Energy Choice Matters

July 23, 2008

PUCT Staff Asks If TDUs Should Be Able to Collect Deposits from REPs

The PUCT Staff has asked whether transmission and distribution utilities (TDUs) should be given greater latitude in managing REP credit risks, such as by allowing TDUs to collect deposits from REPs, as one of several questions issued in advance of an August 15 workshop on REP certification (35767, Matters, 6/16/08).

Staff noted that under current business processes, TDUs can be exposed to providing approximately 85 days of unpaid service due to REP failure. Staff asked how much of that exposure should TDUs be allowed to mitigate, and whether TDUs' latitude to manage REP credit risk should be limited in any way. Should creditworthy REPs be exempt from TDU deposit requirements, or should TDUs offer unsecured credit based on payment history, Staff asked.

The Staff questioned whether the billing cycle in the standard delivery tariff should be shortened to limit exposure and, if so, should REPs be permitted to use shorter billing cycles?

Staff asked whether financial qualifications for REPs should require cash-like assets that can be readily applied to the REP's obligations to refund customer deposits and advance payments and obligations to TDUs, such as posting letters of credit or obtaining surety bonds. Should creditworthy REPs (perhaps those with investment-grade ratings) be exempt from any letter of credit or surety bond requirements, and allowed to continue to maintain customer deposits in restricted cash accounts?

Staff noted that the Commission has drawn funds from letters of credit through the contested-case process, and in one case the process took about six months.

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Ohio Retailers Suggest Credit for Shoppers to Mitigate Anti-competitive Impact of Deferments

Ohio customers served by a competitive retailer (including through municipal aggregation) should be paid a credit reflecting the deferred costs of fuel and power purchases under a utility's standard service offer (SSO), marketers and the Northeast Ohio Public Energy Council told PUCO in comments regarding Staff's proposed default service rules (08-777-EL-ORD, Matters, 7/3/08).

Without such action, deferred power costs would create an artificially low SSO price that would act as a barrier to competition and government aggregation, contrary to statute, the Alliance for Real Energy Options (a group of retailers, IPPs and customers) and NOPEC argued in separate filings. NOPEC called deferrals a "significant economic hurdle" that would prevent large-scale aggregation.

As an initial matter, AREO explained that all fuel and purchased power costs must be bypassable under law. However, when such costs are deferred in an SSO plan, things get complicated. While shoppers could just not pay the deferment at the time it is collected, AREO argued that tracking who does and does not pay deferrals over a long period of time is cumbersome.

Instead, AREO proposed that shoppers receive a per-kWh credit equal to the deferment under the SSO, that would then be paid back by shoppers when the deferred costs are collected under the SSO. The effect would be lowering competitive rates by the same amount that SSO rates are being held down, preserving an apples-to-apples comparison of competitive supply versus default service, AREO noted. NOPEC suggested a similar credit mechanism, though only for customers of municipal aggregation.

Stakeholders predictably varied widely on the types of competitive procurement which should be

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Dominion East Ohio SSO Markup Set at $2.33/mcf

Five winning suppliers competed to set the retail adder for Dominion East Ohio's Standard Service Offer at $2.33/mcf in an auction conducted yesterday. The new markup will take effect Sept. 1, subject to PUCO approval.

The markup, which includes the cost of transporting gas to the LDC, will be added to the monthly NYMEX month-end settlement price for natural gas to set the SSO rate paid by non-shopping customers. Suppliers vied to serve the 400,000 customers (30% of DEO's customer base) who are either not shopping or are not part of a municipal aggregation pool.

The previous markup, set in August 2006, was $1.44/mcf.

The auction was for a bridge SSO until Dominion implements the next phase of its exit from the merchant function, with a Standard Choice Offer, on April 1, 2009 (Matters, 6/19/08).

Potential Penalties In Luminant Case Would be Tied to Bid Curves, not MWs, ALJs Rule

Two ALJs determined in a summary decision that the PUCT's penalty provisions apply to the actions of market participants, and accordingly found that any potential penalties arising from Luminant's alleged manipulation of the market in 2005 would be set according to the number of bid curves involved, rather than the total MWs or MWhs involved (34061, Matters 3/28/08).

In doing so, the ALJs rejected Staff's argument that each allegedly improperly bid MWh would constitute a separate violation, and found Staff's proposed penalty of $171 million to violate the cap on penalties of $5,000/day per violation set in statute and substantive rules.

"[I]t is the act or practice of the market participant that is a violation, not the number of MW or MWh involved in each improper act," the ALJs held. In this case, such acts would be the submission of bid curves. That was the alternate method of calculating any potential penalty proposed by Luminant. Luminant had also proposed that the maximum penalty could only be $5,000/day, or $610,000, but the ALJs rejected that approach.

The maximum penalty potentially faced by Luminant in the case is still in dispute as the number of bid curves involved is a factual question that was not adjudicated in the summary decision. The potential penalty could be either $15,425,000 (according to Staff, who count bid curves in separate zones) or $7,930,000 (according to Luminant).

Luminant had asked for summary decision so that it could gauge its potential liability and factor that into its litigation strategy, including potential for settlement. The ruling did not address any of the factual merits of the case, or make any determination regarding Staff's allegations of manipulation dating back to a 2006 Potomac Economics report.

Direct Access Customers Would Not Get Reprieve from Nonbypassable Charges Under Calif. Draft

The California PUC in a draft decision (R. 06-02-013) would deny the Alliance for Retail Energy Markets' request that bundled service customers who are eligible to return to direct access should be exempt from nonbypassable charges associated with new utility-owned or procured generation when departing bundled service.

The draft affirms that in D.04-12-048, the Commission found that the stranded costs new of generation should be recovered from all customers without exception. Applying the Commission's principle that bundled service customers should be indifferent to the implementation of the nonbypassable charges (neither benefiting nor being harmed), the draft concludes that utilities make procurement commitments on behalf of customers eligible for direct access that are currently on bundled service, and thus such customers should pay a share for supplies bought for their benefit.

Until bundled customers eligible for direct access give notice of their intent to shop, IOUs have no way of knowing if and when such customers will leave bundled service, and thus properly include such customers' load when forecasting supply needs and making procurement decisions, the draft observes.

The draft accepts Southern California Edison's proposal for "vintaging," or assigning a departure date to departing customers in order to determine those customers' generation resource obligations.

Under SCE's plan, customers departing in the first half of the year would have a departure date for vintaging purposes of December 31st of the prior year, while customers departing in the second half of the year would have a departure date for vintaging purposes of December 31st of the year in which they depart. Accordingly, some customers will have an assigned departure date that is earlier than their actual departure date, while others will have an assigned departure date that is later than the actual date.

The draft concedes that grouping customers into two vintaging classes will result in some customers paying for costs incurred after they left, with other customers not paying for obligations made on their behalf before they left. But over time the impact should even out such that the affect on bundled customers is balanced and leaves them indifferent, the draft finds. Tracking the specific date that each customer leaves the utility for cost responsibility purposes would be too cumbersome, the draft added.

Pacific Gas & Electric's alternate proposal which would assign a vintaging date of Dec. 31 for all customers departing in a calendar year would, "almost certainly benefit the remaining bundled customers in the long term," the draft notes, since most departing customers would be assigned a departure date that is later than their actual departure date. That would make them responsible for more costs than what the utility actually incurred on their behalf.

The draft favored SCE's proposal over a similar plan from AReM, which used June 30 as a cutoff instead of Dec. 31, because utilities' Energy Resource Recovery Accounts are based on calendar years.

The draft rejected AReM's recommendation that the nonbypassable charges be included under the 2.7¢/kWh cap applicable to the direct access Cost Responsibility Surcharge, since the cap will have expired for all three IOUs by the end of 2008. The draft is reluctant to reinstate such a cap absent a more definitive showing of need.

Since electric service providers will be receiving Resource Adequacy credits from paying the nonbypassable charges, payments should not be deferred or capped, the draft stated.

The draft also denied AReM's request that the Cost Allocation Mechanism (CAM) be limited to five years, instead of 10. AReM had argued that IOUs' long-term procurement plans are sufficiently flexible to allow them to adjust their portfolios to accommodate significant changes in load within a few years, but the draft found insufficient justification for AReM's proposal. Testimony cited by AReM for setting CAM at five years related to only increased direct access load, the draft observed, while CAM includes existing and increased direct access load, plus departing load due to municipal annexations and customer generation.

Briefly:

Nearly 600 Customers Involved in Green Mountain-W Power Deal

Some 520 residential customers and 60 commercial customers are being sold by W Power and Light to Green Mountain Energy, as we reported yesterday (Matters, 7/22/08). The 60 commercial accounts include 200 ESI IDs.

Christy Continues Wholesale Market Criticism

Few surprises were evident at a Pennsylvania Environmental Resources and Energy Committee hearing on electricity deregulation yesterday, which mainly served as another forum for stakeholders to repeat what they've been saying for over a year as lawmakers debate what to do about rate caps that expire at remaining utilities in 2010 and 2011. Of note is that Commissioner Tyrone Christy continued his criticism of the "broken" wholesale market which, Christy says, isn't producing competitive prices -- a stance Christy has been taking since joining the PUC.

PNM Won't Acquire Cap Rock After All

PNM Resources asked the PUCT to withdraw its pending application to acquire Cap Rock Energy's electric distribution and transmission business (35460, Matters, 3/17/08). The sale of PNM's natural gas business to Cap Rock's parent, Continental Energy Systems, will continue. In order to retain the Cap Rock business, the sale of which was always dependent on the closing of the PNM gas sale, Continental agreed as part of the termination negotiations to pay PNM Resources $15 million, upon the closing of the PNM gas sale.

REP Certification ... *from 1*

By comparison, ERCOT has the ability to draw on a letter of credit and distribute the funds to damaged parties in a matter of days, Staff added. Staff thus asked how the Commission could expedite a draw of funds from a letter of credit, and whether additional authority is needed for such action.

Staff invited market participants to comment on the minimum capital required for the initial start-up operation of a REP, considering initial and near-term liquidity needs for the purchase of wholesale electricity, collateral requirements, computer software and infrastructure, personnel, contract services, commodity risk management, marketing, and legal expenses.

Is it appropriate to incorporate changes in exposure to market risks into the standards, and to limit such risks without added credit (such as restrictions on load growth or the offering of fixed price contracts)?

Staff inquired whether a tiered structure for REP financial standards would be appropriate, with higher requirements for companies with higher levels of exposure to market risks. Should exposure limits (such as load limits or customer deposit restrictions) be imposed on "lower tier" REPs under such a system?

Are separate financial standards for pre-pay REPs needed?

Staff questioned whether REPs should be required to submit quarterly financial reports, and quarterly reports on power acquisition, risk management and current retail contracts.

The Staff sought comments on whether the Commission has the ability to prescribe by rule conditions that would result in automatic suspension or revocation of REP certificates, and under what circumstances would automatic suspension/revocation be appropriate.

If the Commission adopts more stringent certification requirements, should it grandfather existing REPs for a limited period, to permit them to demonstrate that they are in compliance with the new standards, Staff asked.

Comments are due Aug. 12

Ohio SSO ... *from 1*

used to set a Market Rate Offer (MRO) under SB 221.

A descending clock auction or sealed bid RFP could be used, AREO noted, adding that a collaborative workgroup should be established to set the parameters of any method. The FirstEnergy utilities agreed that, "[a] declining clock auction process is a very appropriate method to obtain competitive prices and has been used successfully for a number of years in other states." The FirstEnergy utilities added that an RFP may be more appropriate in other instances, such as for smaller utilities.

The City of Cincinnati, however, cautioned that, "[e]xperiences in other jurisdictions, notably Maryland and Illinois, have shown that a flawed auction structure can produce unnecessarily high prices at auction," though the city did not elaborate as to how the Maryland or Illinois auctions were flawed.

The Ohio Energy Group and several other industrial groups argued that the utility should have an affirmative duty to seek out the "least cost portfolio of generation products." Aluminum manufacturer Ormet suggested a portfolio approach should be contemplated as well.

AREO insisted that bidding should be for full requirements supply because that approach requires wholesale suppliers to take on various risks (weather, fuel price, customer migration) that would otherwise be borne by customers, while producing the lowest fixed price at which customers can be served.

MRO bidding plans should provide for seasonally differentiated summer and winter prices, with retail rates also adjusted seasonally, AREO added.

Congestion costs, which affect the price of energy at a specific point on the grid and are thus "energy" costs, should not be not recovered under a transmission cost recovery rider as currently proposed, AREO contended. They should be in the generation rate.

Adjustments to the transmission cost recovery rate should be automatically triggered if there is an anticipated change of at least 3% in transmission costs, AREO recommended.

The FirstEnergy utilities proposed that PUCO should select winning bidders from the competitive procurement process within three days following the conclusion of the bidding process, since the time period for approval will have a direct impact on price. SSO rates should be published two months before taking effect, AREO urged.

The Staff's proposal that utilities must prove that their SSO filing achieves state policy under SB 221 should be eliminated, Duke Energy Ohio argued, because the statute contains conflicting policy goals. Duke favors evaluating SSO filings on a just and reasonable standard to enable the balancing of interests among the various statutory policies.

While the FirstEnergy utilities agreed that evaluating SSO plans based on their achievement of policy goals is inappropriate given conflicting goals, the utilities argued that the standard of review for an Electric Security Plan (ESP) application under the statute is quite specific. PUCO, by law, must determine whether the ESP "is more favorable in the aggregate as compared to the expected results that would otherwise apply under section 4928.142 of the Revised Code [the Market Rate Offer]," the FirstEnergy EDCs said. Statutes do not authorize PUCO to review whether an ESP or MRO application is generally "just and reasonable" or "achieves" various policies, the FirstEnergy utilities contended.

The FirstEnergy distribution companies also opposed the proposed requirement that the utility list every provision in an ESP that will have an effect to prevent, limit, inhibit, or incent shopping. Since statute contemplates that ESP pricing will be more favorable than current market prices, ESPs, by definition, will adversely affect shopping to some degree, the FirstEnergy utilities noted. "The truism manifested in this proposed rule requirement will not aid the Commission in its determination as to whether to approve an ESP application," the EDCs noted. The FirstEnergy utilities also noted that the proposal, "appears to presuppose that any unavoidable charge will have an effect on shopping." That is not correct, the utilities claimed. Any unavoidable charge related to distribution or past costs will not harm shopping, they argued.

The Ohio Association of School Business Officials and similar groups, however, thought the proposal concerning the disclosure of nonbypassable charges in ESP filings did not go far enough. The proposed rules would require EDCs to provide "an explanation of the component and a descriptive rationale or a quantitative justification" for any unavoidable charges. But, "a descriptive rationale is not sufficient to justify any charges that may inhibit retail competition," the schools maintained. The schools urged that a comprehensive quantitative justification should be required for every unavoidable charge.

Dayton Power and Light opposed the statute's provision that will allow a governmental aggregator to elect to not take back-up service from the utility on behalf of its customers. Customers would be placed on market-based pricing when returning to the utility under such circumstances.

Dayton insisted that government aggregators must obtain customer authorization either through a ballot process or otherwise before the aggregator can place future market price risk on customers without customers understanding the full implications of such a decision.

Dayton also opposed affiliate separation rules which prohibit the utility's affiliate from tying its product or service to the customer taking certain services from the utility.

"This provision is outdated and places the utility affiliate at an unfair disadvantage against other [competitive retail] providers," Dayton claimed.

For example, a competitive retailer may offer certain energy monitoring devices or controls, but those devices may only be beneficial or helpful if the customer is on real-time pricing (RTP) or time-of-use (TOU) rates. Therefore, the affiliate competitive provider may want to only sell such devices to customers that are taking TOU or RTP from the utility, but Dayton believes the rule would prohibit an affiliate from offering such devices, while allowing other competitive providers to offer the products. "There should be no reason why a non-affiliate [competitive retailer] could offer that service and the affiliate [retailer] cannot," Dayton said.

Industrial Energy Users-Ohio complained that Staff's proposal omitted implementing the federal energy advocate contemplated by the statute, and did not address the advocate's role in evaluating the value of the utilities' participation in RTOs.

"The upward trend in electricity prices in recent years is attributable in part to the policies adopted by the Federal Energy Regulatory Commission ('FERC') and the influences and rules of regional electricity markets operated by RTOs," IEU-Ohio stated.

"There are, frankly speaking, too many cases where the organized market advocacy of [distribution utilities] or their affiliates works against the interests of ultimate customers and has an end game that only makes the work of state regulators more difficult. In some cases, the [distribution utility] is not active at all in the organized market debates around issues that affect the physical ability of the [utility] to meet its SSO obligations as well as the [utility's] cost of doing so," IEU-Ohio charged.

In terms of special, discounted contracts to prevent industrials from moving out of state, AREO argued that competitive suppliers should be able to supply such customers under a subsidized contract, in addition to the utilities. Such arrangements should be limited to three years, AREO added, at which time a petition for extension could be filed.