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May 16, 2012

Rosemary Chiavetta, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street, 2nd Floor
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 and P-2011-2273670**

Dear Secretary Chiavetta:

Enclosed for filing on behalf of Washington Gas Energy Services, Inc. ("WGES") is an original of its Reply Brief in this matter. This document has been e-filed at the Pennsylvania Public Utility Commission's website. Copies have been served in accordance with the attached Certificate of Service.

If you have any questions, please do not hesitate to contact me. Thank you.

Best Regards,

STEVENS & LEE


Michael A. Gruin

cc: Honorable Elizabeth H. Barnes, Administrative Law Judge

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A PROFESSIONAL CORPORATION

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

JOINT PETITION OF METROPOLITAN	:	
EDISON COMPANY, PENNSYLVANIA	:	Docket Nos. P-2011-2273650
ELECTRIC COMPANY, PENNSYLVANIA	:	P-2011-2273668
POWER COMPANY AND WEST PENN	:	P-2011-2273669
POWER COMPANY FOR APPROVAL OF	:	P-2011-2273670
THEIR DEFAULT SERVICE PROGRAMS	:	

REPLY BRIEF

Of

WASHINGTON GAS ENERGY SERVICES, INC.

Dated: May 16, 2012

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I. INTRODUCTION AND PROCEDURAL HISTORY

Washington Gas Energy Services, Inc. (“WGES”), by and through its counsel, Stevens & Lee, P.C., hereby files this Reply Brief to respond to the arguments propounded by the First Energy Companies regarding several of their proposed competitive market enhancements. WGES was afforded Intervenor status in the proceeding by Order dated December 22, 2012. WGES did not file testimony in this proceeding, but reserved the right to file Briefs. In this Reply Brief, WGES will respond to the First Energy Companies’ arguments regarding the proposed Market Adjustment Charge (“MAC”) and Retail Opt-in Aggregation Program. As explained below, the MAC should be rejected because it does not comport with the Public Utility Code’s requirements for default supply procurement, and because it provides an improper incentive to retain customers on default service. With respect to the Companies’ Opt-in Aggregation Program, there is sufficient support in the record to warrant imposing a 25% supplier participation cap for the Program.

III. RATE DESIGN AND COST RECOVERY

The only Rate Design and Cost Recovery issue that WGES will address is the Market Adjustment Charge (“MAC”).

C. Market Adjustment Charge

1. Summary and Overview of First Energy Companies’ Proposal

The First Energy Companies argue that the proposed \$.005/kWh MAC will “compensate the Companies for the risks they bear and the value they provide as default service providers”, and that such risks constitute “reasonable costs” of furnishing default service that are

recoverable under 66 Pa.C.S. § 2807(e)(3.9).¹ The Companies argue that without the MAC, the price of default service would be “artificially depressed”.² Finally, the Companies argue that the MAC is a competitive enhancement by providing “headroom” which will result in greater market penetration by EGSs.³

2. The Positions of the Parties Opposing the MAC Are Persuasive

The Commission has never before authorized an EDC to incorporate an “addder” into the price for default service, and the First Energy Companies have failed to make a persuasive case for approving such an adder in this proceeding. The Companies have not provided any cost justification for the MAC, and therefore it does not pass muster under 66 Pa.C.S.A. § 2807 (e) (3.9), which only permits default service providers to recover reasonable costs incurred to provide default service. For that reason alone the MAC should be rejected. But even if the legal prohibitions of Section 2807 did not exist, the MAC should be rejected from a policy perspective because the record reflects that the MAC will undermine competition in Pennsylvania.

As proposed, the MAC would provide the First Energy Companies with an improper incentive to inhibit customer migration to EGSs. The Companies estimate that the MAC will generate approximately \$140 million in revenue over 24 months.⁴ They argue that this amount is necessary to compensate the Companies for the “value” they create for customers and the “risks” they bear,⁵ but the Companies submitted no evidence to quantify the actual costs associated these risks.⁶ The Companies characterize the MAC as providing “compensation” for

¹ First Energy Companies’ Main Brief, at p. 40

² *Id.*, at p. 41

³ *Id.*

⁴ First Energy Companies’ Statement No. 7-R, at p. 11

⁵ First Energy Companies’ Main Brief, at pp. 41-42

⁶ See, OCA Statement No. 1-SR, p. 11

value provided and risks borne,⁷ but without any actual cost-justification, the \$140 million is nothing more than an artificial and arbitrary profit adder for the Companies.⁸ Because the MAC does not relate to actual costs incurred, it is not lawful under Section 2807, as several parties have persuasively argued.⁹

Even if the Commission accepts that the MAC is lawful under Section 2807, the MAC should be rejected on policy grounds. With no correlation to actual costs incurred, the MAC services as a profit adder, and provides a powerful incentive for the Companies to inhibit the migration of default service customers to alternative suppliers.¹⁰ Such an incentive would clearly frustrate the development of competition in the Commonwealth, not enhance it.¹¹

3. RESA's Proposed Modification

RESA's proposal addresses the perverse incentive created by the Companies' MAC (i.e., the incentive to inhibit migration of default service customers). As RESA suggests, if the MAC was structured so that it recovered actual, quantifiable costs of providing default service and to pay for risks that actually materialize, rather than compensate the Companies for amorphous "value-provided", the MAC would not provide an incentive for the Companies to keep customers on default service.¹²

4. Dominion's Proposed Modification

Dominion's proposal is the only one of the three that incorporates a phase-out based on actual shopping statistics. Dominion proposes a 1-cent per kWh MAC that would remain in place until a 50% shopping rate is achieved.¹³ The First Energy Companies indicated

⁷ *Id.*, at 41-44.

⁸ I&E Statement No. 1-R, at pp.3-4

⁹ See, e.g., the Main Briefs of the OCA, at pp. 38-43, the Industrials, at pp. 33-35, CAUSE-PA, at pp. 10-12

¹⁰ RESA Statement No. 2-R, at p. 33

¹¹ RESA Statement No. 2, at p. 31

¹² *Id.*

¹³ Dominion Statement No. 1, at p. 10

that they were receptive to Dominion's 1-cent per kWh MAC proposal, but argued that one-half of the proceeds from the MAC should flow to the Companies as "compensation" for the "value" the Companies provide.¹⁴ Dominion's proposal and the Companies' response highlights the perverse incentive associated with a MAC that is not tied to demonstrated costs. Under Dominion's proposal, the Companies would have an actual switching benchmark to avoid. The Companies would have a huge incentive to keep customer-switching below that 50% benchmark, because under Dominion's proposal, once that benchmark is reached, the MAC "compensation" would disappear. No such incentive should be allowed.¹⁵ If the Commission adopts the Companies' reasoning and allows a MAC to compensate for "value provided", then the Commission should actually adopt the inverse of Dominion's proposal, i.e., only allow such compensation to kick-in if 50% switching occurs. This will provide the Companies with an incentive to migrate customers off default service, whereas Dominion's proposal would provide incentive to keep customers on default service.

IV. COMPETITIVE MARKET ENHANCEMENTS

The only Competitive Market Enhancement that WGES will address is the Retail Opt-In Aggregation Program, and specifically, the Supplier Participation Load Cap sub-issue.

A. Retail Opt-In Aggregation Program

1. Summary and Overview of Each Party's Position

WGES acknowledges that the Companies' Opt-in is largely consistent with the guidance set forth in the Commission's *Intermediate Work Plan Final Order*.¹⁶ However, as set

¹⁴ First Energy Companies' Statement No7-R, at p. 13. See also First Energy Companies' Main Brief, at p. 53

¹⁵ RESA Statement No. 2, at p. 31

¹⁶ *Investigation of Pennsylvania's Retail Electricity Market: Intermediate Work Plan*, Docket No, I-2011-2237952, Order entered March 2, 2012.

forth more fully below, the record in this case supports a deviation from the Commission's guidance, and justifies the imposition of a 25% supplier participation cap for the Companies' Opt-in Aggregation Program.

7. Supplier Participation Load Cap

a) Summary and Overview of Each Party's Position

The Companies modified their proposed Opt-in Aggregation Program to incorporate a 50% supplier participation cap, which is consistent with the guidance provided by the Commission in the *Intermediate Work Plan Final Order*.¹⁷ Dominion argued for lower participation caps, while First Energy Solutions argued for no participation cap. WGES believes the record supports the position of Dominion, and the Commission should modify the Companies' Programs to include a 25% supplier load cap.

b) The Companies' Proposal

The Companies modified their proposed Opt-in Aggregation Program to incorporate a 50% supplier participation cap.

c) Dominion Retail's Proposal

As the Commission noted in the *Intermediate Work Plan Final Order*, "Retail Opt-in Auctions pose a possible safe and easy mechanism to increase customer participation in the competitive market, and to decrease EGS customer acquisition costs."¹⁸ Dominion makes a compelling argument that allowing one EGS to dominate an auction would be counterproductive.¹⁹ To avoid that dominance, Dominion's witness Mr. Butler originally suggested that EDC-affiliates should be prohibited from participating in the opt-in auction and

¹⁷ Companies' Main Brief, at pp. 102-103

¹⁸ *Intermediate Work Plan Final Order*, at p. 33

¹⁹ Dominion Main Brief, at p. 20

that a 25% supplier participation load cap be implemented.²⁰ The Companies argue that a 25% load cap would create an unacceptable risk that the Retail-Opt-In Auction would produce prices that were too high to justify the diversity that a load cap would produce.²¹ But, there is no support in the record for this proposition that higher prices would result from a 25% cap. Mr. Butler subsequently agreed that a 50% load cap could provide adequate protection, but he did not retract his proposal to prohibit EDC affiliates from participating in the Program. First Energy Solutions – the EGS affiliate of the Companies - was the only intervener to object to this proposal by Dominion.²² On this point, Mr. Butler’s initial position is more compelling than First Energy Solutions’ position. The 25% load cap will ensure a greater diversity of suppliers and protect against potential domination by EDC affiliates, and there is no evidence in the record to support a conclusion that a 25% cap will necessarily result in higher prices.

VIII. CONCLUSION

For the foregoing reasons, WGES respectfully submits that the Commission should reject the First Energy Companies’ proposed Market Adjustment Charge. The Companies have not met their burden of proving that the MAC is lawful under 66 Pa.C.S. § 2807(e)(3.9). Furthermore, the MAC would be a grave policy mistake that would provide an improper incentive for the Companies to inhibit customer migration away from Default Service. The Commission should also modify the Companies’ proposed Retail Opt-in Auction to include a 25% supplier participation load cap, to ensure diversity in supplier participation and guard against potential EDC-affiliate dominance.

²⁰ Dominion Statement No. 1, at p. 6

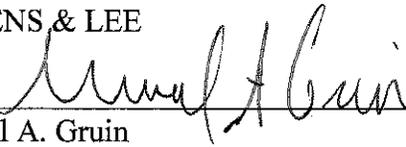
²¹ Companies Main Brief, at p. 103

²² First Energy Solutions Main Brief, at p. 32

Respectfully submitted,

Dated: May 16, 2012

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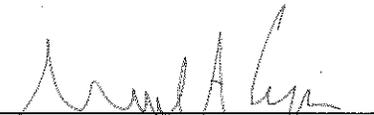
CERTIFICATE OF SERVICE

I hereby certify that I have this day served by First Class U.S. Mail and Electronic Mail a true and correct copy of the foregoing Reply Brief upon the parties listed below, in accordance with the requirements of § 1.54 (relating to service by a party)

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