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March 2, 2007

VIA HAND DELIVERY

James McNulty, Secretary
PA Public Utility Commission
Commonwealth Keystone Bldg.
2nd Fl., 400 North Street
P.O. Box 3265
Harrisburg, PA 17105-3265

Re: Rulemaking re Electric Distribution Companies Obligation to Service Retail Customers at the Conclusion of the Transition Period Pursuant to 66 Pa. C.S. § 2807(e)(2) Advance Notice of Final Rulemaking Order; Docket No. L-00040169

Default Service and Retail Electric Markets Proposed Policy Statement; Docket No. M-00072009

Dear Secretary McNulty:

Enclosed please find the original and 15 copies of the Direct Energy Services, LLC's Comments in the above-referenced matter.

If you have any questions regarding this filing, please contact me at your convenience.

Sincerely,



Kevin J. Moody

For WOLF, BLOCK, SCHORR and SOLIS-COHEN LLP

KJM/jls
Enclosures

cc: Shane Rooney (w/enc) Via E-mail

HAR:71713.1/DIR023-216494

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)
Advance Notice Of Final Rulemaking Order

Docket No. L-00040169

Default Service and Retail Electric Markets
Proposed Policy Statement

Docket No. M-00072009

COMMENTS OF DIRECT ENERGY SERVICES, LLC

INTRODUCTION

Direct Energy Services, LLC (“Direct Energy”) submits these comments pursuant to the Commission’s Advance Notice of Final Rulemaking Order (“ANOFR”) and its related Proposed Policy Statement Order (“Policy Statement”) adopted February 8, 2007. These two orders address the same matters. Accordingly, Direct Energy submits these comments in both dockets.¹ Direct Energy is currently licensed by the Commission to provide electricity and related services to all classes of retail customers throughout Pennsylvania.

Direct Energy applauds the Commission for its continued commitment to competitive market solutions to serve the consumers of the Commonwealth of Pennsylvania. Direct Energy supports the Commission’s evaluation and recommendations for default service rules to be implemented at the conclusion of the rate cap period.

¹ Direct Energy will be submitting separate comments to the other order adopted February 8, 2007, which addresses consumer education relating to the matters addressed by the above-captioned orders. *Policies to Mitigate Potential Electricity Price Increases*, M-00061957 (Tentative Order entered February 13, 2007) (“Price Mitigation” order).

At one point in the not-too-distant past, Pennsylvania was recognized across the country as one of the leading states in developing competitive energy markets. The long-term rate caps and stranded cost recoveries in most of the EDC territories have caused Pennsylvania to lose that crown. It is clear from the approach outlined by the Commission in its ANOFR, Policy Statement and Price Mitigation order that the Commission would like to reclaim that crown. The approach the Commission has taken in this endeavor demonstrates leadership by recognizing that POLR or default service procurement policy is not a stand-alone element of successful electricity market design. Electricity market design must consider issues such as demand response and environmental issues. It also must embrace several of the policy initiatives outlined by the Commission in its Policy Statement. It is clear from the linkage between the ANOFR and Policy Statement that this Commission is headed on the right path to a successful retail energy market. However, the Commission's new default service plan nonetheless falls short of complying with the requirement that post-rate cap default service rates must be based on "prevailing market prices."

Unfortunately, the **end-state** electricity market design is not a negotiable product. In the long-run, only one market design will work independently of Commission intervention. Under that design, the markets will work for all customers and customer classes. Anything short of that design results in the need for Commission intervention and policy initiatives to facilitate the development of the market until the regulatory community is satisfied that a fully competitive market has developed. What the Commission has laid out in its ANOFR, Policy Statement and Price Mitigation order is a set of policy initiatives that ultimately represent the **first step** out of the rate cap era. It is certainly **not the end-state**. The Commission clearly recognizes this in the issuance of its Policy Statement. There is more work ahead.

Absent the effective end state advocated in numerous proceedings by Direct Energy, the Commission will need to “manage” the EDCs/DSPs to ensure cooperation in a non-discriminatory manner in an effort to fully open the retail markets to viable and sustained competitiveness. It appears from the Policy Statement that the Commission is willing to “manage” the EDCs/DSPs in the short-run.

The Commission needs only to tweak its proposed final rules and effectively “manage” the behavior of the EDCs/DSPs in an effort implement the policies laid out in the Policy Statement. Under these provisions, which are outlined below, Direct Energy believes a vibrant competitive retail market will evolve in the Commonwealth.

Of course, as long as the EDCs own the DSP role, effective Commission “management” of their behavior will be required. While strong Commission oversight is not the preferred approach of Direct Energy, the current and proposed default service framework requires it.

I. Default Service Rates Should Reflect Current Market Conditions.

In this proceeding, the Commission has proposed that all default service customers be offered a single rate option known as the price to compare (“PTC”). The PTC is proposed to be adjusted at least quarterly for residential and small business customers and at least monthly for large business customers. The PTC concept, if implemented appropriately, should serve to benefit the market.

The Commission rightly believes that fixed rate options should be provided by the competitive marketplace. Direct Energy fully supports this conclusion. If a utility desires to enter the risk management business or the long-term contracting business, it should do so through a competitive affiliate, being bound by strict codes of conduct, and having its shareholders bear the financial risk of energy management. A utility should not be contracting long-term through a regulated ratepayer funded wires company.

1. Overall Procurement Strategy

The Commission is encouraging DSPs to “acquire a portfolio of generation supply products” instead of “simply procuring all generation at one time for the entire duration of the program. . . .” (ANOFR at 19). The Commission suggests that the DSPs should consider “fixed-term and spot market energy purchases, laddered contracts and the use of both supply and demand resources” (ANOFR at 20), in an effort to have the PTC price more accurately reflect the true market price. Direct Energy supports a market-reflective default service price.² However, as written, it is not outside the bounds of reasonableness to interpret the Commission’s language in these regulations in a manner such that a DSP could procure 90% or more of its power needs under multi-year contracts. In this circumstance the only “market-responsiveness” that will be seen is a slight movement in price when one contract rolls off and another rolls on. This is exactly the New Jersey result, which is not at all conducive to retail competition – and the procurement method and result the Commission expressly rejected (Policy Statement order at 4).

² Market-reflective default service rates are common in many markets around the country. Commissions have been very deliberate in moving to market-reflective rates. For example, in Maryland the Public Service Commission recently moved to quarterly pricing for the mid-size business customers in the state. The Maryland Commission described their decision in a compelling manner:

The Commission concurs with the parties that rate stability is an important public policy goal generally, and particularly with respect to SOS. Recent experience suggests that longer term fixed prices do not contribute to that goal; indeed they create a false sense of complacency that costs are in fact stable, followed by a painful transition when rates are finally adjusted to reflect current costs. . . . The upshot is that frequent, albeit small rate changes, are a better vehicle for insuring relative rate stability (and a more gradual reflection of changes in current market prices) rather than longer periods of frozen rates, followed by rate shock. (Maryland PSC, Case No. 9056, Investigation into Default Service for Type II Standard Offer Service Customers, Order 81019, issued August 28, 2006, at page 16.)

In New York, as the Commission in this ANOFR has recognized, residential customers see monthly market-reflective price adjustments. The Massachusetts utilities are required to implement a quarterly procurement of default service supply for medium and large commercial and industrial customers.

Procurement strategies like this will only enable the utility DSPs to maintain their monopolies over their customers.³

The express right of retail customers to direct access, along with the prevailing market prices requirement for post-rate cap default service, should guide the Commission's regulatory approach and the DSP's procurement strategy, and thus permit the competitive market and customer choice to provide customers with the means to mitigate post-rate cap price increases.

Under the proposed framework, the Commission **needs to be more prescriptive** in its approach, requiring a substantial portion of the DSP's power needs in each DSP's first default term to be procured in contracts of a duration no longer than three months. With this as a starting point (and assuming the other programs outlined are implemented), competitive suppliers will be more likely to enter the market. Absent guidance of this nature, retail competitors such as **Direct Energy will be reluctant** to invest in a residential marketing program.

As the Commission gets more comfortable with the development of the competitive market, it needs to move the DSPs to an Orange & Rockland⁴ style market where, as the Commission noted, "retail customers are charged a 'market supply charge' which changes every month." (ANOFR at 20). The Commission should provide guidance in its Policy Statement that it expects that effective retail competition will begin to materialize after the rate caps expire and, if it does, that in future default service periods an increasingly larger percentage of power must

³ New Jersey has over 3.2 million residential customers being served under laddered contracts. As of December 2006, none of these customers were being served by competitive suppliers. See: <http://www.state.nj.us/bpu/energy/elecSwitchData.shtml>.

⁴ It should be noted that while Orange & Rockland is a reasonable competitive market, it too, has not reached the ideal competitive end state. Its market supply charge giving rise to monthly price adjustments is a positive step, but the utility is still not procuring all of its power in the short term markets.

be procured under shorter-term contracts, ultimately arriving at the goal of monthly or shorter period pricing for all customers.

The Commission understands that “Pennsylvania’s residential gas customers, most of whom are also customers of EDCs, are well accustomed to having their gas rate adjusted quarterly.⁵ We expect that retail electric customers can manage quarterly adjustments as well.” (ANOFR at 19). Direct Energy agrees with this conclusion. Consumers are fully capable of responding to market-based electricity pricing signals and contracting for products they so desire. Consumers make such decisions – some of a much greater financial magnitude – on a daily basis, such as in the procurement computers, credit cards, cars, mortgages, insurance products, cell phones and other products.

2. Long-Term Contracting Should Be Kept To A Minimum.

The Commission appears to be a bit confused on the long-term contract issue. On the one hand, it states that “[l]ong-term contracts should only be used where necessary and required for DSP compliance with alternative energy requirements, and should be restricted to covering a relatively small portion of the default service load.” (Policy Statement, § 69.1805). Direct Energy fully supports that guidance. But, on the other hand, the Policy Statement advises that for residential customers the DSP should consider “procuring most fixed-term supply through full requirements contracts of one to three years in duration.” (Policy Statement order at 4). Most economists would agree that “long-term” is more than one-year. Most customers also believe that “long-term” is more than one year. FERC agrees that long-term is more than one

⁵ While Pennsylvania customers certainly have proven themselves to be comfortable with quarterly adjustments, it should be pointed out that the quarterly gas cost adjustment process in Pennsylvania requires substantial change and improvement. Given that this proceeding focuses on power issues, Direct will comment only briefly on this issue below and reserve further comments on this point to other dockets.

year.⁶ Direct Energy is in agreement that “long-term” is greater than one year and that the use of long-term default service contracts should be kept to a minimum.⁷

The Commission seems to have given a lot of deference to IRRC’s comments in this proceeding, accommodating many of their recommendations. However on what is a very important issue to the long-term viability of competitive markets, the Commission appears to have overlooked IRRC’s suggestions. In their comments, even IRRC realizes the importance of the contract term issue. IRRC states:

We believe this provision [default service term] is important because it will directly affect the procurement strategies of the DSPs and will influence how closely rates for default service will reflect prevailing market prices.

We believe it is appropriate for default service implementation plans to include details on a DSP's procurement strategy which may call for a portion of the energy to be provided under contracts with a duration of more than 12 months. However, the PUC should be cautious about approving plans that will remain in effect for multiple 12 months periods because they may not reflect the prevailing conditions in wholesale energy markets. Where DSPs want to enter long term contracts with energy suppliers, **we recommend that only a limited portion of the energy purchased be for a term of service of greater than 12 months and that the term of service be no longer than 36 months.** (IRRC Comments, ¶ 7, Section 54.185(c))

Long-term contracting for power by the DSP raises the fundamental issue of whether any competition that may happen to occur in the retail markets will be sustainable. Even if many long-term contracts are laddered on top of one another, just one long-term contract could render the PTC "out of market" and, thus, render the retail market non-competitive for the duration of

⁶ FERC views any wholesale supply contract over one year in duration as a “long-term wholesale contract.” See, e.g., *Notice of Proposed Rulemaking* (July 26, 2001), FERC Docket No. RM-01-8-000 at 4, n. 11 (citing Prior Notice Order, 65 FERC ¶ 61,984).

⁷ In two recent developments, long-term contracts for default supply have been rejected by utilities. First, in Delaware, Delmarva Power issued a bid evaluation report to its Commission suggesting that long-term alternatives that the Commission desired were too risky and too costly. See Report on Evaluation of Bids Submitted in Response to Delmarva Power & Light company’s RFP, Delaware PSC Docket No. 06-241. See also: *Rhode Island PUC OKs National Grid RFP*, MW Daily, February 27, 2007, p. 6. National Grid supported short-term RFPs because long-term proposals were priced with a premium.

that contract. Accordingly, it is important not to allow gaming by the EDC/DSP so it can continue its monopoly power over its customers through the use of long-term contracting. Even if the EDC/DSP does not exercise its ability to keep competitors out of the market by employing long-term contracts, **just the threat** that this potential exists may serve to keep suppliers out of the market.

In each respective DSP territory, it should be clear from the Commission that a substantial majority of the contracts should be for a duration of no more than three months. The Commission should also make clear through its Policy Statement that its intent is to move the DSPs away from a long-term portfolio and into a short-term portfolio. Again, evidence shows that in markets where the default service is market-responsive, the retail markets have developed. This includes residential markets in New York and Texas. In markets where the default service is long-term, no meaningful competition has evolved. These conclusions encompass many markets, including the majority of Pennsylvania regions and all business customers in New Jersey up to 1,250 kW.

3. Residential and Small Business Customers

The Commission has suggested that for residential and small business customers, default service rates will be adjusted at least every quarter. Direct Energy supports this mechanism as a starting point for the post-rate cap transition period. However, as mentioned above, the rate changes must be related to the true changes in the market, not just moving up or down because a multi-year long-term contract has expired and a small portion of the DSP portfolio is moving to a more contemporary price. In other words, as a starting point in the post-rate cap era, a significant majority of DSP contracts must come up for renewal on a quarterly basis.

Direct Energy supports positioning residential customers and business customers with peak capacities of under 25 kW into the same classification. However, Direct Energy also

believes that all programs made available to residential customers (e.g., purchase of receivables ("POR") programs and rate shock mitigation programs) should be made available to the business customers in this class. If a business is burdened with residential customer rules, they should have equal access to residential customer benefits.

The Commission noted that it is giving the DSP some flexibility in determining the divisions of customers to preserve existing rate schedules. Direct Energy supports a uniform definition of default service customers and customer classes across the state. Right now, in Western Pennsylvania, it is possible that a small commercial chain would have facilities classified differently in the Penn Power, Duquesne and Allegheny service territories under the Commission's final rule. Leaving the discretion to the utility DSPs could ultimately cause much confusion at the customer level. One customer with three stores, located within about 40 miles of each other, could have three different sets of rules governing its stores. Direct Energy has witnessed this first hand in Maryland where several small commercial entities argued for a low threshold (25 kW) to be classified as small, and they argued for a state-wide definition of what constitutes "small."⁸

4. Mid-sized Business Customers

The Commission has also proposed quarterly pricing adjustments for mid-sized business customers. This Commission should look to Maryland for some guidance in this proceeding. In Maryland, the PSC ordered that 100% of power in this mid-sized customer market (Maryland definition of mid-size is between 25 kW and 600 kW) be procured on a quarterly basis. By the

⁸ Brief of the Mid Atlantic Aggregation Group Independent Consortium, In the Competitive Selection of Electricity Supplier/Standard Offer or Default Service for Investor-Owned Utility Small Commercial Customers and Allegheny Power, Delmarva Power and Light and Potomac Electric Power Residential Customers, MD PSC Case No. 9064. Go to: <http://webapp.psc.state.md.us/Intranet/CaseNum/CaseForm.cfm>. Enter "9064" and see document number 81, filed October 10, 2006.

end of January 2007, 51.8% of mid-size business customers and 66.5% of the electric load consumed by mid-sized business customers was served by competitive suppliers.⁹ The market penetration by retail suppliers has been very robust, predominantly because of the market-responsive nature of the default service in the state. The Commission should look to the results in Maryland in this market segment and be a little more courageous. Direct Energy recommends that most, if not all of this customer class' default service requirements be procured in contracts that are no longer than three months. The Commission should provide guidance in its Policy Statement that it expects 100% of the default energy for this segment to be procured under quarterly or shorter contracts after the first post-rate cap default service program.

5. Large Commercial Customers

The Commission has suggested that the PTC for large business customers (those over 500 kW peak load) be adjusted on a monthly basis, or more frequently. Direct Energy supports moving large business customers to hourly or day-ahead pricing. Every energy market that has moved to competition at the retail level has seen nearly 100% of the large customers that are put on hourly default service move to competitive supply very rapidly. Fixed price products are also available from competitive suppliers to large customers that desire them.

The large customer class is defined differently in markets around the country, but no matter where the threshold is set, suppliers enter the market and offer energy products and services. In Duquesne Light's service territory, where the threshold is set at 300 kW, 86% are being supplied competitively as of January 1, 2007.¹⁰ New Jersey sets the level significantly

⁹ See <http://www.psc.state.md.us/psc/electric/enrollmentrpt.htm>.

¹⁰ See OCA's Pennsylvania Electric Shopping Statistics, found at: <http://www.oa.state.pa.us/Industry/Electric/elecstats/Stat0107.pdf>.

higher at 1,250 kW, but competitive supply is delivered to 85% of the load.¹¹ In Maryland, where the threshold is 600 kW, 94% of the load is on competitive supply.¹² In Texas, customers over 1,000 kW were thrust into an environment with no tariff protection at all (not even an hourly service backstop) on the first day the market opened in 2002. While statistics are not reported in this customer class, 100% of them must be on competitive supply contracts. In each market, no matter the threshold, if customers see a real-time price signal from the default provider, the competitive retail market will evolve and provide customers solutions.

Direct Energy also supports lowering the threshold for the large business classification to 300 kW. This classification level has been tried and has proven to be effective in Pennsylvania already. Duquesne Light's POLR III filing set the large business customer hourly priced service threshold at 300 kW. As mentioned above, supplier responsiveness has been overwhelming with 86% market penetration.¹³ The Commission should implement this threshold as the definition of large business customers across the state.

II. AEPS Procurement Should Be Undertaken By The EDCs Or, Alternatively, Undertaken By The DSP And Sold At Cost To The Competitive Suppliers Entering The Market.

As outlined in the Commission's Policy Statement, AEPS procurement can create many problems in the market. The Commission states that "[m]any parties have asserted that the portfolio requirement of the Alternative Energy Portfolio Standards Act of 2004, 73 P.S. § 1648.1, *et seq.*, cannot be satisfied without the use of long-term power purchase agreements between DSPs and alternative energy suppliers." (Policy Statement order at 5). Direct Energy

¹¹ See: <http://www.state.nj.us/bpu/wwwroot/energy/CIEP.pdf>.

¹² See: <http://www.psc.state.md.us/psc/electric/enrollmentrpt.htm>.

¹³ Duquesne has also proven that moving the customers to hourly service doesn't necessarily mean that they leave the Company's service. They just leave the utility-owned default service. According to its publicly filed documents, Duquesne has a sizable competitive retail business through an affiliate.

does not agree with those “many parties” as Direct Energy has witnessed the development of renewable resources around the country based on market dynamics such as simple demand and “Credit Cap and Trade” type programs. Direct Energy has itself signed long-term purchase agreements for off-take for several hundred megawatts from wind-energy farms.

However, if this Commission determines that regulated long-term contracts are the best way to assure that the necessary AEPS resources are built, it should look to have the EDC procure the AEPS requirements for its entire service territory on a long-term basis and require the EDC to sell the AEPS requirements to the suppliers (including both the DSP and competitive suppliers) at cost. Alternatively, the Commission could require that the DSP fill this role. The DSP would sign the long-term contract and be required to sell off bits and pieces to competitive suppliers at cost. Either of these approaches would allow all market participants to be in compliance with the requirements in a manner that is competitively neutral.¹⁴

III. A Transparent and Competitive Default Bidding Process is the Bedrock of Efficient Energy Markets.

The Commission correctly refers to the declaration in the Electric Competition Act that: “Competitive market forces are more effective than economic regulation in controlling the cost of generating electricity.”¹⁵ Direct Energy agrees that competitive market forces are best at controlling the cost of electricity, and that transparent and competitively bid products are the most reasonable approach to ensuring a prevailing market price for all DSP customers. “Black box” price calculations and “back room agreements” that generate default prices should be expressly forbidden. A robust competitive market exists at the wholesale level where DSP products can be obtained readily. Maryland, the District of Columbia, Delaware and New Jersey

¹⁴ Only EDCs are permitted full and current recovery of the costs of complying with the AEPS requirements. 73 P.S. § 1648.3(a)(2)(ii).

¹⁵ ANOFR at 14-15 (citing 66 Pa. C.S. §2802 (5)) (emphasis in original).

all contract for default supply in competitive auctions. In the most recent bid for Maryland default service, BG&E was seeking bids for 450 MW of load. It received 67 bids from 11 different suppliers for the nine 50 MW tranches.¹⁶ A competitive procurement process is very feasible for each of the EDC territories in this Commonwealth.

Direct Energy has no concerns with the Commission's recognition that sometimes a "circumstance" might require a DSP to enter into a bilateral contract; however, that "circumstance" cannot become the general practice, or else the Commission's efforts on default pricing and their concomitant benefits will be defeated. Nor does Direct Energy have significant concerns with requiring DSPs with aggregate loads under 50 MW to coordinate their procurement.

IV. Rate Reconciliations are not Necessary and Distort the Competitive Markets.

As part of the quarterly-adjusted PTC rate, the Commission would encourage, but not require, interim rate reconciliation to correct under and over-collections. Direct Energy is opposed to such market distorting adjustments. In fact, the suggestion that the DSP would be allowed reconciliation is an admission that the Commission needs to allow the utilities to "correct" prior hedging mistakes. In essence, reconciliations are nothing more than stranded cost recoveries that distort true market price signals significantly.

We have seen first hand in Pennsylvania's gas markets that reconciliations create distortions in the market and make it very difficult for suppliers to maintain a competitive position in the market. This issue was raised in the Commission's Report on Competition in

¹⁶ *Vantage Consulting Inc, Initial Report on Standard Offer Service Bidding Process and Interim Results for 2007 Reserve Tranche*, Submitted to the Maryland PSC In the Matter of Competitive Selection of Electricity Supplier/Standard Offer or Default Service for Investor - Owned Utility Small Commercial Customers; and for the Potomac Edison Company D/B/A Alleghany Power's, Delmarva Power and Light Company's and Potomac Electric Power Company's Residential Customers, Case No. 9064, February 27, 2007.

Pennsylvania's Retail Natural Gas Supply Market.¹⁷ The rate reconciliations could skew the PTC so as not to be reflective of current market conditions, thereby making it more difficult for competitive suppliers to offer a comparable or better rate.

There are two minor provisions that need to be implemented that would alleviate the need for reconciliation. First, the Commission should limit the amount of financial exposure a DSP could take in procuring DSP power. In fact, many default service models exist where no commodity risk is borne by the DSP. These are primarily load following contracts procured by the DSP in competitive solicitations. Second, the DSP could be allowed to recover a simple adder in its retail rates, which could be capped at some level by the Commission. The DSP would have to manage to keep its operations costs within the adder. There need not be any true-ups of the adder, or its components.

The combination of a retail adder that will enable the DSP to "recover fully its costs" and a commodity risk-free procurement strategy, completely mitigates the need for any type of reconciliation mechanism on the energy component. The competitive wholesale market will eliminate commodity risk for the DSP. The competitive retail market will keep the retail adder in check.

V. The Price to Compare Should Reflect All the Costs of Providing Default Service.

Through the ANOFR, the Commission seeks a PTC that would "recover all default service costs for an average member of a customer class. Default service costs shall not be recovered through the distribution rate, and distribution costs may not be recovered twice as a result of any reallocation that occurs as a result of this rulemaking." (ANOFR at 17). The Commission has stated that "distribution rates will be examined in each EDC's next rate case or

¹⁷ Docket No. I-00040103, Report to the General Assembly on Competition in Pennsylvania's Retail Natural Gas Supply Market, October 2005, pages 55-60.

a special cost allocation proceeding to resolve the issue of embedded costs.” (ANOFR at 17-18). Direct Energy supports the Commission’s proposal to examine utility cost allocations to ensure that the PTC reflects all the costs of providing default service. Distribution rate unbundling will ensure that consumers see and understand the full extent of the costs associated with utility default service and permit consumers to make accurate, informed comparisons with competitive offerings. Also, unbundling ensures that customers on retail choice contracts will not be paying energy-related costs to both their EGSs and to the EDCs.

However, unbundling must be done in a prudent manner. In the Commission’s accompanying Policy Statement, a utility purchase of supplier receivables concept is encouraged. In order to maximize market efficiencies, only one residential billing and collections system is needed. It is extremely inefficient from a market perspective to have one monopoly billing system and several others trying to compete with it. Therefore, as long as the customer relationship is shared (energy and transportation), then whoever owns the customer relationship should own the credit and collections process. As long as the EDC/DSP owns the customer relationship, the EDC/DSP should be required to perform consolidated billing and collections services if the customer requests it, just as if they owned the full relationship with the customer, no matter what party is serving the electricity portion of the relationship. Under the existing Pennsylvania framework, the EDC will always own the customer relationship. If a supplier and an EDC dual bill a customer and the customer pays the supplier, but not the EDC, the EDC will terminate the customer’s service. The opposite is not true.

VI. Default Service Should Ultimately Be Rendered by a Competitive Supplier.

The ANOFR explicitly acknowledges that a Commission-approved alternative EGS can also serve as the DSP in a utility service territory. The proposed rules outline three approaches under which this transition can occur: (1) the EDC can petition to be relieved of the default

service obligation; (2) a competitive supplier can petition to be assigned the default service role; or, (3) the Commission can propose to relieve a utility of the default service obligation by its own motion. (ANOFR at 7). Direct Energy supports these approaches, but submits that there may be other circumstances under which an EGS could become a DSP. The Commission has been granted the authority pursuant to the Electric Competition Act to approve an alternative supplier as the DSP.¹⁸ The Commission should not limit its flexibility by attempting to identify all of the circumstances which may lead to a competitive supplier becoming a DSP. Direct Energy suggests adding a fourth category which would be more encompassing, stating that an EGS can serve as the DSP under any other conditions that are deemed reasonable and approved by the Commission.

VII. The Commission's Regulatory Assessment.

The Commission has proposed that the DSP, whether an EDC or an EGS, will be subject to the Commission's regulatory assessment. **This policy should be revisited** prior to releasing a final rule. In this instance, the Final Rule needs to differentiate between the regulated wires company (EDC) and the DSP. The most efficient manner for the Commission to collect its regulatory assessment is through the EDC. This is where the assessment is collected today. The EDC rates are paid by everyone on an equal basis. All kWh will be delivered by the EDC, no matter which electricity supplier the customer uses (DSP or EGS). In the end state of competitive markets, the DSP will have no customers, or could have just a few customers for short periods of time over the course of the year.¹⁹ The Texas POLR providers, for example, serve virtually no load. If an allocation of Commission costs is made based on revenues, some

¹⁸ 66 Pa. C.S. § 2807(e).

¹⁹ "If a customer contracts for electric energy and it is not delivered or if a customer does not choose an alternative electric generation supplier, the electric distribution company or commission-approved alternative supplier shall acquire electric energy at prevailing market prices to serve that customer and shall recover fully all reasonable costs." 66 Pa. C.S. § 2807(e)(3).

DSPs could end up paying virtually nothing compared to other DSPs in the state. Taken to the limit, if the electricity markets were totally competitive, the DSPs would have no customers or revenues and the Commission's allocation of costs would be zero to these DSPs. This assessment should stay on the EDCs.

VIII. Competitive Retail Markets.

The Commission's Policy Statement outlines six (6) different policy positions or programs that are linked directly to the success of retail markets. Each of them, in its own way, serves to “level the playing field” between DSPs and EGSs. Direct Energy supports each of these policies entirely. Information and data access is vitally important to the success of competitive electricity markets. Specifically, as more advanced metering initiatives become available, it will be absolutely critical that the competitive market have this information available to them on a real-time basis so that all customers can receive the benefits of the advanced metering. But even more importantly than what is outlined, customers should have portable access to their data so that a customer can log onto a website to authorize the release of its data to a supplier. It should be made available, like cell phone data today, so that a customer need not know his or her account number to access it. A phone number, or Social Security number, or some other reasonable means of identification should be the threshold for data access.

It is Direct Energy's belief that functional rate-ready billing systems are currently in place in four of the six EDCs in Pennsylvania. Only two additional companies will have to make the investment in rate-ready systems over the coming years to facilitate this policy.

Purchase of receivables programs have been discussed above in this document. These programs are the most efficient way from a system-wide basis to facilitate billing and collections for residential and small business customers. If implemented prior to markets truly opening, the economics of such programs are crystal clear.

Customer referral programs assist the market in several ways. Most importantly, they help educate customers about energy alternatives. They lead to efficiencies in the market and they help move customers off the default service.

A uniform supplier tariff across the state would streamline the market immensely. One of the biggest hurdles a competitive retail supplier faces is the multitude of different rules not only between states, but between utilities within a state. This is certainly true in Pennsylvania. Among other aspects of a retail business, a uniform tariff streamlines operations and compliance, and is especially critical in Pennsylvania in view of the flexibility provided to the DSPs otherwise by the ANOFR and Policy Statement.

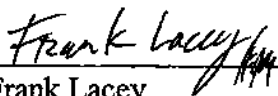
Finally, the Commission proposes a retail choice ombudsman within the Commission and within each EDC. This trend was started by New York. That office was extremely instrumental in developing the retail markets in New York. Recently, the Illinois Governor signed legislation creating a New York-style Office of Retail Market Development. Maryland has bills pending in both houses of the State Legislature this 2007 session to create a similar position within its Commission. Pennsylvania is showing leadership in this arena on two fronts. First, it is proposing this office before the rate caps expire. New York did it when rate caps were not an issue. Illinois implemented the law as rate caps were expiring. Maryland is one year beyond rate cap expiration. The Pennsylvania ombudsman will be on the ground in advance of the caps expiring. Second, Pennsylvania is suggesting that each EDC employ a retail choice ombudsman as well, to monitor the market and act as somewhat of a liaison between the EGSs and the EDCs. This would be a very positive step forward.

Direct Energy enthusiastically supports each and every one of these retail market developing initiatives outlined in the Policy Statement.

IX. Conclusion

The Pennsylvania Commission has demonstrated significant leadership in developing these proposed final rules in conjunction with its Policy Statement and its Price Mitigation order. The combined resolution of the issues raised and outlined in these orders demonstrate a significant understanding of many of the complex issues involved in successful default service design. While Direct Energy does not believe that the policies outlined in these orders represent a viable end state, we do largely support the concepts outlined. A few provisions need to be tweaked, and stronger guidance needs to be given to the EDCs/DSPs in a few areas. If, and only if, these changes are made, Direct Energy believes that Pennsylvania will be recognized as one of the national leaders on energy competition once again.

Respectfully submitted,



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Dated: March 2, 2007