with the planning period of that RTO or other entity." PPL Electric agrees with the proposed approach. Because many elements of a default service procurement plan will be based on criteria derived from RTO data, e.g., registered maximum peak load, it makes sense to coordinate these schedules. PPL Electric is a member of PJM; the PJM planning period begins June 1 each year. However, the Company's generation rate cap was set on a calendar year basis and expires December 31, 2009. To align its default service procurement plan with the PJM

planning period, PPL Electric will need an initial term for its plan of 29 months, within the two to three year range proposed in the Rulemaking.

The Commission revised section 54.185(d) to specify the elements that should be included in a default service program. The first element, a procurement plan, should identify the DSP's generation supply acquisition strategy and identify the means of satisfying the minimum portfolio requirements of the Alternative Energy Portfolio Standards Act ("AEPS Act") for the period of service. As discussed above, the Commission proposes that the period of service for the procurement plan should align with the planning period of the RTO. The proposed regulations also require contingency plans to ensure reliable default service continues in the event a wholesale generation supplier fails to meet its contractual obligations. The second element, an implementation plan, identifies the schedules and technical requirements of the competitive bid solicitations and spot market energy purchases. The third element, a rate design plan, recovers all reasonable costs of default service, and includes a schedule of rates, rules and conditions of default service in the form of proposed revisions to the retail tariff. PPL Electric agrees with the Commission that the default service program should include all these elements to address fully all issues associated with default service.

Section 54.185(e) of the regulations has not been modified by the Commission. PPL Electric believes it is appropriate for DSPs to file joint default service programs to acquire the generation supply for default service customers. The Commission is concerned about the possibility of DSPs scheduling multiple, large procurements at the same point in time and the potential negative impact on the price

bids. This concern is valid, especially if the procurement plans for each DSP are different in terms of products and periods of service. Over time, as more DSPs align their procurement plans with the RTO planning period, all of the DSPs in an RTO could issue competitive bid solicitations at the same time. As discussed above, PPL Electric believes that a statewide descending clock auction would be the preferred approach for obtaining default service supply. To address any concerns related to the effect of a very large procurement on a single day, such a statewide structure could consist of a series of auctions spread throughout the year on a monthly, quarterly, or other regular basis. A statewide process with standard products and terms would eliminate the Commission's concerns regarding DSP coordination and would, PPL Electric believes, result in the most competitive bids.

§ 54.186. Default Service Procurement and Implementation Plans.

The Commission has significantly revised this section of the regulations regarding requirements for the competitive procurement process. The DSP is still required to obtain generation supply at "prevailing market prices." However, the Commission has added a requirement that the procurement plan also must meet the default service obligations at the "lowest reasonable long-term costs." PPL Electric has several concerns with the addition of this new requirement.

First, the Commission has not included a definition of this "lowest reasonable long-term costs" requirement or criteria to determine if it has been met. Second, evaluation of whether this criterion has been satisfied almost certainly will require an after-the-fact review of the procurement plan. PPL Electric believes such a review would not be appropriate. As indicated above, the Commission should

approve each DSP's default service program with no possibility of an after-the-fact review of that program. Third, this requirement improperly adds a criterion for evaluating default service prices not found in the Competition Act. Fourth, and finally, this requirement adds another consideration to the goals of the procurement plan set forth in § 69.1805 of the Policy Statement, i.e., (1) development of a competitive retail supply market, and (2) a prudent mix of arrangements to minimize the risk of over-reliance on any particular source. It will be extremely difficult, if not impossible, for a DSP to weigh all of these different goals and requirements in developing its procurement plan. Accordingly, PPL Electric recommends that the Commission eliminate the "lowest reasonable long-term costs" requirement proposed in § 54.186(b)(1) of the Rulemaking.

Section 54.186(b) identifies the standards to which a DSP's procurement plan must adhere. A change from prior draft regulations is language associated with the procurement of generation supply, which now states that generation supply should be acquired either through competitive bid solicitation process, spot market energy purchases, or a combination of both. This standard would permit the DSP to propose products for a competitive bid solicitation that reflect the characteristics of its default service load, but which may be very different from the procurement plans proposed by other DSPs. These differences may result in less participation by wholesale generation suppliers and less competitive prices for default service customers. PPL Electric believes that the standard products available in the wholesale markets, such as, load following, on-peak, off-peak, and around the clock (ATC), should be the products acquired in the procurement plan.

The Commission's inclusion of spot energy markets as part of the procurement portfolio requirements for DSPs raises some concerns with regard to implementing the default service program. The addition of spot energy market purchases and sales will require the DSP to manage this risk either by establishing a trading operation or obtaining this service from the competitive market. In addition, purchasing generation supply in the spot energy markets can create potentially large energy rate adjustments for default service customers. For instance, 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%. Prices have varied as much as 200% in a year. The default service program should not place too much reliance on the spot energy market because such reliance would expose customers to increased volatility.

Although PPL Electric has identified concerns regarding implementation of the spot market procurement of generation supply, the Company is not recommending elimination of this procurement option. Spot market purchases will have a role in most procurement plans. However, the Commission should be aware of these issues as it reviews default service programs and may want to consider strictly limiting a DSP's reliance on spot market purchases in its procurement of default service supply.

PPL agrees with the Commission's proposal that the bid evaluation criteria should be based on the lowest priced bids, providing the bidder has met all applicable qualification criteria. The proposed regulations now mandate a third party

evaluator to oversee the DSP's procurement and implementation plans of the default service program. PPL agrees with this requirement.

Section 54.186(c) specifies that the relevant load data the DSP provides to bidders must include the capacity peak load contribution by rate schedule, historical monthly retention figures by rate schedule, estimated loss factors by rate schedule, and customer size distribution by rate schedule. However, providing data by rate schedule is inconsistent with § 69.1805 of the Policy Statement which divides default service customers into customer classes separated by maximum registered peak load rather than rate schedule. In its comments to § 54.187 of the Rulemaking, PPL Electric recommends that the Commission permit each DSP to develop its own customer class designations. If the Commission adopts the Company's recommendation, it also should permit the DSP to propose corresponding changes to the data required by § 54.186(c).

§ 54.187. Default Service Rate Design and the Recovery of Reasonable Costs.

PPL Electric strongly agrees with the Commission's statement in paragraph (a) of this section that the default service rate schedule "shall be designed to recover fully all reasonable costs incurred by the DSP." The Company believes that this result is required by Section 2807(e)(3) of the Competition Act, which specifically mandates that the DSP shall recover fully all reasonable costs. The only way to ensure full cost recovery as required by the Competition Act and the Commission's statement cited above is the use of an automatic adjustment clause with a reconciliation mechanism. Accordingly, PPL Electric supports the Commission's statements in paragraphs (e) and (f) of this section that a DSP may

recover its costs through an automatic energy adjustment clause. However, the Company believes that such a clause also must include a reconciliation mechanism. The issue of reconciliation is addressed in the Commission's Policy Statement and PPL Electric provides additional comments on the issue at that docket.

The Company also agrees with the Commission's statements in paragraphs (b), (c) and (d) of this section that the Price to Compare ("PTC") will be a single rate which does not decline with increased usage. The Company also agrees with the Commission's statement in paragraph (d) of this section that an EDC's default service costs should not be recovered through distribution rates. Proper implementation of these directives is essential and those issues are addressed in the Policy Statement. PPL Electric provides comments on those issues at that docket.

The Commission's proposal that default service rates be adjusted on a quarterly basis for residential and small commercial and industrial customers, as set forth in paragraphs (h) and (i) of this section, seems appropriate. Quarterly reconciliation adjustments are required under the Purchased Gas Clause mechanisms used by most natural gas utilities in Pennsylvania. Such an approach generally has been well accepted by customers and should not be difficult for EDCs in the Commonwealth to implement. Moreover, if reconciliation is allowed, as contemplated by the Commission's Policy Statement, quarterly rate adjustments should minimize the size of any reconciliations. Finally, such an approach should keep rates for default service more current and thereby more consistent with prices in the wholesale and retail competitive markets. Quarterly rate adjustments will,

however, result in higher costs for the DSP to notify customers of changes than would be the case with, for example, annual adjustments.

The Commission's proposal that default service rates be adjusted on a monthly basis, or more frequently, for large commercial and industrial customers, as set forth in paragraph (j) of this section, also seems appropriate. PPL Electric anticipates that default service rates for these customers probably will be set on an hourly basis. Hourly pricing of default service for large commercial and industrial customers is appropriate because it should support future development of a competitive retail market. Under such an approach, customers are aware of the hourly market price and, based on that knowledge, can make informed decisions regarding their purchases of electricity. Competitive suppliers will have an opportunity to attract these customers with alternative pricing and service options. Hourly priced default service also will encourage customers to understand and explore demand side options which will help limit wholesale market price volatility. But, at this time, hourly pricing is not an appropriate option for residential customers or small commercial and industrial customers. Many of these customers are relatively unsophisticated regarding the competitive electricity market. Many do not have the resources to manage their electricity use or shop for electricity. For these customers, rates for default service that change on a quarterly basis is preferable at this time.

In setting forth these pricing protocols in paragraphs (h), (i) and (j), the Commission establishes customer classes based upon peak demands of 25 kW or 500 kW. PPL Electric has some concerns with this approach. The Company agrees

that customers generally should be divided into three categories: (1) residential, (2) small commercial and industrial, and (3) large commercial and industrial. However, the Company does not agree that these customer classes should be identified on the basis of arbitrary peak demand designations. Under PPL Electric's retail tariff, this approach cuts across a number of rate schedules such that some customers served under a particular rate schedule would be assigned to one customer class and some customers would be assigned to another customer class. This result could lead to customer confusion and dissatisfaction. A customer's peak demand may change and that, presumably, would lead to reassignment from one customer class to another. When that reassignment would occur and how the customer would be notified are all difficult implementation issues. In addition, the potential for such customer reassignment could increase the supplier's perceived risk and thereby the cost of supply for default service. Accordingly, PPL Electric proposes that the Commission allow each DSP to develop its own customer class designations based upon the unique circumstances of its retail tariff and customer demographics. The DSP's proposed customer class designations could be reviewed by the Commission as part of its review of the DSP's default service program.

§ 54.188. Commission Review of Default Service Programs and Rates.

PPL Electric has no objections to the procedures set forth in this section for Commission review of default service programs and rates. However, the Company does have concerns regarding two provisions of paragraph (d).

First, the Commission states in paragraph (d) that it will "not certify or otherwise approve or disapprove" a DSP's spot market energy purchases made as

part of its procurement plan. This statement could create significant uncertainty as DSPs develop procurement plans. If it is interpreted to mean that the Commission will not approve the use of spot market energy purchases as part of a procurement plan, DSPs simply will not make such purchases. Such a result could increase the cost of default service to customers if spot market prices fall below prices set in bilateral agreements. If the statement is interpreted to mean that the Commission will not approve resulting spot market prices, that interpretation also could discourage DSPs from buying in the spot market. Accordingly, PPL Electric recommends that this statement be deleted from the proposed regulations.

Second, the Commission states in paragraph (d) that it may initiate an investigation “regarding the DSP’s implementation of its default service program” and order lawful and appropriate remedies. If the scope of this investigation is narrowly limited to whether a DSP implemented its approved default service program, the investigation should not cause major concerns. However, if the scope of the investigation expands in any way beyond that single discrete issue, it could become an after-the-fact prudence review. PPL Electric is concerned that such a review could lead to disallowance of costs that were incurred pursuant to an approved default service program, but which were higher than initially anticipated. Such a result is neither fair nor consistent with the requirement in the Competition Act that EDCs fully recover their cost of providing default service. Accordingly, PPL Electric recommends that this provision be deleted from the regulations.

§ 54.189. Default Service Customers.

PPL Electric has no comments to this section of the proposed regulations.

3. Conclusion

As stated above, PPL Electric agrees with the majority of the Commission's proposals in this proceeding. However, as discussed in the foregoing comments, the Company believes that several modifications and clarifications would be appropriate. Accordingly, PPL Electric respectfully requests that the Commission modify its proposed regulations consistent with the Company's comments.

Respectfully submitted,

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Dated: March 2, 2007
at Allentown, Pennsylvania