



COMMONWEALTH OF PENNSYLVANIA

October 10, 2014

E-FILED

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

**Re: Petition of PECO Energy Company for Approval of its Default Service Program
for the Period From June 1, 2015 Through May 31, 2017
Docket No. P-2014-2409362**

Dear Secretary Chiavetta:

Enclosed for filing are the Exceptions, on behalf of the Office of Small Business Advocate in the above-docketed proceeding. As evidenced by the enclosed certificate of service, two copies have been served on all active parties in this case.

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

Sincerely,

A handwritten signature in cursive script that reads "Elizabeth Rose Triscari".

Elizabeth Rose Triscari
Deputy Small Business Advocate
Attorney ID #306921

Enclosures

cc: Parties of Record

Cheryl Walker Davis, Director
Office of Special Assistants

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Petition of PECO Energy Company for :
Approval of Its Default Service Plan for the : **Docket No. P-2014-2409362**
Period from June 1, 2015 through May 31, 2017 :

CERTIFICATE OF SERVICE

I certify that I am serving two copies of the Exceptions, on behalf of the Office of Small Business Advocate, by e-filing, e-mail, and/or first-class mail (unless otherwise noted) upon the persons addressed below:

Hon. Cynthia W. Fordham
Administrative Law Judge
Pa. Public Utility Commission
801 Market Street - #4063
Philadelphia, PA 19107
(215) 560-2105
(215) 560-3133 (fax)
cfordham@pa.gov

Christy M. Appleby, Esquire
Candis A. Tunilo, Esquire
Office of Consumer Advocate
555 Walnut Street - 5th Floor
Harrisburg, PA 17101-1923
(717) 783-5048
(717) 783-7152 (fax)
cappleby@paoca.org
ctunilo@paoca.org
(E-mail and Hand Delivery)

Michael A. Gruin, Esquire
Stevens & Lee
17 North Second Street - 16th Floor
Harrisburg, PA 17101
(717) 255-7365
(610) 988-0852 (fax)
mag@stevenslee.com

David P. Zambito, Esquire
Cozen O'Connor
305 North Front Street - #400
Harrisburg, PA 17101-1236
(717) 703-5892
(215) 989-4216 (fax)
dzambito@cozen.com

Anthony E. Gay, Esquire
Romulo L. Diaz, Esquire
W. Craig Williams, Esquire
Exelon Business Services Company
2301 Market Street - S23-1
P. O. Box 8699
Philadelphia, PA 19101-8699
(215) 841-4635
Anthony.Gay@exeloncorp.com
Romulo.Diaz@exeloncorp.com
Craig.Williams@exeloncorp.com

Daniel Clearfield, Esquire
Deanne M. O'Dell, Esquire
Sarah C. Stoner, Esquire
Eckert Seamans Cherin & Mellott, LLC
213 Market Street - 8th Floor
Harrisburg, PA 17101
(717) 237-6000
(717) 237-6019 (fax)
dclearfield@eckertseamans.com
dodell@eckertseamans.com
sstoner@eckertseamans.com

Todd S. Stewart, Esquire
Thomas J. Sniscak, Esquire
Judith D. Cassel, Esquire
Hawke McKeon & Sniscak, LLP
P. O. Box 1778
Harrisburg, PA 17105-1778
(717) 236-1300
(717) 236-4841 (fax)
tsstewart@hmslegal.com
tjsniscak@hmslegal.com
jdcassel@hmslegal.com

Charles E. Thomas III, Esquire
Thomas Niesen & Thomas
P. O. Box 9500
Harrisburg, PA 17108-9500
(717) 255-7600
(717) 236-8278 (fax)
cet3@tntlawfirm.com

Aundrea Williams
NextEra Energy, Inc.
801 Pennsylvania Ave., N.W. - #220
Washington, DC 20004
aundrea.williams@nexteraenergyservices.com

Thomas P. Gadsden, Esquire
Kenneth M. Kulak, Esquire
Brooke E. McGlinn, Esquire
Morgan Lewis Bockius LLP
1701 Market Street
Philadelphia, PA 19103
tgadsden@morganlewis.com
kkulak@morganlewis.com
bmclinn@morganlewis.com

Amy M. Klodowski, Esquire
FirstEnergy Solutions Corp.
800 Cabin Hill Drive
Greensburg, PA 15601
aklodow@firstenergycorp.com

Richard Hahn
LaCapra Associates, Inc.
One Washington Mall - 9th Floor
Boston, MA 02108
(617) 778-2467
rhahn@lacapra.com
(E-mail Only)

Barbara R. Alexander
83 Wedgewood Drive
Winthrop, ME 04364
(207) 395-4143
barbalex@ctel.net
(E-mail Only)

Date: October 10, 2014

Johnnie E. Simms, Esquire
Bureau of Investigation and Enforcement
Pa. Public Utility Commission
P. O. Box 3265
Harrisburg, PA 17105
(717) 787-4886
(717) 772-2677 (fax)
josimms@pa.gov
(E-mail and Hand Delivery)

Charis Mincavage, Esquire
Adeolu A. Bakare, Esquire
McNees Wallace & Nurick, LLC
P. O. Box 1166
Harrisburg, PA 17108-1166
(717) 232-8000
(717) 237-5300 (fax)
cmincavage@mwn.com
abakare@mwn.com

Harry S. Geller, Esquire
Patrick M. Cicero, Esquire
Pennsylvania Utility Law Project
118 Locust Street
Harrisburg, PA 17101
(717) 236-9486
(717) 233-4088 (fax)
pulp@palegalaid.net

Becky Merola
Noble Americas Energy Solutions, LLC
5325 Sheffield Avenue
Powell, OH 43065
bmerola@noblesolutions.com


Elizabeth Rose Triscari
Deputy Small Business Advocate
Attorney ID # 306921

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

**Petition of PECO Energy Company for :
Approval of Its Default Service Plan for the : Docket No. P-2014-2409362
Period from June 1, 2015 through May 31, 2017 :**

**EXCEPTIONS
ON BEHALF OF THE
OFFICE OF SMALL BUSINESS ADVOCATE**

**Elizabeth Rose Triscari
Deputy Small Business Advocate
Attorney ID # 306921**

**For: John R. Evans
Small Business Advocate**

**Office of Small Business Advocate
300 North Second Street - Suite 1102
Harrisburg, PA 17101**

Dated: October 10, 2014

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I. INTRODUCTION

On March 10, 2014, PECO Energy Company (“PECO” or “the Company”) filed with the Pennsylvania Public Utility Commission (“Commission”) the Petition of PECO Energy Company for Approval of Its Default Service Program for the Period From June 1, 2015 Through May 31, 2017 (“Petition”). The Petition seeks approval of PECO’s proposed third Default Service Program (“DSP III”) to secure default service supply for the Company’s customers for the period from June 1, 2015 through May 31, 2017.

On March 28, 2014, the Office of Small Business Advocate (“OSBA”) intervened and filed an Answer in this proceeding in order to protect the interests of the Company’s small business customers.¹

Answers were also filed by the Office of Consumer Advocate (“OCA”) and the Coalition for Affordable Utility Service and Energy Efficiency in Pennsylvania (“CAUSE-PA”) on April 1, 2014.

Petitions to Intervene were filed by CAUSE-PA, NextEra Power Marketing, LLC (“NextEra”), Philadelphia Area Industrial Energy Users Group (“PAIEUG”), FirstEnergy Solutions Corp. (“FES”), Interstate Gas Supply, Inc. (“IGS”), Direct Energy Services, LLC (“Direct Energy”), Retail Energy Supply Association (“RESA”), Noble Americas Energy Solutions LLC (“Noble”), and PECO Energy Suppliers Group (“PESG”).

This matter was assigned to Administrative Law Judge (“ALJ”) Cynthia Williams Fordham who held a telephonic prehearing conference on April 10, 2014, at which time a

¹ PECO’s non-residential procurement groups are defined on the basis of peak load, rather than by rate class. The Small Commercial procurement group is defined as all non-residential customers with peak demands less than 100 kW. The Medium Commercial procurement group is defined as all non-residential customers with peak demands greater than or equal to 100kW, but less than 500 kW. For the purposes of this proceeding, the OSBA considers customers in PECO’s Small Commercial and Medium Commercial procurement groups to constitute small business customers whose interests the OSBA is authorized and directed to protect.

procedural schedule and discovery modifications were established, all petitions to intervene were granted, and PECO's motion for a protective order was granted.

The OSBA submitted the Rebuttal Testimony and Surrebuttal Testimony of Brian Kalcic on June 26, 2014, and July 9, 2014, respectively.

An evidentiary hearing was held in Philadelphia on July 17, 2014 (the "Hearing"). At the Hearing, PECO presented oral rejoinder testimony and certain witnesses for the parties were cross-examined. The parties agreed to waive cross-examination of other witnesses prior to the hearings and they were excused from appearing. The testimony and exhibits of the parties were entered into the record.

The OSBA filed its Main Brief on August 5, 2014, pursuant to the procedural schedule. Briefs were also filed by PECO, RESA, OCA, PAIEUG, Noble, and NextEra.

Subsequent to the filing of Main Briefs, the parties engaged in further settlement discussions and were able to agree on a partial settlement, reserving only two issues for litigation, Medium Commercial class procurement and recovery of certain PJM charges. On August 18, 2014, the parties notified ALJ Fordham of the partial settlement-in-principle and requested that the date for Reply Briefs be extended until September 4, 2014.

A Joint Petition for Partial Settlement ("Joint Petition") was filed on August 28, 2014. The signatories to the Joint Petition were PECO, OCA, OSBA, CAUSE-PA, NextEra, and RESA. Direct Energy, FES, IGS, PESG, and Noble filed letters of non-opposition to the Joint Petition and PAIEUG filed a letter of opposition to the Joint Petition. However, the issues raised by PAIEUG were reserved for litigation.

Reply Briefs were filed on September 4, 2014, by PECO, OSBA, PAIUEG, and RESA.

ALJ Fordham issued a Recommended Decision (“RD”) dated September 19, 2014, recommending: (1) approval of the Joint Petition without modification; (2) implementation of hourly priced default service for Medium Commercial customers as outlined in the Joint Petition; and (3) approval of a non-bypassable service charge for all distribution customers for certain PJM charges, but with a carve out for large commercial and industrial (“Large C&I”) customers to allow them to continue to remit transmission and transmission-related charges to their respective electric generation suppliers (“EGSs”).

The OSBA submits these exceptions in response to the RD with respect to the issue of Medium Commercial procurement.

II. EXCEPTIONS

Exception No. 1:

The ALJ erred by failing to provide any legal analysis in support of the recommendation to implement hourly priced default service for Medium Commercial customers. (RD, at 44-45)

The RD provides absolutely no legal analysis to recommend implementation of hourly pricing for Medium Commercial default service customers. Rather, it merely quotes the Commission’s End State Order.² In only one sentence, the RD summarizes the OSBA’s position that legislative changes are a necessary precondition for the End State Order’s recommendations to comply with the Competition Act. Astonishingly, there is literally no discussion of the

² *Investigation of Pennsylvania’s Retail Electricity Market: End State of Default Service*, Docket No. I-2011-2237952 (Final Order entered February 15, 2013) (“End State Order”).

OSBA's valid legal argument that hourly pricing for Medium Commercial customers is contrary to the statutory default service standard as well as prior Commission Orders. Instead, this argument is summarily dismissed.

Moreover, the RD does not even accurately reference the OSBA's legal support for its position on Medium Commercial procurement. The RD instead quotes extensively the OSBA's position on and support of the Joint Petition, which is irrelevant since the Joint Petition explicitly reserves the issue of Medium Commercial procurement for litigation.

In lieu of any legal analysis of the relevant statutes, Commission orders, and Commonwealth Court decisions cited in the OSBA's Main Brief and Reply Brief, this RD appears to rely on the fact that the other parties agree with PECO's proposed method for implementing hourly priced default service for Medium Commercial customers while the OSBA is the only party to disagree, as if Medium Commercial procurement should be resolved by vote of the parties. The poll taken by the RD is not even accurate. PAIEUG unambiguously objected to implementation of hourly priced default service for Medium Commercial customers and in fact submitted a letter in opposition to the Joint Petition. Although PAIEUG agreed with PECO that necessary infrastructure upgrades should be completed prior to transferring Medium Commercial customers to hourly pricing, nowhere did PAIEUG take the position that these customers should be transferred.

The RD provides no basis for the Commission to reject the OSBA's legal argument and approve hourly priced default service for Medium Commercial customers, and therefore this recommendation must be rejected.

Exception No. 2:

The ALJ erred by not recommending approval of PECO's initial proposal to use six-month, fixed price, full requirements, load following contracts without overlap to acquire default service supply for Medium Commercial default service customers. (RD, at 44)

The ALJ erred by recommending that the Commission approve PECO's new procurement proposal for Medium Commercial customers (implementation of hourly priced default service as outlined in the Joint Petition) and not its initial proposal (acquisition of default service supply through six-month, fixed priced full requirements ("FPFR"), load following contracts without overlap). PECO's initial procurement plan for Medium Commercial customers consisting of six-month FPFR contracts will provide reasonable price stability for these default service customers, while still promoting EGS participation in the market. This proposal is the same as that approved for Medium Commercial procurement in DSP II, which as of May 2014 has resulted in approximately 80% of Medium Commercial customers and 85% of the Medium Commercial load being served by an EGS.³ Clearly, EGS participation in the competitive retail market is extensive for this class and has not been hindered by PECO's use of six-month FPFR contracts to procure default service supply. This current procurement plan should be approved again for DSP III.

In contrast, the ALJ's recommendation to implement hourly pricing (as interval meters are installed) will subject Medium Commercial default service customers to unreasonable and unnecessary market price volatility and must be rejected. Hourly pricing will only serve to create

³ PECO Statement No. 2-R at 8.

rate volatility in contravention of the Commission's explicit acknowledgment that rate stability must be a concern when implementing default service standards. Moreover, hourly pricing for Medium Commercial customers is not consistent with Act 129's default service standard of a prudent procurement mix designed to provide the least cost to customers over time.

PECO flip-flopped on its initial position with respect to Medium Commercial procurement late in the stages of this proceeding. After the filing of Main Briefs (where PECO maintained its initial proposal for six-month FPFR contracts), PECO adopted a new position. Specifically, PECO abandoned its price stability arguments against hourly pricing and agreed in the Joint Petition to implement hourly pricing for Medium Commercial default service customers, if ordered to do so, so long as it was given adequate time to complete its advanced meter infrastructure ("AMI") deployment, including testing, implementation of back-office and other information technology systems, and integration with its billing system.

PECO's settlement position relies upon arguments made by RESA, who first proposed hourly pricing. RESA claims that in order to promote retail competition, Medium Commercial customers should have hourly priced default service. RESA's support of hourly pricing is in pursuit of a more market-reflective and market-responsive default service rate.

However, the Commission has explicitly rejected RESA's argument that the "least cost" standard of Act 129 mandates that default service prices be "market-reflective" and "market-

responsive” and has explicitly recognized that price stability should remain an important consideration when designing a default service procurement plan:

We disagree with RESA’s overall recommendations as to the proper interpretation of the “least cost” standard as mandating that default service rates approximate, on a prospective basis, the market price of energy. Such an interpretation would signal retention of the “prevailing market price” standard that has been expressly replaced under Act 129. Moreover, this interpretation conflicts with the Act 129 objective of achieving price stability which dictates consideration of a range of energy products, not just those that necessarily reflect the market price of electricity at a given point in time. Price stability benefits are very important to some customer groups in that exposing them to significant price volatility through general reliance on short term pricing would be inconsistent with Act 129 objectives.⁴

...

Finally, we disagree with RESA’s assertion that the “least cost” standard mandates that a default service plan be reasonably likely to result in a “market-reflective and market-responsive” service rate that recovers all costs related to providing default service. We interpret this standard, not contained in either the Competition Act or Act 129, to mean a preference for short term and spot price supplies which ignore both the Act 129 concerns of price stability and a “prudent mix” of products. We do not believe that adoption of RESA’s suggested standard is consistent with the “least cost” standard contained in Act 129 and would not adequately protect retail customers from volatility and risks inherent in the energy market. Price stability benefits are very important to some customer groups, so an interpretation of “least cost” that mandates subjecting all default service customers to significant price volatility through general reliance on short term pricing is inconsistent with Act 129’s objectives. 66 Pa. C.S. § 2807(e)(3.2).⁵

⁴ *Default Service and Retail Electric Markets*, Docket No. L-2009-2095604, Order entered October 4, 2011 (“Final Default Service Rulemaking Order”) at 39-40.

⁵ Final Default Service Rulemaking Order at 41.

The Medium Commercial customers that remain on default service still value price stability. Thus, there is simply no rational reason to subject the small minority of Medium Commercial customers who have chosen not to switch to an EGS (perhaps because they have received no attractive offers) to the unreasonable rate volatility that would result from adopting hourly pricing.

Moreover, the RD's reliance on the Commission's End State Order as support for Medium Commercial hourly priced default service is misguided. The OSBA acknowledges that the Commission has recommended a progression towards a more market responsive default service product, but disagrees that this recommendation is entirely consistent with the current statute or relevant case law. The End State Order may be viewed as a kind of "wish list" regarding what the Commission envisions for the future of default service. However, its recommendations are not at this time consistent with Act 129 and therefore the Order cannot be treated as a mandate to be implemented in the current round of default service proceedings. Even the Commission is not comfortable with treating the End State Order as a mandate, opting instead to seek legislative changes to avoid legal uncertainty. The Commission's End State Order explains as follows:

While the Commission is steadfast in its view that our decisions to permit [100%] spot market approaches in specific situations are appropriate, we are concerned that a general pronouncement directing a 90-day product for residential and small business customers and an hourly LMP product for "medium" C&I customers may raise legal questions about compliance with the above-referenced provisions of the Competition Act. *To avoid any legal uncertainty, the Commission would prefer to pursue legislative amendments that clearly provide the authority to approve default service plans containing products that more closely resemble current market conditions at the time of delivery.*⁶

⁶ End State Order at 45 (emphasis added).

No such legislative changes have been effectuated. Although the Commission is “steadfast in its view” that 100% spot market approaches are appropriate in “specific situations,” it is precisely the RD’s recommendation to approve an hourly pricing product for Medium Commercial customers that gave the Commission pause and raised questions as to compliance with Act 129.⁷

RESA has argued that the Commission has no cause for concern because 100% hourly pricing for Medium Commercial customers is consistent with existing statutory default service standards.⁸ As support for this argument, RESA points to the fact that the Commission has found that hourly pricing for Large C&I customers of the major Pennsylvania electric distribution companies (“EDCs”), and a 100% spot market procurement plan for Pike County Power & Light (“Pike”), is consistent with the “prudent mix” standard. RESA also argues that the Commonwealth Court’s appellate decision in Pike affirming the Commission’s decision was issued after the End State Order, thus relieving any concerns the Commission might have about its recommendations.⁹

There are several flaws with RESA’s argument. As the OSBA explained in its Main Brief, the two examples that RESA cites (where the Commission deemed a 100% spot market product to meet the prudent mix standard) are distinguishable. First, Large C&I customers are

⁷ *Id.*

⁸ RESA Brief at 14.

⁹ *Id.*

different from Medium Commercial customers, and the circumstances in Pike are different from those in PECO's service territory. The Commission must examine the question of what constitutes a prudent procurement mix designed to provide the least cost to customers over time on a case-by-case basis. Hourly pricing may be prudent for Large C&I customers, but that cannot be extrapolated to mean it is prudent for Residential, Small Commercial, or Medium Commercial customers.

Similarly, in the case of Pike, where a majority of customers are not taking default service, 100% spot market prices may be prudent, but this obviously does not mean that 100% spot market purchases are prudent for all EDCs and all customer classes. Pike is anomalous to other Pennsylvania EDCs and as such, the Commonwealth Court's holding must be read fairly narrowly, *i.e.*, that 100% spot market purchases constitute a prudent mix in the specific and unique circumstances of Pike, but not necessarily in other situations.

As the Commonwealth Court noted in its decision upholding Pike's 100% spot market procurement plan, from Spring 2006, through Spring 2011, an Aggregation Program was in effect, under which most of Pike's customers became customers of Direct Energy and remained customers of Direct Energy after the end of the Aggregation Program.¹⁰ Pike's rationale for its proposed plan was that due to the small size of its default service customer base, it was difficult for Pike to estimate its default service requirements and to negotiate favorable long-term contracts.¹¹ The OCA disagreed and argued that Pike's plan should include financial hedges.¹²

¹⁰ *Popowsky v. Pa. PUC*, 71 A.3d 1112, 1113 (Pa. Commw. 2013), *appeal denied*, 2013 Pa. LEXIS 3288 (Pa., Dec. 31, 2013) ("Pike Decision").

¹¹ *Id.* at 1114.

¹² *Id.*

The ALJ issued a recommended decision recommending that Pike's plan be approved as modified by the OCA's proposal of a fixed-price hedge contract for 1 MW or less of on-peak default service.¹³ The ALJ determined that the hedge contract would introduce greater price stability into Pike's default service pricing and that the costs would not be excessive.¹⁴ The Commission rejected the ALJ's recommendation, finding that it placed too much emphasis on price stability at the expense of lower customer costs.¹⁵ The Commission found that the costs of a fixed-price hedge might cost customers more than fluctuation in spot market prices.¹⁶

The OCA appealed the matter to Commonwealth Court arguing that the Commission's concerns regarding a fixed price hedge were not supported by substantial evidence and that the Commission erred as a matter of law in approving a plan when it included only one source of electricity listed in Section 2807(e)(3.2) of the Competition Act.¹⁷ The Commonwealth Court affirmed the Commission's decision, holding that it did have substantial evidence to support its finding with regard to the hedge.¹⁸ The Court also held that a prudent mix of sources may include only one when this is the most prudent course and is likely to incur the least cost over

¹³ *Id.*

¹⁴ *Id.* at 1115.

¹⁵ *Id.*

¹⁶ *Id.*

¹⁷ *Id.*; see also 66 Pa. C.S. § 2807(e)(3.2).

¹⁸ *Pike Decision* at 1116.

time.¹⁹ The Court found that the Commission had properly taken price stability into consideration and had acknowledged its importance and therefore gave deference to the Commission's decision that the additional benefits of a financial hedge would not be justified by the additional costs.²⁰

Notably missing from the Court's decision is any discussion of or reliance on the alleged importance of market-reflective or market-responsive default service rates. Rather, in determining whether a certain default service product or products were prudent, the Court focused on least cost to customers and price stability.

The circumstances surrounding PECO's procurement are entirely different than in Pike. PECO has a large number of default service customers and is able to estimate its default service requirements and negotiate favorable long-term contracts. Moreover, the "alternate" product at issue in Pike was a hedge-contract, not a FPFR load following contract as proposed here. A hedge contract is intended to ensure against large swings in market prices, but it comes at a cost and does not lock in supply at a fixed price like a FPFR contract.

The Commonwealth Court, if presented with the facts in PECO, would not be held to any sort of precedent set in the Pike Decision. The Pike case is distinguishable and gives little to no guidance on whether hourly pricing for PECO's Medium Commercial customers constitutes a "prudent mix."

Furthermore, the Pike Decision provides no safe haven for implementation of the recommendations in the End State Order. The Commission appeared to recognize that fact in its

¹⁹ *Id.* at 1117.

²⁰ *Id.* at 1117-1118

recent Opinion and Order in the First Energy companies third default service proceeding when it chose not to mention the End State Order when describing the legal standard for default service, citing only to sections of the Public Utility Code, the Commission’s default service regulations and policy statement, and other Retail Market Investigation Orders.²¹

RESA’s argument in favor of hourly pricing for PECO’s Medium Commercial customers incorrectly focuses solely on whether one type of product can meet the “prudent mix” prong of the default service statutory standard. The OSBA certainly does not dispute that the Commission approved solely one-year FPF contracts for Small Commercial customers and solely 6-month contracts for Medium Commercial customers in DSP II, and the OSBA supports PECO’s initial proposal to keep those same procurement plans in DSP III. What the OSBA disputes is not the number of sources, but rather whether hourly pricing for PECO’s Medium Commercial customers is prudent and designed to provide the least cost to customers over time.

It is possible for one product to meet this statutory standard, as it did in Pike. However, the RD does not (and cannot) cite to any testimony or brief in this proceeding that provides evidence or analysis of why the increased volatility of hourly pricing is prudent for PECO’s Medium Commercial customers or that this product is designed to provide the least cost to customers over time. This is because RESA, the party that proposed hourly pricing, rests its entire argument on the End State Order’s focus on market-responsiveness, a factor the legislature affirmatively removed from the statute when it replaced “prevailing market prices” with the

²¹ *Joint Petition of Metropolitan Edison Co, Pennsylvania Electric Co., Pennsylvania Power Co. and West Penn Power Co. for Approval of their Default Service Programs*, Docket Nos. P-2013-2391368, P-2013-2391372, P-2013-2391375, and P-2013-2391378 (Order entered July 24, 2014) at 20-21.

current standard. Although RESA did allege that hourly pricing is a more appropriate default structure for Medium Commercial customers because they are more aligned with Large C&I customers,²² it presented no evidence of any “alignment” with respect to their level of shopping sophistication, economic interests, load profiles, numbers of attractive EGS offers received, etc. The OSBA denies that such alignment exists.

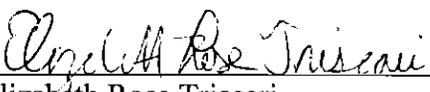
The End State Order’s focus on the market-responsiveness of default service rates rather than a prudent mix of sources designed to provide the least cost to customers over time is simply inconsistent with the plain language of Act 129 and is clearly not what the legislature intended. The RD’s recommendation to implement hourly pricing for Medium Commercial customers because it is consistent with the End State Order must therefore be rejected.

²² RESA Brief at 17.

III. CONCLUSION

Wherefore, the OSBA respectfully requests that the Commission reject the ALJ's recommendation to implement hourly pricing as outlined in the Joint Petition and instead approve PECO's initial proposal to procure default service supply for Medium Commercial customers through six-month, fixed price, full requirements, load following contracts without overlap.

Respectfully submitted,


Elizabeth Rose Triscari
Deputy Small Business Advocate
Attorney ID No. 306921

For:

John R. Evans
Small Business Advocate

Office of Small Business Advocate
300 North Second Street, Suite 202
Harrisburg, PA 17101

Dated: October 10, 2014