BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Rulemaking Re Electric Distribution Companies' Obligation to Serve Retail Customers at the Conclusion of the Transition Period Pursuant to 66 Pa. C.S. § 2807(e)(2)	)	**Docket No. L-00040169**

COMMENTS OF DUQUESNE LIGHT COMPANY

Pursuant to the Commission's December 16, 2004 Proposed Rulemaking Order issued in the above-captioned docket, Duquesne Light Company ("Duquesne") submits the following comments regarding the proposed rules governing the obligation of electric distribution companies ("EDCs") to serve retail customers at the conclusion of their respective transition periods. Duquesne appreciates this opportunity to comment on the proposed regulations governing default service (currently referred to as "provider of last resort" ("POLR") service in the Commonwealth). Duquesne can offer a unique and informed perspective on the proposed regulations because of its extensive experience with post-transition period POLR service. Duquesne completed the transition period for most customers in 2002 and, since that time, has successfully implemented two post-transition period POLR programs.

I. DUQUESNE'S EXPERIENCE WITH POST-TRANSITION PERIOD POLR SERVICE

Duquesne entered its post-transition period earlier than any other major electric utility in Pennsylvania because of a successful generation auction that terminated the competitive transition charge ("CTC") in 2002 for most customers. Duquesne's first post-transition period POLR proposal was to obtain wholesale supply from the purchaser of its generation assets, Orion Power MidWest, L.P., the same entity that had provided wholesale supply during Duquesne's transition period. This program, which was known as "POLR II," evolved through a Commission-sponsored collaborative process and resulted in a settlement joined by both consumer and supplier groups. The POLR II rate plan approved by the Commission in December 2000 included a 14.4 percent increase in generation rates, but nevertheless provided retail customers with an average rate cut of 17 percent from the rates paid at the inception of competition due to the elimination of the CTC. *Petition of Duquesne Light Company for Approval of Plan for Post-Transition Period Provider of Last Resort Service*, Docket No. R-00974104 at 5-6 (Dec. 20, 2000) ("POLR II Order"). During 2002, approximately 23 percent of the load in the Duquesne service area received energy from electric generation suppliers ("EGSs"). The POLR II arrangement with Orion terminated on December 31, 2004.

With the expiration of the POLR II agreement approaching, Duquesne proposed a "POLR III" rate plan that bifurcated small customers (residential and small commercial and industrial customers) from large customers (commercial and industrial customers with greater than 300 kilowatts of demand). For small customers, Duquesne

proposed to obtain wholesale supply through a series of bilateral agreements and the purchase of a generation facility by its affiliate Duquesne Power, L.P. Duquesne proposed to offer small customers fixed rates for a six-year period, which would have brought Duquesne in line with the expiration of the transition periods for other EDCs in the Commonwealth. For large customers, Duquesne proposed two rate options: a fixed rate default service that would be supplied through an annual wholesale competitive procurement process, and an hourly service that would be supplied through markets organized by PJM Interconnection, LLC ("PJM").

After a hearing, the Commission approved, with modifications, the proposed POLR III plan. The Commission agreed to a three-year fixed price term for small customers that locked in rate savings of at least 15% since the commencement of competition. The Commission, however, reserved judgment on the final three years of Duquesne's small customer plan, holding that it "is possible that a second three-year term with a price adjustment as proposed will be adopted." *Petition of Duquesne Light Company for Approval of Plan for Post-Transition Period Provider of Last Resort Service*, Docket No. P-00032071 at 17 (Aug. 23, 2004) ("POLR III Order"). For large customers, the Commission approved an hourly-priced POLR default service, as well as a short-term fixed price service (17 months) that is being supplied through fixed price contracts procured through an RFP process.[1]

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[1] On reconsideration, the Commission extended the fixed price option for an additional 12-month price application period. *Petition of Duquesne Light Company for Approval of Plan for*

The POLR III Plan has resulted in a significant increase in shopping in Duquesne's territory. As of March 2005, shopping in Duquesne's service territory accounts for 46 percent of the retail load, double the level of shopping in 2002, and more than four times the level of shopping in the Pennsylvania utility with the next highest level of retail choice participation.

II. COMMENTS

A. Overview

Duquesne commends the Commission and the participants in the POLR roundtable on the development of proposed regulations that address important and difficult issues. Duquesne agrees with a large portion of the proposed regulations but is concerned that, in some instances, they may limit experimentation and flexibility in designing future default service plans. The Commonwealth has had only limited experience with post-transition period POLR service, and other jurisdictions are just beginning to implement post-transition default service. It is doubtful that any desired "end state" has been developed, much less implemented anywhere in the country. It is therefore important that the Commission not preclude experimentation and flexibility, particularly in the period prior to 2011 when all EDCs in the Commonwealth will have to implement post-transition period default service. This is of particular concern to Duquesne, whose successful plan for small customers was approved through 2007, with the possibility of an extension through 2010.

Post-Transition Period Provider of Last Resort Service, Docket No. P-00032071 at 23-24 (Oct.

To be sure, the proposed rulemaking recognizes the need for flexibility in many respects. The Commission stated that "retail and wholesale energy markets will continue to evolve between now and the expiration of the last of the EDC rate caps." Default Rulemaking at 6. The Commission also acknowledged the importance of ensuring that "regulations promulgated now be flexible enough to accommodate markets as they continue to evolve. . . . Consequently, the Commission seeks to avoid overly prescriptive language that may infringe on both its and all other interested parties' ability to manage the default service obligations." *Id.* Duquesne fully supports these statements, but offers comments on areas in which the proposed regulations appear not to meet this goal.

The need for additional flexibility is apparent in two primary areas. First, the Commission's regulations appear to suggest that the *only* way to procure power for POLR customers is through a wholesale competitive solicitation. Duquesne agrees that a competitive solicitation process is *one* reasonable way to procure power, but that does not mean it is the *most* reasonable method or that it will be reasonable under *all* market conditions. Indeed, in Duquesne's POLR III proceeding, the Commission explicitly recognized that "a competitive procurement process is not the exclusive method to arrive at a prevailing market price." Reconsideration Order at 26.

The second area of concern is the proposed rules regarding supplier gaming. By and large, the proposed rules regarding supplier gaming are drafted to permit creative

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5, 2004) ("Reconsideration Order").

methods of addressing these risks. But in certain circumstances, Duquesne suggests additional modifications that will clarify that EDCs have the flexibility to propose reasonable protections that balance the desire to allow customers to freely switch suppliers with the protections needed to ensure that default service can be provided at a reasonable cost.

Duquesne also provides limited comments on several other aspects of the proposed regulations. First, Duquesne addresses the composition of default service rates, including the elements of hourly service and the nature of the customer charge. Second, Duquesne proposes a number of additional changes to several sections of the proposed regulations that are intended to clarify them. Each of the comments provided by Duquesne are reflected in the attached black-line of the Commission's proposed rules.

B. The Commission Should Ensure that the Regulations Leave it Sufficient Flexibility to Approve Default Service Programs that Reflect Evolving Changes in the Market

1. Competitive Solicitations

The proposed rules provide that "each default service provider should have the option of proposing a default service implementation plan best suited to its service territory." Default Rulemaking at 10. This statement is followed, however, by the statement that an implementation plan must include a competitive procurement process for acquiring generation supply. *Id.* at 12. Duquesne does not oppose the use of competitive procurement processes; indeed, Duquesne proposed such a process for its

large customers in its POLR III plan. Duquesne does not believe, however, that it should be the *only* method for *all* circumstances.

Section 2807(E)(3) of the Electricity Generation Customer Choice and Competition Act ("Competition Act") provides that an EDC will "acquire electric energy at prevailing market prices to serve [a default] customer and shall recover fully all reasonable costs." 66 Pa. C.S. § 2807(E)(3). The legislature could have, but did not, specify a single method or test for establishing "prevailing market prices." The proposed regulations needlessly tie the Commission's hands, however, by equating prevailing market prices with prices realized as a result of a competitive solicitation, and in doing so ignore other available methods for discerning the prices that prevail in a given market. As discussed below, prevailing market prices may be established through benchmarking to other prices in the region, through a market price index formula, or through other means. While a competitive solicitation may be one appropriate way to determine prevailing market prices, it is certainly not the only way, and, under certain circumstances, may well be less preferable than other methods. Duquesne describes below the limitations of competitive auctions.

a) Competitive Solicitations Are Not Always Successful In Stimulating Retail Competition

Recent experience in neighboring jurisdictions demonstrates that competitive solicitations may not always "foster[] a robust retail market for electricity." Default Rulemaking at 5. In many cases, electric generation suppliers have been unable to compete in markets where wholesale auctions are used to determine default service rates

because the resulting prices fail to fully reflect associated retailing costs. The graph below, compiled from 2005 data, compares residential switching in Duquesne's service area with that of utilities in New Jersey, Maryland, and Massachusetts. As the graph demonstrates, Duquesne's residential switching levels are much higher than any of these other markets with mandatory competitive procurement processes. In fact, Duquesne's switching rate for residential customers exceeds that of the Maryland, New Jersey, and Massachusetts utilities combined.[2]

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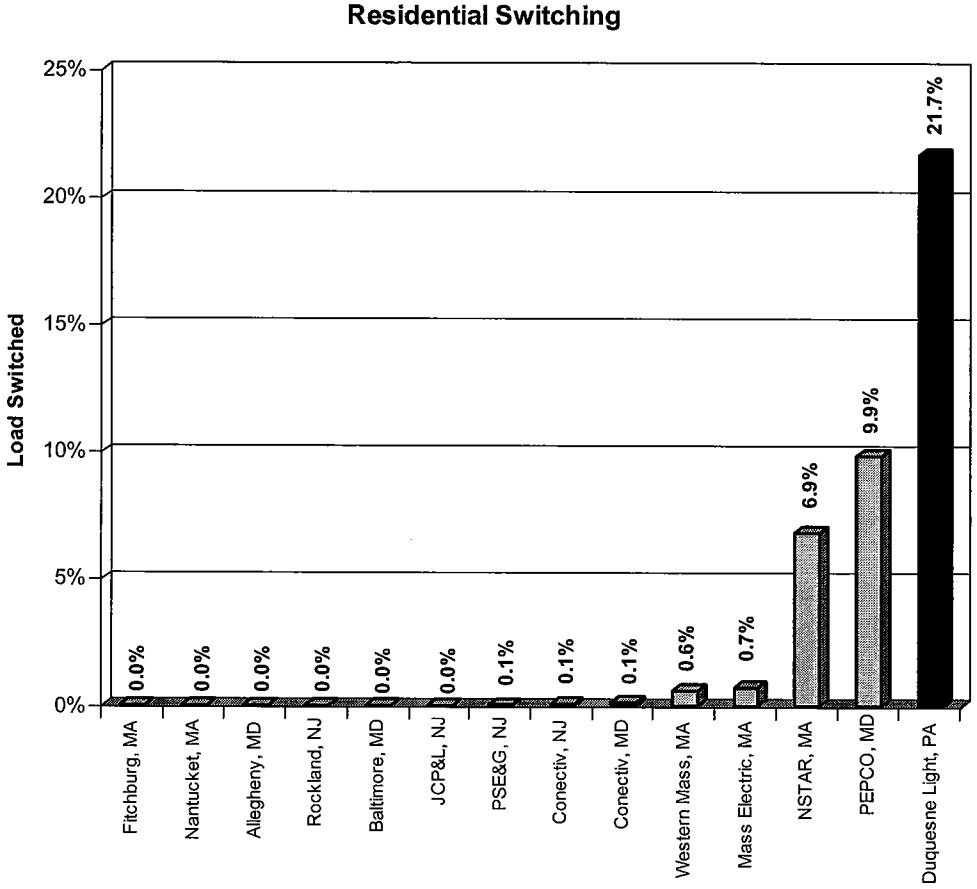
[2] This graph would be even more lopsided if special circumstances in Pepco's and NSTAR's service territories were not present. Two of the alternative retail suppliers in Pepco's region receive discounted wholesale supply from Mirant, the supplier of Pepco's Standard Offer Service. *See* Electric Choice Report 2003, Maryland Office of People's Counsel (July 2003). Switching in the NSTAR region is due to the Cape Light Compact, which serves as an aggregator and collectively purchases electricity for 21 towns. Customers are served by Cape Light rather than NSTAR unless they "opt-out" of the program. *See* http://www.capelightcompact.org.



Sources: 2005 customer switching data from various state utility commissions.

These results have caused electric generation suppliers to oppose wholesale competitive procurement processes in many jurisdictions. In a New York Public Service Commission proceeding, Green Mountain Energy asserted that auctions "eliminate the relationship between [EGSs] and end-use customers and can result in de facto price caps creating a barrier to a competitive supplier."[3] Direct Energy/Centrica

[3] Comments of Green Mountain Energy Company before the New York Public Service Commission at 4, Case 00-M-0504 (Mar. 24, 2004).

North America has taken the position that wholesale auctions foster the continued long-term role of the incumbent utility in the commodity business.[4] Others have argued that because default service rates based on wholesale auctions "do not account for many retail costs that mass marketers incur, there is insufficient headroom to cover acquisition costs and still leave room for savings."[5] The Small Customer Marketer Coalition and Mid-Atlantic Power Supply Association has argued that auctions give the default provider an undue advantage over retail suppliers.[6]

Duquesne does not necessarily endorse all of these views. However, it is important for the Commission to bear in mind that, although competitive auctions may have many virtues, they have, to date, proven less effective in stimulating retail competition than other methods of POLR service and, for that reason, are often opposed by retail suppliers. The Commission should recognize that POLR service inherently

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[4] Comments of Direct Energy/Centrica North America before the New York Public Service Commission at 5-7, Case 00-M-0504 (Mar. 22, 2004).

[5] Patrick Jeffrey, Direct Energy, Retail Energy Foresight at 3-4 (Feb/Mar/Apr 2005).

[6] "As a general matter, acquisition practices that depart from market based supply procurement, such as a utility sponsored auction, should not be employed. Currently utilities go into the marketplace and acquire supplies to meet the needs of their customers and their regulatory obligations. It is reasonable to assume that they will shop around to various wholesalers, determine what products are available in the market place and then make a reasonable purchasing decision. Given this existing structure, utilities can meet the needs of their customers without resorting to an auction process. The competitive standing of the [EGSs] and the utility should, to the maximum extent possible, be comparable and this can only be accomplished if they are both obligated to go into the market place to acquire supplies for their customers." Comments of The Small Customer Marketer Coalition and Mid-Atlantic Power Supply Association before the New York Public Service Commission at 25, Case 00-M-0504 (Mar. 23, 2004).

involves tradeoffs between several competing objectives – particularly facilitating retail competition and providing POLR power at reasonable prices. Competitive solicitations place a heavy premium on achieving the latter, but do not necessarily give equal weight to the former. The Commission should therefore leave open the possibility that the "prevailing market price" standard in the Act can be satisfied through methods other than competitive auctions.

b) Competitive Solicitations Do Not Always Produce Acceptable Results

In addition to the complaints of suppliers, regulators have often been dissatisfied with the prices that result from competitive solicitations. For example, in Maine, the state commission was authorized to conduct auctions on behalf of EDCs, but was given the authority to reject standard offer bids found not to be in the public interest.[7] In that event, the Legislature authorized the commission to direct utilities to provide standard offer service with power the utilities would purchase in the wholesale market. *Id.* When the initial auctions were conducted in late 1999, in most cases the bids received were either non-conforming or were significantly higher than pre-restructuring rates. *Id.* at 2-5. With the exception of Maine Public Service, a small utility in Northern Maine, the state commission rejected most of the auction outcomes, and the default service obligation was retained by the incumbent EDCs.

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[7] Summary of Standard Offer Bids for Central Maine Power Company, Bangor Hydro Electric Company and Maine Public Service Company at 1, Docket No. 99-111 (ME PUC Feb. 1, 2000).

In a subsequent auction attempt in late 2000, Bangor Hydro Energy ("BHE") and Central Maine Power ("CMP") again either received unacceptably high bids (in the range of 8.5 to 10 cents per kWh for BHE residential and small commercial customers and from 8.5 to 9.5 cents per kWh for medium non-residential CMP customers) that were rejected by the PUC or failed to receive bids for all customers.[8] The Maine commission concluded that bids "appeared to be inflated due to recent, substantial run-ups and volatility in natural gas prices as well as the market's response to a December Federal Energy Regulatory Commission (FERC) decision that set a deficiency charge for installed capacity (ICAP) significantly higher than had been expected. Because we believed both of these conditions to be transient, we concluded that accepting standard offer proposals at this particular point in time would not be in the public interest." *Id.* at 3. In September 2001 and January 2002, BHE and CMP finally received bids deemed appropriate given then-current market costs and successfully auctioned their standard offer service for all customer classes.[9]

The Public Utilities Commission of Ohio recently faced a similar situation. In December 2004, that commission rejected the results of FirstEnergy's wholesale auction

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[8] Summary of Standard Offer Bids for Central Maine Power Company, Bangor Hydro Electric Company and Maine Public Service Company at 1-6, Docket No. 2000-808 (ME PUC June 19, 2001).

[9] Order Designating Standard Offer Provider and Directing Utilities to Enter Entitlements Agreements, Docket No. 2001-399 at 1 (ME PUC Sept. 18, 2001).

for its retail electric load, opting to accept the utility's proposed rate stabilization plan.[10] There, the commission found that "it is clear at this time that the [rate stabilization plan ("RSP")] price is more favorable for consumers than the clearing price of the auction, which currently represents the best available market-based price to cover FirstEnergy's retail load. . . . We will analyze the process, procedure and substance of the auction, and will consider another auction next year for the remaining two years of the RSP." *Id.* at 4.

Duquesne is not arguing that auctions represent poor public policy, but these examples are provided to show that, *in certain circumstances,* auctions may not represent the optimum results for customers or regulators. Duquesne faced just such a situation when it prepared the POLR III Plan. The markets were sufficiently undeveloped and unstable that an auction was not appropriate for all customers. Instead, Duquesne successfully developed a fixed rate plan for small customers that nonetheless reflected prevailing market prices and the Commission approved that plan. POLR III Order at 22.

The proposed regulations, however, do not appear to leave the Commission or Duquesne any such flexibility particularly in 2007 when Duquesne's POLR III plan expires. It may be that a competitive solicitation will be appropriate at that time, but it

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[10] In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company for Approval of a Competitive Bid Process to Bid Out Their Retail Electric Load: Finding and Order, Case 04-1371-EL-ATA (PUCO Dec. 9, 2004).

may also be that other methods of setting POLR rates at prevailing market prices will be appropriate. Duquesne is particularly concerned that any auction conducted for supply beginning in 2008 will not include the remainder of the Commonwealth (because the rate caps of other large utilities do not expire until 2010-2011). As Duquesne experienced with its Large Customer plan in POLR III, a solicitation for Duquesne's area alone may not generate significant participation by wholesale suppliers. As reported to the Commission in confidential exhibits following the initial RFP, Duquesne received bids from only six suppliers, most of which offered to supply only a limited number of tranches. In addition, the bids received included a wide variation in price, with the highest price bid almost 100% above that of the lowest bid.[11] It is certainly possible that similar challenges may face Duquesne if it is forced to perform a competitive solicitation for its entire default service load in the near term. The Commission should therefore not preclude Duquesne from proposing another reasonable method for establishing "prevailing market prices."

c) Creditworthiness Can Undermine the Viability of an Auction

The success of a competitive solicitation also can be compromised when winning bidders' financial health and creditworthiness do not allow them to meet their commitments. The past few years have been unkind to wholesale electric marketers.

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[11] *See* RFP Compliance Filing, *Petition of Duquesne Light Company for Approval of Plan for Post-Transition Period Provider of Last Resort Service*, Docket No. P-00032071, Confidential Exhs. 4a & 4b (Oct. 2004).

During the fourth quarter of 2000, all but one of the twenty-five largest wholesale marketers had investment-grade credit ratings.[12] Since then, seventeen of those twenty-five marketers have suffered credit downgrades and eleven are now considered "junk rated" credit risks.[13] In some cases, wholesale suppliers that were obligated to supply utility retail load have filed for bankruptcy. For example, as part of its bankruptcy process, NRG Power Marketing Inc. attempted to void its supply contract with Connecticut Light and Power, thereby threatening the price stability of the utility's standard offer supply.[14] Mirant filed for Chapter 11 bankruptcy in July 2003 and indicated that it may have to renege on its default service deal with Potomac Electric Power Company ("Pepco").[15] In October 2003, Pepco agreed to pay Mirant a higher price for the supply and will seek to recoup over $100 million through Mirant's bankruptcy case.[16]

Wholesale suppliers participating in auctions also may seek additional protections that require retail customers to bear additional risks. Similar to the proposed

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[12] *See* Power Markets Week at 5 (Feb. 26, 2001) (marketer power rankings).

[13] *See* Bloomberg (Dec. 9, 2004) (credit ratings of parent corporations).

[14] *NRG Terminates CL&P Standard-offer Contract After Winning Judicial Go-ahead*, Power Markets Week at 12 (June 16, 2003). NRG's decision was overruled by FERC, *see Richard Blumenthal v. NRG Power Marketing, Inc.*, 103 FERC ¶ 61,344 (2003), and the parties recently entered into a settlement.

[15] Mirant Seeks to Renegotiate Some Supply Contracts with PEPCO, or Terminate Them, Electric Utility Week at 2 (Sept. 1, 2003).

[16] Mirant, Pepco Reach Power Purchase Deal, Associated Press (Oct. 27, 2003).

regulations in this docket, the rules in New Jersey and Maryland provide that if a wholesale supplier defaults during the contract period, the utility is allowed to recover incremental replacement costs from retail customers.[17] In Maryland, retail customers bear the costs associated with certain customer switching risks, as well as the risk of a failure to secure bids, the risk associated with auction pricing anomalies, and the risk of wholesale supplier default.[18] Many of these risks would otherwise be borne by the EDC on behalf of its default service customers in the absence of a competitive procurement process.

d) Other Methods of Establishing Prevailing Market Prices Also May be Appropriate

In addition to competitive solicitations, there are several other methods for determining prevailing market prices that may be appropriate under certain circumstances. Duquesne provides a few examples below.

(1) Duquesne's POLR III Plan

Duquesne's POLR III plan proposed a competitive solicitation for its large customers, but for small customers Duquesne did not believe that such an auction was appropriate. At the time, the wholesale market was experiencing volatility and several

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[17] *See, e.g.*, Public Service Elec. & Gas Co., Proposal for Basic Generation Service Requirements to be Procured Effective June 1, 2005 at 8, Docket No. EO04040288 (Nov. 2, 2004). Incremental supply costs are first covered by a defaulting supplier's credit security; customers are responsible for any costs in excess of this credit.

[18] Phase II Settlement Agreement, Case No. 8908 (MD PSC July 2, 2003); In the Matter of the Commission's Inquiry into the Competitive Selection of Electricity Suppliers/Standard Offer Service, Case No. 8908, Order No. 78710 (MD PSC Sept. 30, 2003).

wholesale suppliers were either in bankruptcy or had defaulted on supply obligations. Duquesne therefore developed a fixed rate offer for small customers that reflected prevailing market conditions, but did not expose customers to the risks of an auction at that time. During the Commission hearings, extensive review of the proposed prices was performed through a benchmarking process, *i.e.*, the Commission compared the prices proposed by Duquesne with retail prices developed in other jurisdictions. The Commission ultimately concluded that Duquesne provided sufficient market evidence to demonstrate that the proposed default service rates represented prevailing market prices for the first three years. *See* Reconsideration Order at 26 ("we relied on the record evidence to determine that the proposed rates reflected prevailing market prices for energy for a three-year term"). Importantly, the Commission ruled that it "is possible that a second three-year term with a price adjustment as proposed will be adopted." POLR III Order at 17.

The Commission, by adopting a strict competitive-solicitation-only rule, could foreclose the possibility that such a case may be made again in the future. Particularly for the bridge period between 2008 and 2010 when the remainder of the EDCs are completing their transition periods, the Commission should allow itself flexibility to approve a default service implementation plan that is appropriate for the circumstances then present in Duquesne's service territory. Duquesne respectfully requests that the Commission reaffirm the decision it entered in Duquesne's POLR III Order to leave open the possibility of a second three-year small customer rate plan that is based on benchmarked prices.

(2) Market-price index formulae

Another possibility for determining reasonable default service rates that reflect prevailing market prices is linking such rates with a market-price index formula. During the POLR III proceeding, Duquesne (as well as other parties) proposed market-price index formulae to establish prevailing market prices for small customers.[19] And the Commission approved an hourly-priced POLR default service for large customers in that case that was based on *one* form of market price index formula. POLR III Order at 32. Similarly, other longer-term (annual and multi-year) market-price index formulae based on forward prices may be used to establish prevailing market prices and already exist elsewhere in the United States. Various versions of this market index model have been implemented around the country, including for New York State Electric & Gas,[20] Rochester Gas & Electric,[21] the State of Illinois,[22] and the State of Texas.[23]

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[19] *See* Duquesne St. No. 2-R at 11-14, Docket No. P-00032071 (Mar. 17, 2004)

[20] NYSEG offers customers fixed retail rates for a two-year period based on forward electric prices. Joint Proposal, Petition of New York State Electric & Gas Corporation for Approval of its Electric Price Protection Plan at 32-33, Case 01-E-0359 (NYPSC Jan. 2002).

[21] RG&E offers customers fixed retail rates for one year based on forward electric prices. Electric Rate Joint Proposal, Proceeding on Motion of the Commission as the Rates, Charges, Rules and Regulations of Rochester Gas and Electric Corporation for Electric Service at 15-17, Case 03-E-0765 (NYPSC Mar. 9, 2004).

[22] Illinois utilities offer non-residential customers a power purchase option service based on a forward market index. Both residential and non-residential customers that shop receive a market value energy credit based on a forward market price formula. Commonwealth Edison Company Retail Tariff, Rider PPO Power Purchase Option – Market Index, Tariff Sheet at 151.1-15.

For example, default retail customers in Texas were assigned to an unregulated retail affiliate of the EDC in 2002, thereby causing the EDC to exit the commodity business altogether. These retail affiliates continue to charge price-to-beat ("PTB") rates tied to a market price index subject to the Texas commission's approval. In the second phase beginning January 1, 2007, these PTB rates will expire, at which time all retail electric rates, including default rates, will be set by individual retail suppliers without regulatory intervention. The New York Commission recently adopted a similar long-term goal for New York – the elimination of the EDC from the commodity business after a transition period. Although Duquesne does not endorse applying the Texas model in Pennsylvania at this time, Pennsylvania may learn important lessons when PTB rates expire at the end of 2006 about the feasibility of having retail suppliers establish prevailing market prices. If the Texas experiment proves successful by both facilitating retail competition and treating customers fairly, and if such a model is demonstrated to be consistent with the Competition Act, the Commission may wish to consider this type of default service program in the future. Its default service regulations therefore should not prevent the Commission from doing so.

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[23] Senate Bill 7, the Texas electric restructuring law, specified that a retail affiliate of the incumbent utility must provide "Price to Beat" (PTB) service. PTB is comprised of a non-fuel "base rate" plus a fuel factor. While the base rate is frozen, the fuel factor is subject to an adjustment mechanism linked to natural gas prices that allows the PTB provider to raise the fuel factor twice per calendar year. Duquesne has explained in the past that the particular market-price formula developed in Texas suffers several design flaws that have resulted in sizeable rate increases for small customers.

For all the reasons discussed above, Duquesne urges the Commission not to limit itself to the particular default service models identified in the proposed rulemaking. In its order, the Commission stated that it had a choice between a "retail POLR model" (in which the default service obligation is auctioned off) with the model ultimately adopted, implying that these are the only two options. Default Rulemaking at 8. However, there are other possibilities – including Duquesne's POLR III model and the market price index model -- that may prove attractive to the Commission given the passage of time and more experience. The Commission should therefore adopt the modifications to the proposed regulations set forth in Attachment A. These revisions would merely authorize the Commission to approve an alternative procurement process if the default service provider demonstrates that such alternative process will result in electric service supply that reflects prevailing market prices. This approach gives the Commission the flexibility necessary to approve an alternative if circumstances warrant one.

2. Switching Rules

Similar to Duquesne's comments with respect to competitive solicitations, Duquesne respectfully requests that the Commission preserve the flexibility to approve default service implementation plans that include reasonable mechanisms designed to prevent gaming of default service and protect the default service provider from subsidizing competition.

The Commission addressed the issue of gaming in three sections of the proposed regulations. First, the subchapter on competitive safeguards sets forth standards for the

return of retail customers to default service. These standards allow an EGS to transfer a customer to default service only if the EGS has abandoned its license, the retail customer has not paid its bill, the retail customer was inadvertently switched to the EGS from default service, or upon the "normal expiration of contracts that are not structured in a way to exploit seasonal variations in market prices." Section 54.123(a). Second, the Commission has proposed in section 54.187(g) that default service implementation plans may "include mechanisms that allow default service providers to adjust their prices during the term of service to recover reasonable, incremental costs of significant changes in the number of default service customers." Finally, the Commission proposed four subsections in section 54.189 that nominally address customer migration. Two of these subsections, relating to the customer's right to depart and return to default service, are applicable only if the customer complies with all Commission regulations. *See* Section 54.189(b) and (d). These provisions thus presumably do not apply if a switch is made for the purpose of exploiting seasonal variations in market prices. Another subsection is identical to a provision in the Competition Act. *See* Section 54.189(c) (requiring a default service provider to treat a customer departing EGS service as it would a new applicant for default service). The final section forbids a default service provider from charging a fee to a retail customer that departs default service. *See* Section 54.189(e).

The Commission's rulemaking order clarifies that the proposed regulations "do not provide for restrictions on the ability of customers to move from default to competitive service, and vice versa." Default Rulemaking at 22. The Commission

further noted that it "decline[s] to endorse restrictions such as minimum stay provisions or switching fees at this time. We conclude that these proposed regulations give default service providers the flexibility to effectively manage the risks associated with customer migration without restricting choice." *Id.*

Duquesne interprets the Commission's regulations on switching to encourage the development of customer migration policies that are appropriate to each service territory. Indeed, the Commission stated that it "does not intend to endorse any particular mechanism, and will allow the default service provider to propose reasonable methods of managing this risk [of customer migration]." Default Rulemaking at 19. At the same time, the Commission acknowledged that customer migration mechanisms currently in use elsewhere, such as seasonal rates, may be appropriate. *Id.* Duquesne supports the Commission's decision to welcome these innovations but to withhold judgment until a specific default service implementation plan is before it. This approach is particularly appropriate for switching rules because the need for customer migration mechanisms depends on the nature of default service options proposed as well as the level of switching in a particular service area.

Duquesne is concerned, however, that certain overly prescriptive language in the rulemaking order may leave the Commission insufficient flexibility to adopt mechanisms that are proven to be necessary and appropriate under the circumstances. As the Commission is aware, it has concluded in other cases that minimum stay provisions and generation rate adjustments can be appropriate under certain circumstances. For example, in mid-2000, the Commission issued a final order

addressing its "concern over the economic impacts on EDCs of short-term returns of C&I customers to PLR service during high-cost periods." *Guidelines Addressing Return of Customers to Provider of Last Resort Service*, Docket No. M-00960890F0017 (June 22, 2000). There, the Commission "suggested that EDCs who are exposed to that activity might submit proposals for 12-month 'stay provisions'" and further "proposed a generation rate adjustment (GRA) mechanism that should be offered by EDCs to afford C&I customers increased flexibility in gaining access to the competitive supply market following a return to PLR service." *Id.* The Commission soon thereafter approved such a proposal when it adopted a GRA mechanism, as well as a twelve-month minimum stay requirement as an alternative to the GRA, for West Penn Power Company. *Pennsylvania Public Utility Commission v. West Penn Power Company*, Docket No. R-00005538 at 4, 8-9 (February 8, 2001). They also were approved for Duquesne in the context of its POLR II plan. POLR II Order at 10-11.

These protections have proven to be not only effective in precluding gaming, but also in facilitating shopping. Customer shopping *increased* in Duquesne's territory *after* the minimum stay and GRA rules were adopted during POLR II. Furthermore, these types of protections have the advantage of preventing gaming *before* it occurs, rather than relying on after-the-fact detection to remedy abuses. Indeed, the rules in POLR II were adopted only after it became clear that the case-by-case approach adopted in Duquesne's restructuring processing had failed.

Very few changes to the proposed regulations would be necessary to implement Duquesne's recommendation. Nearly all of the proposed regulations preserve the

leeway that the Commission stated was important in granting "default service providers the flexibility to effectively manage the risks associated with customer migration." Default Rulemaking at 22. Duquesne suggests that the Commission amend proposed Section 54.189(e) to provide that the Commission may approve an exit fee if the EDC demonstrates that such a fee is consistent with the Competition Act under the circumstances. *See* Attachment A. Duquesne also respectfully requests that the Commission decline in the final rule to rule out a minimum stay or GRA if such mechanism is proven to be necessary or appropriate in the context of a specific default service implementation plan.

Finally, Duquesne notes that the proposed standards in Section 54.123(a) leave a number of questions unanswered. Duquesne recommends that the Commission permit default service providers to provide in their default service implementation plans additional clarifications that will enable the standards to be implemented without unnecessary confusion or litigation. For example, Duquesne expects that default service providers will suggest further details governing how they will determine whether a transfer is upon the "normal expiration" of a contract that isn't structured to exploit seasonal variations in market prices. Such details accordingly would explain the circumstances under which the default service provider will decline an EDI transaction that does not comply with the Commission's rules. A default service plan also may indicate that license revocation is among the penalties that may be applicable to EGSs that violate the Commission's standards. Finally, default service providers may indicate that violations of the standards will prompt expedited procedures and cost recovery

mechanisms to ensure that the default service provider is not financially harmed by prolonged litigation regarding gaming disputes. Duquesne requests that the Commission clarify that such additional details may be submitted in default service implementation plans.

C. The Regulations at § 54.187 Governing Default Service Rates Should be Amended

1. The Commission Should Clarify that Hourly Rates Include a Customer Charge and Renewable Charge

Section 54.187(a) of the proposed regulations provides that the costs for providing default service shall be recovered through three charges – the generation supply charge, the customer charge, and an automatic energy adjustment charge that recovers costs of compliance with the Alternative Energy Portfolio Standards Act ("alternative energy charge"). The next two subsections address fixed rate options. *See* §54.187(b) and (c). Subsections (d) and (e) regulate hourly priced service, and identify the "rate" for hourly priced service as including energy, capacity, ancillary services, taxes and other identified costs. These sections do not explicitly state, however, that hourly priced service rates may include the customer charge and the alternative energy charge. Duquesne assumes that this was an oversight in drafting, and that the Commission does not intend to exclude costs recoverable through the customer charge or the alternative energy charge from recovery from customers who opt for hourly service. Duquesne's requested language clarification is set forth in Attachment A.

2. The Nature of the Customer Charge

The proposed rule states that functions such as "billing, meter reading, collections, uncollectible debt, customer service . . . may be more appropriately recovered through default service rates than distribution rates." Default Rulemaking at 16. Therefore, the proposed regulations include the costs of these functions within the customer charge. *See* Section 54.187(a)(2)(i). Because the Commission is aware that EGSs do not currently provide many of these customer care functions, it acknowledged that shopping customers still would need to receive these services from the default service provider. The Commission therefore stated that the default service provider "can recover these costs through a modified customer charge that recovers the costs for those specific customer care services being provided to shopping customers." Default Rulemaking at 17 (emphasis added). The Commission would expect a "near corresponding drop in distribution rates" as a result. *Id.* No further detail was provided regarding the ratemaking process necessary to develop the customer charge or the "modified customer charge."

Neither the intent behind, nor the precise scope of, this proposal is clear. It appears that the "customer charge" is intended to reflect all customer care costs, while the "modified customer charge" would only recover customer care costs provided to shopping customers. In effect, the difference between these two customer charges would represent the dollars that a customer could avoid paying the default service provider if it shopped and took service from an EGS who provided a specific customer care service. In other words, the difference between the two customer charges would

represent the "price-to-compare" for customer care services. Given that not all EGSs perform the same customer care functions (*e.g.*, generation billing) and costs vary by rate class, Duquesne assumes under the Commission's proposed regulations that the "modified customer charge" and "price-to-compare" would have to be broken out into separate charges for each customer care function and rate class. In effect, this would require the unbundling of all these functions. Duquesne does not believe that unbundling these functions is appropriate at this time. Accordingly, Duquesne recommends that the Commission delete Section 54.187(a)(2)(i) from the customer charge. Even if it was appropriate to unbundle the customer care functions, it is far from clear that it can be done accurately without lengthy, contentious, and cumbersome litigation. After a discussion of why unbundling is premature, Duquesne provides below an explanation of the complexities involved in such an undertaking.

a) Unbundling the Customer Charge Is Not Necessary or Appropriate at this Time

The costs to be recovered in the customer charge are inappropriate candidates for unbundling. Current regulations do not require EGSs to perform many of the customer care functions identified in the proposed regulation (*e.g.*, meter reading and billing). Each of them is being performed by Duquesne (and the other EDCs) and each of them is recovered through distribution rates. Though that could change, it has not yet changed in Duquesne's service territory. Further, uncollectible debt and collections for EGSs, to the extent they exist, are wholly unlike the uncollectible debt and collection costs faced by EDCs. As recognized in proposed section 54.123(a), a shopping customer that fails

to pay its EGS bill can simply be returned to default service by the EGS. Unlike a default service provider, an EGS can choose which customers it wishes to serve, and avoid taking on a customer with bad credit. Moreover, an EGS can protect itself by requiring customer deposits and including more flexible cancellation provisions than Duquesne can under state law. It is therefore questionable whether EGSs face these costs at all, while default service providers continue to bear them in the same fashion as before passage of the Competition Act.

If the proposed regulations are adopted, Duquesne would need to develop the "modified customer charge" suggested by the Commission to encompass the customer care costs currently provided by Duquesne and not provided by EGSs. To avoid shopping customers bypassing those costs, the modified charge would need to be assessed to all customers, shopping and default. Presumably, that charge would simply reallocate customer care costs currently recovered in distribution rates to the new "modified customer charge." Thus, the purpose of the "modified customer charge" under current conditions is unclear because it will have the same effect as if customer care costs remained in distribution rates. Under current conditions, therefore, the Commission's regulations are unnecessary and inject needless confusion into the default service ratemaking process.

b) The Unbundling Process Will Be Lengthy and Difficult if the Commission Attempts it.

If the Commission, however, requires EGSs to perform customer care functions in the future for shopping customers, and those customers would therefore be entitled to

bypass some portion of the default service provider's customer charge, the default service provider and the Commission would need to undertake a proceeding to determine the default service provider's net incremental costs avoided by the EGS's assumption of a particular customer care function under alternative situations. This process is extremely complex and has taken *years* in other jurisdictions where it has been attempted.[24] We offer in the margin just a few examples of the complex cost quantification and allocation questions raised in such an undertaking.[25]

A customer billing system is perhaps the best example of the difficult problems involved with unbundling customer care functions. Though the incremental cost of providing one customer's bill is minute – measurable in the ink necessary to print it and

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[24] *See, e.g., In the Matter of Competitive Opportunities Regarding Electric Service*, Case 94-E-0952 *et al.,* 168 P.U.R. 4th 515 (NYPSC 1996); *see also* Order Establishing Regulatory Policies for Competitive Metering, 181 P.U.R. 4th 324 (NYPSC 1997); Order Providing for Competitive Metering (NYPSC June 16, 1999); Order Denying Petitions for Rehearing and Clarifying June 16 Order (NYPSC Sept. 15, 1999); Order Concerning Competitive Metering (NYPSC Jan. 31, 2001); Order Adopting Practices and Procedures Manual for the Provision of Electric Metering in a Competitive Environment (NYPSC Feb. 26, 2001); *see also* Report of NYPSC Competitive Metering Staff Team, 2001 WL 1131885 at *2 (May 29, 2001) (noting that the competitive metering collaborative in New York lasted "several years").

[25] For example, there are numerous methods that may be used to unbundle costs and many factors that influence the process. Costs may be measured on the basis of embedded costs (the total costs incorporated in regulated rates), the competitive market price of the service (what suppliers will charge), incremental costs (the cost of providing one unit of service), avoided costs (the decrease in the EDC's costs), net avoided costs (the decrease, minus new EDC costs incurred due to another supplier providing the service), or de-averaged net avoided costs (differentiation of avoided costs by customer class, density, location, etc.). Moreover, some costs are avoidable and others are not. Within avoidable costs, some costs are direct (assignable) and others are indirect (non-assignable), and within each of these categories, some costs are variable, semi-variable and fixed. Most costs, however, are not avoidable by the EDCs if a small number of customers switch to an EGS or if the EDC has to stand ready to

the postage necessary to mail it -- the cost of an entire billing system encompasses the software and hardware necessary to run it, the personnel necessary to staff it, as well as numerous other costs. It is not possible to accurately separate these costs by small subsets of customers. Any attempt to do so likely will result in stranded costs.

Finally, it is critical that EDCs maintain the integrity of the metering, billing and customer service processes, and it is questionable whether such integrity can be maintained if these processes are fragmented among various parties. If the Commission decided to make these services competitive, it would need to develop standards and protocols related to safety, reliability, and accuracy first in order to protect consumers.

In any event, few EGSs in the United States have shown an interest in providing metering and billing on a competitive basis in a manner that would allow the EDC to avoid having to maintain the necessary infrastructure to provide these services. If there were significant competition in the provision of these services, it would make sense from a policy perspective to unbundle them from distribution rates. Until there is, the Commission should adhere to the approach it adopted in Duquesne's restructuring case and keep these costs in distribution rates.[26] Section 54.187(a)(2)(i) of the customer charge should be eliminated from the proposed regulations.

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provide these services if customers return. These include sunk costs, plant and capital investment costs, and infrastructure costs.

[26] In Duquesne's restructuring case, the Commission held that these costs should remain in distribution rates. *Application of Duquesne Light Company for Approval of Its Restructuring Plan Under Section 2806 of the Public Utility Code*, Docket No. R-00974104 at 256 (May 21, 1998) ("we note that the mere fact that we can unbundle billing services does not mean that we

c) The Remaining Costs Recovered Through the Customer Charge Should Be Clarified.

The remaining costs set forth in the proposed regulations for recovery through the customer charge should be clarified. First, the Commission should clarify that the costs of performing a competitive solicitation and prosecuting the default service plan at the Commission are administrative expenses properly recovered through the customer charge. These costs are directly related to the provision of default service, and do not come within the costs identified for recovery through the generation supply charge or the alternative energy charge. They should be explicitly recognized in the customer charge subsection. Second, the reference in the customer charge provision to a "reasonable return or risk component for the default service provider" should be clarified to refer to the provision of default service. It is possible to read the proposed regulations as authorizing a return on the customer care costs in the preceding subsection, rather than a return or risk component for the provision of default service generally. The Commission should adopt the clarification proposed by Duquesne in Attachment A.

III. Clarifying Changes

In Attachment A, Duquesne has proposed a number of additional changes that are offered to clarify the regulations.

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should unbundle those services"); *see id.* at 261 ("[n]othing in the record of this proceeding suggests that metering should be unbundled in Duquesne's service territory at this time").

A. Definitions

The definition of default service states that it is the service provided to retail customers that do not choose an EGS or who contract for energy from an EGS but who do not receive such energy. Duquesne recognizes that this terminology is taken from the Competition Act (at § 2807(E)(3)), but technically, if an EGS commits to provide energy but does not deliver it in the normal course of business, energy will be delivered to the customer "from" the EGS in the form of imbalance energy administered by PJM. Only if the customer is returned to default service through electronic data interchange protocols is the customer receiving default service from an EDC. Duquesne's proposed clarification makes that clear. *See* Attachment A.[27]

The definition of competitive procurement process implies that only a default service provider can conduct the process. This is contrary to the proposed regulations (at § 54.186(c)) in which the Commission permitted a third party to implement the competitive solicitation. Duquesne's proposed language leaves open the entity performing the competitive solicitation process.

The definition of fixed rate option includes a reference to the possibility that a fixed rate may not be fixed throughout the term but may vary based on seasonal variations. Duquesne's proposed clarification adopts the approach in section 54.187(g) in which the Commission recognized that a default service plan may include mechanisms (including, but not limited to seasonal rates) that would allow a fixed rate

to adjust to reflect the incremental costs of customer migration and other potential events.

Duquesne has proposed a definition of "reasonable costs" that provides further detail regarding how the Commission will interpret this critical term. In addition to using this term generically (*e.g.*, "The EDC shall fully recover all reasonable costs for acting as a default service provider of electricity"), the Commission has used the term in situations in which an approved default service implementation plan does not result in a reliable generation supply source, as when a supplier defaults or when a competitive solicitation plan does not produce satisfactory results. In those settings, the Commission has authorized the default service provider to acquire supply at prevailing market prices and recover "reasonable costs," which is a term used in the Competition Act but not defined there. Duquesne proposes to define it as:

> The costs of providing default service to retail customers, which shall include (i) identifiable costs; (ii) reasonable estimates of difficult-to-quantify costs; and (iii) a return commensurate with any risks that the EDC may assume to provide default service.

Clarity with respect to the term "reasonable costs" will simplify the process of cost recovery in case these events occur, and will prevent needless debate regarding the cost components eligible for recovery. The Commission should adopt Duquesne's proposed definition. The Commission also should accept Duquesne's proposal to eliminate the term "reasonable costs" in sections of the regulations where costs are more clearly

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[27] Duquesne made the same type of suggestion with respect to Section 54.181. *Id.*

defined. For example, in 54.187(a)(1), the Commission clearly defines the elements of the generation supply charge. There, Duquesne proposes to use the term "costs" rather than "reasonable costs" because the Commission has provided sufficient specificity regarding the cost build-up for that charge.

B. Section 54.184

Proposed section 54.184(c), which identifies the obligations of a default service provider, places the obligation to maintain universal service programs on the default service provider. Because funding for universal service programs is currently recovered through distribution rates, it is unjust and unreasonable to shift the obligation to maintain a universal service program to a default service provider (assuming the default service provider is not the incumbent EDC) without also shifting the funding for such program. Duquesne respectfully requests that the Commission require EDCs to retain the universal service obligation and that EDCs continue to recover these costs in their distribution rates.

C. Sections 54.186(g) and 54.187(i)

In Sections 54.186(g) and 54.187(i), the Commission proposed identical processes for obtaining interim replacement supply when a procurement process does not result in sufficient supply or a supplier defaults. In both cases, the default service provider is authorized to acquire supply at prevailing market prices and fully recover all reasonable costs associated with that activity. The prevailing market price for purposes of these sections is "the price of electricity in the RTO or ISO's administered energy markets." *Id.* No further detail is provided regarding the process by which rates will be

adjusted to reflect these costs or what standard will be applied to determine whether the acquisition strategies of the default service provider were acceptable.

Duquesne is concerned about the absence of critical details in these provisions. While it may not be possible to set forth a standard rate adjustment mechanism in the proposed regulations, at a minimum the Commission should amend the regulations to provide that default service implementation plans may include an automatic rate adjustment mechanism to recover the costs incurred by the default service provider in the event that a procurement process does not result in sufficient supply or a supplier defaults. *See* Attachment A. Duquesne proposes that the Commission require an informational filing by a default service provider that invokes a rate adjustment mechanism approved pursuant to these sections.

D. Section 54.187

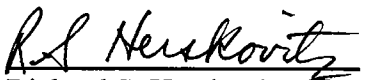
Proposed section 54.187(h) reflects the Commission's view that absent unforeseen, extraordinary circumstances, default service rates are not subject to review and reconciliation. The Commission noted that its proposed regulations "are intended to allow the necessary flexibility for default service providers to manage their risk prospectively." Default Rulemaking at 19. Duquesne's proposed revision to this section would add that element of flexibility in the regulation by allowing the Commission to approve, in a default service implementation plan, further detail regarding the types of circumstances under which reconciliation of default service rates would be permissible. This revision to the proposed regulation would permit, for example, a volumetric rate mechanism that would adjust rates to more appropriately reflect the default service

provider's increased costs of obtaining supply if there is a material shift in customer migration. It would also allow the default service provider to specify the types of unforeseen circumstances that could dramatically affect costs within its service territory. These circumstances potentially could include supplier default, material changes in law or taxes, or significant changes in PJM rules. Without listing specific events in the regulations, Duquesne's proposed revision would give the Commission the flexibility to approve such a provision as part of a default service implementation plan.

IV. CONCLUSION

Duquesne appreciates this opportunity to comment on the proposed regulations. With the modifications suggested above, Duquesne believes the regulations will continue the Commission's responsible movement toward meaningful retail competition for all retail customers in the Commonwealth.

Respectfully submitted,



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April 27, 2005

ATTACHMENT A

TITLE 52. PUBLIC UTILITIES
PART I. PUBLIC UTILITY COMMISSION
Subpart C. FIXED SERVICE UTILITIES
CHAPTER 54. ELECTRICITY GENERATION CUSTOMER CHOICE
Subchapter A. CUSTOMER INFORMATION

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§54.4. Bill format for residential and small business customers.

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(b) The following requirements apply only to the extent to which an entity has responsibility for billing customers, to the extent that the charges are applicable. The [provider of last resort] default service provider will be considered to be an EGS for the purposes of this section. Duplication of billing for the same or identical charges by both the EDC and EGS is not permitted.

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§ 54.5. Disclosure statement for residential and small business customers

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(b) The EGS shall provide the customer written disclosure of the terms of service at no charge whenever:

* * * * *

(3) Service commences from a [provider of last resort] default service provider.

(c) The contract's terms of service shall be disclosed, including the following terms and conditions, if applicable:

* * * * *

(9) The name and telephone number of the [provider of last resort] default service provider.

* * * * *

(h) If the [provider of last resort] default service provider changes, the new [provider of last resort] default service provider shall notify customers of that change, and shall provide customers with their name, address, telephone number and Internet address, if available.

§54.6. Request for information about generation supply.

(a) EGSs shall respond to reasonable requests made by consumers for information concerning generation energy sources.

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(2) The [provider of last resort] default service provider shall file at the Commission the annual licensing report as required by the Commission's licensing regulations in this chapter and shall otherwise comply with paragraph (1).

Subchapter B. ELECTRIC GENERATION SUPPLIER LICENSING

§54.31. Definitions.

* * * * *

[Provider of last resort] Default service provider – [A supplier approved by the Commission under section 2807(e)(3) of the code (relating to duties of electric distribution companies) to provide generation service to customers who ~~contracted for electricity that was not delivered, or who~~ did not select an alternative electric generation supplier, or who are not eligible to obtain competitive energy supply, or who return to the provider of last resort after having obtained competitive energy supply] The incumbent EDC within a certificated service territory or a Commission approved alternative default service provider.

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§54.32. Application process.

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(h) An EDC acting within its certificated service territory as a [provider of last resort] default service provider is not required to obtain a license.

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§54.41. Transfer or abandonment of license.

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(b) A licensee may not abandon service without providing 90 days prior written notice to the Commission, the licensee's customers, the affected distribution utilities and [providers of last resort] default service providers prior to the abandonment of service. The licensee shall provide individual notice to its customers with each billing, in each of the three billing cycles preceding the effective date of the abandonment.

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Subchapter E. COMPETITIVE SAFEGUARDS

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§54.123. Transfer of customers to default service.

The following standards shall apply to the transfer of a retail customer's electric generation service from an EGS to a default service provider within the meaning of §54.182:

(a) An EGS shall not transfer a retail customer from its electric generation service to the default service provider without the consent of the default service provider, except in the following situations:

(1) Upon Commission approval of the abandonment, suspension or revocation of an EGS license, consistent with §§54.41 and 54.42 (relating to transfer or abandonment of license and license suspension; license revocation).

(2) Upon nonpayment by a retail customer for services rendered by the EGS.

(3) To correct an unauthorized or inadvertent switch of a retail customer's account from default service to an alternative EGS's service.

(4) Upon the normal expiration of contracts that are not structured in a way to exploit seasonal variations in market prices for electric generation service

(b) An EGS may initiate transfers in the above situations through standard electronic data interchange protocols.

(c) An EGS may not initiate or encourage transfers of service to a default service provider from the EGS to exploit seasonal variations in market prices for electric generation service.

(d) The Commission may impose a penalty for every retail customer transferred to default service in violation of §54.123, consistent with 66 Pa. C.S. §§3301-3316 (relating to violations and penalties).

Subchapter G. DEFAULT SERVICE

§54.181. Purpose.

This subchapter implements §2807(e) of the Electricity Generation Customer Choice and Competition Act, 66 Pa. C.S. §§2801-2812, pertaining to an EDC's obligation to serve retail customers at the conclusion of the restructuring transition period. These regulations ensure that all retail customers who do not choose an alternative EGS, or who return to default service after having taken service by an EGS ~~contract for electric energy that is not delivered~~, have access to generation supply at prevailing market prices. The EDC shall fully recover all reasonable costs for acting as a default service provider of electricity to all retail customers in its certificated distribution territory.

§54.182. Definitions.

The following words and terms, when used in this subchapter, have the following meanings, unless the context clearly indicates otherwise:

Alternative energy portfolio standards – A requirement that a certain percentage of electric energy sold to retail customers in the Commonwealth of Pennsylvania be derived from alternative energy sources, as defined in the Alternative Energy Portfolio Standards Act, No. 213 of 2004.

Alternative procurement process -- A Commission-approved process, submitted as part of a default service implementation plan, which provides for the acquisition of generation supply at prevailing market prices.

Commission – The Pennsylvania Public Utility Commission.

Competitive procurement process – A fair, transparent, and non-discriminatory process ~~by which a default service provider~~ to acquires electric generation supply to serve ~~its~~ default service customers through a bid solicitation process.

Default service –

(i) Electric generation service provided by a default service provider to a retail electric customer who does not choose an alternative EGS or who is returned to default service after having taken service from an EGS~~contracts for electric energy and it is not delivered~~.

(ii) Electric generation service provided pursuant to a Commission approved default service plan.

Default service implementation plan – A filing submitted by a default service provider to the Commission that identifies the means for procuring generation supply for default service customers at prevailing market rates, the reasonable costs associated with default service, and all other necessary terms and conditions of service.

Default service provider – The incumbent EDC within a certificated service territory or a Commission approved alternative default service provider.

EDC – Electric Distribution Company – This term shall have the same meaning as defined in 66 Pa. C.S. §2803.

EGS – Electric Generation Supplier – This term shall have the same meaning as defined in 66 Pa. C.S. §2803.

FERC – The Federal Energy Regulatory Commission.

Fixed rate option – A default service price that is set in advance for the entire term of the default service implementation plan that may include seasonal differences, volumetric rate adjustments, or other variations described in Section 54.187(g).

Hourly priced service – A default service price where the energy component of the generation supply charge is based on the RTO or ISO's LMP for energy, or other similar, mechanism.

ISO – A FERC approved independent transmission system operator.

LMP – Locational marginal pricing – A pricing mechanism used by some RTOs and ISOs, as defined in their FERC approved tariffs.

Prevailing market price –

(i)The price of electric generation supply for a term of service realized through a default service provider's implementation of and compliance with a Commission approved default service implementation plan.

(ii) The price of electric generation supply in the RTO or ISO administered energy markets in whose control area default service is being provided, acquired pursuant to the conditions specified in §§54.186(g), 54.187(i) or 54.188(e).

Reasonable costs – The costs of providing default service to retail customers, which shall include (i) identifiable costs; (ii) reasonable estimates of difficult-to-quantify costs; and (iii) a return commensurate with any risks that the EDC may assume to provide default service.

Replacement procurement process – A Commission approved process, submitted as part of the default service implementation plan, which provides for the acquisition of generation supply in the event that a supplier fails to deliver generation contracted for under the terms of a competitive procurement process.

Retail customer or retail electric customer – These terms shall have the same meaning as defined in 66 Pa. C.S. §2803.

RTO - A FERC approved regional transmission organization.

§54.183. Default service provider.

(a) The default service provider shall be the incumbent EDC in each certificated service territory, except as provided for pursuant to §54.183(b).

(b) An EDC may petition the Commission to be relieved from the default service obligation. In the alternative, the Commission may propose through its own motion that an EDC be relieved from the default service obligation. The Commission may approve such a request if it is in the public interest. In such circumstances, the Commission will announce through an order a competitive process to determine the alternative default service provider, which may be either an EDC or a licensed EGS.

(c) When the Commission finds that an EDC should be relieved of the default service obligation, the competitive process for the replacement of the default service provider shall be as follows:

1. Any EDC or EGS that wishes to be considered for the role of the alternative default service provider shall apply for a certificate of public convenience, consistent with 66 Pa. C.S. §§1101-1103 (relating to certificates of public convenience).

2. Applicants shall demonstrate their operational and financial fitness to serve and their ability to comply with all Commission regulations, orders and applicable laws pertaining to public utility service.

3. If no applicant can meet this standard, the incumbent EDC shall be required to continue the provision of default service

4. If one or more applicants meet the standard provided in §54.183(c)(2), the Commission shall grant a certificate of public convenience to act as a default service provider to the applicant best able to fulfill the obligation

5. An EGS that is granted a certificate of public convenience to act as an alternative default service provider shall be considered a public utility within the meaning of 66 Pa. C.S. §102.

§54.184. Default service provider obligations.

(a) A default service provider shall be responsible for the reliable provision of default service to all retail customers who are not receiving generation services from an alternative EGS within the certificated territory of the EDC that it serves.

(b) A default service provider shall comply with all applicable Commission regulations and orders to the extent that such obligations are not modified by this subchapter.

(c) In the event that a replacement ~~A~~ default service provider is chosen pursuant to §54.183(b), the replacement default service provider shall not continue the universal service program in effect in the EDC's certificated service territory. The EDC

shall retain the obligation to maintain existing universal service programs and recover such costs in its distribution rates- ~~or implement, subject to Commission approval, a similar customer assistance program consistent with the provisions of the Electricity Generation Customer Choice and Competition Act, 66 Pa. C.S. §§2801-2812.~~

§54.185. Default service implementation plans and terms of service.

(a) A default service provider shall file a default service implementation plan with the Commission's Secretary's Bureau no later than fifteen months prior to the conclusion of the currently effective default service plan or Commission approved generation rate cap for that particular EDC service territory, unless the Commission authorizes another filing date.

(b) Default service implementation plans shall comply with all Commission regulations pertaining to documentary filings, except when modified by this subchapter. The default service provider shall serve copies of the default service implementation plan on the Pennsylvania Office of Consumer Advocate, Pennsylvania Office of Small Business Advocate, the Commission's Office of Trial Staff, and the RTO or ISO in whose control area the default service provider is operating.

(c) A default service implementation plan shall propose a minimum term of service of at least twelve months, or multiple twelve month periods, or for a period necessary to comply with §54.185(f).

(d) A default service implementation plan shall propose a fair, transparent and non-discriminatory competitive procurement process consistent with §54.186 for the acquisition of sufficient electric generation supply, at prevailing market prices, to meet the demand of all of the default service provider's retail electric customers for the term of service. The default service plan shall identify its method of compliance with the Alternative Energy Portfolio Standards Act, No. 213 of 2004.

(e) The Commission may direct that some or all default service providers file joint default service implementation plans that propose a competitive procurement process to procure electric generation supply for all of their default service customers. In

the absence of such a directive, some or all default service providers may jointly file default service plans that propose a competitive procurement process to procure electric generation for all of their default service customers. A multi-service territory competitive procurement process shall comply with §54.186.

(f) A default service provider shall document that its proposal is consistent with the legal and technical requirements pertaining to the generation, sale and transmission of electricity of the RTO or ISO in whose control area it is providing service. The default service plan's term of service and generation supply acquisition processes shall align with the planning period of that RTO or ISO.

(g) The default service implementation plan shall include a schedule of rates, rules and conditions of default service in the form of proposed revisions to its tariff. The default service provider may use the already effective retail customer classes in the EDC's service territory, or may propose a reclassification of retail customers.

(h) The default service implementation plan shall identify the costs, consistent with §54.187, that will be recovered through a schedule of rates for the provision of default service.

(i) The default service implementation plan shall include reasonable credit requirements, or other reasonable assurances of any supplier of electric generation services' ability to perform, as approved by the Commission.

(j) The default service implementation plan shall identify the load size and end date of all existing long-term generation contracts that are in effect between the EDC and a retail customer within its service territory.

(k) The default service implementation plan should include copies of any proposed confidentiality agreements for the protection of proprietary information of the default service provider and generation suppliers. The Commission will approve reasonable confidentiality agreements, including expiration provisions, that will be binding on the default service provider, generation suppliers and any third party involved in the administration, review or monitoring of a default service supply procurement process.

(l) The default service provider shall include in its implementation plan a replacement procurement process to ensure the reliable provision of default service in the event a supplier fails to deliver electric generation supply it has agreed to provide pursuant to the terms of a Commission approved competitive procurement process.

(m) The Commission may issue orders further specifying the form and content of default service implementation plans when necessary to enforce or carry out the provisions of the Electricity Generation Customer Choice and Competition Act, 66 Pa. C.S. §§2801-2812, and other applicable law.

§54.186. Default service supply procurement.

(a) A default service provider shall procure the electricity needed to provide default service only through a competitive procurement process, alternative procurement process, or replacement procurement process approved by the Commission, with the following exceptions:

(1) Hourly priced service provided pursuant to §54.187(e).

(2) Supply procured through RTO or ISO administered energy markets consistent with §§54.186(g), 54.187(i) or 54.188(e).

(b) A default service provider's competitive procurement process shall adhere to the following standards:

(1) A default service provider's supplier affiliate may participate in any competitive procurement process. The default service provider shall propose and implement protocols to ensure that its supplier affiliate does not receive an advantage in either the solicitation and evaluation of competitive bids, or any other aspect of the competitive procurement process. The process shall comply with the codes of conduct promulgated by the Commission at §54.122 (relating to code of conduct).

(2) A default service provider's proposed competitive procurement process shall include:

(i) A bidding schedule.

(ii) A definition and description of the power supply products on which potential suppliers shall bid.

(iii) Bid price formats.

(iv) The time period during which the power will need to be supplied for each power supply product.

(v) Bid submission instructions and format.

(vi) Bid evaluation criteria.

(vii) Relevant load data, including the following:

(A) Aggregated customer hourly usage data for all retail customers.

(B) Number of retail customers.

(C) Capacity peak load contribution figures by rate schedule.

(D) Historical monthly retention figures by rate schedule.

(E) Estimated loss factors by rate schedule.

(F) Customer size distribution by rate schedule.

(c) A default service provider may employ a third-party to design and implement the competitive procurement process or alternative procurement process.

(d) The competitive procurement process or alternative procurement process may be subject to direct oversight by the Commission or an independent third party. Any third party shall report to the Commission. Commission staff and any third party involved in oversight of the procurement process shall have full access to all information pertaining to the competitive procurement process, and may monitor the process either remotely or where the process is administered. Any third party retained for purposes of monitoring the competitive procurement process shall be subject to confidentiality agreements identified in §54.185(k).

(e) The default service provider shall evaluate and select winning bids submitted in a competitive procurement process in a non-discriminatory manner based on bid evaluation criteria set forth consistent with §54.186(b)(2)(vi).

(f) The Commission may conclude that an alternative procurement process is an acceptable alternative to a competitive procurement process if the default service provider submits evidence sufficient to demonstrate that such alternative procurement process will result in electric service supply that reflects prevailing market prices.

(g~~f~~) The Commission shall review the acquisition of generation supply and verify compliance with the approved competitive procurement process or alternative procurement process as follows:

(1) The Commission's review shall occur within a time period as specified in the approved ~~competitive~~ procurement process.

(2) The review period may not be less than 3 business days.

(3) The Commission's verification of compliance with an approved ~~competitive~~ procurement process shall constitute its certification of the default service provider's compliance with the approved default service implementation plan.

(h~~g~~) If the implementation of a competitive procurement process or an alternative procurement process under this section does not result in sufficient electric supply to meet the default service provider's full load requirements, the default service provider shall repeat the competitive procurement process or implement an alternative procurement process. The default service provider may petition for necessary changes to the previously approved ~~competitive~~ procurement process to ensure the acquisition of sufficient supply. When necessary to procure electric generation supply before the completion of another ~~competitive~~ procurement process, a default service provider shall acquire supply at prevailing market prices and shall fully recover all reasonable costs associated with this activity. In this circumstance, the prevailing market price shall be the price of electricity in the RTO or ISO's administered energy markets in whose control area that service is being provided. The default service provider shall follow acquisition strategies that reflect the incurrence of reasonable costs, consistent with 66 Pa. C.S. §2807(e)(3), when selecting from the various options available in these energy markets. A default service implementation plan shall include a proposed rate adjustment

mechanism designed to recover the costs associated with supply acquisition performed pursuant to this subsection.

(ih) The bids submitted by a supplier under a ~~the~~ competitive procurement process shall be treated as confidential through the expiration date identified in the confidentiality agreement approved by Commission pursuant to §54.185(k). The default service provider, the Commission, and any third party involved in the administration, review or monitoring of the procurement process, shall be subject to this confidentiality provision.

§54.187. Default service rates and the recovery of reasonable costs.

(a) The costs incurred for providing default service shall be recovered through the following mechanisms or charges:

(1) Generation supply charge – the generation supply charge is a non-reconcilable charge that includes all ~~reasonable~~ costs associated with the acquisition of generation supply, exclusive of the costs of generation supply recovered through §54.187(a)(3), to meet default service demand. The associated costs with this charge include:

(i) The prevailing market price of energy.

(ii) The prevailing market price of RTO or ISO capacity or any similar obligation.

(iii) FERC approved ancillary services and transmission charges.

(iv) Required RTO or ISO charges.

(v) Applicable taxes.

(vi) Other reasonable, identifiable generation supply acquisition costs.

(2) Customer charge – The customer charge is a non-reconcilable, fixed charge, set on a per customer class basis, that includes all identifiable, reasonable costs associated with providing default service to an average member of that class,

exclusive of generation supply costs and costs recovered through §54.187(a)(3). The associated costs with this charge include:

(i) ~~Default service related~~ Ceosts related to design and implementation of a competitive procurement process. ~~for customer billing, collections, customer service, meter reading, and uncollectible debt.~~

(ii) A reasonable return or risk component on the provision of default service. ~~for the default service provider.~~

(iii) Applicable taxes.

(iv) Other reasonable and identifiable administrative or regulatory expenses.

(3) A default service provider shall use an automatic energy adjustment clause, consistent with 66 Pa. C.S. §1307 to recover ~~reasonable~~ costs incurred through compliance with the Alternative Energy Portfolio Standards Act, No. 213 of 2004.

(4) The costs recovered through the preceding charges and mechanisms shall not be recovered by an EDC acting as a default service provider through its Commission approved distribution rates.

(b) A default service plan shall include a fixed rate option for all residential customers.

(c) A default service implementation plan shall include a fixed rate option for non-residential default service customers whose load test indicates a registered peak demand of 500 or less kilowatts.

(d) The default service provider shall include an hourly rate in its implementation plan for all default service customers whose load test indicates a registered peak demand of greater than 500 kilowatts. The default service provider may propose a fixed rate for these customers in its default service implementation plan.

(e) The rate for hourly priced service shall include:

(1) The RTO's or ISO's LMP or the equivalent pricing mechanism.

(2) The prevailing market price of RTO or ISO capacity or any similar obligation.

(3) FERC approved ancillary services and transmission charges.

(4) Required RTO or ISO charges.

(5) Applicable taxes.

(6) Other FERC approved or reasonable, identifiable RTO or ISO charges and costs directly related to the hourly priced service.

(7) Other reasonable and identifiable administrative or regulatory expenses.

(8) The charges set forth in subsections 54.187(a)(2) and (3).

(f) The default service implementation plan shall include rates that correspond to demand side response and demand side management programs available to retail customers in that EDC service territory.

(g) The default service implementation plan may include mechanisms that allow default service providers to adjust their prices during the term of service to recover reasonable, incremental costs of significant changes in the number of default service customers or reasonable, incremental costs of other events that would materially prejudice the reliable provision of default service and the full recovery of reasonable costs.

(h) The default service provider's projected and actual incurred costs for providing service may not be subject to Commission review and reconciliation except in extraordinary circumstances, or as provided pursuant to a Commission-approved default service implementation plan, or as provided in §54.187(a)(3).

(i) When a generation supplier fails to deliver generation supply to a default service provider, the default service provider shall be responsible for acquiring replacement generation supply consistent with its Commission approved replacement procurement process. When necessary to procure electric generation supply before the completion of the replacement procurement process, a default service provider shall acquire supply at prevailing market prices and shall fully recover all reasonable costs

associated with this activity. In this circumstance, the prevailing market price will be the price of electricity in the RTO or ISO's administered energy markets in whose control area the default service is being provided. The default service provider shall follow acquisition strategies that reflect the incurrence of reasonable costs, consistent with 66 Pa. C.S. §2807(e)(3), when selecting from the various options available in these energy markets. A default service implementation plan shall include a proposed rate adjustment mechanism designed to recover the costs associated with supply acquisition performed pursuant to this subsection.

§54.188. Commission review of default service implementation plans.

(a) A default service implementation plan shall initially be referred to the Office of Administrative Law Judge for further proceedings as may be required.

(b) The Commission will issue an order within six months of a plan's filing with the Commission on whether the default service implementation plan demonstrates compliance with this subchapter and the provisions of the Electricity Generation Customer Choice and Competition Act, 66 Pa. C.S. §§2801-2812. The Commission may order modification of the terms of the proposed plan to ensure that a default service plan is compliant.

(c) The Commission will evaluate the default service implementation plan to ensure that it includes a fair, transparent and non-discriminatory ~~competitive~~ procurement process for all potential suppliers provided under §54.186.

(d) Upon entry of the Commission's final order, the default service provider shall acquire generation supply for the term of service in a manner consistent with the terms of the approved ~~competitive~~ procurement process provided under §54.186, and report the bids submitted by EGSs in writing to the Commission.

(e) The Commission will certify the results of a ~~competitive~~ procurement process in their entirety or reject them due to non-compliance with the approved procurement process. If the Commission rejects the results due to non-compliance, the

default service provider shall repeat the approved ~~competitive~~ procurement process. When necessary to procure electric generation supply before the completion of the subsequent ~~competitive~~ procurement process, a default service provider shall acquire supply at prevailing market prices and shall fully recover all reasonable costs associated with this activity. In this circumstance, the prevailing market price will be the price of electricity in the RTO or ISO's administered energy markets in whose control area that service is being provided. The default service provider shall follow acquisition strategies that reflect the incurrence of reasonable costs, consistent with 66 Pa. C.S. §2807(e)(3), when selecting from the various options available in these energy markets.

(f) Upon completion of the ~~competitive~~ procurement process, the default service provider shall provide written notice to all default service customers and the named parties identified in §54.185(b) of the Commission certified default service prices and terms and conditions of service no later than 60 days before their effective date, unless another time period is approved by the Commission. The default service provider shall also provide written notice to the named parties identified in §54.185(b) containing an explanation of the methodology used to calculate the price for electric service.

(g) A default service provider may petition for a waiver of any part of these regulations, in a manner consistent with 52 Pa. Code §5.43 (relating to petitions for issuance, amendment or waiver of regulations). The Commission may grant waivers of these regulations to ensure the reliable provision of default service and to enforce and carry out the provisions of the Electricity Generation Customer Choice and Competition Act, 66 Pa. C.S. §§2801-2812 and any other applicable laws.

§54.189. Default service customers.

(a) At the conclusion of an EDC's Commission approved generation rate cap, all retail customers who are not receiving generation service from an EGS shall be assigned to the Commission approved default service implementation plan.

(b) A default service provider shall accept all applications for default service from new retail customers and retail customers who switch from an EGS, if the customers comply with all Commission regulations pertaining to applications for service.

(c) A default service provider shall treat a customer who leaves an EGS and applies for default service as it would a new applicant for default service.

(d) A default service customer may choose to receive its generation service from an EGS at any time, if the customer complies with all Commission regulations pertaining to changing generation service providers.

(e) Unless assessed pursuant to a Commission-approved default service implementation plan, a~~A~~ default service provider may not charge a fee to a retail customer that changes its generation service provider in a manner consistent with Commission regulations.

CHAPTER 57. ELECTRIC SERVICE
Subchapter M: STANDARDS FOR CHANGING A CUSTOMER'S ELECTRIC GENERATION SUPPLIER

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§57.178. [Provider of Last Resort] Default service provider.

This subchapter does not apply when the customer's service is discontinued by the EGS and subsequently provided by the [provider of last resort] default service provider because no other EGS is willing to provide service to the customer.

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