Committee on Consumer Protection and Professional Licensure
Pennsylvania Senate
Testimony on Senate Bill 1134
Secretary Kathleen A. McGinty
Pennsylvania Department of Environmental Protection
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Chairman Tomlinson, Chairwoman Boscola and members of the Committee: I appreciate the opportunity to appear before you today to discuss about Senate Bill 1134. Senate Bill 1134 recognizes the critical need comprehensively to address looming electricity rate increases and long term energy security for the Commonwealth. While this bill takes important steps to mitigate rate increases after generation rate caps expire, promote energy efficiency and demand response measures, and address how electricity is procured by default service providers, it is lacking in detail and does not go far enough to ensure that Pennsylvania residents are afforded the lowest reasonable electricity rates on a long term basis.

The proposed amendments build upon the foundation laid by SB 1134 and more clearly articulate the steps utilities must take to provide the lowest reasonable electricity rates and to mitigate drastic rate increases after generation rate caps expire.

Energy Procurement by Default Service Providers

How Default Service Providers (DSPs) acquire electricity is of critical importance to millions of consumers. As stated in the Electricity Generation Customer Choice and Competition Act, "The cost of electricity is an important factor in decisions made by businesses concerning locating, expanding and retaining facilities." 66 Pa.C.S. § 2802(6). In addition, "…electric service should be available to all customers on reasonable terms and conditions." 66 Pa.C.S. § 2802(9). It is fundamentally important to all consumers that, electric service should be available at the lowest reasonable rates on a long-term basis.

Unfortunately, the Competition Act is not being implemented in a manner that promotes low, stable rates over time. Instead, default service customers will soon be facing high and unstable electricity prices. This is a result of an overly narrow interpretation of the phrase "prevailing market prices" which discourages long-term contracts in favor or short term and spot market purchases. In addition, current regulations will require quarterly changes in the price default service customers pay for electricity, ensuring that customer prices are unpredictable.

Short-term prices and spot market procurements do not accommodate purchasing strategies that provide the lowest stable rate for reliable electric service. DSPs should acquire electricity through a portfolio of contract lengths and products, including long-term contracts, bilateral contracts short term contracts, spot market purchases, demand side resources and resources needed to comply with the Alternative Energy Portfolio

Standards Act. This portfolio approach will result in reasonable and stable rates for consumers over the long term.

In addition, expressly permitting long-term contracts will promote the construction of new generation resources. These resources provide a clear path to energy security, clean air and water, long-term health benefits to Pennsylvania citizens, and dynamic new businesses with good paying jobs. These facilities need long-term power purchase agreements to securing financing for development.

SB 1134 embraces the fundamental concepts needed to support prices that are as low and stable as possible in the long term. DSP energy purchase would no longer be held to the "prevailing market prices" standard. Instead, DSPs would be required to procure electricity through competitive procurement process that could include a variety of contract lengths - including long-term contracts. However, SB 1134 does not sufficiently address several important aspects of default service and does not provide clear guidelines for the Public Commission to follow. The proposed amendments follow the competitive procurement path laid by SB 1134 but provide greater detail on the standards DSPs must meet and more clearly delineates the role of the Commission.

Specifically, the proposed amendments expressly state that the Commission approved competitive procurement plan must be designed to produce the lowest reasonable rates on a long-term basis. The plan must also provide for mechanisms to comply with the Alternative Energy Portfolio Standards Act and must include a portfolio of contract lengths.

While long-term contracts (5-20 years in length) must be included as part of a procurement plan and are expressly permitted for alternative energy credits and demand side resources, limitations are specified. These limitations include restricting long-term contracts to no more than 20% of the DSP's projected load and prohibiting the Commission from ordering DSPs to purchase electricity from a specific generator or fuel type.

Bilateral contracts could be employed as part of the procurement process - but the proposed amendments remove the ability of the DSP to enter into these contracts "at their sole discretion". If the goal of providing the lowest reasonable rates on a long-term basis is to be achieved, every option should be available and a utility should not be able to avoid this responsibility at its sole discretion. To state this more precisely, it is important for the Commission to retain the ability to find a procurement plan lacking in achieving the 'lowest reasonable rate' test if the plan fails to include one or several of the contracting types provided. If some contracts are relegated to the sole discretion of the DSP, the Commission's ability to act on behalf of ratepayers is unduly and unwisely constrained.

SB 1134 provides no guidance on the process by which DSPs submit procurement plans, what the Commission's duties are or how often plans and default service regulations

should be revised address changing market conditions. The proposed amendments address each of these issues in detail and include the following provisions:

The Commission must promulgate DSP regulations by December 31, 2008 and review such regulations every 5 years.

The Commission must approve a procurement plan within 9 months and must approve contracts within 2 days after bids are selected.

The Commission may reject the results if they produced unreasonably high prices due to abnormal, transient market events.

The DSP must file an updated procurement plan every three years. The Commission will hold hearings as necessary to review the plan and issue findings regarding whether the updated plan is designed to produce the lowest reasonable rates on a long-term basis.

This specificity is important because it avoids costly, time-consuming litigation and rulemaking that would otherwise be necessary to establish these standards. With rate caps expiring in the very near future, time is of the essence.

Finally, the proposed amendments include provisions that ensure low, stable rates across all customer classes. For example, the procurement process must be conducted by rate class and cannot result in cross subsidization; large customers with a peak demand of 7 megawatts (as opposed to the existing floor of 15 megawatts) may receive a negotiated rate from the DSP; and residential and small-business customers are offered a rate that can only be changed on an annual basis as opposed to the Commission's policy of quarterly changes.

Rate Change Mitigation

SB 1134 recognizes that electricity rates will rise dramatically once generation rate caps expire in 2010 and 2011. If rates increase by more than 12%, SB 1134 requires DSPs to offer residential and small business customers using 25kW or less in maximum registered peak load the opportunity to prepay or phase-in the increase over a three year period.

Although the intention is to provide voluntary programs to ease the transition from capped rates, as written, SB 1134's protections would only kick in after utility rates have risen by more than 12%. Because the requirement arises after rates increase, no "prepay" option is possible. In addition, it is not clear whether participation would be on an opt-in or opt-out basis. Finally, the role of the Commission is not addressed - although it is no doubt assumed that the Commission would be able to oversee a utility's mitigation program.

The proposed amendments clarify SB 1134's intent by requiring electric distribution companies to file rate mitigation plans with the PUC within 90 days of the effective date of the Act. At a minimum, EDCs must offer customers the opportunity to opt-in to phase

the rate increase over time. Because the degree to which rates will increase for all EDCs is not known at this time, and will vary from one DSP to the next, the phase-in period is not specified. Instead, the rate increase is capped at 15% in any given year for customers who choose to participate.

In addition, EDCs may also file a plan to provide customers with an opt-in program where customers could prepay generation rate increases prior to rate cap expiration. The prepayment plan would essentially be a savings account receiving 6% interest and if a customer discontinues service, the EDC would refund any unused balance.

The benefits of the proposed amendments are, the plans are proactive, universally applicable and ensure that customers who opt-in to the mitigation programs do not experience a financially devastating rate increase. To underscore, it should be fully the customer's choice whether to opt-in to a prepayment or a post rate cap mitigation plan, and the legislation needs to be explicit on this point. In addition, the role of the Commission in reviewing and approving the mitigation plans is clearly spelled out - as is the EDC's right fairly to recover their costs.

By allowing all customers the choice to participate in these mitigation plans and by ensuring that the transition from capped rates to market rates will occur gradually over time, the proposed amendments provide superior protection for Pennsylvania's electricity customers and ensure a more robust economic future.

Energy Efficiency and Demand Response

SB 1134 requires EDCs to provide cost effective energy efficiency and demand-response measures. By 2013, electricity consumption must be reduced by 2%. If the Commission determines that the benefits of energy conservation measures exceed the costs, it will set additional conservation targets for 2018 and beyond.

SB 1134 also seeks to lower peak load by 3% in the 100 hours of the year when the highest wholesale prices occur from June 1, 2007 through May 31, 2008. The 3% peak load reduction is to be achieved by May 31, 2012. If the Commission determines that the benefits of peak load reduction exceed the costs, it will set additional peak load reduction targets for 2017 and beyond.

Aggressively promoting energy efficiency and demand response measures is essential to providing reliable electric service at reasonable rates. It is also essential for providing a secure energy future for the Commonwealth. SB 1134 recognizes this and takes steps in that direction.

However, a significant drawback to SB 1134 is that electric utilities are afforded a monopoly in the delivery of conservation services. The bill vests the utilities with complete control in administering conservation and demand side reduction programs. Instead, the utilities should have to compete to offer this service and demonstrate that they are delivering the service in the most cost effective manner possible. This is

especially important given the inherent conflict of interest at most utilities where they have an unregulated generation-owing affiliate and a single corporate parent. In addition, the percentage goals may not be a sufficiently aggressive. To address these issues, the energy efficiency and demand response programs should be provided by an entity selected through an open bid process and rewards for superior performance (as well as penalties for failure) should be provided.

HB 31, which is sponsored by Representative Ross, takes this approach and requires an independent program administrator to solicit bids to implement the energy efficiency and demand response programs within each EDC service territory. HB 31 also sets higher efficiency and demand response standards, which will save consumers more money and promote more reliable electric service.

HB 31 proposes to achieve the 2% energy efficiency standard using 2007 as the base year rather than June 1, 2012 - May 31, 2013. HB 31 then sets a firm10.1% peak demand reduction standard for 2020 as opposed to a 3% demand reduction standard for 2012 with the possibility of greater reductions in the future. As with SB 1134, HB 31 requires these programs to pass the total resource cost test. Therefore, more aggressive goals should be pursued because consumers are assured to receive a greater benefit. SB 1134 should be amended to be consistent with HB 31 and provide a combination of aggressive energy efficiency and demand response measures administered by an independent party and implemented by an entity selected through the competitive bid process.

Smart Metering/Real Time Pricing

Smart meters are thought of as an optional part of a conservation package-a tool that might be used to reduce load or other tools could be used instead. That is a mistake. The job and value of smart or advanced metering technology is much more expansive and is fundamental to ensuring electric reliability and low electricity rates.

Smart meters have been shown in Pennsylvania to provide vital operational improvements that lower utility costs while providing a significantly higher quality of service to customers. Smart meters efficiently and frequently record customer consumption. This enables accurate billing. Vastly improved metering accuracy and the ability to remotely check meter operations enable quicker and more satisfactory utility response to customer complaints and billing inquiries. The specific causes of outages can be pinpointed which enables timely dispatch of utility crews to the right point, thus minimizing the amount of time the lights are out. In addition, theft can be identified quickly and accurately so that losses that other customers would have to cover are minimized. Unfortunately this technology is ignored in SB 1134.

The proposed amendments require EDCs to deploy smart meters over a sensible time period and require DSPs to offer time of use and real time pricing to all customers who have smart meters. Both utilities and competitive suppliers of demand side services can provide a variety of options based on the availability of accurate hourly consumption data.

Even if a customer does not choose to participate in these pricing programs, smart meters still provide significant benefits. Smart meters are a more efficient way for utilities to record electricity consumption. Smart meters enable utilities to better respond to power outages. Smart meters enable all customers to more closely monitor their electricity consumption. Therefore, even customers who are receiving a flat rate from the utility will have an incentive to reduce their consumption.

Ultimately, smart meters are much more than a piece of equipment in customer's home or on a utility pole. They are an advanced piece of technology that is part of a larger "smart grid." As transmission and distribution systems age and serve greater loads, the value of smart meters will be more and more apparent. It is critically important that consumers realize that value now rather experience the costs of failing to take this proactive step.

Micro Grids, Low Income and Customer Education

The proposed amendments contain provisions that promote small-scale electricity generation and distribution and small-scale natural gas distribution by expressly exempting micro-grids and natural gas providers who serve 4 or fewer customers from the definition of "public utility". This is simply a codification of current interpretations of what constitutes a public utility and will provide the certainty financial institutions need to fund these projects. Micro-grids have proven to be a vital and successful part of the Commonwealth's strategy to retain and expand manufacturing operations in the state. Landfill gas micro-grids in the southcentral and southwest parts of the state are delivering substantially below market gas to industrial off-takers and are thereby supporting thousands of good jobs. Red tape and lawyers fees currently hamper these projects, however, and so a clarification of the law as provided here is vital to realizing the full potential of these under-developed energy resources.

Finally, because generation rates will increase after rate caps expire, it is important to ensure that the public is well prepared. Consumer education and low income programs will play an important role in assisting Pennsylvania's more vulnerable populations during the transition to market rates. I'd be happy to answer any questions you have at this time.