Energy Choice Matters

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NRG More Than Triples Earnings on Strength of Reliant Energy

Reliant Energy posted net income of $233 million and adjusted EBITDA (excluding mark-to-market impacts) of $230 million for the last two months of the second quarter, driven by strong margins, parent NRG Energy said in an earnings report.

Reliant gross margin totaled $320 million, including "strong" margins in the residential customer segment and "expanding" margins in the commercial and industrial segment driven by the lag between significant declines in energy costs and corresponding retail price reductions. Average customer margin was $30.77/MWh.

NRG said this benefit will be partially offset in future periods as a result of two price reductions undertaken since acquiring Reliant.

"Competition, along with the Company's pricing and supply decisions, will likely drive lower margins in the future and the Company believes that, in order to stabilize customer count, this level of margins will not be sustainable," NRG added.

Still, while NRG CEO David Crane does not expect to achieve such margins continuously, Crane said that in a low commodity price environment, Reliant can probably get above the "mid-level" margin of around $20/MWh Reliant previously used as a goalpost.

Warm weather resulted in higher volumes despite a 1% decrease in customer count over each of the past two months. Mass market weighted average customer count stood at 1.6 million, with the larger C&I customer count standing at 71,000.

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PUCT Defers Ruling on Termination Fee Petition

The PUCT took no action on an emergency petition to require REPs to suspend termination fees for the months of August and September, and invited stakeholders to file briefs on legal questions raised by the petition by next Thursday.

Rep. Sylvester Turner and several consumer groups, after the Commission denied a disconnect moratorium, asked that the Commission impose a suspension on termination fees to facilitate customer switching to low priced plans through the end of the summer, and also asked that REPs be required to send additional notices to customers regarding the Lite-Up discount (Matters, 7/20/09).

At yesterday's open meeting, Turner suggested that the termination fee suspension

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ICC Broadly Defines ABC in Licensing Rule

"Based on a plain reading of the [ABC] Act," the Illinois Commerce Commission ruled that the definitions of "attempts to procure" and "attempts to sell" are broader than what an ALJ recommended in a proposed order to establish rules governing ABC licensing and behavior. Accordingly, the ICC modified the ABC rules, and directed that the rules be submitted to the Joint Committee on Administrative Rules to begin the second notice period.

Under the ABC law, ABCs subject to the law's code of conduct and licensing provisions are those entities which attempt to procure or attempt to sell electricity, with various exceptions (such as for a retail supplier acting on its own behalf).

As only reported in *Matters*, an ALJ had

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One-Off Bad Debt Charge Weighs Direct Energy Results

Direct Energy reported "disappointing" results for the first half of the year, parent Centrica said, as a one-off bad debt charge and lower commodity prices impacting Direct's upstream business offset retail customer growth and improved commercial and industrial results.

Direct's operating profit fell 50% to $91 million from $181 million for the first half of 2008, largely on a one-off charge of $75 million to increase the bad debt provision against final debt in Texas following a change in methodology to better reflect the chances of collection from customers who have left Direct. Mass market operating profit was down at $60 million from $122 million a year ago. Commercial and Industrial operating profit grew to $29 million from $16 million for the first half of 2008.

Centrica Group Finance Director Nick Luff said Direct did experience high gross margins, and absent the one-off bad debt charge, mass market results would have shown a "healthy" increase.

Mass market customer count increased 2.7% to 3.12 million from 3.03 million a year ago. Direct said it has surpassed 500,000 customers in the U.S. North market, with over 100,000 additions in the Northeast in the last 12 months.

In Canada, Direct scaled back customer acquisition activity, particularly on fixed-price long-term contract deals, where the capital support required is significant. As a result, customer numbers there were broadly flat.

Direct said its customer count in Texas fell as competitors passed through wholesale price reductions quicker than Direct did, as a portion of Direct's power requirements for 2009 had been bought forward at higher prices in 2008, restricting pricing flexibility.

Mass market revenues were down 21% at $2.1 billion.

Commercial and Industrial electric sales were up 68% at 15.5 GWh, and C&I gas sales were up 10% at 400 mmth, primarily from the Strategic Energy acquisition. C&I revenues increased 38% to $2 billion. Luff said Direct has been able to achieve higher C&I margins due to the capital constraints of several competitors.

Cost synergies resulting from the Strategic acquisition are expected to exceed original expectations of $15 million per annum, Direct said.

Centrica Chairman Roger Carr said North America will be an increasing focus for Centrica, and reiterated Centrica's intent to develop North America as an integrated business similar to the U.K. model. Centrica Chief Executive Sam Laidlaw said priorities for the North American market include:

- Improving efficiency in operations;
- Expanding Direct's presence in key markets
- Supporting Direct's supply positions with appropriate levels of asset integration to provide robust returns through the commodity cycle

Direct's Home and Business Services unit saw flat operating profit of $5 million as improvements in the Canadian business were offset by deteriorating conditions in the U.S. Direct grew Canadian home services customer relationships by 29,000 over the first six months and also reduced costs.

Upstream and wholesale energy delivered an operating loss of $4 million versus a profit of $37 million for the first half of 2008. Aside from lower spark spreads in Texas, Direct recorded a one-off exceptional charge of $82 million on its wind farm tolling agreements in west Texas with current forward prices being significantly below its contract cost, due to the combination of lower general wholesale prices and the local impact of transmission congestion over the next few years.

Direct has also temporarily curtailed its ongoing drilling program in Alberta as it became less economic. Direct did increase its reserves base in the first half of the year by around 50 bcfe through some small scale acquisitions.

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Next week, *Matters* will be re-launching its subscriber referral program. As part of that, please feel free to share this issue with any co-worker or colleague, sales channel, vendor, or other market participant/stakeholder that might be interested in today's stories.

SouthStar Continues to Battle Fierce Georgia Competition

SouthStar Energy Services reported second-quarter 2009 EBIT of $5 million, compared with $6 million in the second quarter of 2008, as the marketer continues to face increased competition in the Georgia market, AGL Resources said yesterday.

Earnings were hurt by a decline in average customer count and a change in the retail pricing mix, with a higher number of customers on lower-margin fixed pricing plans as compared to last year. Georgia margins continue to be compressed from increased competition, and churn induced by competitive pressures produced a 4% decline in average customer count and a 6% decline in market share at SouthStar for the six months ended June 30, 2009, as compared to the same period of 2008.

Operating margins in the Ohio and Florida markets also were down slightly during the period relative to the prior year, though customer growth in those markets continues to be more rapid than anticipated.

AGL Resources said it has resolved a lawsuit filed by Piedmont Natural Gas over their respective ownership shares of the SouthStar joint venture. Under the settlement to be effective January 1, 2010 with Georgia PSC approval, SouthStar will purchase an additional 15% ownership share in SouthStar from Piedmont for $57.5 million, resulting in AGL owning 85% of the SouthStar joint venture. AGL Resources will be entitled to 85% of the annual earnings from the business, while Piedmont will retain the remaining 15% share. AGL's interest will remain a non-controlling interest and AGL will not have any further option rights to Piedmont's remaining 15% ownership interest.

MISO Files Changes to Limit Certain Interchange Schedules

The Midwest ISO filed proposed tariff revisions at FERC to clarify the timeline for submitting Interchange Schedules, reflecting recent Business Practices Manual changes, to prevent potentially inefficient schedules meant to take advantage of profit opportunities caused by Interchange Schedule timing requirements.

The Midwest ISO permits Interchange Schedules to begin or end every 15 minutes on the hour, quarter-past the hour, half-hour, or quarter-till the hour. In addition, the Midwest ISO requires that all Interchange Schedules be submitted at least 30 minutes prior to the start of the Interchange Schedule. This effectively allows a market participant to submit or modify an Interchange Schedule for the last 15 minutes of an operating hour up to fifteen 15 minutes into the same operating hour, therefore allowing the market participant to see the real-time Locational Marginal Price for a portion of the hour in which the transaction will take place.

Additionally, the Midwest ISO's market settlement rules provide for the integration of five minute prices over the operating hour to create an integrated hourly LMP at which all transactions in the operating hour are settled. The combination of interchange scheduling flexibility and the settlement of transactions at the integrated hourly LMP regardless of the length of the transaction has created an incentive for market participants to submit or modify Interchange Schedules during the last 15 minutes of the operating hour in a manner that may not result in efficient dispatch for the 15 minute period, but when settled at the hourly LMP, may result in a profitable transaction.

The Independent Market Monitor has noted various potential impacts of such behavior, including requiring MISO to ramp generation up or down substantially to accommodate the schedules, and the fact that an intra-hour schedule may not bear the full cost of the schedules' impact on Revenue Sufficiency Guarantee charges.

Accordingly, in June, MISO implemented revisions to its Physical Scheduling Business Practices Manual which prohibit the submission or modification of Interchange Schedules during the operating hour except for reliability purposes as determined by the Midwest ISO. MISO said during the period of May 31, 2009 through, June 4, 2009, only 1.3% of the total transactions for the time-period would have been affected by the proposed change, which is designed to prevent the submission of Interchange Schedules during an operating hour after a market participant has seen LMPs that will be included in the integrated hourly settlement price for that operating hour.

MISO is applying at FERC to clarify its tariff to be consistent with the new Business Practices Manual language. Specifically, the tariff revisions would hold that a market participant may not submit, or modify, Interchange Schedules during the operating hour except for reliability purposes as determined by the Midwest ISO. MISO said that the clarification does not disallow "intra-hour" scheduling in the sense that market participants may continue to submit, or modify, Interchange Schedules up to 30 minutes prior to the start of a transaction to the extent that the submission or modification does not occur within the operating hour (i.e., a market participant may submit an Interchange Schedule 15 minutes prior to the hour with a start time of quarter past the operating hour).

Briefly:

Scana Energy Loss Grows on Bad Debt, Lower Volumes

Scana Energy reported a seasonal loss of $3 million in the second quarter of 2009, compared to a seasonal loss of $1 million a year ago, due to increased reserves for bad debt, lower volume, and share dilution. At June 30, 2009, Scana Energy was serving approximately 447,000 customers in the Georgia gas market, which it said maintained its position as the state's second largest natural gas marketer.

PUCT Says HB 1822 Requirements Take Effect Upon Adoption of Rules

The PUCT agreed with Staff's interpretation that various provisions of HB 1822, governing fixed price contract expiration notices and common billing terms, take effect upon adoption of rules by the Commission, which must be adopted by December 1, 2009. Accordingly, REPs will not have to meet a September 1 compliance date for HB 1822 provisions. However, the Commission declined to provide any guidance on enforcement of new Substantive Rule §25.475 for the period between when it takes effect August 15 and whenever subsequent changes to the rule related to HB 1822 are adopted. Chairman Barry Smitherman said enforcement should be left at Staff's discretion. The Commission also approved for comment, as recommended by Staff, proposals for publication regarding fixed price contract expiration notices (37214, Matters, 7/30/09), and common billing terms (37070, Matters, 7/24/09).

ICC Estimates Alternative Compliance Payment Rates

The Illinois Commerce Commission issued an order reporting that the current estimates of the actual alternative compliance payment rates applicable to alternative retail electric suppliers for the June 2009 to May 2010 plan year is 0.0645¢/kWh at the Ameren utilities and 0.0764¢/kWh at Commonwealth Edison. The actual alternative compliance payment rates will not be known until the completion of the planning year, but since the sole utility REC procurement has concluded, Staff said the alternative compliance payments (which are linked to utilities' renewable compliance costs) may be estimated with a relatively high degree of accuracy. The ICC also established the maximum alternative compliance payment rates as 0.0938¢/kWh at Ameren and 0.1007¢/kWh at ComEd.

Md. PSC Delays Constellation-EDF Decision Beyond Desired Closing Date

The Maryland PSC has pushed back its timeline for reviewing EDF's proposed 49.99% investment in Constellation Energy's nuclear unit such that it will not begin hearings until September 14 (lasting through September 18), meaning the Commission will not issue a ruling on the application by the desired closing date of September 17. The Commission said additional time is required to allow parties to conduct discovery, and said an order would be issued by October 16. Constellation said it was "disappointed" in the procedural ruling, adding that, "[a]ny delay in a transaction of this magnitude adds to the risk of it not closing, which would be a real loss for Maryland."

PUCT to Study Quickstart Generation, Administrative Scarcity Pricing Issues

The PUCT will open a project and/or workshop on quickstart generation in the context of wind and reserve margin needs and related issues, including, at the request of Commissioner Donna Nelson, the issue of administrative scarcity pricing.

PUCT to Open New Docket on Entergy Issues

The PUCT will open a new docket to cover issues related to the newly formed Entergy regional state committee, which will be evaluating whether the Independent Coordinator of Transmission should continue, whether Entergy should join the SPP RTO, and related issues. The Commission also formally closed Entergy's transition to competition docket.

PUCT Approves Direct Energy Billing Settlement

The PUCT approved a settlement with Direct Energy under which Direct will pay $200,000 for the failure of Direct to timely remit monthly bills to customers in April 2009, caused by a complication with the move to a new billing system (Matters, 6/22/09).

PUCT Staff Moves to Dismiss Texas Electricity Aggregation Application

PUCT Staff, in an unopposed motion, moved to dismiss without prejudice the aggregation application of Texas Electricity Aggregation, which has been abated due to a dispute regarding its similar name to current aggregator Texas Energy Aggregation (Only in Matters, 2/13/09). Texas Electricity Aggregation said it wished to withdraw the application but was unable to formally do so at this time.

ACE, JCP&L Issue Solar REC RFP

Atlantic City Electric Company and Jersey Central Power & Light announced an RFP for solar RECs (www.njedcsolar.com). A total of 61 MW of solar generating capacity - 19 MW for ACE and 42 for JCP&L -- will be procured over the next three years. The New Jersey BPU also approved solar REC procurements for Rockland Electric totaling 3.8 MW.

Reliant ... from 1

"The recent price reductions for certain mass customers are expected to improve customer retention. Further price reductions may be necessary if current attrition trends continue," NRG said in a 10-Q.

Total revenue from Reliant was $1.25 billion on 10,431 GWh. Mass market revenues were $761 million; larger C&I revenues were $437 million; and revenues from the sale of excess supply were $52 million. Regarding its re-launched larger C&I business, Reliant said it has seen increased interest in its product offerings and is experiencing profitable margins within the segment. Variable rate contracts tied to the market price of natural gas accounted for approximately 68% of the contracted volumes as of June 30, 2009

Cost of energy, excluding unrealized gains and losses on derivative contracts for energy supply, totaled $930 million. Other operating expenses incurred during the quarter totaled $90 million and included $25 million of expenses associated with the call center, billing, credit and collections; $40 million of selling, general and administrative expenses; $16 million of gross receipts tax; and $9 million of bad debt expense.

Although NRG has begun the process of becoming the primary provider of Reliant's supply requirements, Reliant presently purchases a substantial portion of its supply requirements from third parties. Crane said NRG would provide more details on how the hedge books of its generation business in Texas and Reliant's wholesale supply will be synchronized at an analysts day in November.

Crane is also confident, due to high demand in June and July, that Reliant should comfortably exceed its guidance of $400 million in adjusted EBITDA for the year.

Wholesale, Corporate Results

At the corporate level, NRG reported higher net income of $433 million versus $127 million a year ago, driven by Reliant's contribution and the sale of its stake in German mining company Mibrag. Income from continuing operations before taxes was $582 million versus a $94 million loss a year ago. Operating expenses for the second quarter included $4 million in Exelon defense costs, $21 million of acquisition costs and $2 million of integration costs associated with the acquisition and integration of Reliant. Adjusted EBITDA, excluding mark-to-market impacts, for the second quarter was $747 million, an all-time high for NRG.

Total generation declined 13% and 20% in NRG's baseload and gas fleets respectively, driven by the economic slowdown, an unseasonably cool start to summer in the

Northeast, lower natural gas prices, and the scheduled outages to install environmental back-end controls at Dunkirk. The Northeast coal fleet was particularly impacted by the reserve shutdowns across the region.

Texas generation adjusted EBITDA (excluding mark-to-market) decreased by $169 million to $346 million compared to the second quarter of 2008. Realized power prices in the 2008 quarter were $17/MWh higher which, combined with higher volume, resulted in $114 million higher energy margins in the second quarter of 2008 versus 2009.

Northeast generation adjusted EBITDA (excluding mark-to-market) was $117 million, a $4 million increase compared to the same quarter in 2008. Energy margins were $13 million higher in 2009 as contributions realized from NRG's hedging program and contract revenue more than offset lower market prices and reduced generation. Generation in the second quarter of 2009 was 50% lower compared to 2008, resulting in a $39 million decrease to energy margin. The lower volume was offset by an increase of $24 million in contract revenue due to lower cost to serve load obligations and a $29 million increase in realized margin per MWh due to portfolio hedging.

Termination Fees ... *from 1*

only apply to REPs not offering superior customer protection alternatives such as a voluntary disconnect moratorium.

While withholding judgment until the next open meeting, Commissioners appeared wary of the requested relief with respect to termination fees, as it would change the applicable market rules on a retrospective basis to previously negotiated contracts. Chairman Barry Smitherman had serious concerns about the legality of disrupting privately negotiated contracts and any termination provisions contained therein, and was especially concerned about selectively applying a termination fee suspension to only a subset of REPs.

Commissioner Donna Nelson noted that if the Commission engages in retroactive changes, it will impose a cost on REPs. Those costs will either be passed through to customers, or cause REPs to go bankrupt or opt to leave the ERCOT market, either of which would harm customers as well. Nelson said that the Commission should not take any action that would cost all customers in the long run.

Smitherman said that the question of termination fees should be evaluated in the Commission's proceeding to develop a permanent set of disconnection rules, but in his initial thoughts, the Chairman fears preventing their use will simply cause REPs to raise prices to cover churn-related risks. Smitherman also noted that in the past he has opposed attempts to change the rules in the middle of the game, adding that regulatory certainty has attracted investment to Texas.

Turning to Turner's report filed Wednesday which alleged some 17 REPs were not complying with PUCT substantive rules regarding levelized payment plans (Only in Matters, 7/30/09), Commissioner Kenneth Anderson said he has directed the Enforcement and Customer Protection Staffs to investigate the issue. Anderson was "disturbed" by the information presented by Turner, and Nelson likewise said it is "unacceptable" for REPs not to follow Commission rules. Smitherman reminded stakeholders that the Commission wants to know when REPs misbehave and encouraged parties to bring any instances to the Commission's attention. REPs operating outside the boundaries will be punished, Smitherman said.

Texas Ratepayers Organization to Save Energy also reported that a customer calling the Lite Up Texas call center was denied enrollment as the customer service representative said that, due to the enrollment timeline, the customer would not be placed in the program prior to the final seasonal discount. However, enrollments are supposed to be accepted at all times as enrollment with LIDA also triggers customer eligibility for waivers from late payment fees and the ability to pay deposits in installments. After the matter was brought to Staff's attention, the LIDA call center underwent retraining and the representative involved is no longer working on the LIDA program.

Texas Legal Services Center corrected an error in a pleading filed yesterday by Rep. Sylvester Turner, which referenced an unsuccessful suit against the PUCT's 2006 disconnect moratorium. TLSC said the suit was brought by Firefly, and not REPower as incorrectly stated in Turner's pleading due to TLSC's incorrect information.

ABC Law ... from 1

recommended that "attempts to procure" should be defined as meaning only ABCs that have been provided with the authority by a retail customer to sign contracts for the purchase of electric power and energy on behalf of that customer (Matters, 1/15/09). The Commission called such a definition inconsistent with the Act's stated purpose of customer protection. The ICC found that Section 16-115C of the Public Utilities Act necessitates that ABC licensing must occur before ABCs enter contractual relationships with either buyers or sellers, not afterward.

Accordingly, the Commission modified the definition of "attempts to procure" to be:

> "Attempts to procure" means a third-party individual or entity which takes a substantial step to Procure electric power and energy, such as but not limited to preparing solicitations, notifying potential bidders of the solicitation, or determining the results of a solicitation; except, it shall not include an individual or entity providing professional services incidental to the procurement of retail service, such as but not limited to legal, accounting or engineering services.

The provision exempting services incidental to procurement is meant to assuage concerns raised by certain suppliers that the broader definition would cause attorneys, accountants, bookkeepers, or financial advisors to be licensed as ABCs.

The Commission also modified the definition of "attempts to sell" as follows:

> "Attempts to sell" means a third-party individual or entity which takes a substantial step to sell electric power and energy to end user customers, such as but not limited to soliciting customers, making offers or preparing contracts; except, it shall not include an individual or entity providing professional services incidental to the sale of retail service, such as but not limited to legal, accounting or engineering services.

The ICC removed a second part of the proposed "attempts to sell" definition which had referenced, "an individual or entity who receives compensation, salary or other remuneration from a [retail supplier]." The Commission was concerned that the stricken language could have been construed as applying to salaried employees of a supplier, even though the ABC Act exempts any licensed retail supplier acting on its own behalf from the ABC rules.

Rejecting a recommendation from several suppliers, the Commission declined to allow ABCs to comply with the required disclosure to customers of ABCs' anticipated remuneration through an oral disclosure. Consistent with the Act, the ICC will require all ABCs to provide written disclosure of their remuneration prior to entering into the contract. The disclosure statement must also be signed by the customer.

The ICC also rejected recommendations from certain suppliers to prevent competitors from filing complaints under the ABC rules and from requesting hearings in ABC license applications.

First Choice, Constellation Earnings Preview

First Choice Power is announcing today ongoing quarterly earnings of $12.6 million, compared with losses of $13.0 million in 2008. GAAP earnings were $16.0 million, compared with 2008 losses of $60.4 million. Lower power prices significantly improved average retail margins during the quarter. Margins are expected to return closer to traditional levels as wholesale markets stabilize. Bad-debt expense increased $1.1 million to $10.1 million in 2009. Customer count at quarter-end was 243,300 versus 253,800 a year ago.

Constellation Energy posted lower quarterly net income of $8.1 million, compared with $171.5 million a year ago, reflecting the negative impact related to several divestitures plus merger and joint venture transaction costs. Excluding those impacts, earnings beat analyst expectations, driven by "strong" wholesale and retail margins. Constellation's customer supply unit, however, was flat versus a year ago as lower operating costs and earnings from the sale of wholesale contracts were offset by lower wholesale volumes.

More coverage in Monday's issue.