



Default Service: Regulated Generation Supply Service in a Competitive Marketplace

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Electric Restructuring in Pennsylvania: Main Elements



- The Electricity Generation Customer Choice and Competition Act (the “Act”) took effect January 1, 1997. 66 Pa.C.S. §§ 2801-2812.
- The Act unbundled electric utility service into generation, distribution and transmission components. Generation represents 60-70% of total bill.
- Electric utilities were reclassified as “electric distribution companies” (“EDCs”), and retained their monopoly on local distribution and transmission service within their territories. Prices for these services would remain regulated through traditional ratemaking principles.
- Retail customers may choose an alternative electric generation supplier (“EGS”) for generation service using the EDC’s distribution and transmission system. EGS prices are not regulated by the Commission.
- EDCs would be entitled to recover the costs of past generation related investments (i.e. stranded costs) from ratepayers. EDCs’ existing generation assets were transferred to their wholesale affiliates.



Transition to Competition: 1998 - 2010



- An EDC was required to offer generation service to all retail customers for as long as the EDC was recovering stranded costs. 66 Pa.C.S. § 2807(e)(1).
- The Act capped the rates that EDCs could charge for these generation services during the stranded cost recovery period. 66 Pa.C.S. § 2804(4).
- The Commission approved stranded costs recovery schedules for each EDC that varied in duration. About 85% of customer load is served under generation rate caps through December 31, 2009. All rate caps will expire in all territories by December 31, 2010.



Post-Transition Period: 2011 -



- The Commission is to promulgate regulations defining the obligation of EDCs towards retail customers not receiving generation service from an EGS. 66 Pa. C.S. §2807(e)(2)
- The incumbent EDC or a Commission approved, alternative supplier shall provide generation service to those retail customers who have not contracted for service with an EGS. 66 Pa. C.S. §2807(e)(3).
- Generation supply for these customers will be acquired at “prevailing market prices.” 66 Pa. C.S. §2807(e)(3).
- This provider of last resort (“POLR”) shall recover “all reasonable costs” of providing this service. 66 Pa. C.S. §2807(e)(3).

Policy Considerations



- Ensure reliable provision of electric generation service to retail customers.
- Ensure that customers' right to choose their own electricity supplier is protected.
- Ensure that electricity prices are set by the market, and not by the Commission.
- Ensure that protections for low-income customers are continued.
- See 66 Pa. C.S. §2802 for complete list of policy findings by the Pennsylvania General Assembly.



Main Elements of Rule

- Regulated generation service is described as “default service.”
- Incumbent EDC shall continue to act as the “Default Service Provider” (“DSP”) within its historic service area.
- EDCs will file a default service program that will identify how it will meet its DSP obligation for a period of several years. Program filing will include an energy procurement strategy, an implementation plan, and a rate design plan.
- All of the DSPs load shall be procured competitively using a bid-based approach, or acquired in the spot market of an RTO like PJM, MISO or NYISO.
- Procurement process will be subject to independent, third-party monitoring.

Default Service Provider Selection

- As a general rule, the EDC shall continue to serve as the DSP for all retail customers within its service territory.
- An EDC may ask the Commission to be relieved of the DSP obligation.
- In that event, a competitive process will be held to determine alternative DSP.
- If no alternative DSP can satisfy technical and financial fitness requirements, EDC must continue to act as DSP.



DSP Obligations



- DSP shall procure sufficient load to meet full requirements of all distribution customers within the EDC territory that it is responsible to serve.
- DSP shall adhere to all applicable Commission rules and regulations
- DSP shall offer same or similar universal service program that was offered by the EDC of that service territory.



DSP Program



- Plan will be for a minimum twelve month period, or a multiple twelve month period.
- Plan will identify fair, transparent, non-discriminatory procurement mechanism.
- Plan will include terms of service for customers.
- Plan will identify a replacement procurement process in the event a supplier defaults.
- Plan will identify the method for complying with Alternative Energy Portfolio Standards Act of 2004.



Default Service Supply Procurement



- All load must be procured through a competitive process or acquired in a spot market.
- DSP's wholesale energy affiliates may be a supplier. Affiliated supplier may not receive any advantage over nonaffiliated suppliers.
- Commission will review procurement process to ensure compliance with plan.



Commission Review Process



- DSP programs will be subject to an evidentiary hearing process.
- Commission will render decision within seven months of filing.
- Commission will evaluate plans to ensure they comply with the regulation and include a reasonable procurement strategy and rate design.
- DSP may implement procurement strategy upon Commission approval of their program.



Customer Migration



- A DSP must accept all new applicants for service, or customers who switch from an EGS, as long as they comply with regulations for applications for service.
- A new applicant for service and an old customer returning to the DSP from an EGS shall be treated the same.
- A default service customer may leave the DSP for an EGS at any time, provided they comply with regulations on changing service.
- A DSP may not charge a fee to a customer that changes service provider in a way consistent with Commission regulations.



Power Procurement Models Managed Portfolio



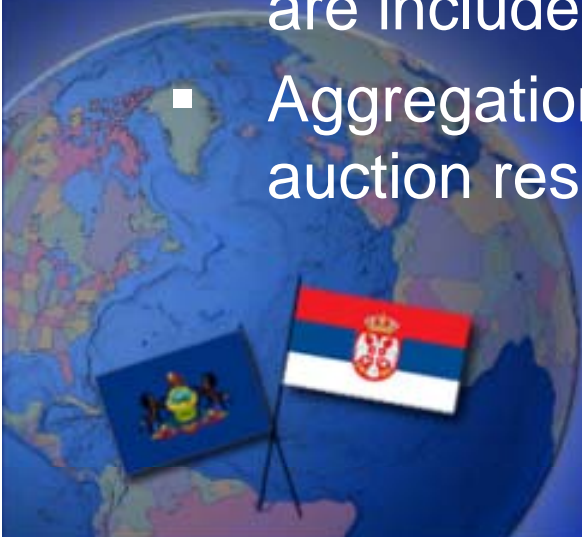
- Two different companies combined default service customer load to improve seller interest due to small load < 70 MW combined.
- Managed program combines specific electric products with target purchase price and/or buy dates. Spot market used as balancing/hedge mechanism.
- Program managed by approved administrator.



Power Procurement Models Aggregation



- Small load unattractive to sellers < 20 MW
- Isolated from dominant Regional Transmission Organization
- load is aggregated for procurement purposes – customers must “opt out” to be excluded
- Sellers bid on aggregated load, knowing all customers are included
- Aggregation model used to correct “perfect storm” auction results



Power Procurement Models

Laddered Contracts



- Auction or RFP based procurement
- Utility load bid out over a series of years
- 1, 2 and 3 year rolling contracts are used to avoid a single point in time market rate
- Bidding can be set up for rate class, slice of load or other load categories



Default Service Rates and Cost Recovery



Funding Mechanisms: Cost Recovery and Reconciliation

Cost Recovery

- The EDC or EGS shall acquire electric energy at prevailing market prices to serve POLR customers and shall recover fully all reasonable costs.

66 Pa. C.S. § 2807(e)(3)



Default Service Rates and Cost Recovery



Funding Mechanisms: Cost Recovery and Reconciliation

Reconciliation of Costs

- **Cost Elements Include:** (1) wholesale energy; (2) capacity; (3) ancillary charges; (4) applicable RTO or ISO administrative and transmission costs. (Congestion Costs will be included within the wholesale energy price)



Default Service Rates and Cost Recovery



- Funding Mechanisms: Cost Recovery and Reconciliation
- **Frequency of Reconciliation**
- Residential and Small Business Classes: will be adjusted at least every quarter providing some variability reflecting market prices
- Large Customer Classes: will be adjusted at least monthly reflecting current market prices
- Rates will be flat, and the price will not decline with cumulative level of demand. No “declining blocks”.



Metering & Billing



- Distribution company function
- Costs recovered in distribution rates
- Data exchange protocols uniform across the state
- Generator information must be provided in “bill ready” or “rate ready” format
- Bills show distinct charges for generation, transmission and distribution
- A “Price to Compare” will be included as a separate line item on each monthly bill to facilitate comparisons to competitive generation service offers of EGSs.

Pricing Policy



- Commission examines acquisition methodology to determine if it will produce appropriate, market-based prices
- If approved methodology is followed, price is assumed to be appropriate unless evidence of fraud or market manipulation exists
- Commission can step in if market anomalies produce skewed prices – see Pike



POLR Service Models Examined by the Commission



- Statewide Competitive Procurement of Wholesale Supply: New Jersey
- Separate Competitive Procurement of Wholesale Supply in each EDC territory: Maryland
- Competitive Assignment of Retail Customer Accounts to EGSs: Texas



Further Information



- Pennsylvania Default Service Rulemaking Process:
www.puc.state.pa.us/electric/electric_last_resort.aspx
- Pennsylvania's Electric Competition Law:
www.puc.state.pa.us/electric/pdf/HB1509P4282.pdf
- New Jersey BGS Auction: www.bgs-auction.com
- Maryland SOS Service:
www.psc.state.md.us/psc/Electric/SOSrates.htm
- Texas Electricity Regulations:
www.puc.state.tx.us/rules/subrules/electric/index.cfm

