COMMONWEALTH OF PENNSYLVANIA

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May 16, 2012

Rosemary Chiavetta
Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street
Harrisburg, PA 17120

RE: 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-2011-2273650; P-2011-2273668, P-2011-2273669, P-2011-2273670

Dear Secretary Chiavetta:

Enclosed please find the Office of Consumer Advocate's Reply Brief, in the above referenced proceeding.

Copies have been served as indicated on the enclosed Certificate of Service.

Respectfully Submitted,

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Enclosures
cc: Hon. Elizabeth H. Barnes
Certificate of Service
151293

BEFORE THE

PENNSYLVANIA PUBLIC UTILITY COMMISSION

Joint Petition of Metropolitan Edison	:		
Company, Pennsylvania Electric Company,	:	Docket Nos.	P-2011-2273650
Pennsylvania Power Company and West	:		P-2011-2273668
Penn Power Company For Approval of	:		P-2011-2273669
Their Default Service Programs	:		P-2011-2273670

REPLY BRIEF OF THE OFFICE OF CONSUMER ADVOCATE

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I. INTRODUCTION

On May 2, 2012, the Office of Consumer Advocate (OCA) filed its Main Brief in this proceeding. Main Briefs were also filed by the FirstEnergy Companies (Met-Ed/Penelec/PennPower/West Penn, or the Companies), the Bureau of Investigation and Enforcement (BI&E), the Office of Small Business Advocate (OSBA), the Retail Energy Supply Association (RESA), FirstEnergy Solutions (FES), Dominion Retail, Inc. (Dominion), CAUSE-PA, Constellation Energy (Constellation), Exelon Generation and Exelon Energy (Exelon), and the Industrial coalitions (MEIUG/PPUC/PICA/WPPII). The OCA submits that nothing argued in the Main Briefs of the parties changes the positions detailed in the OCA Main Brief.

In its Main Brief, the OCA supported the use of a prudent mix of energy products designed to achieve default service rates at the least cost over time as required by Act 129 of 2008. See, OCA M.B. at 9-33. The residential supply mix proposed by the OCA is the same mix currently in use for Met-Ed, Penelec, and Penn Power. Under the OCA proposal, the Companies would meet 75% of their residential default service load through Full Requirements Contracts (FRCs), and 25% through a mix of one year block energy purchases, a four year "around the clock" block energy purchase, and spot market transactions. The OCA submits that the Companies' proposal to move to 100% reliance on two year FRCs, all starting June 1, 2013 and ending May 31, 2015, is inconsistent with the policy established by the General Assembly through Act 129. The Companies' Plans rely on a single product, for a single term, purchased over a two month period in what will likely be under singular market conditions. The parties opposed to the OCA's proposed residential procurement argue that it would result in risks to customers and rate volatility – but the success of the Companies' existing default supply plans shows that is not the case. As a result, the OCA submits that including a diverse mix of products

in the residential supply mix as recommended by the OCA is the prudent and reasonable approach that should be adopted in this proceeding.

The OCA further argued in its Main Brief that the Companies' proposed Market Adjustment Charge (MAC) must be soundly rejected. See, OCA M.B. at 36-50. The MAC represents an unprecedented profit adder for the Companies – despite the fact that they are recovering all of their reasonable costs of default service on a dollar for dollar basis pursuant to a Commission-approved reconcilable rate mechanism. The parties supporting the MAC have advanced a wide range of goals, rationales, and principles to support implementation of this one half cent per KWh adder. The OCA submits, however, that all of these arguments must fail. The MAC does not reflect any cost, nor is there any reasonable relationship between the MAC and any valid efforts to enhance retail competition. The MAC is simply an unjustified addition to the Price to Compare (PTC) that will increase the price of electricity to both switching and non-switching customers. The MAC must be totally rejected as contrary to law and contrary to sound public policy.

The OCA also addressed in great detail the issues related to the market enhancement proposals and Time of Use rates included in the Companies' proposed Plans. See, OCA M.B. at 51-96. The OCA submits that the modifications to these programs contained in its Main Brief will help ensure their success, while at the same time ensuring that important consumer protections are in place. Additionally, the OCA's modifications help ensure that a successful default service procurement can go forward. The parties opposed to the OCA's modifications at times point to the Commission's recent Intermediate Work Plan Order. The Commission, however, has clearly recognized the need to develop its decision in this proceeding on record evidence related to the Companies. The OCA submits that its positions are fully reflective of

substantial evidence adduced in this proceeding that reflects the needs of the Companies' customers and should be adopted.

For the reasons detailed in the OCA's Main Brief, and those detailed below in this Reply Brief, the OCA submits that the Companies should be directed to amend their Plans as recommended by the OCA. The OCA further submits that its Main Brief provides a comprehensive statement of its positions, and the OCA will not repeat all of those arguments here. To the extent an argument is not addressed in this Reply Brief, the OCA relies on those positions already advanced in the OCA Main Brief. In this Reply Brief, the OCA will respond to specific arguments advanced by other parties, referring to relevant sections of its Main Brief as appropriate.

II. DEFAULT SERVICE PROCUREMENT AND IMPLEMENTATION PLANS

A. Procurement Groups.

1. West Penn's Proposed Consolidation of Service Types 20 and 30.

The OCA takes no position on this issue.

B. Residential and Commercial Class Default Service Procurement.

1. Summary of OCA Position.

The OCA provided a full summary of its position in its Main Brief (at 9-21).

2. Term of Contracts.

a. OCA Response to the Companies.

The OCA has recommended a default service procurement plan that includes a mix of one year and two year Full Requirements Contracts (FRCs), and one year block energy contracts, four year block energy contracts, and spot market purchases. Under the OCA proposal, FRCs would comprise 75% of residential supply, with the remaining 25% of residential supply being

met through block energy contracts and spot market purchases. In contrast, the Companies have proposed to procure all two year full requirements contracts. These contracts would all start on June 1, 2013 and come to a hard stop on May 31, 2015.

In their Main Brief in the "term of contract" section, the Companies address the risk of higher supplier risk premiums as a result of their proposed reliance on two year FRCs. FE M.B. at 9-10. In response to the OCA's concerns, the Companies first argue that the OCA is concerned that two year FRCs will bring added risk over one year contracts and that such concern is unwarranted. FE M.B. at 9. Second, the Companies argue that the OCA's concerns regarding the impact of the Opt-in Retail Auction on the risk premiums inherent in FRCs is overstated. FE M.B. at 10. As a result the Companies argue that the two year terms are reasonable and should be approved. FE M.B. at 9.

As an initial matter, the OCA submits that Mr. Kahal did not testify specifically about the concerns that bidders would incorporate higher risk "premiums" in a two year FRC as compared to a one year FRC. The risks that Mr. Kahal testified about being incorporated into winning FRC bids are the general risks that any full requirements provider incurs, *i.e.*, the "volumetric risk" that expected load will be higher or lower than can be reasonably anticipated. See, OCA St. 1 at 14-15. It is important to note that Mr. Kahal recommended the continued use of both one and two year FRCs as a major part of a prudent mix. OCA St. 1 at 24-26. While there is volumetric risk in those products, it is reasonable to continue to incur those potential costs for the stability benefits associated with those products and to ensure that a prudent mix of contracts is included in the Companies' residential procurement.

With regard to the Companies' second argument, the OCA is very concerned that risk premiums may be particularly high if the Companies' proposed residential supply plan is

approved. To address this issue, OCA witness Kahal developed a "hold back" procurement methodology that limits these risks. These risks are fully explained in Section II.B.6, below.

In response to the Companies' argument in this section, the potential for volumetric risk is particularly acute under the Companies' proposal because full requirements suppliers would be exposed to an open-ended risk created by the proposed Opt-In Retail Auction. Id. As Mr. Kahal concluded, it is reasonable to assume that wholesale suppliers would price their subjective evaluations or assessments of volumetric risk into their bids. Id.[1]

The Companies also argue that OCA witness Kahal does not explain why FRC suppliers, with full knowledge of the Opt-In Retail Auction details, would not be able to consider the risks of that program. FE M.B. at 10. The OCA submits, however, that the Companies have not addressed the correct issue. The question is not whether FRC suppliers can consider the risk, but rather, whether the costs of an adder to cover themselves for the risk would be unreasonable to consumers. As explained in the OCA's Main Brief (at 10-14), Act 129 requires that there be a prudent mix of supplies designed to achieve the least cost to customers over time. Mr. Kahal's proposal is designed to ensure that the Act's requirements are met.

b. OCA Response to RESA.

Instead of two year contracts as proposed by the Companies, RESA argues that rates must be made more "market responsive" to support competition. RESA M.B. at 12. RESA proposes that the Companies amend their Plans to include two year FRCs and one year FRCs. RESA M.B. at 18. OCA witness Kahal testified that RESA's proposed modifications were

[1] In its Main Brief, Constellation agreed with OCA witness Kahal's assessment of the open-ended risks that are present in the Companies' proposed full requirement contracts. Constellation M.B. at 28. Constellation is a major provider of full requirements power in PJM.

partially consistent with his proposed continuation of the existing Met-Ed/Penelec/PennPower supply plans:

> Witness Williams proposes replacing the 100 percent reliance on two-year contracts with a mix of one- and two-year contracts. This is at least partially consistent with my own portfolio proposal which includes also a mix of one- and two-year contracts (including 25 percent block and spot which is entirely one year). The one difference is that in the second year of the program, my portfolio would procure some two-year contracts to provide some contract laddering and mitigate the "hard stop" problem. Witness Williams appears to recommend that no contract extend past May 2015.

OCA St. 1-R at 12. The OCA submits that under RESA's proposal there would be no price protection for service beginning on June 1, 2015. While both RESA witness Williams and OCA witness Kahal proposed a mix of products, OCA witness Kahal's proposal includes contract laddering that will allow for a smooth transition beyond the end of the current two-year plan. As Mr. Kahal testified, eliminating the "hard stop" problem is important because there is exposure to significant risk of sharp price increases if market conditions change adversely. OCA St. 1 at 18-19.

With regard to RESA's argument that prices should be "market responsive," the OCA notes that the Commission has rejected the argument that the "least cost" standard envisioned in Act 129 should solely reflect fluctuating market prices. The Commission recently stated as follows:

> We disagree with RESA's overall recommendations as to the proper interpretation of the "least cost" standard as mandating that default service rates approximate, on a prospective basis, the market price of energy. Such an interpretation would signal retention of the "prevailing market price" standard that has been expressly replaced under Act 129. Moreover, this interpretation conflicts with the Act 129 objective of achieving price stability which dictates consideration of a range of energy products, not just those that necessarily reflect the market price of electricity at a given point in time. Price stability benefits are very important to some customer groups in that exposing them to significant price volatility through general reliance on short term pricing would be inconsistent with Act 129 objectives.

Implementation of Act 129 of October 15, 2008: Default Service and Retail Electric Markets, Docket No. L-2009-2095604 (Final Rulemaking Order entered October 4, 2011) (Slip op. at 39-40)(Final Rulemaking Order). RESA's proposal to create a "market responsive" default service plan, without considering rate stability, should be rejected.

RESA's primary argument against the OCA's proposed residential contract terms is that it will incorporate a four year contract for Met-Ed, Penelec and West Penn. RESA argues that incorporating a four year contract will hinder competition because it will "decouple" market prices from default service rates. RESA M.B. at 16. RESA further argues that the "prudent mix" requirements of Act 129 should be understood to require a mix that is likely to result in a competitive retail market. Id. RESA argues that including a four year contract in the residential supply mix would result in the "shattering" of the shopping that has occurred in the Companies' service territories. Id.

As the OCA argued in its Main Brief, the inclusion of a four year block contract is consistent with Act 129's mandate to provide stable and reasonable default service through a prudent mix of contracts. The OCA further notes that customer switching has expanded dramatically for Met-Ed and Penelec since their residential supply portfolios (with four year blocks) became effective on June 1, 2011. See, OCA St. 1 at 29.

The OCA submits that RESA's interpretation of Act 129 advanced in its Main Brief is flawed. The Commission has explicitly recognized the goals of Act 129 that must be met in establishing a procurement plan, as follows:

> We agree with the majority of parties that the "prudent mix" of contracts be interpreted in a flexible fashion which allows the DSPs to design their own combination of products that meets the various obligations **to achieve "least cost to customers over time," ensure price stability, and maintain adequate and reliable service**.

Final Rulemaking Order at 60 (emphasis added). The Commission has recognized that flexibility should be permitted to provide each default service provider the ability to achieve price stability, reliability and adequacy as it develops its "prudent mix" of supplies. RESA fails to adequately address the need for price stability when considering the Companies' Plans.

Here, RESA's objection to the inclusion of a longer term contract is that it will result, essentially, in default service rates that do not reflect prevailing market prices.[2] RESA M.B. at 16. This standard, however, was repealed by the General Assembly and the Commission has recognized the need for rate stability under Act 129. The OCA submits that RESA's opposition to the four year block of energy is without merit and should be rejected.

c. OCA Response to FES.

FES argues in favor of the Companies' reliance on two year full requirements contracts. FES M.B. at 5. FES argues that residential default service contracts shorter than 24 months will not provide the rate stability envisioned by Act 129 (FES M.B. at 9-12), and that the OCA procurement proposal will not enable the Companies' to minimize the procurement of default service after May 31, 2015 in a manner consistent with the Commission's December 16 Final Order. FES M.B. at 7; citing, Investigation of Pennsylvania's Retail Electricity Market: Recommendations Regarding Upcoming Default Service Plans, Docket No. I-2011-2237952 (Order entered December 16, 2011) (Slip op. at 19) (December 16 Final Order). FES argues that the OCA's proposed residential procurement plan will "contradict" the Commission directive that supplies not extend beyond May 31, 2015. FES M.B. at 7.

[2] For example, RESA argues that a procurement with two year and four year contracts "virtually guarantees that prices will be substantially out of line with current market conditions at the time of delivery" (RESA M.B. at 17), in other words, they would not be prevailing market prices.

The OCA agrees with FES that Act 129 requires price stability. As FES correctly points out, the Commission has recognized that Act 129 specifically repealed the "prevailing market price" standard for default service, and replaced it with the requirement that service be provided at the least cost to customers over time. FES M.B. at 11. The OCA strongly disagrees, however, with FES' conclusion that the Companies' reliance on a single product (simultaneous two year FRCs) meets Act 129's requirement that the Companies procure a prudent mix of contracts designed to achieve least cost over time.

While FES argues that price stability is an essential requirement for default service under Act 129 (FES M.B. at 9-12), FES argues that contracts that extend beyond the upcoming plans should not be included in the residential supply mix. FES M.B. at 7. The OCA submits, however, that the inclusion of a modest level of contract laddering, including four year contracts as currently procured by the Met-Ed, Penelec, and Penn Power, provides added price stability and should be part of the prudent mix of contracts that are called for by Act 129. The OCA submits that FES's argument in favor of the stability provided by two year contracts applies with even greater force to the inclusion of four year contracts. Given the need for rate stability, particularly for service continuing past May 31, 2015, the OCA submits that contract laddering and four year contracts should be included in the Companies' residential supply mix.

FES seems to argue that the price stability benefits of longer term contracts should be ruled out because the Commission has decided that contracts should be limited to two years. FES M.B. at 7, 14. The Commission has clearly stated, however, that the Act 129 requirements for default service, including the procurement of a prudent mix of contracts that achieve the least cost to customers over time must be met. December 16 Final Order at 19. As detailed below in Section II.B.4 of this Reply Brief, the Commission explicitly recognized that each DSP must

meet its statutory obligations to provide default service at least cost to customers over time. Id. at 19-20. The Commission stated that "laddering supply purchases at different times and having overlapping delivery periods may promote rate stability." Id. at 20. The Commission recognized that various contract lengths may be needed to achieve Act 129's mandates, and the OCA submits that the inclusion of a modest level of four year contracts is appropriate at this time. Id.

3. Procurement Dates.

The Companies have proposed to procure half of their residential default service FRCs for the 2013-2015 period in November 2012, and half in January 2013. FE M.B. at 7. As OCA witness Kahal explained, purchasing all of their power only two months apart raises concerns:

> [v]irtually 100 percent of supply for all four EDCs for the two years is acquired within an extremely short time window of about two months (i.e., November 2012–January 2013) largely eliminating the long-standing practice of Pennsylvania EDCs (and those in other states) of diversifying the timing of market purchases and staggering contracts.

OCA St. 1 at 17. The OCA submits that the purchasing of all of the Companies' supplies in such a truncated period creates the potential for significant harm. While market conditions have remained depressed in recent months, there is no certainty that the November 2012-January 2013 period will reflect similar conditions. The OCA supports a more diversified purchasing strategy to prevent the reliance on a singular market condition.

In their Main Brief, FES argues that the OCA's proposed procurement plan would require the Companies to conduct procurements during the delivery period. FES M.B. at 13. FES further argues that the OCA proposal would not allow for the price stability which is required under Act 129. Id. The OCA submits, however, that its proposed procurement schedule would allow for laddering of purchases in order to ensure price stability over time. FES completely

ignores the fact that purchasing all products for the upcoming plan period in November 2012 and January 2013 and having all contracts end on the same day, results in 100% exposure to market conditions at the end of the contract terms (*i.e.*, June 1, 2015). The OCA proposal to ladder purchases throughout the terms of the Plans is designed to ensure price protection against potential price spikes and provide stability over time.

4. Laddering of Contracts Beyond June 1, 2015.

In its Main Brief, the Companies argue that the planned termination of all contracts at the end of the two year Plans (*i.e.*, May 31, 2015) is consistent with their existing default service Plans. FE M.B. at 15. The Companies note that the existing Residential plans expire on May 31, 2013, and only the 48 month residential blocks continue past that date. Id. The Companies further argue that "there is no reason that a future default service plan could not include similar multiple procurements to avoid a future "hard stop" in June 2015." FE M.B. at 15. RESA, FES, and Dominion argue that the OCA's proposed procurement plan which ladders some contracts beyond June 1, 2015 would hinder development of an end state default service model beginning on June 1, 2015. RESA M.B. at 23; FES M.B. at 14; Dominion M.B. at 7. The OCA submits that the parties have not adequately addressed the need for rate stability and the requirement that service be provided at least cost "over time." The Companies' proposed Plans provide a relative degree of price stability in the near term, but fail to ensure longer term stability by limiting all purchases to the two year length of the Plans.

Initially, the OCA would note that the Companies do not have a "hard stop" under their existing plans. Met-Ed, Penelec, and Penn Power each have an "anchor" block of power that continues for two years past the expiration of the existing plan. These existing 48 month block products will act as a hedge extending into the 2013-2015 period and adding stability to

residential rates. To the extent that the existing default service plans can be improved through the use of additional laddering, the OCA submits that these principles should be incorporated in the upcoming Plans.

The Companies also argue that buying power nine months and three months before power is needed on June 1, 2015 would result in their avoiding a "hard stop." Id. The OCA submits that purchasing power over two procurements is a better design than purchasing all supply on one date. That said, however, such a procurement plan does not change the fact that the Companies would be required to replace 100% of their supplies for service beginning June 1, 2015. The OCA submits the supply plan should be laddered so that the Companies are never fully exposed to changing market conditions at a single point in time. The OCA submits that there is simply no justification to leave customers fully exposed to potential dramatic price spikes in the future. As OCA witness Kahal testified, the risk of rate shock from such exposure is real:

> The FE Companies' proposal has almost no market timing diversity. Under its plan almost 100 percent of residential wholesale default procurement takes place within a narrow three-month period, November 2012 – January 2013 for all supply to May 31, 2015. Both spot and forward market conditions today are extremely favorable due to today's weak load growth, capacity sufficiency and the natural gas surplus. I am therefore cautiously optimistic, though not certain, that the Companies' planned auctions will obtain favorable pricing results. But at the same time, it leaves default customers completely exposed for supply costs after June 1, 2015. If forward market conditions change adversely over the next two to three years, default customers could see abrupt price increases at that time.
>
> While this problem of the potential for sharp price increases cannot be entirely avoided, I believe that through the widely-accepted practice of contract laddering, it can be mitigated and smoothed. I propose doing so by procuring two-year FRCs in year 2 of the upcoming default program (i.e., procure in late 2013, early 2014). This would provide a fraction of the default supply for year two of the proposed default plan period and the first year of the next default plan period (i.e., June 1, 2014 – May 31, 2016). This would provide for some rate smoothing.

OCA St. 1-SR at 5. As explained above, the Companies should develop a more laddered approach that reduces the risk of an abrupt price spike at the end of the upcoming Plans.

The OCA also submits that a laddered approach will not harm retail competition. RESA, FES and Dominion oppose the OCA proposal because it would include contracts beyond June 1, 2015. RESA M.B. at 23; FES M.B. at 14; Dominion M.B. at 7. The obligation here, however, is to develop a procurement plan that meets the legal requirements of Act 129 – not to restrict the development of a compliant plan based on speculation of a new or different default service model. See, OCA M.B. at 10-14. Under the OCA's proposed residential procurement plan, the Companies would be required to enter into contracts over time, capturing market pricing and adding stability to default service to meet the requirements of Act 129. If the Commission or General Assembly requires modifications to the Companies' Plans in the future, those issues can be addressed prospectively at that time. Notably, the OCA submits that contracts can be assigned in the future if necessary. FE Companies Exh. RLS-1 at 63-64.

RESA, Dominion, and FES rely on the Commission's December 16 Final Order that provided "Recommendations Regarding Upcoming Default Service Plans." RESA M.B. at 23, 25; Dominion M.B. at 7; FES M.B. at 14. But the Commission explicitly recognized that its recommendations were not intended to impede a DSP from meeting its statutory obligations by prohibiting contract lengths extending beyond May 31, 2015. December 16 Final Order at 19-20. The Commission addressed the legal implications of its recommendations contained in the December 16 Final Order, as follows:

> Notably, these guidelines are not intended to inhibit EDCs from developing default service plans that include a prudent mix of contracts that achieve the "least cost to customers over time." The Commission reiterates that it will not mandate a prescriptive portfolio of contract lengths and **will allow EDCs to retain flexibility in developing plans that meet Act 129 requirements**.

December 16 Final Order at 19-20 (Emphasis added).

The Commission further explained that it was not prohibiting a laddered approach that avoided a "hard stop." The Commission stated as follows:

> [S]everal parties, including Exelon, Duquesne and OCA, raised the concern that if no short-term contracts extend beyond the end date of the default service plan, this will result in a "hard stop" that will require default service providers to purchase significant supply at the end of the plan under a singular market condition. These commenters recommend that the Commission permit EDCs to use a laddering approach, and suggest that laddering supply purchases at different times and having overlapping delivery periods may promote rate stability**. The Commission believes that these concerns may be legitimate and we recognize that some EDCs may have delivery periods that extend beyond the end date of the next plan under a laddered approach, hence the use of our language recommending that EDCs ". . . limit or eliminate. . ." overhanging short-term contracts**.

December 16 Final Order at 20-21 (Emphasis added).

The OCA submits that the Commission's guidelines must be considered in light of the requirements of Act 129. The Commission has recognized the General Assembly's intent to move away from a "prevailing market price" standard and to instead require each EDC to procure a prudent mix of products to achieve least cost over time. Of critical importance, the Commission recognized that Act 129's "least cost" standard must be considered in conjunction with the Act's requirements that prices be stable and that service be reliable. The Commission's recent Final Rulemaking Order states:

> Finally, it should be noted that the "least cost over time" standard should not be confused with the notion that default prices will always equal the lowest cost price for power at any particular point in time. In implementing default service standards, Act 129 requires that the Commission be concerned about rate stability as well as other considerations such as ensuring a "prudent mix" of supply and ensuring safe and reliable service. *See* 66 Pa. C.S. §§ 2807(e)(3.2), (3.4) and (7). In our view, a default service plan that meets the "least cost over time" standard in Act 129 should not have, as its singular focus, achieving the absolute lowest cost over the default service plan time frame but, rather, a cost for power that is both adequate and reliable and also economical relative to other options.

Final Rulemaking Order at 11-12. As the Commission Order makes clear, default service providers must consider price stability and reliability when developing a procurement plan that meets the "least cost over time" standard. The OCA submits that contract laddering is essential to achieve such price stability and reliability.

As detailed above, and in the OCA's Main Brief (at pp. 10-14), the default service legislative and regulatory framework requires the default service provider to develop a procurement plan that meets several goals. The default service provider must obtain a prudent mix of supplies designed to provide service at the least cost to customers over time. Default service must be reliable, adequate, and designed to reduce price instability. The Commission has recognized that "least cost to customers over time" requires that price stability and reliability must be considered when determining the prudent mix of supplies that the Commission approves. The OCA submits that laddering contracts throughout the term of the Companies' default service plans is prudent, and will provide rate stability benefits for customers.

5. The OCA's Proposal To Continue The Use Of Block Purchase Components With Spot Transactions For Residential Customers.

a. OCA Response to the Companies.

In their Main Brief, the Companies note that the OCA proposes that all four companies adopt the "block and spot" approach for the Residential Class which is currently in use by Met-Ed and Penelec. FE M.B. at 15. The Companies provide two primary criticisms of the OCA's support for the incorporation of block energy and spot market purchases. First, the Companies argue that the incorporation of block purchases introduces the risk that the Companies would have to sell back excess power at a potential loss. Id. at 16. Second, the Companies argue that the block and spot portion of their existing default service plans have been more costly than the full requirements portion, thus calling the benefits of block energy and spot market purchasing

into question. The OCA submits that both concerns are overstated, and do not outweigh the benefits of a diversified portfolio (rather than sole reliance on a single contract type, as the Companies now propose) as envisioned by the "prudent mix" standard established under Act 129.

With regard to their first critique, the Companies' argument that there is a risk of incurring a loss through the sale of excess power is overstated. Under the existing block and spot portfolio used by Met-Ed and Penelec, the Companies procure power based on their anticipated demands. Spot market purchases are designed to supply 20% of the non-FRC portion of supply, but the actual percentage varies based on actual load conditions. The Companies are able to balance their load through the wholesale market with relative ease. As OCA witness Kahal explained:

> The EDC acquires one-year block energy products, 12-month on-peak and off-peak strips. The amount purchased is based on the corporate forecast at the time of procurement for monthly residential default loads with the EDC targeting the purchase of 80 percent of on-peak and off-peak MWhs. The blocks of energy purchased will not match up with the customer hourly load profiles. Thus, the EDC will purchase balancing energy in hours when needed, and sell balancing energy in low load hours when the 80 percent block exceeds load. The EDC also purchases the required PJM capacity credits, ancillary service, and alternative energy credits. In essence, the EDC becomes the LSE for this 25 percent segment of default load, assembling all necessary generation products. This is a mostly (i.e., 80 percent of energy) but not entirely hedged product, and it is specifically tailored to the utility's updated default load forecast.
>
> * * *
>
> The type of block and spot supply used in the current Met-Ed and Penelec portfolio does not involve either active management, strategic planning or discretionary decision making. The EDC (or its contractor) is assigned certain defined tasks associated with supplying the block and spot product, but they are mechanical and administrative in nature. The blocks are procured using a standard RFP process, selecting the low bidder for a standard product. The balancing energy, ancillary services and capacity credits are purchased, as needed, from the PJM-administered markets. All costs are recovered as part of the PTC and reconciliation charge. The block procurements are linked to the corporate

> forecasts, but load forecasting is a normal utility activity that occurs anyway. In short, there is no actively managed portfolio issue in this case.

OCA St. 1 at 21-22. As Mr. Kahal explained, the sale of excess power through PJM procedures is a standard operation that is functioning as designed. The extent to which these transactions will occur will be based on the Companies' load forecasts. These load forecasts should reflect switching activity.

The Companies argue that Met-Ed and Penelec have been obligated to sell excess energy into PJM's real-time markets at a cost during operation of their existing default service plans. FE M.B. at 16; Tr. at 146-147. As explained above, the balancing of energy in PJM is a key component of the block and spot purchases. It is critical to note, however, that the extent to which these "balancing" transactions in the upcoming Plans would result in a cost or a credit in the upcoming Plans is dependent on future market conditions and the Companies' load forecasts.

Moreover, the "costs" of balancing of the block and spot portion of Met-Ed, Penelec, and Penn Power's existing plans are fully incorporated into the Companies' study of block and spot purchases. During the short period that block and spot has been used by these companies, market conditions have been depressed. OCA St. 1 at 19; OCA St. 1-SR at 5. Using Met-Ed as an example, even with depressed market conditions, the Companies' eight month comparison of residential block and spot (plus market costs) vs. Full Requirements shows block and spot at $68.18 per MWh, as compared to $68.92 for the 24 month FRC and $67.39 for the 12 month FRC. FE Exh. DWS-5. These results suggest that even in depressed market conditions, the "balancing" of block and spot supply has not produced unreasonable results.

The OCA further notes that the risk of selling energy back at a loss is further overstated because, under Mr. Kahal's proposal, the Companies would continue to meet 75% of their default service loads with power supplied through FRCs. Mr. Kahal explained that there is very

little volumetric risk with the block purchases that he has proposed to continue because they are simply too small of a percentage of load. OCA St. 1 at 23.

The Companies' second main criticism of block and spot purchasing is that the costs of the block and spot portion of their existing plans have "generally exceeded" the costs of their full requirements supply. FE M.B. at 16. The Companies rely on a study produced in the Rebuttal phase of this proceeding, sponsored by Companies' witness Stathis, to bolster their argument. The OCA submits, however, that the Companies' study does not compare similar contract terms and is not a reliable indicator of the benefits of either block and spot, or full requirements, procurements.

As OCA witness Kahal testified, the block and spot study covers only eight months of results (June 2011 through January 2012) and is therefore preliminary in nature. OCA St. 1-SR at 8. Prior to the Company's development of the study, Mr. Kahal recognized the difficulty in comparing the block and spot portion with the FRC portion of their portfolio, where he explained:

> [T]he companies are only about half way through the current default plan, and therefore any comparison would be incomplete and very tentative. I therefore recommend that the Joint Applicants perform and submit such a study at the conclusion of the current default service plan.

OCA St. 1 at 23.

Importantly, the OCA submits that the study is not "apples to apples" because it compares one and two year FRCs with a block and spot mix that includes four year contracts. See, Exh. DWS-5. The Study fails to acknowledge that the block and spot portion (which comprises 25% of the Residential default load) contains a four year, "around the clock" block of

power. As OCA witness Kahal further explained, the four year contract is more expensive than the one year blocks.[3] OCA St. 1-SR at 8.

The OCA recommends that the Companies continue to study the results of their residential supply plans. At this time, however, the inclusion of block and spot purchasing provides needed product diversity. As OCA witness Kahal testified:

> As compared with a 100 percent FRC portfolio, the inclusion of block and spot provides some needed product diversity and has the potential to lower overall supply costs, consistent with the goals of Act 129. While a systematic cost comparison analysis has yet to be done, by continuing to include a meaningful portion of supply from block and spot, the EDCs and this Commission can gain valuable experience. This is part of a legitimate search for best practices in the supply of default service.

OCA St. 1 at 24.

The OCA submits that the benefits of continuing with a diversified mix of one year and two year FRCs, one year and four year block energy contracts and spot market purchases better achieves the requirements of Act 129 than the Companies' approach of procuring only 24 month FRCs. As explained above, due to the size of the block product purchases, there is little risk that customers will have to bear significant "losses" from the sale of excess block energy into the PJM markets. In addition, the block and spot portion of the existing portfolios have performed well, particularly when the rate stability benefits of the 48 month blocks are considered. The Companies' concerns with regard to the continuing use of block and spot market purchases do not outweigh the benefits of the OCA proposed residential procurement supply plan.

b. OCA Response to RESA.

[3] The prices of the FRCs and block purchases, including the four year contracts, were included in the Companies' confidential response to OCA interrogatory II-6. See, OCA St. 1-SR at 8. OCA II-6 was introduced into the confidential record in this proceeding by RESA as RESA Cross Examination Exhibit 1. As explained by OCA witness Kahal, the information contained in OCA II-6 implies that the 48 month round the clock block is more expensive than the one year blocks. OCA St. 1-SR at 8. While the four year block prices may be more expensive than the shorter contracts, the four year blocks provide a hedge against longer term market adjustments and add stability in prices.

RESA argues that the OCA procurement proposal must be rejected for several reasons. First, RESA objects to a segment of the full requirements portion of the OCA's proposed residential procurement plan because it would replace one year contracts with two year contracts in the second year of the Plans. RESA M.B. at 24. RESA contends that moving to additional two year contracts could result in default service prices diverging from market prices. Id. As detailed above in Section II.B.2, the Commission has already rejected RESA's "market responsiveness" arguments. In addition, the use of two year contracts in the second year of the plan will result in a laddered portfolio designed to limit sudden price increases. OCA St. 1-SR at 5.

RESA's second argument is that the OCA's proposal would include energy contracts that would extend beyond May 31, 2015. RESA M.B. at 25. As explained above in Section II.B.4, however, the Commission has recognized that flexibility is needed when approving default service plans. RESA argues that the OCA has provided no "compelling basis" to include contracts that extend beyond 2015. The OCA submits that in light of the requirements of Act 129 to provide stable, reasonable default service at least cost over time, and the testimony of OCA witness Kahal as to the importance of contract laddering when developing a supply portfolio, it is appropriate to protect against potential price spikes through the widely-accepted practice of contract laddering. See, OCA St. 1 at 17-20; OCA St. 1-SR at 5.

RESA also argues that the block and spot (25%) portion of the OCA's proposed plan would impose additional costs on customers and would harm competition. RESA M.B. at 26. As addressed above and in the OCA's Main Brief, however, the block and spot study conducted by the Company in the Rebuttal phase of this proceeding does not support such a conclusion. See, OCA M.B. at 24-26. It is too preliminary to draw any significant conclusions based on the

eight months of data utilized by the Companies. Furthermore, shopping has increased substantially in the Met-Ed and Penelec service territories in the short time that block and spot purchases have been included in the residential supply mix. The OCA submits that RESA's position on this issue should be rejected.

c. OCA Response to Dominion.

Dominion claims that block and spot will add volatility to the default service rates. Dominion M.B. at 7. The OCA submits that Dominion's argument is overstated and that block and spot purchases are designed to reduce volatility over time. See, OCA M.B. at 27-28.

As OCA witness Kahal testified, the block and spot portion of his recommended residential supply portfolio is only 25% of total residential default supply. Of that 25%, the vast majority (80%) of supply would be composed of fixed price products. OCA St. 1-SR at 7-8. The OCA proposal also would eliminate the 10% spot market pricing feature contained in the full requirements contracts in the Companies' proposal. Because the spot market portion of "block and spot" supplies replaces the spot market pricing component of the full requirements contracts proposed by the Companies, there is no additional volatility introduced into the default service price. For these reasons, and as explained more fully in the OCA response to Dominion in its Main Brief (at 26-28), the OCA submits that its proposed plan should be adopted.

6. The OCA's Proposed "Hold Back" for the Retail Opt-In Auction.

Due to the unprecedented nature of the Commission-endorsed "opt-in auction" being proposed in this proceeding, OCA witness Kahal recommended setting aside 20% of the default residential load from the procurement process to reduce the risk premium that may be added to the FRC contracts given the uncertainty of this program. The purpose of the "hold back" is to ensure that those parties bidding for the full requirements portion of default service load are

protected from an open ended, "one of a kind" risk that the load they are bidding on will actually "show up" in expected amounts once they are required to be served.[4] By protecting the default suppliers from this risk, the OCA submits that customers will be protected from the risk premiums that suppliers would otherwise include in their bids to compensate them for the risk from this unprecedented program.

The Companies and RESA argue that the OCA's proposal to "hold back" a portion of residential non-shopping load from the default service procurements would needlessly complicate the procurement and should be rejected. In addition, the Companies argue that suppliers are capable of handling the risk created by the opt-in program. FE M.B. at 18. RESA argues that because the hold back proposal would limit participation in the opt-in program to 20% it should be rejected. RESA M.B. at 27.

With regard to the Companies' position, the OCA submits that the Company has missed the point. It is not a question of whether wholesale suppliers can properly mitigate the risks associated with the opt-in program, but a question of what they will charge, *i.e.* what risk premium they will add to their bids in order to accept the risk. The type of "volumetric risk" (i.e., the risk of losing customers) that will result from the Opt-In Auction is not comparable to normal shopping. There is no experience that any party can point to that is remotely similar to this setting. As such, extra care must be taken to ensure that default service customers are not harmed under this process by additional risk premiums included in bids for such uncertainty.

The Companies provided testimony in this proceeding that wholesale providers can manage this volumetric risk. As OCA witness Kahal testified, however, the solution offered by

[4] Constellation agrees with the OCA that there is substantial risk to full requirements suppliers as a result of the Opt-In Retail Auction, as proposed. Constellation M.B. at 28.

the Companies as to how to manage this risk is unworkable. Mr. Kahal described the "solutions" offered by the Companies, as follows:

> Dr. Reitzes makes two key points in this regard in his rebuttal testimony. First, he observes that even under my set aside proposal, wholesale FRC suppliers would continue to be exposed to volumetric risk from a number of sources, *e.g.*, weather variations, changes in the economy, normal customer shopping, etc. Second, with respect specifically to the Opt-In Retail Program, he maintains that wholesale FRC suppliers can manage this risk. He acknowledges that the FRC suppliers will not know the load responsibility implications of the Opt-In Retail Program (i.e., potentially up to 50 percent of load) at the time of the wholesale auctions when they must submit their bids. However, he claims that these suppliers simply can wait until the program sign-up period is over (presumably in March 2013) to hedge their supply risk, since at that time the default load impact will be known. At that time, the FRC suppliers can hedge forward their supply obligations based on the revealed program subscription.

OCA St. 1-SR at 20. The first area of risk, Mr. Kahal then explained, was the normal "status quo" risks in effect today. Id. Mr. Kahal further explained that the 20% hold back is not designed to address this "normal" volumetric risk, so Dr. Reitzes' comments are inapposite. Id.

As to the "solution" that FRC suppliers can simply wait to hedge their obligations, Mr. Kahal explained that this "solution" to the risk created by the Opt-In Retail Auction is unlikely to work:

> The initial wholesale FRC auction is to be held in November 2012. Assuming customer sign-up for the Opt-In Retail Program is not completed until March 2013, Dr. Reitzes implies that wholesale suppliers must submit bids for supplying an unknown load and then wait four to five months before they hedge their open positions (or fully hedge their positions). Wholesale procurement programs have been designed intentionally to minimize the amount of time that suppliers' positions are left open. This is one reason why commission approvals for wholesale auctions in Pennsylvania and elsewhere typically take place only a few days after bids are submitted. Even in this case, Mr. Fullem acknowledges EGS supplier concern about holding open their price bids for an extended period, and he therefore limits the customer sign-up period to 25 days.
>
> The four to five months for open price bids proposed by Dr. Reitzes is impractical and illustrates precisely why there is a compelling operational reason to (a) limit the program size to about 20 percent of default customers; and (b) to withhold that 20 percent load from the wholesale FRC auctions.

OCA St. 1-SR at 20-21. The OCA submits that the Companies have not adequately addressed the OCA's concerns regarding the impact of the Opt-In Retail Auction on default service prices.

RESA argues that the OCA's 20% hold back provision is designed to limit the success of the Opt-In Auction and retail competition, thereby limiting risk premiums included in default service bids. RESA M.B.at 27. The OCA submits that RESA's argument is off base. The point of Mr. Kahal's hold back proposal is to recognize the potential for a successful auction and ensure that default service is reasonably priced, in compliance with Pennsylvania law, while allowing customers the opportunity to take advantage of competitive offers if they so choose. Of critical importance, the OCA notes that the opt-in proposal is unique, and the default suppliers may not be in a position to adequately account for or assess the risks associated with this program. Mr. Kahal further explained why the 20% cap will not limit the program's success:

> Even if the 20 percent cap is reached, this will represent a huge success for this program when coupled with recent trends in residential retail shopping. It would represent a major increase in the percentage of residential customers taking EGS service within the space of a relatively short period of time. Moreover, as emphasized in my direct testimony, the 20 percent is a soft cap since there is nothing to prevent the winning EGSs (or any EGS) from making precisely the same offer to any customer seeking to participate but restricted by the cap. In that sense, the cap is not a binding constraint.

OCA St. 1-SR at 21. The OCA submits that there is a distinction between the normal risks associated with default supplies, and the unique risks inherent under the proposed Opt-In Retail Auction. This distinction must be addressed in order to ensure that default service is provided as intended under Act 129.

The OCA submits that the 20% hold back provision helps ensure that the Retail Opt In Auction can bring benefits to consumers, while at the same time ensuring that the program does

not interfere with the legal requirement that default service be "least cost over time." As such, the OCA submits that its 20% hold back recommendation should be adopted.

7. Procurement Method – Descending Price Clock Auction.

The OCA addressed these issues in its Main Brief (at 31-33).

C. Industrial Class Hourly Priced Default Service.

The OCA takes no position on this issue.

D. Use of Independent Evaluator.

The OCA takes no position on this issue.

E. AEPS Requirements.

The OCA addressed these issues in its Main Brief (at 33).

1. Non-Solar Photovoltaic Requirements

2. Solar Photovoltaic Requirements

F. Contingency Plans.

The OCA takes no position on this issue.

G. Supplier Master Agreements.

The OCA addressed issues concerning Supplier Master Agreement confidentiality in its Main Brief (at 34-35).

III. RATE DESIGN AND COST RECOVERY

A. Residential and Commercial Classes: Price to Compare Default Service Rider.

The OCA is opposed to the Companies' proposed Market Adjustment Charge (MAC) in any form, and to any effect the MAC would have on the PTC Default Service Rider. See, OCA Main Brief (M.B.) at 36-50. The OCA also supports an annual reconciliation methodology. See,

OCA M.B. at 59-62. The OCA has no opposition to the composition of the PTC Default Service Rider beyond these areas.

B. Industrial Class: Hourly Pricing Default Service Rider.

The OCA takes no position on this issue.

C. Market Adjustment Charge.

1. Summary and Overview of the OCA's Position.

The OCA submits that the MAC is a wholly unjustified profit adder to default service rates, and is in conflict with the Public Utility Code and well-established case law. If implemented, the MAC would increase costs for both shopping and non-shopping customers, and provide a substantial windfall for FirstEnergy shareholders. The Companies' proposal to implement a MAC must be rejected. The OCA will address the other parties' differing views on this topic in the following section.

2. The OCA's Position.

In its Main Brief, FirstEnergy attempts to justify its MAC proposal. Specifically, FirstEnergy alleges that parties opposed to the MAC, such as the OCA, have three principal arguments: "(1) that it is not permitted under 66 Pa.C.S § 2807(e)(3.9); (2) that it represents a "return" that, allegedly, is not justified because the Companies cannot identify any "investment" to which the "return" relates; and (3) it would not foster greater competition and EGSs would simply raise their prices." FE M.B. at 46. The OCA will address each of these issues in turn. The OCA's brief answer, however, is that the implementation of a MAC is unsound public policy and is in direct contravention of the Public Utility Code and the laws of the Commonwealth.

Section 2807(e)(3.9) is the Public Utility Code provision that is directly on point here. Section 2807(e)(3.9) does not provide for, nor authorize, a public utility to include a profit adder for the provision of default service through a reconcilable automatic adjustment clause. The Public Utility Code provides, in relevant part:

> The default service provider shall have the right to recover on a full and current basis, pursuant to a reconcilable automatic adjustment clause under section 1307 (relating to sliding scale of rates; adjustments), all reasonable costs incurred under this section and a commission-approved competitive procurement plan.

66 Pa. C.S. § 2807(e)(3.9). As the OCA explained in its Main Brief, see, OCA M.B. at 39-40, a public utility is allowed to "recover … all reasonable costs incurred." 66 Pa. C.S. § 2807(e)(3.9). FirstEnergy's recitation of the OCA's argument as to the first point here is accurate; the Public Utility Code does not provide for a profit adder over and above the dollar for dollar recovery of reconcilable default service costs. As such, FirstEnergy's invitation to the Commission to change the law in the Commonwealth must be rejected.

FirstEnergy next alleges that the OCA argues against the MAC by stating "that it represents a "return" that, allegedly, is not justified because the Companies cannot identify any "investment" to which the "return" relates". FE M.B. at 46. FirstEnergy's attempt at phraseology here is misplaced, as the plain words of the statute are clear. The operative word is "cost", and there is nothing that FirstEnergy can do to escape this clear imperative. It is not only the statute, but the courts of the Commonwealth that have made this point abundantly clear. A public utility may only *recover expenses* or *costs* that it has *actually incurred*. Cohen v. PA PUC, et al., 468 A.2d 1143, at 1150 (Pa. Commw. Ct. 1983) (internal citations omitted); See also, Barasch v. PA PUC, 532 A.2d 325, at 336 (Pa. 1987); Popowsky v. PA PUC, 695 A.2d 448, at 455 (Pa. Commw. Ct. 1997).

FirstEnergy goes on to provide two different sub-arguments in support of the MAC. FE M.B. at 47-51. The first argument is that the "brand name" of the Companies should enable a premium price for the provision of default service. OCA witness Kahal responded on this issue, as follows:

> Value and cost are two entirely different concepts. It is generally the case that in both competitive and non-competitive markets the subjective value to consumers of a product exceeds the costs of supply. This is true regardless of whether we are discussing default supply, EGS service or any other product. But this does not justify extracting this valuation that consumers attribute to a product in the form of a higher price. The central point is that it is totally incorrect to define a subjective value that consumers place on a product as being an EDC's supply "cost". This is the ultimate confusion of supply and demand.

OCA St. 1-SR at 12 (footnote omitted). As Mr. Kahal testified, FirstEnergy is attempting to substitute the concept of "value" for the "cost" language found in the Public Utility Code. As to the corollary issue of "goodwill" somehow supporting the MAC, OCA witness Kahal testified that:

> Mr. Fullem correctly concedes that it is not proper to include any goodwill in setting the EDC delivery service rates. It is equally true that it should have no bearing on default service rates, and it clearly is not a reasonable cost incurred by the EDCs in connection with providing default service.

OCA St. 1-SR at 14; see also Tr. at 217.

As to its second sub-argument, FirstEnergy declares that "[d]epressing the price of default service by regulatory fiat, as currently occurs, not only fails to adequately compensate EDCs; it makes it very difficult for EGSs to compete on the basis of price while trying to build brand loyalty of their own." FE M.B. at 50. It should be clear from this statement that: (1) the Companies recognize and admit that current regulations (which must track the statute) prohibit a profit adder such as the MAC; and (2) the Companies are not seeking to "recover" expenses or costs, but rather are looking to be "compensated" for some element other than cost. The OCA

submits that FirstEnergy's intent to change the law is clear, and it is just as clear that such intention must be rejected.

FirstEnergy alleges that the MAC is necessary in order for EGSs to fairly compete against the default PTC. FE M.B. at 45-46. The OCA disagrees with this position. As OCA witness Kahal testified:

> EGSs can certainly compete effectively with default service, as they have demonstrated, by being more efficient in acquiring generation supply than the EDCs and by offering alternative or more creative product types.

OCA St. 1-SR at 13. And, it is not only the OCA's opinion on this matter, but the facts that provide support for the OCA's position. Customers are switching to EGS service at an increasing pace across all four of the FirstEnergy EDCs. See OCA Cross Exam. Exh. 1 at 25-26. If FirstEnergy was correct about the inability of EGSs to compete against the default PTC, such robust switching numbers would simply not exist.

As to its last defense of the MAC, FirstEnergy alleges that the OCA and OSBA are wrong in claiming that the MAC would not increase competition, but rather simply raise prices for all consumers. FE M.B. at 51-52. The OCA notes at this point that the economics of the MAC and the legality of same are different issues. The OCA submits that the MAC is inconsistent with the Public Utility Code and the laws of the Commonwealth, and thus should be rejected on that basis. As to the economics of the MAC, if implemented, the OCA submits that the MAC will simply increase costs for all consumers. See OCA M.B. at 43-45.

As OCA witness Kahal testified:

> The 0.5 cent/kWh adder to the market cost of default service is certainly a sizeable rate increase. I am not suggesting that EGSs would move their price offers in lock step with the MAC. However, I believe that it is entirely plausible, if not likely, that the adder could have some influence on EGS pricing, and it could induce EGSs to raise price offers to residential customers by some fraction of the 0.5 mills. In such a case, not only will default customers be harmed by the

> MAC, but the price umbrella effect of the artificially high default service price could also harm shopping customers, albeit by less than the full MAC.

OCA St. 1 at 39-40. As Mr. Kahal indicated, an increase in the PTC could lead to an increase in the prices that EGSs offer. Customers accepting a "percent-off-the-PTC" offer will undoubtedly also see higher rates with the MAC in place. The OCA submits that the MAC would increase the rates that residential customers pay in a variety of ways.

The Companies have a substantial evidentiary burden as to the proposed MAC – which they have completely failed to carry. The proposed MAC finds no support in the Public Utility Code, the controlling case law in Pennsylvania or sound public policy. The OCA respectfully requests the Commission to deny FirstEnergy's request for the MAC.

3. RESA's Proposed Modification.

RESA suggests that the MAC be implemented but that FirstEnergy use the revenue to pay for retail market enhancement costs and coverage of any "risks" the Companies incur; and, then the Companies return the rest to all ratepayers through the non-bypassable DSSR. For all the reasons set out in the OCA's Main Brief, the OCA is opposed to RESA's proposal. See OCA M.B. at 47-49. As OCA witness Kahal testified:

> As an administrative matter, witnesses Kallaher and Butler would create an enormous slush fund, obtained from default customers, for ill-defined and hypothetical costs and risks.

OCA St. 1-R at 8. As to the disbursement of this slush fund, the RESA proposal would create unacceptable cross subsidies between customers, as only default service customers are charged for the MAC, but all residential customers pay the DSSR and thus all residential customers would receive the credit from the "leftover" MAC revenues. Through the MAC, default residential service customers would be providing a subsidy to residential customers who switched to EGS service, creating an inequitable and discriminatory situation.

4. Dominion's Proposed Modification.

Dominion supports the MAC, and in fact has suggested that the ½ cent/kwh as proposed by FirstEnergy should probably be increased to 1 cent/kwh.[5] Dominion's proposal is similar to that of RESA except that Dominion proposes that the revenues be mainly used as a credit to offset Non-Market Based Transmission (NMB) costs that FirstEnergy plans to collect through the DSSR, with any remaining revenue to accrue to the benefit of FirstEnergy. In its Main Brief, Dominion argues that artificially increasing the PTC will not cause all EGS prices to also rise, much the same as the FirstEnergy argument on this issue. Dominion M.B. at 8-10. The OCA disagrees with this assertion.

As OCA witness Kahal testified:

> As I discussed in my Direct Testimony, a MAC adder has the potential in less than fully mature markets to raise EGS price offers by at least a portion of the MAC. Thus, MAC can harm both default and shopping customers. I base this on my training and experience as a professional economist. Mr. Joseph Raia, a business manager testifying on behalf of a business coalition, correctly makes a similar point in opposing the MAC:
>
> If the price of the default service option artificially increases [due to the MAC], so could the prices of competitive products. For these reasons, I am deeply concerned by the Companies' proposed MAC. [WPP II/MEIUG/PICA/PPUG Joint Statement No. 1, page 13]

OCA St. 1-R at 9.

The OCA opposes the Dominion proposal on this issue. The MAC should not be authorized in this proceeding as it is inconsistent with the law. Similarly, the OCA opposes any redistribution of MAC revenues. See OCA M.B. at 47-50. The MAC collection and subsequent redistribution will create unacceptable and discriminatory cross subsidies to the detriment of

[5] The specific proposal by Dominion to increase the MAC to 1 cent/kwh, as found in its witness' testimony, is not discussed in its Main Brief. Accordingly, the OCA is unclear as to whether Dominion continues to advocate this idea, but if so, the OCA opposes the MAC in any form including the proposal to increase the size of this artificial adder.

remaining default service customers. Finally, as discussed above, the MAC would result in an artificial increase in all EGS' pricing offers to customers.

D. Default Service Support Rider.

FirstEnergy proposes to recover all costs of the retail market enhancements proposed in their DSP from all residential customers through the non-bypassable Default Service Support Rider (DSSR). The OCA is opposed to ratepayers being charged for the costs of these programs, and instead supports the Commission's recommendation that EGSs pay for the costs of these programs. See OCA M.B. at 82-84, 95-96; see also, Investigation of Pennsylvania's Retail Electricity Market: Intermediate Work Plan, Docket No. I-2011-2237952 (Order entered March 2, 2012) (IWP Order) at 78.

1. Non-Market Based Transmission Charges.

The OCA takes no position on this issue.

2. Generation Deactivation Charges.

The OCA takes no position on this issue.

3. Unaccounted-For Energy Costs.

The OCA agrees with FirstEnergy as to the handling of Unaccounted-for-Energy costs.

4. Economic Load Response Charges.

The OCA takes no position on this issue.

E. Solar Photovoltaic Requirements Charge Rider.

The OCA takes no position on this issue.

F. Time of Use Rate Proposals for West Penn and Penn Power.

1. Summary of the OCA's Position.

The OCA submits that the Commission's recommendation that EDCs consider fulfilling the TOU requirement through a competitive bidding process is reasonable. FirstEnergy's proposed TOU rate program, however, is too costly, lacks significant benefits for ratepayers, contains areas of potential harm to ratepayers, and is premature for a program of this type due to the limited deployment of fully-operational smart meters. The OCA submits that the residential TOU proposal for Penn Power and WPP should not be adopted for use in the upcoming DSP. See OCA M.B. at 51-58. In the following section, the OCA will respond to the differing viewpoints of the other parties on this issue as set out in their Main Briefs.

2. The OCA's Position.

FirstEnergy opposes the OCA position on several grounds. FE M.B. at 76-79. FirstEnergy claims that by the summer of 2013, West Penn will have 15,000 smart meters operational and thus the program will be viable. FirstEnergy alleges that by spreading the costs of the TOU programs to all customers the program will be cost effective. The Companies also disagree with OCA as to the merits of utilizing on-peak times that run from 7 am to 11 pm every day. FirstEnergy suggests that contrary to the OCA position, there is "very limited downside" in offering the program because if it fails then customers would be offered a TOU rate like what is currently in place for Penn Power. FE M.B. at 77. FirstEnergy also takes issue with the OCA's recommendation that the West Penn Critical Peak Rebate (CPR) could simply continue on and serve as the TOU program for West Penn customers. FE M.B. at 78. The OCA will address each of these arguments in turn.

As to the issue of WPP having 15,000 smart meters installed by the summer of 2013, uncertainty still remains at this time as to whether WPP will have sufficient quantities of fully-operational smart meters to enable a sufficient number of residential customers to participate in

the proposed TOU Program. OCA St. 2-SR at 15. What is certain at this time, however, is that Penn Power currently has no smart meters installed for residential customers and FirstEnergy has no estimate of when such fully-operational smart meters will be available. See OCA Cross. Exam. Exh. 1 at 3-4, 20. In the OCA's view, it is premature to launch a program of this type, at this time.

As to the Companies' assertions that the program will be cost effective and that there is "very limited downside" in trying it out, the OCA disagrees. The costs to conduct the proposed descending clock auction (DCA), and the annual costs of operating the program are substantial. See OCA Cross. Exam. Exh. 1 at 7 ($200,000 to $300,000 annually). The Companies' assertions that the problem is resolved by spreading these costs over a larger customer base, and that, even if it does not work out, that is also acceptable, should be rejected. The OCA submits that ratepayer funds should not be expended in such a manner.

As to the proposed on-peak periods, OCA witness Alexander succinctly captured the OCA's main concern, as follows:

> [t]he rate structure being proposed for TOU in which the entire day from 7:00 AM to 11:00 PM at night is charged at an on-peak rate is excessive. I am not aware of any residential TOU rate that charges an on-peak price for 16 hours a day. Typically, TOU rates identify a portion of each day to send the price signal that reflects the highest demand or wholesale market price for electricity. To suggest that residential customers can accommodate higher on-peak prices from 7 AM to 11 PM every weekday and shift enough usage to the middle of the night and on weekends in order to experience bill savings is unrealistic.

OCA St. 2 at 21-22. As such, the FirstEnergy proposed TOU Program is unlikely to provide benefits or attract participation even if there were sufficient customers with operational smart meters.

Finally, as to West Penn's CPR Program there appears to be a continued misunderstanding on the part of FirstEnergy as to what the OCA's position is. OCA witness Alexander clarified this point in her Surrebuttal Testimony, as follows:

> Furthermore, Mr. Fullem's assertion in his Rebuttal testimony that I recommended that West Penn's Critical Peak Rebate (CPR) program be continued beyond its current approved term without further approval misunderstands my intent. My intent was to suggest that West Penn seek continuation of the CPR program as part of its energy efficiency/demand response programs since it has also been approved to serve as a TOU rate option. If West Penn cannot obtain such approval, then I recommend that West Penn adopt a similar program to Penn Power pending the development of a future bid-based TOU program.

OCA St. 2-SR at 16. As Ms. Alexander testified, the OCA did not suggest that the CPR Program could continue on indefinitely without further Commission approval, even though at the present time it is an extremely popular program. See OCA Cross. Exam. Exh. 1 at 21.

In conclusion, FirstEnergy's TOU rate option is costly, is premature due to the limited availability of fully-operational smart meters in the service territories of WPP and Penn Power, and contains an on-peak time period that encompasses 16 hours of every weekday. For the reasons discussed above, the OCA requests the Commission to reject the Companies' proposal regarding a TOU program at this time.

3. RESA's Proposal.

RESA also responded to the OCA's proposals on the TOU Program. RESA M.B. at 45-46. In RESA's Main Brief, it set out a few of the OCA's positions concerning the Companies' proposed TOU Program, and then concluded that it was opposed to the OCA on this issue. Id. In the subsequent discussion, however, RESA never elaborated on why it was opposed to the OCA on this issue, but instead set out to explain its view of the TOU Program. RESA M.B. at 46-50.

Interestingly, the RESA approach bears many similarities to the EGS-sponsored offer alternative as discussed by OCA witness Alexander in her Direct Testimony. OCA St. 2 at 22. As such, the OCA is uncertain as to exactly what RESA's objections are as to the OCA proposals for a TOU Program. As the OCA provided in its Main Brief, the OCA had no opposition to the general framework set out by RESA through its testimony. The OCA was concerned that the proposal was not sufficiently fleshed out. See OCA M.B. at 58.

The OCA has no overarching objections to the RESA proposal, but would have to see complete details of the proposal in order to determine whether such a program would be in the best interest of consumers.

G. Reconciliation of Default Service Costs and Revenues.

1. Summary and Overview of the OCA's Position.

The OCA does not oppose the Companies' proposal to change its PTC rate on a quarterly basis. The OCA does, however, submit that an annual, rather than quarterly, reconciliation period would be of benefit to consumers and would also create a more positive shopping atmosphere. FirstEnergy's current quarterly reconciliation methodology creates unnecessary volatility in the PTC. The OCA supports changing to an annual reconciliation process, in order to provide a smoother and more consistent PTC. See OCA M.B. at 59-62. The OCA will address the other parties' arguments on this issue below.

2. The OCA's Proposal.

FirstEnergy posits three arguments as to why the OCA's proposal should not be accepted: (1) a particular class could consistently cause an under or over collection, and not switch back and forth as the OCA suggests; (2) the interest amounts over a 12-month period would be much larger; and (3) increased shopping levels could create more volatility in the PTC under the OCA

approach. FE M.B. at 81-83. The OCA disagrees with FirstEnergy on these purported failings in the OCA approach. As Mr. Kahal testified:

> With regard to the second argument, this assumes that the average deferred balance will be higher under the 12-month as compared to a three-month amortization. While this might be true, Mr. Valdes has not offered an opinion on whether the dollars involved are even material, and if so, why interest on accrued balances is particularly harmful or a more important "problem" than rate stability.

OCA St. 1-SR at 23. As to the other arguments advanced by FirstEnergy, Mr. Kahal responded that:

> His arguments (1) and (3) are theoretically possible outcomes but not really plausible. The track record that I have seen on reconciliation charges is that historically they do go in both directions – sometimes positive and sometimes negative. If they all went in one direction, there would be something wrong with the EDC's estimation procedures.
>
> …
>
> While I agree with Mr. Valdes to some extent on this outlook, this is all the more reason why a 12-month amortization is probably more appropriate and more consistent with rate stability. That is, if default loads shrink over time (due to increased shopping), then amortizing a given deferred balance over a smaller three-month sales projection will result in a larger reconciliation charge (or credit) than using a 12-month sales projection, even with the declining load outlook.

OCA St. 1-SR at 24.

As is apparent from the discussion above, FirstEnergy's arguments hinge on worst-case scenarios, where a consistent over or under collection occurs for many quarters in a row. As Mr. Kahal testified, however, this view is not supported in the normal course of reconciliation charges.

Dominion also took issue with the OCA's suggestion on this issue. Dominion alleges that a longer reconciliation period would likely result in rates that are not market reflective. Dominion M.B. at 13. OCA witness Kahal responded to this issue, as follows:

> As I discussed earlier, Dominion witness Butler expressed concern that default rate stability and predictability can promote an orderly transition to EGS service by making it easier for customers to evaluate EGS offers and compare them with

> default service. I concur with this observation. Large quarterly reconciliation charge changes can have the unintended effect of unduly moving the PTC away from pricing that reflects market conditions. For this reason, I believe that a quarterly reconciliation charge that uses a 12-month amortization period can be beneficial for promoting an orderly residential generation market.

OCA St. 1-SR at 24-25.

The OCA submits that its proposed reconciliation method will promote a better atmosphere for shopping as it will create a more stable and predictable PTC. The OCA requests that the Commission adopt the OCA position on this issue.

3. The OSBA's Proposal.

The OCA takes no position on this issue.

H. Other Tariff Changes (Conforming West Penn to Other Companies).

The OCA takes no position on this issue.

IV. COMPETITIVE MARKET ENHANCEMENTS

A. Retail Opt-In Aggregation Program.

1. The OCA's Position.

The OCA submits that, at a minimum, a successful Opt-In Auction Program should contain the following terms: the contract term should be for 12-months; the offered price should be guaranteed to be lower than the PTC for the entire contract term; a participation cap of 20% of the total, default residential customers should be enforced; the terms and conditions should be provided up front before a customer opts in; participants should receive a separate notice advising them that the program is coming to an end; participants who do not respond at the end of the program should remain with their current EGS on a month-to-month fixed price product; an RFP method should be used to solicit offers for the program; and the winning EGSs in the

auction should pay for all of the incremental costs of implementing the Opt-In Auction Program. See OCA M.B. at 62-84.[6]

In the following sections the OCA will address additional Opt-In Auction Program details, and also respond to the position of the other parties as found in their Main Briefs.[7]

2. Customer Eligibility.

a. Small Commercial and Industrial.

The OCA takes no position on this issue.

b. Shopping Customers.

The OCA agrees with the FirstEnergy position on this issue. Totally precluding residential shopping customers from participation could raise the specter of discrimination. Nothing contained in the other parties' Main Briefs have caused the OCA to reconsider its position, nor requires the OCA to submit a further reply here on this topic.

3. Program Length.

The OCA agrees with FirstEnergy that a 12-month contract term for the Opt-In Auction Program is reasonable. A longer term could introduce pricing risk for the winning EGSs and could inhibit EGS participation. OCA St. 1 at 33-34. Nothing contained in the other parties'

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[6] The IWP Order provided the following provision as to retail market enhancements:

> To the extent that an EDC chooses to deviate from these guidelines, we expect the differences to be justified by good cause shown, which includes showing operational constraints, or supported by evidence produced during an EDC's default service proceeding and supported substantially by interested parties in the default service proceeding.

IWP Order at 6-7. The OCA submits that where the OCA's recommendations deviate from the guidelines found in the IWP Order, the OCA has submitted substantial record evidence to support its recommendations.

[7] RESA provides its opinion that the OCA's proposals regarding the Opt-In Auction Program are meant "to limit the effects on default service in terms of customer loss." RESA M.B. at 57. Since the beginning of the RMI process, the OCA has worked towards the goal of seeing successful retail market enhancements employed in the various EDC service territories without harm to default service. In the OCA's view, the retail market enhancements must be a success for all stakeholders, not just shopping customers and not just a select few EGSs.

Main Briefs have caused the OCA to reconsider its position, nor requires the OCA to submit a further reply here on this topic.

4. Timing of Solicitation and Auction.

The OCA agrees with the FirstEnergy position as to the timing for the EGS auction and also as to the timing of solicitation of customers for participation. Constellation and RESA argue that the solicitation and sign up of customers should come before the EGS auction is held. Constellation M.B. at 25-27; RESA M.B. at 62-64. The OCA disagrees with this method for various reasons.

The IWP Order provides that enrollment should only occur after the EGS auction concludes. IWP Order at 55. OCA witness Alexander echoed this idea, as follows:

> [T]he suggestion that customers should be asked to enroll prior to receiving the price and full terms and conditions is unreasonable. This process would transform the opt-in auction into an opt-out auction by requiring customers to take affirmative action to de-enroll after receiving the actual price and terms. Nor is this proposal remotely similar to the retail competitive market in which customers agree to accept a specific EGS offer based on knowledge of the price and other terms of service.

OCA St. 2-R at 7. The OCA submits that full disclosure and the complete provision of terms and conditions must occur prior to enrollment.[8] The OCA supports the Commission's view on this issue and submits that such position should be adopted.[9]

5. Timing for Providing Full Terms and Conditions to Customers.

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[8] It is interesting to note that Constellation and RESA have the same concern over the EGS auction, that being the uncertain number of customers/load that the successful bidder would actually obtain. This is the crux of their argument that customers should enroll first, in order for the EGSs to know exactly the pool of customers they are bidding on. That said, OCA has proposed a 20% carve out from the Full Requirements Contract auctions for the pool of customers that could participate in the EGS auction. Under the OCA proposal, the uncertainty as to customers/load would be reduced. Yet, in their respective Main Briefs, Constellation is silent on the issue and RESA is opposed to it.

[9] In regards to RESA footnote 268 in its Main Brief, Ms. Alexander's qualifications are set out in the OCA Main Brief at page 8, footnote 15 and are detailed in OCA St. 2 at Attachment BA-1.

The OCA's position is that customers must be supplied with the full terms and conditions, including price, before participating in the Opt-In Auction Program. See OCA M.B. at 68-69. The OCA submits that the offer must be complete in order for customers to fairly evaluate the offer prior to opting in. See OCA St. 2 at 11. The OCA's position on this issue is consistent with that of FirstEnergy. Nothing contained in the other parties' Main Briefs have caused the OCA to reconsider its position, nor requires the OCA to submit a further reply here on this topic.

6. Customer Participation Cap.

a. Summary and Overview of the OCA's Position.

All residential default service customers should be solicited for participation in the Opt-In Auction Program. The maximum number of customers who should be authorized to enroll in the program, however, should be limited to no more than 20% of the total number of non-shopping customers eligible for solicitation. The OCA's primary concern in this regard is that a larger pool of potential Opt-In Auction enrollees will directly contribute to uncertainty for Full Requirement Suppliers (FRSs) bidding in the Companies' default service procurement auctions that will take place prior to the EGS auction. Such uncertainty will likely increase the level of risk premiums that such FRSs will include in their default service bids, and thus the price paid by default service customers will be higher than is reasonably necessary. See OCA M.B. at 69-72. In the following sections the OCA will respond to the recommendations of the other parties on this issue.

b. The Companies' Proposal (50%).

FirstEnergy originally included no participation cap in its case-in-chief. During the rebuttal phase of this proceeding the Companies amended their proposal to include a customer

participation cap of 50%. For the reasons just discussed, the OCA is opposed to a customer participation cap of 50%.

c. The OCA's Proposal (20%).

In its Main Brief, FirstEnergy argues that the OCA 20% participation cap could create negative perceptions of the program as customers may need to be turned away when the cap is reached. In addition, FirstEnergy asserts that the 20% cap is not in line with the Commission's goals of increasing retail competition. FE M.B. at 101-102. RESA, FES and Dominion are also opposed to the 20% cap, and make essentially the same arguments against it as FirstEnergy. RESA M.B. at 27-28; FES M.B. at 30; Dominion M.B. at 19.

The OCA is not attempting to limit the number of customers who can participate in the retail market for generation service. The OCA is recommending a pragmatic, reasoned approach that should enable a successful Opt-In Auction Program. As OCA witness Alexander testified, the current statistics indicate that the percentage of customers taking service from an EGS across all four of the FirstEnergy EDCs is continuing to trend upward at a robust pace. OCA St. 2-R at 14-15.[10] The very issue that Mr. Kahal described in his Direct Testimony, full requirements suppliers already dealing with customer migration due to increased switching activities, is an increasing reality in the Companies' service territories due to the continued growth of customers taking generation service from EGSs. OCA St. 1 at 30. As OCA witness Alexander testified:

> This program should limit enrollment to 20% of residential default service customers. My position is a not a reflection of any objection to customer choice and the development of a retail market. Rather, opening up this program that has little or no precedent or experience to rely upon to predict results carries significant risks that may adversely impact customer opinion about the retail market. If 50% of the default service customers can enroll and far less agree to enroll, the retail opt-in auction may be publicly viewed as a failure. If 20% can participate and far more seek to enroll and participate, this would be an excellent

[10] See also OCA Cross. Exam. Exh. 1 at 25-26 for the most recent shopping statistics.

> indication of customer interest in the retail market and EGSs would have the option to offer the same terms to additional customers outside the auction process itself.

OCA St. 2-SR at 6.

The OCA submits that the combination of the current shopping levels along with a 20% participation level could result in very robust overall shopping numbers, while still mitigating harm to default service. In addition, the Opt-In Auction Program as proposed here, to the best of the OCA's knowledge, has never been attempted before – in any jurisdiction.[11] In the OCA's view, it would be more reasonable to proceed in the fashion that the OCA has recommended in light of these facts.

As to the argument that customers will need to be turned away under the 20% participation cap, the OCA disagrees that this is a real issue. If participation is so great that the 20% cap is reached, then the process could certainly be viewed as a huge success and the end result would be some very robust overall shopping numbers. In addition, no customers would need to be "turned away". As OCA witness Alexander testified, EGSs would be free to offer the same terms and conditions to interested consumers outside of the Auction Program. OCA St. 2-SR at 6; see also OCA St. 1 at 31. The perceived threat of customer regret or dissatisfaction from the 20% cap simply does not exist. As such, the OCA submits that the Commission should adopt the OCA's recommendation on this issue.

7. Supplier Participation Load Cap.

The OCA takes no position on this issue.

8. Composition of Product Offer.

a. Discount from PTC.

[11] FirstEnergy is also unaware of a program of this type and size being conducted anywhere else. See OCA Cross. Exam. Exh. 1 at 10.

The OCA supports a product offer for the Opt-In Auction Program that contains a guaranteed percent off the PTC for the duration of the contract term. OCA St. 1 at 10. In the OCA's view, the retail market enhancements in this proceeding are being proposed in order to generate further interest in the competitive retail market for generation service. Such Commission-sponsored programs should allow current default customers to experience the competitive market without fear of harm and with some assured level of savings. See OCA M.B. at 72-75.

FirstEnergy was the only party to directly address the OCA's position on this issue. In its Main Brief, FirstEnergy alleged that OCA witness Alexander's position on this issue changed during the course of the proceeding, such that in her Direct Testimony she advocated for a fixed-price product that was below the PTC at the time of the default service auctions, whereas in her Surrebuttal Testimony her position changed. FE M.B. at 106-107. As this issue first surfaced during Mr. Fullem's rebuttal testimony, the OCA made certain that its position was clear in the Surrebuttal Testimony of Mr. Kahal and Ms. Alexander. Apparently, some level of misinterpretation still exists.

On this issue, Mr. Kahal testified as follows:

> MR. FULLEM STATES THAT ON THE PRICING ISSUE YOUR POSITION AND THAT OF MS. ALEXANDER DIFFER. IS THAT THE CASE?
>
> No, that is a misunderstanding. Mr. Fullem is entirely correct that my position is identical to the FE Companies' original position. Ms. Alexander also supports a pricing structure with a fixed discount to the PTCs that prevail during the full one-year term of the program, a structure that is different than a fixed cents-per-kWh price.

OCA St. 1-SR at 19. Ms. Alexander also testified that:

> FirstEnergy's proposal to allow winning EGSs to obtain customers based on a fixed price that is 5% less than the PTC in effect at the time of the EGS bid should be rejected. Such an approach will not assure participating customers of any

> savings compared to the PTC that will be in effect as a result of the default service procurement plan under consideration in this proceeding. Furthermore, such an approach does not assure the customer of any savings during the 12-month term of the contract proposed by FirstEnergy since the PTC will change every quarter. I find that Mr. Fullem's concern about "teaser rates" (as the basis for his rejection of a six month program and the rejection of a bonus payment) confusing since the design of the price proposed by FirstEnergy carries a significant risk that customers will pay more than the PTC after enrollment, thus contributing to the same situation that Mr. Fullem describes. *As I recommended in my direct testimony*, the price offered to customers should assure savings during the term of the contract compared to the PTC that will be in effect during the term of the contract.

OCA St. 2-SR at 7 (emphasis added, footnote omitted).[12]

Contrary to FirstEnergy's assertions, there is no conflict between the OCA witnesses on this issue, nor did OCA witness Alexander change her position during this case. The OCA's position is identical to the position that FirstEnergy initially proposed in its case-in-chief, customers should receive an offer that guarantees a percent off the PTC for the entire term of the contract. To be clear, as the PTC changes on a quarterly basis, the percent off would apply to the new PTC and thus the customer would be assured that they were paying a price that is lower than the PTC for the entire term of the contract.

b. Bonus Payments.

The OCA does not object to the inclusion of a bonus payment as an incentive for customers to enroll in the Opt-In Auction. The OCA would note, however, that, as the Opt-In Auction Product is currently being proposed by FirstEnergy, with or without a bonus, auction participants may end up paying more than they would have if they had remained on default service. There is no assured level of savings, as the percent off the PTC does not track quarterly changes. Accordingly, and for all the reasons discussed above, the OCA respectfully requests

[12] In Ms. Alexander's Surrebuttal Testimony she included footnote 1, which clarified that her position and that of OCA witness Kahal on this issue were identical. OCA St. 2-SR at 7, fn 1.

the Commission to view the entire record on this matter and adopt the OCA's recommendations as to the composition of a product offer for the Opt-In Auction Program. See OCA M.B. at 75-76.

c. Provision of Standard Contracts Specifying All Terms and Conditions of Service.

The OCA takes no position on this issue.[13]

9. RESA's Proposal to Conduct Testing of Various Marketing Channels Before Implementing the Program.

The OCA opposes the RESA recommendation to implement a test program. See OCA M.B. at 77-78. The OCA agrees with the Commission's recommendation in the IWP Order that this type of pilot program should not be implemented. Nothing contained in the other parties' Main Briefs have caused the OCA to reconsider its position, nor requires the OCA to submit a further reply here on this topic.

10. Customer Options on Program Expiration and Notices to Customers of Contract Expiration.

The OCA disagrees with the Companies' proposed handling of customers and also the notice provisions that would occur at the expiration of the Opt-In Auction Program. Under the FirstEnergy proposal, customers would receive two notices from the EGS, and non-responders would remain with their EGS at such terms and conditions as the EGS may set. The OCA submits that three notices should be provided to customers prior to the end of the program, one from the EDC stating that the program is coming to an end and two from the EGS as required by

[13] In the OCA's Main Brief there is a discussion in this section, IV. A. 8. c., as to the enrollment forms for customers. It has now become apparent that this section was meant to discuss EGS/EDC contracts. As such, the OCA takes no position on this issue, and would note that its discussion in this section of its Main Brief at pages 76-77, properly belongs with section IV. A. 5.

the Commission's regulations. Customers who do not respond to a notice would stay with their current EGS on a fixed-price, month-to-month product. See OCA M.B. at 77-81.

In its Main Brief, FirstEnergy alleges that it has operational constraints that would preclude it from sending the EDC notice recommended by OCA, and that in its opinion the three-notice requirement is unnecessary. FE M.B. at 114-115.[14] RESA agrees with FirstEnergy that two notices are sufficient, and also states that "OCA's position is also not consistent with moving customers into the competitive market". Dominion also disagrees with the three-notice requirement, but does agree with the OCA that customers should be given a fixed-price product at the end of the initial contract term in order to avoid any surprise when the fixed-price product suddenly turns variable. Dominion M.B. at 22.

The OCA submits that customers participating in the Opt-In Auction Program, which is sponsored by FirstEnergy and backed by the Commission, deserve some extra layer of protection. The EDC should be involved in the end-of-contract notice, if for no other reason than to maintain the good customer relations and trust that Mr. Fullem has repeatedly testified is important to the Companies. In the OCA's view, the three-notice recommendation is an important consumer protection that should be ordered by the Commission in this matter.

11. Structure of Opt-In Auction – Descending Price Clock Auction versus Sealed Request for Proposals.

[14] FE M.B. at 114-115. FirstEnergy Solutions (FES) also disagrees that three notices are necessary, but mischaracterizes part of the OCA's recommendation as to the disposition of customers at the end of the contract period. FES alleges that CAUSE-PA and OCA advocate for the automatic return of customers to default service. FES M.B. at 43. That is not the OCA's position. The OCA recommends that customers who do not respond to the end of contract notices would stay with their current EGS on a fixed-price, month-to-month product.

The OCA opposes the use of a DCA for the EGS auction. The OCA recommends that an RFP approach be used. The OCA's primary objection to the DCA approach is the substantial costs to operate such a method. See OCA M.B. at 81-82.

FirstEnergy defends the use of a DCA as being a more effective method and also alleges that the opposing parties, namely RESA, Dominion and the OCA have failed to quantify why an RFP approach is superior.[15] Mr. Butler testified on behalf of Dominion that he has personal experience with both types of processes. Dominion St. SR-1 at 6. From his practical experience, Mr. Butler testified that the cost disparities are great and that there is no real difference in results either way. Id. The OCA agrees with RESA and Dominion on this issue. See also Dominion M.B. at 23.

12. Recovery of Costs.

a. All Customers versus EGSs.

The OCA agrees with the Commission that participating EGSs should be responsible for the costs created by the Opt-In Auction Program. See OCA M.B. at 82-83; IWP Order at 78. FirstEnergy argues in its Main Brief that EGSs may not participate if they have to foot the costs, some EGSs may participate but then never satisfy their financial obligations to the Companies, and that customers may not get the best offers if the EGSs have to price the cost of the program into their bids.[16]

In his Surrebuttal Testimony, OCA witness Kahal commented on these arguments, as follows:

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[15] FE M.B. at 116-118. FES also supports the DCA method. FES M.B. at 43-45.

[16] FE M.B. at 118-119. FES supports FirstEnergy on this issue. FES M.B. at 44-46.

> The Joint Petitioners in rebuttal testimony continue to support charging all program costs to residential customers, and they have provided no compelling operational argument for their position. Notably, Dominion witness Butler supports the Commission's guidance on this issue in his rebuttal testimony. (Rebuttal testimony, page 5) I believe that participating EGSs, who also stand to benefit by expanding market shares, should be willing to accept the program implementation costs. If the program implementation costs are merely imposed on customers (including those that do not participate), it runs the risk of being a net harm to customers.

OCA St. 1-SR at 17. As Mr. Kahal testified, FirstEnergy's arguments on this issue ring hollow for several reasons.

As to EGSs not participating or increasing their bids to compensate for the costs of the Auction, the OCA submits that these EGSs are being given an opportunity to acquire large numbers of customers without the individual transaction and marketing costs that are normally required. Accordingly, since the EGSs already stand to significantly reduce their per-customer transaction costs by participating in the Auction, FirstEnergy's arguments lack merit. The OCA respectfully submits that the Commission should authorize the Companies to collect the Auction costs from participating EGSs, as the IWP Order provides.

b. Recovery through the Market Adjustment Clause as Proposed by RESA.

The OCA is opposed to the implementation of a MAC. As such, the OCA is opposed to the RESA recommendation that revenues from the MAC be used to cover costs of the Opt-In Auction Program. See OCA M.B. at 83-84. Nothing contained in the other parties' Main Briefs have caused the OCA to reconsider its position, nor requires the OCA to submit a further reply here on this topic.

c. Form of Recovery if EGSs to be Responsible for all Costs.

The OCA supports the recovery of all costs for the implementation of the Opt-In Auction Program from participating EGSs. FirstEnergy witness Fullem testified as to a method that

could be used for the recovery of such costs from the EGSs. FE M.B. at 120-121; FE St. 7-R at 40. The OCA has no opposition to this approach.

B. Standard Offer Customer Referral Program.

1. The OCA's Position.

The OCA submits that the Referral Program as proposed by FirstEnergy is overly complicated, entails substantial costs and is likely to result in customer confusion and potential dissatisfaction. In the OCA's view, FirstEnergy should scale back and modify its Referral Program in order to provide a more gradual implementation. The OCA submits that additional key elements for a successful Referral Program should include: customers who do not affirmatively respond to the notices at the end of the contract should be returned to default service; the EDC should only solicit those customers who call to establish service, are moving to a new location within the service territory or specifically inquire about choosing an electric generation supplier; the term of the Referral Program contract should be four months in order to ensure that customers will realize savings; the product offer should be a guaranteed percent-off-the PTC for the entire four months; and the EGSs participating in the Referral Program should pay for the incremental costs to implement this program. See OCA M.B. at 84-97. In the following sections, the OCA will address details of the Referral Program and also respond to the arguments of the other parties as found in their Main Briefs.

2. Customer Eligibility.

Consistent with its discussion above, the OCA submits that the Referral Program should be affirmatively offered to new customers, those customers moving within the EDC service territory, and those who specifically inquire about customer choice or the Referral Program, but other customer calls to the EDC should not trigger a requirement to offer the Referral Program. This

approach will serve to offset any perceived bias in favor of default service and also tend to minimize program costs. OCA St. 2-SR at 14. Nothing contained in the other parties' Main Briefs have caused the OCA to reconsider its position on this issue. See OCA M.B. at 84-94.

3. Term of the Standard Offer Product and Length of 7% Discount.

The OCA submits that the Referral Program should be for a term of four months and that throughout that term, the customer should be guaranteed a specific percent off the PTC. This method would ensure that customers participating in the program would receive guaranteed benefits in the form of savings. At the end of the contract term, customers who do not affirmatively respond to the EGS' notices should not be retained by the EGS, but rather should be transferred back to default service.

FES disagrees with the OCA as to the length of the product offer, as FES supports a 12-month contract. FES M.B. at 50. The OCA's objective in recommending a four-month time frame is to allow customers to experience the competitive retail market, but to enable that experience without risk of harm. If FES was proposing that the product was 12 months, and that the offer price would always be lower than the PTC during the entire term of the contract, then OCA and FES would have no disagreement on this point. But, that is not the case.

OCA witness Alexander captured the essential OCA position here, as follows:

> I object to a 12-month Referral program contract if the price is offered as a percentage discount off the PTC in effect at the time of the offer. Similar to my concerns expressed about the pricing method for the 12-month Opt-In Auction contract, a 12-month Referral program contract carries a risk that the price during the contract term will be higher than the PTC. The best way to ameliorate this concern is to limit the Referral program contract to four months, during which time the PTC is unlikely to change significantly and the required notices that I have recommended in my Direct testimony can be issued.

OCA St. 2-SR at 15. In addition, it is important to recognize that a large percentage of customer calls to the Companies will be from new/moving customers. The OCA remains doubtful that

consumers engaged in moving their entire household will understand or appreciate that the 7% off-the-PTC only applies until the next quarterly change. Accordingly, the OCA supports a four-month product with guaranteed savings as compared to the default PTC.

4. Recovery of Costs.

a. All Customers Versus EGSs.

The OCA supports the Commission's recommendation that the costs of the Referral Program should be recovered from EGSs. The OCA respectfully submits that the Companies' proposal to recover these costs through the DSSR from all residential customers should be denied. The EGSs will be the primary beneficiaries through substantially reduced transaction costs, and, as such, should be responsible for the costs of the Referral Program. See OCA M.B. at 84-94

b. Recovery Through the Market Adjustment Clause as Proposed by RESA.

The OCA opposes the implementation of the MAC. As such, the OCA opposes the use of the MAC as a funding mechanism for the Referral Program, or for any other purpose. Nothing contained in the other parties' Main Briefs have caused the OCA to reconsider its position.

c. Form of Recovery if EGSs to be Responsible for All Costs.

The OCA supports the recovery of Referral Program costs from EGSs. In his rebuttal testimony, FirstEnergy witness Fullem describes a recovery methodology whereby the Companies would recover these costs from EGSs. FE M.B. at 128; FE St. 7-R at 46. The OCA has no opposition to this approach.

5. Constellation's Proposal to Require Customers to "Opt In" in Order to Be Eligible to Participate.

The OCA agrees with FirstEnergy witness Fullem's comments as to the Constellation proposal on this issue. See FE St. 7-R at 49. As discussed by Mr. Fullem, witness Fein for Constellation recommended that customers should be notified of the Referral Program, in advance, and asked to indicate whether they wished to be given the chance to participate in the Referral Program, at some future date. Id. Requiring customers to opt in to a program that they do not have full and complete details about will likely only result in customer confusion.[17] Accordingly, the OCA opposes this recommendation by Constellation.

6. The OCA's Proposal to Sequence the Implementation of the Customer Referral Program.

The OCA submits that FirstEnergy should scale back and modify its Referral Program in order to provide a more gradual implementation. Under FirstEnergy's proposal, the Referral Program would roll out in very close proximity to the implementation of the Opt-In Auction Program. These two programs share many similarities and could easily cause unnecessary levels of customer confusion. Consistent with a more gradual, reasonable implementation of a customer referral program, the OCA supports a bifurcated approach to implementation that would include a more basic first-year program along with a ramped up program for year two.

FirstEnergy alleges that the OCA's criticisms regarding the complexity of the Referral Program are now a moot point, since the Companies amended their original proposal as a result of the IWP Order. FirstEnergy also alleges that OCA's recommendations to delay the implementation or to bifurcate the Referral Program are really just attempts to "kill" the program

[17] This idea is discussed briefly in Constellation's Main Brief. Constellation M.B. at 31. It appears that Constellation is suggesting that the Companies mail a letter or postcard to all of its residential customers, explaining the Referral program, and then seeking an affirmative response as to whether, at some future date when the customer calls one of the EDCs, the customer wishes to be apprised further as to the Referral Program. In the OCA's view this would only serve to further complicate the implementation process.

altogether. FE M.B. at 129-130. RESA also opposes any recommendation that the Referral Program be implemented in the manner recommended by OCA. RESA M.B. at 85.

The OCA disagrees that its concerns over the complexity and confusion factor that may accompany the implementation of the Referral Program at the same time as the Opt-In Auction Program are a moot point. As OCA witness Alexander discussed in her Surrebuttal Testimony, in response to FirstEnergy's amended Program:

> Both FirstEnergy and RESA oppose my recommendation to delay the standard Referral Program as described above until after the one-time opt-in auction has concluded. The implementation of both the opt-in auction and the referral programs during the same period of time (even if separated by 4-6 weeks) is likely to lead to customer confusion and the potential for customer dissatisfaction. This potential for confusion is exacerbated by the fact that the Opt-in Auction program will offer a 5% reduction off the PTC and the Referral Program will offer a 7% reduction from the then-current PTC, a distinction that does not appear to make sense in explaining the various programs to customers. Furthermore, the potential that customers who enroll in the Opt-In Auction may end up paying more than the PTC during the auction term whereas those who did not participate will be offered a 7% reduction in the then-current PTC will create the potential for customer dissatisfaction and complaints. In the meantime, a referral program "light" should be implemented by FirstEnergy which I described in my Direct Testimony.

OCA St. 2-SR at 13-14. It is not the OCA's intent to discard the Referral Program, but rather to modify how and when it is implemented in order to provide the best chance for successful outcomes. The implementation of the Referral Program on the heels of the initial implementation of the Opt-In Auction Program will create unnecessary customer confusion. As the OCA recommends, a reasonable period of time following the Opt-In Auction Program before the Referral Program is rolled out could make a substantial difference as to its ultimate success. This is a minor modification in timing that the Commission can and should authorize.

7. <u>RESA's Proposal to allow the Standard Offer Customer Referral Program to Displace the New/Moving Customer Referral Program</u>.

While there are aspects of RESA's proposal that the OCA agrees with, such as the recommendation to simplify the Referral Program, the OCA continues to support the OCA's own suggested referral program elements as discussed above. See OCA M.B. at 84-94. Specifically, the OCA submits that a bifurcated approach to the Referral Program, which includes a modest first-year new/moving program, will provide a more reasoned and pragmatic method for implementation of this retail market enhancement activity. OCA St. 2 at 15-18.

C. Limiting Participation By Low-Income Customers In Proposed Retail Market Enhancements.

1. CAUSE-PA's Proposal.

The OCA has maintained throughout the RMI proceeding that CAP customers, and other customers who pay the CAP shortfall, must be held harmless if CAP customers are allowed to participate in any of the proposed retail market enhancements. Accordingly, the OCA supports the position of CAUSE-PA on this issue at this time that CAP customers should not be allowed to participate in either the Opt-In Auction Program or the Referral Program. See OCA M.B. at 97-98.

FirstEnergy adheres to the belief that CAP customers should be authorized to participate in the retail market enhancements. FE M.B. 132-137. RESA also advocates for CAP customer participation in the retail market enhancements.[18] The OCA notes that none of the parties in favor of authorizing CAP customers to participate have addressed the OCA's concern on this issue – that being not only potential harm to individual CAP customers but also to the CAP program as a whole.

[18] RESA M.B. at 88-91. FES also supports this idea. FES M.B. at 57-58.

During the cross-examination of FirstEnergy witness Fullem, he was asked about CAP customers paying for the MAC through the Default Service Support Rider (DSSR). Mr. Fullem agreed that CAP customers who are not shopping would be assessed the MAC charges just like all other default residential customers. Tr. at 204. The actual exchange was, as follows:

> Q. So any CAP customer under the default service would have to pay their cost of that rider?
>
> A. They would pay the cost -- the rider would be included in the calculation of their energy burden. And through the CAP credit we reduce them down to a three or a nine percent income level, *so I would argue that they probably in effect are not paying that price.*

Id. (emphasis added). Mr. Fullem precisely framed the issue that the OCA has raised throughout, if CAP customers costs increase all other customers who pay the CAP shortfall (the difference between the "asked to pay amount" and the actual bill) will be harmed if CAP customers are authorized to participate in the retail market enhancements and their energy burden, or costs, go up. The CAP shortfall is charged to all residential, non-CAP customers, even those who are themselves low income.[19] For all the reasons discussed here, the OCA supports the position of CAUSE-PA regarding CAP customers participating in the retail market enhancements at this time.

2. The OCA's Proposal.

The OCA agrees with CAUSE-PA on this issue, as set out above.

V. OPERATIONAL ISSUES

A. System "Enhancements" Proposed by Constellation.

[19] As yet another form of collateral damage from the proposed MAC, all non-shopping residential customers would be charged the MAC. CAP customers would also be assessed the MAC as part of their energy burden, as Mr. Fullem explained, yet CAP customers would not actually pay the MAC. Those surplus charges would accrue to the CAP shortfall, be charged to all other default service residential customers, and thus non-shopping, non-CAP, residential customers would be paying even more for the MAC.

Constellation's System Enhancement recommendations were addressed by FE witness Valdes in his rebuttal testimony. FE St. 2-R at 27-29. Constellation's Main Brief provided that this issue is something that Constellation will not pursue further in this docket. Constellation M.B. at 32. Accordingly, the OCA has no further comment on this issue.

B. RESA's Proposal that that Companies Investigate Implementing a Secure, Web-Based System to Provide EGS Electronic Access to Customer Usage and Account Data.

The OCA lacks sufficient information from any of the testimony or other record evidence in this proceeding in order to fairly judge the "Operational Enhancements" proposed by RESA. In its Main Brief, RESA discussed the idea of having the Companies create a secure supplier website and other system enhancements. RESA M.B. at 91-93. No information is provided, however, as to the potential costs of such enhancements, or what entity would be assigned such costs under the RESA proposal.

FirstEnergy discusses the issue in its Main Brief, and recommends that this is an item that should be pursued through the RMI process. FE M.B. at 139-140. Alternatively, FirstEnergy states that if the Commission were to order such enhancements to be made, then the Companies must be authorized to collect those costs either from ratepayers through the DSSR or from the EGSs through some other mechanism. Id.

The OCA submits that this is an issue best left for a separate working group, whether within the RMI process or elsewhere. In addition, no cost estimates are available at this time, nor are there any proposals from RESA as to how these enhancement costs should be allocated. This issue should not be finally decided here on such sparse facts.

VI. AFFILIATED INTEREST APPROVAL

A. Approval of Contracts under Chapter 21 as Requested in the Joint Petition.

The OCA takes no position on this issue.

VII. OTHER ISSUES

If the Standard Offer Customer Referral Program is authorized to proceed, the Companies request that "all customer telephone calls regarding high bill complaints and new service requests be excluded from the data to which the Commission applies its metrics for measuring the percentage of calls answered within thirty seconds." FE M.B. at 141. The OCA objects to this proposed waiver and the degradation in customer service that will result. As OCA witness Alexander testified:

> I do not recommend that any Referral program or other market enhancement program result in or be used as an excuse for a deterioration of customer call center standards. This concern in part is reflected in my proposals for the design of a Referral Program.

OCA St. 2 at 18. The IWP Order provided the following relevant guidance as to referral programs:

> As to program costs, we agree with the assertions of OCA and UGIES that the bulk of the costs, including the costs of maintaining the referral programs once they are put into place, should be the responsibility of the participating EGSs.

IWP Order at 32. If FirstEnergy needs to devote additional resources to ensure that its call center metrics do not deteriorate as a result of the Referral Program, then such incremental costs should be borne by the EGSs as the Commission provided. As the Public Utility Code provides, in relevant part:

> **(d) Consumer protections and customer service.--**The electric distribution company shall continue to provide customer service functions consistent with the regulations of the commission, including meter reading, complaint resolution and collections. Customer services shall, at a minimum, be maintained at the same level of quality under retail competition.

66 Pa.C.S. § 2807(d).

The OCA submits that the implementation of retail market enhancements should in no way compromise the Companies' duty to provide reasonable service to customers.

VIII. CONCLUSION

For the reasons detailed in this Reply Brief, and those contained in the OCA's Main Brief, the OCA submits that the Company should be directed to modify their default service Plans. The OCA's proposed modifications are designed to ensure that default service is provided through a prudent mix of contract designed to be the least cost to customers over time, recognizing the benefits of price stability, and without any unjustified profit adders. These modifications will further ensure that retail competition continues to grow in the Companies' service territories through successful retail enhancement programs. The OCA respectfully submits that its positions on the issues addressed in its Briefs be adopted.

Respectfully Submitted,

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CERTIFICATE OF SERVICE

Joint Petition of Metropolitan Edison Company,	:	Docket Nos.
Pennsylvania Electric Company, Pennsylvania	:	P-2011-2273650
Power Company, and West Penn Power	:	P-2011-2273668
Company for Approval of Their Default Service	:	P-2011-2273669
Programs	:	P-2011-2273670

I hereby certify that I have this day served a true copy of the foregoing document, the Office of Consumer Advocate's Reply Brief, upon parties of record in this proceeding in accordance with the requirements of 52 Pa. Code §1.54 (relating to service by a participant), in the manner and upon the persons listed below:

Dated this 16nd day of May 2012.

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