Energy Choice Matters
October 27, 2008

ICC Staff Oppose Nicor's Proposed Reduction in Flexibility for Transportation Customers

Several proposals suggested by Nicor Gas in its rate case would reduce the value of transportation service and should be rejected, Illinois Commerce Commission Staff said in rebuttal testimony filed Friday (08-0363).

Among the Staff recommendations is the rejection of Nicor's proposed reductions in Maximum Daily Nominations (MDN) in July through October. Nicor had justified the changes by arguing they would reduce the need to issue delivery caps on interstate pipelines, but Staff noted the caps are not occurring during the affected months (Matters, 9/29/08).

Proposed reductions in MDN in March and April should be rejected as well, Staff said, as Nicor has not provided compelling proof that transportation customers' actions impose an economic cost on sales (bundled) customers. Nicor's assertion that limiting nomination rights during March and April may reduce the need for delivery caps is not supported, Staff added, as there have not been any caps issued in the past 16 months.

The various MDN reductions would limit nominating flexibility for transportation customers, Staff explained. Nicor data responses show transportation customers would average a 23% loss in injection rights, and a 69% loss in nomination rights during March and a 41% loss in April. "The loss of rights is a detriment to transportation customers," Staff noted.

While Nicor attempts to document and price the lost flexibility that sales customers incur when transportation customers use their storage assets differently than is optimal, Staff found Nicor's study to be based on "faulty analysis and assumptions," as it fails to account for the actions of sales customers.

... Continued Page 5

Accent Not Eyeing Acquisition to Enter New Markets

Accent Energy's heightened focus on acquisition (Matters, 10/24/08) is concentrated on potential asset purchases in its two main markets of ERCOT and New York, and the retailer is not seeking to branch into new markets via acquisition, CEO Lance Schneier told us Friday.

While Schneier would not dismiss any acquisitions which include customers in new markets to Accent, the driving force behind any potential purchase would be the value it holds for Accent's existing markets, Schneier said. Schneier believes such existing market acquisitions would be more productive, because they would allow Accent to bring efficiency gains to the acquired customer book.

The completion of Accent's 2007 acquisition of Dynowatt, including customer integration, took just six weeks, Schneier reported.

Schneier confirmed that a confluence of factors is driving retailers to consider M&A. While this spring's unprecedented volatility in ERCOT alone caused some retailers to pursue asset sales (while others failed), since then more and more factors are piling on retailers' balance sheets. Hurricane Ike hurt retailers from loss of load, the resulting long supply positions, and expenses related to emergency operations or relocation.

The week after Ike hit, Lehman Brothers filed for bankruptcy. Even if retailers were fortunate enough not to have Lehman as a trading partner or creditor, the effects reverberated through the trading and credit markets, pushing up the cost of collateral. Constellation, another active trader, ran into its own troubles, and led to the sale of at least one marketer (Catalyst Natural Gas to MXenergy)

... Continued Page 5

Utility Results Weigh Gains at Exelon Generation

Higher bad debt at Commonwealth Edison and PECO mitigated gains at Exelon Generation and produced quarterly earnings for Exelon Corp. of $700 million on a GAAP basis, down from $780 million in the year-ago quarter.

Adjusted earnings, which exclude hedging gains and other items, were down at $706 million from $823 million in the prior-year quarter. This year's GAAP earnings included mark-to-market gains of $65 million, primarily from Generation's economic hedging activities.

On a GAAP basis, Generation benefited from rising energy prices and higher output with after-tax earnings rising to $635 million, up from $548 million a year earlier. But when adjusted for hedging gains and other items, Generation's quarterly income only grew by $1 million. Revenue from the generation unit grew to $3.1 billion from $2.8 billion a year ago.

Generation's "Market and Retail" sales, which include competitive retail sales in addition to non-affiliate wholesale sales, were down at 29,900 GWhs for the quarter, from 33,100 GWhs a year earlier. Market and Retail margin was up at $65.98/MWh versus $56/MWh a year ago.

Generation's average realized margin on all electric sales, including sales to affiliates and excluding trading activity, was $36.54/MWh in the third quarter of 2008, up from $32.60/MWh in the third quarter of 2007.

Exelon-operated nuclear plants achieved a 97.2% capacity factor for the third quarter of 2008 compared with 97.0% for the third quarter of 2007. The fossil fleet's commercial availability was 95.1% in the third quarter of 2008, compared with 91.6% a year ago.

Generation is over 90% financially hedged for 2009 and over 80% hedged for 2010.

Both ComEd and PECO saw higher levels of bad debt, and ComEd is also seeing lower load growth. While the number of customers being served in the ComEd region increased by 0.3% versus the third quarter of 2007, weather-normalized retail kWh deliveries decreased by 0.2% from the third quarter of 2007, primarily reflecting a decline in usage per customer.

Asked about the lack of resolution regarding potential rate mitigation upon the expiration of rate caps at PECO, CEO John Rowe expects that the issue will continue to come up in every session of the legislature until some solution has been reached. While Rowe doesn't not know the form of an exact solution, his, "best guess continues to be a statewide cost ... something on the level of the statewide cost in Illinois," though he stressed that his statement was not a commitment on the part of Exelon.

As of October 20, 2008, Exelon had $7.3 billion of aggregate bank commitments with a group of 24 banks, excluding commitments previously made by Lehman Brothers Bank. No single bank has more than 10% of the aggregate outstanding commitments at Exelon, and the commitments extend largely through 2012. As of October 20, 2008, Exelon had utilized approximately $500 million of its capacity under its facilities, leaving $6.8 billion of the total $7.3 billion of capacity available to Exelon. In addition, Exelon had a total of $35 million of commercial paper outstanding.

Shoppers Won't Benefit, Could Be Harmed from Delmarva Land-Based Wind PPAs

The costs and benefits from land-based wind PPAs between Delmarva's Delaware distribution company and three wind projects will initially be allocated to all SOS customers (including hourly-priced customers), the Delaware PSC said in a written order released last week following the approval of the PPAs earlier this month (Matters, 10/9/08, 08-205).

However, the Commission ordered Staff to monitor customer migration away from SOS, and reserved the right, pursuant to statute, to implement a nonbypassable surcharge in the event that any of the PPAs carry above-market costs and SOS experiences significant migration.

In effect, shoppers lose out almost regardless how things work out. If the wind PPAs are below market as expected to be, shoppers won't share any of the benefits. However, if the PPAs suddenly become above-market, shoppers, who were denied any benefits when the PPAs were below market, could be forced to shoulder the above-market costs of the PPAs.

New Energy Opportunities, a consultant for the PSC, expects the wind contracts to be below-market and provide savings to SOS

customers of $0.64/MWh (for the AES contract), $0.14/MWh (Synergics Roth Rock), and $0.22/MWh (Synergics Eastern).

In light of the relatively small size of the PPAs relative to customer loads (up to 170 MW nameplate capacity), the PPAs would have to be substantially above-market or below-market to make a significant difference, New Energy Opportunities said.

Pricing for both Synergics contracts is $81/MWh (2009 dollars), with an annual escalation rate at the lower of 50% of the increase in the consumer price index or 2.5%.

The bundled rate for energy and RECs for the 70-MW option under the AES PPA is $94/MWh without any escalation factor.

Consumer Advocates Assail Peevey Alternate on AB1X Rate Protections

Consumer advocates urged the California PUC to reject an alternate proposed decision by PUC President Michael Peevey which would decline to rule on when residential rate caps under AB1X end (A. 07-01-047).

The question arose in an application from San Diego Gas & Electric, which sought to roll-off the existing residential rate caps (Matters, 10/3/08). The original proposed decision concluded that the AB1X protections last through 2022, when the Department of Water Resources bond charges for power procurement are fully paid off. DWR will have ceased physically supplying power before then (2016 or sooner), but will still be paying bond charges through 2022.

Peevey's alternate draft decision concludes SDG&E cannot raise residential rates as proposed because DWR at this moment is still physically supplying power to the IOUs. Because DWR is still supplying power, Peevey's proposal sees no need to address the question of when the AB1X protections expire, as the question would not affect the current case. Essentially, the Peevey draft would decline to rule on whether the DWR bond charges should be treated as a "cost of power," as AB1X imposed the rate cap until all the costs of DWR power have been recovered.

However, TURN argued that the Commission should adopt the original proposal because the issue at hand is purely one of law and not of policy. "Prolonging the current state of regulatory uncertainty for any longer than is absolutely necessary does not serve the public interest and only threatens to consume the resources of this Commission and the parties on additional rounds of repetitious and wasteful litigation," TURN said.

The legal question which the Peevey draft refrains from deciding is "clear cut and not at all difficult to resolve," TURN added.

The Division of Ratepayer Advocates made similar arguments, noting that the Peevey draft, "acknowledges the Commission's lack of authority to terminate AB1X protections, but unnecessarily prolongs an issue that currently has a clear legal answer that should put the matter to rest."

SDG&E found the Peevey proposal to be only "marginally" better than the original draft, because it fails to recognize that if the Commission doesn't address the termination of the AB1X rate cap, "disastrous consequences will ensue." SDG&E cited the cost shifting currently occurring under the AB1X rate caps, explaining that the caps contravene Commission goals for transparent pricing, cost-based rates, energy efficiency, demand response, and dynamic pricing.

Integrys, Enbridge Marketers Fined for Capacity Release Violations

Integrys Energy Services will pay an $800,000 civil penalty and disgorge $194,505.78 plus interest in unjust profits under a stipulation between the marketer and FERC's Office of Enforcement approved by the Commission last week.

The stipulation resolves self-reported violations of FERC's capacity release policies by Integrys Energy Services, including circumvention of the posting and bidding requirements for released capacity, and violations of the shipper-must-have-title (SMHT) requirement.

As part of an internal investigation, Integrys Energy Services determined its predecessors WPS Energy Services and WPS ESI Gas Storage engaged in "flipping" transactions involving approximately 5.8 Bcf of natural gas

transported intermittently during the period January 2004 through April 2006.

Flipping involves a series of repeated short-term releases of discounted rate capacity to two or more affiliated replacement shippers on an alternating monthly basis, which avoids the competitive bidding requirement for discounted long-term capacity releases. The effect of flipping can be to create a long-term, non-competitive discounted rate release.

The two WPS companies engaged in flipping by taking discounted short-term firm capacity released by a shipper on the ANR LINK system on an alternating basis during thirteen of the winter months of 2004, 2005, and 2006, FERC said. The flipping transactions were used by the WPS companies on 277 days to transport 5,808,437 Dth of gas.

The flipping transactions denied other market participants an opportunity to bid for discounted, long-term releases of capacity that may not have otherwise been available from the pipeline or other releasing shippers, FERC said. In addition, as a result of the flipping arrangement, Integrys Energy Services obtained pipeline capacity at favorable rates and in a manner that adversely affected the transparency of the secondary market for natural gas transportation and storage served by the ANR LINK system, the Commission added.

While flipping is a "serious" violation because it avoids competitive bidding for discounted capacity, FERC said that Integrys Energy Services' flipping was not wide-spread, as it was limited to a series of winter period releases on the ANR LINK system, and involved less gas than other cases previously before the Commission. The $194,000 disgorgement stems from the flipping transactions.

Integrys Energy Services also committed shipper-must-have-title violations involving the transportation or storage of up to approximately 6.7 Bcf of natural gas between April 1, 2004 and April 1, 2007, occurring on two interstate pipelines and storage facilities.

Violations of the shipper-must-have-title requirement interfere with the Commission's oversight of natural gas markets and interfere with the Commission's goal of market transparency.

FERC also approved a stipulation between enforcement staff and Enbridge Marketing under which Enbridge will pay a civil penalty of $500,000 for self-reported shipper-must-have-title violations. The violations involved the transportation of approximately 30 Bcf of natural gas between August 2004 and May 2007 over several interstate pipelines.

Briefly:

Md. PSC Orders Reserve Bid for Some Residential, Type I Load

The Maryland PSC accepted most of the Type I and Type II SOS procurements conducted on October 20, but ordered a reserve auction for the Baltimore Gas & Electric residential blocks and the Delmarva combined residential and Type I blocks because no acceptable bids were made for those blocks. All the winning bids for the Type II blocks, BGE's Type I block, Allegheny Power's residential blocks, and Pepco's combined residential and Type I blocks were found to be acceptable and were awarded. Liberty Consulting Group, the bid monitor, found that "the most severe financial crisis in generations" had a "substantial impact" on bid prices. While the Office of People's Counsel recommended rejecting the combined Pepco residential and Type I blocks, the Commission approved all of the acceptable bids, with its reasoning to be detailed in a forthcoming order. The reserve tranche bid date for BGE's residential blocks (17) and Delmarva's combined residential and Type I blocks (3) is November 10, 2008.

Mass. DPU Sets Renewable Long-Term Contracting Meeting

The Massachusetts DPU set for November 5 a stakeholder meeting in Boston to assist with development of rules necessary to implement provisions of the Green Communities Act requiring distribution companies to enter into cost-effective long-term contracts with renewable energy generators (08-88). Statute defines a long-term contract as a contract with a term of 10 to 15 years, and may be for energy, RECs, or both.

Reach Energy Adds Trade Name

The PUCT approved Reach Energy's application to add the trade name Gulf Coast Distribution Company to its REP certificate.

Usource Sales Margin Ticks Upward

The sales margin at broker Usource grew to 1.1 million in the third quarter from 1.0 million a year ago as parent Unitil reported net income of $1.5 million for quarter, a down a tick from earnings of $1.6 million in the year-ago quarter.

Commerce Energy to be Own QSE, Retain Expertise of Tenaska

Commerce Energy has applied to ERCOT to act as its own QSE, although it will continue to use the services of Tenaska Power Services, its current QSE, through an Agency Agreement, Commerce reported in an SEC filing. As part of the change, Commerce and Tenaska jointly terminated their August 1, 2005 QSE and Marketing Services Agreement effective on the earlier of (i) November 5, 2008 or (ii) the time ERCOT completes the move of Commerce's LSE from Tenaska's QSE to the new Commerce QSE. Commerce said there are no early termination penalties with Tenaska.

Allegheny Urges Speed for Smart Grid Review

Allegheny Power asked the Maryland PSC to expedite its review of Allegheny's proposed advanced utility infrastructure pilot project, which would test smart grid applications for 1,140 customers (Matters, 9/2/08). Allegheny proposed the smart grid pilot because traditional demand response products are not cost effective in its territory. With smart grid technologies, however, load response benefits could be pooled with other operational benefits. Allegheny wants to have the pilot ready for summer 2009, and will need 16 weeks to procure needed equipment.

Nicor ... from 1

Staff suggested that Nicor Gas should implement a pilot program to provide the evening nomination (6 PM) on a firm basis and the Intra-day 1 nomination (10 AM) on a best-efforts basis to determine the feasibility of such service. "This pilot program would provide a measured step toward balancing the flexibility clearly enjoyed by Nicor Gas while not burdening Nicor Gas with an unworkable solution," Staff said.

Nicor should also implement the trading of stored gas under the same circumstances approved at Peoples Gas and North Shore Gas, Staff recommended.

Staff detailed additional objections to Nicor Gas using its website and call center to market affiliates' products, and offered further support for an investigation into Nicor's affiliate agreement (Matters, 10/24/08).

"Any website that appears on a customer's bill should not have a link to affiliates' resources," Staff argued, which is currently occurring at Nicor.

Nicor Gas' bills direct customers to a Nicor, Inc. website which houses the Nicor Gas utility's online services, but also links to Nicor's competitive supply and energy services affiliates, promoting non-regulated products and services. Nicor Gas technically does not have its own website as its online services are hosted by Nicor, Inc. Through the site, customers can access information about the products and services of Nicor Gas' unregulated affiliate, Nicor Advanced Energy. While all the other alternative gas suppliers are linked on the site, they are not allowed to solicit customers through the Nicor, Inc. website.

Staff is "troubled" by the use of Nicor Gas' website for affiliate marketing, and said it would be advisable for Nicor Gas to have its own website instead of a website owned or operated by a parent or affiliate.

Data responses from Nicor also make it clear that Nicor Gas is using its call centers to market affiliate products and services to its customers.

"This is inherently unfair to other providers of gas commodity and related products and services," Staff said.

Accent ... from 1

when it terminated a supply and credit agreement. Just as credit becomes more costly and the market more illiquid, retailers are facing heightened liquidity requirements to continue operations in Texas (Matters, 10/23/08).

Throw in ongoing margin compression, and it's easy to see why some entrepreneurs may be questioning their business model and looking to get out. But it's not just troubled REPs which may be up for grabs, Schneier noted. Principals at successful retailers may see this as the perfect time to monetize their investment, given some of the challenges ahead. Whatever the reason, Accent is looking for its next growth opportunity.