

Prepared Testimony of

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*before the*

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Consumer Protection & Professional Licensure Committee

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Chairman Tomlinson, Chairwoman Boscola, and members of the Committee, I appreciate the opportunity to testify today on various proposals to ease the transition to electricity market prices, including the Department of General Services' application for Commonwealth membership in PJM, creation of a state power authority, purchasing of wholesale power at the municipal level through aggregation of customers, and a proposed ordinance introduced in Philadelphia City Council to create a Philadelphia Energy Authority under the state Municipalities Authorities Act.

My name is Jim Cawley. I am Chairman of the Pennsylvania Public Utility Commission. I appear today with my colleagues to voice my support for some of the mentioned proposals and my disagreement with others.

I *support* municipal aggregation of electric customers (as I did in testimony before the House Consumer Affairs Committee on March 3, 2010). I also support the Department of General Services' attempt to save taxpayers money by having the Commonwealth become a member of PJM, if it obtains the waivers that it has requested and it retains appropriate PJM wholesale market risk management experts.

I *do not support* the creation of a Pennsylvania Power Authority, nor do I support Bill No. 100163 as written creating a Philadelphia Energy Authority.

### **Municipal Aggregation of Electric Customers**

When it enacted the Electricity Generation Customer Choice and Competition Act in 1996, the Legislature clearly hoped that most customers of

investor-owned electric utilities would obtain their electricity supply from a PUC-licensed “electric generation supplier” (EGS) and that only a small residue of customers would remain with the “electric distribution company” (EDC) as the “provider of last resort” or “safety net” provider. In other words, the legislative design was that the new EGSs would generate the electricity or obtain it in the wholesale market (regulated by the Federal Energy Regulatory Commission—FERC) and supply it to almost all customers, with the traditional electric company being the “wires” company that delivered the electricity under PUC-regulated rates, maintained the electric transmission and distribution system, and acted as the supplier of last resort for customers who would not or could not obtain their electricity from an EGS.

The legislative intent has been frustrated by the passage of time since the introduction of electric choice, which has caused a general lack of understanding of the benefits meant to be conferred and the process necessary to obtain them; misplaced brand loyalty to one’s electric utility; needless fears of second-class treatment by the electric utility if an emergency arises or distribution system repairs are required once the customer has chosen an alternative supplier; a natural tendency, especially among older persons, to maintain the status quo and to resist change; the unavailability of computers and even telephone service to contact alternative suppliers by low income households; and, alas, just plain apathy.

The problem is not with larger commercial and industrial customers who make it their business to cut costs wherever possible. In great numbers, they have

consistently chosen alternative suppliers. Small commercial and residential customers are a different story. However, when properly educated, they, too, switch away from the “wires” company’s default service. For example, only three months after PPL Electric Utilities’ rate caps expired, 28.3 percent of its customers (394,950, with 332,369 of them residential customers)—who use almost half of the electricity that PPL delivers—have switched.

But how do we convince the elderly, the poor and near poor, the merely reluctant or suspicious, and the apathetic to switch in their own self-interest?

The answer is customer aggregation, which can best be accomplished by relying on the credibility and leadership of local elected officials to assuage the fears, overcome the apathy, and dispel the confusion about electric choice among many customers.

If enacted, opt-out municipal aggregation will go a very long way to achieving the original legislative goal of near universal switching to alternative electricity suppliers so that customers may enjoy many price and product choices to suit their individual needs—“green” energy offerings (which jibes nicely with the goals of the Alternative Energy Portfolio Standards Act of 2004); discounts to senior citizens, veterans, and current military personnel; fixed and variable pricing; contract terms of one to three years; time of use rates; discounts from promotional rates being phased out; contributions to local charities with each sign-up; and perhaps someday even airline miles, home energy audits, free or

discounted CFL bulbs or home weatherization, and any number of other creative enticements.

The discussion draft that was the subject of the House Consumer Affairs Committee hearing on March 3 accomplishes the legislative goal to promote electric choice by providing for:

- Licensing by the PUC of municipalities as Electric Generation Suppliers for service to eligible customers within the municipality's borders.
- Adoption by municipal ordinance of municipal aggregation.
- Contracts for electricity supply between the municipality and other PUC-licensed EGSs, with transparent terms and conditions.
- Notice to municipal citizens with clear and complete terms and conditions of service, including disclosure of all fees and charges, and any credit, collection, and deposit policies and requirements.
- Adequate opportunity to opt-out of the program before it begins, and defined opt-out procedures and methods.
- Inclusion of only residential and small commercial customers who have not already selected an alternative electric generation supplier, and sensible exclusion of certain customers.
- A three-year cap on program lengths.
- A requirement for the provision of customer lists and customer data by the EDC, with appropriate privacy protections.

- A return to the status quo ante of any inadvertently included customer, plus adequate compensation.
- Distribution of adequate educational materials to customers.
- A requirement for reasonable cooperation from EDCs, with recovery of appropriate administrative costs by them.
- Promulgation of PUC regulations “to encourage and promote large-scale opt-out municipal aggregation in this Commonwealth.”

As an amendment to the discussion draft, the Commission suggested that the contract be competitively bid. In the absence of such a requirement, municipal officials may have the good sense to solicit competing offers in a transparent selection process, but perhaps not. If current law does not require competitive procurement (or if this law is intended to supersede such existing law), it would be wise to prevent opportunities for undesirable favoritism or other mischief. Municipalities should also be encouraged to minimize any imposed switching penalties to reserve a customer’s option to affirmatively select his, her, or its electric generation supplier.

### **DGS Application for Membership in PJM**

As I understand DGS’s proposal, it wishes to become a PJM member in order to buy power directly from the wholesale market on behalf of some (but not all) Commonwealth accounts in order to save taxpayer money.

DGS has indicated to the PJM membership that it intends to hire outside expertise to manage its PJM purchasing, scheduling, risk management, back office

and recordkeeping. These outside experts would assist DGS in the development of a wholesale purchasing program, including strategic buys in the day-ahead and real-time markets, location of generation partners for the purchase of blocks of power through bilateral contracts, and management of activities in other PJM markets (capacity, congestion, Financial Transaction Rights, and Auction Revenue Rights).

DGS has indicated, however, that it must be given waivers of certain obligations specified in the PJM Operating Agreement:

(a) the general obligation of all PJM members to bear a share of any defaults of other members (the “default allocation assessment”), an exemption already afforded to municipal electric system members. This is required because the Commonwealth is prohibited by sovereign immunity from indemnifying third parties.

(b) the PJM’s contract dispute resolution procedures, because Chapter 17 of the Procurement Code, 62 Pa.C.S. § 1721.1 establishes the statutory dispute resolution procedures that apply to contract controversies between DGS and a contracting party. Also, Section 1724(a)(1) provides that the Board of Claims has exclusive jurisdiction to arbitrate contract claims against a Commonwealth agency.

(c) PJM’s working capital and capital contribution requirements, because Article VIII, Section 8 of the Pennsylvania Constitution prohibits the

pledge or loan of the credit of the Commonwealth to any individual, corporation, or association.

I also understand DGS's proposal to include the development of renewable generation projects, including landfill methane recovery and solar photovoltaic and wind power projects. These appear to be already authorized by a subchapter of the Procurement Code known as the Guaranteed Energy Savings Act, 62 Pa.C.S. § 3751 et seq. The definitional section (62 Pa.C.S. § 3752) defines "Energy conservation measure" as "A program or facility alteration designed to reduce energy consumption or operating costs. The term may include, without limitation: ... (15) Renewable and/or on-site distributed power generation systems."

The members of the Commission met with Secretary Creedon and his staff about this proposal several months ago. The Commission members were aware that DGS had already taken commendable steps to save electricity by contracting with a PUC-licensed electricity supplier for discounted electricity, and with a Conservation Service Provider for the implementation of energy efficiency and conservation measures. At least a majority of the Commission members were generally supportive of DGS's PJM application if the substantial risks of such an undertaking could be mitigated by the granting of the waivers discussed above and the retention of PJM experts (which we felt could not be obtained at Commonwealth salary levels).

I therefore support DGS's PJM membership proposal under these conditions, and note the existing statutory authority for competitively-bid development of renewable energy projects.

### **A Pennsylvania Power Authority**

I see no need for such an entity, principally because Act 129 of 2008 already requires the PUC to ensure that wholesale power is acquired at the “least cost to customers over time” by the competitive procurement of default supply by providers of last resort under PUC-approved plans. The Commission has fully implemented that provision, including a requirement that the default supplier (in every case the electric distribution company) retain, at its expense, a reputable expert firm to oversee the actual competitive process and to certify the fairness thereof to the Commission (even though fairly conducted, the Commission has not hesitated to reject the bids anyway). Adding a duplicative layer of government to achieve the same ends would only add costs to ratepayers.

Federal law governs the wholesale electricity market. It permits state regulatory agencies to require competitive procurement of wholesale power. But, once that process determines wholesale costs to retail suppliers, those costs must be passed through to customers without modification. Under this “filed rate doctrine,” states are required to recognize federally approved wholesale rates in their retail ratemaking pursuant to the Supremacy Clause of the U.S. Constitution. *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953 (1986); *see also* *Mississippi Power & Light Co. v. Mississippi ex rel. Moore*, 487 U.S. 354 (1988).

Rates that do not fully recognize the level of rates approved by the Federal Energy Regulatory Commission are likely to be deemed unlawful, even if those wholesale rates are obtained through “market based” rates that are not specified in a tariff. *Public Utility Dist. No. 1 of Snohomish County v. Dynegy Power Marketing, Inc.*, 384 F.3d 756 (9<sup>th</sup> Cir. 2004). At the same time, the Pennsylvania courts also recognize that states are not obligated to pass on to consumers wholesale costs incurred for unnecessary quantities of high cost power, or for costs incurred where the utility has made unreasonable or imprudent choices among wholesale suppliers. *Pike County Power & Light Co. v. Pa. Pub. Util. Comm’n*, 465 A.2d 735 (Pa. Cmwlth. 1983).

The proposal for a state power authority has facial appeal—development of power generation at lower cost than is available in the existing marketplace (which is driven by private investment) in order to subsidize power costs of Pennsylvania businesses and thus encourage economic development. The proposal would be funded by lower cost public debt and, at least in part, by a tax on existing privately-owned generation. That is, those who have already invested in Pennsylvania will be rewarded with the privilege of subsidizing their competition.

The real issue is whether an unsubsidized, privately-owned competitive market generator, with its own capital on the line, will be better at selecting generation technology, minimizing construction costs, and maintaining and operating generation plants than will a public entity with artificially cheap funding, assured cost recovery, tax-free status, little or no incentive to contain

costs and maintain efficient operations, and inevitable political pressures governing its actions. With the possible exception of Niagara Falls and the Columbia River being moved to Pennsylvania, I believe experience and common sense overwhelmingly favor private investment and ownership subject to competitive market forces rather than government investment and ownership.

The greatest benefit of the Electric Choice Act was to get all the cost overruns, operational inefficiencies, and bad generation decisions off the backs of captive electric ratepayers. All of those burdens and risks are now borne by private investors. If the plant is poorly operated or does not run, the owner is paid less or nothing; ratepayers do not pay all or most of the costs in any event. Creation of a state power authority would put those burdens and risks back onto ratepayers or taxpayers, or both. Why should the Legislature do such a thing when electric restructuring has resulted in the construction in Pennsylvania of 9,000 megawatts of new, privately-built generation since passage of the Act in 1996? Pennsylvania is a net exporter of electricity and will remain so for the foreseeable future. All Pennsylvania generation competes with all the generators across several states who can economically transmit power to Pennsylvanians (e.g., 11 suppliers from half a dozen states bid successfully to provide PPL Electric Utilities' default supply in 2010). Can anyone seriously contend that a Pennsylvania Power Authority can compete with such expertise and such diverse generation resources?

Finally, I do not believe that the wholesale electric market is perfect, but I do believe that the PJM Interconnection, with its vast experience and multitude of experts, is in a far superior position to incent new transmission and generation investment in Pennsylvania than any newly-created state power authority.

### **A Philadelphia Energy Authority**

If this entity were organized and operated under the same provisions as described in the proposed electric municipal aggregation statute, I would support it. The bill is, however, too broadly worded and unrevealing to judge its merit. It authorizes the creation of a PUC-licensed “electric generation supplier, electricity supplier, broker, arranger, aggregator or marketer of electricity or related services for sale to end-users utilizing the jurisdictional transmission and distribution facilities of an electric distribution company.” Until more is known about its actual purpose and operation, I cannot support it.

Thank you again for your invitation to testify before you today, and I look forward to any questions that you may have.