PENNSYLVANIA PUBLIC UTILITY COMMISSION
Harrisburg, Pennsylvania 17105-3265

Investigation of Pennsylvania's Retail Electricity Market

Public Meeting: September 27, 2012
2237952-DIR
Docket No. I-2011-2237952

CONCURRING AND DISSENTING STATEMENT OF COMMISSIONER CAWLEY

There is much to like in the proposal released with today's Secretarial Letter, but not enough. I therefore must respectfully dissent and be counted as a negative vote because the key reform in the proposal is too inadequate to achieve what is truly needed to bring the benefits of electricity choice to most Pennsylvanians who receive service from an investor-owned electric company.

Overview

Much discussion since April 28, 2011 has centered on how optimally to bring competitive market forces to bear in order to reduce electricity prices and to improve the quality and types of services provided to electricity customers. This discussion has resulted in a recommendation to change the default service supply portfolio standard from a "prudent mix" of short and long term contracts, meeting a "least cost over time standard," to a spot or very short term supply portfolio for default service. As will be explained, this fundamental shift in the supply portfolio does not address the more fundamental structural problems that have thwarted the Commission's efforts to maximize the full benefits of retail competitive markets in Pennsylvania.

As described in more detail below, any end-state recommendation must address directly the propensity of many electricity consumers not to make any decision at all regarding switching their energy supply in the presence of a default service alternative. That is, if customers do nothing, by default they receive service from their electric distribution company (EDC) as the "provider of last resort," when, in effect, the utility is acting instead as the "provider of first resort" contrary to the legislative intention that the distribution company act primarily as the energy delivery entity and serve as the supplier of the energy only for a small residue of customers, after the vast majority of them have chosen an Electric Generation Supplier (EGS) for their energy supply.

Why current utility-based default service structures are not in the public interest

The fundamental problem with the current default supply structure is that the majority of consumers will not make a proactive decision to choose an energy supplier when they are provided a default supplier if they do not chose one. This is especially so when customers are accustomed to receiving complete service from their electric utility. This situation will persist indefinitely, even if competitive retail offerings are well below the utility default service option. One only needs to examine the Duquesne Light Company service territory in Western Pennsylvania to drive this point home.

Under Duquesne's default service plan Settlement, Duquesne agreed to provide a fixed price of 7.86 cents/kWh for generation supply to residential customers for the period January 1, 2011 through May 31, 2013. This was based on a non-competitive bid process where Duquesne would manage its own portfolio of supply to attain this price over this 29-month period, either profiting or losing money on its default service offer. It has not been a surprise that this static price has turned out to be well above market prices. Meanwhile, many suppliers logically entered the market, providing much lower, more market-based pricing to residential customers. One would expect that such a sustained period of opportunities for consumers to save money by multiple firms would result in the loss of the vast majority of sales by Duquesne. However, to the contrary, Duquesne maintains the vast majority of commodity sales in its service territory. As of March 15, 2011, Duquesne served 75.7% of the residential sales market. As of September 19, 2012, Duquesne still serves 58.6% of the residential market, even though there are offers on the Commission's website for fixed-priced supply which are well below Duquesne's default service Price to Compare (PTC).[1] In fact, the top fixed-price offer for twelve month's supply is currently <u>35% cheaper than Duquesne's PTC</u>. Furthermore, there are currently over 9 alternative Electric Generation Suppliers (EGSs) with <u>fixed-priced offers ranging from 6 months to 24 months which are over 20% lower than Duquesne's prices</u> for supply. Moreover, this pricing information is readily available to consumers over the papowerswitch.com website, which this Commission and others have gone to great pains to bring to the attention of consumers.

Having customers pay up to 35% more for their energy supply is not just and reasonable. As is demonstrated by this very simple example, mass market customers, including residential and small commercial customers, often will not make affirmative choices for their supplier unless they are required to. Any end-state proposal by this Commission should change the current default mechanism which is an injustice to the public.

Competitive retail opt-out programs to provide better supply prices for consumers

Retail auctions for default service can optimally ensure that customers receive a reasonably priced supply service by embracing competitive bid processes for that purpose.

Briefly described, multiple EGSs would bid for the right to make energy supply offers to large segments of default customers (i.e., those who have not chosen an alternative energy supplier). A cap would be placed on the number of customers any one EGS could "win," and, to promote market diversity, smaller (but financially secure to the Commission's satisfaction) EGSs would be given an opportunity to "win" a share of the available customers.

Winning EGSs would offer a fixed price (presumably lower than the EDC's default price) for a year to those customers it "won" in the auction. Any customer receiving this offer could accept it (but still be able to switch to another supplier or to default service within the year) or reject it by "opting out" (i.e., staying with the default service rate).

A retail opt-out model is attached to this statement in order to provide details on how such a program could be structured. This is but one example and by no means should be adopted

[1] For example, Reliant Energy Services offers a 12-month fixed-price offer of 6.39 cents/kWh relative to Duquesne's PTC of 9.89 cents/kWh. Source: www.papowerswitch.com.

without in depth stakeholder review. It is only a starting point from which to begin discussions of how such a model could improve electricity choice in Pennsylvania.

Examples of retail opt-out processes

The experience of Pike County Light and Power Company (Pike) demonstrates the effectiveness of retail opt-out programs. On March 10, 2006, Direct Energy Services, LLC petitioned the Commission for approval of its Retail Aggregation Bidding Program for Customers of Pike County Light & Power Company. The petition was in response to the increase in rates that was the outcome of Pike's default service auction that resulted in a more than 70% increase in Pike County's previous retail rates, on a total-bill basis, and further implemented a 129% increase in generation rates for Pike's customers. The outcome of this proceeding was *a competitive retail opt-out program* that resulted in significant savings to consumers compared to Pike's existing rates. Specifically, the Commission approved an opt-out aggregation program with an initial term through December 31, 2007, and a subsequent renewal term from January 1, 2008, through May 31, 2009.[2] While unique conditions justified the opt-out auction, the Pike experience nevertheless also provided a firm example of the effectiveness of such proposals.[3]

Other retail market development options:

There are a number of means of promoting retail markets. To their credit, my colleagues have steadfastly pursued these policies, including:

- Access to customer data necessary to price, enroll, and serve customers
- Customer lists
- Commission retail choice website for comparison shopping made easy
- Standardized business practices and Electronic Data Interchange
- Purchase of receivables programs
- New/Moving customer programs
- Accelerated supplier switching time frames
- Referral programs
- Retail opt-in programs
- Default service rate design
- Default service cost unbundling

This Commission has made great strides in each of these policies, and my colleagues and Commission staff are to be commended for their diligent efforts to enhance retail competition. This hard work, combined with the efforts of EGSs and EDCs, has resulted in commendable results. Thirty-one percent of residential customers and 38% of commercial customers are taking advantage of competitive offers for electricity supply.[4] However, that necessarily means that 69% of residential customers are paying more for supply than they currently need to.

[2] See Docket P-00062205, order entered April 20, 2006.
[3] Only about 10-15% of customers remained on Pike Default Service following the opt-out retail auction.
[4] Commission weekly electric shopping report, September 19, 2012.

The alternative method of advancing competition, as suggested by this Commission in its end-state proposal, is to move to more market responsive default service pricing. There are positive aspects of such a default service design. Such pricing provides a more appropriate price signal to stimulate economic growth when prices are low, and stimulates energy efficiency investments when prices are high. Furthermore, more market reflective prices help Pennsylvania avoid the boom/bust nature of retail markets that are characterized by long term hedges for default service supply.

For this reason, more short term, market-responsive pricing is a better policy than our current statute, which contains conflicting provisions. Arguably, the "least cost over time" standard logically supports shorter term default service pricing, whereas the "prudent mix" portfolio requirement arguably requires a short, medium, and long term supply portfolio. Such a portfolio involves the payment of hedge premiums that cost consumers money. Legislative amendment of this standard would allow this Commission to better develop competitive retail programs more optimally tuned to and consistent with market prices for the benefit of electricity customers.

With this said, I differ from my colleagues because attuning supply to market prices alone will not resolve the propensity of most customers to do nothing regarding their electricity supply, even in the face of very significant savings opportunities. Why? For starters, basic human nature leads to decision avoidance when the subject is not readily or easily understood. Unreasoning adherence to the status quo. Misguided loyalty to the distribution company when, in fact, it is indifferent if its customers switch away from default service to an energy supplier because it is paid for delivery, not energy supply. Needless fear of delayed supply restoration when, in fact, distribution companies are held to reliability standards and wish to keep their customers satisfied about distribution service. Wealth, where saving a hundred or a few hundred dollars a year is insignificant. Or just plain apathy.

Whatever the reason for these customers not choosing an alternative supplier, a "default" construct is simply not in their best interest.

Additionally, a spot and short term market-based default service model may present potential issues for low income customers who may see their bills fluctuate strongly upward under certain market and supply conditions. A retail opt-out program for these customers could help mitigate such volatility.

Furthermore, with less than stellar success, other, more mature retail electricity markets have experimented with more market-based, progressively shorter term supply portfolios and implemented monthly changes in default service prices. For example, in New York, such efforts of some utilities have resulted in a statewide residential shopping rate of only 24%, far less than what we have already achieved in Pennsylvania. Even in the best EDC market in New York, that of innovative Orange and Rockland Utilities (O&R), only a shopping level of 37% as of March, 2012, has been achieved after the sustained benefits of O&R's referral program initiated as far back as 2000, combined with early implementation of a purchase of receivables program.

For these reasons, it does not appear that merely *changing the underlying supply portfolio* will have a significant impact on encouraging most customers to shop for lower cost supply alternatives that are readily available on the Commission's website and actively marketed daily by numerous EGSs. It is only by *removing the barriers related to the current default service market structure* that the full benefits of competitive markets can be delivered to consumers.

Adopting a more short term market based default service will probably lead to lower, long term default prices to consumers (likely, but not necessarily, with even lower EGS offers), and remove potential boom/bust cycles in Pennsylvania's maturing retail electricity markets. But making only that major reform disserves the 70% of Pennsylvania customers who rely on this Commission to do what is necessary to make electricity choice really work. They rely on us to fashion the program—with legislative help if needed—to make it as easy as possible for them to make a decision in their best interests.

With the assurance conveyed by a Commission-backed opt-out process, customers will accept and even welcome the need to decide between staying one year with a competitively-determined supplier offering a significantly lower price than the default one, or opting to stay with the higher default rate.

My compliments and thanks to the OCMO staff who have labored so hard to move us forward, but, alas, not far enough.

With utmost respect to my colleagues whose minds can, admittedly, reasonably differ,

James H Cawley

DATE: September 27, 2012 **James H. Cawley, Commissioner**

RMI

Opt-Out Construct

Retail Opt-Out Product and Structure

- Eligibility – All Default Service residential and small commercial customers, including low income/CAP customers.
- Price – fixed price, 1 year
- Terms and Conditions: No switching restrictions, as long as the customer is on the opt-out product, and any extensions thereto. If customer opts into any subsequent product offering, all terms and conditions are determined by the contract. EGS Participants must offer net-metering pricing consistent with fixed-price bid.
- Auction Structure: Declining block Auction
- Auction Timing: March 15, 2015 Auction;
- Customer assignment – random customer assignment into tranches of customers
- EGS Market Share Caps: 50%
- Tranches: 10,000 residential customers; smaller EDC specific commercial customers tranches [could be smaller tranches for smaller utilities if necessary and appropriate]
- Consumer Protections: After 1 year, a one-year fixed price product would be the default; such 2 year extensions would be subject to market based rate cap [formulaic cap which is calculated using NYMEX forward prices for energy, and RPM and transmission capacity price changes, applicable to any contract price increases]. Bar on switching restrictions would continue, as long as the customer did not opt-in to an alternative product or offer indefinitely.
- Timing

  March 15, 2015 – Retail Opt-Out auction held.

  April 1, 2015 – Consumer Education material goes out to default service customers. Customers are informed that they will receive the one-year fixed priced, competitively bid supply from supplier X, and have 3 weeks to opt out, to receive a variable, quarterly changing default service price from their utility or an alternative DSP [function of whether or not the EDC petitions to exit the merchant role]. Customers also informed that the retail opt-out suppliers will receive necessary customer usage and enrollment information necessary to serve their requirements if they provide the customer supply.

  April 15, 2015 – EGS informed of customer opt-out elections by the EDC; EDCs provide EGSs necessary usage and enrollment information [including meter read schedule, budget billing status, CAP status, and net metering status] to enable EGSs to enroll the customers.

  April 15-May 15, 2015 – customer enrollments submitted by winning retail-opt out EGSs. EDCs modify enrollment letter response for default service customers accordingly, noting that they have been enrolled with the EGS pursuant to the lowest cost bidder(s) in the retail auction to provide their supply, and that customers continue to have the right to chose an alternative supplier at any time, without penalty, upon their own election to do so.

June 1-June 30, 2015 – customers begin receiving competitive supply under the retail auction.

Default Service

- Eligibility – residual customers who opt out of Retail Auction Opt-Out Product, and who do not choose an alternative EGS; customer's whose EGS has terminated service to customer, and whose customers do not thereafter select another EGS.
- Supply portfolio: residential and small commercial – litigated proceeding to determine prudent mix given the number of customers and transient characteristics of the residual default service customer profiles. [note – it is likely that if the number of customers are small and volatile, that a shorter term portfolio may be more prudent and recommended to avoid stranded costs]
- Supply portfolio: Medium and Large C&I – LMP (spot)
- Auction Process – RFP or declining block auction initially for wholesale supply bids to meet portfolio requirements.
- Transition to non-EDC Default Service Provider (DSP) – utilities to file alternative DSP program, if it is determined that they no longer have the economies of scale to efficiently provide default service. The EDC or another stakeholder can file a petition if they believe that default service can be provided more efficiently and cost effectively than the EDC.
- Default Service Reconciliation – residential and small commercial – quarterly reconciliation; medium and large C&I – monthly reconciliation initially. Reconciliation can be on a monthly basis for all classes upon changes in the statute.
- PTC – no change from today; consideration of additional merchant function charge, similar to that used in Maryland, to capture merchant costs not already unbundled from delivery rates. Eventually, all merchant related costs should be unbundled from base rates.

Related capabilities

- Net Metering – ensure that EDI transactions are consistent and adequate to convey usage information necessary to bill/refund/carry forward net metering usage information.
- Portability of low income credits