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June 15, 2010

VIA MESSENGER

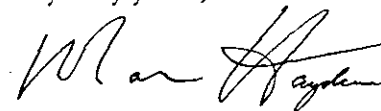
Rosemary Chiavetta, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street, 2nd Floor North
Harrisburg, PA 17120

Re: *Implementation of Act 129 of October 15, 2008; Default Service*
Docket No. L-2009-2095604

Dear Secretary Chiavetta:

Enclosed for filing are an original and fifteen (15) copies of the *Reply Comments of FirstEnergy Solutions Corp.* These Reply Comments are submitted in accordance with the Commission's Order entered January 19, 2010 in the above referenced proceeding. Also enclosed is an additional copy of the Reply Comments, to be date stamped and returned to our messenger. Please call me if you have any questions.

Very truly yours,



Mark Hayden

Enclosures

cc: Elizabeth Barnes, Assistant Counsel (via e-mail ebarnes@state.pa.us w/encs.)

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**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Implementation of Act 129 of October 15, 2008; Default Service)	Docket No. L-2009-2095604
Proposed Policy Statement Regarding Default Service And Retail Electric Markets)	Docket No. M-2009-2140580

**REPLY COMMENTS OF
FIRSTENERGY SOLUTIONS CORP.**

I. INTRODUCTION

On January 19, 2010, the Pennsylvania Public Utility Commission (“Commission”) entered its Proposed Rulemaking Order and Proposed Policy Statement in the above-referenced dockets, opening proceedings to consider amendments to the Commission's default service regulations and the current Policy Statement regarding default service and retail electric markets, as required by the enactment of Act 129. Initial Comments were filed in either or both proceedings by seventeen parties. FirstEnergy Solutions Corp. (“FES”) appreciates this opportunity to file Reply Comments. FES's Reply Comments will address a number of comments related to certain “Additional Issues” set forth in the Proposed Rulemaking Order.

II. REPLY COMMENTS REGARDING THE PROPOSED REGULATIONS

- A. While the term “least cost to customers over time” is open to a number of interpretations, each of which presents its own set of risks, full requirements procurements best balance competitively low prices and risk management, to the benefit of customers.**

The Energy Association of PA comments that the phrase “least cost to customers over time” “is ambiguous because it is not clear what period of time is being contemplated...It is impossible to know with certainty what particular strategy will result in the ‘least cost over time,’

and the longer the period of time, the less certain one can be of the results.”¹ FES agrees, and believes that “least cost to customers over time” is open to a number of interpretations. For instance, “least cost to customers” could be interpreted to mean providing customers with the lowest average cost over time, even though there may be periods of sharp rate increases. Or it could be interpreted to mean that customers should be provided with stable pricing, even though this stability may mean higher rates than may sometimes be achieved with a measure of volatility. In the alternative, “least cost” may require an incentive for energy efficiency and energy conservation, even though this might mean higher prices and volatile costs.

FES also agrees with the comment of PPL Electric Utilities Corporation, which stresses the importance in noting that the term “least cost to customers over time” does not mean the absolute lowest possible cost to customers. The energy markets are subject to volatility based on many factors such as generation supply, customer usage, and weather conditions, making it impossible to precisely time purchases to acquire supply at the lowest possible market prices². For this reason, FES maintains that compliance with the “least cost to customers over time” requirement can only be determined in retrospect, and there may be no way to know until years later. Indeed, a process that yields the lowest cost on one occasion is just as likely to yield higher costs when applied a second time.

Of course, the use of hindsight would contradict the prospective nature of the Commission's default service procurement plan approval process under the Competition Act. It is impossible for the Commission, a utility, a wholesale supplier or alternative energy supplier to accurately “time the market” and get the lowest cost.

¹ June 1, 2010 Comments of the Energy Association of PA; Docket No. L-2009-2095604 p4.

² June 1, 2010 Comments of PPL Electric Utilities Corporation to the Proposed Rulemaking Order; Docket No. L-2009-2095604 p7.

For these reasons, FES submits that there is no approach to procurement guaranteed to result in the least cost to customers over time. Every approach involves its own set of risks. The question becomes how best to manage the risks, to provide customers with the best combination of competitively low prices and insulation from risk. In FES's experience with procurements for electric distribution companies (“EDCs”) with larger default service load obligations, full requirements procurements establish the best balance of competitively low prices and expert management of price variation. Bidders compete on the basis of the lowest competitive price to satisfy all aspects of the default service customers' load requirements. A full requirements procurement requires the winning suppliers to manage price uncertainty, volumetric uncertainty, and other risks at the lowest price. While the risks are monetized into the price of a full requirements product, the supplier is assuming those risks on behalf of default service customers, who benefit from price certainty for the duration of the contract. Wholesale suppliers have valuable expertise in managing the risks, and may be able to use this expertise to reduce the monetized risk and the overall cost of the full requirements product. Also, the fixed price option gives customers a benchmark price with which customers can more easily evaluate offers from alternative retail suppliers. Therefore, all customers benefit from competition at the wholesale level.

This is particularly the case for EDCs in the control area of PJM Interconnection L.L.C. (“PJM”). In PJM, a full requirements solicitation allows more sophisticated wholesale market participants who are experts in managing generation portfolios to compete to supply the lowest cost fixed price, full requirements product from the wholesale markets, based on each competitor's assessment of data from PJM's transparent markets, and each competitor's own expertise in managing costs and risks. These benefits of full requirements procurements

recommend this procurement method as the one most likely to ensure the least cost to customers over time.

B. The Commission’s default service regulations should not provide for integrated resource planning.

FES differs with the Industrial Customers Groups' suggestions that (1) the Commission should seek to promote the construction of new generation capacity, and (2) administratively mandated additional units can reduce prices for customers. FES supports the comments of those participants that promote the Competition Act, which emphasizes the benefits of controlling the cost of electricity generation through competitive market forces rather than regulatory mandates.³

The Industrial Customer Groups believe the Commission should seek to promote the construction of new generation capacity and should require that a portion of the capacity be dedicated to economic development on a cost of service basis⁴. FES disagrees. As an initial matter, the Competition Act provides that the Commonwealth no longer regulates the generation of electricity as a public utility function.⁵ The policy underlying the Competition Act is to allow the market to decide when new generation is required through signals sent by capacity and energy prices. If the generation is needed, the market will deliver the additional Megawatts required. Further, adequate processes, such as PJM’s Reliability Pricing Model, are already in place to send accurate price signals to wholesale suppliers.

FES agrees with the comment of the PECO Energy Company (“PECO”), which also accepts that the need for and construction of generation capacity in Pennsylvania is best determined by competitive markets, particularly in light of the Regional Transmission

³ 66 Pa.C.S. § 2802(6) (finding “competitive market forces are more effective than economic regulation in controlling the cost of generating electricity.”).

⁴ June 1, 2010 Comments of the Industrial Customer Groups; Docket No. L-2009-2095604 p3.

⁵ 66 Pa.C.S. §§ 2802(14), 2806(a).

Organizations (“RTOs”) that serve Pennsylvania to ensure the reliability of the regional electricity grids and the numerous mechanisms that these RTOs have established to meet this responsibility.⁶ PECO even goes further and postulates that creating additional state regulations intended “to ensure the construction of needed generation capacity” would be unnecessarily duplicative of, and disruptive to, the RTOs’ programs and market mechanisms.⁷

Indeed, administratively mandating additional generation would require the Commission to attempt to “time the market.” As explained further below in Section C of these Reply Comments, neither the Commission, nor any EDC or wholesale or retail supplier, can time the market with any reasonable expectation of success. The Commission should not be placed in such an untenable position.

For the same reasons, FES agrees with the PJM Power Providers Group (“P3”) that the Commission should not specify technologies or favor new generation over existing generation.⁸ Various technologies should compete on an even playing field. Any perceived regulatory preference for one type of generation over another could have the unintended effect of causing suppliers to site their generation in surrounding markets with more predictable rules. This would lead to higher prices in the Pennsylvania market, contrary to the Industrial Customer Groups’ intention to reduce prices for customers through the addition of baseload and strategically sited peaking units.⁹ P3 correctly points to the additional risk associated with construction, including

⁶ June 1, 2010 Comments of PECO Energy Company on Proposed Amendments to the Commission’s Default Service Regulations and Policy Statement on Default Service and Retail Electric Markets; Docket No. L-2009-2095604 p8-9.

⁷ June 1, 2010 Comments of PECO Energy Company on Proposed Amendments to the Commission’s Default Service Regulations and Policy Statement on Default Service and Retail Electric Markets; Docket No. L-2009-2095604 p8-9.

⁸ June 1, 2010 Comments of the PJM Power Providers Group; Docket No. L-2009-2095604 p2.

⁹ June 1, 2010 Comments of the Industrial Customer Groups; Docket No. L-2009-2095604 p 3.

cost overruns and delays, fuel risks, environmental compliance costs, outage risk, and other risks, which are borne by the consumers.¹⁰

C. There is no “one-size-fits-all” approach to supply procurement, which should be determined on a case-by-case basis.

While FES believes a full requirements solicitation is the best proven method of supply procurement in most circumstances, each utility has a special set of circumstances, and there is no “one-size-fits-all” approach that will work in every market. Each default service provider should be able to work with stakeholders in its default service proceedings to craft a solution that appropriately balances competing interests for the particular service territory involved, and that would be subject to Commission approval.

Nonetheless, a few commenters, including Citizens’ and Wellsboro Electric Companies, the Pennsylvania Office of Consumer Advocate, and Citizen Power, support an actively managed portfolio approach as the optimal solution for all Pennsylvania service territories. Under this approach, the EDC would purchase a blend of energy in longer-term and shorter-term increments to meet anticipated load obligations. This approach requires the EDC to attempt to “time” the market, to attempt to take advantage of favorable price conditions.

FES believes that this approach generally entails an unacceptably high level of risk and is not appropriate for default service supply procurements. A single EDC is unlikely to outperform the experienced participants in wholesale competitive procurements, whose expertise is discussed above, when it comes to managing risk in the market. Also, the timing approach creates greater exposure to cost changes arising from load and price uncertainty. For example, a utility needing to buy extra power on the spot market to meet unexpectedly high demand may have to purchase

¹⁰ June 1, 2010 Comments of the PJM Power Providers Group; Docket No. L-2009-2095604 p4.

the power at a high price relative to prior forward prices. On the other hand, when the utility has excess purchased power it needs to sell back into the market, it will command a relatively low price. Resulting increases in default service rates could encourage default service customers to switch to a competitive retail supplier, compounding the problem for the remaining default service customers.

FES agrees with the comment of Exelon Generation Company, LLC and Exelon Energy Company (“Exelon Companies”) that a fundamental difference between the managed portfolio and full requirements approaches is the allocation of risk.¹¹ The consequences of failure under a managed portfolio approach are more problematic than with full requirements products, because the managed portfolio approach shifts the significant risks associated with full requirements products from the wholesale supplier to the EDC, and ultimately to the consumer. Full requirements procurements protect customers from price variation, consistent with the Commonwealth's established policy that “competitive market forces are more effective than economic regulation in controlling the cost of generating electricity.”¹² Unlike a competitive wholesale supplier, an EDC implementing a managed portfolio is not motivated to strive to minimize its costs for managing risk by competitive concerns. In addition, active portfolio management is likely to incur greater transaction and administrative costs, including the costs of adding staff and establishing trading operations, and may include the risk of substantial prudence review by the Commission. Therefore, FES believes an actively managed portfolio is an inappropriate method of procurement in most circumstances.

The intent of Act 129 is not just least cost but also price stability and a “prudent mix” of contracts. There is no way for parties to time the market and develop a plan that is guaranteed to

¹¹ June 1, 2010 Comments of Exelon Generation Company, LLC and Exelon Energy Company; Docket No. L-2009-2095604 p 7.

¹² 66 Pa.C.S. § 2802(6).

be the right approach. As such, the perfect plan is created by collaboration between the utility, wholesale suppliers, retail suppliers, the Commission and other interested parties. Only through this collaborative effort will the plan creator not be subject to second guessing by the parties involved. The utility and intervening parties should be allowed to create a plan that works in the specific circumstances involved.

D. There should be flexibility in determining what should constitute a “prudent mix” of contracts, for each EDC and each customer class.

Constellation NewEnergy, Inc., and Constellation Energy Commodities Group, Inc. (collectively, “Constellation”) comment that there exists no universal definition of specific percentages of each type of product which would represent a “prudent” mix of such contracts for each customer class, for each EDC.¹³ FES agrees that there is no “one-size-fits-all” and that supply procurement should be decided on a case-by-case basis. The utility and intervening parties should be allowed to create a plan that works in the specific circumstances involved and present that plan to the Commission for approval.

FES disagrees with the comment of the Industrial Customer Groups that, at a minimum, two types of products must be included to constitute a “mix.” According to the Industrial Customer Groups, providing only hourly priced service does not result in a prudent mix for Large commercial and industrial (“C&I”) customers because it only includes one product.¹⁴ To the contrary, FES believes there should be flexibility in determining what constitutes a “prudent mix” of contracts. Act 129 appropriately provides discretion to the Commission, EDCs and interested parties to review characteristics of each individual customer class of each separate

¹³ June 10, 2010 Comments of Constellation NewEnergy, Inc. and Constellation Energy Commodities Group, Inc. on Proposed Rulemaking Order Regarding Default Service Regulations; Docket No. M-2009-2140580 p31.

¹⁴ June 1, 2010 Comments of the Industrial Customer Groups; Docket No. L-2009-2095604 p4.

EDC, respectively, on a case-by-case basis, in order to pre-determine and pre-approve what mix of product lengths would be “prudent” to meet such customer class’ needs for default service supply, while continuing to promote competition and customer choice.¹⁵ Consistent with Constellation’s comments, FES is also in agreement with P3, which believes the Commission should allow EDCs the flexibility to propose what they believe to be a prudent portfolio of competitive procurements, invite comments and then exercise informed discretion to determine the most appropriate procurement mix based on the established record.¹⁶

PPL Electric Utilities Corporation adds one more element to the “prudent mix” standard by both recognizing that an infinite number of procurement plans can be considered a prudent mix and introducing the concept of not allowing discretionary changes to an approved default service plan. After the Commission has approved a default service provider's (“DSP's”) plan, the mix of contracts should remain in place for the term of the plan, and the DSP should not have discretion to change that mix¹⁷. Utilities and intervening parties should be allowed to craft a plan that works for the specific circumstances involved, but once the plan has gone through the appropriate regulatory channels, the “prudent mix” of contracts should remain unchanged until the development and approval of a new plan. This is not to say that contracts within separate plans cannot overlap. Rather, FES believes that providing contract stability (with whatever mix has been deemed reasonable) within a plan will nurture an environment which is most likely to result in a sustainable, competitive retail market.

¹⁵ June 10, 2010 Comments of Constellation NewEnergy, Inc. and Constellation Energy Commodities Group, Inc. on Proposed Rulemaking Order Regarding Default Service Regulations; Docket No. M-2009-2140580 p31.

¹⁶ June 1, 2010 Comments of the PJM Power Providers Group; Docket No. L-2009-2095604 p3.

¹⁷ June 1, 2010 Comments of PPL Electric Utilities Corporation to the Proposed Rulemaking Order; Docket No. L-2009-2095604 p10.

E. If the Commission were to implement an actively managed portfolio approach to procurement, it should not subject the EDC to after-the-fact prudence review of the “cost reasonableness standard.”

As detailed at length above, FES opposes the use of an actively managed portfolio approach to procure default service supply. One of the disadvantages of a managed portfolio approach that FES discussed was the likely requirement of prudency review. FES believes that in those very limited instances in which an actively managed portfolio approach may be considered appropriate, there should be no after-the-fact prudency review. FES strongly disagrees with the comments of the Pennsylvania Office of Small Business Advocate (“OSBA”), which believes that requiring a prudency review should cause the DSP both to prepare defensible analyses of its portfolio purchases and to exercise more caution before engaging in risky procurement strategies.¹⁸ If an EDC is going to pursue a procurement strategy as risky as an actively managed portfolio, the only way to allow retail customers to receive any benefit of the competitive wholesale power markets is not to include an after-the-fact review. Such a review discourages competition, prejudices the perceived “cost reasonableness,” and injects unnecessary regulatory uncertainty into the market, outcomes contrary to the goals set out in Act 129. Any uncertainty, such as establishing an after-the-fact “cost reasonableness standard,” is likely to discourage participation by wholesale suppliers, which may lead to higher prices. The Exelon Companies correctly point to the possibility that a DSP would not recover all of its default service costs, which creates a cost recovery risk for potential suppliers.¹⁹ This risk would cause potential suppliers either not to bid, decreasing the competitiveness of the procurement, or to bid

¹⁸ June 1, 2010 Initial Comments of the Office of Small Business Advocate; Docket No. L-2009-2095604 p32.

¹⁹ June 1, 2010 Comments of Exelon Generation Company, LLC and Exelon Energy Company; Docket No. L-2009-2095604 p10.

with a significantly higher risk premium.²⁰ Further, once the Commission has approved a default service plan, Act 129 provides only for review of procurement plan costs in two specific circumstances: where, after hearing, a DSP is found to be at fault for (1) not complying with the Commission-approved procurement plan; or (2) committing fraud, collusion, or market manipulation with regard to generation supply contracts.²¹

In addition, a hindsight review improperly takes advantage of information that was not available at the time of the procurements and could prejudice the perceived “cost reasonableness.”²² Under an actively managed portfolio, the EDC times its purchases simply as a “best-guess.” Even the experts in the field of generation portfolio management and risk management, the wholesale suppliers, cannot predict what will happen to prices in the future with guaranteed 100% accuracy. If EDCs, who are far less accustomed to portfolio management, are given the latitude to decide when to make purchases as part of a Commission order, they cannot reasonably be subjected to second-guessing after the fact.

²⁰ June 1, 2010 Comments of Exelon Generation Company, LLC and Exelon Energy Company; Docket No. L-2009-2095604 p10.

²¹ June 1, 2010 Comments of PECO Energy Company on Proposed Amendments to the Commission’s Default Service Regulations and Policy Statement on Default Service and Retail Electric Markets; Docket No. L-2009-2095604 p19 (referring to 66 Pa.C.S. § 2807(e)(3.9)).

²² June 1, 2010 Comments of Metropolitan Edison Company, Pennsylvania Electric Company, and Pennsylvania Power Company; Docket No. L-2009-2095604 p11.