

**Met-Ed/Penelec/Penn Power/West Penn
Statement No. 1**

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

**METROPOLITAN EDISON COMPANY
DOCKET NO. P-2015-_____**

**PENNSYLVANIA ELECTRIC COMPANY
DOCKET NO. P-2015-_____**

**PENNSYLVANIA POWER COMPANY
DOCKET NO. P-2015-_____**

**WEST PENN POWER COMPANY
DOCKET NO. P-2015-_____**

DEFAULT SERVICE PROGRAMS

**For the Period
June 1, 2017 to May 31, 2019**

**Direct Testimony
of
Robert B. Reeping**

**List of Topics Addressed
Product Definitions
Procurement Process and Schedule
Default Service Supplier Master Agreement
Alternative Energy Portfolio Standards Act Requirements
Contingency Plans**

TABLE OF CONTENTS

	Page
I. INTRODUCTION AND PURPOSE	1
II. PROCUREMENT PLAN PRODUCT DEFINITIONS.....	3
III. PROCUREMENT PROCESS AND SCHEDULE.....	11
IV. DEFAULT SERVICE SUPPLIER MASTER AGREEMENT.....	19
V. ALTERNATIVE ENERGY PORTFOLIO STANDARDS ACT REQUIREMENTS.....	23
VI. CONTINGENCY PLANS.....	30

1 **DIRECT TESTIMONY**
2 **OF**
3 **ROBERT B. REEPING**
4

5 **I. INTRODUCTION AND PURPOSE**

6 **Q. Please state your name and business address.**

7 A. My name is Robert B. Reeping. My business address is 800 Cabin Hill Drive,
8 Greensburg, Pennsylvania 15601.

9 **Q. By whom are you employed and in what capacity?**

10 A. I am employed by FirstEnergy Service Company as a Manager for the Regulated
11 Commodity Sourcing Department ("RCS"). RCS¹ is primarily responsible for procuring
12 power for all of FirstEnergy Corp.'s ("FirstEnergy") regulated utilities.²

13 **Q. Please describe your educational background and professional experience.**

14 A. I am a graduate of Indiana University of Pennsylvania with a Bachelor of Science degree
15 in Business Administration. I have over twenty-four years of experience in the electric
16 industry and have extensive experience in both physical and financial power supply. My
17 professional experience is more fully detailed in Appendix A.

18 **Q. Please describe your responsibilities as Manager, RCS.**

19 A. I am primarily responsible for the procurement and management of the regulated energy
20 supply and renewable energy portfolio that FirstEnergy's electric utilities are required to

¹ RCS is independent of, and separate from, FirstEnergy Corp.'s ("FirstEnergy") unregulated power supply subsidiary, FirstEnergy Solutions ("FES").

² Jersey Central Power & Light Company, Metropolitan Edison Company ("Met-Ed"), Monongahela Power Company, Ohio Edison Company, Pennsylvania Electric Company ("Penelec"), Pennsylvania Power Company ("Penn Power"), The Potomac Edison Company, The Cleveland Electric Illuminating Company, Toledo Edison Company and West Penn Power Company ("West Penn").

1 maintain as load serving entities (“LSEs”) to serve their Pennsylvania, West Virginia, and
2 Maryland retail electric customers. I have either directed or participated in over fifty
3 competitive power and renewable energy credit procurements in Pennsylvania, Maryland,
4 Ohio, New Jersey and Virginia utilizing both auction and request for proposal (“RFP”)
5 formats. As a result, I am very familiar with the attributes of these procurement
6 processes, which are tailored for the specific markets in which the solicitations are
7 conducted. One of the primary functions of RCS is to provide oversight in the
8 implementation of these power procurement processes, including, but not limited to,
9 supporting the procurement plans of the FirstEnergy utilities in regulatory proceedings;
10 developing both solicitation and contract materials; interacting with independent
11 evaluators; executing contracts; and handling many of the operational aspects of these
12 solicitations requiring interface with regional transmission organizations such as PJM
13 Interconnection, L.L.C. (“PJM”).

14 **Q. Have you previously testified in regulatory proceedings?**

15 A. Yes. I have previously testified before the Pennsylvania Public Utility Commission
16 (“Commission”), state regulatory commissions in Maryland, Virginia, West Virginia and
17 Ohio, and before the Federal Energy Regulatory Commission (“FERC”).

18 **Q. On whose behalf are you testifying in this proceeding?**

19 A. I am testifying on behalf of Met-Ed, Penelec, Penn Power and West Penn (each of which
20 may be referred to as a "Company" and, in any combination, as the "Companies").

21

1 **Q. Please describe the purpose of your testimony.**

2 A. The purpose of my testimony is to describe: (i) the proposed products to be procured
3 under each Company's Default Service Program ("DSP") for the period June 1, 2017
4 through May 31, 2019; (ii) the proposed procurement process and schedule of the
5 multiple procurements by the Companies; (iii) the proposed supplier master agreement
6 for execution between the Companies and winning suppliers; (iv) compliance with
7 Pennsylvania's Alternative Energy Portfolio Standards Act ("AEPS" or the "AEPS Act");
8 and (v) the Companies' contingency plans in the event of default service supplier default
9 or unfilled solicitations due to lack of bids or the Commission's rejection of bids.

10 **Q. Have you prepared any exhibits to accompany your testimony?**

11 A. Yes. Met-Ed/Penelec/Penn Power/West Penn Exhibits RBR-1, RBR-2, RBR-3, RBR-4
12 and RBR-5 were prepared by me or under my supervision and are described in detail later
13 in my testimony.

14 **II. PROCUREMENT PLAN PRODUCT DEFINITIONS**

15 **Q. Please provide an overview of the Companies' DSPs.**

16 A. The term of the Companies' DSPs will be for the twenty-four months spanning June 1,
17 2017 through May 31, 2019. The proposed DSPs will procure the required power supply
18 in the wholesale marketplace, by Company and rate class, through multiple solicitations.
19 Power to serve the loads of each of the Companies will be procured in tranches of
20 approximately 50 MW each for the residential and commercial rate classes and in
21 tranches of approximately 100 MW each for the industrial rate class.

1 The DSPs are designed to offer non-shopping customers power through a prudent mix of
2 spot-priced products for industrial customers and a blend of fixed-price 12 and 24-month
3 products for residential and commercial customers. Default service suppliers who are
4 successful bidders in the competitive procurement process will be responsible for
5 satisfying the AEPS Act requirements, with the exception of 100% of the solar
6 requirements for Met-Ed, Penelec and Penn Power which the Companies will continue to
7 procure through market-based purchases.³

8 **Q. What are the benefits of the DSPs?**

9 A. Under the DSPs, customers will be served by products reflecting market-based generation
10 rates, which will provide opportunities for electric generation suppliers ("EGSs") to offer
11 competitive alternatives in accordance with the provisions of the Electricity Generation
12 Customer Choice and Competition Act and the Commission's default service regulations.
13 The DSPs will continue to offer fixed generation rates that change on a quarterly basis,
14 and will be synchronized with the PJM energy year beginning June 1st for residential and
15 commercial customers and continue to make hourly pricing available to industrial
16 customers. The DSPs will enable the Companies to procure their generation supplies
17 through multiple solicitations, providing price diversity to the DSP rates while protecting
18 residential and commercial customers from short-term price variations due to anomalies
19 in the marketplace for generation supply. The 24-month term product will provide
20 assured, stable pricing for fixed-price customers while the 12-month product will refresh
21 the default service rate to make it more reflective of current market trends over the term

³ As discussed later in my testimony, a limited number of Tier I alternative energy credits ("AECs") and solar photovoltaic AECs ("SPAECs") will be assigned to West Penn's default service suppliers as a result of existing, long-term purchases by West Penn.

1 of the DSPs. At the same time, the 12-month products will reduce residential and
2 commercial customers' exposure to significant price volatility associated with shorter
3 term products (e.g., spot and 3-month) due to short-term market anomalies as
4 experienced during the 2014 Polar Vortex and the 2015 Siberian Express. The DSPs also
5 provide bidding flexibility in that the Companies will simultaneously procure their
6 generation supplies, a feature which is expected to increase the number of bidders and,
7 thereby, the competitiveness of the procurement process. In total, the Companies' DSPs
8 are designed to yield market-reflective rates through a prudent mix of products acquired
9 at the least cost over time.

10 **Q. What is the nature of the products the Companies seek to obtain under the DSPs?**

11 A. The proposed products are full-requirements, load-following energy and energy-related
12 services for the customers of Met-Ed, Penelec, Penn Power and West Penn who have not
13 chosen an EGS or whose EGS fails to provide service. Each Company's non-shopping
14 load will be segregated into customer classes, each with its own product specifications.
15 The load of each class will be divided into tranches, with each tranche representing a
16 fixed percentage of the Company's non-shopping load. Procurement winners will be
17 responsible for fulfilling all obligations of a PJM LSE and, as such, will be required to
18 provide energy, capacity, and transmission service, as well as all PJM administrative
19 expenses and any other services or fees as required by PJM of an LSE, with some limited
20 exceptions. Specifically, winning bidders will not be responsible for the following
21 charges: Regional Transmission Expansion Plan charges ("RTEP"); Expansion Cost
22 Recovery Charges ("ECRC"); Reliability Must Run/generation deactivation charges
23 ("RMR") associated with generating plants for which specific RMR charges begin after

1 July 24, 2014; historical out of market tie line, generation and retail customer meter
2 adjustments; and unaccounted for energy (“UFE”) (collectively referred to as “non-
3 market based charges,” or “NMB charges”).

4 Default service suppliers in the Met-Ed, Penelec and Penn Power service territories will
5 also be responsible for meeting 100% of the non-solar Tier I and Tier II AEPS Act
6 requirements. Met-Ed, Penelec and Penn Power will procure all necessary solar
7 photovoltaic requirements on behalf of both default service suppliers and EGSs that serve
8 load in their respective service areas. In the West Penn service territory, default service
9 suppliers will be responsible for all Tier I and Tier II AEPS Act requirements (including
10 solar photovoltaic requirements) less any Tier I AECs or SPAECs that are allocated to the
11 default service suppliers from existing long-term purchases made by West Penn.

12 Consistent with Commission Orders and existing practice, the NMB charges will be paid
13 by the Companies on behalf of all customers and recovered from all customers through
14 the Default Service Support (“DSS”) Rider in the respective Company tariff. Ms. Bortz
15 discusses these costs and their proposed recovery in Met-Ed/Penelec/Penn Power/West
16 Penn Statement No. 3.

17 **Q. What are the customer classes being proposed by the Companies?**

18 A. The Companies propose to segregate load into the same three classes that they have
19 traditionally used for default service purposes: a residential class, a commercial class and
20 an industrial class. Ms. Bortz discusses the customer classes and changes in rate
21 schedules in Met-Ed/Penelec/Penn Power/West Penn Statement No. 3.

1 **Q. How many and what size customer class tranches are being proposed by the**
2 **Companies?**

3 A. The Companies propose to bid out a total of 72 residential class tranches of
4 approximately 50 megawatts ("MW") each; a total of 50 commercial class tranches of
5 approximately 50 MW each; and 33 tranches of approximately 100 MW each of an
6 hourly pricing service for their industrial customers.

7 **Q. You mentioned that the Companies will hold simultaneous procurement processes.**
8 **Will residential, commercial and industrial class products be offered simultaneously**
9 **using the same type of procurement process as well?**

10 A. Yes. There will be procurement processes for the Companies' fixed-price residential and
11 commercial products and the hourly-priced service for industrial customers that occur on
12 the same day, each using a descending-price clock auction process run by CRA
13 International, Inc. d/b/a Charles River Associates ("CRA"), the independent auction
14 manager (i.e., independent evaluator) that has also been used by the Companies under
15 their most recent DSPs.

16 **Q. What are the residential class products proposed by the Companies?**

17 A. Each residential class tranche is a fixed-price, load-following full requirements product,
18 with either a 12-month or 24-month term. All required residential tranches will be
19 secured over six procurement dates.

20

1 **Q. What are the commercial class products proposed by the Companies?**

2 A. The commercial class product will be the same as the residential class product: a fixed-
3 price, load-following full requirements product, with either a 12-month or 24-month
4 term, and with all tranches secured over six procurement dates.

5 **Q. What are the industrial class products proposed by the Companies?**

6 A. The Companies are not proposing any changes to the products offered to their industrial
7 classes under today's programs. That is, the Companies propose to continue to secure
8 power supply for the industrial class utilizing a service referred to as the hourly pricing
9 service ("HPS"). Contracts for HPS will be for 12-month terms beginning June 1 in both
10 2017 and 2018. The HPS is not a fixed-price service, but a variable hourly service that is
11 priced to the PJM real-time hourly energy market for each Company's PJM delivery
12 zone. Default service suppliers will be bidding for the right to serve a portion of a
13 Company's HPS load – for a total of 33 tranches across all the Companies. Customers on
14 HPS will pay, and winning default service suppliers will receive: 1) the winning price
15 bid by the winning default service supplier in the hourly-priced auction; 2) the applicable
16 PJM zonal real-time hourly locational marginal price ("LMP"); and 3) a fixed adder of
17 \$4/MWh. This additional adder is intended to capture an estimate of costs of other
18 supply components associated with meeting this full-requirements obligation, including
19 capacity, ancillary services, Network Integration Transmission Service ("NITS"), AEPS
20 compliance, and other costs.

21

1 **Q. Do you believe the residential and commercial class fixed 12 and 24-month tranche**
2 **products paired with the Companies' proposed continuation of industrial HPS**
3 **service are consistent with Act 129 of 2008 and the Commission's default service**
4 **regulations and policy statement?**

5 A. Yes. The proposed product mix, along with previously procured long-term alternative
6 energy portfolio standard credit agreements, meets the current legislative standard under
7 Act 129 and the Commission's default service regulations and policy statement, which
8 require a default service procurement plan to include a prudent mix of spot market
9 purchases, short-term contracts and long-term purchase contracts, informed by recent
10 activity in the wholesale and retail markets, that provides adequate and reliable service
11 and is designed to ensure least cost to customers over time. 66 Pa.C.S. § 2807(e)(3.2); 52
12 Pa. Code § 54.186; 52 Pa. Code § 69.1805. This is supported by the fact that the
13 Commission, in approving the Companies' current DSPs, previously approved a
14 similar product mix.

15 **Q. Please describe the general obligations of default service suppliers with respect to**
16 **PJM requirements.**

17 A. Winning default service suppliers will schedule delivery to the applicable PJM zone of
18 the Company which they have bid successfully to supply. It is mandatory that winning
19 default service suppliers be members of PJM and be cognizant of and compliant with all
20 regulations, business rules, scheduling protocols and all other aspects of doing business
21 within PJM. All operational supply risk to perform under this procurement process will
22 be borne by the winning default service suppliers.

23

1 **Q. Are the Companies proposing any modifications to the procurement process?**

2 A. Yes. The Companies propose to increase the load cap percentages under the proposed
3 DSPs over those in place as part of their current DSPs.

4 **Q. What is a load cap?**

5 A. Load caps are a restriction on the amount of supply any one bidder can win in an auction.
6 Load caps, which have the potential to attract additional bidders, especially to a novice
7 procurement process, are generally used in competitive solicitations to encourage
8 supplier diversity and mitigate the impact of a supplier default on retail customers.

9 **Q. What is the load cap as set under the Companies' current DSPs?**

10 A. The Companies' current DSPs call for a 50% load cap.

11 **Q. What percentage are the Companies proposing to increase the load cap to?**

12 A. The Companies propose increasing the load cap to 75%.

13 **Q. What is the basis for the Companies' proposal to increase the load cap?**

14 A. The level at which the load cap is set must balance supplier diversity with setting
15 conditions conducive to achievement of the lowest price in the supply auctions. All other
16 factors being equal, supplier diversity can mitigate the impact on customers of a
17 supplier's default. However, a load cap can also limit the amount of default generation
18 supply that the lowest cost bidder can provide, which can increase the total average cost
19 to serve default load.

20

1 **Q. Are the Companies worried this change will impact supplier diversity of the DSPs?**

2 A. No. The Companies' DSPs are mature. As such, competition under the current DSPs'
3 auctions has been vigorous, with up to 13 bidders participating on any given procurement
4 date, and the percentage of bidders winning load as compared to the total who submitted
5 bids in each solicitation running from 60% to 80%. Given this demonstrated diversity
6 rate, supplier participation has become less of a concern for the Companies over time
7 than would be under a less established process.

8 **Q. Have the Companies experienced a default by any of their default service suppliers?**

9 A. No. The Companies have not experienced a default by any of their default service
10 suppliers since the inception of their default service programs. While a default remains a
11 possibility and should be planned for, the Companies believe the likelihood of a default is
12 very low.

13 **Q. How does the Companies' proposed load cap compare to other utility service
14 territories in Pennsylvania and other neighboring jurisdictions?**

15 A. The Companies' proposed load cap is in the middle of the comparison stack. Load caps
16 are currently not imposed at all in Maryland, Delaware and the District of Columbia.
17 Further, 75% is a slightly lower cap than the current 80% cap applied in Ohio.

18 **III. PROCUREMENT PROCESS AND SCHEDULE**

19 **Q. What are the procurement dates and terms proposed by the Companies?**

20 A. The Companies are proposing a procurement plan for all customer classes using six
21 separate procurement dates. As shown in Exhibit RBR-1, the Companies propose

1 procurements occurring in October 2016 and 2017, January 2017 and 2018, and April
2 2017 and 2018.

3 For the residential and commercial class products, the Companies' initial auctions in
4 October 2016, January 2017 and April 2017 in aggregate will procure the 12 and 24-
5 month agreements for delivery starting June 1, 2017. The subsequent auctions held in
6 October 2017, January 2018 and April 2018 will be for the procurement of the remaining
7 12-month agreements for the second 12-month term starting June 1, 2018. Exhibit RBR-
8 1 provides a detailed breakdown of the proposed procurements by product.

9 The total industrial class load will be procured through two separate auctions to be held
10 in January 2017 and January 2018 for 12-month agreement terms.

11 **Q. What auction design will be used for the default service auctions?**

12 A. The Companies propose to continue their current approach of using a version of the
13 simultaneous, multiple-round, descending-price clock auction format to procure default
14 service supplies. This auction platform is commonly used for multiple commodity types
15 and has been successfully used in numerous electricity procurements in Pennsylvania and
16 across various states since the late 1990s.

17 The bidding format is simultaneous in that multiple products and/or multiple tranches are
18 bid on simultaneously. Bidding takes place online using web-based software in a series
19 of bidding rounds, with pre-specified starting and ending times for each round. Prior to
20 the start of each round, the announced price for each product is disclosed to bidders. The
21 announced price is the same for each tranche for a product, but may differ across
22 products. The announced round 1 starting price for each product is set sufficiently high

1 enough so as to encourage bidder participation. At the end of each round, the bidding
2 software (with oversight of CRA) determines which products are over-subscribed and
3 which products are under-subscribed. A product is over-subscribed if suppliers bid to
4 supply more tranches than the number of tranches needed of that product. Likewise, a
5 product is under-subscribed if fewer tranches were bid on it than needed. If a product is
6 over-subscribed, the announced price for that product will be reduced by a decrement for
7 the next round. If a product is not over-subscribed, its announced price will not change
8 for the next round. The bidding process continues in this manner, with prices tending to
9 tick down like a countdown clock. As prices change across the products, bidders are
10 allowed to change the number of tranches they bid, subject to certain restrictions. Subject
11 to these restrictions, in each round, a bidder simply specifies the number of tranches that
12 it is willing and able to supply for each product at the announced price for each product.
13 There is no pre-determined number of rounds before the auction closes. The auction
14 closes after the first round in which no product is over-subscribed. The clearing price for
15 a product is the lowest price at which the product is not under-subscribed. Winning
16 tranches for the product are tranches that were bid at a price no higher than the clearing
17 price. Winning bidders are those bidders who bid the winning tranches.

18 The Bidding Rules and appendices for the default service procurement auctions are
19 attached as Exhibit RBR-2 and provide a more detailed description of the bidding
20 process.

21 **Q. How are prospective bidders qualified for participation in the DSP auctions?**

22 A. Prospective bidders will be required to satisfy financial and non-financial requirements
23 through a two-part application process designed to demonstrate their ability and

1 commitment to meet the requirements of participation in the auction process and the
2 requirements of being a default service supplier. The Part 1 Application and Part 2
3 Application forms, as well as pre-bid credit documents, are attached as Appendices 1
4 through 3 to Exhibit RBR-2 and will be available through the CRA web-based data room.
5 If a prospective bidder is interested in participating in both the fixed-price residential and
6 commercial auction and the hourly-priced auction for industrial customers, it will need to
7 complete and submit only one Part 1 Application and, subsequent to that, only one Part 2
8 Application. As much as possible, the application process will be conducted
9 electronically via the CRA web-based data room using protocols CRA has used
10 successfully in other similar auction processes including the current DSPs. The CRA
11 process is designed to be secure and to make it easier and less time consuming for
12 applicants to submit application materials. The process further provides: (i) for the
13 review and assessment of the applications; (ii) timely feedback to applicants; (iii) the
14 ability of applicants to easily check on the status of their applications; and (iv) the ability
15 of applicants to cure any deficiencies.

16 **Q. Are the bid rules reflected in Met-Ed/Penelec/Penn Power/West Penn Exhibit RBR-**
17 **2 and the associated Appendices consistent with those that are being used by the**
18 **Companies in their current DSPs for the June 1, 2015 - May 31, 2017 term?**

19 A. Yes. The bid rules and associated Appendices are consistent between the proposed DSPs
20 and the current DSPs, with mostly minor updates to dates and addresses. In particular,
21 the Part 1 Application and Part 2 Application processes to qualify and register bidders,
22 the web-based data room, the frequently asked question process, the communications

1 protocol, the bidding format and the post-auction process will all be the same as under the
2 Companies' current DSPs.

3 The Companies have, however, added provisions for the prescribed treatment of
4 associated bidders. This new section of the Bidding Rules outlines the specific protocols
5 that will be followed when two or more associated entities submit Part 1 and/or Part 2
6 applications to participate in an auction for the Companies, and specifies potential
7 remedies that are available to the Independent Evaluator, the Companies, and the
8 Commission in such cases.

9 **Q. What are associated bidders and what are the issues that may arise from such**
10 **bidders participating in an auction?**

11 A. If a qualified bidder is associated with another qualified bidder, the associated
12 relationship could allow them to act in concert, or could prevent them from actively
13 competing against each other as they otherwise would if the relationship did not exist. In
14 such cases, the competitiveness of the auction and the ability of the auction to produce
15 competitive prices may be harmed by the unintended or intended coordinated or collusive
16 behavior that associations among bidders may facilitate.

17 **Q. Briefly describe the protocols related to bidder associations proposed as additions to**
18 **the existing Bidding Rules.**

19 A. In some cases, potential associations among applicants may become apparent after the
20 Part 1 Applications are submitted. In other cases, the potential relationship among
21 qualified bidders will not be known to the Independent Evaluator until the qualified
22 bidders submit final certifications along with their Part 2 applications. In both cases,

1 upon receipt of complete applications (either Part 1 or Part 2), the Independent Evaluator
2 will initiate a request for additional information regarding the relationship among the
3 potentially associated parties, the structure of their organization, and the independence of
4 the respective bidding teams. Concurrently, the Independent Evaluator will notify
5 representatives of the Companies and Commission Staff that there is a potential
6 association among applicants.

7 After the Independent Evaluator has received additional information from each associated
8 bidder, the Independent Evaluator will work with representatives of the Companies and
9 Commission Staff to determine:

- 10 a) Whether each of the associated bidders will be allowed to participate
11 independently in the auction(s); and, if so,
12 b) Any restrictions on indicative offers and/or pre-bid security or collateral
13 requirements that may be applied as a result of the participation by associated
14 bidders.

15 **Q. When will the Companies and the independent evaluator hold information sessions**
16 **for interested participants?**

17 A. A bidder information session will be held generally at least a month before each auction.
18 The purpose of these sessions will be to describe the bid rules, the two-part qualification
19 process, the Supplier Master Agreement, and the procurement information website and its
20 contents, as well as other pertinent information bidders will need to evaluate this
21 procurement opportunity.

22

1 **Q. How can prospective default service suppliers learn more about the load**
2 **characteristics of the Companies' default service products?**

3 A. Prospective default service suppliers will have access to the web-based data room
4 administered by CRA as part of the auction information website which will be
5 operational prior to the start of the procurement process. The data room will include
6 hourly historical load characteristics of each product and the most current customer
7 shopping statistics by customer class by Company. This will afford prospective default
8 service suppliers an opportunity to view product load volatility through time to help
9 gauge volume risk. Furthermore, participants will have the opportunity to ask questions
10 about any of the default service products in the procurement process at an information
11 session or via a frequently asked question feature via the CRA web-based data room.

12 **Q. Please describe the process following the close of the default service auctions.**

13 A. After the last round of the auction, bidders who remained active in the auction will see
14 preliminary auction results on the bidding website. The bidders will see the clearing
15 price for each product and the number of tranches the bidder tentatively won for each
16 product. CRA will also provide to the Companies the identities of the winning bidders,
17 the number of tranches each winning bidder has won for each product, and the associated
18 clearing prices, which results are subject to Commission approval.

19 After the close of the auction, CRA will provide a report to the Commission that will
20 include, among other things, the list of winning bidders and the clearing price for each
21 product. The Commission will have one business day after receiving the CRA auction
22 report to approve the results of the auction.

1 Upon approval by the Commission, the winning bidders and the Companies will execute
2 a Supplier Master Agreement (“SMA”), the form of which is attached as Exhibit RBR-3.
3 Pre-bid security will be returned to all bidders upon execution of the SMA on or before
4 the third business day after the Commission has rendered its decision on the auction
5 results. Pre-bid security may be held for any bidder that violated any of the rules or
6 certifications of the auction process.

7 **Q. Do you believe that the use of a descending-price clock auction is the appropriate**
8 **auction design for the default service auctions?**

9 A. Yes. As previously mentioned, the Companies' proposed descending-price clock auction
10 process is identical to the auction process used under the Companies' current DSPs as
11 well as similar to auction processes used in other jurisdictions to successfully procure
12 electric power service. It is a process that default service suppliers and other stakeholders
13 accept and are experienced with. Further, its design encourages participation because it
14 is fair, open, transparent, and non-discriminatory, and provides low barriers to
15 participation for a variety of prospective bidders. The tranche sizes and the range of
16 contract durations appeal to various bidders because they are consistent with products
17 available in energy markets. With the simultaneous bidding on products that are related
18 in value (the residential and commercial products across the Companies, and the
19 industrial products across the Companies), bidders are able to switch their bid quantities
20 across the Companies' products and bid simultaneously on substitutable and/or
21 complementary products in response to changes in pricing. Because these factors
22 encourage active participation and allow participants to bid efficiently, the auctions will
23 yield competitive outcomes.

1 **Q. Will the Companies' unregulated generation supply affiliate be permitted to bid in**
2 **the competitive procurements?**

3 A. Yes. In the supply plans that the Commission previously approved for Met-Ed, Penelec,
4 Penn Power, and West Penn,⁴ the Companies' unregulated generation supply affiliate,
5 FES, was expressly permitted to participate in the competitive procurements. Similarly,
6 the DSPs proposed in this case would permit FES to participate in the competitive
7 procurements. Additionally, as the Commission's default service regulations require, the
8 Companies have retained CRA as the independent evaluator to manage the procurement
9 process and evaluate the bids in order to eliminate any possibility of inappropriate
10 "self-dealing" or bias. FES's participation, with appropriate safeguards and transparency,
11 will enhance the competitive environment and help ensure that vigorous competition will
12 yield competitive outcomes for the products being procured.

13 **IV. DEFAULT SERVICE SUPPLIER MASTER AGREEMENT**

14 **Q. What is the default service SMA?**

15 A. The default service SMA is the agreement executed by each Company and each
16 successful bidder that governs specific duties, rights and obligations in connection with
17 the sale and purchase of default service supply to serve the Companies' retail default
18 service customers.

⁴ See Docket Nos. P-2013-2391368 (Met-Ed), P-2013-2391372 (Penelec), P-2013-2391375 (Penn Power), and P-2013-2391378 (West Penn) (Order entered July 24, 2014); P-2011-2273650 (Met-Ed), P-2011-2273668 (Penelec), P-2011-2273669 (Penn Power), and P-2011-2273670 (West Penn) (Order entered August 16, 2012); Docket Nos. P-2009-2093053 and P-2009-2093054 (Met-Ed and Penelec) (Order entered November 6, 2009); Docket No. P-2010-21576862 (Penn Power) (Order entered October 21, 2010).

1 **Q. How was the Companies' proposed form SMA developed?**

2 A. In its Order entered on February 15, 2013 in *Investigation of Pennsylvania's Retail*
3 *Electricity Market: End State of Default Service* at Docket No. I-2011-2237952, , the
4 Commission directed its Office of Competitive Market Oversight ("OCMO") to create a
5 procurement collaboration working group, which was tasked with formulating, among
6 other things, a uniform SMA. The Companies participated actively in the working
7 group's development of the uniform SMA to be used on a statewide basis. The resulting
8 OCMO collaborative SMA, with minor modifications, was adopted by the Companies
9 and is currently in use under the Companies' current DSPs. The Companies are
10 proposing a similar form SMA for use under the proposed DSPs, subject to minor
11 modifications as discussed below. The proposed form SMA is attached as Exhibit RBR-
12 3.

13 **Q. Does each Company propose to have a unique SMA?**

14 A. No. All the Companies will use the uniform SMA template. However, they will adjust
15 the SMA Appendices to their individual needs based on the product mix, pricing, and
16 other terms specific to each Company and each customer class.

17 **Q. How are suppliers to be paid under the proposed form SMA?**

18 A. It depends largely upon the class being served. For residential and commercial products,
19 default service suppliers will be paid a fixed price. The fixed price, in dollars per
20 megawatt-hour ("MWh"), will be for 100% of the delivered supply each hour, will be
21 established through the Companies' competitive procurement process, and will be
22 included in Exhibit 1 to the SMAs when known. The fixed price will cover all cost
23 components associated with meeting the full-requirements default service supply

1 including capacity, ancillary services, NITS, AEPS compliance, and all PJM
2 administrative expenses and any other services or fees as required by PJM of an LSE, but
3 will exclude the NMB charges as previously discussed herein.

4 For industrial products, default service suppliers will be paid a variable price for each
5 hour during the applicable period equal to the delivered supply multiplied by the sum of
6 the real-time hourly LMP for the applicable PJM delivery point, the winning price for the
7 winning default service suppliers in the hourly-priced auction, and an additional \$4/MWh
8 to capture an estimate of costs of other supply components associated with meeting this
9 full-requirements obligation, including capacity, ancillary services, NITS, AEPS
10 compliance, and all PJM administrative expenses and any other services or fees as
11 required by PJM of an LSE, but excluding the NMB charges.

12 **Q. Will payment to a supplier for default service load for Residential and Commercial**
13 **customers vary seasonally?**

14 A. No. Residential and commercial SMAs will no longer contain provisions that adjust the
15 price paid to default service suppliers for each MWh of load by a seasonal billing factor,
16 representing anticipated seasonal differences in energy prices. Because non-summer
17 month volatility has been much more pronounced in recent years, there is no longer a
18 need to “summer-weight” prices paid to suppliers. By example, the seasonal billing
19 factor under the Companies’ current DSPs is currently 1.0 meaning there is no summer
20 weighting. As was the case in prior DSPs, the seasonal billing factors do not apply to the
21 industrial SMAs because the price paid for energy under the industrial product is based
22 upon a real-time, hourly LMP.

1 **Q. Please describe how the proposed uniform SMA compares to those currently used**
2 **by the Companies.**

3 A. The proposed form SMA that will be used by the Companies contains the following
4 limited, yet key modifications:

5 (1) For residential/commercial products, there will no longer be a spot component to
6 the product mix and, therefore, there will be only a fixed component for these
7 products for the forthcoming default service period; and

8 (2) As explained above, the Companies will no longer employ seasonal factors for
9 residential and commercial prices.

10 **Q. Please explain how the credit requirements work in the uniform SMA.**

11 A. An unsecured credit matrix was developed to allow each Pennsylvania utility to have a
12 tailored unsecured credit table based on its own credit policy. A supplier's credit
13 exposure ("Total Exposure Amount") is based upon a fixed amount corresponding to the
14 total default service load the supplier is obligated to serve. The maximum unsecured
15 credit will be based on Appendix A of the uniform SMA and will be determined as the
16 lesser of the percentage of tangible net worth ("TNW")⁵ or the Credit Limit Cap. The
17 credit matrix will define the maximum amounts to be used for these metrics based on the
18 default service supplier's average credit ratings by Standard & Poor's Rating Service,
19 Moody's Investor Service, Inc., and/or Fitch Investor Service, Inc.

20 If a default service supplier's Total Exposure Amount exceeds the default service
21 supplier's maximum unsecured credit limit, the default service supplier will have to

⁵ TNW is defined as total assets less intangible assets and total liabilities.

1 furnish either cash or an acceptable letter of credit equal to the excess amount. The
2 standard form for the letter of credit is provided in Appendix F of the uniform SMA.

3 **Q. Will bidders be permitted to propose modifications to the SMA once approved?**

4 A. No. The Companies intend to treat all bidders uniformly, which requires that each bidder
5 have the same rights and obligations under the SMA. Moreover, a standardized contract
6 permits bidders to be selected on the sole criterion of price. The uniform SMA proposed
7 by the Companies contains provisions that were developed as part of the working group
8 process and are already well-understood by bidders. Additionally, the OCMO working
9 group that developed the uniform SMA provided ample opportunity for input from the
10 wholesale supplier community during the development process.

11 **V. ALTERNATIVE ENERGY PORTFOLIO STANDARDS ACT REQUIREMENTS**

12 **Q. What are the AEPS Act requirements for the Companies?**

13 A. The AEPS Act requires the Companies and other electric distribution companies
14 (“EDCs”), as well as EGSs, to derive an increasing percentage of electricity sold to
15 Pennsylvania retail customers from certain alternative energy sources, such as wind,
16 solar energy and biomass. Compliance is measured through alternative energy credits or
17 “AECs,” which are equal to one megawatt-hour of energy from approved “Tier I” or
18 “Tier II” alternative energy sources. The AEPS Act also includes a solar “set-aside,”
19 which mandates that a specific portion of the Companies’ Tier I requirements be satisfied
20 through AECs derived from solar photovoltaic energy. The AEPS Act defines Tier I and
21 Tier II alternative energy sources and the dates and percentages of supply required for

1 compliance.⁶ The Tier I, Tier II and solar photovoltaic alternative energy percentage
2 requirements during the proposed DSPs are more fully described in Exhibit RBR-4.

3 **Q. Are winning default service suppliers responsible for all of the AEPS Act**
4 **requirements described in Exhibit RBR-4?**

5 A. Default service suppliers in the Met-Ed, Penelec and Penn Power service territories will
6 be responsible for meeting 100% of the non-solar Tier I and Tier II AEPS Act
7 requirements. Met-Ed, Penelec and Penn Power will procure all necessary solar
8 photovoltaic requirements on behalf of default service suppliers and EGSs that serve load
9 in their respective service areas. In the West Penn service territory, default service
10 suppliers will be responsible for all Tier I and Tier II AEPS Act requirements (including
11 solar photovoltaic requirements) less any Tier I AECs or SPAECs that are allocated to the
12 default service suppliers from existing long-term purchases made by West Penn.

13 **Q. How will the 100% of Solar Photovoltaic AEPS Act requirements described in**
14 **Exhibit RBR-4 be met for Met-Ed, Penelec and Penn Power?**

15 A. Consistent with the Commission's Final Order approving their current DSPs, Met-Ed,
16 Penelec and Penn Power will procure SPAECs for 100% of their shopping and non-
17 shopping load. Those Companies will conduct one RFP for SPAECs in November 2017
18 to procure the estimated additional SPAEC requirements for the new DSP term beginning
19 June 1, 2017, after adjusting for the SPAECs already purchased through the 10-year
20 SPAEC RFPs conducted under previously approved DSPs. The estimated volumes under
21 the RFP will be determined based upon the most recent load forecast for the Companies
22 at the time of the RFP. At the end of the 2017/2018 or 2018/2019 AEPS compliance

⁶ 73 P.S. §§ 1648.2 and 1648.3.

1 period, if necessary for compliance purposes, the Companies will conduct short-term
2 SPAEC procurements at market prices.⁷ Copies of the Companies' SPAEC Request for
3 Proposals Rules, SPAEC Purchase and Sale Agreement ("SPAECPSA") and additional
4 applicable RFP documentation are attached as Exhibit RBR-5. As is the case with the
5 procurement documents discussed from Exhibit RBR-2, the bid rules, SPAECPSA and
6 additional documentation found in Exhibit RBR-5 are consistent between the proposed
7 DSPs and the current DSPs.

8 **Q. You mentioned that West Penn default service suppliers are responsible for all**
9 **AEPS Act requirements less any Tier I AECs or SPAECs that are allocated to the**
10 **suppliers from existing long-term purchases made by West Penn. Please explain.**

11 A. Consistent with the Commission's Final Order approving West Penn's current default
12 service plan at Docket P-2013-2391378, West Penn will continue to require each default
13 service supplier to provide Tier I AECs and SPAECs associated with the load served by
14 the default service supplier. However, Tier I AECs and SPAECs that West Penn
15 procured under existing long-term contracts previously approved by the Commission will
16 be used to reduce the number of Tier I AECs and SPAECs that those default service
17 suppliers would otherwise be obligated to transfer to West Penn under the SMAs. These
18 Tier I AECs and SPAECs will be allocated on a pro rata basis in accordance with the
19 percentage of default service load served by default service suppliers, and default service
20 suppliers will be informed through the frequently asked question feature of the exact
21 amount of Tier I AECs and SPAECs that will be allocated in each procurement of default

⁷ In the event the Companies hold excess SPAECs at the end of a compliance period, the excess SPAECs will be banked for future compliance periods unless such SPAECs are set to expire at the end of the current compliance period. In that instance, the expiring SPAECs will be sold and revenues collected from such sales will be credited back through the Solar Photovoltaic Requirements Charge Rider.

1 service supply so that the reduction in Tier I AEC and SPAEC obligations may be
2 factored into default service supplier bids.

3 **Q. Are winning default service suppliers responsible for any additional Tier I and/or**
4 **Tier II AEPS requirements imposed prior to the effective date of the SMA?**

5 A. Yes. Winning default service suppliers are responsible for additional Tier I and/or Tier II
6 AEPS requirements imposed prior to the execution of the SMA. For example, Act 129
7 provides that “the commission shall at least quarterly increase the percentage share of
8 Tier I alternative energy sources required to be sold by an EDC or electric generation
9 supplier under Section 3(b)(1) of the Alternative Energy Portfolio Standards Act to reflect
10 any new biomass energy or low-impact hydropower resources that qualify as a Tier I
11 alternative energy source under this Section.” 66 Pa.C.S. § 2814(c). Winning default
12 service suppliers will be responsible for compliance with the Tier I percentage increases
13 resulting from that provision of Act 129.

14 **Q. Are winning default service suppliers responsible for any additional AEPS**
15 **requirements resulting from legislative or administrative changes implemented**
16 **following the effective date of the SMA?**

17 A. No. The Companies recognize that having winning default service suppliers bear the risk
18 of additional future legislative or administrative changes to the AEPS requirements
19 following the effective date of an executed SMA may cause these default service
20 suppliers to add an additional risk premium into their bids. To alleviate this uncertainty
21 and the risk premium associated with it, the Companies propose that the Companies
22 themselves be responsible for any incremental AEPS compliance requirements to ensure
23 these additional requirements are met through procurements at market prices. The costs

1 associated with any incremental AEPS compliance requirements and/or potential
2 penalties will be recovered from default service customers through the reconciliation
3 process and added to the weighted average cost of default service supply.

4 **Q. What is the procedure the Companies will use to verify that winning default service
5 suppliers have complied with the AEPS Act?**

6 A. The Companies will continue to only accept AECs from Tier I and Tier II sources
7 approved by the Commission’s AEPS Program Administrator and generated through PJM
8 Environmental Information Services Inc.’s Generation Attributes Tracking System
9 (“GATS”), which the Commission has designated under the AEPS Act as the “registry”
10 for issuance of AECs. It will be incumbent on the winning default service supplier to
11 open and maintain, at its own expense, a GATS account in order to satisfy the AEPS Act
12 requirements. This process is currently and successfully being used for compliance with
13 the AEPS Act requirements by the Companies.

14 **Q. What happens if a portion of the default service supplier-sourced AECS are found
15 by the Commission to be non-compliant with the AEPS Act requirements and a
16 penalty is levied against the Companies?**

17 A. The default service supplier that failed to acquire the necessary AECs during the
18 compliance periods will be identified by the Companies and will be assessed a penalty.⁸
19 Customers will not be at risk for default service supplier non-compliance.

⁸ The default service supplier that failed to acquire the necessary AECs during the compliance periods will be identified by the Companies and will be assessed any alternative compliance payment or other penalty imposed by the Commission for the AEPS non-compliance.

1 **Q. Is the Companies' plan to meet AEPS Act obligations consistent with Act 129 and**
2 **the Commission's default service regulations?**

3 A. Yes. Act 129's requirement that EDCs procure power through a competitive process also
4 applies to the Companies' procurement of SPAECs or AECs to satisfy AEPS Act
5 obligations. 66 Pa.C.S. § 2807(e)(3.5). Further, the Commission's AEPS regulations
6 state that a default service provider "shall demonstrate compliance" with the AEPS
7 regulations and default service regulations "by identifying a competitive procurement
8 process for acquiring alternative energy credits" in its default service plan. 52 Pa. Code §
9 75.67(b). The Companies propose to use competitive processes to fulfill their AEPS
10 obligations through the default service procurement and a separate RFP for SPAECs for
11 Met-Ed, Penelec and Penn Power, consistent with the Companies' current Commission-
12 approved DSPs.

13 **Q. Are the Companies seeking any changes for the procurement of short-term market**
14 **AECs from the currently approved DSPs?**

15 A. Yes. As discussed above, if necessary for compliance purposes, the Companies conduct
16 short-term AEC procurements at market prices to fulfill any shortfalls for compliance.
17 This currently includes bilateral purchases from Commission-approved AEC
18 providers/facilities or transactions conducted through AEC brokers. Under the proposed
19 DSPs, the Companies will continue to address potential shortfalls through market
20 purchases. However, the Companies are seeking approval for the additional ability to
21 make market-priced sales and purchases of excess AECs produced by non-utility
22 generators ("NUGs") which currently sell these AECs as part of their total output to Met-
23 Ed and Penelec under existing Commission-approved NUG contracts.

1 **Q. Why are these AECs not available for use today?**

2 A. Under Docket Nos. P-2009-2093053 (Met-Ed) and P-2009-2093054 (Penelec), Met-Ed
3 and Penelec received approval to sell the output of the NUGs, including all associated
4 AECs, into the PJM-administered markets, the revenues from which would be credited
5 back to customers through the Companies' respective NUG Charge Riders. At the time
6 this approval was granted, sales amongst the Companies' affiliates were not
7 contemplated.

8 **Q. Why are the Companies recommending a change to this approved process?**

9 A. The AECs Met-Ed and Penelec receive from the NUGs qualify as Tier II resources in
10 Pennsylvania. The Pennsylvania Tier II AEC market historically has been and continues
11 to be significantly oversupplied. Thus, the Companies have not been able to sell all Tier
12 II AECs they have received from the NUGs. Meanwhile, the Companies have been
13 forced to separately purchase Tier II AECs from other vendors in order to meet their
14 AEPS Act obligations. The proposed change to the approved process will allow Met-Ed
15 and Penelec to sell more of the Tier II AECs that they cannot otherwise dispose of,
16 thereby creating revenue for the benefit of their retail customers while helping their
17 Pennsylvania affiliate EDCs fulfill their own AEC shortfalls.

18 **Q. What affiliates would be eligible to purchase these excess AECs under the**
19 **Companies' proposal?**

20 A. In the event Met-Ed was in possession of excess credits, those credits could be purchased
21 by any of Penelec, Penn Power or West Penn. Likewise, should Penelec find itself
22 holding excess credits, Met-Ed, Penn Power or West Penn would be eligible buyers, as
23 needed to fill their own shortfalls.

1 **Q. How would the Companies ensure that purchases amongst one another would be**
2 **conducted at market prices?**

3 A. On the date of transaction, market quotes will be obtained from three AEC brokers
4 through their published broker sheets. The offer portion of the quote for the applicable
5 AES product from the three AEC brokers would be averaged to determine a
6 representative market price for the affiliate transaction.

7 **Q. What happens to the money paid for any AECs purchased under this proposal?**

8 A. Monies received by Met-Ed or Penelec would be returned to retail customers through the
9 applicable Non-Utility Generation Charge Rider in the same manner as revenues
10 associated with such AECs are today.

11 **VI. CONTINGENCY PLANS**

12 **Q. What default service supply contingencies do the Companies propose to address in**
13 **their DSPs?**

14 A. While not every contingency can be anticipated, the Companies have identified the
15 following possible scenarios for which contingency plans have been developed:

16 (a) The Companies' competitive solicitations for full requirements load-
17 following tranche products or SPAECs are not fully subscribed due to lack
18 of bids or rejection of bids by the Commission; or

19 (b) A default by any of the winning suppliers prior to the start of the delivery
20 period or at any time during the delivery period.

1 **Q. What is the contingency plan if the Companies' competitive solicitation for full**
2 **requirements, load-following products is not fully subscribed due to lack of bids or**
3 **rejection of bids by the Commission?**

4 A. In the event that a scheduled solicitation is not fully subscribed following the initial
5 proposed procurement due to a lack of bids or due to rejection of bids by the
6 Commission, the Companies will rebid the unfilled tranches from that solicitation in the
7 next scheduled procurement for which there is sufficient calendar time to include the
8 tranches. For any unfilled tranches still remaining, the Companies acting as the LSE will
9 purchase the necessary physical supply through PJM-administered markets. The
10 Companies' procurements will be made at real-time zonal spot market prices, plus other
11 supply costs including capacity, NITS, ancillary services and AEPS Act compliance. The
12 Companies will not enter into hedging transactions to attempt to mitigate the associated
13 price or volume risks to serve these tranches. The Companies will also propose to satisfy
14 AEPS compliance requirements for unfilled tranches at market prices. At the next
15 quarterly rate adjustment, the Companies will include an estimate of these costs in the
16 weighted cost of the default service supply calculation and utilize the reconciliation
17 process to recover from default service customers the difference between the estimated
18 and actual costs that the Companies incur as a result of purchasing the necessary supply
19 and AEPS requirements.

20

1 **Q. What is the contingency plan if a winning bidder of a full service load-following**
2 **tranche product were to default prior to the start of or during the Companies'**
3 **delivery periods?**

4 A. If a winning bidder defaults prior to the start of or during the delivery period, the
5 Companies will offer the unfilled tranches to the other registered bidders who
6 participated in the most recent solicitation. The Companies may enter into an agreement
7 with the registered bidder or bidders offering the best terms for the unfilled tranches
8 resulting from the default, provided the prices offered by such bidder or bidders are
9 consistent with the original prices under which the unfilled tranches were procured
10 adjusted for changes in market conditions from the time when the original tranches were
11 procured. If the Companies are not able to enter into such an agreement and a minimum
12 of thirty calendar days exists prior to the start of the delivery period, the Companies will
13 seek to bid the defaulted tranches in a separate supplemental competitive solicitation. As
14 with other unfilled tranches described above, if insufficient time exists to conduct an
15 additional competitive solicitation, or if the supplemental solicitation is unsuccessful, the
16 Companies will supply the tranches using PJM-administered markets with recovery and
17 reconciliation of estimated and actual costs as described previously.

18 **Q. Please describe the Companies' contingency plan in case the RFP to solicit bids for**
19 **SPAECs is not fully subscribed due to lack of bids or rejection of the bids by the**
20 **Commission, or in the case of a winning SPAEC supplier default before or during**
21 **the delivery period.**

22 A. If any SPAEC tranches remain unfilled due to a lack of bids or rejection of bids by the
23 Commission, or if a winning SPAEC supplier defaults before or during the delivery

1 period, the Companies will conduct short-term procurements at market prices to ensure
2 compliance with all solar photovoltaic AEPS requirements until such time as the
3 Commission approves an alternative mechanism.

4 **Q. Does this conclude your direct testimony?**

5 A. Yes, it does.

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

**METROPOLITAN EDISON COMPANY
Docket No. P-2015-_____**

**PENNSYLVANIA ELECTRIC COMPANY
Docket No. P-2015-_____**

**PENNSYLVANIA POWER COMPANY
Docket No. P-2015-_____**

**WEST PENN POWER COMPANY
Docket No. P-2015-_____**

DEFAULT SERVICE PROGRAMS

**For the Period
June 1, 2017 to May 31, 2019**

**Direct Testimony
of
James D. Reitzes**

List of Topics Addressed

Analysis of Default Service Supply Plans

TABLE OF CONTENTS

	Page
I. INTRODUCTION AND PURPOSE OF TESTIMONY	1
II. THE DESIGN OF THE SUPPLY PLAN FOR DEFAULT SERVICE CUSTOMERS CONFORMS WITH THE REQUIREMENTS OF ACT 129, SUCH THAT IT WILL RESULT IN THE LEAST COST OVER TIME FOR THOSE CUSTOMERS.....	4
III. CONCLUSION	20

1 **DIRECT TESTIMONY**
2 **OF**
3 **JAMES D. REITZES**

4 **I. INTRODUCTION AND PURPOSE OF TESTIMONY**

5 **Q. Please state your name, title, business address, and for whom you are testifying.**

6 A. I am James D. Reitzes, Principal of The Brattle Group (“Brattle”), located at 1850 M
7 Street NW, Washington, District of Columbia. I am testifying on behalf of Metropolitan
8 Edison Company, Pennsylvania Electric Company, Pennsylvania Power Company, and
9 West Penn Power Company (“Met-Ed,” “Penelec,” “Penn Power,” and “West Penn,”
10 respectively, or collectively, the “Companies”).

11 **Q. What is your educational and professional background?**

12 A. I hold a Ph.D. in economics from the University of Wisconsin and a B.A. in economics
13 and history from Stanford University. My areas of specialization within economics are
14 industrial organization, which includes the examination of firm behavior under various
15 market conditions, and international trade. I also have completed field courses in finance.
16 I have been involved in competition and regulatory matters for over twenty-five years,
17 including five years while working at the Federal Trade Commission and more than
18 twenty years in private consulting practice. Appendix A provides further detail as to my
19 professional and educational experience.

20 **Q. Please summarize your prior professional experience with respect to electric power**
21 **matters.**

22 A. For over seventeen years, I have participated in a variety of regulatory and competition
23 matters involving the electric power industry. I have provided testimony to the Federal

1 Energy Regulatory Commission and in state regulatory proceedings addressing such
2 issues as the competitive implications of mergers and acquisitions and assessing whether
3 energy, transmission rights, renewable energy credits, or other assets were purchased or
4 sold at the best possible price. On several occasions, I have been involved in the design
5 of procurement processes to satisfy default service obligations (also known as standard-
6 offer service (“SOS”), Provider of Last Resort (“POLR”), and other names), including
7 the analysis of costs and risks associated with full-requirements auction-based
8 procurements and portfolio procurement strategies. I have submitted testimony on these
9 issues to state public utility commissions, including previously to the Pennsylvania Public
10 Utility Commission (“Commission”).

11 My past experience also includes the design and management of auction and request for
12 proposal (“RFP”) processes to purchase or sell various energy-related products, including
13 energy, transmission rights, renewable energy credits, and other products. This includes
14 participation in a working group that evaluated the design of a full-requirements,
15 descending-clock bidding process to procure power supplies for standard-offer service
16 customers in New Jersey.

17 I have authored several articles concerning price determination and competition in
18 general, as well as in electric power markets specifically, which have been published in
19 economics journals and trade journals for the energy sector.

20

1 **Q. Have you submitted testimony previously to the Commission on behalf of the**
2 **Companies?**

3 A. Yes, I submitted testimony on behalf of Met-Ed and Penelec regarding their Default
4 Service Supply Plans and procurement of Solar Photovoltaic Alternative Energy Credits
5 (“SPAECs”) in Docket Nos. P-2009-2093053 and P-2009-2093054 (“DSPI”). My
6 testimony examined least-cost methods of procuring power for default service customers
7 and purchasing SPAECs for meeting requirements under Pennsylvania’s Alternative
8 Energy Portfolio Standards Act (“AEPS” Act). In addition, I submitted rebuttal
9 testimony on behalf of Penn Power regarding its Interim Default Service Supply Plan in
10 Docket No. P-00072305.

11 More recently, I submitted testimony on behalf of Met-Ed, Penelec, Penn Power, and
12 West Penn in Docket Nos. P-2011-2273650, P-2011-2273668, P-2011-2273669, and
13 P-2011-2273670 (“DSPII”), as well as in Docket Nos. P-2013-2391368, P-2013-
14 2391372, P-2013-2391375, and P-2013-2391378 (“DSPIII”). Among other topics, my
15 testimony again examined least-cost methods of obtaining power for default service
16 customers.

17 **Q. Have you prepared any exhibits to accompany your testimony?**

18 A. Yes.

19 **Q. What is the purpose of your testimony?**

20 A. My testimony analyzes the proposed procurement of full-requirements service for
21 residential, commercial, and industrial default service customers by Met-Ed, Penelec,
22 Penn Power and West Penn, as described in the testimony of Witness Keeping. I explain

1 why the nature of the products being procured, as well as the procurement method itself,
2 will produce the “least cost over time” and satisfy other applicable provisions of
3 Pennsylvania’s Act 129 of October 15, 2008 (“Act 129”). In so doing, I explain why the
4 proposed procurement should be approved by the Commission.

5 **Q. Is Brattle an independent third party?**

6 A. Yes. Brattle is not owned, managed, controlled, or directed by any of the Companies or
7 their affiliates. Brattle has no ownership in or control over the Companies or any of the
8 FirstEnergy Corp. (“FirstEnergy”) affiliates. Neither the Companies nor any other
9 FirstEnergy affiliate has any ownership in or control over Brattle. We have performed
10 consulting work on a contract basis for the Companies and other regulated affiliates of
11 FirstEnergy in the past, but we have not performed work on behalf of any of its
12 unregulated affiliates.

13 **II. THE DESIGN OF THE SUPPLY PLAN FOR DEFAULT SERVICE CUSTOMERS**
14 **CONFORMS WITH THE REQUIREMENTS OF ACT 129, SUCH THAT IT**
15 **WILL RESULT IN THE LEAST COST OVER TIME FOR THOSE CUSTOMERS**

16 **Q. Have you reviewed the description of the Default Service Programs for the**
17 **Companies, provided by Witness Reeping?¹**

18 A. Yes, I have.

19 **Q. Can you provide an overview of the “highlights” of the Default Service Programs?**

20 A. Yes, I can. The Companies propose to acquire full-requirements, load-following
21 generation service for residential and commercial default service customers through
22 descending-clock auctions for the service period beginning June 2017 and ending May

¹ See Met-Ed/Penelec/Penn Power/West Penn Statement No. 1.

1 2019. All default service load will be priced based on equal shares of 12-month and
2 24-month full-requirements fixed-price purchases. As a result, at any point in time
3 during the default service period, 50 percent of the load obligation will effectively be
4 priced based on one-year purchases, while the remaining 50 percent will be priced based
5 on two-year purchases.

6 Under the Companies' proposal, the auction participants will make offers to supply
7 "tranches," where each tranche represents the full-requirements, load-following
8 generation service obligation for a defined slice (*i.e.*, percentage) of load for a particular
9 default service customer class. All energy requirements will be supplied at a fixed price
10 per megawatt hour ("MWh") as bid by the winning auction participants. The customers
11 receiving default service will be billed at a fixed price per kilowatt hour that will change
12 quarterly, with the quarters synchronized to PJM Interconnection, LLC's ("PJM") energy
13 year (that begins on June 1 and lasts through May 31).

14 There will be separate default service products for each electric distribution company
15 ("EDC") and for commercial and residential customer classes, but these products will be
16 procured simultaneously in the same auction. Auctions will be held for 12-month and
17 24-month products in October 2016, January 2017, and April 2017. Starting in October
18 2017, auctions will be held only for 12-month products, taking place in October 2017,
19 January 2018, and April 2018.

20 The winning bidders of the full-requirements, load-following procurements for the
21 residential, commercial, and industrial classes will be responsible for energy, capacity,
22 ancillary services, relevant PJM fees and administrative expenses, and certain

1 transmission costs associated with their share of default service load (including
2 congestion costs and marginal transmission losses, and PJM's Network Integration
3 Transmission Service ("NITS") costs. They will not be responsible for Regional
4 Transmission Expansion Plan charges ("RTEP"), Expansion Cost Recovery Charges
5 ("ECRC"), Reliability Must Run/generation deactivation charges ("RMR"),² historical
6 out of market tie line, generation, and retail customer metering adjustments, and
7 unaccounted for energy (UFE) (collectively referred to as "non-market-based charges,"
8 or "NMB charges"). The costs associated with NMB charges will be charged to
9 customers directly in the form of a non-bypassable tariff rider (*i.e.*, the Companies'
10 Default Service Support Riders).

11 For the industrial class, 100 percent of load will be acquired through an auction process
12 in which suppliers bid on a full requirements, load-following product whose energy price
13 is set at the PJM real-time price. In addition to a fixed adder of \$4/MWh intended to
14 cover capacity, ancillary services, NITS, AEPS Act compliance, and other costs
15 associated with meeting this full-requirements obligation, suppliers may bid an additional
16 adder over the PJM real-time price to cover any remaining costs or provide a potential
17 profit margin. Industrial class auctions for each EDC will be held in January 2017 and
18 January 2018, and these procurements will occur at the same time as the auctions for the
19 residential and commercial classes.

20 In addition to the above areas of responsibility, suppliers of the full requirements,
21 load-following tranches will bear the costs of complying with AEPS Act requirements.

22 In particular, default service suppliers in the Met-Ed, Penelec and Penn Power service

² Limited to unit declarations and deactivation of plants for which charges were set on or after July 24, 2014.

1 territories will be responsible for meeting 100% of the non-solar Tier I and Tier II AEPS
2 Act requirements. Met-Ed, Penelec and Penn Power will procure all necessary solar
3 photovoltaic requirements on behalf of default service suppliers and competitive electric
4 generation suppliers (“EGSs”) that serve load in their respective service areas. In the
5 West Penn service territory, default service suppliers will be responsible for all Tier I and
6 Tier II AEPS Act requirements (including solar photovoltaic requirements), less any
7 Tier I alternative energy credits (“AECs”) and SPAECs that are allocated to the default
8 service suppliers from existing long-term purchases made by West Penn.

9 **Q. Do you believe that the Default Service Program is consistent with the requirement**
10 **in Section 3.4 of Act 129 that it be designed to ensure “the least cost to customers**
11 **over time?”**

12 A. Yes, I do. As I have explained in prior testimony,³ the use of a competitive process to
13 procure a full-requirements product is designed to induce aggressive bidding among
14 suppliers who can manage portfolios of energy, transmission, and capacity products to
15 meet the load obligations of a given class of customers. The competitiveness of the
16 bidding process, coupled with the nature of the product that is being procured, will result
17 in an outcome where the suppliers who can manage those portfolios at the least cost over
18 time (or who believe that they can obtain the components of their portfolios at the lowest
19 prices over time) are the winning bidders.

³ See DSPI, Met-Ed/Penelec Statement No. 8; DSPII, Met-Ed/Penelec/Penn Power/West Penn Statement No. 6; and DSPIII, Met-Ed/Penelec/Penn Power/West Penn Statement No. 3.

1 **Q. How does the reliance upon a full-requirements product contribute to a**
2 **procurement strategy that is designed to ensure “the least cost to customers over**
3 **time” as required under Act 129?**

4 A. A full-requirements product, known as a “tranche,” is a clearly defined product. It
5 represents a defined percentage of the load of a particular customer class that the default
6 service supplier must serve, including the provision of energy, capacity, ancillary
7 services, transmission services and NITS (but excluding NMB charges). Default service
8 suppliers also are responsible for fulfilling some requirements of the AEPS Act, as I
9 described earlier in my testimony. With a clear product definition established in this
10 fashion, all bidders will bid to supply an identical product, so that winning bidders are
11 chosen purely on the basis of their price offers. This will lead to a transparent and
12 efficient bidding process.

13 By bidding on a full-requirements product that must be supplied at a fixed price per
14 MWh, the suppliers assume various risks, such as those relating to price uncertainty and
15 volumetric uncertainty due to variations in weather, customer shopping behavior, fuel
16 prices facing generators, and other market factors. Those suppliers who consider
17 themselves to be the most adept portfolio managers (or who are the most optimistic
18 portfolio managers) in terms of handling these risks will place the lowest bids in the
19 procurement. Thus, the procurement process is intended to rely on the skills of the best
20 electric power portfolio managers to achieve the least cost over time for default service
21 customers while maintaining a certain degree of rate stability.

22 The Commission appears to accept this viewpoint as well, as stated in its discussion of
23 full-requirements (“FR”) procurements in the Final Rulemaking Order in Docket No.

1 L-2009-2095604 (Implementation of Act 129 of October 15, 2008; Default Service and
2 Retail Electric Markets):⁴

3 The major benefit associated with the FR approach is that the procurement
4 function is delegated to the electric supplier which is presumably better
5 equipped with the necessary personnel and infrastructure to perform the
6 activities associated with acquiring electric supplies in the complex and
7 ever changing wholesale market environment. The FR process insulates
8 default supply customers from the volatility associated with wholesale
9 market conditions with the supplier bearing the risks of factors such as
10 customer migration, weather, load variation and economic activity (p. 54).

11 **Q. How does the reliance upon full-requirements products compare to the alternative
12 where the EDC instead uses a managed portfolio (“MP”) approach?**

13 A. In comparing the merits of a full-requirements approach versus a managed portfolio
14 approach to procuring generation supply for default service customers, the Commission
15 has previously expressed concern that the managed portfolio approach could produce
16 higher costs and greater pricing risk for consumers if the EDC does not prove to be an
17 adept portfolio manager.

18 For example, the Commission has previously stated as follows:⁵

19 On balance, we are not persuaded that the MP approach is superior to the
20 FR approach in achieving the “least cost to customers” while also
21 achieving the other objectives of “prudent mix” of products and price
22 stability. The MP approach has clear advantages to the retail markets and
23 the retail customer provided the EDC is capable of performing the full
24 range of portfolio management functions....Our principal concerns are
25 that EDCs do not currently possess the requisite expertise and
26 infrastructure to perform these portfolio management duties and the risks
27 to retail customers from EDC inexperience in performing these functions
28 is too great. We are also mindful of the fact that the current default supply

⁴ The Commission’s Tentative Order and Final Order in *Investigation of Pennsylvania’s Retail Electricity Market: End State of Default Service*, Docket No. I-2011-2237952, also support the use of FR procurements to serve default service customers. See pp. 16-18 in the Tentative Order and p. 41 in the Final Order.

⁵ Final Rulemaking Order, *Implementation of Act 129 of October 15, 2008; Default Service and Retail Electric Markets*, Docket No. L 2009-2095604, pp. 55-56 (entered October 4, 2011) (“2011 Final Rulemaking Order”).

1 process, with the EDC acting as the default supplier and distribution entity
2 purchasing its supply from electric suppliers knowledgeable about the
3 workings of the wholesale electric market, is a product of the Competition
4 Act, which created the market structure we now operate within.

5 Not only is the full-requirements approach intended to conform with the principles of
6 least-cost procurement, the winning bidders are supplying a product that is designed to
7 provide adequate and reliable service. The default service suppliers themselves will not
8 be expected to have difficulty providing such a product, given that its components (*e.g.*,
9 energy, capacity, ancillary services) can readily be acquired through the PJM market.

10 Moreover, the use of 12-month and 24-month full-requirements purchases for residential
11 and commercial customers should provide some measure of cost stability, which is a
12 desired attribute in procuring generation supplies for default service customers.⁶

13 **Q. Have previous full requirements default service procurements resulted in**
14 **substantial participation?**

15 A. Yes, there has been substantial participation, based on recent experience with competitive
16 procurements of full-requirements supplies for default service customers in Pennsylvania.
17 For example, the number of bidders in default service supply auctions for Met-Ed,

⁶ The 2011 Final Rulemaking Order recognized that relative cost stability is an objective in procuring default service supply:

As stated earlier in this Order, the “least cost over time” standard should not be confused with the presumption that default prices will always equal the lowest cost price for power at any particular point in time. In implementing default service standards, the Commission must be concerned about rate stability as well as other considerations such as ensuring a “prudent mix” of supply and ensuring safe and reliable service. In our view, a default service plan that meets the “least cost over time” standard should not have, as its singular focus, the achievement of the absolute lowest cost over the default service plan time frame but rather a cost for power that is both relatively stable and also economical relative to other options. (Final Rulemaking Order, p. 40.)

1 Penelec, Penn Power, and West Penn has ranged from 3 to 13 for procurements that have
2 taken place since the beginning of 2014.⁷

3 **Q. Have the Companies' previous default service auctions resulted in reasonable prices**
4 **that reflected expected wholesale market conditions?**

5 A. Yes, they have. My analysis of the prices resulting from recent default service auctions
6 conducted for residential and commercial customers of Met-Ed, Penelec, Penn Power,
7 and West Penn shows that these prices were only slightly above the combined wholesale
8 energy, capacity, ancillary service, and NITS costs that were projected at the time of each
9 auction for the corresponding delivery periods.⁸ This analysis is shown in Met-
10 Ed/Penelec/Penn Power/West Penn Exhibit JDR-1.

11 I first estimated the expected wholesale energy costs to serve retail loads of residential
12 and commercial customers. For this calculation, I have used PJM West forward prices,
13 which I adjusted for the delivery location by using the difference in spot energy prices
14 between the PJM West hub and the corresponding zonal price (METED, PENELEC,
15 PENN POWER AGGREGATE, or APS).⁹ I then adjusted these flat prices by the load
16 shape factor of residential and commercial non-shopping customers to reflect the fact that
17 the retail load of these customer classes is, on average, higher during hours with higher

⁷ Data for the number of participating bidders for Met-Ed, Penelec, Penn Power and West Penn default service auctions was provided by the Companies.

⁸ I did not include costs associated with alternative energy credits needed to satisfy AEPS requirements, or PJM RTEP and ECRC costs that were included in default service supplier obligations for auctions with delivery periods falling between June 1, 2011 and May 31, 2013. Given the exclusion of these costs, my estimates of implied risk premiums in providing default service may be somewhat overstated.

⁹ For this "basis" adjustment, I used 2010 as my reference year for default service auctions that occurred during 2010 and 2011, 2012 as my reference year for default service auctions that occurred in 2012 and 2013, and 2014 as my reference year for default service auctions that occurred in 2014 and 2015.

1 prices. The resulting energy prices were in the range of \$37-\$54/MWh for Met-Ed, \$36-
2 \$47/MWh for Penelec, \$2-\$33/MWh for Penn Power, and \$36-\$42/MWh for West Penn.

3 To calculate the capacity cost component of serving residential and commercial
4 customers, I relied on the PJM Base Residual Auction (“BRA”) prices (and the Fixed
5 Resource Requirement (“FRR”) Integration Auction prices for Penn Power before Penn
6 Power joined the PJM BRA) for the appropriate delivery periods. Then I converted these
7 capacity prices expressed in \$/MW-day into levelized capacity costs (expressed in
8 \$/MWh) by using the ratio of peak to average load for each customer class.¹⁰ The
9 resulting levelized capacity prices were in the range of \$11-\$25/MWh for Met-Ed, \$10-
10 \$26/MWh for Penelec, \$2-\$33/MWh for Penn Power, and \$4-\$15/MWh for West Penn.

11 For ancillary service costs, I used the actual 2010 (2012, 2014) costs of \$1.94 (\$1.92,
12 \$2.41) for default service auctions that occurred in 2010-11 (2012-13, 2014-15).

13 For NITS costs, I used costs expressed in \$/MW-day as provided by the Companies
14 starting when NITS became the default service supplier’s responsibility in June 2013. As
15 I did with the capacity prices, I converted NITS costs into levelized costs (expressed in
16 \$/MWh) by using the ratio of peak to average load for each customer class.¹¹ The
17 resulting levelized NITS costs were in the range of \$3-\$4/MWh for Met-Ed, \$3-\$4/MWh
18 for Penelec, \$6-\$9/MWh for Penn Power, and \$4-\$6/MWh for West Penn.

19 Finally, I added together the energy, capacity, ancillary service, and NITS costs to
20 estimate the expected wholesale market cost of serving the residential and commercial

¹⁰ For this capacity price adjustment, I used 2010 load data for default service auctions that occurred during 2010 and 2011, 2012 load data for default service auctions that occurred in 2012 and 2013, and 2014 load data for default service auctions that occurred in 2014 and 2015.

¹¹ I used the same load data for the NITS cost adjustment as for the capacity price adjustment.

1 customers. This represents my estimate of the expected cost of serving retail customers
2 without accounting for any potential risk-premium that default service suppliers may
3 include in their bid prices to reflect volumetric and price uncertainty. I refer to this
4 estimated cost as the “Estimated No-Risk Price”, as shown in Met-Ed/Penelec/Penn
5 Power/West Penn Exhibit JDR-1.

6 My estimated cost of serving retail customers is conservative as it does not include the
7 costs of alternative energy credits needed to meet AEPS requirements, as well as any
8 other costs not described above that are incurred by suppliers of default service.
9 Therefore, the “risk premium” referenced in Met-Ed/Penelec/Penn Power/West Penn
10 Exhibit JDR-1, which is calculated as the difference between the auction price and the
11 sum of the expected cost of serving the customer (*i.e.*, the sum of energy, capacity,
12 ancillary services, and NITS costs), may be larger than the “true” risk-premium to the
13 extent that any material costs have been omitted.

14 In spite of the conservatism of my cost calculations, the average difference between the
15 auction price and expected cost is relatively modest. The average risk premium
16 expressed in \$/MWh was \$3.70/MWh for Met-Ed, \$3.09/MWh for Penelec, \$3.38/MWh
17 for Penn Power, and \$3.65/MWh for West Penn. Expressed as a percentage of the
18 Estimated No-Risk Price, the risk premiums were, on average, 5.94% for Met-Ed, 5.25%
19 for Penelec, 2.82% for Penn Power, and 6.24% for West Penn. My results are
20 summarized in Table 1, and further detail is provided in Met-Ed/Penelec/Penn
21 Power/West Penn Exhibit JDR-1.

Table 1
Average Estimated Risk Premium in Default
Service Full Requirements Auctions

EDC	Risk Premium (\$/MWh)	Risk Premium (% of No-Risk Price)
Met-Ed	3.70	5.94%
Penelec	3.09	5.25%
Penn Power	3.38	5.07%
West Penn Power	3.65	6.24%

Source: The Brattle Group.

Q. What are the advantages of conducting a simultaneous procurement for Met-Ed, Penelec, Penn Power and West Penn?

A. By conducting a simultaneous procurement for the Companies for all classes, more potential bidders can be attracted to the procurement process. Transaction costs for both bidders and those soliciting supply also can be reduced through a simultaneous procurement. When the procurement mechanism is a simultaneous, multi-round, descending-clock procurement, bidders can switch from one utility's product to another in response to price differences that they believe are not reflective of underlying supply cost differences. This behavior leads to a potentially more economically efficient outcome and contributes to pricing that is more consistent among the four Companies.

By procuring in this fashion, the prices of default service for Met-Ed, Penelec, Penn Power and West Penn customers are not out of relation to each other (*i.e.*, one is not low-priced or high-priced relative to the other simply because of when it was procured). This provides the added benefit of simplifying administration and regulatory oversight.

By contrast, even if the auctions occur only days apart, a sequential default service auction process among the different Companies could lead to price disparities that do not

1 reflect actual differences in generation supply costs across the EDCs. Under a sequential
2 auction process, generation suppliers for default service customers must make strategic
3 decisions on how much supply to offer and what price to accept in one EDC's auction,
4 based on their expectations of the results of subsequent EDCs' auctions. With a
5 simultaneous auction process, a generation supplier can determine how much supply to
6 offer to a given EDC based on the current auction prices for that EDC and all other
7 Companies.

8 **Q. Do the proposed procurement formats conform with the requirements of Section 3.1**
9 **of Act 129?**

10 A. Yes, they do. Section 3.1 specifies that:

11 “...the default service provider shall provide electric generation supply to
12 that customer pursuant to a commission-approved competitive
13 procurement plan. The electric power acquired shall be procured through
14 competitive procurement processes and shall include one or more of the
15 following:

- 16 (i) auctions;
- 17 (ii) requests for proposal;
- 18 (iii) bilateral agreements entered into at the sole discretion of the
19 default service provider....”

20
21 The procurement format proposed by the Companies is a descending-clock auction
22 process, as explicitly permitted by Section 3.1(i).

23 **Q. Are the proposed procurement formats designed to achieve a competitive result,**
24 **which would be essential to achieving the least cost to customers over time?**

25 A. Yes, the auctions are designed to produce competitive outcomes as they are
26 nondiscriminatory, fair, and open. An auction mechanism encourages supplier

1 participation and is therefore aimed at achieving the least cost by selecting the
2 lowest-priced bids.

3 The descending-clock auction format is nondiscriminatory because any party can
4 participate as long as they satisfy the criteria used in the application process.
5 This procurement format is fair and transparent, because suppliers clearly understand
6 how the final solicitation prices are determined and how to compete for a winning
7 position.

8 The rules of the descending-clock auction are pre-specified in a way that can be
9 thoroughly replicated and verified. Because bidders are pre-qualified, the evaluation of
10 submitted bids is on a price-only basis, which is intended to produce a fair, least-cost
11 result.

12 The openness and transparency of the auction format encourages participation in the
13 bidding process. With a procurement format that encourages supplier participation, the
14 winning bidders are those that offer to supply full-requirements service at the lowest
15 prices (*i.e.*, the least cost). This process is consistent with achieving a competitive
16 outcome.

17 **Q. Why is it that the superior portfolio managers will place the lowest bids in these full-**
18 **requirements procurements?**

19 A. To serve default service customers, a prospective supplier must assemble a portfolio
20 comprised of competitively priced wholesale products, such as fixed-price, fixed-quantity
21 forward energy purchases and long-term energy contracts. Prospective suppliers are
22 likely to pay similar prices for forward energy purchases, implying that differences in

1 their auction bids are principally related to perceived differences in the cost of satisfying
2 uncertain customer load, as well as perceived differences in the cost of bearing other
3 sources of risk.

4 The suppliers submitting the lowest bids will be those that are the most efficient portfolio
5 managers (or otherwise require the least compensation for bearing pricing and volumetric
6 risk) or those that are most optimistic about the possibility of relatively low spot and
7 forward prices over the course of the delivery period. In this fashion, the Companies'
8 default service supply plan is designed to achieve the least cost to customers over time.

9 **Q. Doesn't the competitiveness of the auction procurement process depend on the**
10 **competitiveness of the underlying wholesale market?**

11 A. Taking the competitiveness of the wholesale market as given, the auction process, by
12 itself, can be competitive if it has sufficient participation. A concern might arise,
13 however, that the wholesale market is not competitive, leading to insufficient auction
14 participation and a less than fully competitive outcome because prospective suppliers are
15 not confident in their ability to obtain physical power supplies at reasonable prices.

16 However, there is ample reason to believe that the wholesale market is sufficiently
17 competitive to support a competitive pricing outcome for the Companies' default service
18 auction process. The PJM wholesale market, including the forward and spot markets that
19 are relevant to supplying Met-Ed, Penelec, Penn Power and West Penn, has numerous
20 potential suppliers.

21 PJM's markets have an active market monitor, and the PJM day-ahead and real-time
22 markets have procedures in place to mitigate abuses of market power. Specifically, PJM

1 has stringent *ex ante* mitigation processes that impose cost-based restrictions on the bids
2 of wholesale suppliers in its day-ahead and real-time markets whenever structural
3 conditions exist that may lead to potential exercises of market power. This mitigation
4 indirectly constrains longer-term forward prices as well, given that forward prices are
5 representative of expected future spot prices and that energy purchasers can substitute
6 between products of different durations.

7 Besides its energy markets, PJM also has market power mitigation processes in its
8 capacity markets.

9 As mentioned above, participation in the Companies' default service supply auctions
10 would likely be hindered if prospective participants were concerned that PJM's wholesale
11 markets were not competitive, or that energy trading in PJM was not sufficiently robust
12 to avoid incurring substantial transactions costs. However, past results suggest that this is
13 not the case, as there have historically been between 3 and 13 bidders in recent
14 full-requirements procurements for Met-Ed, Penelec, Penn Power, and West Penn.

15 **Q. Are there contingency plans in place for alternative procurement strategies if any**
16 **given auction appears to attract limited interest or if a winning supplier**
17 **subsequently defaults on its obligation before or during a delivery period?**

18 A. Yes. As described in detail by Mr. Reeping, the Companies are proposing to continue the
19 contingency plans that were previously approved by the Commission as part of their
20 current default service programs.

21

1 **Q. Do you agree with the proposed 75-percent load cap for the default service supply**
2 **auctions?**

3 A. Yes. The purpose of a load cap is to encourage supplier diversification, frequently as a
4 means of reducing the magnitude of default risk facing the purchaser. With proper
5 qualification requirements for participating in the default service supply auctions, and
6 with the significant collateral requirements associated with the agreement to provide
7 default service supplies, both the risk of default and the potential harm to customers from
8 default are substantially reduced.

9 As a matter of economic theory, when there are substantial costs involved in entering an
10 auction and preparing a bid, it is possible that the number of bidders in the auction may
11 be greater if the maximum share of the procurement that any single bidder can win is
12 sufficiently limited. As this “maximum share limit” is reduced, a bidder’s chances of
13 becoming a winning bidder increase, which may increase the expected value of
14 participating in the auction sufficiently to foster additional auction participation.

15 However, in the specific case of the default service supply auctions discussed herein,
16 the bidders are typically sophisticated market participants that often have ample financial
17 resources and substantial experience with buying and selling power in the energy
18 markets. So, it is unclear that raising the load cap in the default service supply auctions
19 will negatively affect participation in these auctions.

20 At the same time, raising the load cap may directly lead to lower auction prices.
21 An increase in the load cap allows a market participant that is willing to accept a lower

1 winning auction price to acquire more tranches of load. This could cause the auction to
2 clear at a lower price.

3 **III. CONCLUSION**

4 **Q. Can you summarize how the proposed plan to procure full-requirements service for**
5 **default service customers leads to the “least cost to customers over time” in the**
6 **provision of default service supply?**

7 A. Yes. Under the proposed plan, the Companies will use an auction process to acquire
8 generation to satisfy residential and commercial default service load through equally
9 proportioned full-requirements load-following procurements of 12-month and 24-month
10 duration. All load obligations will be priced based on the results of these fixed-priced
11 procurements of differing duration.

12 Industrial default service load will be priced based on the PJM real-time market, plus a
13 \$4/MWh adder. Suppliers will compete for this load through an auction process where
14 they will bid an additional adder to cover any costs (or profit margin requirements) that
15 remain after the \$4/MWh adder, which is intended to defray a portion of the capacity,
16 ancillary services, NITS, AEPS Act, and other costs that are part of the full-requirements
17 obligation.

18 The winners of the fixed-price full-requirements, load-following auctions must function
19 as portfolio managers by procuring a combination of energy, capacity, ancillary services,
20 and certain transmission products needed to ensure adequate and reliable service to
21 default service customers in the face of load and price uncertainty. Because the winners
22 in these auctions will be the ones that offer default service supply at the lowest

1 reasonable prices, the proposed descending clock auctions necessarily choose as winning
2 bidders those suppliers that can provide this portfolio of products at the least cost over
3 time (or that believe that they can provide this portfolio at the least cost). As a result, the
4 proposed supply plan produces the least cost over time relative to other procurement
5 methods, assuming that the procurements themselves are competitive.

6 The procurement format (a descending-clock auction) is designed to be open, fair, and
7 transparent. Supplier participation is encouraged as bidders are pre-qualified through an
8 open, transparent application process, where relevant information about the procurement
9 is posted to a public website. By accounting for any non-price factors such as bidder
10 creditworthiness in the qualification requirements, the bids are evaluated on a price-only
11 basis, which leads to a lowest price outcome. In this fashion, the procurement process
12 and the supply plan work together to achieve the least cost to customers over time.

13 **Q. Does this conclude your direct testimony at this time?**

14 A. Yes, it does.

James David Reitzes
Principal

Washington, DC

+1.202.955.5050

James.Reitzes@brattle.com

Dr. James D. Reitzes received his B.A. in economics and history from Stanford University in 1978, and his Ph.D. in economics from the University of Wisconsin in 1986. He specializes in providing economic analyses and expert testimony pursuant to regulatory proceedings in the energy and transportation sectors and litigation in the areas of antitrust, competition, and intellectual property.

Dr. Reitzes has provided expert analysis and testimony in energy-related competition and regulatory matters before the Federal Energy Regulatory Commission, state public utility commissions, and federal antitrust agencies. In the transportation sector, he has offered expert analysis and testimony in proceedings involving the U.S. Department of Transportation, U.S. Department of Justice, the European Commission, the European Court of First Instance, and national antitrust authorities. He also has provided economic consulting services to clients in the United States, Canada, the European Union, South America, and Africa.

Since joining The Brattle Group as a Principal in April 1998, Dr. Reitzes has been involved in energy regulatory, strategy, and litigation matters for utilities, RTOs, cooperatives, municipal power providers, and industrial customers. Most recently, Dr. Reitzes has been involved in formulating and managing auction and RFP processes for procuring electric power supplies (including renewable power and renewable energy credits), valuing investments in specified generation assets as well as purchases of energy and capacity (in comparison to other generation or procurement alternatives), analyzing the value and risks associated with particular features of power purchase agreements and EPC contracts, designing energy procurement strategies to support standard-offer service obligations, critiquing RTO market-monitoring policies and market design features, assessing the competitive implications of mergers and acquisitions in power markets, providing analyses of alleged market manipulation and exercises of market power in the energy sector, and designing transitional regulation strategies.

Dr. Reitzes has authored several articles on firm strategies with respect to pricing, quality, R&D investment, and merger behavior, published in leading economics and legal journals. He also is an author of a book that assesses the domestic impact of U.S. international trade policies.

REPRESENTATIVE ENERGY SECTOR EXPERIENCE

Retail Market Design and Power Procurement for Standard-Offer Service Customers

- For a utility in Pennsylvania, submitted testimony that analyzed cost and risk differences associated with full-requirements versus block-and-spot procurements of power supplies for default service customers. Analysis included estimates of the implied price premium for covering volumetric and pricing risk that was associated with past procurements of full-requirements power supplies, showing that this premium was relatively modest in size.

James David Reitzes

- For a utility in Pennsylvania, submitted testimony that estimated the expected level and variance in procurement costs associated with different portfolio strategies for providing electric power to default service customers. Analysis showed how different portfolio combinations of spot and forward purchases were likely to perform under different assumptions regarding the timing and frequency of forward purchases.
- For a utility in Maryland, submitted testimony that assessed differences in the expected cost and risk profile of different portfolio strategies for procuring power supplies for standard offer service customers. Analyzed how the use of a fixed-price default service product without switching restrictions provides customers with a potentially valuable option that may significantly increase the cost of supplying default service customers with full-requirements power. Assessed how load uncertainty affects the cost and risk of providing default service.
- For a utility in Pennsylvania, submitted testimony that assessed methods of supplying default service customers and the relationship between various facets of default service policy and the development of increased shopping by retail residential and commercial customers. Testimony analyzed the impact on customer shopping rates (and the competitive retail electric market) arising from the imposition of an “adder” to the price-to-compare, as well as from holding a retail opt-in auction subsequent to the purchase of power supplies for default service customers. Testimony also analyzed the magnitude of the “risk premium” embedded in the prices of past auctions to acquire full-requirements power supplies for default service customers.
- For a utility in Ohio, assessed a proposed utility rate plan for self-providing generation service to standard service offer customers and compared its costs against the costs of procuring power from market sources under full-requirements contracts.

Procurement (Auction) Management, Design, and Bidding Strategy

- For three utilities in Pennsylvania, designed and managed the procurement of solar photovoltaic alternative energy credits (SPAECs) on multiple occasions and submitted testimony describing the procurement process and benchmarking the results against expected market prices. Responsibilities included: (i) designing the auction rules and bid forms; (ii) overseeing the provision of auction-related information on the procurement website; (iii) corresponding with interested bidders; (iv) interacting with company

James David Reitzes

personnel regarding bidder credit issues; (v) hosting bidder information sessions; (vi) evaluating bid materials; (vii) building a financial model to determine the likely value of the solar energy credits; (viii) providing a benchmarking study to determine if the bids were reflective of market fundamentals; and (ix) drafting a report to the Pennsylvania Public Utility Commission to secure approval of the procurements.

- For utilities in Ohio, submitted testimony that described the design, management, and implementation of an auction process to serve standard service offer customers. Also participated in the development of software to implement the auction process and identify the winning bidders.
- For an owner of a merchant transmission line connecting PJM with NYISO, designed and managed an RFP process to sell transmission scheduling rights on multiple occasions. Responsibilities included: (i) designing the auction, its rules, and the bid forms; (ii) developing marketing materials and conducting various types of market analyses to assist bidders in understanding the value proposition offered by the transmission rights; (iii) assisting in the development of other auction materials including bidder participation agreements and purchase and sale contract provisions; (iv) hosting a website and overseeing the provision of auction-related information through the website; (v) communicating with potential bidders; (vi) responding to bidder questions and posting answers to those questions on the auction website; (vii) interacting with the client regarding a variety of bidder-related issues; (viii) selecting the winning bidders; and (ix) preparing a report describing the auction process for submission to the Federal Energy Regulatory Commission.
- For a municipal power provider that was a partial owner of a power plant in Illinois, designed and managed an RFP process to either sell the ownership stake in the plant or alternatively sell the output entitlement through a long-term PPA agreement. Responsibilities included: (i) developing target sale structures; (ii) formulating a schedule for completing the sale; (iii) developing the RFP documents and bid process tools; (iv) soliciting interest for the sale; (v) managing the RFP bid process; (vi) qualifying the bids; (vii) evaluating final bids and assisting in the negotiation of final terms; and (viii) preparing a report summarizing the RFP process.
- For an unregulated trading affiliate of a regulated utility, provided strategic bidding advice and financial analysis in a multi-round ascending clock auction to acquire PPAs for virtually divested generation assets. Assisted in the development of financial models

James David Reitzes

to value the various PPAs, and in formulating between-round bidding strategies, including helping with algorithms to estimate the remaining amount of eligibility of competing bidders.

- Have been part of the Brattle team serving as the Independent Auction Monitor (IAM) for the Southern Company energy auction. Southern Company must supply its excess power resources under specified terms and conditions into a day-ahead and hour ahead energy auction that is overseen by an external monitor. Our role is to: (i) verify Southern's calculations of available capacity to offer into the auctions; (ii) confirm that any transmission service necessary to accommodate a purchase under the auction is not unreasonably withheld; (iii) verify that the auction has cleared properly; (iv) ensure that internal data control restrictions are maintained to protect bidder information; (v) report complaints to the FERC; and (vi) independently file reports with the FERC regarding the auction.
- For industrial customers and municipalities in Texas in a stranded cost proceeding, submitted testimony to the Public Utility Commission of Texas that analyzed auction design issues pertaining to the sale of generation assets, including the potential impact on sale prices of conducting an auction when an outside entity has a right-of-first-refusal (ROFR) to purchase the assets at the winning auction price.

Asset Valuation

- For the City of San Antonio, performed a valuation of a nuclear power plant, and compared its value against alternative technologies including gas-fired, wind, and solar powered generation. Our analysis included a risk assessment of how the plant's value could be affected by changes in natural gas prices, environmental policy, and construction costs. Historical volatilities and implied volatilities derived from options were used to derive a distribution of potential valuation outcomes. Our results were submitted in a public report and hearing, as well as in briefings to the Mayor, City Manager, City Council, and the public.
- For a major overseas utility and investor in generation assets, performed a valuation of a proposed nuclear power plant in ERCOT and estimated the values of different types of PPAs associated with the output of the power plant. Made recommendations as to various structures for potential PPA agreements, and performed valuations associated

James David Reitzes

with changes in individual PPA features. Identified potentially interested counterparties for PPA agreements. Also, performed a valuation analysis for the power plant for the “residual” period beyond the expiration of the PPA agreements. This analysis required predicting the expected level and variance of future power prices under differing outcomes regarding the price of natural gas and greenhouse gas policy.

- For a group of municipal power providers and industrial customers, performed a valuation of various power plants for a stranded cost proceeding. Built a financial model to estimate the assets’ values at the time as sale, as well as analyzed comparable transactions to form an alternative valuation estimate.
- Built financial model to perform valuation analysis of renewable energy credits. This model was used to evaluate the results of several procurements of solar renewable energy credits conducted by Pennsylvania utilities, and the results of the model were presented to the Pennsylvania Public Utility Commission.
- On several occasions for utilities in the Mid-Atlantic and Midwest regions, have used multi-factor risk models to estimate the expected cost and cost distribution associated with different portfolio strategies for procuring power supplies for default service customers.

Competition Analysis

- For a merger of two major utilities in the western United States, estimated the pricing impacts associated with alternative generation divestiture scenarios through the use of a Cournot oligopoly simulation model. Assisted in the drafting of testimony related to the merger’s impact on competition and other issues.
- For an independent power producer, submitted testimony to FERC assessing the competitive impacts of a high-profile merger involving two major utilities and generation owners within PJM, as well as the competitive effects associated with specific proposed market power mitigation measures.
- For a group of municipal power companies, analyzed a proposed merger involving two major utilities with generation supplies in the mid-atlantic and midwest regions. Reviewed the Delivered Price Test (DPT) analysis conducted on behalf of the merger applicants, and analyzed the sensitivity of applicants’ results to changes in assumptions

regarding power prices, gas prices, and available suppliers of imported power into the geographic area of interest.

- For two merging utilities in New York, analyzed vertical market power issues related to the merged entities' ownership of both transmission and generation assets, including the strategic use of transmission outages and other forms of transmission withholding to effect increases in power prices. Examined potential pricing impacts with the aid of security-constrained, least-cost dispatch generation model.
- For PJM, served as the lead author of a Brattle study that analyzed PJM's protocols for mitigating market power, comparing those protocols to the ones used in other major RTO markets and internationally (e.g., the United Kingdom, Australia, and Nordpool). Made recommendations for potential changes to PJM's market power mitigation practices, and presented findings to various PJM member committees.
- For two merging electric and gas utilities with overlapping service territories in New England, analyzed the competitive impacts of their merger, specifically as it related to market power concerns arising from the supply of gas to dual-fuel industrial customers, interconnection policy with respect to industrial customers, and vertical market power issues related to supplying gas to competitive generation suppliers. Presented analysis to Federal Trade Commission attorneys and economists.
- For the U.S. government, analyzed the pricing impacts arising from an alleged cornering of a major commodity market for an oil and gas derivative product. Formulated and estimated an econometric model to identify whether an "artificial price" had resulted from the alleged behavior consistent with the exercise of significant market power. Also provided estimates of damages attributable to the price overcharges stemming from the alleged manipulation.

PUBLICATIONS

Journals

"Domestic Versus International Capital Mobility: Some Empirical Evidence," with Donald J. Rousslang, *Canadian Journal of Economics*, Vol. 21, No. 2 (May 1988): 312-323.

"The Impact of Quotas and Tariffs on Strategic R&D Behavior," *International Economic Review*, Vol. 32, No. 4 (November 1991): 985-1007.

“Anticompetitive Effects of Mergers in Markets with Localized Competition,” with David T. Levy, *Journal of Law, Economics, and Organization*, Vol. 8, No. 2 (April 1992): 427-440.

“Quality Choice, Trade Policy, and Firm Incentives,” *International Economic Review*, Vol. 33, No. 4 (November 1992): 817-835.

“Basing-Point Pricing and Incomplete Collusion,” with David T. Levy, *Journal of Regional Science*, Vol. 33, No. 1 (February 1993): 27-35.

“Ocean Shipping Economics: Comment,” *Contemporary Policy Issues*, Vol. 11, No. 3 (July 1993): 81-85.

“Product Differentiation and the Ability to Collude: Where Being Different Can Be an Advantage,” with David T. Levy, *Antitrust Bulletin*, Vol. 38, No. 2 (Summer 1993): 349-368.

“Antidumping Policy,” *International Economic Review*, Vol. 34, No. 4 (November 1993): 745-763 [reprinted in Douglas R. Nelson and Hylke Vandenbussche editors, *The WTO and Anti-Dumping: Volume 1* (Cheltenham, UK: Edward Elgar Publishers, 2005): 392-410].

“The Importance of Localized Competition in the 1992 Merger Guidelines: How Closely Do Merging Firms Compete?” with David T. Levy, *ABA Antitrust Law Journal*, Vol. 62, No. 3 (Spring 1994): 695-716.

“Market-Share Quotas,” with Oliver R. Grawe, *Journal of International Economics*, Vol. 36, No. 3/4 (May 1994): 431-447.

“Price Discrimination and Mergers,” with David T. Levy, *Canadian Journal of Economics*, Vol. 28, No. 2 (May 1995): 427-436.

“In the Matter of Weyerhaeuser Company: The Use of the Hold-Separate Order in a Merger with Horizontal and Vertical Effects,” with Robert P. Rogers and Laurence Schumann, *Journal of Regulatory Economics*, Vol. 11, No. 3 (May 1997): 271-289.

“Market Power and Collusion in the Ocean Shipping Industry: Is a Bigger Cartel a Better Cartel?” with Paul S. Clyde, *Economic Inquiry*, Vol. 36, No. 2 (April 1998): 292-304.

“Is it Efficient to Impose Costs on Small-Volume Equity Traders?” with Paul S. Clyde, *International Journal of the Economics of Business*, Vol. 6, No. 1 (April 1999): 81-92.

“Lessons from the First Year of Competition in the California Electricity Markets,” with Robert Earle, Philip Hanser, and Weldon Johnson, *The Electricity Journal*, Vol. 12, No. 8 (October 1999): 57-76.

“Entry Policy and Entry Subsidies,” with Oliver R. Grawe, *Review of International Economics*, Vol. 7, No. 4 (November 1999): 715-731.

“Deregulation and Monitoring of Electric Power Markets,” with Robert L. Earle and Philip Q. Hanser, *The Electricity Journal*, Vol. 13, No. 8 (October 2000): 11-25.

“Strategic Pricing When Electricity Is Storable,” with Alfredo Garcia and Ennio Stachetti, *Journal of Regulatory Economics*, Vol. 20, No. 3 (November 2001): 223-247.

“Rolling Seas in Liner Shipping,” with Kelli L. Sheran, *Review of Industrial Organization*, Vol. 20, No. 1 (February 2002): 51-59.

“Regional Interactions in Electricity Prices in the Eastern United States,” with Gregory R. Leonard, Adam C. Schumacher, and James G. Bohn, in Michael A. Crew and Joseph C. Schuh editors, *Markets, Pricing, and Deregulation of Utilities* (Boston: Kluwer Academic Publishers, 2002): 109-142.

“Designing Standard-Offer Service to Facilitate Electric Retail Restructuring,” with Lisa V. Wood, J. Arnold Quinn, and Kelli L. Sheran, *The Electricity Journal*, Vol. 15, No. 9 (November 2002): 34-51.

“Can Mergers to Monopoly, Price Fixing, and Market-Division Agreements Raise Welfare?” with Paul S. Clyde, *International Journal of the Economics of Business*, Vol. 11, No. 1 (February 2004): 69-90.

“Forward and Spot Prices in Electricity and Gas Markets: Does ‘Storability’ Matter?” with J. Arnold Quinn and Adam C. Schumacher, in Michael A. Crew and Menahem Spiegel editors, *Obtaining the Best from Regulation and Competition* (Boston: Kluwer Academic Publishers, 2005): 109-135.

“Incentive Contracts for Infrastructure, Litigation and Weak Institutions” with Alfredo Garcia and Juan Benavides, *Journal of Regulatory Economics*, Vol. 27, No. 1 (January 2005): 5-24.

“Dynamic Pricing & Learning in Electricity Markets,” with Alfredo Garcia and Enrique Campos, *Operations Research*, Vol. 53, No. 2 (March-April 2005): 231-241.

“Estimating the Economic ‘Trade’ Value of Increased Transmission Capability,” with Andrew N. Kleit, *The Electricity Journal*, Vol. 19, No. 2 (March 2006): 69-78.

“International Perspectives on Electricity Market Monitoring and Market Power Mitigation,” with Jose A. Garcia, *Review of Network Economics*, Vol. 6, No. 3 (September 2007): 397-424.

“Downstream Price-Cap Regulation and Upstream Market Power,” *Journal of Regulatory Economics*, Vol. 33, No. 2 (April 2008): 179-200.

“Airline Alliances and Systems Competition,” with Diana Moss, *Houston Law Review*, Vol. 45, No. 2 (Summer 2008): 293-332.

“The Effectiveness of FERC’s Transmission Policy: Is Transmission Used Efficiently and When Is It Scarce?” with Andrew N. Kleit, *Journal of Regulatory Economics*, Vol. 34, No. 1 (August 2008): 1-26.

“Competition for Exclusive Customers: Comparing Equilibrium and Welfare under One-Part and Two-Part Pricing,” with Glenn A. Woroch, *Canadian Journal of Economics*, Vol. 41, No. 3 (August 2008): 1046-1086.

Books

The Regional Welfare Effects of U.S. Import Restraints on Apparel, Petroleum, Steel and Textiles, with Randi Boorstein, Michael Metzger, and Morris Morkre, Avebury Press, 1996.

Completed Studies

“Case Studies of the Price Effects of Horizontal Mergers,” *Staff Report of the Federal Trade Commission*, April 1992, with coauthors.

“The Effectiveness of Collusion under Antitrust Immunity—The Case of Liner Shipping Conferences,” *Staff Report of the Federal Trade Commission*, December 1995, with coauthor.

“The Effectiveness of Dutch Airport Transport Policy,” study prepared for the Dutch Ministry of Transport, December 2002, with coauthors.

“The Economic Impact of an EU-US Open Aviation Area,” study prepared for the European Commission - Directorate-General for Energy and Transport, December 2002, with coauthors.

“Study to Assess the Potential Impact of Proposed Amendments to Council Regulation 2299/89 with regard to Computerised Reservation Systems,” study prepared for the European Commission - Directorate-General for Energy and Transport, October 2003, with coauthors.

PRESENTATIONS

“Genco Pricing & Genco Asset Values under Deregulation,” presented to the Center for Business Intelligence Conference, Chicago, IL, September 18, 1998.

“Ancillary Services: New Business Opportunities in Competitive Ancillary Services Markets,” presented at Electric Utility Consultants Workshop on Strategies for Pricing and Selling Ancillary Services, Denver, CO, September 9, 1999.

“Profit-Maximizing Strategies and Gaming: Market Power and Power Markets,” presented to the Center for Business Intelligence Conference on Pricing Power Products and Services, Chicago, IL, October 14, 1999.

James David Reitzes

“Strategic Behavior and Power Market Prices,” presented to the EPRI Asset & Risk Management Group, Washington, DC, June 23, 2000.

“Regional Interactions in Electricity Prices in the United States,” presented to the CRRI Research Seminar, Newark, NJ, May 3, 2002.

“Standard-Offer Service and Retail Restructuring of Electric Markets,” presented to the CRRI Eastern Conference, Newport, RI, May 23, 2002.

“The Economic Impact of an EU-US Open Aviation Area,” presented to the U.S. Department of State, the European Commission (US office), and the Heritage Foundation, Washington, DC in 2002 and 2003, and the Association of European Airlines, Brussels, Belgium, 2003.

“Transactions Costs Across Electricity Markets: Does Restructuring Matter?” presented to the CRRI Eastern Conference, Skytop, PA, May 22, 2003.

“Identifying the Relationship between Spot and Futures Prices for Electricity and Natural Gas,” presented to the Center for Research in Regulated Industries (CRRI) Research Seminar, Newark, NJ, May 7, 2004, and the CRRI Eastern Conference, Skytop, PA, May 21, 2004.

“Geographic Integration, Transmission Constraints, and Electricity Restructuring,” presented to the Federal Energy Regulatory Commission, Federal Trade Commission, Energy Information Administration, in Washington, DC, in 2004 and 2005, and the 10th Annual POWER Research Conference on Electricity Industry Restructuring of the University of California Energy Institute, Berkeley, CA, March 18, 2005.

TESTIMONY/EXPERT REPORTS

Testimony before the Advisory Commission on Conferences in Ocean Shipping, 1991, relating to an econometric analysis of the determinants of ocean freight rates, and the conclusions of that study with respect to the existence of market power in ocean shipping.

Expert Submission - Appendix J, Volume 1, Prehearing Brief on Behalf of Petitioner, Certain Flat Rolled Carbon Steel Products, June 21, 1993, U.S. International Trade Commission Investigation Nos. 701-TA-319-332, 334, 336-342, 344, and 347-353 (final); 731-TA-573-579, 581-592, 594-597, 599-609, and 612-619 (final). Analysis included a critique of methods used to evaluate domestic injury in trade cases. Also authored part of submission for post-hearing brief.

Expert Report Submitted to the European Court of First Instance on Behalf of the European Commission relating to the Petition of the Transatlantic Agreement to Annul the Commission's Decision of October 19, 1994, including a rebuttal of the expert economic analysis offered by the members of the Transatlantic Agreement in support of their collective restrictions on capacity utilization and their coordinated activity in setting certain types of freight rates.

Testimony in the Matter of Henry H. Godfrey v. Benjamin F. Hofheimer, III, *et. al.*, 1995, on behalf of defendant relating to the appropriate calculation of damages in a breach-of-contract dispute.

Expert Report Submitted to the Environmental Protection Agency, 2000, on behalf of a trade group of aluminum smelters assessing the economic costs of revised land-disposal restriction standards for spent aluminum potliners (K088), 2000.

Two Expert Reports Submitted to the U.S. District Court for the District of Maryland, 2001, in the matter of Charles River Associates Inc. v. Hale Trans, Inc., assessing the quality and cost effectiveness of economic expertise provided in a predatory-pricing matter.

Expert Report Submitted to the U.S. District Court for the District of Columbia in the Matter of DAG Enterprises Inc. v. Exxon Mobil Corporation, 2003, regarding the suitability of a prospective purchaser as an acquirer of Mobil assets under the antitrust standards used by the Federal Trade Commission.

Expert Report Submitted to the Federal Energy Regulatory Commission (Docket No. EC05-43-000) 2005 on behalf of Midwest Generation, regarding the competitive impact of the proposed merger of Exelon Corporation and Public Service Enterprise Group and the mitigation measures offered by the parties.

Expert Reports submitted to the U.S. Department of Transportation (Docket No. OST-2004-19214), 2005, on behalf of American Airlines, regarding the competitive impact of the proposed application for antitrust immunity of an airline alliance consisting of Delta, Northwest, KLM, Air France, Alitalia, and Czech Airlines.

Expert Report and Testimony before the Public Utility Commission of Texas (Docket No. 31056), 2005, on behalf of the Cities served by AEP Texas Central Company, the Texas Industrial Energy Consumers, and the Alliance for Valley Healthcare, regarding the competitiveness of an auction held to sell an ownership share in a nuclear power plant and the commercial reasonableness of the actions taken by the seller.

Expert Reports submitted to the U.S. Department of Transportation (Docket No. OST-2005-22922), 2006, on behalf of American Airlines, regarding the competitive impact of the proposed Star alliance expansion to include LOT and Swiss airlines and expand antitrust immunity between Air Canada and United Airlines.

Expert Report and Testimony before the Public Service Commission of Maryland, (Case No. 9117, Phase 1), 2007 on behalf of Potomac Electric Power Company and Delmarva Power & Light Company, regarding the risks and costs associated with portfolio procurement of electric power supplies as opposed to relying on a full-requirements auction-based procurement method.

Expert Report submitted to the Pennsylvania Public Utility Commission (Docket No. P-0072305), 2008, on behalf of Pennsylvania Power Company, regarding the risks and costs associated with different procurement methods for obtaining electric power supplies to serve default-service customers.

Expert Report and Testimony before the Public Utility Commission of Ohio (Case No. 08-936-EL-SSO), 2008, on behalf of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company, regarding the rationale for using an auction process to procure full-requirements electric power supplies for standard-service-offer customers, as well as a description of the responsibilities undertaken by myself and The Brattle Group as manager of that procurement.

Expert Report submitted to the Pennsylvania Public Utility Commission (Docket Nos. P-2009-2093053 and P-2009-2093054), 2009, on behalf of Metropolitan Edison Company and Pennsylvania Electric Company, describing the design of an RFP process for procuring solar photovoltaic alternative energy credits and the management of that process by myself and The Brattle Group, as well as an analysis of the desirability of meeting default service obligations through the auction-based procurement of full-requirements power supplies.

Various Expert Reports submitted between 2008 and 2010 to the U.S. Department of Transportation (Docket No. OST-2008-0252) and the European Commission describing the competitive impact of the proposal by the oneworld alliance to receive antitrust immunity, including various assessments of the impact on non-stop and connecting passengers that relied on econometric analysis of airline fare data and other empirical methods.

Reports submitted to the Pennsylvania Public Utility Commission, 2010, 2011, 2012, and 2013 as the Independent Procurement Manager for the procurement of Solar Photovoltaic Alternative Energy Credits by Metropolitan Edison Company, Pennsylvania Electric Company, and Pennsylvania Power Company including a description of the RFP process, a benchmarking of procurement prices against both current short-term prices and expected long-term prices for solar credits (based on a proprietary financial model), and the conformity of the procurement to the standards of least-cost procurement provided under Pennsylvania law.

Expert Reports (and Deposition) submitted to the U.S. District Court for the Middle District of Tennessee, 2012, in the matter of Watson Carpet & Floor Covering Inc. v. Mohawk Industries Inc., regarding the competitive effects of a carpet manufacturer's alleged refusal to sell its products to a carpet dealer serving production homebuilders in Nashville and surrounding counties.

Expert Reports and Testimony before the Pennsylvania Public Utility Commission (Docket Nos. P 2011-2273650, P-2011-2273668, P-2011-2273669, and P-2011-2273670), 2011 and 2012, on behalf of Metropolitan Edison Company, Pennsylvania Electric Company, Pennsylvania Power Company, and West Penn Power Company, analyzing the Companies' procurement strategies for supplying default service customers, describing the design of an RFP process for procuring solar photovoltaic alternative energy credits (and the management of that process by myself and The Brattle Group), proposing an auction process for outsourcing the provision of generation service for time-of-use customers, describing an "opt-in" auction process to promote the switching of default service customers to competitive retail supply, and describing a customer referral program that is also designed to promote retail competition.

Expert Reports before the Pennsylvania Public Utility Commission (Docket Nos. P-2013-2391368, P-2013-2391372, P-2013-2391375, P-2013-2391378), 2013 and 2014, on behalf of Metropolitan Edison Company, Pennsylvania Electric Company, Pennsylvania Power Company, and West Penn Power Company, analyzing the Companies' procurement strategies for supplying default service customers.

PROFESSIONAL ACTIVITIES

Consultant to the *World Bank* on the formation of regional trading blocs, the *European Community* (DG IV) on antitrust and transportation issues, and the *Government of Canada* (Competition Bureau) on antitrust and transportation issues.

Advisory Board Member of the Center for Research in Regulated Industries

Member of the Atlantic Energy Group

Referee for the following journals: *American Economic Review*, *Canadian Journal of Economics*, *Contemporary Policy Issues*, *European Economic Review*, *International Economic Review*, *International Journal of the Economics of Business*, *Journal of Economics*, *Journal of Economics and Business*, *Journal of Economic Integration*, *Journal of Industrial Economics*, *Journal of International Economics*, *Journal of Regulatory Economics*, *Oxford Economic Papers*, and *Review of International Economics*.

Teaching Experience: Introductory Macroeconomics; Introductory Microeconomics

July 14, 2014

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

**METROPOLITAN EDISON COMPANY
Docket No. P-2015-_____**

**PENNSYLVANIA ELECTRIC COMPANY
Docket No. P-2015-_____**

**PENNSYLVANIA POWER COMPANY
Docket No. P-2015-_____**

**WEST PENN POWER COMPANY
Docket No. P-2015-_____**

**DEFAULT SERVICE PROGRAMS
June 1, 2017 to May 31, 2019**

**Direct Testimony
of
Kimberlie L. Bortz**

**List of Topics Addressed
Customer Notice
Rate Design and Cost Recovery
Customer Referral Program
Purchase of Receivables Program
Related Tariff Matters**

TABLE OF CONTENTS

	Page
I. INTRODUCTION AND BACKGROUND.....	1
II. CUSTOMER NOTICE.....	2
III. RATE DESIGN AND COST RECOVERY.....	4
IV. CUSTOMER REFERRAL PROGRAM	11
V. PURCHASE OF RECEIVABLES PROGRAM	12
VI. RELATED TARIFF MATTERS.....	21
VII. CONCLUSION	21

1 **DIRECT TESTIMONY**
2 **OF**
3 **KIMBERLIE L. BORTZ**

4 **I. INTRODUCTION AND BACKGROUND**

5 **Q. Please state your name and business address.**

6 A. My name is Kimberlie L. Bortz, and my business address is 2800 Pottsville Pike, Reading,
7 PA 19605.

8 **Q. By whom are you employed and in what capacity?**

9 A. I am employed by FirstEnergy Service Company as a Rates Advisor - Rates and Regulatory
10 Affairs - Pennsylvania. The Pennsylvania Rates Department provides regulatory support
11 for Metropolitan Edison Company (“Met-Ed”), Pennsylvania Electric Company
12 (“Penelec”), Pennsylvania Power Company (“Penn Power”) and West Penn Power
13 Company (“West Penn”) (individually, a “Company” and in any combination, the
14 “Companies”). I am responsible to the Director - Rates and Regulatory Affairs -
15 Pennsylvania for tariff interpretation, tariff filings and the design of rates.

16 **Q. What is your educational background?**

17 A. I have a Bachelor of Science degree in Accounting from the University of Maryland, and
18 I am a Certified Public Accountant in Pennsylvania. My educational background and work
19 experience are more fully described in Appendix A to this statement.

20 **Q. On whose behalf are you testifying in this proceeding?**

21 A. I am testifying on behalf of Met-Ed, Penelec, Penn Power and West Penn. My testimony
22 equally applies to all of the Companies, unless otherwise stated.

1 **Q. What is the purpose of your direct testimony?**

2 A. My testimony will describe the following elements of the Default Service Programs
3 (“DSPs”) that are the subject of this proceeding: (i) customer notice; (ii) the proposed rate
4 design and cost recovery plans; (iii) the Customer Referral Program (“CRP”); (iv) proposed
5 changes to the Companies’ Purchase of Receivables (“POR”) programs; and (v) related
6 tariff issues.

7 **Q. Have you prepared any exhibits to accompany your testimony?**

8 A. Yes. Met-Ed/Penelec/Penn Power/West Penn Exhibits KLB-1 through KLB-7 were
9 prepared by me or under my supervision and are described in detail later in my testimony.

10 **II. CUSTOMER NOTICE**

11 **Q. Please describe how the Companies will provide notice to customers of this filing.**

12 A. Pursuant to 52 Pa. Code § 54.188(e)(1), the Companies must provide all customers with
13 notice of the filing of their DSPs in a manner similar to that described in 52 Pa. Code §
14 53.68, which deals with changes in purchased gas cost rates under Section 1307(f) of the
15 Public Utility Code. Accordingly, within thirty days of filing the Joint Petition seeking
16 approval of their DSPs, each of the Companies will provide public notice of the filing by
17 publishing a notice in the major newspapers serving their respective service areas. The
18 notice will contain information about the Companies’ filings; the Companies’ proposed
19 competitive solicitations of generation resources; how the Companies’ plans may affect
20 customers; where the filings are being made available for public inspection; how comments
21 or complaints can be filed; and how customers can participate in these proceedings. The
22 Companies’ Joint Petition, direct testimony and exhibits are being made available for
23 inspection at Met-Ed’s principal office in Reading, Penelec’s principal office in Erie, Penn

1 Power's office in Clark, and West Penn's principal office in Greensburg. Additionally,
2 this material will be posted to the Companies' public internet domain, where it will be
3 available electronically for public inspection. Finally, the Companies are providing
4 additional public notice by means of a press release.

5 In accordance with 52 Pa. Code § 54.185(c), the Companies are also serving copies of the
6 Joint Petition, direct testimony and exhibits on the Pennsylvania Office of Consumer
7 Advocate ("OCA"), the Pennsylvania Office of Small Business Advocate ("OSBA"), the
8 Pennsylvania Public Utility Commission's ("Commission") Bureau of Investigation and
9 Enforcement ("BI&E"), PJM Interconnection L.L.C. ("PJM"), and all electric generation
10 suppliers ("EGSs") registered to provide service in the Companies' service territories. As
11 a courtesy, the Companies are also serving copies of the Joint Petition, direct testimony
12 and exhibits on: the Met-Ed Industrial Users Group ("MEIUG"), the Penelec Industrial
13 Customer Alliance ("PICA"), the Penn Power Users Group ("PPUG"), and the West Penn
14 Power Industrial Interveners ("WPPII") (collectively, the "Industrials"); the Pennsylvania
15 State University ("PSU"); and the Retail Energy Supply Association ("RESA").

16 **Q. Please describe the proposed customer notices that will be provided for any default**
17 **service rate changes.**

18 A. The Companies will submit tariff supplements on a quarterly basis to recover the costs
19 reasonably incurred in acquiring electricity at market prices the latter of: forty-five days
20 prior to the effective date of each change in their default service rate; seven days after the
21 last supply auction; or more frequently. The tariff supplements will be accompanied by
22 the calculations that translate procurement plan results into retail rates. Written notice of
23 the submission of these tariff supplements will be provided to the OCA, OSBA, BI&E,

1 Industrials, PSU, and other parties included on the service list for this proceeding. The
2 tariff supplements will be posted on the Companies’ public internet domain when they are
3 filed with the Commission. In addition, the Companies will post the filed price-to-compare
4 (“PTC”) rates for the residential and commercial classes on the Commission’s website at
5 www.papowerswitch.com. Also, within one business day of the effective date of the
6 revised PTCs for the residential and commercial customer classes, the revised PTCs will
7 be posted on the Companies’ public internet site.

8 Consistent with the Companies’ current practice, as approved in their current DSPs,
9 customers will be provided notice, via bill message, that new default service rates will take
10 effect for each upcoming default service quarter. The notices will enable customers to
11 analyze how the new rates will affect their bills and provide an opportunity for customers
12 to seek competitive alternatives from EGSs.

13 **III. RATE DESIGN AND COST RECOVERY**

14 **Q. Are the Companies proposing any changes to their existing retail customer**
15 **classifications – residential, commercial and industrial?**

16 A. No. The Companies will continue to procure default service supplies separately for each
17 of the three retail customer classes. However, the rate schedules that comprise each
18 customer class in the proposed DSPs have changed as a result of rate schedule additions
19 and eliminations approved during the Companies’ recent base rate cases.¹

¹ *Pa.P.U.C. v. Metropolitan Edison Co.*, Docket No. R-2014-2428745 (Order entered April 9, 2015); *Pa.P.U.C. v. Pennsylvania Elec. Co.*, Docket No. R-2014-2428743 (Order entered April 9, 2015); *Pa.P.U.C. v. Pennsylvania Power Co.*, Docket No. R-2014-2428744 (Order entered April 9, 2015); and *Pa.P.U.C. v. West Penn Power Co.*, Docket No. R-2014-2428742 (Order entered April 9, 2015).

1 **Q. Please describe the rate schedule changes resulting from the Companies' recent base**
2 **rate cases that will affect the customer class rate schedule groupings.**

3 A. The Met-Ed and Penelec residential customer class groupings will reflect the elimination
4 of Rate Schedules RT and the commercial class groupings will include the addition of the
5 LED Street Lighting Services. There are no changes to the Met-Ed and Penelec industrial
6 rate schedule groupings.

7 The Penn Power residential customer class grouping will no longer include the following
8 eliminated rate schedules and riders: RS Optional Controlled Service Rider, Rate Schedule
9 RH and Rate Schedule WH. The Penn Power commercial customer class grouping will
10 exclude the General Service – Secondary Voltages Optional Controlled Service Rider and
11 the Commercial and Industrial Optional Heating Rate, as these offerings were eliminated
12 in the Company's recent base rate case. Additionally, the Penn Power commercial
13 customer class grouping will reflect the addition of the GS-Large and Rate LED schedules.
14 There are no changes to the Penn Power industrial rate schedule grouping.

15 The West Penn residential class grouping will not change. The commercial class grouping
16 for West Penn will exclude eliminated Rate Schedules 22, 23, and 24, and will now include
17 Rate Schedule 72. The West Penn industrial class will exclude eliminated Rate Schedules
18 30 (large), 41 and 86 and now include Rate Schedule 35.

1 **Q. Are the Companies proposing any changes to the design of the default service rates**
2 **for each of their customer classes?**

3 A. No. The default service rates for the Companies' residential and commercial customer
4 classes consist of a single per kilowatt-hour ("kWh") energy charge, which changes
5 quarterly.

6 For the Companies' industrial customer classes, default service rates are based upon the
7 PJM real-time hourly Locational Marginal Price ("LMP") for the Companies' respective
8 PJM-designated delivery zone, plus associated costs incurred to provide hourly-priced
9 service, such as capacity, ancillary services, PJM administrative expenses and costs to
10 comply with Alternative Energy Portfolio Standards ("AEPS") requirements.

11 **Q. What costs would the Companies recover under the default service rates they are**
12 **proposing in this case?**

13 A. The default service rates would continue to recover: (1) generation costs, certain
14 transmission costs, ancillary service costs, and AEPS compliance costs, as described by
15 Mr. Reeping in Met-Ed/Penelec/Penn Power/West Penn Statement No. 1; (2) supply
16 management and administrative costs, as permitted by 52 Pa. Code § 69.1808; and (3)
17 applicable taxes. In addition, the default service rates will continue to include a quarterly
18 reconciliation component, or "E-factor," to recoup or refund, as applicable, under or over-
19 collections from prior periods.

1 **Q. How are default service rates charged to the Companies’ residential and commercial**
2 **default service customers?**

3 A. The default service rates of each of the Companies’ residential and commercial customer
4 classes are charged through Rider H, Price to Compare Default Service Rate Rider (“PTC
5 Rider”) as part of each of the Companies’ tariffs which sets forth rates for default service
6 that are then incorporated into and referenced by the applicable rate schedules.

7 **Q. Are the Companies proposing any changes to their PTC Riders?**

8 A. No. The Companies are not proposing to change the design or components of their PTC
9 Riders as part of their proposed DSPs.

10 **Q. Do you believe the design of the PTC Rider rates for the residential and commercial**
11 **customer classes is consistent with the Commission’s default service regulations and**
12 **the Public Utility Code?**

13 A. Yes. The Commission’s regulations at Section 54.187(d) state that default service rates
14 may not use a declining block structure. For the residential class, the Public Utility Code
15 at Section 2807(e)(7) and the regulations at Section 54.187(i) provide that rates shall
16 change no more frequently than on a quarterly basis. The Companies’ proposed PTC Rider
17 rates for the residential and commercial customer classes employ a flat per kWh rate
18 design, with rates that will continue to change quarterly.

19 The Commission’s regulations also provide that the default service rates for customers with
20 a maximum registered peak load² of 25 kW to 500 kW should be adjusted no less frequently

² I.e., the single time - usually fifteen minutes - of highest demand throughout the day.

1 than quarterly, except that default service providers may propose, for Commission
2 approval, a different grouping of customers based on a dividing line other than 500 kW in
3 order to avoid splitting existing customer and rate classes. Accordingly, when the
4 Companies proposed their current DSPs, they sought approval of commercial customer
5 classes that differed somewhat from the 500 kW threshold recommended in the
6 Commission's regulations. As such, the commercial customer classes for Met-Ed, Penelec
7 and West Penn have been defined to generally include customers with peak monthly
8 demands that do not exceed 400 kW, while the commercial customer class for Penn Power
9 was defined to include all customers served at secondary voltage on specified rate
10 schedules that apply generally to commercial customers.

11 As such, the Commercial Customer Class definitions approved as part of the Companies'
12 currently effective DSPs and the recent base rate cases preserve the existing customer and
13 rate classes which were previously approved by the Commission. Consequently, in this
14 case, the Companies are requesting that the Commission approve the continued use of their
15 existing residential and commercial customer class definitions and the concomitant
16 quarterly adjustment procedures.

17 **Q. How are default service rates charged to non-shopping customers that are part of the**
18 **Companies' industrial class?**

19 A. The industrial customer class default service rates of each of the Companies are charged
20 through Rider I, Hourly Pricing Default Service ("HP") Riders as part of each of the
21 Companies' tariffs. The HP Rider applies to the industrial customer class but may also be
22 elected on a voluntary basis by qualifying commercial customers that have smart metering
23 technology in place.

1 **Q. Are the Companies proposing any changes to their HP Riders?**

2 A. No. The Companies are not proposing to change the design or components of their HP
3 Riders as part of their proposed DSPs.

4 **Q. Do you believe the design of the rates set forth in the HP Rider is consistent with the**
5 **Commission’s default service regulations?**

6 A. Yes. For the reasons I previously explained, the hourly-priced service offered under the
7 HP Rider is consistent with the Commission’s regulations at 52 Pa. Code § 54.187(j) and
8 (k), other applicable provisions of those regulations, and the Commission’s prior approval
9 of the Companies’ customer class definitions and service offerings.

10 **Q. What is the Default Service Support (“DSS”) Rider and what costs will be recovered**
11 **through these Riders under this DSP?**

12 A. Each of the Companies has a DSS Rider in its respective tariff, which recovers various
13 categories of costs on a non-bypassable basis. The Companies’ DSS Riders recover four
14 categories of costs: (1) the uncollectible accounts expense incurred through the provision
15 of default service and on behalf of EGSs through the POR programs; (2) retail enhancement
16 costs for the CRP; (3) customer education costs; and (4) Non-Market Based (“NMB”)
17 Services Transmission Charges.³ In addition to those four categories, Penn Power’s DSS
18 Rider also recovers any FERC-approved Midcontinent Independent System Operator

³ NMB Services Transmission Charges include Federal Energy Regulatory Commission (“FERC”) approved costs for: (i) PJM Regional Transmission Expansion Plan (“RTEP”) charges; (ii) PJM Expansion Cost Recovery charges (“ECRCs”); (iii) PJM charges for Reliability Must Run (“RMR”) generating unit declarations and charges associated with plants deactivated on or after July 24, 2014; (iv) historical tie line, generation, and retail customer meter adjustments; (v) unaccounted for energy (“UFE”); and (vi) any other FERC-approved PJM transmission charges billed by PJM that will not be reconciled through the PTC Rider and/or HP Rider and as approved for recovery under the DSS Riders by the Commission.

1 (“MISO”) Transmission Expansion Plan costs, PJM Integration fees, and MISO exit fees
2 associated with Penn Power’s move from MISO to PJM.

3 **Q. Are the Companies proposing any changes to the DSS Riders?**

4 A. No. The Companies are not proposing to make any changes to the DSS Riders in this
5 proceeding.

6 **Q. Will the Solar Photovoltaic Requirements Charge (“SPVRC”) Rider remain in place
7 for the upcoming default service term?**

8 A. Yes. Met-Ed, Penelec, and Penn Power are not proposing any changes and will continue
9 to recover costs attributable to complying with solar AEPS requirements through Rider N,
10 the non-bypassable SPVRC Rider that applies to all delivery service customers. West Penn
11 does not have an SPVRC Rider and is not proposing one as part of its DSP.

12 **Q. Are the Companies proposing any modifications to their existing reconciliation
13 mechanisms?**

14 A. No. The Companies believe the mechanisms as already approved by the Commission in
15 prior proceedings to be appropriate and effective for continued application during the
16 upcoming default service term. The Companies recognize that there are open proceedings
17 at Docket Nos. L-2014-2421001 (Automatic Adjustment Clauses Related to Electric
18 Default Service) and Docket No. M-2013-2345492 (Section 1307(e) Reconciliation
19 Statement Pilot Program). The Companies will determine whether the outcome of those
20 proceedings requires a revision to their reconciliation mechanisms once final orders are
21 entered at those dockets and, if so, will make any necessary filings to effectuate those
22 changes at that time.

1 **IV. CUSTOMER REFERRAL PROGRAM**

2 **Q. Are the Companies proposing to continue the CRP as part of their DSPs?**

3 A. Yes. The Companies propose to continue the CRP market enhancement program as part
4 of this proceeding.

5 **Q. Are the Companies proposing any modifications to the CRP?**

6 A. Yes. The Companies are proposing limited changes to the Customer Referral Program
7 Agreement (“CRP Agreement”) between the Companies and participating EGSs.

8 **Q. What is the CRP Agreement?**

9 A. The CRP Agreement is the contract established between the Company and qualified EGSs
10 that wish to participate in the CRP. The CRP Agreement outlines the terms and conditions
11 to which a supplier must agree and meet in order to qualify to serve load through the CRP.

12 **Q. What modifications to the CRP Agreement are the Companies proposing as part of
13 this proceeding?**

14 A. First, the Companies are proposing to reduce the notice period for those EGSs (“CRP
15 Suppliers”) that have already participated in the program from 60 days to 30 days.
16 Reducing the notice period allows CRP Suppliers to see the PTC, which will be posted the
17 latter of forty-five days prior to the effective date or seven days after the last supply auction,
18 before committing to participate in the CRP. This differs from the CRP as designed today,
19 under which CRP Suppliers must notify their intent to participate before posting of the
20 upcoming quarter’s PTCs, while being allowed to rescind that intent after the quarter’s
21 PTC becomes approved.

1 Second, the Companies propose to assess an hourly rate for research required and legal
2 fees incurred to address customer complaints related to CRP Supplier activity that does not
3 follow Commission regulations or adhere to the terms and conditions of the CRP
4 Agreement. The Companies have recently experienced several situations in which a CRP
5 Supplier has failed to adhere to the CRP Agreement terms and conditions, requiring the
6 affected Company to expend valuable resources in order to research and correct the
7 deviation from the CRP terms of participation. This proposal allows the Companies to bill
8 CRP Suppliers for administrative and legal fees incurred rather than passing such costs on
9 to all customers. Met-Ed/Penelec/Penn Power/West Penn Exhibit KLB-1 reflects these
10 revisions to the CRP Agreement, which the Companies propose to be effective June 1,
11 2017.

12 **V. PURCHASE OF RECEIVABLES PROGRAM**

13 **Q. Please describe the POR program included in the Companies' Supplier Tariffs.**

14 A. Consistent with the Commission's Policy Statement at 52 Pa. Code § 69.1814, each of the
15 Companies agreed to provide, and the Commission approved, POR programs for
16 residential and small commercial accounts served by EGSs.⁴ Under each of the
17 Companies' existing POR programs, accounts receivable are purchased from participating
18 EGSs at a zero discount rate (meaning the Companies pay the face value of the account

⁴ See, *Joint Petition of Metropolitan Edison Company and Pennsylvania Electric Company for Approval of Their Default Service Programs*, Docket Nos. P-2009-2093053 and P-2009-2093054 (Opinion and Order approving settlement entered November 6, 2009) (Met-Ed and Penelec); *Petition of Pennsylvania Power Company for Approval of its Default Service Programs*, Docket No. P-2010-2157862 (Opinion and Order approving settlement entered November 17, 2010) (Penn Power); *Joint Petition of Metropolitan Edison Company, Pennsylvania Electric Company, Pennsylvania Power Company and West Penn Power Company for Approval of Their Default Service Programs*, Docket Nos. P-2013-2391368, *et al.* (Opinion and Order approving settlement entered July 24, 2014) (revising West Penn).

1 receivable regardless of what they are actually able to collect from customers), which
2 eliminates the risk to EGSs of uncollectible accounts expense associated with serving
3 residential and small commercial customers.

4 **Q. Do the Companies recover uncollectible accounts expense associated with their POR**
5 **programs through their tariffed rates?**

6 A. Not entirely. Allowances for uncollectible accounts expense were approved in the
7 Companies' recent base rate cases which split uncollectibles into a portion attributable to
8 distribution rates and a separate portion attributable to default service and POR rates, with
9 the default service/POR-related portion recovered through the Companies' DSS Riders.
10 The default service/POR-related portion of uncollectible accounts expense for each
11 Company is incurred, in part, as a result of the Companies' POR programs. However, the
12 Companies' uncollectibles have grown and continue to grow at a rate that exceeds their
13 ability to gain approval of revised allowances.

14 Met-Ed/Penelec/Penn Power/West Penn Exhibit KLB-2 reflects the growth in
15 uncollectible accounts expense by Company forecasted for 2015 as compared to the
16 allowance currently in rates as a result of the Companies' most recent base rate
17 proceedings. The Companies' forecasted 2015 uncollectible accounts expense has grown
18 to \$46.9 million – a significant increase over the \$33.3 million allowance reflected in rates,
19 representing a 41% increase.

1 **Q. Have the Companies identified any factors contributing to this growth in**
2 **uncollectibles?**

3 A. Yes. In analyzing this large increase in uncollectible accounts expense, the Companies
4 noticed several trends. First, the Companies identified a quickly growing trend in
5 increasing POR-related net write-offs since 2012, when they began tracking discrete
6 categories of write-offs. Specifically, the Companies' aggregate net POR-related write-
7 offs have grown from a total of roughly \$1.2 million in 2012 to a current year aggregate as
8 of September of over \$8.2 million. These figures are referenced in Table 1 below.

9 **Table 1: Annual Purchase of Receivable Net Write-Offs**

Year	Total EGS Write-Offs (\$)
2012	1,163,753
2013	3,115,549
2014	7,050,907
2015*	8,267,166

10 *As of September 30

11 At these levels, the Companies' POR-related write-offs account for an aggregated average
12 of 26.5% of total write-offs, with individual Company levels ranging between 23% and
13 29%. See Table 2 below.

14 **Table 2: Write-Off Analysis (July 2014-June 2015)**

	Distribution and Default Service Write-Offs (\$)	EGS Write- Offs (\$)	Total Write-Offs (\$)	EGS Write-Offs as a % of Total
Met-Ed	12,274,148	4,938,783	17,212,931	29%
Penelec	9,928,821	3,789,532	13,718,353	28%
Penn Power	1,989,929	586,581	2,576,510	23%

West Penn	8,494,352	2,474,018	10,968,370	23%
Total	32,687,250	11,788,914	44,476,164	26.5%

1
2 The Companies further identified a wide variance in percentages for EGS write-offs as a
3 percentage of generation revenues billed over a twelve-month period. For example, for the
4 twelve-month period ended June 2015, EGS write-offs as a percentage of revenues for Met-
5 Ed were on average 1.81%; however, the percentages by specific EGS varied from a low
6 of 0.04% to a high of 36.4%. Page 1, Column 3 of Met-Ed/Penelec/Penn Power/West Penn
7 Exhibit KLB-3 reflects these averages for each Company, while pages 2 through 4 of
8 Exhibit KLB-3 anonymously depict those EGSs whose write-offs exceed 150% of the
9 respective Company average. While these POR-related write-offs may not be the only
10 factor contributing to the growth of the Companies' uncollectibles, they are certainly a
11 significant one.

12 **Q. Are the Companies proposing any modifications to their POR programs to address**
13 **this problem?**

14 A. Yes. In order to address this disparity in EGS-related write-off percentages, the Companies
15 propose to collect a portion of this growing uncollectible accounts expense from EGSs;
16 specifically, those EGSs whose practices are driving higher write-offs as a product of the
17 types of offers they make to customers. Because collection is not an issue EGSs must
18 concern themselves with, the Companies believe that those EGSs with a higher percentage
19 of write-offs are unfairly burdening the Companies and their customers, through their
20 pricing practices, with disproportionately higher write-offs than their peers.

1 Such predatory pricing practices are not employed by the majority of those EGSs serving
2 in the Companies' territories, however. In fact, those EGSs identified in Exhibit KLB-3
3 represent only 30% of Met-Ed registered EGSs, 31% of Penelec's registered EGSs, 21%
4 of Penn Power's registered EGSs, and 18% of West Penn's registered EGSs for the same
5 period. Given this data, absent such POR revisions, all customers, shopping and non-
6 shopping alike, will continue to be saddled with the costs of excessive uncollectible
7 accounts expense associated with the business practices of a minority of EGSs that are
8 driving such costs.

9 **Q. How did you determine the appropriate amount to charge EGSs on an annual basis?**

10 A. First, it was important to identify a baseline of acceptable uncollectible levels associated
11 with EGS activity. Because write-offs are the primary driver of uncollectible accounts
12 expense, a review of EGS write-offs as a percentage of EGS billed revenues provides a
13 reasonable basis for comparison between EGSs participating in the POR program. As
14 discussed earlier, the results of this analysis for the Companies' EGS-related write-offs
15 clearly reflect that those EGSs with significantly higher write-offs are the same EGSs that
16 are charging variable rates with prices substantially above the PTC.

17 Once that baseline of typical behavior had been identified across all EGS write-offs, it
18 became clear that the Companies' EGSs write-off levels averaged between 0.76% to 1.81%
19 as a percentage of EGS revenues.⁵ From there, the Companies ultimately determined that
20 150% of the EGS average would serve as a reasonable and moderate standard against
21 which to measure all individual EGS write-off percentages. In applying this type of

⁵ Met-Ed: 1.81%; Penelec: 1.40%; Penn Power: 0.76%; West Penn: 0.89%.

1 standard, EGSs will be measured against their peers' actual activity, rather than by some
2 arbitrary and static standard.

3 **Q. Specifically, what mechanism are the Companies proposing to utilize to determine the**
4 **amount to charge EGSs with significantly higher write-offs and when will that**
5 **amount be billed to the affected EGSs?**

6 A. In order to be able to maintain the POR program for all EGSs serving residential and small
7 commercial customers, the Companies propose the addition of a clawback clause to their
8 POR programs related to EGS write-offs. Under this clause, an annual charge would be
9 assessed, beginning September 2016, to those EGSs that exceed 150% of the average
10 supplier write-offs as a percentage of revenue as calculated separately for each of Met-Ed,
11 Penelec, Penn Power and West Penn for each twelve-month period ending August 31st.
12 Because EGSs do not presently bear the risk that typically follows the decision to charge
13 exorbitant prices, they have no incentive to consider the uncollectible accounts expense
14 that may stem from their marketing strategies. As explained earlier, write-offs associated
15 with EGS accounts receivable balances are a significant contributor to the Companies' total
16 uncollectible accounts expenses. The charge would in effect serve as a disincentive to
17 those EGSs that offer customers unreasonable or variable rates that are likely to result in
18 higher write-offs for the Companies – costs which would eventually be passed along to
19 other customers in subsequent rate proceedings. To illustrate the significance of the value
20 of this proposal to the Companies and their customers, had such a mechanism been in place
21 for the period of July 2014 through June 2015, qualifying EGSs would have paid Met-Ed
22 \$2.2 million, Penelec \$1.7 million, Penn Power \$0.3 million and West Penn \$1.2 million,
23 or \$5.4 million in total. See Met-Ed/Penelec/Penn Power/West Penn Exhibit KLB-3 for

1 details. This procedure will reduce the Companies' (and thereby, customers') exposure to
2 unreasonable EGS-driven uncollectible accounts expense by providing a fresh source of
3 cost recovery from the EGSs benefiting from the PORs, while at the same time
4 incentivizing EGSs to consider the results of their pricing programs on a customer's ability
5 to pay. In turn, the revenues generated by this mechanism would accrue to customers over
6 time by reducing uncollectible accounts expense that would otherwise have to be collected
7 in the Companies' retail rates.

8 **Q. How would the Companies calculate the charge to those EGSs with write-offs that**
9 **exceed 150% of the average EGS write-offs as a percentage of revenues?**

10 A. EGSs would be charged the difference between their actual annual write-off amount and
11 150% of the respective Company's average annual EGS write-offs as a percentage of billed
12 EGS revenues. The charge would recover the amount of EGS write-offs over 150% of the
13 operating company average and would be billed to the EGS annually.

14 **Q. Why did the Companies base the charge to EGSs on write-offs that exceed 150% of**
15 **the average EGS write-offs?**

16 A. The Companies' proposed charge is intended to impact only those EGSs with excessive
17 write-offs over a twelve-month period. Although the Companies could have proposed to
18 bill out all charges greater than average EGS write-offs over a twelve-month period, the
19 Companies chose to take a conservative approach by assessing the charge only to those
20 EGSs with write-offs that are more than 150% of the overall average for Met-Ed, Penelec,
21 Penn Power or West Penn, as appropriate.

22

1 **Q. What would the Companies do with the amounts collected from EGSs?**

2 A. The Companies would retain the amount charged to EGSs if each individual Company's
3 actual uncollectible accounts expense is higher than the amount of uncollectible expense
4 in base rates plus the amount included in the DSS Rider for the twelve-month period ended
5 August 31st of each year. Alternatively, the Companies would refund the EGS charge to
6 customers through a reduction to their respective DSS Rider if the Companies' actual
7 uncollectible expense is less than the amount of uncollectible expense recovered in base
8 rates and the DSS Rider.

9 **Q. A reconciliation of uncollectible accounts expense is prohibited under provisions of**
10 **Section 1408 of the Public Utility Code, 66 P.S. § 1408. Is that what you are**
11 **proposing?**

12 A. No. Section 1408 eliminates the possibility of a full reconciliation of all revenues and
13 expenses associated with uncollectible accounts expense. My proposal consists of two
14 separate and distinct parts. In the first part, I am merely proposing a supplemental means
15 of cost recovery which would relieve customers of having to pay for the uncollectible
16 accounts expense driven by excessive EGS pricing proposals. The proposed uncollectible
17 accounts expense billing procedure and mechanism is clearly not a reconciliation of any
18 type and is thus, permissible under the Public Utility Code.

19 The second part of the uncollectible accounts expense cost recovery proposal merely seeks
20 to provide customers with the benefits of any collections obtained from EGSs by passing
21 back a portion of those collections under certain circumstances. In that way, the
22 Companies will not excessively collect uncollectible accounts obligations through the three

1 sources of cost recovery available: (1) distribution rates, (2) DSS Rider; or (3) EGS
2 uncollectible accounts expense billings. While some may view it as a partial reconciliation
3 because it compares revenues collected to total uncollectible accounts expense, the goal is
4 for the Companies to pass any extra revenue collections back to customers through the DSS
5 Rider when, and if, any excessive funding is recovered. This provision is designed to serve
6 as a customer protection from EGSs driving uncollectible accounts expense to
7 unreasonable levels. Because current rates reflect a much lower uncollectible accounts
8 expense, the Companies do not anticipate any refunds will be made to customers during
9 the initial operation of this EGS uncollectible accounts expense billing mechanism.

10 **Q. Are the Companies proposing any other modifications to the POR programs?**

11 A. Yes. Currently, EGSs serving customers under the Companies' PORs are providing
12 refunds associated with their service directly to the customer, rather than providing refunds
13 through the Companies' billing systems using the same mechanisms that apply charges to
14 the customers' billing statements. The Companies are proposing that EGS refunds under
15 the POR go directly to the Companies to apply to the customer's account balance first, if
16 necessary. Under today's practice, because a Company already would have paid the EGS
17 the billed amount under the POR and the Company's payment to the EGS is not contingent
18 upon the Company being paid by the customer, it is the Company from which the EGS
19 would have been paid. As a result, in many instances the Companies are learning from
20 their customers that although refunds are received by the customers, those refunds are not
21 being used to pay the Companies' bills, leading to collections and initiation of termination
22 efforts against many of these customers. The Companies' proposal would ensure that the
23 EGS refund is applied first to a customer's open account balance before refunding any

1 remaining amounts to the customer. The changes proposed to the Companies' Supplier
2 Tariffs to accommodate for this process are reflected in Met-Ed/Penelec/Penn Power/West
3 Penn Exhibits KLB-4 through KLB-7 to this testimony.

4 **VI. RELATED TARIFF MATTERS**

5 **Q. Do the Companies have any generation contracts to provide retail customers with**
6 **service in their respective service territories?**

7 A. No, they do not.

8 **Q. Do the Companies have time-of-use rates available for residential customers, as**
9 **required by Act 129?**

10 A. Yes. As approved by the Commission in the Companies' previous default service
11 proceedings (for Penn Power and West Penn) and recent base rate cases (for Met-Ed and
12 Penelec), each Companies' tariff now includes a Rider K, Time-of-Use Default Service
13 Rider, which offers residential customers time-of-use rates. The Companies are not
14 proposing any changes to those Riders as part of their DSPs.

15 **Q. What is the proposed effective date of the tariff changes described in your testimony?**

16 A. Changes to the Companies' supplier tariffs are proposed to become effective on or before
17 August 1, 2016, while the retail tariff changes are proposed to become effective on June 1,
18 2017, which is the start of the delivery period for the proposed default service term.

19 **VII. CONCLUSION**

20 **Q. Does this complete your direct testimony?**

21 A. Yes, it does.

Appendix A
Resume: Education and Experience of Kimberlie L. Bortz

Education:

Bachelor of Science Degree in Accounting - University of Maryland

Professional Certification:

Certified Public Accountant - Pennsylvania

Experience:

1989 – 1992	Senior Accountant - Deloitte & Touche
1992 – 1994	Senior Auditor - GPU Service Corporation
1994 – 1996	Financial Analyst - Metropolitan Edison Company
1996 – 1997	Sales and Marketing Team Lead - GPU Energy
1997 – 1999	Accounting Team Lead - GPU Advanced Resources
1999 – 2001	Comptroller - GPU Advanced Resources
2001 – 2004	Manager, Met-Ed Region Business Services - FirstEnergy Service Company
2004 – 2007	Manager, Customer Service Business Services - FirstEnergy Service Company
2007 – 2012	Director, PA Business Services - FirstEnergy Service Company
2012 – 2014	Accounting Lead, Financial Transformation Project - FirstEnergy Service Company
2014 – Present	Rates Advisor, Pennsylvania Rates and Regulatory Affairs - FirstEnergy Service Company

Prepared and presented testimony in the following rate-related cases:

Pa. P.U.C. Cases:

<i>Docket Nos.</i>	<i>Case Name</i>
R-2014-2428745	(Metropolitan Edison Company Base Rate Case)
R-2014-2428743	(Pennsylvania Electric Company Base Rate Case)
R-2014-2428744	(Pennsylvania Power Company Base Rate Case)
R-2014-2428742	(West Penn Power Company Base Rate Case)