

COMMONWEALTH OF PENNSYLVANIA  
SENATE OF PENNSYLVANIA

PUBLIC HEARING ON ENERGY POLICY FOR PENNSYLVANIANS

BEFORE

CONSUMER PROTECTION & PROFESSIONAL LICENSURE COMMITTEE:

SENATOR ROGER M. TOMLINSON, CHAIR  
SENATOR LISA M. BOSCOLA, MINORITY CHAIR  
SENATOR EDWIN B. ERICKSON  
SENATOR JOHN R. GORDNER  
SENATOR MARY JO WHITE  
SENATOR GERALD J. LaVALLE

- and -

ENVIRONMENTAL RESOURCES AND ENERGY COMMITTEE

SENATOR MARY JO WHITE, CHAIR  
SENATOR EDWIN B. ERICKSON, VICE CHAIR  
SENATOR RAPHAEL J. MUSTO, MINORITY CHAIR  
SENATOR MICHAEL W. BRUBAKER  
SENATOR DONALD C. WHITE  
SENATOR ANDREW E. DINNIMAN  
SENATOR BARRY J. STOUT

Date : June 5, 2007, 10:00 a.m.  
Place : Majority Caucus Room, No. 156  
Capitol Building  
Harrisburg, Pennsylvania  
By : Patricia M. Brown  
Reporter - Notary Public

1       SPEAKERS:

2

3       DEPARTMENT OF ENVIRONMENTAL PROTECTION

4       OFFICE OF ENERGY AND TECHNOLOGY DEPLOYMENT

5             DANIEL J. DESMOND, DEPUTY SECRETARY

6

7       PUBLIC UTILITY COMMISSION

8             WENDELL F. HOLLAND, CHAIRMAN

9             JAMES H. CAWLEY, VICE CHAIRMAN

10            KIM PIZZINGRILLI, COMMISSIONER

11            TERRANCE J. FITZPATRICK, COMMISSIONER

12

13       OFFICE OF CONSUMER ADVOCATE

14            IRWIN A. POPOWSKY, CONSUMER ADVOCATE OF PENNSYLVANIA

15

16

17

18

19

20

21

22

23

24

25

1           CHAIRMAN TOMLINSON: Good morning. I'd like  
2           to call this joint hearing to order, and I'd like  
3           to thank everyone who has joined the committee  
4           today to hear the testimony on energy policy for  
5           Pennsylvania.

6           The Consumer Protection Committee and  
7           Professional License Committee has jurisdiction  
8           over the regulations of the Public Utility  
9           Commission which sets the prices for electric and  
10          gas rates to customers, ensuring the energy is  
11          provided in a safe and reliable manner.

12          I would like to thank Senator Mary Jo White  
13          and her counsel Patrick Henderson for their help  
14          in planning and executing this hearing.

15          For the Consumer Protection Committee, this  
16          is the second hearing that we've had in a series  
17          of public hearings on the cost of energy and what  
18          the future of the market is in Pennsylvania. We  
19          have already had one hearing specific to the issue  
20          of electric rate caps.

21          With respect to the history of the energy  
22          policy in Pennsylvania, I am one of the few  
23          remaining legislators that was originally here at  
24          the first vote on the restructuring. Overall, I  
25          believe it has brought benefit to Pennsylvania in

1           ways, in more ways than just freezing the cost of  
2           electric rates.

3           The law of 1996 stimulated discussion about  
4           what the future of energy systems and the  
5           consumption would be in 1996 and beyond. It also  
6           started policy makers thinking about alternative  
7           energy and conservation.

8           Our purpose today is to begin to measure the  
9           success of these policies and to begin to shape  
10          the policies for the next few years and perhaps  
11          the decades to come. I would like to thank those  
12          who are here to testify for their thought  
13          provoking ideas and their attendance to the  
14          hearing.

15          With that, I'd like to introduce Senator Mary  
16          Jo White.

17          CHAIRWOMAN WHITE: Thank you, Senator  
18          Tomlinson. I will waive opening remarks in the  
19          interest of leaving plenty of time for questions  
20          because I know there will be plenty. As you can  
21          see, there is considerable overlap on the Consumer  
22          Protection Committee and the Environmental  
23          Resources and Energy Committee. And I thank the  
24          chairman for agreeing to combine these so that the  
25          members can efficiently gather a great deal of

1 information, so thank you for being here today.

2 CHAIRMAN TOMLINSON: With that, we'll get  
3 started. And with that, I'd like to introduce  
4 Daniel J. Desmond, Deputy Secretary, Office of  
5 Energy and Technology development.

6 MR. DESMOND: Thank you, Senator. Chairwoman  
7 White, Chairman Tomlinson, Chairwoman Boscola,  
8 Chairman Musto, we very much appreciate, and  
9 members of the committee, the opportunity to be  
10 here to provide some views and some testimony  
11 regarding some of the very real energy supply and  
12 affordability issues facing all Pennsylvanians and  
13 in addition the significant economic development  
14 opportunities that will ensue with the passage of  
15 Governor Rendell's energy independence legislative  
16 initiatives.

17 I emphasize that because from the beginning,  
18 this administration has wanted to make the case at  
19 every turn that the protection of the environment  
20 is not at all an undue burden on the economy.  
21 Indeed, no economy can exist where there is  
22 unrelenting depletion of the resource base upon  
23 which that economy depends.

24 And so we have wanted to show how green tech,  
25 clean tech, environmentally beneficial and benign

1 jobs and investment in Pennsylvania can serve the  
2 dual objectives of enhancing and growing the  
3 Pennsylvania economy as well as protecting our  
4 environment.

5 We have a number of legislative initiatives  
6 before you. You're familiar with Senate Bills  
7 715, 716, and also our PennSecurity Fuel  
8 Initiative 789 and the energy independence fund  
9 initiative. Now, rather than go into that in  
10 detail, I'm going to give, as I said, an overview  
11 of the energy situation both globally and here in  
12 Pennsylvania as we see it.

13 If anything can be agreed upon in an area  
14 that is often contentious and which has numerous  
15 views and points of departure from one another, it  
16 is that the past is not likely to be prologued  
17 when it comes to energy supply and energy prices.

18 This country peaked its oil production in  
19 1970. The North Sea peaked in 1998. We've got  
20 states all over the Persian Gulf that are  
21 beginning to peak. And when an oil field peaks,  
22 it doesn't mean that it's running out. But it  
23 does mean that production henceforth will begin to  
24 decline.

25 And running short is what we're finding in

1 the world today, not only in our capacity to bring  
2 more crude oil online because at a global level,  
3 we're drawing down three barrels of oil from  
4 ancient declining fields for every one new field  
5 that is being discovered, despite record high  
6 prices and the natural incentive to go out and  
7 explore for more oil.

8 Much of the oil as you may know is in the  
9 hands of nation states. Our U.S. oil companies  
10 are drilling mightily, and some of them have made  
11 some important finds. But alas, those finds are  
12 enough barely to keep pace with the rate of growth  
13 and demand.

14 On top of that, we have a situation with  
15 refining in this country which is driving the  
16 price of gasoline ever skyward. With the oil  
17 mergers of the last fifteen years, we've had more  
18 and more refineries, especially the smaller  
19 marginal refineries that were closed while the  
20 larger refineries were expanded and run perhaps  
21 greater than a ninety-five percent capacity.

22 That's put a lot of strain on the system.  
23 And as our demand for liquid fuels continues to  
24 grow, because we don't have all the refinery and  
25 supply, elasticity that we would like to have, we

1           have been depending more and more on imported  
2           gasoline.

3                     There's gasoline going into your tank here in  
4           Harrisburg that's coming from the Virgin Islands,  
5           from France, from the United States, from India.  
6           Gasoline is fungible. Once it comes into New York  
7           harbor and goes in the pipeline system, we never  
8           know from whence it came.

9                     However, it's important to note that just as  
10          our dependence on foreign oil has grown from  
11          twenty-five percent back in the early 1970's to  
12          around sixty-five percent today, the same thing is  
13          happening with a dependence on imported foreign  
14          gasoline.

15                    For example, up until recently we might have  
16          had only about ten percent of our gasoline in this  
17          country come from abroad. But because inventories  
18          are at a record low, last week alone we hit  
19          seventeen percent. Some of this gasoline is not  
20          always coming from friendly sources. And again,  
21          dependence on foreign supply chains for something  
22          that is absolutely essential to our economy is  
23          something that we cannot continue to let go  
24          unattended. That's why our energy independence  
25          strategy is so important, the independence fuels

1 fund called PennSecurity.

2 We believe that we can offset with  
3 Pennsylvania based biofuels at least a billion  
4 gallons of liquid refined product that's currently  
5 going into our marketplace. That happens to be  
6 the equivalent of what we're importing from the  
7 Persian Gulf at present.

8 And so for those who say that we are forever  
9 going to be dependent on oil from unstable parts  
10 of the world, we think that that's profoundly  
11 untrue. We think that helping Pennsylvania  
12 farmers and Pennsylvania biofuel industry  
13 investors who want to build these clean fuel  
14 refineries here in Pennsylvania is the right path  
15 for us going forward, and we encourage your  
16 support of that.

17 In addition, our legislation asking for a  
18 systems benefit charge to be put in place on  
19 electric rates that will generate over seventy  
20 million dollars a year we think is absolutely  
21 vital. We're going forward into an era where  
22 electric prices as has happened in adjacent states  
23 are going to continue to rise, and we can do one  
24 of a few things.

25 We can shrug and say, Well, the price of

1 everything is going up, therefore the price of  
2 electric power has to go up. Or we can examine  
3 some of the drivers behind the increases in  
4 electric power both now and in the future and see  
5 what we might do about it.

6 One of the drivers, of course, has been a  
7 pricing formula which worked well at the time  
8 called locational marginal pricing. It worked  
9 well because at the beginning of this decade there  
10 was not much of a disparity between the energy  
11 cost of a thousand cubic feet of natural gas and  
12 coal or nuclear.

13 But what happened is that there was some  
14 severe underestimates of the rate of depletion of  
15 natural gas both here and in Canada. And as a  
16 consequence, its demand continued to grow.  
17 Natural gas prices began to decline.

18 And what happens today is because natural gas  
19 powered electric power plants are usually  
20 dispatched at the very end on the margins when  
21 there's a call for demand, we have a pricing  
22 policy where the cost of natural gas is given to  
23 everybody.

24 So it's like you went to a farmers' market  
25 and you were buying apples from five or six

1 different vendors and they all had different  
2 prices; but before you left, you were going to be  
3 obliged to pay everybody the price the highest  
4 priced vendor sold. And that is the problem that  
5 we are facing with pricing right now.

6 So one of the ways to mitigate that -- well,  
7 there's several ways to mitigate that. One of the  
8 ways to mitigate that is to have policies in place  
9 that will encourage much more in the way of  
10 conservation and managing peak demand load. If we  
11 can manage peak demand load during the hundred,  
12 two hundred hottest hours during the year or  
13 heaviest hours during the year, sometimes it's a  
14 winter peak, we can drive down prices because  
15 we're not using so much expensive high priced  
16 marginal fuel.

17 Nearly thirty percent of the hours last year,  
18 we had the cost of natural gas driving the cost of  
19 coal fired and nuclear fired electricity. This is  
20 an unnecessary and needless burden for  
21 Pennsylvania rate payers that is avoidable.

22 To give you an idea of how easy it is to  
23 conserve energy, the building that we're sitting  
24 in here in the capitol is part of the fleet of  
25 buildings that is managed by our Department of

1           General Services. In the past year, the  
2           Department of General Services has cut our energy  
3           bill by nearly ten percent in these buildings.  
4           And it was not necessarily by installing new  
5           energy conservation equipment. All of that  
6           savings came as a result of what we call habits of  
7           mind, turning the thermostat up or down when it's  
8           no longer needed for extra heating or cooling,  
9           turning the lights off, doing other things to use  
10          our energy wisely.

11                   And so if we can shave off ten percent just  
12          with habits of mind, with a program of consumer  
13          education and the right kind of price signals  
14          offered to the purchasers of electric power in all  
15          sectors, we can have a very significant cut off  
16          our peak demand. That in turn will lower our  
17          electricity bills that all of us are paying.

18                   The other thing that I wanted to address is  
19          where we see this going in terms of the broader  
20          level of investment in jobs and economic  
21          opportunity. Let's look at our solar industry,  
22          for example. We have had in the past year half a  
23          dozen foreign solar companies plus one successful  
24          Pennsylvania-based company knocking on our door  
25          talking to us about plans to expand solar

1           electricity. I can tell you that for all of the  
2           people who are concerned about the price of  
3           alternative energy, if you integrate it properly  
4           with today's grid, it needn't be expensive at all.

5                     For example, I have 1500 watts of solar power  
6           on my garage roof. I also have a ground source  
7           heat pump. When I'm away at work and the sun is  
8           shining, my meter is running backwards. That  
9           builds up a credit against my home energy bill,  
10          and my cost of heating and cooling therefore is  
11          virtually nil.

12                    Now, imagine if I and you and all of us had  
13          what we call smart meters where we not only could  
14          build up this credit for generating power at small  
15          and medium scale facilities but supposing we could  
16          take that power using smart meters and aggregate  
17          it. If you can aggregate power in megawatt  
18          quantities, you can then go out and sell that  
19          power in the wholesale market the same as if it  
20          was a power generator. It's just that it's  
21          thousands of small distributed sites rather than  
22          one large central generation site.

23                    So smart meters will allow us to grow the  
24          market for solar and small scale wind and biomass  
25          which includes farm methane digesters that will

1 help cut down not only on pollution from farm  
2 nutrients but will help farmers enhance their  
3 bottom line by generating electric power from  
4 something that otherwise would be an  
5 environmentally hazardous waste.

6 So we have opportunities if we implement this  
7 legislation to spur entire new industries and  
8 entire new markets, to use energy and particularly  
9 electric power in ways that we had not considered  
10 before.

11 Similarly, our cool small appliances bill,  
12 the largest energy user in any given household  
13 after the air conditioner typically is the  
14 refrigerator. Refrigerators last a very long  
15 time. If we can have incentives to help consumers  
16 swap out inefficient old air conditioners and  
17 refrigerators, that alone is a whole set of  
18 appliances that happen to turn on at the  
19 residential and small business level at the very  
20 wrong time of day sometimes, adding to the load on  
21 the power grid. So we can have initiatives in  
22 place that will promote the sales and marketing of  
23 new appliances, that will cut power on the grid,  
24 and will make it unnecessary to build new electric  
25 power plants.

1           The most important aspect of our package  
2           though is what we call, commonly called megawatts.  
3           The least expensive power we will ever use is  
4           power that we never use, and the way to achieve  
5           that is to recognize that to invest in  
6           conservation and efficiency is considerably less  
7           expensive than investing in new capacity. And we  
8           know that investing in conservation and efficiency  
9           will not only save rate payers money, but it will  
10          certainly contribute less in terms of harmful  
11          emissions to our environment.

12           However, looking forward, we have some  
13          significant challenges before us. As you know,  
14          the demand for electric power, the demand for  
15          motor fuels continues to grow in an unrelenting  
16          fashion; and yet our resource base is not  
17          infinite.

18           If you were to build a new environmentally  
19          compliant power plant today and started with a  
20          blank piece of paper, it would be easily five  
21          years and probably the better part of a billion  
22          dollars before that plant was up and running.

23           As a consequence, we have to do things now,  
24          not a year from now or two years from now. We  
25          cannot chose the times that we live in, nor can we

1 determine whether the times that we spend on this  
2 earth will become historic times. But it so  
3 happens that these are historic times for America  
4 and for Pennsylvania's energy future.

5 I don't believe that a future governor, a  
6 future legislature, a future set of public  
7 officials will be able to have the impact that all  
8 of us will if we work together now and find some  
9 common strategies and some common focus to put in  
10 place policies and initiatives that will not only  
11 reduce our electric energy costs, help our  
12 environment, but will create a vibrant and  
13 important new green economy for the Commonwealth  
14 of Pennsylvania.

15 So with that, I'm going to wrap up and ask if  
16 there are any questions. I'd be happy to answer  
17 them.

18 CHAIRMAN TOMLINSON: Thank you very much.  
19 I'd like to recognize Senator Mary Jo White.

20 CHAIRWOMAN WHITE: Thank you, Senator.

21 I agree with a lot of what you said. I'm  
22 particularly interested in your observations about  
23 the shutting down of the small refineries and the  
24 impact that it had on energy supplies in this  
25 country because I'm very concerned about the

1 potential for the shut-down of the small  
2 coal-fired power plants, and I'm afraid that we're  
3 headed in exactly the same directions.

4           Legislation given us by the governor for the  
5 energy independence strategy, I didn't see  
6 anything and I'm wondering if the administration  
7 would be adverse to the idea of providing some of  
8 this money to keep the small coal-fired power  
9 plants operating by giving them whether it be  
10 loans, grants, things to help them comply with the  
11 new environment regulations so that they can be  
12 clean burning and continue to be part of our  
13 energy supply.

14           MR. DESMOND: I think that all of the  
15 provisions will be on the table for discussion.  
16 And I agree with you that the small emergent power  
17 plants -- first of all, many of them are  
18 circulating fluidized bed plants; and they are  
19 among the cleanest of the fossil fuel generators  
20 that we have. The contracts under which many of  
21 them are operating right now, the so-called PURPA  
22 contracts are set in expire in the last few years.  
23 And frankly, our power system cannot afford even a  
24 small deficit of supply.

25           So if there are strategies that we can

1 continue to use these power plants, especially if  
2 we can enhance them and improve -- they're  
3 already, you know, clean emissions -- and build  
4 additional clean coal plants that could have  
5 things like carbon sequestration built in and  
6 engineered into the design to anticipate some  
7 future time when carbon sequestration will be  
8 either mandated or technically and economically  
9 feasible, I think we do need to understand that  
10 coal will remain a critical energy asset for  
11 Pennsylvania going forward.

12 Even the small emergent plants, especially if  
13 they were, say, able to do long-term contracts  
14 with off-takers, that would be another very good  
15 way of refinancing and reinvesting in these  
16 important assets.

17 CHAIRWOMAN WHITE: I'm going to ask about the  
18 eight hundred pound gorilla because there is  
19 nothing being said about the possibility of  
20 attracting nuclear power plants.

21 We have Westinghouse in Pittsburgh building  
22 nuclear power plants all over the world, and yet  
23 we haven't sited any in the United States. It  
24 seems to me if you're looking for a long term  
25 solution, particularly one that is pollution free,

1 that nuclear should be part of the discussion.

2 MR. DESMOND: Nuclear continues to be  
3 discussed seriously and in some instances by  
4 people who heretofore were opposed. But I must  
5 say, just looking at our own history, the ghost of  
6 TMI like Marley's ghost continues to rattle its  
7 chains here in the Commonwealth of Pennsylvania,  
8 Senator.

9 And while it is likely that there will be  
10 some reexamination of the role of nuclear power in  
11 the US, I don't think get the feeling that that  
12 would happen any time soon in our state.

13 That's a personal view. It's not an official  
14 administration view.

15 CHAIRWOMAN WHITE: There's a little known  
16 tradition in the governor's legislative proposal  
17 that essentially turns PETA into a state power  
18 authority with the ability to buy and sell and  
19 trade and hold power. Why aren't we doing that,  
20 and would they be subject to public utility  
21 regulations?

22 MR. DESMOND: Yes, I believe they would. But  
23 the issue here is not to become a state public  
24 power authority. That provision is to allow us to  
25 do joint ventures with large scale projects that

1           might be building advanced small-scale clean power  
2           where we might want to take some of the power as  
3           part of the deal. It's not for us to become a  
4           public power authority. That was not the intent.

5           CHAIRWOMAN WHITE: Thank you. Thank you, Mr.  
6           Chairman.

7           CHAIRMAN TOMLINSON: Thank you, Senator  
8           White. Senator Erickson? Senator Gordner?

9           SENATOR GORDNER: Good morning. A number of  
10          the type of energy such as ethanol or wind  
11          actually have generated issues with local places  
12          where these might be sited. And certainly I think  
13          wind energy was one of those. Looking at our  
14          state, it seemed like a great opportunity.  
15          Ethanol as well in regard to the products used to  
16          make it.

17          How do we go about dealing with some of the  
18          public issues and local issues that have risen up,  
19          and is there different things the administration  
20          is doing in order to address them?

21          MR. DESMOND: Yes. That's a good question.  
22          One of the things we can do is to make sure that  
23          people who have concerns about either biofuel  
24          plants or wind farms understand what current best  
25          practice and state of the art is.

1           Some of the early biofuel plants may have had  
2           some local problems with neighbors that are not  
3           part of the engineering design or the output of  
4           current biofuel plants. We have to make sure that  
5           the developers of these plants communicate  
6           adequately. For example, if they have organic  
7           filters, to make sure that there's no odors,  
8           things like that.

9           As far as wind farms are concerned, again, we  
10          need to make sure that people understand that with  
11          natural gas which is our marginal generating fuel  
12          right now, at a certain price point, wind  
13          completes directly with it on the power grid.

14          Once you're over about five dollars and a  
15          half per cubic feet, wind is the next cheapest  
16          fuel. So as long as we have occasional marginal  
17          pricing, we need to be sure people understand that  
18          we need inexpensive marginal energy generators.

19          Finally, Governor Rendell has made it clear  
20          that Pennsylvania is a very diverse state. And  
21          there are some communities frankly that don't want  
22          new development of any kind, energy or no. There  
23          are other communities which welcome the jobs.

24          And the governor has said that given a  
25          choice, he would much rather see us work with

1 communities around the state who welcome these new  
2 economic investment opportunities, and there are  
3 many, rather than go into areas where it will be  
4 contentious and possibly delayed.

5 CHAIRMAN TOMLINSON: Senator Brubaker?

6 SENATOR BRUBAKER: Thank you, Mr. Desmond,  
7 for your excellent testimony. It's always a  
8 pleasure to be with you.

9 I read recently, I believe it was Wall Street  
10 Journal about a week ago, eighty-six percent of  
11 the nation's fuel comes from fossil sources, eight  
12 percent nuclear, and six percent renewable. Are  
13 those numbers reasonably accurate in your opinion?

14 MR. DESMOND: They may be accurate  
15 nationwide. They're not accurate for  
16 Pennsylvania. I believe our nuclear contribution  
17 is better than twenty, twenty-five percent, in  
18 that area.

19 SENATOR BRUBAKER: Thank you. And you said  
20 in your testimony that it's your goal to create a  
21 billion dollars of Pennsylvania biofuels. Is that  
22 accurate?

23 MR. DESMOND: We want to offset a billion  
24 gallons of existing gasoline and diesel.

25 SENATOR BRUBAKER: Is that a one-to-one

1 offset?

2 MR. DESMOND: Yes. We want a billion gallons  
3 in the market. There are some triggers in the  
4 legislation to make sure that we don't get ahead  
5 of the market in having this requirement. We  
6 will, both our agency and the Department of  
7 Transportation, will certify that both the  
8 production and the transport infrastructure is in  
9 place to supply those quantities of fuels, both  
10 for biodiesel and for ethanol.

11 SENATOR BRUBAKER: I'm a huge proponent of  
12 moving in that direction, although I do have some  
13 concerns about market overreaction. Is it true  
14 that we typically plant seventy-two million acres  
15 of corn in the country and this year we're going  
16 to plant ninety million acres of corn and we're  
17 doing that because of the speculative market,  
18 looking for corn to fuel our ethanol plants? Is  
19 that accurate?

20 MR. DESMOND: That has been alleged by many  
21 in the agricultural community. One of the things  
22 though that I do want to point out, there is I  
23 think some misinformation going about to the  
24 effect that to make ethanol is to deprive us of  
25 food.

1           Right now every ethanol plant operating in  
2           the United States has contract market outputs for  
3           the distillers' grain that is left over. All we  
4           do is take the starch out of the corn. We leave  
5           the protein and other nutrients for animal feed,  
6           so I think it's important to understand that if we  
7           build an ethanol plant and it uses a cereal grain  
8           like corn, the residual from that operation still  
9           goes into the animal feed market.

10           SENATOR BRUBAKER: Understood. But we have a  
11           hundred and thirty ethanol plants in the United  
12           States today approximately. Is that accurate?

13           MR. DESMOND: Yes.

14           SENATOR BRUBAKER: And we have seventy that  
15           have been green lighted for construction in this  
16           country. Is that accurate?

17           MR. DESMOND: Sounds reasonable. I don't  
18           have the exact data. It sounds reasonable.

19           SENATOR BRUBAKER: That's a very, very  
20           significant market shift in a very short period of  
21           time.

22           MR. DESMOND: Here in Pennsylvania while they  
23           all aren't at the permit or financing stages,  
24           there's forty-six biofuel plants being proposed.  
25           About three quarters of them are biodiesel.

1           But let's say half of them get built. This  
2           will become a very important biofuel refinery and  
3           distribution economy as a consequence.

4           SENATOR BRUBAKER: I just want to be very  
5           clear that again I'm very supportive of an  
6           initiative like this moving forward, but I am  
7           concerned about market overreaction. I'm fearful  
8           we're right close to that edge.

9           We have record corn prices right now, record  
10          soy bean prices; and most people believe that that  
11          is speculative markets in effect because of the  
12          soy diesel and the ethanol.

13          MR. DESMOND: Yes. But, Senator, one of the  
14          things that is not too many years away is what we  
15          call cellulosic ethanol and also biodiesel from  
16          algae. We're going to have other means and other  
17          feed stocks from which to make these biofuels, and  
18          that will have a mitigating effect on speculative  
19          prices for cereal grains.

20          SENATOR BRUBAKER: I'm glad you brought that  
21          up. Mr. Chairman, may I ask one more question?

22          CHAIRMAN TOMLINSON: Okay.

23          SENATOR BRUBAKER: On cellulosic technology,  
24          I'm glad you brought that up, are plants being  
25          built today so that they can convert from corn

1 base to cellulosic technology?

2 MR. DESMOND: Yes. Indeed the ethanol plant  
3 that's being built in Clearfield County has into  
4 its design a pilot cellulosic production  
5 component, and we think that upwards of ten  
6 percent of the fuel coming out of that plant may  
7 indeed be cellulosic ethanol in a few years.  
8 So it's not if you build a conventional distillery  
9 that all of the hardware and infrastructure then  
10 becomes redundant if in future cellulosic becomes  
11 the dominant technology.

12 CHAIRMAN TOMLINSON: Senator Dinniman?

13 SENATOR DINNIMAN: There's always unintended  
14 consequences with our efforts at alternative  
15 energies. What is the department doing,  
16 administration doing to keep track so that we  
17 don't have something occur that we don't want to  
18 have occur?

19 For example, we talked about wood chips  
20 becoming now part of diesel fuel. Would there  
21 might be an environmental consequence of that as  
22 there is in ethanol the possibility of  
23 environmental consequences? What is the  
24 administration doing on a continuing basis to make  
25 sure that we don't do damage to the environment

1           that we didn't intend to do?

2           MR. DESMOND: Well, any of the facilities  
3           that come into the marketplace to the extent that  
4           they use water resources or have emissions going  
5           into the air are going to have to meet the same  
6           stringent state and federal guidelines that  
7           conventional fuels needs to make, so that's one  
8           check.

9           But the other thing that we're looking at,  
10          Senator, is more related to market and volatility  
11          of price. For example, the pellet stove market  
12          recently has played havoc with the price of wood  
13          chips which has had an impact on, say, poultry  
14          houses that use it for litter.

15          So one of the things we're looking into is  
16          ways that we can encourage what are called biomass  
17          plantations. We have millions of acres of  
18          reclaimed coal lands in this state that easily you  
19          could plant switch grass, you could plant hybrid  
20          poplar or willow, very, very fast growing trees  
21          that could be turned into wood chips.

22          And the nice thing about it, if we establish  
23          these separate large-scale biomass plantations, we  
24          will not then have undue impact on the forest  
25          products market for pellets or for broiler litter

1 or other things.

2 So we are definitely looking down the road  
3 and looking where our sources of supply will come  
4 from as well as making sure that these  
5 technologies are not only compliant, but we expect  
6 them to be cleaner and do a better job than the  
7 fuels that they supplant.

8 SENATOR DINNIMAN: Thank you.

9 CHAIRMAN TOMLINSON: Senator Don White?

10 SENATOR DON WHITE: No questions.

11 CHAIRMAN TOMLINSON: Senator Stout?

12 SENATOR STOUT: Yes. Thank you, Mr.

13 Chairman. Mr. Desmond, I'm very confused. Does  
14 Pennsylvania have the ability to meet all the  
15 energy needs here in the Commonwealth today and  
16 over the projected next five years?

17 MR. DESMOND: Over the projected next five  
18 years if we do nothing, we will have a shortfall  
19 in generating capacity and we will continue to  
20 export more of our potential investment capital  
21 out of the country, not just for foreign oil, not  
22 just for foreign gasoline, but for foreign natural  
23 gas.

24 We have the potential in our biomass  
25 reserves, our clean coal technology, and coal

1 reserves to become far, far more energy  
2 independent than we are. Right now we're  
3 sixty-five percent dependent. I think we can  
4 reduce that significantly. Whether we can get to  
5 a hundred percent is a function of how diligently  
6 and how purposefully we all work together over the  
7 next few years.

8 SENATOR STOUT: The reason I ask this  
9 question, are you familiar with the trail power  
10 project presented by Allegheny Power to the PUC?

11 MR. DESMOND: Trail power. I'm sorry. I  
12 don't recognize that.

13 SENATOR STOUT: Trail power is a subsidiary  
14 of Allegheny Energy that wants to build a five  
15 hundred thousand KV line in southwestern  
16 Pennsylvania from Washington County to Greene  
17 County, the districts that I represent, on down to  
18 the West Virginia line, through West Virginia and  
19 Maryland, to the markets on the east coast, in the  
20 Baltimore, DC area.

21 It's a project that will export a sizable  
22 amount of power out of Pennsylvania to that  
23 eastern shore market. Now, the market price for  
24 energy for the eastern shore is much higher than  
25 it is here in southwestern Pennsylvania. And

1 recently the federal government under an act of  
2 2005 -- always for years, the PUC-regulated  
3 utilities in this Commonwealth and their rights  
4 away and the needs and the prices.

5 Now, the federal government has given to the  
6 Department of Energy to create national energy  
7 corridors. It's not only the Washington, Greene  
8 Counties; but it affects fifty counties of our  
9 sixty-seven in this Commonwealth. And there's  
10 going to be other projects to move power from  
11 central Pennsylvania to New Jersey and the east  
12 and southeastern market.

13 So how can Pennsylvania afford to ship our  
14 massive amounts of these five hundred thousand KB  
15 lines to the eastern market? We've a need right  
16 here in the Commonwealth.

17 MR. DESMOND: We cannot; and we should not,  
18 Senator. We have provided testimony and gone down  
19 to Washington and testified before the Congress in  
20 opposition to this new federal imperative.

21 It not only will be routing even more of  
22 Pennsylvania's power out of state, and keep in  
23 mind that we export thirty-five percent of our  
24 electricity already to other states; but it will  
25 be a means whereby very dirty power plants to the

1 west of us can run at full tilt and export their  
2 electrons our way on way to lucrative markets in  
3 Maryland and DC and New York whilst, you know, we  
4 have the transmission lines and get the pollution  
5 and they get the customers.

6 So our position is, first of all, there are  
7 some places in Pennsylvania where we need some  
8 transmission upgrading simply because some of our  
9 instate power plants right now are a bit  
10 vulcanized. They don't have access to even good  
11 eastern Pennsylvania markets.

12 But we would like to see power line  
13 strategies that are controlled and guided by  
14 decisions made here in Pennsylvania, not at the  
15 federal level. And we would like to see as much  
16 as possible transmission upgrades that benefit  
17 Pennsylvania customers first.

18 If there are secondary benefits to the rest  
19 of the grid and the rest of the market, so be it.  
20 But we don't want to disadvantage our citizens  
21 simply to supply markets elsewhere.

22 SENATOR STOUT: I thank you for your  
23 testimony because last week I introduced a  
24 resolution, Senate Resolution 129, that's going to  
25 ask the federal government to reconsider their

1 decision of giving eminent domain rights from the  
2 federal government to utilities that operate in  
3 Pennsylvania. That's not right. We opposed that  
4 eminent domain here in the Commonwealth before, so  
5 it's not right to turn it over.

6 It seemed to be the very thing we talked  
7 about, all the conservation, not only the power  
8 going to higher markets in the east coast, those  
9 people in the east coast, they don't want to be  
10 inconvenienced by a power plant. We have to put  
11 up with power plants, particularly in southwestern  
12 Pennsylvania, coal-fired facilities; and those  
13 people in the east coast don't want those  
14 facilities.

15 Again, thank you for your testimony. Thank  
16 you, Mr. Chairman.

17 CHAIRMAN TOMLINSON: Thank you, Senator  
18 Stout. Senator Don White?

19 SENATOR DON WHITE: Thank you, Mr. Chairman.  
20 I appreciate your testimony today, Mr. Secretary.  
21 I'm just listening to some of the testimony, the  
22 word dirty power plants. We talked earlier about  
23 the fact that one of the problems this nation has,  
24 not only the state, is the fact we don't have  
25 enough refineries. Nobody wants them in their

1 backyard. I'm here as an advertisement to tell  
2 you the forty-first district, we'll be happy to  
3 take whatever you invest in it.

4 We have the coal bed methane development,  
5 natural gas, utilization of the bony piles for  
6 production. Also we have the ethanol plant you're  
7 talking about in Earlyville in the forty-first  
8 district.

9 There was an issue, I don't know if it came  
10 through your department here recently, in regards  
11 to the prospect of looking at a -- I don't  
12 remember the technical term. It was called a coal  
13 gasification project.

14 MR. DESMOND: That's right.

15 SENATOR DON WHITE: And as I recall, I think  
16 we were the only area that actually was deemed  
17 feasible for a project of this sort because of the  
18 underground storage capabilities with all our  
19 mining and everything else. So I just want to  
20 keep this in mind.

21 MR. DESMOND: Senator, let me be sure that I  
22 clarify our position. When I was talking about  
23 dirty power plants, I was talking about forty- to  
24 sixty-year-old plants with, you know, marginal  
25 emissions controls on them right now sending

1 pollution our way and electrons to other states.

2 What we are a clear and passionate advocate  
3 for is advanced clean coal gasification here in  
4 Pennsylvania, not just to make electricity but  
5 what we call poli-generation plants.

6 For example, the coal-to-liquids plant being  
7 proposed in Schuylkill County will generate not  
8 only liquid fuels from waste coal, but it will  
9 generate electricity as well. There's one being  
10 proposed in Fayette County that would make not  
11 only electric power but synthetic natural gas  
12 which could be sold directly to merchant  
13 off-takers or into the wholesale gas markets.

14 So there are things we could do in an  
15 environmentally responsible fashion with advanced  
16 coal gasification liquefaction and poli-generation  
17 right here in Pennsylvania, and DEP is fairly  
18 supportive of that idea.

19 SENATOR DON WHITE: And those power plants  
20 we're talking about have also made commitments and  
21 long-term investments on the new technology, the  
22 scrubbers for them. I believe Reliance has  
23 committed a six hundred million dollar investment  
24 on the one plant that's considered the largest  
25 polluter in Pennsylvania, the one located in

1 Armstrong County.

2 MR. DESMOND: And I just wanted to mention  
3 that the underlying -- there are two underlying  
4 rationales for wanting to see as an option for the  
5 free market long-term contracts. One is simply to  
6 give buyers and sellers all the choices free  
7 markets should afford them; but the other is if  
8 you're putting up billion dollar plants, the  
9 people who are financing these plants need to know  
10 how they're going to be paid off.

11 And one of the ways you know they can be paid  
12 off is if you have long-term contracts with credit  
13 worthy counter-parties. So that's a critical  
14 issue for us. It can do much to advance the clean  
15 coal economy here in the Commonwealth.

16 SENATOR DON WHITE: That county cooperation  
17 is really necessary, and I think that the --  
18 especially in a district where there will be  
19 twenty-five percent of our GNP as energy related.

20 Thank you, Mr. Secretary.

21 MR. DESMOND: Yes.

22 CHAIRMAN TOMLINSON: Deputy Secretary, just  
23 to follow up on that, I was going to ask this  
24 question anyway; but it dovetails right into what  
25 Senator Stout and Senator Don White were talking

1           about.

2           You talk about your systems energy charge in  
3           here to benefit the system. Yet you don't  
4           incentivize the old traditional power plants. You  
5           don't help them upgrade into new clean coal  
6           technology. Conservation is very important, and I  
7           agree with that. I'm going to ask you to explain  
8           that in detail, not at this time, but you can  
9           submit it to us.

10          Why have you not sought in any of the energy  
11          policies or in this testimony here for our old  
12          traditional -- I mean, I keep hearing that  
13          Pennsylvania is the Saudi Arabia of coal. I don't  
14          understand why we're not incentivizing the  
15          cleaning up of clean coal technology.

16          MR. DESMOND: Well, Senator, the existing  
17          legacy coal burning plants already, those that are  
18          going to stay in the market, already have  
19          investment underway in emissions control equipment  
20          to meet upcoming federal clean air requirements,  
21          so there's little more that can be done with an  
22          optimized existing legacy atmospheric power plant.

23          But the advanced closed vessel gasifiers  
24          where you can design in future carbon off-take  
25          ports into these technologies and infuse your

1 take-off CO-2, those technologies are where we  
2 need to go.

3 It would not be very cost effective to  
4 continue to invest in a forty- or fifty- or  
5 sixty-year-old legacy plant that was already  
6 scrubbed to full federal standards.

7 CHAIRMAN TOMLINSON: You're not saying we  
8 have -- we don't have any coal plants out there  
9 that are not in compliance, that are not being  
10 fixed now?

11 MR. DESMOND: Well, all of them will have to.  
12 Under the new federal cares regulation, they will  
13 all have to come into compliance. There are some  
14 legacy plants operating today which were  
15 grandfathered, if you will; but all of those that  
16 stay in the market will have to come into  
17 compliance.

18 CHAIRMAN TOMLINSON: In your testimony you  
19 submitted, I buy into the conservation, I buy into  
20 the investment. I like that. But, you know, when  
21 the wind's not blowing and the sun's not shining,  
22 you still, we still need to produce energy in the  
23 old traditional ways. And that's why I'm going to  
24 -- not at this time because we've gone over. I  
25 need to see how you've done the math. I need to

1 see how you've accounted for the ten billion  
2 dollars and how you computed that. I'm not asking  
3 you to do that now, but I'm asking you at some  
4 point to get to Senator White and myself so that  
5 we can get to the committee how you've really done  
6 the math of that.

7 Because to me, just common sense tells me  
8 there's going to be demand. I mean, we're going  
9 to incentivize conservation. We're going to try  
10 to get more efficient. But the wind doesn't blow  
11 some days, and the sun doesn't shine. Some of  
12 those things aren't going to produce the  
13 electricity that we need, and the meter is not  
14 going to spin backwards.

15 We're still going to need that old coal-fired  
16 plant that I understand are still not to the  
17 standards that we would have them be or  
18 encouraging Pennsylvania -- I'm from the  
19 southeast. This speaks to Senator Don White's  
20 issue. If Pennsylvania is sitting on top of all  
21 this coal, I don't understand why we're not doing  
22 more to develop the economies of that and the  
23 efficiencies of that and the clean air of that.

24 And I don't see anything in your proposal. I  
25 was just wondering why. And maybe this isn't the

1 time for you to answer because we've gone fifteen  
2 minutes beyond your testimony. But please get  
3 back to us, particularly as it relates to how did  
4 you calculate the ten billion dollars, you know,  
5 how many years, how many refrigerators did you  
6 think people would buy, or how many window air  
7 conditions and how did you come to those  
8 assumptions. You had to do that, I would think,  
9 in a scientific way.

10 MR. DESMOND: Yes. Those are important  
11 questions. We do have the data, and we'd be very  
12 pleased to meet with you and Senator White and go  
13 over the basis for our calculations.

14 CHAIRMAN TOMLINSON: Senator LaValle left.  
15 Senator Boscola?

16 SENATOR BOSCOLA: Thank you. Mr. Desmond, I  
17 just have one question. I want to know how the  
18 systems benefits fee is going to be affected when the  
19 rate caps expire in 2011, 2012, because it's now,  
20 say, about a six dollar fee and I guess it's based  
21 on a per kilowatt charge.

22 As the rate caps expire, and I've read  
23 articles where PPL, for instance, says, you know,  
24 a conservative number is thirty percent increase.  
25 How is that service benefit fee going to be

1 affected? Is it not going to be six dollars  
2 anymore? Is it going to sixty dollars in twenty  
3 years?

4 MR. DESMOND: No. It would simply be the  
5 proportion on the bill. One twentieth percent per  
6 kilowatt hour. That would be fixed. If somebody  
7 uses more electricity, that would be a different  
8 story. But if their power use is fixed, it would  
9 still be the same price per kilowatt hour.

10 SENATOR BOSCOLA: Just so Wendell knows,  
11 Wendell Holland, that's a question I'm going to  
12 ask you, so prepare for it. That's what I'm  
13 really concerned about.

14 Five dollars, six dollars might not be a  
15 concern to a lot of people. But when their  
16 electric bill is going up by thirty and forty  
17 percent when the rate cap expires, tacked onto  
18 another six dollars, I mean, we are pickpocketing  
19 people, you know, because they're paying more for  
20 gas, they're paying more for food, they're paying  
21 more for housing. And it's going up in  
22 everything, and their wages aren't. That's really  
23 what my concern is.

24 MR. DESMOND: Well, Senator, one of the  
25 things you should know, at present and until the

1 rate caps lift, we have on all of our electric  
2 bills something called a transition fee which was  
3 the fee paid as part of the deregulation  
4 settlement to cover the cost of stranded  
5 investments.

6 That fee right now amounts to, I recall,  
7 approximately 1.1 billion dollars per year that  
8 rate payers are paying. That fee will be lifted  
9 when the rate caps go away. So if our incremental  
10 cost to invest in the systems benefit charge is  
11 seventy million on the bill and a billion-one off,  
12 the rate payers still are going to see lower  
13 costs.

14 SENATOR BOSCOLA: I understand. But they've  
15 been hearing that for a long time now. Thank you.

16 CHAIRMAN TOMLINSON: Thank you. The last  
17 question I'd like to leave is you provide for  
18 additional weatherization, expansive  
19 weatherization. Not for here, but I'd like to  
20 know where you think that expansion will go.  
21 We're way past our time now.

22 MR. DESMOND: Senator, can I get back with  
23 you on that? I don't have detail with me.

24 CHAIRMAN TOMLINSON: Sure. That's why I'm  
25 asking. Get back to Senator White and myself on

1 the expansion of weatherization, where you think  
2 that money is going to go, and where we are in  
3 weatherization, what additional benefits that will  
4 get us.

5 MR. DESMOND: Be happy to, Senator.

6 CHAIRMAN TOMLINSON: Thank you very much.

7 CHAIRWOMAN WHITE: Just one additional  
8 observation. You know, we capped the systems  
9 benefit charge for industrial users. Perhaps we  
10 should consider a cap for residential users as  
11 well, as Senator Boscola suggested.

12 CHAIRMAN TOMLINSON: Thank you. Thank you  
13 very much, Mr. Desmond.

14 MR. DESMOND: Thank you very much.

15 CHAIRMAN TOMLINSON: Mr. Desmond, you're  
16 dismissed at this time. At this time I'd like to  
17 have the Public Utility Commission with Chairman  
18 Wendell Holland, Vice Chairman James Cawley, Kim  
19 Pizzingrilli, and Terrance Fitzpatrick move to  
20 center stage.

21 Mr. Chairman, as soon as you get that laptop  
22 lit up, you may begin your testimony. I hope it's  
23 an energy saving device.

24 MR. HOLLAND: Less trees, Mr. Chairman.

25 Thank you, Chairman Thompson and Chair White and

1 Chair Boscola as well as all members of the  
2 committee, for giving us, my colleagues, Jim  
3 Cawley, Commissioner Pizzingrilli, and Terry  
4 Fitzpatrick an opportunity to share our thoughts  
5 on energy policy in Pennsylvania. As I  
6 understand, all four of us will be given about  
7 five minutes to present, after which there will be  
8 a Q and A period.

9 This year we celebrate seventy years in the  
10 energy business. We continue working every day on  
11 this, and we thank you for the opportunity to  
12 discuss these issues.

13 I applaud the governor and the legislature  
14 for being involved in energy issues. We think  
15 that they are absolutely critical. And it's my  
16 pleasure to be here in person, as I regard the  
17 energy business one of Pennsylvania's primary  
18 concerns.

19 The eyes of the nation are on Pennsylvania as  
20 we work toward a comprehensive energy policy. We  
21 look forward to the opportunity to assist in this  
22 effort as we've been engaged in complex energy  
23 matters throughout our seventy year existence.

24 We have the Alternative Energy Portfolio  
25 Standards Act. A recent audit by the LBFC found

1 the commission is doing a good job in implementing  
2 the act. We also have the acts which restructured  
3 both the electric and natural gas industries,  
4 including the commission's obligation to serve the  
5 provision of default service. Each of these must  
6 be administered within the context of the  
7 overarching mandates of the Public Utility Code  
8 which requires safe, reliable, and adequate  
9 utility service throughout the state.

10 Given these various initiatives that impact  
11 energy markets, policies, and rates, the  
12 Commonwealth needs a comprehensive energy policy  
13 that will provide additional direction for state  
14 agencies tasked with ensuring Pennsylvanians have  
15 safe yet affordable energy available for years to  
16 come. That's exactly the right time to engage in  
17 a wide range of energy discussion in the state and  
18 to move forward with this legislation.

19 The PUC has been working with legislators and  
20 advocates in the media to ensure that customers  
21 know about what's going on around them in both the  
22 electric and natural gas markets, how it impacts  
23 them, and what they can do about.

24 Many of the things that this commission has  
25 been working on is consistent with the goals of

1           this proposed legislation. When you pass  
2           legislation that complements our work, we take a  
3           significant step together in establishing sound  
4           energy policy that inures to the benefit of all  
5           Pennsylvanians.

6                     Just last month we unanimously approved  
7           policies to help mitigate any possible price  
8           spikes that could result from the expiration of  
9           long-term rate caps that were put in place as part  
10          of the restructuring of the electric utility  
11          industry. That culminated a year's worth of work  
12          where the commission engaged all stakeholders in  
13          the process of developing sound policy.

14                    In engaging in a collaborative process, we  
15          have demonstrated that complex energy issues can  
16          be resolved effectively in contrast to the  
17          difficulties that occurred in the last eighteen  
18          months in the state of Maryland and are presently  
19          happening right now in the state of Illinois.

20                    I am so glad to note that we have been  
21          recognized as the most consumer friendly state  
22          commission in the Mid-Atlantic region.

23                    As part of the overall strategy for  
24          addressing generation rates, the commission  
25          developed the final default service regulations

1           and a policy statement. The default service  
2           regulations are the most important rulemaking  
3           before the commission since the restructuring of  
4           the industry.

5           In developing these, the commission attempted  
6           to craft rules that represented a balanced  
7           approach to acquiring reasonably priced supply in  
8           a manner that carefully balanced the interest of  
9           all stakeholders while meeting the requirements of  
10          the 1996 competition law.

11          Similar to a proposal in the legislation, our  
12          default service policy statement required the  
13          electric utilities to offer customers the choice  
14          of opting into a prepay or a deferral option if  
15          the total bill increase exceeds twenty-five  
16          percent at the expiration of the rate caps. The  
17          policy statement also addresses other retail  
18          market issues, interim price adjustments, and cost  
19          reconciliation.

20          It's important to note that one thing that  
21          the rulemaking did not expressly mandate nor  
22          prohibit is long-term contracts. This seems to be  
23          an issue that's generating significant confusion  
24          and is one that we've taken a keen interest in  
25          because of its effects on development. I believe

1 my colleagues will add further thoughts on this  
2 subject.

3 Because the wholesale electricity markets did  
4 not reached maturity, the markets of today may not  
5 be the markets that we see tomorrow. This is a  
6 lesson that we all learned over the last ten  
7 years. In passing legislation, it's my hope that  
8 you would paint with a very broad brush when it  
9 comes to such issues as to how electricity supply  
10 is obtained.

11 Demand side response is yet another issue  
12 that the proposed legislation complements our  
13 agency's efforts. Study after study in the  
14 electric utility industry has shown that providing  
15 customers with the tools they need to help shave  
16 the peak effectively reduces demand while  
17 increasing reliability of the grid and in the end  
18 should help to moderate the cost of electricity.

19 As proposed in the legislation, one way to  
20 reduce demand is through the use of smart meters.  
21 The technology that empowers consumers to control  
22 their energy usage is available.

23 It's important to note that the smartest part  
24 of the meter is the customer. Let me reiterate  
25 that. The smartest part of the meter is the

1 customer.

2 But in Pennsylvania, we have few residential  
3 customers that currently have access to it. In  
4 the coming weeks, we'll act on staff  
5 recommendations based upon the work of the  
6 commission's DSR working group which again engaged  
7 the stakeholders in the process.

8 The proposed legislation also included a  
9 systems benefit charge. Recently that charge was  
10 for consideration before the commission. At that  
11 time, the majority of the commission didn't  
12 believe that the commission had statutory  
13 authority to act or to enact such a charge. The  
14 proposed legislation would give the commission  
15 that authority. I encourage you to adopt the  
16 systems benefit charge.

17 In other states, it's been used as a  
18 relatively inexpensive means to further a diverse  
19 generation source which will have a potential  
20 downward impact on rates.

21 The proposed legislation is expansive and  
22 includes many new innovative ideas. While these  
23 are fine details that may need to be worked out,  
24 they should not delay prompt action on the  
25 legislation. Their resolution is well within the

1 ability of the general assembly of the agencies  
2 involved in the process.

3 Finally, I'll note, though not part of this  
4 generation, this legislation, if I were to respond  
5 to a question with respect to what are the big  
6 picture energy issues, perhaps not that need to be  
7 acted on immediately but something you might want  
8 to consider later in the year, those issues would  
9 include distribution surcharges for energy  
10 companies; the next era of coal generation;  
11 nuclear waste disposal, not nuclear waste  
12 construction, but nuclear waste disposal; and  
13 transmission sitings.

14 With that, I'll defer now to my colleague,  
15 Vice Chairman James Cawley.

16 MR. CAWLEY: Senator Tomlinson, Senator  
17 White, Senator Boscola, Senator Musto, and members  
18 of the committee, thank you for this opportunity  
19 to talk about energy policy with you and  
20 thankfully through PCN with our fellow  
21 Pennsylvanians.

22 My testimony, Senators, is on electricity,  
23 not that an energy policy doesn't include a lot of  
24 other things; but I think it seems to be mostly  
25 uppermost on people's minds right now.

1           In the few minutes given to each of us, I  
2           would like to give a brief overview of what I  
3           regard as vital for Pennsylvania energy policy and  
4           to relate why in my opinion retreat if not out of  
5           the question at least will be fraught with great  
6           difficulties.

7           In brief, we must make every effort to  
8           empower customers, electric customers, to make  
9           vital energy choices about how much energy they're  
10          going to use and how much they are willing to pay  
11          for it; and we must encourage market entry by  
12          competitors who have fled the market when  
13          wholesale prices got above the rate caps that were  
14          set in 1996. We've got to get those competitors  
15          to come back and give the choices customers were  
16          promised in the 1996 Electric Competition Act.

17          Now, because my colleagues have already and  
18          will talk about what we have been doing, I'm going  
19          to only briefly mention what we have done to  
20          promulgate regulations and policies in two areas.

21          First, on the demand side, this is the  
22          customer side, we have recently after long  
23          deliberation and much effort by a lot of parties  
24          promulgated default service regulations. These  
25          are the regulations for our electric utilities and

1           how they go about acquiring energy for those who  
2           do not chose an alternative energy supplier.

3           On that demand side, we have done much to  
4           empower customers to take control of their energy  
5           costs. And as my colleagues will relate, we've  
6           talked about things like demand side management.  
7           Well, what is that? Demand side management  
8           focuses on efforts to reduce energy when the costs  
9           are highest. On a hot August day, in July, for  
10          instance, whether to use electricity then and what  
11          you can do to reduce usage at that time.

12          Energy efficiently. Energy efficiency refers  
13          to using less energy for the same use. For  
14          instance, more efficient light bulbs. And  
15          finally, conservation, which is simply modifying  
16          your behavior and doing without.

17          Our orders have also dealt with the supply  
18          side of how electric utilities are going to go  
19          about acquiring supply. And we have mandated a  
20          procurement process where energy is acquired over  
21          a period of time and ahead of time using auctions  
22          and competitive priced electricity.

23          We have also dealt with removing the barriers  
24          so the competitors will come back when it is  
25          economic for them to come back and offer products

1 to Pennsylvanians.

2 They won't come back, by the way, until they  
3 can make money. They can't make money by buying  
4 high and selling low and trying to make it up on  
5 volume. You can't make money buying high and  
6 selling low. You lose on every transaction.  
7 That's why they have fled the market.

8 When the rate caps come off, prices are going  
9 to go up. There is no question about that, and we  
10 have been making great effort to try to mitigate  
11 that transition period.

12 But you simply cannot cap generation rates  
13 for a period of ten to fifteen years and expect  
14 the prices are not going to go up somewhat,  
15 particularly when everything else has gone up and  
16 particularly when the cost of generating  
17 electricity has gone up during that time.

18 So we've adopted orders that will try to  
19 mitigate that transition, and we have ordered  
20 utilities to come up with a plan by the end of the  
21 year how they're going to educate their customers  
22 about what they can do to help mitigate that  
23 transition.

24 And finally, our orders made it clear that we  
25 are going to continue to be active before the

1 Federal Energy Regulatory Commission and PJM  
2 Interconnection which is based in Valley Forge and  
3 is an economic dispatch center where most economic  
4 generation is dispatched as it is needed.

5 Now, let me make the point that I really want  
6 to make this morning. And that is that retreat is  
7 not an option. We have got to make electric  
8 competition work in Pennsylvania because the  
9 bridges have been burned behind us by the federal  
10 government.

11 What do I mean by that? Well, before 1992,  
12 we had in Pennsylvania and across the United  
13 States vertically integrated, meaning vertically  
14 integrated utilities. They generated the power.  
15 They distributed it. They transmitted the power.  
16 They distributed the power. It was a vertically  
17 integrated model.

18 In 1992, Congress passed the Federal Power  
19 Act which required a number of changes. After  
20 that date, most if not all the utility-owned  
21 generation was converted or sold as so-called  
22 exempt wholesale generation. In other words,  
23 generation assets were now within the jurisdiction  
24 of the Federal Energy Regulatory Commission and  
25 not within the Pennsylvania Public Utility

1 Commission or any other state commission.

2 So now we have PJM which controls and  
3 dispatches power economically within Pennsylvania.  
4 We have the Midwest Independent Service Operator  
5 which does the same thing for Penn Power in the  
6 western part of the state. And for tiny little  
7 Pike County Light and Power Company in Pike  
8 County, they're within the New York Independent  
9 System Operator.

10 Electric public utilities became electric  
11 distribution companies which owned distribution  
12 facilities in their rate base and upon which they  
13 earned a return; but they are not permitted to  
14 have generation assets, power plants in their rate  
15 base any longer. They're under FERC jurisdiction.

16 Interstate transmission facilities were  
17 declared under FERC jurisdiction; and under FERC's  
18 Oder 888, they were made open access for others to  
19 convey power on.

20 So we no longer have traditional electric  
21 public utilities in Pennsylvania. So let's say we  
22 want to return to the so-called good old days.  
23 Can we do it? Well, what are the obstacles? The  
24 first is that generation is no longer in  
25 Pennsylvania utility rate bases. They do not have

1 all their power plants in the rate base anymore  
2 upon which to earn a return. Those are FERC  
3 jurisdictional. They are exempt wholesale  
4 generators, not subject to state regulation. In  
5 some cases they are owned by entities that do not  
6 directly serve any retail customers in  
7 Pennsylvania.

8 On the other side of the coin, some low cost  
9 generation that Pennsylvania uses is located  
10 outside of Pennsylvania. We have no control over  
11 any of that generation.

12 Now, what we could do is mandate our existing  
13 electric companies build new capacity and serve  
14 our Pennsylvanians from these new plants; and they  
15 could put the new plants in the rate base.

16 Of course, they'd have to be built at today's  
17 prices and subject to today's siting and  
18 environmental and land use laws. As you've  
19 already heard Deputy Secretary Desmond say, that  
20 would take a number of years and cost a lot of  
21 money.

22 We could provide incentives or mandates even  
23 requiring our electric utilities to furnish  
24 default service with our own generation, even  
25 though they have now been placed in unregulated

1 subsidiaries and are under FERC jurisdiction.

2 Again, this power would have to be priced at  
3 what that power is worth today. Why would they  
4 sell it to Pennsylvania at a low price when they  
5 can sell it elsewhere outside of Pennsylvania at a  
6 much higher price? And again, we would have  
7 nothing to say about that.

8 We could require our electric utilities to  
9 reacquire the generation they have sold, but they  
10 couldn't do that unless the existing owners wish  
11 to sell. And, of course, they would have to pay  
12 today's prices to get those plants back.

13 I could go on and on, but I think you get the  
14 picture. We no longer have jurisdiction because  
15 of Congress over generation. And even though we  
16 could force our utilities to build in  
17 Pennsylvania, it would cost a lot of money and  
18 take a lot of time to do it.

19 Therefore I believe there's really no way to  
20 unscramble this egg, at least not without working  
21 very closely with Congress. And even then, I  
22 think it would result in major increases in retail  
23 prices, lengthy litigation over what the value of  
24 plants would be and how much they would be  
25 charged, and I believe economic disruption in

1 Pennsylvania that we can ill afford.

2 For good or ill, we have to make electric  
3 competition work in Pennsylvania. And to the  
4 extent possible, we have to use our resources to  
5 fix the foibles and flaws of the present system.  
6 There is really no going back.

7 And therefore, when you hear us talk about  
8 demand side management and energy efficiency and  
9 conservation and competitive procurement of power,  
10 all of these things are not Pollyanna. These are  
11 not things that we really ought to do but need not  
12 do. We need to do these things, and that's why we  
13 have spent so much time and talked to so many  
14 diverse parties about how best to go about it.

15 With that, I will await your questions.

16 MR. HOLLAND: Commissioner Pizzingrilli?

17 MS. PIZZINGRILLI: Thank you. Good morning,  
18 Chairman Tomlinson, Chair White, Chair Boscola,  
19 and Chairman Musto, members of the committee.  
20 Thank you for the opportunity to be here today.

21 I would like to commend the committee for  
22 holding this joint hearing. By working together,  
23 you set the stage for the type of open process  
24 that is essential in considering so many diverse  
25 interests as you contemplate a comprehensive

1 policy for Pennsylvania.

2 It is critically important that we continue  
3 to establish programs and policies to reduce  
4 consumer energy costs and to expand the  
5 availability and use of alternative energy. The  
6 ultimate challenge, though, is to establish such a  
7 strategy that accomplishes that by considering  
8 interests of all stakeholders.

9 I will not read my prepared testimony that I  
10 submitted to the committee, and I will try to  
11 avoid repeating what you have heard or will hear  
12 from my colleagues.

13 I'd also like to applaud the administration  
14 for putting forth the initiatives. Many are  
15 policy decisions that are best made by the general  
16 assembly.

17 As you've heard from the chairman and the  
18 vice chairman, the commission continues to move  
19 energy policy forward pursuant to our existing  
20 statutory and regulatory authority. Attached to  
21 my written testimony is a summary of the  
22 commission's proceeding with respect to our  
23 default service regulation and alternative energy  
24 regulations and policies.

25 We need to continue to evaluate and establish

1 policies that empower our consumers to conserve  
2 energy, to provide them with the tools to better  
3 manage their energy use and costs, and to attract  
4 and enhance the availability of alternative energy  
5 sources.

6 However, the impact of any energy policy has  
7 different costs and benefits associated with  
8 various classes of customers, residential, small  
9 business, and large commercial and industrial.

10 The needs of consumers and utilities also  
11 vary among our service territories. That's why  
12 it's so important that you have convened these  
13 hearings to listen to all affected parties, all  
14 affected by the comprehensive energy strategy.

15 The regulation of utility service is impacted  
16 by several facets of federal, state, and local  
17 government, all with varying statutory and  
18 regulatory responsibilities. As you evaluate  
19 energy policies, it's important to be aware that  
20 the commission does continue to actively  
21 participate in federal and regional proceedings  
22 that impact electricity to ensure Pennsylvania's  
23 interests are considered.

24 As you heard earlier, we are actively  
25 represented in proceedings before the FERC. We

1           also work closely with PJM Interconnection, and we  
2           also serve on the organization of PJM's state's  
3           board as well as the organization of Mid-West  
4           states' board.

5                     As the demand for electricity increases, we  
6           continue to explore options for demand response  
7           initiatives. In doing so, we actively participate  
8           in the Mid-Atlantic distributed resource  
9           initiative, which includes five Mid-Atlantic  
10          jurisdictions.

11                    A recent study completed by the MADRI  
12          concluded that a modest reduction in electricity  
13          usage during peak hours would reduce energy prices  
14          by at least fifty-seven million to a hundred and  
15          eighty-two million annually in the Mid-Atlantic  
16          region. This study and the MADRI's efforts will  
17          be invaluable for states such as Pennsylvania as  
18          we continue to successfully implement alternative  
19          energy laws and to empower consumers with  
20          innovative energy efficiencies, demand response,  
21          and advance metering programs.

22                    Also consistent with this regional focus, we  
23          participate in a similar initiative, the midwest  
24          demand side response initiative. Participation at  
25          the regional level on demand response initiatives

1 goes hand in hand with the commission's  
2 investigation of issues relating to demand  
3 response, conservation, and advanced metering.

4 The investigation that we initiated in the  
5 fall of 2006 was in response to significant  
6 increases in fuel prices and the associated impact  
7 on utility costs. We should soon be in the  
8 position to share the findings of our demand side  
9 working group which will include utilities'  
10 current efforts to assist the customers to reduce  
11 usage and increase energy efficiency; the nature  
12 and cost of such programs; whether advanced  
13 metering infrastructure should be developed by  
14 utilities, and if so, what is the time line and  
15 standards that should be established for  
16 implementation of these systems and for the  
17 various classes of customers; and also what  
18 mechanisms are necessary or appropriate to ensure  
19 that utilities aggressively encourage and  
20 implement conservation and energy efficiency in  
21 the service territories. These findings may serve  
22 as a valuable resource to your committee as you  
23 look forward to the energy policy.

24 Last month, as you heard, the commission took  
25 action on an overall strategy to prepare consumers

1           for potential increases in generation costs. We  
2           finalized the plan to mitigate and prepare  
3           Pennsylvania electric customers for potential  
4           increases. While I won't go into the details of  
5           that program, the centerpiece of it is a potential  
6           five million dollar consumer education campaign to  
7           help our consumers for potential increases.

8                     Our staff has invited stakeholders to a  
9           meeting to be held this June to help craft a  
10          campaign which will include messages and education  
11          about energy efficiency, conservation, and demand  
12          side response in low income programs.

13                    As was also mentioned this morning, our  
14          companies will also implement consumer education  
15          plans for their service territories.

16                    We also have approved the final regulations  
17          and the policies that affect default service. The  
18          default service regulations are one of the most  
19          important rulemakings of the commission, and they  
20          are now before the Senate and House standing  
21          committee. And the IRRC is scheduled to consider  
22          that rulemaking package on July 19th, 2007.

23                    The commission looks forward to working with  
24          the committees as you continue to evaluate the  
25          governor's energy initiatives. Our staff

1 continues to analyze the legislation and  
2 amendments as they come forward.

3 There are many agencies of state government  
4 as you know that have an interest in developing  
5 the energy strategy going forward. As you heard  
6 this morning, the DEP advises the administration  
7 on new legislation regarding biofuels, renewable  
8 energy, energy efficiency, and also shares some  
9 responsibility with the implementation of the AEPS  
10 Act.

11 The Department of Community and Economic  
12 Development is involved in energy policies as the  
13 impasse of energy costs on businesses and the  
14 growth of new alternative energy infrastructure  
15 are among a multitude of issues relating to  
16 economic development in Pennsylvania.

17 The PUC has a broad range of statutory  
18 responsibilities, primarily to ensure the state  
19 reliable and reasonably priced utility service.  
20 Any legislative changes should preserve that  
21 important role for the commission.

22 Going forward, these agencies need to play an  
23 active role cooperatively in providing input to  
24 the general assembly. I also believe that it is  
25 important that any legislation should provide

1 regulatory certainty but at the same time  
2 regulatory flexibility, invest in consumer  
3 education, empower our consumers through new  
4 technology, and at the same time it must balance  
5 the interest of utilities and consumers.

6 I believe it's important for all parties to  
7 work cooperatively to address the energy issues in  
8 Pennsylvania to ensure that the costs and benefits  
9 are fully analyzed prior to the passage of the  
10 legislation.

11 I agree with the question raised this morning  
12 by Chairman Tomlinson, although the systems  
13 benefit charge appears to be a nominal charge on  
14 consumers, I believe the benefits should be fully  
15 realized and look forward to receiving that  
16 analysis.

17 We appreciate the opportunity to testify  
18 today and look forward to working with you.

19 MR. FITZPATRICK: Chairmen, Chairwomen,  
20 members of the committee, I'm Terry Fitzpatrick, a  
21 member of the commission. Thank you very much for  
22 the chance to be here to talk to you about the  
23 important issue of energy policy.

24 I, and I guess we, speaking for my  
25 colleagues, recognize the challenges that are

1           posed by the expiration of the generation rate  
2           caps which is coming at the beginning of 2011.

3           Escalating prices are not unique, of course,  
4           to electricity. Energy prices generally are  
5           rising. I give some specific numbers in my  
6           testimony and would ask you to look at those.

7           Let me tell you. I had a classic  
8           over-the-backyard-fence conversation with a  
9           neighbor a couple weeks ago. He read the  
10          newspaper story that said that PPL's prices could  
11          be going up by thirty percent in a few years. He  
12          said, Is that true, Is that really going to  
13          happen. And I said, Well, the rates are going to  
14          go up, Nobody really knows how much, We'll see  
15          what the market prices are. And he kind of shook  
16          his head like something was wrong with that, and I  
17          understood that reaction.

18          And I said, But think about what the impact  
19          would be if gasoline prices had been capped for  
20          the last ten years and then all of a sudden you  
21          woke up and saw ten years' worth of changes in  
22          that market and it hit you all at one time,  
23          Wouldn't that kind of shock you too. And he  
24          acknowledged that it would.

25          That's what we're facing. I mean, with these

1 caps in place for so long, with the changes that  
2 have taken place nationally and internationally in  
3 energy, it's a real challenge.

4 Contributing factors to all of this, the  
5 increase in fuel prices, natural gas, and coal  
6 used to generate electricity; increasing  
7 congestion on our transmission network. Since  
8 1990, demand for electricity, of course, is up.  
9 But transmission investment is down on the order  
10 of twenty percent. That congestion problem shows  
11 up in higher charges on your bill, although I do  
12 think there is some increase in investment  
13 transmission now.

14 Environmental policy is something else which  
15 is linked to electricity prices and are one of the  
16 factors that's driving prices up. And I expect  
17 that that's going to be true in the future because  
18 with more stringent mercury regulations, with all  
19 of the talk about global warming and about  
20 limiting carbon emissions, those things if they're  
21 done are going to put upward pressure on energy  
22 prices.

23 That's not to say necessarily that those  
24 policies can't be justified by their environmental  
25 benefits. But I think policy makers have to keep

1 in mind that there is that trade-off. They are  
2 going to put upward pressure on prices.

3 The commission, as my colleagues said, is  
4 responding in what I believe is a rational,  
5 logical manner to these challenges. We issued an  
6 order in our price mitigation proceeding. The  
7 main policies that we're pursuing there are, as  
8 you heard, customer education. We're also going  
9 to be, as part of that education process, we're  
10 going to be encouraging customers to conserve  
11 energy.

12 Dan Desmond talked about some of the things  
13 that they've encouraged people to do as habits  
14 that have saved some money here in the capitol.  
15 We're going to take a lot of those same things to  
16 the customers to encourage them to conserve.

17 Another thing we're going to do is we're  
18 going to have to look at our low income assistance  
19 programs. All of the utilities have customer  
20 assistance programs designed to help those with  
21 lower income. And of course, there's probably  
22 going to be more -- it's going to be necessary to  
23 make more assistance available as each price is  
24 increased. That's just one of the realities.

25 Another thing we're going to do is giving

1 customers the option of a phase-in plan in order  
2 to mitigate the initial impact of this on their  
3 bills. And as my colleagues also said, we have  
4 our default service rules.

5 Let me turn now to the question of what you  
6 might be considering doing beyond what the  
7 commission is doing on electricity prices. First  
8 of all, I want to commend the governor and his  
9 administration for putting a proposal on the table  
10 here. Some of the ideas in the energy plan of the  
11 governor are similar policies that the commission  
12 is also pursuing in the proceedings that I've been  
13 talking about here.

14 Let me just try to make a couple general  
15 points and give you a couple of opinions about  
16 some other things in the plan. First of all, as a  
17 general matter, as I think you know, this is a  
18 very complex area. And I believe that great care  
19 ought to be exercised in crafting the legislation.

20 I believe perhaps a unique experience of  
21 having been involved when I worked here in this  
22 body in drafting the electricity competition law  
23 and then later in my career being responsible as  
24 one of the members of the commission for  
25 implementing that law. And I can't tell you how

1           many times I sat and thought, Why did we draft  
2           this that way, This would have been better if we  
3           had done this another way.

4                     Now, I think it's inevitable in complex  
5           legislation that you're going to have some of  
6           that; but the more care that's exercised up front  
7           in drafting, I think you minimize that. And I  
8           think that would be a good thing, so I would  
9           encourage a deliberate approach with full input  
10          from all of the parties who are going to be  
11          impacted on something like this.

12                    Second, I'm concerned over the approach in  
13          some of the legislation to implement the  
14          governor's plan with the degree of minute detail  
15          contained there on how the commission should  
16          define the duties of electric utilities in  
17          providing default generation service.

18                    This lack of flexibility is risky because it  
19          assumes that future events can be predicted with  
20          certainty. The approach is contrary to the  
21          tradition of giving the commission some  
22          flexibility and latitude to make adjustments as  
23          circumstances change. Now, I believe that overall  
24          that's a tradition that has worked well in the  
25          past.

1           Third, I want to talk about long-term  
2           contracts which I know is a big issue. I think  
3           you should consider the issue of long-term  
4           contracts. I would be doing that, frankly, if I  
5           were in your position.

6           Proponents of the governor's energy plan  
7           claim that the plan will allow customers, large  
8           customers, to enter into, quote, stable and  
9           cheaper long-term contracts with electricity  
10          suppliers.

11          I think this is in response to decisions of  
12          the commission that have restricted the ability of  
13          the electric utility in its role as the provider  
14          of last resort from entering into such contracts  
15          with customers. These decisions were based upon  
16          several factors, including the recognition of the  
17          need to link at least some retail prices to  
18          wholesale prices in order to develop more demand  
19          response in wholesale markets.

20          In addition, consistent with the policy that  
21          the supply service offered by the utility should  
22          be a back-up service, a service of, quote, last  
23          resort, close quote, in terms of the competition  
24          law, the commission reasoned that large customers  
25          would always be free to enter into contracts of

1 different lengths, including long-term contracts,  
2 with competitive suppliers in the market.

3 These decisions that we've made have been  
4 supported by, among others, the market monitoring  
5 unit at PJM as the kind of things that need to be  
6 done to improve the competitiveness of the  
7 wholesale market, thereby lowering prices across  
8 the board to everyone. In addition, these  
9 decisions have contributed to the development of a  
10 robust market with several competitive suppliers  
11 in the Duquesne and now Penn Power service areas.  
12 But at the same time, I certainly understand that  
13 the general assembly doesn't take the concerns of  
14 large customers lightly. I know some of them have  
15 been complaining about this.

16 In considering this issue, I would ask you  
17 keep in mind that electric utilities no longer own  
18 generating plants. Therefore, they have to go  
19 into the market, the wholesale market, to buy  
20 power that they sell to retail customers.  
21 Accordingly, it is not clear to me why it should  
22 be assumed that utilities are going to be able to  
23 secure this power more cheaply than competitive  
24 suppliers were going to. Utilities are big, and  
25 they're credit worthy; but so are a lot of the

1 suppliers, competitive suppliers out there, who  
2 are affiliates of utilities operating in other  
3 regions.

4 In addition, I am concerned that allowing  
5 utilities to offer such contracts is going to be  
6 interpreted as a lack of faith in the ability of  
7 competitive retail markets to provide benefits to  
8 customers.

9 But if the general assembly does decide to  
10 move forward and allow utilities to offer these  
11 contracts to customers, I think careful  
12 consideration should be given to the language that  
13 amends the competition law.

14 The legislation that has been introduced to  
15 enact the governor's plan contains language that  
16 appears to me to be inconsistent. On the one  
17 hand, it states utilities may offer rates of any  
18 duration to customers, which I believe is what is  
19 being relied on to allow these contracts. But on  
20 the other hand, the proposed legislation  
21 specifically restricts the ability of utilities to  
22 enter into long-term wholesale contracts.

23 Without such long-term wholesale contracts,  
24 it's unclear to me how the utilities are going to  
25 be able to offer long-term retail contracts

1 without putting their financial health at risk.

2 And finally, the governor's plan calls for  
3 the initiation of a systems benefit charge. I  
4 think it's important to remember this charge is  
5 going to continue for thirty years to fulfill the  
6 obligation of a bond. Those proceeds will then be  
7 used by the Pennsylvania Energy Development  
8 Authority and some other agencies for a variety of  
9 things, including providing additional subsidies  
10 to alternative energy projects and to allow these  
11 agencies to engage in buying and selling energy  
12 commodities such as electrical and natural gas.

13 I question whether this proposal for a  
14 systems benefit charge is good public policy.  
15 While proponents seek to minimize the amount of  
16 this charge by saying that it's only \$5.40 per  
17 year, I prefer to look at the total amount that's  
18 going to be raised here, eight hundred and fifty  
19 million dollars. That is a substantial sum of  
20 money, I think, by any measure. And I think it  
21 raises the question, how do the proposed uses of  
22 this eight hundred and fifty million dollars fit  
23 into the spending priorities of state government.

24 In my view, it should not be a high priority  
25 to provide additional subsidies to alternative

1 energy projects. The developers of these projects  
2 already receive federal tax incentives, and they  
3 benefit from the mandate contained in the  
4 Alternative Energy Portfolio Standards Act that  
5 electricity suppliers must purchase increasing  
6 percentages of alternative energy products.

7 In considering spending priorities, I would  
8 ask that you keep in mind that there are serious  
9 issues in Pennsylvania and the United States  
10 generally regarding the condition of our  
11 transportation and utility infrastructures.

12 The American Society of Civil Engineers has  
13 issued a report card in infrastructure and has  
14 given Pennsylvania a grade of D. That's the same  
15 grade that was given to the United States  
16 generally.

17 This is an issue that I've become  
18 particularly interested in because I see it so  
19 much in my role in the PUC. I've written a paper  
20 on the challenges that we're facing on  
21 infrastructure. I'd be happy to submit that for  
22 anyone who's interested.

23 But to give just a couple of examples, first  
24 of all, I think everybody here knows about the  
25 transportation infrastructure issue. Ultimately I

1 think there's going to be pressure for people in  
2 Pennsylvania to put up more money in take care of  
3 that problem. I know Senator Stout is on the  
4 transportation committee, and he as well as the  
5 others are very familiar with that.

6 Another example of infrastructure needs, we  
7 still have combined sewage overflow systems in the  
8 state, which when it rains really hard dumps  
9 untreated sewage into the waters of the  
10 Commonwealth.

11 I'm trying to make a point that when you're  
12 asking the citizens of Pennsylvania to give up  
13 more money, that needs to be fit into a system of  
14 priorities about what is most important to use  
15 that sort of money for.

16 Thank you very much, Senators. Along with my  
17 colleagues, we're happy to answer your questions.

18 CHAIRWOMAN WHITE: Thank you. It was very  
19 interesting. Thank you. Every time I hear from  
20 the PUC commissioners, I learn something, it's  
21 amazing, on the demand side; and we're hearing a  
22 lot about that from both the governor's office and  
23 from the PUC.

24 Just skimming some of the materials you've  
25 given us, you said in here that supply appears to

1           be adequate in Pennsylvania for the foreseeable  
2           future which I think you define as roughly the  
3           next five years. But I'm assuming that you still  
4           believe that we need to reduce demand and educate  
5           consumers.

6                     The last time the PUC had a big consumer  
7           education program as I recall was when we were  
8           trying to encourage people to shop for an electric  
9           supplier. I think that whole thing was sort of a  
10          resounding thud.

11                    It's very difficult to get consumers to  
12          change their ways of behavior unless there is some  
13          linkage between usage and price. So a smart meter  
14          telling me how much I'm using, whether that's  
15          going to change a family's decision about their  
16          routines and when they do their dishes and when  
17          they take their showers and when they do  
18          everything else and use electric power, unless  
19          they see some financial incentives that the prices  
20          will be lower during off peak times, is that part  
21          of the process?

22                    Because, you know, I'm looking at the  
23          governor's proposal. It says we're going to  
24          encourage people to buy an energy efficient  
25          refrigerator; and if they do so, we'll give them

1           some money. Well, you know, most people aren't  
2           going to be able to replace their refrigerator.  
3           They're very expensive items, and they won't  
4           replace them until, you know, water starts  
5           dripping out on the floor and the thing doesn't  
6           work anymore.

7                     The very wealthy people can afford the  
8           refrigerators, can go out and buy one today. And  
9           chances are, they'll go out and do what my son  
10          did, buy a nice beautiful energy efficient  
11          refrigerator and put the old one down in the  
12          basement for the kids' soda pop. You know,  
13          there's no reduction in the electric usage there,  
14          folks. And I'm not sure that the plans are very  
15          well thought out. So what are we going to do on  
16          the demand side to make sure the consumer really  
17          changes behavior?

18                    MR. HOLLAND: I'll start, and then defer to  
19          Commissioner Fitzpatrick.

20                    I said it earlier, Senator White, the  
21          smartest part of the meter is the customer. And  
22          your son's experience proves that very point.

23                    We're being very aggressive with respect to  
24          education. As you might recall, during the price  
25          mitigation hearing, we had a number of parties

1           come before us. Virtually all thirty-nine of the  
2           parties said that we needed some kind of consumer  
3           education program.

4           It's interesting because they tried to attach  
5           a price tag to the consumer education program. It  
6           ranged from about ten million up to twenty-five  
7           million. We think that five million is the proper  
8           place to start. As Commissioner Pizzingrilli I  
9           think alluded to earlier, we're prepared to start  
10          our education hearings, I believe before the end  
11          of this month.

12          With that, I'll ask Commissioner Fitzpatrick  
13          to add to that.

14          MR. FITZPATRICK: Thanks, Mr. Chairman. I  
15          want to applaud Vice Chairman Cawley for starting  
16          a proceeding that we still have going on, a  
17          collaboration on demand response, how to reduce  
18          peak crisis.

19          This issue with the meters is one that we  
20          haven't decided yet. We're going to have to look  
21          at that, and I'm not sure how I'm going to come  
22          out on the question of should everybody have an  
23          advanced meter. There is an argument that that's  
24          part of the advanced infrastructure we're going to  
25          need going forth, we ought to do it for everybody.

1           But there's also the argument I think if  
2           people want to pay flat prices, they're not  
3           interested in paying time-bearing prices, do we  
4           really need to be putting that metering in for  
5           those folks.

6           Because it is possible, if you're making  
7           different pricing options available to people, you  
8           just put in the meters for the folks who want  
9           those kind of pricing options. You don't  
10          necessarily have to put it in for everybody.  
11          That's an issue which I haven't decided yet.  
12          We're going to give that careful consideration.  
13          We know there's a variety of viewpoints out there.

14          But the other thing with conservation is  
15          we're also going to have a baseline consumer  
16          education message. Whether it's done statewide,  
17          whether you agree there ought to be money for  
18          that, and it will be up to you, or whether the  
19          utilities themselves do it within their service  
20          territories, we're going to continue to emphasize  
21          to people the basic things you can do to save  
22          energy such as turning off the lights, you know,  
23          watching where your refrigerator is set, pulling  
24          blinds on hot days, that sort of thing.

25                 CHAIRWOMAN WHITE: I still think price will

1 affect more than consumer education.

2 MR. FITZPATRICK: Senator, I agree. There's  
3 nothing like higher prices to get the attention of  
4 people. That combined with the education we hope  
5 will have some effect.

6 CHAIRWOMAN WHITE: Do we have any authority  
7 over that, or is that going to be up to the  
8 individual sellers of electricity?

9 MR. CAWLEY: We do have control over that,  
10 and price is the greatest motivator.

11 As usual, Senator, you've put your finger on  
12 a vital point. You ask, Why are we encouraging  
13 demand side response, Why are we encouraging  
14 conservation and insisting the utilities have  
15 programs to do that. The answer is this. It lies  
16 in the numbers. The demand on our grid is  
17 increasing every year. There's approximately 1.2  
18 percent annual base load growth, thirteen percent  
19 peak load growth in the 2004 to 2006 area. It's  
20 projected by 2017, there will be a sixteen percent  
21 increase demand on our grid.

22 Without aggressive conservation and  
23 investment in alternative energy resources that  
24 are going to take or reduce the need to build new  
25 power plants, we've got to meet the demand by

1 building new expensive power plants, more  
2 transmission lines. Senator Stout, I know you  
3 don't want to hear that.

4 Congress has seen that. That's why, you  
5 know, they're imposing on the states these  
6 national electricity corridors. They are  
7 narrowing the discretion that people like us have  
8 to determine whether transmission lines get built.

9 CHAIRWOMAN WHITE: What do you think about  
10 that?

11 MR. CAWLEY: What do I think about that?  
12 Number 1, I can't do anything about it except join  
13 with you in urging some restraint. I've got to be  
14 careful because we have a couple cases before us.  
15 One is the project in Senator Stout's territory,  
16 in his district.

17 I don't think there's any question that we  
18 need more transmission. I mean, you've got to  
19 operate with what you've got. You've got to build  
20 some new ones if only for reliability reasons if  
21 nothing else.

22 So really what that case is going to come  
23 down to, Senator Stout, are they projecting that  
24 piece, proposing to built that piece in  
25 Pennsylvania simply to be able to sell more power

1           farther east in markets or are they doing it  
2           because they need it for reliability purposes in  
3           your district in western Pennsylvania. Those are  
4           the essential issues.

5                     But when it comes right down to it, we can  
6           vote no and say no; and we can be overturned by  
7           the Federal Energy Regulatory Commission in the  
8           final analysis.

9                     CHAIRWOMAN WHITE: One last question. On the  
10          long-term contract issue, I've gone around and  
11          around on this in my head. I've listened to a  
12          number of things.

13                    I take it, am I correct in assuming that the  
14          commission tends to take the position that the  
15          default service provider, that it is not a good  
16          thing to enter these long-term contracts because  
17          it will have a dilatory effect on competition, on  
18          new competitors coming into the marketplace, if  
19          that big industrial load is all tied up by the  
20          providers?

21                    MR. CAWLEY: May I just answer briefly?  
22          There are two kinds of long-term contracts.  
23          There's acquisition of supply, and our recent  
24          orders have encouraged some use of long-term  
25          contracts to bring along new technologies so that

1           they can be financed and have a guarantee of a  
2           long-term contract with the utility. We've  
3           encouraged long-term contract use for reliability  
4           purposes. So acquisition of supply long-term  
5           contracts is one thing.

6                     Retail contracts are what the controversy is.  
7           Our larger customers are chaffing at the fact that  
8           they can no longer receive from their utility  
9           company a long-term contract at two and a half or  
10          three cents a kilowatt hour when the market price  
11          is eight to eleven cents a kilowatt hour.

12                    And as you've already heard Commissioner  
13          Fitzpatrick say, Why not --

14                    CHAIRWOMAN WHITE: I have the same question  
15          he has.

16                    MR. HOLLAND: -- why not get it from the  
17          utility.

18                    CHAIRWOMAN WHITE: Why wouldn't the utility  
19          be able to provide it cheaper when they both have  
20          to buy it from a generator? Why can't they  
21          compete? I don't understand.

22                    MR. FITZPATRICK: When we had our price  
23          mitigation proceeding, we had some customers in  
24          front of us. We opened it up. We listened to  
25          everybody about this. We had some customers

1           testify they wanted to be able to get these  
2           contracts from the utility. The vice chairman had  
3           a long, as I recall, a long discussion with a  
4           customer about that. We didn't really get an  
5           answer.

6                     Now, there's a study out there by Carnegie  
7           Mellon which was prepared for the Team  
8           Pennsylvania Foundation. And they said, Well,  
9           long-term contracts by the utility may save some  
10          money if the utility is more credit worthy. But  
11          that's the only basis.

12                    And further, long-term contracts are  
13          generally going to be more expensive because that  
14          contract price is going to be based on what's  
15          going on in the market at that time plus a risk  
16          premium to protect against what's going to happen  
17          in the future.

18                    Just one other thing, Senator. If you're  
19          talking about the utility as a provider of last  
20          resort making a lot of long-term contracts to  
21          serve the general body of customers, if that's  
22          going to be considered, there's going to need to  
23          be some other changes made to the competition law.

24                    What that can mean over time is the utility's  
25          price that it's charging for generation could get

1 really out of touch with what's going on in  
2 markets at any particular time. That can give  
3 customers incentive to jump off a utility service.  
4 And if the utility has a right to full recovery of  
5 their costs, those costs are then going to go on  
6 the remaining customers who don't have choices.  
7 So we're going to have to rethink, I believe, a  
8 lot of things if that's going to be a change of  
9 policy.

10 CHAIRWOMAN WHITE: I think that is my bottom  
11 line. How do we keep one class of customers from  
12 subsidizing prices to another class of customer?  
13 Isn't that the bottom line on the retail side?

14 MR. CAWLEY: And the governor's legislation  
15 sponsored by Senator Musto says may, an electric  
16 utility may offer a long-term contract. The  
17 leaders of our electric utility, they're  
18 investor-owned utilities. They have a fiduciary  
19 responsibility to their shareholders, but they may  
20 offer long-term contract. It's up to them.

21 They could do like Duquesne Light recently  
22 did where there was a quid pro quo. We're going  
23 to give you a lower price over a long period of  
24 time. What are you going to do for Pennsylvania  
25 in return? Are you going to promise to stay in

1 Pennsylvania? Are you going to add jobs in  
2 Pennsylvania? Are you going to add capacity? Are  
3 you going to use more electricity? Are you going  
4 to create more jobs and pay more taxes in  
5 Pennsylvania in exchange for shareholders pay part  
6 of the bill and other customers pay part of the  
7 bill? That's a fair trade, and that's why I think  
8 may in the legislation is important.

9 MR. HOLLAND: The final aspect that kind of  
10 complicates this is the action of the Commonwealth  
11 Court with respect to recent rate design and  
12 cross-subsidization issues. That's made our job a  
13 little bit more complex than it was before. So  
14 we've got to kind of liberally balance all these  
15 issues.

16 CHAIRMAN TOMLINSON: Thank you very much.  
17 Senator Musto?

18 SENATOR MUSTO: Thank you, Mr. Chairman.  
19 Good morning. Chairman Holland, in the case  
20 before the PUC where the systems benefit charge  
21 was considered, do you recall how much that charge  
22 was to be and how it would be used?

23 MR. HOLLAND: Yes, I do. I believe the  
24 charge, subject to check, was about six dollars a  
25 year, I believe. And I believe it was to be used

1           amongst other things to try to support and  
2           encourage the development of alternate forms of  
3           energy here in Pennsylvania, much as systems  
4           benefit charges in the thirteen states that have  
5           adopted those changes tried to achieve.

6           SENATOR MUSTO: Commission Fitzpatrick  
7           brought up a good point about a systems benefit  
8           charge. Many items and issues should be taken  
9           into consideration.

10          Commission Fitzpatrick, I certainly  
11          appreciate you addressing the issue of CSO's. Not  
12          that I'm disappointed, but I do hope that we can  
13          do something about CSO's. The paper that you have  
14          written should be passed on to the federal also.  
15          I would like to see that and share it with you.

16          MR. FITZPATRICK: Thank you, Senator.

17          SENATOR MUSTO: Also, Commissioner  
18          Fitzpatrick, in the Alternative Energy Portfolio  
19          Standards Act, we provided for a solar share, that  
20          a certain amount of solar energy will have to be  
21          purchased. Do you feel that this is enough of an  
22          incentive for the solar industry to develop in  
23          Pennsylvania, or should we be doing something else  
24          or something more?

25          MR. FITZPATRICK: Senator, I will say at the

1           outset, not everybody agrees with this; but I tend  
2           to be a free market person rather than somebody  
3           who likes a lot of mandates.

4           The alternative energy act does require that  
5           there be a start at least for solar. And I think  
6           it's good that we're going to make a start with  
7           all of these technologies to diversify a bit. But  
8           again, when you talk about providing more  
9           assistance for more subsidies, I think you need to  
10          balance that against all the other demands that  
11          there might be for money.

12          I'm not sure myself that it's justified or  
13          would fit the priorities that I think are there.  
14          But if somebody would disagree with me, I wouldn't  
15          tell them they're wrong. It's a judgment call  
16          that has to be made.

17          SENATOR MUSTO: Thank you. I have no further  
18          questions, Mr. Chairman.

19          CHAIRMAN TOMLINSON: Senator Stout?

20          SENATOR STOUT: Thank you. First I want to  
21          congratulate the co-chairs of today's hearing for  
22          putting together such an expert panel of  
23          information.

24          I know you heard the question I asked the  
25          gentleman from the DEP about the trail project in

1 southwestern Pennsylvania. Now, you dwell on the  
2 fact that there will be an energy shortage in  
3 Pennsylvania and need for additional capacity to  
4 meet our domestic demands. How in the world can  
5 we afford to shift power out of the Commonwealth  
6 to these other markets simply because they'll make  
7 more money by taking our coal-fired generating  
8 capacity in southwestern Pennsylvania and ship it  
9 to the eastern seaboard? It doesn't seem right.

10 We were taking all of these actions to try to  
11 conserve energy here in Pennsylvania, but we're  
12 allowing this to happen. You talked about rates.  
13 Will not the rate payers of my district, the  
14 customers of Allegheny Power, have to help pay for  
15 that line? It's going to basically transport  
16 power to the east coast. You talked about rates.  
17 Why should the rate payers have to contribute to a  
18 multi-billion dollar project to transport power  
19 outside of Pennsylvania? That doesn't seem to be  
20 right.

21 MR. HOLLAND: I'd be glad to -- I'm sorry.

22 SENATOR STOUT: Go ahead, Mr. Chairman.

23 MR. HOLLAND: Thank you, Senator Stout. Let  
24 me make a general disclaimer for myself and all of  
25 my colleagues that as the trail project is

1           presently before us, we'll respectfully decline to  
2           comment on that.

3           The greater issue seems to be a point at  
4           least that I touched upon earlier, that we are, as  
5           a commission, very excited that this legislature  
6           and the executive branch is turning their eyes on  
7           energy issues, the kinds of things that we've been  
8           doing day after day after day after day.

9           While we're here to talk largely about the  
10          proposed energy package, I suggested at the top of  
11          my testimony that somewhere down the road this  
12          joint committee should look at a few other stuff,  
13          namely the question of transmission, transmission  
14          not just in a domestic context, transmission in a  
15          regional context. And I look forward to working  
16          with you and members of your commission on that  
17          issue.

18          MR. CAWLEY: Senator, as you know, at your  
19          urging, I'm going to come out and walk a good part  
20          of the line. I'm not a mountain goat, so I'm not  
21          going to do the whole line.

22          SENATOR STOUT: Well, you have a lot of hills  
23          to climb.

24          MR. CAWLEY: I think we have resolved that  
25          with the presiding administrative law judge that

1 we're going to give people that want to hear and  
2 want us to look at a particular section of the  
3 line, we're going to go out and we'll have a  
4 hearing right on the spot. We're going to go out  
5 and look. I'm going to be there at your urging,  
6 and I suspect some of my colleagues will be there  
7 with me.

8 SENATOR STOUT: You're more than welcome to  
9 the forty-sixth senatorial district. I know you  
10 can't comment directly on the trail application  
11 because it's before you, but does the PUC have  
12 power to restrict the utility from transporting  
13 power outside of Pennsylvania? You encourage them  
14 to increase generation, but can you restrict a  
15 generator from shipping his power outside of the  
16 Commonwealth?

17 MR. HOLLAND: I think subject to checking it  
18 out, I'll defer to my colleagues. Outside of  
19 Pennsylvania would be controlled by the Federal  
20 Energy Regulatory Commission, and I think our  
21 power to so restrict would be very limited.

22 MR. CAWLEY: It doesn't just end there. Let  
23 me put another acronym in your lexicon, RPM,  
24 something called the reliability pricing model.  
25 Probably the next time to invite us over to



1 state commission, Senator Stout, I am president of  
2 the organization of PJM states for the last two  
3 years. It's a seventeen member body. We opposed  
4 it as a regional body as well. But it is an issue  
5 you're going to continue to hear about.

6 And again, I will say as we look at the  
7 energy picture here in Pennsylvania, we can't be  
8 blind to the fact that energy should be looked  
9 upon also in a regional context because of the  
10 interconnection.

11 SENATOR STOUT: Thank you, Mr. Chairman.

12 CHAIRMAN TOMLINSON: Thank you, Senator  
13 Stout. Senator Boscola?

14 SENATOR BOSCOLA: I want to thank the entire  
15 commission, Chairman Holland, for your testimony.  
16 And I know you really work hard to protect  
17 consumers from unreasonable rates, and I'm very  
18 confident that we have one of the best commissions  
19 in the entire country with your expertise.

20 So with that, I agree with the smart meters  
21 and other aspects of this proposal, this  
22 independent strategy.

23 But again, coming back to the systems benefit  
24 fee, I see it as a small tax now. And in this  
25 business that I'm in, it seems like every time we

1           enact a new tax, it never goes away. It just  
2           keeps going up. The occupational privilege tax  
3           went from ten to fifty-two dollars. This is the  
4           way this place operates.

5                     And I want to commend Chairman Fitzpatrick  
6           for saying this because I think you're dead right  
7           here. I mean, we have a free market. These are  
8           private companies. I don't understand why this  
9           tax is necessary.

10                    I would hope that the entire commission would  
11           take that into consideration because I really feel  
12           that these are the questions that consumers are  
13           going to be asking all of us. Was this absolutely  
14           necessary in this free market? These are private  
15           companies. It kind irritates me a little bit.

16                    And why I say this, I think Commissioner  
17           Pizzingrilli talked about the classes. I felt  
18           that deregulation really benefited the commercial  
19           industrial class but not really the residential,  
20           and this fee is going to impact them. I think we  
21           have to really consider that.

22                    MR. HOLLAND: Thank you, Senator Boscola. In  
23           anticipation of the question that you asked  
24           earlier, I've done some last minute research.

25                    Subject to check, the simple answer is I've

1           been advised that the six dollars stays six  
2           dollars. The rationale is that in Senate Bill 716  
3           in Section F-1, it states, Each electrical  
4           distribution company shall apply and collect the  
5           charge of five mils for each KWH of electricity  
6           sold. This is a per kilowatt hour charge. It's  
7           not a percentage of the bill, so it stays at about  
8           the six dollars per year for the life.

9                     Again subject to check, it will not increase  
10           what a customer pays because of increased  
11           electricity costs. I would love to reserve the  
12           right to do more involved research and get back to  
13           you and the committee on this issue.

14                    MR. CAWLEY: Senator, with respect, let me  
15           stick up for the systems benefit charge.

16                    SENATOR BOSCOLA: I wish you wouldn't, but...

17                    MR. CAWLEY: You know, for the monthly cost  
18           of a pack of cigarettes or a carton of orange  
19           juice, we can do a lot of good things with the  
20           money.

21                    As usual, we all are sent to Harrisburg to do  
22           the public's business. I view this as an  
23           investment, a very small investment; but it all  
24           really comes down to how do we do the public's  
25           business, how wisely do we spend the money. This

1 is an insignificant amount of money relatively  
2 speaking.

3 If it's leveraged and the money that is  
4 derived from it is spent wisely, it's a good  
5 investment. If we impose the charge and we  
6 foolishly use the money, then that's another  
7 question.

8 So I think the debate should not be on  
9 whether there's a systems benefit charge. Every  
10 other state in the northeast has already adopted  
11 this, twenty states altogether. The debate ought  
12 to be, if we do this, how do we wisely use the  
13 money to encourage conservation, demand side of  
14 the industry, to wisely use the energy?

15 SENATOR BOSCOLA: I agree with you to some  
16 extent, but I think the public can do a lot of  
17 things if you let them keep some of their own  
18 money in their own pockets. They'll do things  
19 wisely too.

20 CHAIRMAN TOMLINSON: Thank you, Senator  
21 Boscola. If I can leave you with the same charge  
22 that I left the deputy secretary. Do the math for  
23 me, please. Try to put this together for us and  
24 the committee: the increase in demand; the  
25 potential loss of production of power because of

1 DEP, because of regulations; how much is the new  
2 alternative energy going to produce; how much  
3 savings. There's an equation here.

4 You're going to have people wanting more  
5 power. We're going to try to conserve more power.  
6 We're going to lose generation, I understand, up  
7 to ten percent because of regulations on the  
8 generating plants.

9 So there's got to be an equation here that  
10 tells us what's the best way to use a systems  
11 benefit charge or how we manage this. Are we  
12 going to be in a -- we are in a debtor's situation  
13 as far as producing our own electricity.

14 How do we best manage this problem that I see  
15 coming with increased demand, the loss of  
16 generation? I'm hearing that solar and wind can  
17 generate maybe two percent of the power. So we  
18 incentivize one, and it gives us two percent more.  
19 We encourage conservation. How much does that  
20 save us? And yet we still have increasing demand  
21 coming at us, and we're losing ten percent  
22 generation.

23 Would you folks do the math for me and get  
24 back to me and give me an opinion on how these  
25 figures and all these concepts are coming at us?

1           What is the result of that? What is the  
2           conclusion of that?

3           MR. HOLLAND: Yes, sir. Do you have a time  
4           frame?

5           CHAIRMAN TOMLINSON: Tomorrow. You have the  
6           laptop in front of you. You can do that tomorrow.

7           Thank you very much. This has been a great  
8           session of give and take. And as I stated  
9           earlier, I look forward to seeing the ideas coming  
10          from all of you and the deputy secretary. Thank  
11          you very much. We're a half hour beyond our time;  
12          and we do have another very important presenter,  
13          so thank you very much for your time.

14          CHAIRWOMAN WHITE: And congratulations to  
15          Chairman Holland and Commissioner Pizzingrilli on  
16          your reappointment.

17          MR. HOLLAND: Thank you, Senator White.

18          CHAIRMAN TOMLINSON: At this time I'd like to  
19          ask the officer of consumer advocate, Irwin  
20          Popowsky, to please step forward and present his  
21          testimony.

22          Thank you very much, Mr. Popowsky, for taking  
23          the time in presenting your testimony; and I'd ask  
24          for some order in the room. Would you please  
25          begin?

1                   MR. HOLLAND: Thank you, Senator Tomlinson,  
2                   Boscola, Senator White, Senator Musto, Senator  
3                   Stout. It's a great honor to be here on this  
4                   matter of utmost importance to the consumers of  
5                   Pennsylvania whom I represent.

6                   I don't think it's an exaggeration to say  
7                   that we are at a critical crossroads in the  
8                   history of the Pennsylvania electric industry.  
9                   The stakes are extraordinarily high, not just for  
10                  the utilities, but for the millions of  
11                  Pennsylvania consumers whom they serve and for the  
12                  economic environmental health of the Commonwealth  
13                  as a whole.

14                 As the members of this committee are well  
15                 aware, the generation rate caps that have  
16                 protected most Pennsylvania consumers from the  
17                 winds of change in the electric industry will be  
18                 coming off at the end of this decade. But they'll  
19                 be coming off in a world that is much different  
20                 than the one that many of us expected when the  
21                 general assembly passed and Governor Ridge signed  
22                 the landmark Pennsylvania Electric Restructuring  
23                 Law in 1996.

24                 The policies that we develop between now and  
25                 2010 could determine whether Pennsylvania has

1 crash landed as has occurred in several of our  
2 neighboring states when rate caps came off or  
3 whether we can continue on what has generally been  
4 I think a positive path toward restructuring our  
5 electric industry in a reasonable and beneficial  
6 manner.

7 I think the time has come today for the  
8 general assembly to act, that is, for the general  
9 assembly to reexamine some of the provisions of  
10 the 1996 act, not to retreat, but to reexamine the  
11 1996 act in light of current realities.

12 We can't in my opinion or at least we  
13 shouldn't wait until the rate caps come off as  
14 occurred in states like Maryland, Delaware, and  
15 Illinois, where the respective state legislators  
16 have had to react in crisis situations for public  
17 demands for legislative solutions after the fact.

18 The time to act is now before the rate caps  
19 come off. And I think certain provisions of the  
20 act need to be amended, particularly along the  
21 lines suggested by Senator Musto in Senate Bill  
22 716 in accordance with some of the provisions of  
23 the governor's energy strategy.

24 Let me mention in addition to Senator Musto's  
25 bill -- and again, let me just say it's been an

1 honor to work with you, Senator Musto, over all  
2 these years on consumer utility issues; and I  
3 appreciate your leadership on this as well.

4 There's also a bill in the House, House Bill  
5 697, which has been introduced by Representative  
6 Ross who many of you will remember along with  
7 Senator Erickson was a leader in the passage of  
8 the Alternative Energy Portfolio Standards Act in  
9 2004 which I supported then and I continue to  
10 support as a means of ensuring a diversity of  
11 resources for Pennsylvania consumers to their  
12 long-term benefit.

13 But I do think it's necessary to take another  
14 look at the provisions of the 1996 act. When the  
15 law was enacted in 1996, it was widely assumed  
16 that competition would drive down the price of  
17 generation which is why we allowed the utilities  
18 to recover billions of dollars of stranded costs.

19 Senator Tomlinson, I'm sure you remember.  
20 The primary concern we had was that competition  
21 was going to drive prices down. We weren't  
22 worried about rate caps coming off and rates going  
23 up. We were worried the prices were going to come  
24 down, the utilities would be bankrupted. And  
25 that's why we had to pay them billions of dollars

1 to stay in the Commonwealth.

2 In addition, we were concerned that everyone  
3 was going to leave their utility, that they were  
4 going to flock. We were worried about getting,  
5 you know, getting calls at 6:00 at night from  
6 marketers.

7 We even passed a law again, if you recall,  
8 that said that only one-third of customers could  
9 leave each year. Remember that we phased in the  
10 competition because we were so concerned that  
11 everyone was going to flock. But of course,  
12 that's not what happened.

13 But even in 1996, the general assembly did  
14 have a safety valve which was called at that time  
15 the provider of last resort of service for those  
16 customers who for whatever reason did not switch  
17 to an alternative supplier.

18 And the rate caps were put in place as  
19 another safety valve, that is, just in case during  
20 the period when the utilities were recovering  
21 stranded costs, just in case rates didn't go down,  
22 we were going to make sure at least they didn't go  
23 up. That's why we had the rate caps.

24 Now with rate caps coming off, ninety-nine  
25 percent of our residential customers in most of

1           our service territories are still being served by  
2           their utility. This is no longer just a matter of  
3           a provider of last resort. This is the service  
4           that most people are going to be receiving in  
5           2010, 2011, and I believe in 2015 and 2020, that  
6           is, the service, the continued basic service for  
7           residential customers from their utility.

8                     Now, when we passed the law in 1996, we said  
9           that for those handful of customers who weren't  
10          shopping, the utility would continue to be the  
11          provider of last resort and they would serve those  
12          customers with what's called prevailing market  
13          prices. Basically you could look it up. What's  
14          the prevailing market price? That's the charge  
15          that the customers would pay.

16                    But again, that's not the situation we're in  
17          here in 2007. We're in a situation where this is  
18          the most important thing that we can do, which is  
19          to make sure that the service that's provided by  
20          our utilities when the rate caps come off is not  
21          simply reflecting whatever the prevailing market  
22          price, whatever the prevailing wholesale market  
23          price is on that day or at that time.

24                    Rather, as set forth in Senator Musto's bill  
25          and in House Bill 697, Representative Ross's bill,

1 I believe that the goal, the job of the utilities  
2 when the rate caps come off, at least the  
3 residential customers and customers that have very  
4 little choice, should be to make sure that they  
5 are acquiring the least costly resources.

6 Yes, they should be using the wholesale  
7 market; but they should be acquiring the lowest  
8 priced resources to provide stable and reasonable  
9 prices over time, not simply taking whatever the  
10 prevailing market price is, but to provide stable,  
11 reasonable prices over time.

12 For that reason, again, in Senate Bill 716  
13 and the governor's energy strategy and House Bill  
14 697, there's a requirement that the utilities  
15 acquire -- we're talking about now contracts  
16 between the utility and their suppliers -- that  
17 the utilities acquire a portfolio of resources,  
18 including long-term and short-term contracts, spot  
19 market prices.

20 But the goal, the job of the utility would be  
21 to go into the market starting today, not waiting  
22 until 2010, but starting today to acquire the  
23 portfolio of resources that would best serve their  
24 customers.

25 There's several reasons why I think long-term

1 contracts should be a part, not all or not even a  
2 majority, but should be a part. And the most  
3 important of those is I think probably for a  
4 reason perhaps mentioned by you, Senator White, is  
5 we need to have some assurance that people will  
6 actually add resources in Pennsylvania, that  
7 people will actually build things.

8 We have some experience that relying on these  
9 short-term markets, which I think is where, if you  
10 look at the commission regulations, while  
11 long-term contracts with suppliers are permitted  
12 under very narrow circumstances, they're certainly  
13 not favored.

14 In my opinion, they should be a fundamental  
15 part of the resource portfolio of every utility  
16 that continues to serves so many millions,  
17 millions of Pennsylvania consumers. And if we  
18 don't do this, my fear is that this continued  
19 reliance on short-term resources, short-term  
20 contracts, short-term prices, prevailing market  
21 prices will lead us to the situation that we're  
22 finding in places like Maryland and Delaware and  
23 Illinois where when the rate cap comes off, chaos  
24 ensues.

25 So if we can get these long-term contracts in

1 place, I think it would be a critical factor; and  
2 I think legislation is needed, not that we need to  
3 tell the commission or the utilities what to do in  
4 every circumstance, what contract they should  
5 enter into, but we should at least change the  
6 goal. The goal should be the lowest reasonable  
7 cost on a stable basis over a long period of time.  
8 The goal should not simply be to provide power at  
9 prevailing market prices.

10 And by the way, we have had some success in  
11 this area. One of our utilities, Duquesne Light  
12 Company, with respect to residential customers has  
13 provided long-term fixed prices to their  
14 customers. They have not gone into the market,  
15 rolled the dice, and had it auctioned at the last  
16 minute. Instead, they developed a portfolio of  
17 resources to serve their customers.

18 The other critical issue I think is here, I  
19 would certainly agree with the commissioners and  
20 again with Senator Musto and the governor's energy  
21 strategy, which is that the demand resources have  
22 to be part of that portfolio. Energy efficiency  
23 in particular in my view is fundamental. We just  
24 have to sort of lower that baseline because the  
25 way the PJM market works and the way prices are

1 set, we're always paying the highest price at any  
2 given hour.

3 If we can lower that price by reducing demand  
4 at the highest priced hours and throughout the  
5 year, then I think we have a better chance, at  
6 least a fighting chance in 2010, 2011, to ensure  
7 that customers are not hit with the kind of price  
8 spikes and kind of fiascoes that we've seen in  
9 other states.

10 I just want to mention in my written  
11 testimony, I discuss it's almost amazing. If you  
12 look at the states that have come out of their  
13 rate caps, Maryland, Delaware, Rhode Island,  
14 Maine, they have in 2006 all passed legislation to  
15 develop portfolio standards, that is, to require  
16 their utilities to engage in a broader array of  
17 resource procurement, to secure a long-term and  
18 short-term portfolio, to move away from spot  
19 prices and short-term market prices. I've given  
20 details of some of these states in my written  
21 testimony that have done that.

22 Again, we have the chance to act now. We  
23 have a chance to act before chaos hits, and I  
24 would certainly urge you to take advantage of  
25 that.

1           So in closing, I think we do have a choice in  
2           Pennsylvania. We can do nothing, and we can hope  
3           that the prevailing market prices in 2010 are  
4           favorable to Pennsylvania consumers and that we  
5           will have adequate resources to sustain the  
6           Pennsylvania economy.

7           Or we can begin to take proactive steps now  
8           such as those contained in Senator Musto's Senate  
9           Bill 716, House Bill 697, and the governor's  
10          energy independence strategy to at least try to  
11          protect customers and support the development of  
12          the supply and demand resources that can help  
13          ensure adequate service at reasonable prices.

14          So with that, I'll conclude and thank you  
15          again for inviting me here today.

16          CHAIRMAN TOMLINSON: Thank you, Mr. Popowsky.  
17          Senator White?

18          CHAIRWOMAN WHITE: On the long-term contract  
19          issue, what you seem to be saying is that you  
20          support the concept of having a mix of perhaps  
21          long-term, short-term in order to get a stable  
22          long-term good price, not just whatever happens to  
23          be the good price at the moment on the wholesale  
24          side. But what about the retail contract side  
25          where we are currently prohibiting the supplier

1 from entering long-term contracts with the large  
2 industrial users?

3 MR. HOLLAND: First of all, let me say on the  
4 residential side, if I could, under the  
5 commission's regulations, the prices would change  
6 at least every three months for residential  
7 customers and even more frequently if the utility  
8 chose to do so.

9 My belief is that even residential customers  
10 don't want to constantly be not knowing what the  
11 price of electricity is. And in my view, we  
12 should have a more stable price, perhaps one that  
13 changed every year, but it would only change  
14 gradually because there would be a portfolio that  
15 only a portion of the portfolio would change every  
16 year.

17 CHAIRWOMAN WHITE: It would be volatile.

18 MR. POPOWSKY: Right. So there wouldn't be  
19 that volatility, and I don't think that volatility  
20 is what customers want. I think they want a  
21 stable price.

22 In terms of the provision of the law  
23 regarding large customers, the most important  
24 provision there to me is the sentence that says,  
25 And none of the costs of those contracts shall be

1 borne by any other customer or customer class.

2 CHAIRWOMAN WHITE: How do we know that  
3 though? I mean, it's like spaghetti sauce. When  
4 it all gets in there, how do you know whether one  
5 class of customer is subsidizing another?

6 MR. POPOWSKY: I think the only way to know  
7 that is the way rates are set now, because they're  
8 what is, quote, unquote, unbundled. That is, we  
9 no longer have this big pot of spaghetti. We have  
10 a lot of strands out there, and each one of them  
11 is priced separately.

12 I think it is possible in today's market  
13 because of the fact that you have unbundled rates.  
14 And if a utility does acquire resources  
15 separately, that is, they have one resource  
16 procurement for residential customers, one for  
17 commercial, and one for industrial customers, I  
18 think it's possible. But I think that is the  
19 test.

20 From my perspective, if an arrangement can be  
21 made between a utility and a large customer where  
22 that customer says, Yes, you know, I will stay  
23 here for five years, ten years, and I will enter  
24 into this contract, I have no problem with that as  
25 long as the cost of that are not borne by other

1 customers.

2 CHAIRWOMAN WHITE: Thank you, Mr. Chairman.

3 CHAIRMAN TOMLINSON: Senator Musto?

4 SENATOR MUSTO: Thank you, Mr. Chairman. I  
5 have no questions, but I certainly commend you for  
6 your testimony this morning. In fact, this has  
7 been a very successful hearing. We did receive a  
8 tremendous amount of information.

9 As you have stated, regarding Senate Bill  
10 716, I have introduced it in plenty of time to  
11 receive input from yourself and the PUC,  
12 consumers, the industry. Everyone has an  
13 opportunity to comment and of course have input in  
14 developing Senate Bill 716, and I really  
15 appreciate it. Thank you.

16 MR. HOLLAND: Thank you, Senator.

17 CHAIRMAN TOMLINSON: Senator Stout?

18 SENATOR STOUT: Thank you, Mr. Chairman. I  
19 have no questions at this time. We have to get  
20 back to the senate floor in a few minutes. I  
21 appreciate your testimony and look forward to  
22 hearing from you, Sonny. Thank you.

23 MR. HOLLAND: Thank you. And I'm sure we'll  
24 be working together on the transmission  
25 application.

1                   SENATOR STOUT: You're welcome to walk the  
2 hills of southwestern Pennsylvania.

3                   MR. HOLLAND: I'll be there.

4                   CHAIRMAN TOMLINSON: Thank you, Senator  
5 Stout. Senator Boscola?

6                   SENATOR BOSCOLA: Sonny, all the states that  
7 you cited, I guess they required the utilities to  
8 have long- and short-term portfolios, did any of  
9 them have a systems benefit fee or tax associated  
10 with it?

11                  MR. HOLLAND: Not associated with that, per  
12 se. But I think it is true that nearly all the  
13 states in our region, a majority of the states in  
14 our region do have a systems benefits charge.  
15 That is separate from that, but they have had them  
16 for several years now.

17                  SENATOR BOSCOLA: So you're saying the  
18 solution would be long- and short-term portfolios,  
19 so that seems to be working? So we can enact  
20 legislation like some other states did that will  
21 help?

22                  MR. POPOWSKY: Yes. I think the key is to  
23 try to get pressure on the wholesale market; and  
24 one way to do that is to develop more resources,  
25 develop more resources, demand and supply.

1           I think in answer to your question, I think  
2           where the systems benefit charge, as I understand  
3           it, would be of assistance in that it would help  
4           finance, for example, some of the energy  
5           efficiency programs and other programs to help  
6           bring those resources in Pennsylvania.

7           SENATOR BOSCOLA: Could you get back to me  
8           with those then? You cited Maine, Rhode Island,  
9           Maryland, Delaware.

10          MR. POPOWSKY: Sure. I can find out what  
11          they have in terms of systems benefits charges.  
12          Sure.

13          CHAIRMAN TOMLINSON: Thank you. Sonny, if  
14          you're going to do that homework for us, find out  
15          what they use their systems benefits charge for.

16          MR. POPOWSKY: Good point.

17          CHAIRMAN TOMLINSON: As you heard earlier,  
18          many of us are very concerned about the  
19          infrastructure. We're concerned about, as I was  
20          in '96, concerned about reliability, whether we  
21          have enough generation. When we separated those,  
22          I was very concerned about if we'd have  
23          generation. As you're looking that up, if you  
24          can, find out what they do use that for.

25          The time has run out. We're almost an hour

1 over. I want to thank you. I do look forward to  
2 discussing some of the things that were brought up  
3 here today. I think it was an excellent hearing.  
4 It brought a lot of issues out.

5 And the overriding issue that comes to me is  
6 that you hear that generation is going to be down  
7 ten percent because of regulation, demand is going  
8 to be up sixteen percent. How much will the  
9 alternative energy portfolio produce? How much  
10 does wind, how much does sun power produce? That  
11 equation has got to have an answer where we stand  
12 in the energy policy.

13 I congratulate Senator Musto and those  
14 working on moving these issues forward. With  
15 that, don't answer now. I know you don't have it,  
16 but we look forward to following through on many  
17 of the questions asked here today.

18 MR. POPOWSKY: Thank you. And I look forward  
19 with working with members of both of these  
20 committees.

21 CHAIRMAN TOMLINSON: Thank you. That does  
22 it. We're finished for the day. This concludes  
23 the hearing, and thank you all for participating.

24 (The proceeding concluded at 12:20 p.m.)  
25

1           I hereby certify that the proceedings and  
2           evidence are contained fully and accurately in the  
3           notes taken by me on the within proceedings, and  
4           that this copy is a correct transcript of the  
5           same.

6           Dated at Wormleysburg, Pennsylvania, this 8th  
7           day of June 2007.

8

9

10

11

12

---

Patricia M. Brown  
Reporter - Notary Public

13

14

15

16

17

18

19

20

21

22

23

24           (The foregoing certification of this  
25           transcript does not apply to any reproduction of  
          the same by any means unless under the direct  
          control and/or supervision of the certifying  
          reporter.)