

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Investigation of Pennsylvania’s)
Retail Electricity Market) **Docket No. I-2011-2237952**

**Comments of the
National Energy Marketers Association**

The National Energy Marketers Association (NEM)¹ hereby submits its comments on the questions set forth in the Commission’s Order of April 28, 2011, in the above-referenced proceeding [hereinafter “Order”] for the purpose of initiating an investigation into the retail electricity market in Pennsylvania, “with the goal of making recommendations for improvements to ensure that a properly functioning and workable competitive retail electricity market exists in the state.” The questions in the Order mark the beginning of the initial phase of this two phase investigation. The first phase of the investigation being aimed at, “assess[ing] the status of the current retail market and explor[ing] what changes need to be made to allow customers to best realize the benefits of competition.” The second phase, “will examine and address how to best resolve the issues raised and implement the prudent changes identified based upon [the Commission’s] review of the comments received during the initial phase.”

NEM strongly supports the retail choice program initiatives the Commission has adopted to facilitate retail market development thus far. Going forward, NEM recommends, as set forth more fully herein, that default service in its current form should be considered as a transitional step to the utilities exit from the merchant function. The next step in market evolution should be the provision of increased market-based pricing signals for no-notice default commodity service. The final step should be the provision of default service by the competitive marketplace. By virtue of these measures, consumers throughout Pennsylvania will realize the full benefits of energy choice.

1. What is the present status of competition for retail electric generation for customers, by class and service territory, and for alternative suppliers?

In preparation for the expiration of the rate caps in PPL on December 31, 2009, and subsequently followed in the service territories of PECO, MetEd, Penelec and Allegheny on December 31, 2010, the Commission identified a number of barriers to retail competition and solutions. These

¹ The National Energy Marketers Association (NEM) is a non-profit trade association representing both leading suppliers and major consumers of natural gas and electricity as well as energy-related products, services, information and advanced technologies throughout the United States, Canada and the European Union. NEM’s membership includes independent power producers, suppliers of distributed generation, energy brokers, power traders, global commodity exchanges and clearing solutions, demand side and load management firms, direct marketing organizations, billing, back office, customer service and related information technology providers. NEM members also include inventors, patent holders, systems integrators, and developers of advanced metering, solar, fuel cell, lighting and power line technologies.

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included: 1) Implementation of a purchase of receivables (POR) program; 2) Improving data access for suppliers by revising EDI transactions; 3) Utility provision of bill ready and rate ready billing; 4) Requiring timely utility completion of EDI certification and recertification; 5) Provision of updated customer lists to suppliers; 6) Conduct of a customer awareness education program about electric power choices and how to contact competitive suppliers; 7) Development of a uniform supplier tariff; and 8) Requiring the appointment of utility ombudsmen.² Additionally, the Commission established its Office of Competitive Market Oversight, and Commission Staff has proactively engaged stakeholders in identifying and resolving competitive market issues as they arise through its leadership of the CHARGE process. These market measures provided precisely the “jump start” to mass market competition that the Commission envisioned. A number of statistics relevant to the present status of competition reveal this to be true.

In particular, the present status of competition can be measured by the following indicia: number of customers migrated, amount of load migrated, number of competitive suppliers making offers indicating ease of competitive entry, and differentiated product offerings. As shown on the Commission’s PAPowerSwitch website, 1,146,479 electric customers have migrated, representing 20.3% of total customers and 49.66% of load.³ Over 925,000 of those are residential customers (representing an 18.7% migration rate), over 200,000 are commercial customers (representing a 29.4% migration rate) and over 7,500 are industrial customers (representing a 59.1% migration rate). While C&I customer participation in the retail energy market had been relatively well established when the rate caps expired, residential customer participation was limited. The growth in mass market customer participation in energy choice, particularly in the PPL and PECO service territories, has been truly exceptional. Indeed, in October 2009, there were no residential consumers participating in choice in the PPL service territory.⁴ Less than two years later, over 470,000 residential consumers are participating in choice in the PPL service territory alone.⁵

The Commission’s website shows 205 licensed electric aggregators, brokers, marketers, and consultants operating in Pennsylvania. Marketers have made a significant resource investment in the utility service territories to serve consumers with an increasingly expanding array of energy products and services. Competitive offers in the marketplace include multiple fixed and variable rate plans as well as green power rates. These product offerings will continue to evolve as the marketplace continues to mature.

Clearly, the leadership the Commission exhibited in identifying barriers to retail competition and acting to remove those barriers has yielded increased energy choice opportunities for consumers and facilitated supplier entry and participation in the Pennsylvania market. The Commission is to be commended for the bold decisions it made to effectuate the requirements of Pennsylvania law that consumers be provided with meaningful energy choice.⁶

² Docket No. M-2009-2104271, PPL Electric Utilities Corporation Retail Markets, Opinion and Order, August 6, 2009.

³ Pennsylvania Public Utility Commission, Weekly PAPowerSwitch Update, June 1, 2011.

⁴ Pennsylvania Office of Consumer Advocate – Electric Shopping Statistics.

⁵ Pennsylvania Public Utility Commission, Weekly PAPowerSwitch Update, June 1, 2011.

⁶ There is an affirmative requirement that consumers in Pennsylvania be provided with meaningful energy choice options on a sustained, continued basis. The Competition Act in Section 2804(2) states that, “[T]he commission **shall** allow customers to choose among electric generation suppliers in a competitive generation market through

Just as the Commission foresaw the need for retail market measures to jump start retail competition at the expiration of rate caps, the Commission in the instant case has also foreseen that certain overarching market design issues have been and will continue to prevent the realization of a fully competitive market. Additionally, as the foregoing migration statistics reveal, progress in retail market development has not been proceeding at the same pace in all utility service territories. The economics of supplier entry in more rural service territories differ and may warrant different approaches to the achievement of a fully competitive market. As discussed more fully herein, these market design issues include the provision of true market-based pricing signals as well as the proper allocation of costs between the utility's no-notice, default commodity service rate and its delivery service rate. Moreover, a truly competitive market cannot be attained so long as utilities remain in the merchant function with the associated level of regulatory intervention required to attempt to maintain a level competitive playing field.

2. Does the existing retail market design in Pennsylvania present barriers that prevent customers from obtaining and suppliers from offering the benefits of a fully workable and competitive retail market? To the extent barriers exist, do they vary by customer class?

Notwithstanding the implementation of the retail choice measures identified in PPL and subsequently implemented at other utilities to reduce barriers to competition, chief among them being POR, there are overarching retail market design issues that prevent consumers from realizing and suppliers from offering the benefits of a fully workable and competitive retail market. Retail choice measures alone cannot be expected to sustain the long-term growth and development of the market if the fundamentals are not in place. There can be no doubt that the retail choice programs have gone a long way in helping marketers cost effectively enroll, aggregate and serve customers.

However, to attain the next level of retail market development the issue of market-based pricing, particularly for mass market consumers must be addressed. In general, NEM recommends that utility pricing of commodity to large commercial and industrial customers who can be billed hourly should be based on an hourly, time of day rate. With respect to small commercial and residential customers, utility default service pricing should be a monthly-adjusted, market-based commodity rate to which should be added a utility's fully allocated embedded costs associated with providing all of the otherwise competitive commodity related products, services, information and technologies currently bundled in full service rates. There are also interim steps that should be taken to improve the market-based pricing signals provided to consumers. These include:

direct access" (emphasis added) and defines "direct access" in Section 2803 as, "the **right** of electric generation suppliers and end-use customers to utilize and interconnect with the electric transmission and distribution system on a non-discriminatory basis at rates, terms and conditions of service comparable" to the utilities own use in the transport of electricity. (emphasis added). Likewise, the Competition Act mandates that, "all customers of electric distribution companies in this Commonwealth **shall** have the opportunity to purchase electricity from their choice of electric generation suppliers. The ultimate choice of the electric generation supplier is to rest with the customer." (emphasis added). § 2806(a). Indeed, by requiring that consumers SHALL have choice and suppliers SHALL have non-discriminatory access to the system, the legislature makes clear that the Commission is to adopt measures that lay the foundation for robust, on-going market activity.

- Phasing out heating versus non-heating rates;
- Phasing out blocked rates; and
- Shortening the default service auction cycles such that the length of products procured are shorter in duration and bear a better correlation to current market conditions.

Overall, the efficiency of the retail market could be improved if commodity pricing signals followed the market more closely rather than the pricing peaks and valleys that do not reflect current market conditions and are the result of the utilities' default service procurements.

Additionally, the utilities' default commodity service rate must reflect the full costs of providing this 24/7 no-notice, last resort service to consumers. Rate unbundling permits consumers to see and understand the full extent of the costs associated with utility commodity default service and permit consumers to make accurate, informed comparisons with competitive offerings. Also, consumers that migrate will not be penalized by a double payment of commodity-related costs, once to their competitive supplier that is currently providing the service, and once to the utility that is no longer providing the service but is collecting the cost through bundled distribution rates.

At the most fundamental level, the current default service procurement approach that retains the utility in the commodity merchant function role, should only be viewed as a transitional step in retail market development. The ultimate end goal, which is recognized by Pennsylvania law⁷ and is a model employed in other retail choice jurisdictions, is for the utility to exit from the commodity merchant role and for competitive suppliers to act as default service providers.

3. What are the economic and managerial costs associated with electric distribution companies (EDCs) fulfilling the default service role? Are the EDCs accurately passing those costs along to default service customers? Do default service rates include any elements that are not cost-based? Is an examination of distribution rates needed to ensure proper cost allocation? Are there barriers to competition as a result of having EDCs provide default service?

The Commission identified default service cost elements in Section 69.1808⁸ of its regulations. NEM agrees that these elements are representative of the costs incurred in rendering default

⁷ See NEM Response to Question 9 infra.

⁸ **§ 69.1808. Default service cost elements.**

(a) The PTC should be designed to recover all generation, transmission and other related costs of default service. These cost elements include:

(1) Wholesale energy, capacity, ancillary, applicable RTO or ISO administrative and transmission costs.

(2) Congestion costs will ultimately be recovered from ratepayers. Congestion costs should be reflected in the fixed price bids submitted by wholesale energy suppliers.

(3) Supply management costs, including supply bidding, contracting, hedging, risk management costs, any scheduling and forecasting services provided exclusively for default service by the EDC, and applicable administrative and general expenses related to these activities.

(4) Administrative costs, including billing, collection, education, regulatory, litigation, tariff filings, working capital, information system and associated administrative and general expenses related to default service.

(5) Applicable taxes, excluding Sales Tax.

service. However, NEM recommends, in order to ensure that proper utility delivery service rate unbundling pursuant to this has occurred, that an examination of delivery rates be undertaken with the goal of separating out the full retail costs to the utility of providing 24/7 no-notice, last resort default service. The failure to fully and properly unbundle means that consumers are paying hidden cross-subsidies in their delivery rates of what should properly be accounted for as commodity rates. In addition, if no-notice default service costs are not fully unbundled from delivery service rates, then the utility is still permitted to profit from rendering default commodity service rather than it being a direct pass through of those costs. It is critical to ensure that no-notice last resort commodity service is accurately priced and consumers have real apples-to-apples price comparisons in the marketplace until the utilities exit from the merchant function.

4. Are there unintended consequences associated with EDCs providing default service, and related products, such as time-of-use rates?

Retaining the utility as the default provider of energy supply services long term in a restructured environment will have a negative impact on the development of competitive markets. The structure and pricing of default service are critically important issues in determining whether consumers will receive the benefits of meaningful price competition. Retaining incumbent utilities in the default service role for all consumers and setting a price for default service that does not bear a close correlation to market-based pricing and that fails to fully capture the cost of providing no-notice last resort service, creates a significant barrier to competitive suppliers and perpetuates the same non-competitive energy services that restructuring is designed to replace.

Commodity supply and related services, information and technologies are inherently competitive functions. Allowing the utility to remain in the default service role, and provide other competitive products such as time of use rates etc., can discourage competitive entities from doing so. Competitive entities lack the instant scope and scale that captive customers offer the utilities and therefore different cost considerations underly said entities offerings versus those of the utility. Additionally, retaining a regulated monopoly in a competitive marketplace inherently distorts the competitive playing field and requires a significant amount of regulatory intervention and oversight to try to ensure a level competitive playing field.

5. Should default service continue in its current form? Does default service impede competition or otherwise prevent customers from choosing electricity products and services tailored to their individual needs? Does default service provide an advantage to the incumbent EDC and/or its generation affiliate(s)?

Default service in its current form should be considered as a transitional step to the utilities exit from the merchant function. The retail choice programs instituted by the Commission provided a low cost means to enable retail market development. The next step in market evolution should

(6) Costs for alternative energy portfolio standard compliance.

(b) EDC rates should be scrutinized for any generation related costs that remain embedded in distribution rates. This review should occur no later than the next distribution rate case for each EDC filed after September 15, 2007. The Commission may initiate a cost allocation case for an EDC on its own motion if such a case is not initiated by December 31, 2007. Changes to rates resulting from the examination would take effect after the expiration of Commission-approved rate caps.

be the provision of increased market-based pricing signals and the correct cost allocation associated with no-notice default commodity service. The final step should be the provision of default service by the competitive marketplace.

So long as the utility is in the default service role there will be a group of consumers that will fail to shop, even when it is in their best economic interest to do so. Consumer apathy to shopping, apathy to educating themselves about energy choice, and apathy to choosing a competitive supplier are all by-products of this market structure. Moreover, because the utilities current default service procurement for mass market customers is a blended rate of short- to long-term products and costs that are associated with no-notice last resort service are not added to these prices, the default service rate it yields is inherently a misrepresentation of current market conditions. This distorts consumers perceived value of market-based competitive offerings in the marketplace and will cause consumers to make faulty decisions based on inaccurate utility price to compare information. When competitive suppliers can truly compete on the basis of price, this will yield the lowest price for consumers. The blunt instrument of utility default service procurement is not necessary to, nor an appropriate means, of achieving it.

Default service does provide an advantage to the utility. For instance, because the utility has a dual function in the marketplace as a competitive provider of energy but also as the entity with whom the supplier must interact and interface in order to effectuate changes in customer service, sharing of billing and other customer information, and administering POR programs amongst other things, the utility wields a significant amount of control over the market vis a vis its competitors. In addition, in a market that has opened to competition, the assumption that consumers who have not selected a competitive supplier have made an affirmative decision to receive service from the utility is unwarranted and an unfair advantage to the utility.

6. Can/should the default service role be fulfilled by an entity, or group of entities, other than the EDC? If the default service role should be filled by an entity other than an EDC, what mechanisms could be employed to transition the default service role away from the EDC and onto competitive electric generation suppliers (EGSs)? Are different approaches appropriate for different customer classes? What criteria should be used to ensure that EGSs are qualified to assume the default service role and maintain reliable service?

Yes, the default service role can be fulfilled by an entity or entities other than the utility. Indeed, the commodity merchant function is a naturally competitive function. It is not necessary for the utility to act as the default service provider because marketers have the ability and experience to supply these services to customers. Marketers have long been involved in developing and aggregating electric generation supply, and providing utilities with energy as a commodity. Indeed, in many cases marketers have supplied utilities with energy and related services on an outsourced basis for years, enabling those utilities to provide energy supply services. A utility supplying delivery is not inherently more reliable than a contractual obligation to serve by a qualified supplier, unless there are anti-competitive remnants that remain in law or practice. In addition, competitive suppliers have risk management assets that historically have not been part of a utility's business model since the Commission normally has acted as the utility's risk manager. As part of the transition to competitive entities acting as default service provider, the Commission may want to examine the validity of separating the performance of this backstop

role by the need being met, i.e, low income consumers, credit challenged consumers, consumers that do not currently have a competitive supplier.

There are different costs and risks associated with providing default service to different customer classes. C&I customers already have more experience shopping for energy and more sophistication in making such decisions. This may indicate that a more abbreviated timeline for a transition for these customers to a competitive default service provider would be appropriate. Likewise, residential and C&I consumers will have different educational needs attendant with a transition. Proactive education of mass market consumers about a pending change in default service provider will be critical. The proactive educational approach taken by the Commission in anticipation of the expiration of electric rate caps and expanded availability of energy choice options was very successful and should be capitalized upon as the market continues to evolve. The current licensing and financial responsibility requirements that a competitive supplier must satisfy to serve customers in the state should be sufficient to demonstrate their ability to assume the default service role and maintain “reliable”⁹ service.

In phase one of this proceeding, the Commission may want to review the different approaches taken in other jurisdictions to transitioning the utility from the default service role. Below are illustrative examples of these approaches.

A. Declaration of Competitive Service

A transitional mechanism in place in the electric market in Illinois involves the declaration of a utility’s tariffed service to become a competitive service.¹⁰ A service can be declared competitive by the Illinois Commerce Commission upon a showing that 33% of eligible customers have migrated from the tariffed service to a competitive supplier and that at least three competitive suppliers provide a comparable service in the utility’s service territory.¹¹ The Illinois statute explicitly declared that the provision of electric power and energy to retail customers in the service territories of ComEd and Ameren for customers with peak demands of 400 kilowatts and above is a competitive service.¹² Upon the declaration of service as competitive, service to those customers by the utility will only be rendered on an hourly-pricing basis. The Illinois Commerce Commission also granted ComEd’s petition to declare the provision of power and energy to customers with peak demands of 100 kilowatts and above but less than 400 kilowatts as a competitive service.¹³

B. Auction of Supply Obligation

In Ohio, beginning in the service territory of Dominion East Ohio¹⁴ and then subsequently followed by the additional natural gas utilities in the state, the utilities utilized a transitional,

⁹ The utilities role should be converted to an obligation to connect and maintain a reliable delivery infrastructure.

¹⁰ Illinois Public Utilities Act, Section 16-113.

¹¹ Illinois Public Utilities Act, Section 16-113(a).

¹² Illinois Public Utilities Act, Section 16-113(f).

¹³ Illinois Commerce Commission Docket Nos. 08-0619, 08-0620, and 08-0621.

¹⁴ See, e.g., Public Utilities Commission of Ohio, Case No. 05-474-GA-ATA, In the Matter of the Application of The East Ohio Gas Company, dba Dominion East Ohio, for Approval of a Plan to Restructure Its Commodity

phased process to exit the gas merchant function. This began with the recognition that the Gas Cost Recovery Mechanism that had been in place was hampering retail market development. In its place, the utilities first used a descending clock auction, called a Standard Service Offer (SSO) Auction, through which suppliers bid to provide wholesale supply volumes. Through the auction a Retail Price Adjustment is derived to which is added the monthly NYMEX settlement price to arrive at the SSO rate for customers. Subsequently, in Phase 2 of the exit from the commodity merchant function, a Standard Choice Offer (SCO) Auction was utilized through which suppliers bid to provide commodity to choice eligible customers. In other words, suppliers establish a direct retail relationship with the consumer as a result of the SCO auction.

C. Establish Date Certain for Utility Exit of Merchant Function

Atlanta Gas Light exited the merchant function in 1999. Georgia's Natural Gas Competition and Deregulation Act of 1997¹⁵ permitted gas utilities to elect to exit the merchant function upon a showing that sufficient competition existed in their service territory. Once the determination was made that market conditions were sufficiently competitive, customers that had not chosen a marketer were randomly assigned to one based on the marketer's market share at the time. The Georgia PSC instituted an interim pooler to serve customers in the event their marketer can no longer provide service.¹⁶ Legislation in 2002 provided for the creation of a "regulated provider" to serve low income and high-risk customers unable to receive service from a marketer.¹⁷ Marketers serving customers in this service territory perform their own billing and customer care.

D. Separation of Generation and Transmission

Texas law required that all electric customers have the option of choosing a competitive supplier by January 1, 2002.¹⁸ The electric utilities were required to unbundle their business activities into three entities: a wholesale power generation company, a retail electric provider (REP), and a transmission and distribution company.¹⁹ When competition began on January 1, 2002, standard offer service was transferred to the affiliated REP of the utility company, to provide service at the Price to Beat, which could be adjusted twice per year for fuel cost changes. Affiliated REPs were prohibited from offering competitive rates to residential and small commercial customers in the utility service territory, other than as the standard offer provider, until 40% of residential and small commercial customer load had chosen a competitive supplier. Provider of last resort service is rendered by competitive providers on a customer class-specific basis. Marketers serving customers in Texas perform their own billing and customer care.

Service Function; Case No. 07-1224-GA-EXM, In the Matter of the Application of The East Ohio Gas Company d/b/a Dominion East Ohio for Approval of a General Exemption of Certain Natural Gas Commodity Sales Services or Ancillary Services.

¹⁵ O.C.G.A. § 46-4-150 et. seq.

¹⁶ Georgia Public Service Commission Docket No. 8390-U, Order Designating Interim Pooler, November 4, 1999.

¹⁷ Natural Gas Consumers Relief Act of 2002. See O.C.G.A. § 46-4-166.

¹⁸ Texas Utility Code Ann. Section 39.102.

¹⁹ Texas Utility Code Ann. Section 39.051.

7. How can Pennsylvania's electric default service model be improved to remove barriers to achieve a properly functioning and robust competitive retail electricity market? Are there additional market design changes that should be implemented to eliminate the status quo bias benefit for default service?

This question appears to imply the circumstance in which the utility is retained as the default service provider. As discussed in NEM's previous responses, we recommend that default service should ultimately be provided by competitive suppliers. However, in the interim until this is achieved, improvements could be made to the current model. As NEM explained in response to Question 2, utility default service should include more timely, market based pricing signals to consumers to provide an environment for sustained competitive activity and more accurate basis upon which consumers can evaluate competitive energy offerings. This should be accompanied by utility default service pricing that fully captures the cost of providing no-notice last resort service.

NEM also suggests that default service could be improved if there was no longer a presumption that new service customers begin on utility service and then have the opportunity to switch to a competitive provider. Consumers should have a choice of supplier from the start of service.

8. What modifications are needed to the existing default service model to remove any inherent procurement (or other cost) advantages for the utility?

The utility remains the dominant actor in the marketplace. Notwithstanding migration rates achieved to date, the utility still has the majority of the market share in the retail electric market. Attendant with that dominant position, the utility benefits from economies of scale in power procurement for a larger consumer base, which it serves at a lower risk than competitive providers (both because of the relative certainty of the size of the customer base it will serve and the regulatory cost recovery mechanisms that permit the utility to serve consumers at low or no risk). Because of its market share, the utility has a buying advantage and volume advantage when it is procuring power. These procurement advantages may be diminished to a degree as consumers continue to migrate to competitive suppliers but they cannot be fully compensated for so long as the utility remains in the default service provider role. As explained in response to Question 2, proper market-based pricing and cost allocation of all commodity-related activities to default service rates is also necessary to avoid a significant procurement and cost advantage to the utility.

9. What changes, to Regulations or otherwise, can the Commission implement on its own under the existing default service paradigm to improve the current state of competition in Pennsylvania?

NEM strongly supports what the Commission has done by regulation thus far to adopt retail choice programs that have reduced barriers to retail energy competition. NEM's recommendation to utilize a transitional process by which competitive suppliers will ultimately be the providers of default service is consistent with current state law and industry development. The Commission has the express authority pursuant to the Electricity Generation Customer Choice and Competition Act to approve one or more competitive supplier(s) as the default

service provider(s). The law clearly contemplates and authorizes entities other than the utility to serve as default service provider. This is clear beginning with the definition of “default service provider” in Section 2803 which explicitly includes “alternative supplier[s].” This is further supported by statutory language in Sections 2802(14) and 2806 declaring that “[t]he generation of electricity will no longer be regulated as a public utility function.” And, Section 2807(e) discusses a “default service provider’s obligation to provide electric generation supply service” which is not limited to the utility functioning in that role. This language is coupled with the affirmative statutory requirement that consumers in Pennsylvania be provided with meaningful energy choice options on a sustained, continued basis.²⁰

To support the transition to the competitive provision of default service, NEM recommends that the Commission establish by regulation a timeline and benchmarks of required goals. This will give all stakeholders, especially consumers, a clear idea of the market end-state and how and when it will be achieved. The Commission may wish to consider benchmarks in terms of customer migration, load migration, number of suppliers, number of competitive offerings as well as the amount of time that has elapsed since rate cap expiration after which transitional migration strategies must be implemented. Different timelines may be appropriate for different customer classes and/or different service territories.

10. What legislative changes, including changes to the current default service model, should be made that would better support a fully workable and competitive retail market?

There are a number of legislative changes that could be made to clarify the current law that would better support a fully workable and competitive retail market.

A. 66 Pa. C.S. Section 2807(e)(3.4)(ii)

The Act 129 “least cost” standard for electric utilities’ generation purchases set forth in Section 2807(e)(3.4)(ii) has injected uncertainty into the statutory framework. NEM suggests that the “least cost to customers over time” standard should be consistent with the competitive electric market principles adopted for the Commonwealth in the Electricity Generation Customer Choice and Competition Act. In a true “least cost” regime the market-based rate will yield the lowest cost over time to consumers with the appropriate time frame for evaluating whether a utility’s procurement plan will yield the “least cost” to consumers correspondingly keyed to current market conditions. Any deferred costs in rates may carry with it a cost plus return on investment plus interest to the consumers. Consumers can be significantly harmed by utility long-term pricing that bears little resemblance to market conditions. Either the utility will have unnecessarily locked in an above market rate, resulting in higher prices for ratepayers over a prolonged period, or the utility will lock in a below market rate that distorts the value of competitive market offerings. Long term contracts are akin to prolonged rate freezes. When utilities are permitted to lock in rates that are below market, consumers may experience rate shock when those contracts expire and rates need to be adjusted upward, possibly dramatically. NEM urges against adopting a “least cost” procurement standard that puts consumers in the position of either paying above market rates for energy, or alternatively, facing rate shock. Additionally, consumer price comparisons of supplier offerings are undermined when there is a

²⁰ See supra note 3.

lack of market-based utility rates and a failure to fully allocate commodity service related costs to default service rates. Both situations occur to the detriment of consumers. Moreover, just as a market-based default rate should represent a “least cost” offer, by supporting robust competition amongst EGSs that participate in the marketplace, it should also encourage “least cost” offers from these providers. In other words, utility market-based pricing plus the proper allocation of costs related to providing such services will encourage suppliers to enter the market to serve Pennsylvania consumers. In so doing, this will exert downward price pressure on competitive market offerings.

B. 66 Pa. C.S. Section 2807(e)(3.2)

Section 2807(e)(3.2) requires default service procurements to include a “prudent mix” of spot market purchases, short term contracts and long term contracts spanning from four up to twenty years in duration. Consistent with our comments herein, NEM suggests that the price derived under the laddered, portfolio approach does not bear enough resemblance to actual market conditions and ultimately has a stifling effect on competition. NEM submits that no cost, no risk utility hedging places all other market participants at a competitive disadvantage. Month-ahead hedging until the utility exits commodity functions minimizes the anti-competitive impact of the status quo.

C. 66 Pa. C.S. Section 2807(e)(7)

Section 2807(e)(7) requires that the default service rate for residential and small business customers, “shall change no more frequently than on a quarterly basis.” For the reasons set forth in NEM’s response to Question 2, we recommend that default service pricing for these consumers should be a monthly-adjusted, market-based commodity rate that reflects the actual costs of providing no-notice last resort service.

11. Are there, or could there be, potential barriers being created by the implementation of the EDC Smart Meter plans?

As the utilities implement their Smart Meter plans, it is critical that access to the smart grid infrastructure be provided in a manner that avoids the creation of new information and/or demand or demand response-related monopolies. We urge the Commission to ensure that all authorized market participants have secure, reliable, non-discriminatory (non-proprietary), open access to the information that will be created to facilitate the “smart grid.” This will entail the use of “open standards” to implement new generations of smart meters and smart IT infrastructures needed to “interoperably” handle a virtual tsunami of near real-time usage and pricing data. Open standards and non-discriminatory (non-proprietary) access to smart grid infrastructure will serve to incent a new critically-needed generation of services, application developers and information technologies, to securely, reliably and interoperably collect (meters), process (analyze), store and provide secure access to the substantial increase of data needed to develop new demand response-related products, services, information technologies and price offerings. Commission approval of Smart Meter plans and cost recovery should be premised upon the utility’s provision of open, non-discriminatory access to the smart grid infrastructure to competitive energy marketers and other third parties authorized by consumers to receive and

manage their energy usage information. Real-time data should be provided by the utility to market participants on a real-time basis.

Conclusion

The results of the Commission's investigation into default service will be critical to the on-going success of the retail energy marketplace. NEM looks forward to participating in both phases of this proceeding to develop a default service provider transition plan that permits consumers to realize the full benefits of a competitive market.

Sincerely,

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