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August 20, 2020

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

Re: Petition of PECO Energy Company for Approval of its Default Service Program for the Period from June 1, 2020 Through May 31, 2025 – Docket No. P-2020-3019290

Dear Secretary Chiavetta:

Enclosed for electronic filing please find Electric Supplier Coalition's Main Brief with regard to the above-referenced matter. Copies to be served in accordance with the attached Certificate of Service.

Sincerely,

Karen O. Moury
Karen O. Moury

KOM/lww
Enclosure

cc: Hon. Eranda Vero w/enc.
Cert. of Service w/enc.

CERTIFICATE OF SERVICE

I hereby certify that this day I served a copy of the ESC's Main Brief upon the persons listed below in the manner indicated in accordance with the requirements of 52 Pa. Code Section 1.54.

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Dated: August 20, 2020

Karen O. Moury

Karen O. Moury

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Petition of PECO Energy Company for Approval of its Default Service Program for the Period from June 1, 2021 through May 31, 2025	: : : :	Docket No. P-2020-3019290

MAIN BRIEF OF ELECTRIC SUPPLIER COALITION

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I. INTRODUCTION AND SUMMARY OF ARGUMENT

By adopting the approach proposed by the Electric Supplier Coalition ("Coalition" or "ESC")[1] for the recovery of Network Integration Transmission Service ("NITS") costs, the Commission can ensure that both shopping customers and non-shopping customers are paying no more than the actual NITS costs incurred by load-serving entities ("LSEs") on their behalf. All LSEs, including both electric generation suppliers ("EGSs") and wholesale default service providers, incur NITS costs in the wholesale market. All customer load, including that of shopping and non-shopping customers, on an electric distribution company's ("EDC's) system is allocated a share of transmission service costs. While NITS costs have traditionally been difficult to predict, their uncertainty and volatility has been exacerbated by the recent approval of formula rates by the Federal Energy Regulatory Commission ("FERC"). Through formula rates, NITS charges can change very quickly and forecasting has become more challenging, which warrant a modification in the way these costs are recovered.

Today, and as proposed by PECO Energy Company ("PECO"), the recovery of NITS costs is handled differently depending on whether the customer is purchasing default generation service from PECO or purchasing competitive generation service from an EGS in the retail market. Under its proposal, PECO would continue to: (1) recover actual NITS costs for default service customers through a fully reconcilable bypassable charge in the price to compare paid by default service customers; and (2) leave the recovery of NITS costs for shopping customers to the EGSs, which must estimate the charges and determine whether and how much of a risk premium to include in the supply price. As a result of this inconsistent approach, only default

1 The Electric Supplier Coalition's members are NRG Energy, Inc., Direct Energy Services LLC, Interstate Gas Supply Inc., d/b/a IGS Energy, Vistra Corp., Shipley Choice LLC, ENGIE Resources LLC and WGL Energy Services, Inc.

service customers are assured that they pay no more than the actual costs of NITS. By contrast, shopping customers might pay more than their actual NITS costs, due to the inclusion of a risk premium in their supply price. This scenario creates an inherently unlevel playing field between PECO as the default service provider and EGSs selling electric supply in the competitive retail market. This inequity is made worse by the unpredictable nature and volatility of the actual NITS costs.

The difficulty of recovering the actual NITS costs from customers arises when LSEs need to predict future NITS rates and incorporate those predictions (aka "risk premiums") into their retail pricing. On June 27, 2017, PECO received FERC approval to implement a formula rate methodology for calculating NITS costs. This change substantially increases the difficulty of accurately predicting future NITS costs. The result is that either (i) the LSE will include risk premiums in supply prices that may cause customers to pay more than the actual NITS costs, or (ii) the LSE may have to absorb losses if it includes no risk premium or sets the premium too low to cover actual costs. Either outcome is harmful to customers - whether they are paying more than the costs or having less access to competitive offerings because suppliers cannot sustain long-term losses from failing to fully recover the actual costs of NITS.

Under the Coalition's proposal, PECO would recover actual NITS costs incurred by both wholesale default service providers (as it does today) and EGSs (which it does not do today) from all customers through a reconcilable non-bypassable charge in distribution rates. Both approaches make customers ultimately responsible for paying NITS costs that are incurred by the LSEs. However, the recovery of all NITS costs through a non-bypassable charge would mean that <u>all</u> customers would be paying <u>no more than</u> their actual NITS costs. Adoption of the Coalition's approach would eliminate the inequities created by the current practice of default service customers paying their actual NITS costs while customers of EGSs may also have to pay a risk premium included in their supply prices that may or may not reflect their actual NITS costs. It would also place PECO as the default service provider and EGSs selling electric supply in the competitive retail market on a level playing field with respect to the way that NITS costs are recovered and reflected in pricing.

II. PROCEDURAL HISTORY

Consistent with the requirements of the Electricity Generation Customer Choice and Competition Act ("Competition Act"),[2] PECO filed its Petition for Approval of its Default Service Program for the Period from June 1, 2021 through May 31, 2025 ("DSP V Petition") or March 13, 2020. Through its DSP V Petition, PECO proposed to establish terms and conditions under which it will procure default service supply, provide default service to non-shopping customers, satisfy requirements imposed by the Alternative Energy Portfolio Standards Act ("AEPS Act")[3] and recover all associated costs on a full and current basis. Notice of the filing was published in the *Pennsylvania Bulletin* on April 18, 2020. The Commission assigned the DSP V Petition to the Office of Administrative Law Judge ("OALJ") for hearing and decision. The OALJ designated Administrative Law Judge ("ALJ") Eranda Vero as the presiding officer.

The Coalition filed a Petition to Intervene on May 5, 2020. Members, affiliates and subsidiaries of the Coalition are licensed to sell electricity in the markets of Pennsylvania's major EDCs, including the service territory of PECO. Issues of interest identified by the Coalition included: (i) PECO's proposed default rate design; (ii) the proposal to solicit new ten-year contracts for Solar Alternative Energy Credits; (iii) the proposed time-of-use ("TOU") rate option; (iv) PECO's proposal for the recovery of NITS costs; (v) the proposed continuation of

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[2] 66 Pa.C.S.§§2801-2815.
[3] 73 P.S. §§1648.1 - 1648.8 and related provisions of 66 Pa.C.S §§2813-2814.

the existing Standard Offer Program ("SOP"); and (vi) the proposed plan for shopping by low income customers.

By Prehearing Order dated May 8, 2020, ALJ Vero granted the Coalition's Petition to Intervene. This order also adopted a litigation schedule providing dates for the submittal of pre-served testimony by the parties, an evidentiary hearing and the filing of briefs. As scheduled, the evidentiary hearing was held on July 30, 2020. During that hearing, the pre-served Direct Testimony and Surrebuttal Testimony of the Coalition's witness, Travis Kavulla, along with the accompanying exhibits, were admitted into the evidentiary record.[4]

Prior to the commencement of the hearing, PECO informed ALJ Vero of a partial settlement in principle among the parties, other than the Environmental Stakeholders. A Joint Petition for Partial Settlement ("Partial Settlement") was filed by the settling parties on August 13, 2020. Through that Partial Settlement, two issues were reserved for litigation, including TOU cost allocation and the recovery of NITS costs. As a signatory to the Partial Settlement, the Coalition filed a Supporting Statement explaining its reasons and identifying record references that are relevant to those issues. The Coalition files this Main Brief to oppose PECO's proposal for the recovery of NITS costs and to advocate for adoption of its alternative proposal.

III. <u>ARGUMENT</u>

NITS charges reflect an LSE's share of the transmission service rate. All LSEs, including EGSs supplying electricity to customers in the retail market and wholesale suppliers providing electricity for PECO's default service program, are assessed this wholesale cost by the PJM Interconnection L.L.C. ("PJM"). LSEs then allocate a share of transmission service costs to all customer load on an EDC's system, including that of shopping and non-shopping

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[4] The Coalition's Direct Testimony is marked as ESC Statement No. 1, which is accompanied by Exhibits TK-1 through TK-19. The Coalition's Surrebuttal Testimony is marked as ESC Statement No. 1-S.

customers.[5] The recent changes approved by FERC regarding how PECO establishes NITS charges has created more difficulties for accurately and timely predicting the future costs of NITS. Notably, formula rates result in annual changes to the NITS charges, while retail supply contracts often cover multiple years. PECO passes on the actual NITS costs to default service customers through its reconcilable processes. However, EGSs need to make predictions about the future cost of NITS and determine how to incorporate those forecasts into retail pricing. Moreover, EGSs do not have any "after the fact" way of reconciling their predictions with actual costs, meaning that customers may pay more for NITS or EGSs are forced to absorb the losses, which is not a sustainable long-term business model.[6]

A. <u>PECO's NITS cost recovery proposal treats shopping and non-shopping customers differently</u>

In its DSP V Petition, PECO proposes to continue its existing approach for the recovery of NITS costs, which is two-fold. For NITS costs associated with the default service load, PECO recovers the NITS costs for default service customers through its bypassable Transmission Supply Charge ("TSC"), which is a component of its price to compare for default service.[7] For NITS costs associated with shopping customers, EGSs must recover these costs through their supply prices.[8]

The difference between these two methods lies in how the LSEs have to factor in the NITS costs into their prices. EGSs must bear the risk of estimating NITS charges and may need to include risk premiums in the supply price. To the contrary, PECO's wholesale default suppliers bear no risk associated with NITS charges and the prices they bid to provide default service need not include any risk premiums. This means that shopping customers are paying

5 ESC Statement No. 1 at 31.
6 ESC Statement No. 1 at 33-36.
7 Petition, Para. 20; PECO Statement No. 1 at 15.
8 ESC Statement No. 1 at 33.

potentially widely differing amounts for NITS costs, depending on how much risk premium their EGSs factor into the supply price, which may or may not reflect their actual NITS costs. By contrast, non-shopping customers are paying only their actual NITS costs. This scenario creates an inherently unlevel playing field between PECO as the default service provider and EGSs selling electric supply in the competitive retail market. The inequities are exacerbated by the unpredictable nature and volatility of the actual NITS costs assessed on all LSEs.[9]

Especially with the volatility of these rates, PECO should not be permitted to protect itself (and auction winners) against the risk of those price fluctuations, while EGSs must absorb that risk in the prices they offer to retail customers in the competitive market.[10] Rather, it is appropriate to establish a level playing field and include NITS costs associated with both non-shopping and shopping customers in PECO's existing Non-Bypassable Transmission ("NBT") Charge.

B. <u>Recent FERC approval of formula rates have increased the volatility and unpredictability of NITS costs</u>

The Coalition is aware that in the past, the Commission has rejected proposals that would have required EDCs to be responsible for the recovery of NITS costs for all LSEs, citing a lack of evidence that the cost of NITS is volatile and unpredictable.[11] Notably, however, since the Commission last rejected such proposals, circumstances have significantly changed due to FERC's approval of "formula" rates for NITS charges. Under this new rate-setting approach, predicting NITS costs has become even more challenging for LSEs.

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[9] ESC Statement No. 1 at 33-34.
[10] ESC Statement No. 1 at 40.
[11] *See, e.g., Petition of PECO Energy Company for Approval of its Default Service Program for the period from June 1, 2015 through May 31, 2017,* Docket No. P-2014-2409362 (Order entered at December 4, 2014) at 53-54.

1. <u>Most transmission owners now charge "formula" rates</u>

In a major departure from traditional transmission ratemaking, most transmission owners in PJM now charge formula rates. This change promotes more frequent and sudden changes in NITS costs. Therefore, it is even more difficult for EGSs to estimate likely NITS costs over the term of the offers they make to consumers in the market.[12]

Traditionally, utilities had to file a rate case with FERC showing their alleged cost of service in order to justify significant rate increases. FERC-approved rates are "stated" rates, which are not subject to substantial change without rather involved regulatory proceedings. The length of those proceedings gave transmission customers like EGSs time to plan and forecast likely rate changes.[13]

More recently, through approval of formula rates, FERC has allowed transmission owners to change the rates more frequently and more quickly. As explained by Mr. Kavulla, the inputs to the formula rates include: (i) the capital investments a transmission owner *expects to make* next year; (ii) the operating expenses it expects to have to pay; and (iii) a return on the existing investments in its system. These rates are then trued up annually. As a result, if a transmission owner spent more or spent less than it initially projected, the rate can swing up and down in line with the under- or over-recovery.[14] Thus, NITS costs are in part driven by the transmission owner's managerial decisions on investments and accounting, which are not visible to EGSs.[15]

12 ESC Statement No. 1 at 35.
13 ESC Statement No. 1 at 36.
14 ESC Statement No. 1 at 36.
15 ESC Statement No. 1 at 34.

On June 27, 2017, PECO received FERC approval to implement a formula rate starting December 1, 2017, which allows PECO to receive current recovery of its costs.[16] PECO files its transmission formula rate update as part of an annual process to reconcile the prior year's rate to reflect any over- or under-recovery and to set the current year's rate based on projected costs. PECO filed its 2020 Formula Rate Annual Update on May 29, 2020.[17]

2. <u>The use of the formula rate has resulted in significant fluctuations in NITS charges</u>

Under the formula rate, each LSE's NITS charge is calculated by determining its daily Network Service Peak Load ("NSPL") and dividing its NSPL by the annual revenue requirement of the transmission owner's projected cost of service. NSPLs are updated annually based on the prior year's peak load, which can drive significant rate fluctuations. When NSPL changes unexpectedly due to load increases—or as we have more recently seen, load decreases due to the COVID-19 pandemic[18]—that affects the rate charged to LSEs.[19]

In his Direct Testimony, Coalition witness Kavulla provided concrete and compelling examples of the actual impacts on LSEs of NITS rate increases implemented through the formula rate. In one example, the Public Service Electric and Gas Company ("PSEG") filed an update on December 5, 2019, which resulted in a 30.7% increase in the NITS rate over the prior year – and

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[16] ESC Statement No. 1 at 36; *FERC Order Accepting and Suspending Filing, Subject to Refund, Establishing Hearing and Settlement Judge Procedures*, FERC Docket No. ER17-1519 dated June 27, 2017 available at: https://elibrary.ferc.gov/idmws/common/OpenNat.asp?fileID=14623778

[17] ESC Statement No. 1 at 36; PECO Energy Company Informational Filing of 2020 Formula Rate Annual Update, FERC Docket No. ER17-1519 dated May 29, 2020 available at: https://elibrary.ferc.gov/idmws/common/opennat.asp?fileID=15548295

[18] ESC Statement No. 1 at 37; PJM Details COVID-19 Impacts on Electricity Demand, Apr. 15, 2020. https://insidelines.pjm.com/pjm-details-covid-19-impacts-to-electricity-demand/ (accessed June 15, 2020).

[19] ESC Statement No. 1 at 36-37.

LSEs received approximately 25-days' notice of the change.[20] Below are similar increases for the FirstEnergy Companies:[21]

NITS Rates	Current NITS Rate	Current NITS Rate Effective Dates	Future NITS Rate	Future NITS Rate Effective Date
ATSI Zone	$55,074.34/MW/Year	Since January 1, 2019	$57,340.35/MW/Year	January 1, 2020
Allegheny Power Zone	$15,396.00/MW/Year	Since March 1, 2002	$15,396.00/MW/Year	March 1, 2002
MAIT Rates for ME & PN Zones	$28,796.22/MW/Year	Since January 1, 2019	$37,083.18/MW/Year	January 1, 2020

The Coalition also presented evidence showing that the actual costs of NITS have recently been increasing. Examples of these increases are shown in the table below:[22]

NITS Rates ($/MW-Y)	Jan-20	Jan-19	% Increase Jan 2019 - Jan 2020
MAIT	$37,083.18	$28,796.22	28.8
PPL	$68,031	$58,865	15.6
PSEG	$156,503.24	$119,735.80	30.7

3. NITS costs are very difficult to predict

The core issue is that NITS rates are unpredictable. One reason for the difficulty in tracking them is that one must know or estimate a number of factors related to transmission

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20 ESC Statement No. 1 at 37; Public Service Electric and Gas Company Informational Filing of 2020 Formula Rate Annual Update (Second Revision) FERC Docket No. ER09-1257 dated January 17, 2020 and available at: https://elibrary.ferc.gov/idmws/common/OpenNat.asp?fileID=15073350. The original filing for the 2020 Formula Rate Annual Update was October 15, 2019 and is available at: https://elibrary.ferc.gov/idmws/common/OpenNat.asp?fileID=15073350. PSEG filed several revisions to the original filing.

21 ESC Statement No. 1 at 38; https://www.firstenergycorp.com/supplierservices/pa/me_pn/NITSRateInformation.html

22 ESC Statement No. 1 at 39; Information from https://www.pjm.com/markets-and-operations/billing-settlements-and-credit.aspx under the heading "Network Integration Transmission Service Revenue Requirements & Rates."

projects. While PJM provides data related to each transmission owner's rates, that data must be verified against actual sources of new project information filings and updates. Since the rates are not final until approved by FERC, and are subject to adjustment during those proceedings, the available updates are not always timed in a way that allows an EGS to accurately estimate what NITS costs will be during the relevant contract period with its customers.[23] The witness for the Philadelphia Industrial Energy Users Group ("PIEUG"), Jeffry Pollock, claims that it is possible to anticipate changes in NITS costs because the formula rate uses FERC Form 1 data.[24] However, as Mr. Kavulla explained, the FERC Form 1 filings are made on a lagging basis, while formula rates are made on a forward basis. Also, they do not reflect the NSPL fluctuations or the volatility associated with forecasts of the roll-in to rates of large capital projects.[25]

Due to the unpredictability of the rates, EGSs need to forecast them, while PECO as the default service provider does not. Forecasting, as explained by Mr. Kavulla, will likely result in a risk premium being added to EGS pricing.[26] Besides the uncertainty associated with NITS rates, the EGSs have no control because the costs are driven by PECO's decisions on transmission spending. With the inputs the transmission owners make to the formula rate, they have even more control over these charges than they once did, which warrants a change in PECO's approach for recovering these costs.[27]

C. The Coalition's NITS cost recovery proposal treats shopping and non-shopping customers the same way

To address these inequities, the Coalition proposes that PECO include all NITS costs – those incurred by both wholesale default suppliers and EGSs – in its NBT charge, which is

[23] ESC Statement No. 1 at 38.
[24] PAIEUG Statement No. 1 at 6-7.
[25] ESC Statement No. 1-S at 25.
[26] ESC Statement No. 1 at 39.
[27] ESC Statement No. 1 at 39-40.

recovered from both shopping and non-shopping customers. Notably, this is the approach that PECO already uses for the recovery of other Non-Market Based ("NMB") charges, including Generation Deactivation/Reliability Must Run charges; Regional Transmission Expansion Plan charges; and, Expansion Cost Recovery charges (collectively, "Other PJM Charges"). The Other PJM Charges, like the NITS charge, are wholesale cost obligations assessed by PJM that all LSEs are required to pay.[28] All of these costs share a common theme in that they are not a function of market fundamentals and, therefore, can be subject to very significant changes over what can reasonably be anticipated.[29] Thus, the most equitable way to treat the recovery of these costs is to be consistent and recover all NMB charges from all customers.

Despite the Commission's prior rejection of the proposal advanced by the Coalition in this proceeding, the Commission has found that nothing in the Public Utility Code precludes the implementation of the approach for NITS recovery that the Coalition is proposing here.[30] Also, the Commission has been open to other alternatives to level the playing field for recovering NITS costs, which is shown through its approval of an approach that requires the wholesale supplier to include the costs of NITS as part of their bids to provide default service.[31]

Moreover, adoption of the Coalition's proposal would address the Commission's obligation in Section 2804(6) of the Competition Act. Under Section 2804(6), the Commission is obligated to require a public utility that owns or operates jurisdictional transmission and distribution facilities to provide transmission and distribution service to all retail electric customers and EGSs "on rates, terms of access and conditions that are comparable to the utility's

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[28] ESC Statement No. 1 at 31, 33.

[29] ESC Statement No. 1 at 32.

[30] *Joint Petition of Metropolitan Edison Company, Pennsylvania Electric Company, Pennsylvania Power Company and West Penn Power Company for Approval of their Default Service Programs*, Docket Nos. P-2013-2391368, P-2013-2391372, P-2013-2391375, P-2013-2391378 (Order entered July 24, 2014), at 38 ("*FE DSP III Order*").

[31] *FE DSP III Order* at 31-32.

own use of its system."[32] As PECO is using a different cost recovery method in providing transmission service to EGSs' customers than it is employing for its own default service customers, a modification is warranted to level the playing field and ensure compliance with Section 2804(6). By assuming the cost recovery responsibility for only the customers of wholesale default service suppliers, PECO unfairly places a competitive advantage on its default service because wholesale default service suppliers do not need to factor in the risk of future increases in NITS costs. The only way to ensure equal access to the transmission facilities and also ensure that all customers pay only the true costs of NITS is to adopt the Coalition's proposal for PECO to assume NITS cost recovery responsibility for all of the load on its system.

PECO's witness, John J. McCawley, P.E., raises concerns about two possible transition issues if the Coalition's proposal is adopted. Neither of those concerns should prevent the Commission's adoption of the Coalition's proposed approach. Mr. McCawley's first concern is that a shopping customer would pay twice for NITS, which he calls the "double-charge" problem. His second concern is associated with fairly unbundling bundled generation price agreements, which he refers to as the "unbundling" problem.[33]

Under Mr. McCawley's "double-charge" problem, he explains that when the EDC begins to charge NITS costs to all customers on a non-bypassable basis, some shopping customers may have contracts with EGSs that extend beyond that date and still reflect NITS costs. These customers could end up paying twice for NITS service. Mr. McCawley describes the "unbundling" problem as occurring when the EGS has structured its retail pricing in a way that combines generation and NITS into a single supply price. He states that even if the EGS agrees

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32 66 Pa.C.S. §2804(6).
33 PECO Statement No. 1-R at 17-18.

to credit the NITS component to the customer when the NITS charge becomes non-bypassable, the amount of the credit owed will not be clear and may require negotiation.

Both of the concerns raised by Mr. McCawley concern the impact on existing customers' contracts. However, as explained by Mr. Kavulla, neither concern is a barrier to implementing the Coalition's proposed NITS cost recovery approach, but rather represents transition issues. A reasonable transition mechanism could easily address concerns related to existing contracts with shopping customers. Mr. Kavulla noted that just as PECO did when it first created the NBT, the change in cost responsibility can be limited to only new charges associated with NITS occurring after the Commission's final order in this proceeding. By limiting the change in cost responsibility to new charges, there is no concern over "double recovery" or a need for "unbundling" of customers' existing EGS contracts. Alternatively, the change in cost responsibility could be deferred to a later date, such as June 2022, to provide a transition period during which many EGS contracts would expire and renew. The new renewal rates offered would reflect removal of the cost obligations from EGSs and address any concerns about existing contracts. In sum, a variety of transition mechanisms can be considered such that the Coalition's proposed method can smoothly be implemented without any adverse consequences.[34]

D. <u>The Commission should adopt the Coalition's proposed approach for the recovery of NITS costs</u>

By adopting the approach proposed by the Coalition for the recovery of NITS costs, the Commission can create a level playing field and ensure that both shopping customers and non-shopping customers are paying no more than the actual NITS costs incurred by LSEs on their behalf. All LSEs, including both EGSs and wholesale default service providers, incur NITS

[34] ESC Statement No. 1-S at 24.

costs in the wholesale market. All customer load, including that of shopping and non-shopping customers, on an EDC's system is allocated a share of transmission service costs.

Under the Coalition's proposal, PECO would recover actual NITS costs from all customers through a reconcilable non-bypassable charge in distribution rates. Recovery of all NITS costs through a non-bypassable charge would mean that customers would be paying their actual NITS costs. Adoption of the Coalition's approach would eliminate the inequities created by the current practice of default service customers paying their actual NITS costs while customers of EGSs are paying a risk premium included in their supply prices that may or may not reflect their actual NITS costs. It would also place PECO as the default service provider and EGSs selling electric supply in the competitive retail market on equal footing with respect to the way that NITS costs are recovered and reflected in pricing.

IV. CONCLUSION

For all the foregoing reasons, the Electric Supplier Coalition respectfully requests that the Commission (1) reject the proposal in PECO Energy Company's DSP V Petition to continue its existing approach for the recovery of NITS costs; (2) direct PECO to revise its cost recovery method to reflect the approach proposed by the Coalition of recovering all NITS costs through the Non-Bypassable Transmission charge; and (3) grant such other relief as may be appropriate.

Respectfully submitted,

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