BEFORE THE
PENHNSYLVANIA PUBLIC UTILTY COMMISSION

Implementation of the Alternative Energy Portfolio Standards Act Of 2004	:	Docket No. M-00051865
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 STRATEGIC ENERGY, LLC

Strategic Energy, LLC (Strategic) is a licensed Electricity Generation Supplier (EGS) with load in various utility territories throughout the state and in numerous other states with retail choice. Strategic submits these comments on certain issues identified in the Commission's November 18, 2005 Order relating to cost recovery and other matters under the Alternative Energy Portfolio Standards Act of 2004 (Act 213 or Act). Strategic understands that the Commission is considering whether additional opportunities for discussion through additional workshops are needed and fully supports additional workshops for discussion of the important issues currently under consideration.

The resolution of a number of the issues raised by the Commission will impact whether competitive electricity suppliers are treated fairly under the rules. While not diminishing the importance of any of the Act 213 issues identified by the Commission for additional comment, Strategic believes that the resolution of issue Nos. 2 and 5 below will have a significant impact on developing competitive retail markets in Pennsylvania. Strategic also offers brief comments on issue No. 3, the force majeure provision.

2. Do the prevailing market conditions require long-term contracts to initiate development of alternative energy resources? May Default Service Providers employ long-term fixed price contracts to acquire alternative energy resources? What competitive procurement process may be employed if the Default Services Provider acquires alternative energy resources through a long-term fixed price contract?

5. Should the Commission integrate the costs determined through a § 1307 process for alternative energy resources with the energy costs identified through the Default

Service Provider regulations? How could these costs be blended into the Default Service Providers Tariff rate schedules?

Both of these issues deal with the structure of default service – the single most important factor in the success or failure of competitive retail markets. This concept applies with equal force to the structure imposed upon the default service provider for acquiring alternative energy resources and for passing through compliance costs associated with Act 213. An inappropriate market structure could harm not only retail choice but wholesale markets for renewables.

Requiring Long-Term Fixed Price Contracts Would be Detrimental to Competitive Markets and Contrary to the Choice Act (Issue No. 2)

Default service providers should not be required to employ long-term fixed price contracts to acquire alternative energy resources. Procurement through long-term contracts may have the undesirable consequence of eliminating liquidity for short- and medium-term renewable resources needed by all load serving entities, whose load can vary significantly from day to day due to Pennsylvania's weather sensitive electricity markets and customer migration.

In addition, the competitive market should be relied upon to develop renewable resources mandated under the Act without regulatory mandates on contract that could distort market price signals. As the Commission made clear in its proposed Default Service rulemaking, "To foster a competitive market, any POLR service model must be carefully designed to avoid distortions to the market."[1] Alternative Compliance Payments (ACPs) provide a clear price incentive to build and contract for new facilities that will be constructed in the future.

The situation in Texas confirms that long-term contracts are not necessary to develop renewable resources. Texas **has not** mandated long-term contracting and it is not experiencing any shortfall in renewable generation development. In fact, the 2005 Public Utility Commission of Texas' Report to the Texas Legislature states that the development of renewable energy facilities has proceeded more rapidly than the timelines outlined in the state's renewable legislation. The Texas goal of 850 megawatts by January 1, 2005 was met early by actual renewable capacity

[1] *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, Order entered December 16, 2004, at 5.

development of 1,187 MW by November 2004. This milestone was achieved without any contract requirements or bundling of attributes and energy. The report concludes that additional transmission capacity and the federal production tax credits were the most critical development factors for renewable generators.[2] Although the Texas Public Utility Commission will not release its 2006 report until April of this year, the Commission issued a Press Release on March 15, 2005, stating that the 2009 mandate of 2,000 additional megawatts of renewable generating capacity will be met three years early.[3]

Lack of POLR Price Transparency for AEPs is Detrimental to Competitive Markets(Issue No. 2)

The AEPS Act guarantees EDCs dollar-for-dollar pass through of all costs associated with complying with the Act's requirements, including administrative costs and costs of credits, through a reconciliation mechanism under 66 Pa. C.S. § 1307 as costs of generation supply under 66 Pa. C.S. § 2807(e)(3). EGSs, on the other hand, are not guanteed recovery of their compliance costs and must include these costs in the price of their competitive offers to customers. It is impossible to accurately represent charges that are reconciled after the fact in the electricity market in a price to compare. The collection of commodity costs through a reconciliation mechanism that is never representative of the actual and timely market costs causes a distortion between the prices marketers can offer and the prices that the utility customer will use as a benchmark in evaluating the offer. This lack of transparency will inhibit a customer's willingness to select an EGS. This is exactly the situation caused by the quarterly reconciliation of gas costs, as the Commission has recognized.[4]

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[2] 2005 Report to the 79th Legislature, Scope of Competition in Electric Markets in Texas, Public Utility Commission of Texas, January 2005.

[3] http://www.puc.state.tx.us/nrelease/2005/021505.cfm

[4] *Investigatory Gas Competition Report*, Docket No. I-00040103, Order entered October 6, 2005, at 5 ("The regulatory lag in establishing and implementing quarterly price adjustments by natural gas distribution companies tends to mask the current market price of natural gas.").

The only way to avoid the competitive harm that would result from after-the-fact reconciliation and also advance the goals of the Electric Choice Act[5] is for the Commission to require that EDCs purchase AEPS credits for all customers in their service territory and pass through all costs in a separate line item. In fact, this could be, by default, a non-bypassable charge on all customer bills unless the customer affirmatively elects to bypass the charge and satisfy the requirement through an EGS. This approach would have no negative impact on the purpose of Act 213 – to encourage the purchase of energy from alternative energy resources and to provide funds for the construction of such resources. However, to permit an automatic, anti-competitive recovery method would clearly negatively impact the development of retail competition and run afoul of Section 2807(e)(3) of the Electric Choice Act which requires the Default Service Provider (DSP) to acquire generation supply at "prevailing market prices" to serve default service customers and requires that the DSP "shall recover fully all reasonable costs" of providing the retail default service.

3. Should the force majeure provisions of Act 213 be integrated into the Default Service procurement process? Should Default Service Providers be required to make force majeure claims in their Default Service implementation filing? What criteria should the Commission consider in evaluating a force majeure claim? How may the Commission resolve a claim of force majeure by an electric generation supplier?

Under the Act's force majeure provision, "[I]f the commission determines that alternative energy resources ***are not reasonably available in sufficient quantities in the market place*** for the electric distribution companies and electric generation suppliers to meet their obligation under this act, then the commission shall modify the underlying obligation of the electric distribution company of electric generation supplier or recommend to the general assembly that the underlying obligation be eliminated." If EDCs and EGSs do not have substantial advance notice about the reduction or elimination of an obligation under the Act, the risks to EDCs and EGSs are significant, especially with respect to Tier I photovoltaic obligations which carry a hefty penalty for non-compliance. In addition, this type of regulatory uncertainty is extremely detrimental to the development of competitive retail markets. In weighing the risks and benefits of making service

[5] Electricity Generation Customer Choice and Competition Act, 66 Pa C.S. §§ 2801-2812.

offerings in utility territories, retail suppliers will place a big check mark in the regulatory uncertainty category because they won't have advance notice of what their obligations under the AEPS are since those obligations could change.

The Commission must recognize too that the inquiry about whether resources are ***reasonably available in sufficient quantities in the market place*** is multi-faceted. For example, there may be a sufficient quantity of a particular group of resources within a utility service territory but, due to banking or refusal to sell, there may be no credits available. In addition, with the case of Tier I photovoltaic resources, if owners of those resources demand prices for credits far in excess of what is reasonable, those resources are not "reasonably available" in the market place.

Conclusion

Strategic Energy requests that the Commission consider these comments when crafting its final regulations for post-transition Default POLR Service, and that the Commission convene additional workshops as the Commission deems necessary to address all the issues concerning post-transition Default POLR Service.

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