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March 23, 2007

Mr. James McNulty, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street
Harrisburg, PA 17120

Re: Reply Comments of PECO Energy Company to The Advanced Notice of Final Rulemaking Order and Proposed Policy Statement (Default Service and Retail Electric Markets (Docket No. L-00040169 and L-00070183)

Dear Secretary McNulty:

Enclosed please find an original and 15 copies of PECO Energy's Reply Comments in the above referenced proceeding.

Please acknowledge receipt of the foregoing on the enclosed copy of this letter. A business reply envelope is enclosed for your convenience.

If you have questions please contact me at 215-841-5777.

Sincerely,

Richard G. Webster, Jr.
Director
Regulatory Affairs

cc: Cheryl Walker-Davis, Esquire, Director, Office of Special Assistants
Veronica Smith, Executive Director
Mitchell A. Miller, Director, Bureau of Consumer Services
Robert Rosenthal, Director, Bureau of Fixed Utility Service
Robert Wilson, Manager, Bureau of Fixed Utility Services
H. Edwin Rodrock, Supervisor, Bureau of Fixed Utility Services
Office of Consumer Advocate
Office of Small Business Advocate

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. L-00070183**

REPLY COMMENTS OF PECO ENERGY COMPANY TO THE ADVANCE NOTICE OF FINAL RULEMAKING ORDER AND PROPOSED POLICY STATEMENT

I. INTRODUCTION

On March 2, 2007, PECO Energy Company ("PECO") filed its comments to the Pennsylvania Public Utility Commission's ("Commission") February 9, 2007 Advance Notice of Final Rulemaking Order (the "Rulemaking Order" or "Regulations") and Proposed Policy Statement ("Policy Statement"). PECO expressed support for the default service rules published by the Commission, but recommended certain revisions, which, in its view, would clarify and strengthen such rules in a number of material respects.

Hundreds of pages of additional comments were submitted by twenty-six other stakeholders, including incumbent utilities, consumer representatives, wholesale suppliers and retail marketers. Most of their comments fall into one of two categories - - (1) those that claim the Regulations and Policy Statement are too prescriptive and fail to accord Default Service Providers ("DSPs") sufficient flexibility to tailor implementation plans to their individual circumstances and the needs of their customers and (2) those that believe the Regulations and Policy Statement are not prescriptive enough and stop short of facilitating entry by competitive

suppliers. The heart of the debate has always been and remains a fundamental difference of opinion over the goals of the Electric Competition Act in general and the meaning to be ascribed the phrase "prevailing market prices" in particular. Consequently, before responding to specific default service proposals, PECO offers its views on the critically important issue of legislative intent.

II. GOALS OF THE ELECTRIC COMPETITION ACT

The Electric Competition Act did not relieve electric distribution companies (EDCs) of their statutory obligation to furnish adequate, efficient, safe and reasonable service and facilities (66 Pa. C.S. § 1501). To the contrary, the Legislature, in restructuring the electric industry, specified that EDCs would continue to be responsible for safeguarding system reliability; maintaining (at a minimum) existing levels of customer service, including meter reading, complaint resolution and collections; promoting energy conservation; and assisting low income customers (66 Pa. C.S. § 2807). In addition, the EDC, in its capacity as DSP, must acquire energy and capacity to meet the needs of customers who cannot or do not shop and, unlike alternative electric generation suppliers (EGSs), a DSP cannot freely enter and exit the market. Rather, it must stand ready to meet the generation-related needs of a constantly fluctuating body of customers on a 24/7 basis. It is therefore reasonable to assume that the Legislature did not intend to handicap a DSP in the satisfaction of its responsibilities.

Certain parties, primarily retail marketers, nonetheless contend that the Legislature's primary objective in restructuring the electric industry was to ensure that consumers had multiple generation suppliers from which to choose. They would, therefore, measure success in achieving the Legislature's goals in terms of shopping statistics (i.e., the number of customers or percent of load shopping), and not in terms of customer satisfaction or preference or, for that matter, price

levels. Such parties further assert that the only way to assure market entry is to limit the procurement and pricing options available to incumbent utilities in their role as the default service provider. All of this leads them to conclude that the phrase "prevailing market prices" must mean hourly prices for large customers and prices that change frequently for smaller customers. PECO respectfully submits that this vision of the future is not supported by the history of and debate over electric restructuring in Pennsylvania.

1. The Commission's Investigation

On April 14, 1994, the Commission launched an investigation to examine the structure, performance and role of competition in Pennsylvania's electric utility industry. The investigation culminated in a 50-page Report setting forth the Commission's findings and recommendations (the "July 3 Report"), which provided the Governor and Legislature a blueprint for transitioning Pennsylvania to a new era of retail electric competition. Of particular relevance to this proceeding, the Commission, at pages 30 and 31, outlined "a mere sampling" of the "generation services" it anticipated would be made available and identified a variety of options that incumbent EDCs could offer:

> iii. From the LDU [Local Distribution Utility], purchasing electricity through the power market exchange at the average hourly price on a monthly basis. This option will make the same market rate available to all customers without requiring significant consumer effort or knowledge.
>
> iv. From the LDU, purchasing electricity through the power market exchange at an hourly time of use price. With this option, consumers who are able to adjust their usage to off-peak hours can achieve even greater savings.
>
> * * *
>
> **vi. Through the LDU providing electricity as an aggregator. The LDU may acquire electricity through any source of supply. This option provides another competitor for consumers and**

> **permits existing utilities to have an equal opportunity to provide electricity to its present customers.**

Later in its Report (p. 40), the Commission suggested that EDCs utilize the transition to customer choice as an opportunity to develop and test many new services and pricing arrangements:

> The Commission encourages utilities to prepare tariffs which address flexible tariffs, real-time pricing, multiple location conjunctive billing, interruptible buy-through options, commodity index pricing, and other innovative proposals for all customer classes. **These developments will give customers the opportunity to ascertain their needs and have some of them met while utilities gain experience with product variations as they prepare for customer choice.**

In short, when the Commission urged the General Assembly to facilitate the introduction of retail customer choice in Pennsylvania, it did so with the expectation that incumbent EDCs would fully participate in the new competitive regime and would not be hamstrung as to the manner in which they procured power or the services and products they could provide.

2. The Legislative Process

House Bill No. 1509 (the Electric Competition Act) was introduced on April 27, 1995 and quickly gained passage. On June 19, 1995, it was referred to the Senate Committee on Consumer Protection and Professional Licensure, where it remained for over a year pending completion of the Commission's investigation. However, after the Commission issued the July 3 Report, a broad spectrum of interested parties, including utilities and the representatives of various consumer, public interest and power marketing groups, worked with the Commission and Senate leadership to build consensus around legislation acceptable to all. The end result was a substantially revised bill that was passed by the House and Senate on November 25, 1996. Given the foregoing timeline, the role played by the Commission and its July 3 Report in forging

a consensus and the final language of House Bill No. 1509, there can be little doubt that the Legislature embraced the Commission's vision of electric competition, as laid out in the July 3 Report including the range of EDC procurement and pricing options discussed in that Report.

3. The Statute

If the Legislature had intended to narrowly prescribe the terms of DSP procurement and/or pricing, it could have, and arguably would have, required EDCs to divest their generation; directed them to install meters capable of measuring real-time consumption, and mandated hourly pricing. In fact, it did none of those things. To the contrary, it left generation divestiture to the discretion of incumbent utilities (66 Pa. C.S. § 2804(5)); authorized, but did not require enhanced metering (66 Pa. C.S. § 2807(a)); and reaffirmed the Commission's power "to approve flexible pricing and flexible rates, including negotiated, contract-based tariffs designed to meet the specific needs of a utility customer and to address competitive alternatives" (66 Pa. C.S. § 2806 (h)).

In other words, there is no evidence that the Commission or the Legislature intended to severely limit a DSP's procurement and/or pricing options. To the contrary, the background, history and language of the Electric Competition Act all belie that conclusion. Moreover, by denying EDCs a level playing field, the Commission would suppress competition, not promote it. If incumbent (DSP) suppliers can procure power and, for whatever reason, make available lower prices or a more attractive product than those offered by others, there is absolutely no reason - - and certainly no economic justification - - why consumers should be denied that option.

PECO believes that the phrase "prevailing market prices" must be construed in this broader context. At any given time, there will be a number of different "prevailing" market prices. For example, there will be a "prevailing" hourly price, but there will also be a

"prevailing" price for energy to be delivered well into the future. The Legislature recognized this by declining to specify an hourly, monthly, annual or any other pricing model. Rather, by adopting a "prevailing market prices" approach, the Legislature intended that DSPs be accorded sufficient flexibility to fashion default service rates that were neither so high as to take unfair advantage of customers who could not shop nor so low as to unfairly drive out potential competitors. PECO believes that the proposed Regulations and Policy Statement, if properly construed, generally achieve this goal.

III. RESPONSE TO SPECIFIC PROPOSALS

A. Procurement

1. Mechanism - How to Buy

Bilateral Contracts. Virtually all who commented endorsed, or at least did not oppose, the use by DSPs of competitive bidding solicitations (i.e., auctions or RFPs) and/or spot market purchases to procure default service supplies. Duquesne (pp. 5-6) and IECPA (pp. 17-19) would expand the menu of available procurement options to include bilateral contracts. The OCA, in turn, would have the DSP serve as a "portfolio manager" (p. 8), in which role it could purchase energy on a bilateral basis (if it so chose), but would be barred from entering into supply agreements with affiliated entities (p. 12).

As explained in its March 2, 2007 comments, PECO fully supports the competitive procurement of default service requirements and, of the various models that have been promoted, believes that an auction for full-requirements, load following supply, preferably coordinated on a statewide basis, is best-suited to procure reasonably priced reliable power and satisfy the "prevailing market price" standard.[1] In our view, an open and transparent bidding process is

[1] PPL also supported a "statewide descending clock auction" (p. 8).

more likely to further the development of competitive markets than the use of bilateral contracts. However, if bilateral agreements are to be authorized, affiliated generation suppliers should be subject to precisely the same rules as everyone else, i.e. neither accorded preferential treatment nor discriminated against so as to maximize the available competitive supply.

"Portfolio Management." PECO opposes the OCA's recommended "portfolio management" approach. We are particularly concerned that, in actual practice, this "model" reverts to a form of Integrated Resource Planning, complete with substantial regulatory intervention, contentious litigation and prudence reviews, and the pursuit of non-market-related societal goals, all of which will lead to higher power prices.[2] While the Commission may wish to encourage DSPs to acquire a mix of generation, it should not specify that certain percentages of that supply portfolio must be obtained from specific resources or be of a particular contractual duration. Indeed, reliance on such centralized command-and-control planning and regulation is what the Electric Competition Act was designed to eliminate.[3]

AEPS. Several parties comment upon, and make recommendations with respect to, the interplay between the Commission's default service regulations and compliance with the Alternative Energy Portfolio Standards Act ("AEPS"). For example, PV Now supports a separate statewide auction for solar renewable energy credits (p. 3) and Allegheny contends that default service is "the wrong tool to use to try to pursue fuel diversity" (p. 10). In contrast,

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[2] In describing its proposal (p. 8), the OCA states: "The portfolio or procurement plan should emphasize a diversity of resources, including supply side and demand side, a variety of contract terms and lengths, and any state-mandated or Commission-mandated public policy requirements."

[3] As Allegheny notes (p. 7): "[T]he premise behind recent arguments for a complex 'portfolio' approach to default service is that it is possible for a complex 'portfolio' to provide better prices than the markets. This is simply untrue, and contrary to all the evidence that led Pennsylvania and other states to seek access to the benefits of retail and wholesale competition in the first place."

Constellation would require winning default service bidders to provide a pro rata share of the DSP's AEPS requirements (pp. 3, 15), while Direct would have the EDC or DSP (if different than the EDC) procure needed alternative energy resources and then resell them, at cost, to wholesale suppliers (p. 12).

PECO believes that it should be left to each individual DSP and EGS to determine how best to achieve AEPS compliance. For that reason, we oppose the efforts of Constellation and Direct to dictate, as part of this proceeding, the terms by which alternative energy and alternative energy credits must be procured. Rather, those issues, in our view, are more appropriately taken up in the context of individual utility filings and the Commission's AEPS rulemaking at Docket No. M-00051865.

Joint Procurement. Hess endorses, in concept, what it characterizes as "the Commission's proposal to combine default service procurement of smaller Pennsylvania EDCs such as Pike County with those of neighboring larger Pennsylvania EDCs" (p. 8). Although PECO does not necessarily concur with Hess' reading of Section 54.186(b)(2), we do not oppose joint procurement arrangements, provided that it is left up to DSPs, and not the Commission, to determine whether a pooling of buyer interests is desirable.

2. Product - What to Buy

Although there is general agreement that default service requirements should be procured, for the most part, through some form of competitive process, no such consensus has emerged regarding the products to be acquired. Incumbent utilities and most consumer representatives (i.e., the OSBA, IECPA and U.S. Steel) tend to favor multi-year supply contracts, tempered by the use, where necessary, of spot market resources. Not surprising, most retail marketers would rewrite the Regulations and Policy Statement to mandate hourly and/or monthly

purchases. The OCA for its part, encourages the use of all available procurement options, including long-term contracts, provided the end result satisfies the Commission's proposed "lowest reasonable long-term cost" standard.

Cost Standard. As PECO explained in its comments (p. 6), the "lowest reasonable long-term cost" standard should be deleted for two reasons - - (1) it is inconsistent with Section 2807(e)(3) of the Electric Competition Act, which directs DSPs to "acquire electric energy at prevailing market prices;" and (2) it will invite debate and litigation. Notably, its adoption is opposed not only by several EDCs (PECO, FirstEnergy and PPL), but by the OSBA as well ("It is questionable whether imposing [the lowest reasonable long-term cost] standard is permitted under the Competition Act") (p. 5).

In its comments (p. 3), the OCA defends the Commission's proposed standard by reference to a natural gas distribution company's obligation to pursue a "least cost fuel procurement policy" under Sections 1317 and 1318 of the Public Utility Code (66 Pa. C.S. §§ 1317 and 1318). PECO would simply observe that the gas-related Code sections cited by the OCA predate, by over ten years, the restructuring of Pennsylvania's energy utilities, and clearly envisioned and, indeed, imposed a far more pervasive regulatory scheme than implemented by the Electric Competition Act. Moreover, if the Legislature wished to subject DSPs to a "least cost" procurement standard (or, for that matter, a "lowest reasonable long-term cost" standard), it could have adopted the appropriate statutory language, but chose not to.

Procurement Guidelines. Duquesne (p. 24), the OCA (pp. 13-14), IECPA (pp. 17-18), U.S. Steel (p. 3) and the OSBA (p. 6) each urge the Commission to allow DSPs to enter into multi-year wholesale procurement contracts. Approaching it from a different angle, PPL (p. 12) and Constellation (pp. 12-14) would impose limits on a DSP's spot purchases. In contrast,

Direct (p. 5), Reliant (pp. 10-12) and Strategic (pp. 5-7) would bar the ongoing use of long-term supply arrangements, and likewise Hess (p. 5) and RESA (p. 2) would require DSPs to procure all or substantially all of their default service requirements on an hourly, monthly or quarterly basis.

PECO believes that it would be a serious mistake for the Commission to adopt arbitrary rules dictating the extent to which DSPs may, or may not, rely on multi-year supply agreements on the one hand and "spot" purchases on the other. Nor is it our sense that it was the Commission's intent to do so. Unfortunately, some parties have misconstrued the three procurement strategies outlined at Section 69.1805 of the Policy Statement as establishing norms against which future DSP implementation plans will be measured. As explained in our March 2, 2007 comments (p. 7), the Commission can eliminate confusion on this score by either deleting those examples or by making it clear that they are presented for illustrative purposes only. In this way, DSPs would be free to do precisely what the Policy Statement encourages them to do, namely "craft an approach best suited to [their] own service territory" (p. 4). In any event, the appropriate mix of multi-year contracts and spot purchases can and should be evaluated upon review of individual DSP implementation plans and need not be resolved here.

Customer Groupings. The same observation would seem to apply to "customer groupings." In this instance, however, there arguably is less reason for confusion - - the Policy Statement expressly notes that "DSPs may propose alternative divisions of customers by registered peak load to preserve existing customer classes" (Section 69.1805). Notwithstanding this guidance, several marketers (e.g., Direct, Hess, Reliant) go to great lengths trying to convince the Commission to redefine the breakpoint between "small" and "large" business customers by reducing the 500 kW threshold for hourly pricing. In fact, Direct goes even

further, recommending that the Commission adopt "a uniform definition of default service customers and customer classes across the state" (p. 9). Again, PECO respectfully submits that the classification of customers for default service purposes does not readily lend itself to generic rules of thumb, but given the disparities in rate-class definitions across EDCs, should be addressed on a utility-specific, case-by-case basis.

3. Timing and Frequency - When to Buy and How Often

By eliminating the use of multi-year supply agreements and/or laddered contracts, and by denying DSPs the option of offering fixed price service (see discussion, *infra*), NEMA and several of the individual marketers would essentially force DSPs to procure power on at least a quarterly and, in some instances, a monthly or hourly basis. However, as PECO explained in its comments (pp. 8-9), multiple procurements and quarterly (or more frequent) rate adjustments may not be appropriate for residential and small commercial customers. Because such customers generally prefer rate stability, DSPs are unlikely to commit a substantial portion of the default service supply earmarked for them to spot market purchases. For that reason as well, PECO has proposed that the Regulations be revised to permit DSPs to adjust their rates for residential and commercial customers once a year (p. 9).[4]

4. Procedural Issues

Effective Date. Duquesne (pp. 4-5), the OSBA (p. 3) and UGI (p. 9) each recommend that the Regulations become effective for all DSPs at the same time, namely on January 1, 2011 when the last EDC generation rate caps expire. PECO does not disagree with this proposal as a matter of principle, but notes that the Commission may need to consider a staggered filing

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[4] Several other parties, including Duquesne (pp. 7-8) and the OCA (pp. 18-20), similarly would not mandate quarterly price updating and/or cost reconciliation for smaller customers.

scheduling for DSP implementation plans to avoid the concurrent litigation of ten or more proceedings.

Bid Selection Criteria. The Regulations provide that winning bids procured through a competitive bid solicitation process shall be based on "price determinative bid evaluation criteria" (Section 54.186(c)(4)). In commenting upon this provision in its Rulemaking Order (p. 16), the Commission notes: "It is our expectation that the energy suppliers who submit the lowest priced bids, providing they have met all bidder qualification criteria, will be awarded generation contracts by the DSP." PPL (p. 12) and PSEG (p. 4) support the Commission's proposal, while FirstEnergy (p. 4) and the OCA (pp. 42-43) contend that price should not be the sole criterion in evaluating bids.

PECO firmly believes that bids which otherwise comply with the requirements of the competitive bidding process including credit terms should be evaluated solely on the basis of price of a uniformly defined product. The introduction of uncertainty and significant risk into the procurement process might well force potential suppliers to increase their bid prices or, alternatively, to refrain from participating altogether, both of which could result in higher retail prices.

PUC Review. Sections 54.188(e)(3) and (f) set forth procedures for customers to challenge initial default service tariffs and subsequent updates and specifically provide that exceptions taken to such filings "shall be limited to whether the DSP properly implemented the procurement plan approved by the Commission and accurately calculated the rates." IECPA takes issue with this standard, arguing that "[c]ustomers should be permitted to address not only the DSP's arithmetic, but also any matters related to the substance of the filing and the DSP's use of the PTC rate" (p. 21).

IECPA's proposal essentially would allow intervenors to contest default service rates on any ground imaginable (i.e., "any matters related to the substance of the filing") and would expose DSPs to the kind of administrative litigation and hindsight review that the Electric Competition Act was designed to eliminate. The Commission, in ruling upon a DSP's implementation plan following full input from interested parties, will ensure that it is fair, transparent and non-discriminatory. Once that process is completed, the Commission need only confirm that the procurement of default service supplies and the quantification of PTCs were carried out in a manner consistent with the approved plan. IECPA's recommendation should, therefore, be rejected.

B. Pricing

1. Rate Design - - "Single Rate Option," Declining Block Rates and Demand Charges

There are very different views when it comes to the pricing of default service. For the most part, the customer representatives oppose the "single rate option" and would require DSPs to make available fixed-price service in addition to other tariff offerings (OCA, p. 46; IECPA, pp. 3-9; OSBA, pp. 12-13; U.S. Steel, p. 4). Retail marketers, on the other hand, would limit commercial and industrial customers (and, in the case of Strategic, residential customers) to a single monthly or hourly rate (Direct, p. 10; Hess, pp. 3-5; NEMA, pp. 4-5; Reliant, p. 8; RESA, p. 12; Strategic, p. 7).

As discussed in Section II of these Reply Comments, *supra*, the history of the Electric Competition Act reveals that the Commission anticipated EDCs/DSPs would fully participate in the new competitive regime and would not be constrained in terms of the services and products they could furnish. This is not to say that DSPs should be required to offer fixed-price service to large customers, as IECPA recommends. Indeed, unless the Commission considers tight

switching rules, especially as they might apply to large customers, it is unlikely that this option would be very attractive to incumbent suppliers. That having been said, DSPs should nonetheless be given the discretion, should they choose to exercise it, to design flexible rate offerings for their default service customers.

On a more practical level, the conversion to a "single rate option," particularly if coupled with the elimination of demand charges and declining block rates as the Commission and others have proposed (*see, e.g.*, Duquesne, p. 22; PPL, p. 14; PennFuture, p. 1; Constellation, p. 4); could have a very disruptive effect on individual customers' bills. As explained in our March 2, 2007 comments (pp. 10-12), PECO's existing rates were designed to reflect the different costs of serving different kinds of customers. PECO believes that default service rates, to the extent practicable, should continue to adhere to cost causation principles and that DSPs should therefore be allowed to demonstrate, in their implementation plans, why the elimination of demand charges and/or declining block rates would not be in the public interest. Moreover, even in those instances where a fundamental change in the design of rates was found to be in order, consideration should be given to the gradual, and not immediate, phase-out of these demand-based features. The elimination of declining blocks and demand charges is likely to produce price increases for many customers that will far exceed the impact of lifting the generation rate cap. For these customers, such changes in rate design would overwhelm the Commission's efforts to mitigate the effects of transitioning to market-based retail generation rates.

Several retail marketers also commented on Section 69.1811 of the Policy Statement, which proposes that residential and small business customers be given the opportunity to either prepay or defer some portion of any rate increase imposed by a DSP upon expiration of its (or predecessor EDC's) generation rate cap that exceeds 25%. For example, Consolidated Edison

would require that any amount deferred come off a DSP's distribution charges, and not its PTCs (pp. 4-5). Dominion, on the other hand, would have DSPs extend "deferral loans" to shopping customers (p. 10), while Strategic seemingly would preclude DSPs from offering a phase-in option (pp. 12-13).

Based on current projections, PECO does not expect that the increases its residential and small business customers will face upon the expiration of its generation rate caps will approach the 25% threshold specified in the Policy Statement. Nonetheless, PECO strongly opposes the retail marketers' recommendations on deferral issues and believes that their adoption would be fundamentally inconsistent with the Electric Competition Act's directive that rates be unbundled into separate distribution, transmission and generation components (66 Pa. C.S. § 2804 (3)).

2. Cost Allocation

The other parties' comments generally touch upon two issues: (1) what costs should be recoverable through default service charges; and (2) when and how should that determination be made? As to the first issue, several parties, including the OCA (p. 22), the OSBA (p. 9) and Constellation (p. 9), contend that only incremental (i.e., avoidable) costs should be allocated to the PTC. Otherwise, they reason, non-shopping customers will be forced to bear fixed costs left behind by shoppers. PECO believes that the term "all reasonable costs," as set forth in Section 2807(e)(3) of the Public Utility Code, should be narrowly construed to encompass only those incremental (i.e., avoidable if a customer shops) costs directly or functionally related to the DSP's statutory obligation.

Another cost allocation matter concerns the treatment of transmission and ancillary service costs. Section 54.187(d)) of the Regulations provides that transmission costs should be rolled into the PTC. However, IECPA (pp. 12-13) contends that the Electric Competition Act

and cost causation principles require that such costs remain unbundled and separately stated. PECO has no serious disagreement with either position, provided that rates can be designed to ensure full recovery of transmission-related costs.

With respect to the second issue, PECO opined in its March 2, 2007 comments (p. 13) that the identification and quantification of specific costs properly recovered through a PTC were beyond the scope of this proceeding and should await the filing of individual DSP implementation plans. Consistent with that view, PECO sees no useful purpose to be served by launching a generic cost allocation proceeding, as proposed by the OSBA (p. 10).

C. Cost Recovery

Sections 54.187(b) and (f) of the Regulations permit, but do not mandate, DSPs to propose reconciliation of their default service rates.[5] In commenting upon these provisions, the PUC observes: "The Commission now concludes that reconciliation of default service costs may be necessary and in fact is more desirable, to enable the DSP to "... recover fully all reasonable costs so that the PTC reflects market prices" (Rulemaking Order, p. 18). PECO agrees with the Commission's assessment, as do the OCA (pp. 20-21) and the OSBA (pp. 10-11).

As they have throughout this proceeding, the marketers strenuously oppose reconciliation. Dominion is particularly out-spoken in this regard, asserting that reconciliation is unlawful and would be poor public policy because EGSs lack the ability to true-up their costs (pp. 1-3). There is, of course, no basis for Dominion's conclusion that reconciliation is somehow contrary to the Electric Competition Act. In fact, Section 2807(e)(3) authorizes DSPs to "recover fully all reasonable costs" of providing default service. In addition, while EGSs may be

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[5] In contrast, and as the Commission properly notes (Section 54.187(g)), AEPS compliance costs must be recovered through a reconcilable Section 1307 automatic energy adjustment clause.

unable to reconcile their costs and revenues, they are free to enter and exit the retail market as they see fit and to price their service as they wish. DSPs, with their statutory obligation to serve as the provider of last resort, will not have that luxury.

D. Fixed-Price Option for Large Customers and Switching Rules

The Policy Statement provides that DSPs "may propose a fixed-price option [for large customers] for the Commission's consideration," but does not mandate that they do so (Section 69.1805(3)). IECPA would not leave that decision to the discretion of DSPs, but instead would require that fixed-price service be made available to any customer which requested it ("Although IECPA, et al. appreciate the Commission's recognition of its prior arguments by including [fixed-price service] as a permissive default service offering, to meet the goals of the Competition Act it should be a mandatory default service offering.") (p. 7)(emphasis in original).

A case can be made that large customers need no "provider-of-last-resort" service in the first instance, as all large customers have available many retail suppliers from whom they can take competitive supply. In fact, in states such as Illinois and Texas that offer no fixed-priced default service to large customers, retail competition has flourished and customers have obtained competitive supply in the market. This is not surprising, as large customers are well informed and have sophisticated energy-procurement experience.

PECO recognizes, though, that under Section 2807(e) of the Pennsylvania Public Utility Code, EDCs may be required to provide some backstop for large customers. If so, PECO believes that hourly pricing should be the default-service product for large customers. Indeed, some 16 utilities in four retail-competition states offer hourly-only default service to large

customers.[6] If large customers desire longer-term, fixed-price contracts to provide certainty, they obtain such contracts from competitive suppliers.

If, nevertheless, IECPA's view -- that DSP's should be required to provide a longer-term, fixed-price default-service product to large customers – were to be given serious consideration, then the Commission should make clear that wholesale procurement for such long-term supply should be through a competitive process – i.e., an auction or RFP – that matches the term of the retail offer. And the Commission should impose strict switching rules to protect against the "seasonal gaming" that will otherwise compel wholesale suppliers to build substantial risk premiums into their competitive bids, thereby increasing the PTC for all members of the class. Without strict switching rules, large customers would enjoy "free optionality," in trading parlance, and will flip on and off fixed-rate default service as short-term market prices fluctuate. Ideally, given the ability and propensity of large customers to shop for competitive supply, switching rules would require that large customers (1) sign up for longer-term fixed-price default service **before** the DSP goes to the market to secure power on behalf of those customers, and (2) commit to take the service over the full term of the contract.

E. Proposals That Go Beyond The Scope Of This Proceeding

PennFuture makes a number of far-ranging proposals in its comments that, in PECO's view, go beyond the scope of this proceeding and simply cannot be considered without reopening the Regulations and proposed Policy Statement for yet another round of comments and/or hearings, which PECO would strongly oppose. These include recommendations to (1) mandate DSPs to procure energy efficiency and demand side resources; (2) impose a system

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[6] APS, Atlantic City Electric, Central Hudson, ComEd, ConEd, BG&E, Delmarva, Duquesne, JCP&L, Niagra Mohawk, NYSEG, Orange & Rockland, PEPCO, PSE&G, Rochester Gas & Electric, and Rockland Electric.

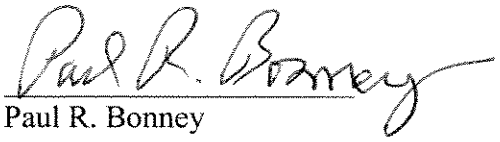
benefits charge on all electricity sold in Pennsylvania; (3) "decouple" energy sales and profits; and (4) require that 10% of all default service load be enrolled in voluntary real-time pricing programs by 2010. Moreover, PECO notes that several of the issues raised by PennFuture already are being explored in other pending Commission proceedings. *See, e.g., Implementation of the Alternative Energy Portfolio Standards Act of 2004*, Docket No. M-00051865; *Investigation of Conservation, Energy Efficiency Activities, and Demand Side Response by Energy Utilities and Ratemaking Mechanisms to Promote Such Efforts*, Docket No. M-000601814.

In addition, the OSBA makes certain proposals purportedly designed to protect the interests of shopping customers that previously participated in PECO's Market Share Threshold ("MST") program (p. 14). As the OSBA seems to acknowledge, however, any issues relating to the current or future status of these customers should be taken up, if at all, during review of PECO's default service implementation plan. In any event, PECO is not aware of any obstacle that would prevent the customers in question from returning to it for default service now, or at any time, if that were their preference. PECO, however, has no authority to switch them back itself as that decision rests entirely with either the customer or their current retail supplier.

IV. CONCLUSION

PECO appreciates this opportunity to comment on issues raised by the Commission's proposed Regulations and Policy Statement and looks forward to working with the Commission and other stakeholders as this process moves forward.

Respectfully submitted,



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Date: March 23, 2007