

**STATE OF CONNECTICUT**

**DEPARTMENT OF PUBLIC UTILITY CONTROL**

DEPARTMENT OF PUBLIC UTILITY : Docket No. 06-01-08  
CONTROL DEVELOPMENT AND :  
REVIEW OF STANDARD SERVICE :  
AND SUPPLIER OF LAST RESORT :  
SERVICE : February 14, 2006

**INITIAL COMMENTS OF RETAIL ENERGY SUPPLY ASSOCIATION**

**I. INTRODUCTION**

The Department of Public Utility Control (the “Department”) has initiated this proceeding pursuant to the mandate of Section 16-244c of the Connecticut General Statutes. That statute continues the progression toward fully competitive retail markets in Connecticut. It requires the Department to perform certain regulatory reviews and approvals to set the stage for the implementation of standard service and supplier of last resort (“SOLR”) service on January 1, 2007. The most crucial task before the Department is the authorization of plans that will guide the utilities’ procurement of power supply and shape the rates for standard service and SOLR customers. These plans – more than any other feature of the future service design – will be the principal determinant of whether Connecticut’s electricity consumers will be allowed to reap the benefits of retail choice and avoid the jarring rate shocks that are inherent in the existing transitional standard offer (“TSO”) regime.

The Retail Energy Supply Association (“RESA”) is a nonprofit organization and trade association that represents the interests of its members in regulatory proceedings in the New

England, New York and Mid-Atlantic regions.<sup>1</sup> RESA's members include providers of competitive supply products to gas and electricity consumers in the five New England states that have restructured their electric markets. RESA therefore has substantial knowledge with respect to the procurement policies adopted by neighboring states and the extent to which they have nurtured or inhibited retail markets in those jurisdictions. RESA is pleased to submit these initial comments to assist the Department as it prepares for its upcoming review of the procurement plans of The Connecticut Light and Power Company ("CL&P") and the United Illuminating Company ("UI").<sup>2</sup>

RESA has been an active participant in Docket No. 05-11-05 in which the Department is conducting a review of the state of retail competition in Connecticut. In its Comments, Brief and Testimony filed in that proceeding, RESA stated that the most critical factor that influences the ability of retail markets to develop and flourish is the design of the utility retail offering (generically labeled "basic service" herein). *See* Docket No. 05-11-05, RESA Comments dated December 13, 2005 at 2; RESA Brief dated January 18, 2006 at 10; Testimony of Thomas Bessette on behalf of RESA at January 9, 2006 public hearing. When long-term wholesale procurements of basic service power supply by utilities mask price signals to which customers should be responding, retail competition will flounder as it has in Connecticut.

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<sup>1</sup> RESA's members include Amerada Hess Corporation; Constellation New Energy, Inc.; Direct Energy Services, LLC; Reliant Energy Solutions; Select Energy, Inc.; Sempra Energy Solutions; Strategic Energy, LLC; SUEZ Energy Resources NA, Inc. and US Energy Savings Corp. The opinions expressed in this filing may not represent the view of all members of RESA.

<sup>2</sup> In the January 25, 2006 Notice of Request for Written Comments ("Notice"), the Department sought input regarding the transparency and the manner of participation of the Office of Consumer Counsel and the Attorney General for the State of Connecticut in the solicitation and review of bids for the power supply of standard service and SOLR service customers. Notice at 1-2. RESA offers no opinions on that topic. The Notice, however, also invited comments on the regulatory processes that will lead to implementation of standard service and SOLR service, which, as the Notice recognizes, include the application of statutory mandates governing pricing and procurement requirements for both service models. *Id.* RESA therefore believes that the comments embodied herein are relevant to the Department's review.

Long-term procurements also exact another terrible price: they expose customers to extraordinary rate hikes like that announced by CL&P in early January 2006 and a much larger increase that likely will inure to customers of UI when its long-term supply contracts expire at this year's end. What's more, because long-term procurements stymie retail competition, customers have nowhere to go to avoid these disruptive price spikes. Similarly, if markets unexpectedly decline during the term of basic service contracts, consumers are deprived of retail products that would enable them to quickly capitalize on the price drop and escape the rigid, one-size-fits all model that underlies Connecticut's present regime.

Unlike the TSO, the bifurcated service model scheduled for 2007 is designed to foster energy choices for electricity customers that prefer a commodity price structure that differs from the utility offerings and – if properly implemented -- will enable customers to effectively manage their energy costs while avoiding jarring rate shocks. Under the new paradigm, only residential customers and small and medium-sized business customers will be allowed to receive standard service. Conn. Gen. Stat. § 16-244c(c)(1)<sup>3</sup> Large customers, by contrast, will be able to procure only SOLR service from a utility, evincing the legislature's clear desire that these customers see and experience current market prices so that they will reach out to the competitive marketplace for more advantageous offerings. *Id.* at (e)(1)<sup>4</sup> The statute further requires that utilities purchase power supply for both standard service and SOLR customers in a manner that will allow the respective service rates to reflect accurate market signals as appropriate for the class. *Id.* at §§

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<sup>3</sup> This limitation is embodied in Conn. Gen. Stat. § 16-244c(c)(1), which states: "On and after January 1, 2007, each electric distribution company shall provide electric generation services through standard service to any customer who (A) does not arrange for or is not receiving electric generation services from an electric supplier, and (B) does not use a demand meter or has a maximum demand of less than five hundred kilowatts."

<sup>4</sup> With respect to SOLR, the statute states in pertinent part: "On and after January 1, 2007, an electric distribution company shall serve customers that are not eligible to receive standard service pursuant to subsection (c) of this Section as the supplier of last resort."

(c)(3) & (e)(2). To that end, the statute states that SOLR service should be priced on a monthly basis, while standard service should be priced not more frequently than every calendar quarter.

*Id.* at §§ (c)(2) & (e)(2).

## **II. THE STATUTORY DESIGN OF STANDARD SERVICE AND SOLR SERVICE REQUIRES SHORTER-TERM PROCUREMENTS TO FOSTER RETAIL COMPETITION**

Every state that has developed a vibrant retail market subscribes to the theory that basic service rates must reflect timely price signals from wholesale markets. That goal is most commonly attained by procuring basic service power supply through contracts with relatively short durations. Maine, for example, solicits proposals for its medium and large basic service customers every six months, and it has developed one of the most thriving retail markets in the nation.<sup>5</sup> Massachusetts has adopted a three-month procurement cycle for its medium and large customers and retail competition dominates in the Commonwealth too.<sup>6</sup> Both Maine and Massachusetts provide for monthly pricing of basic service within the three and six-month procurement terms of their wholesale supply contracts.

The Connecticut legislature wisely recognized the importance of timely price signals in fostering retail choice when it fashioned the new bifurcated service model nearly three years ago. In fact, it created a clear roadmap to guide the Department in achieving that goal through the

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<sup>5</sup> Maine's power supply solicitations and customer switching statistics are available on the Maine Public Utility Commission web site at <http://www.me.us/mpuc.html>. As of January 1, 2006, between 53 percent and 90 percent (depending upon the service territory) of Maine's large customer load had migrated to competitive supply. The comparable numbers for medium customers are 33 percent to 46 percent. *Id.* Thus, in Maine, customers are not so readily poised to "blame" regulators if or when utility rates spike upward because, unlike in Connecticut, Maine businesses can turn to the retail market for products that avoid such a result.

<sup>6</sup> The Massachusetts Department of Telecommunications ("D.T.E.") most recently articulated its procurement policies in D.T.E. 02-40-C, *Investigation by the [D.T.E.] on its Own Motion into the Provision of Default Service* (2002) at 22. The Commonwealth's customer migration statistics are posted on the D.T.E. web site at <http://www.mass.gov/dte/restruct/competition/index.htm>.

adoption of plans that limit terms of supply contracts for both standard service and SOLR customers.

**A. Standard Service Supply Should be Procured Through Overlapping Six-Month Contracts Consistent With the Statute**

In its design of the standard service model, the legislature directed the Department to establish the standard service price on October 1, 2006 and periodically thereafter, “but not more often than every calendar quarter.” Conn. Gen. Stat. § 16-244c(c)(2). It also articulated substantial guidance with respect to the procurement of default service supply:

An electric distribution company providing electric generation services pursuant to this subsection shall mitigate the variation of price of the service offered to its customers by procuring electric generation services contracts in the manner prescribed in a plan approved by the department . . . . Such plan shall require that the portfolio of service contracts be procured in an overlapping pattern of fixed periods at such time and in such manner and duration as the department determines to be most likely to produce just, reasonable and reasonably stable rates *while reflecting underlying wholesale prices over time*. The portfolio of contracts shall be assembled in such manner as to invite competition; guard against favoritism, improvidence, extravagance, fraud and corruption; and secure a reliable electricity supply while avoiding unusual, anomalous or excessive pricing. *The portfolio of contracts procured under such plan shall be for terms of not less than six months*, provided contracts for shorter periods may be procured under such conditions as the department shall prescribe to (A) ensure the lowest rates possible for end-use customers; (B) ensure reliable service under extraordinary circumstances; and (C) ensure the prudent management of the contract portfolio.

*Id.* at § (c)(3) (emphasis added). This statutory provision makes clear that the legislature intended to balance the competing goal of price stability with the desire to promote retail competition for the small and medium customer classes. It sought to attain that balance by providing that supply contracts should generally have terms of at least six months and be solicited in an overlapping pattern. Although the statute affords the Department discretion to

authorize supply contracts for terms greater than six months, such an approach would undermine the overarching legislative goal of fostering retail choice by compromising the requirement that rates reflect the “underlying wholesale price.” *Id.* Longer-term procurements would also expose customers to further rate shocks as standard service inevitably returns to market levels, could compromise participation in conservation measures, as further discussed below, and could lead wholesale suppliers to include expensive risk premiums in bids. In light of these facts, RESA recommends that the terms of standard service wholesale supply contracts be limited to six months and that the standard service price be reset every calendar quarter.

**B. SOLR Power Supply Should Ideally be Procured on a Monthly Cycle Consistent with the Statute**

The SOLR design embraced by the legislature envisions even timelier price signals than that articulated for standard service. The statute reads: “The Department shall determine a price for [SOLR] customers that reflects the full cost of providing the electricity on a monthly basis.” *Id.* at § (e)(2). Thus, it is clear that the legislature envisioned frequent procurements of SOLR power supply and thought that SOLR should have a two-fold purpose consistent with that articulated by the Massachusetts Department of Telecommunications and Energy (“D.T.E”) for the Commonwealth’s large customers: (1) to provide a service that is invoked only in situations of emergency or special circumstances; and (2) to foster incentives for such customers to turn to the competitive market for more sophisticated and advantageous offerings. Docket No. 02-40-B, *Investigation by the [D.T.E.] on its own Motion into the Provision of Default Service* (2002) at 37.

In order to advance these twin goals, RESA recommends that the Department require monthly procurements of SOLR service, which dovetails with the statutory mandate that SOLR prices be refreshed on a “monthly basis.” Conn. Gen. Stat. § 16-244c(e)(2). In the event the

Department concludes that monthly procurements are not administratively feasible in the near term, RESA suggests that the Department require quarterly procurements of SOLR power supply, consistent with the highly successful Massachusetts model. Not only will monthly or quarterly procurements spawn retail competition, they also may have the ancillary effect of lowering the price of SOLR service because they will alleviate the need for wholesale suppliers to incorporate risk premiums into their bids to cover longer-term uncertainties of load and price volatility as the state's large consumers migrate toward competitive supply.

### **C. Long-Term Procurements are Not Good for Customers**

At the January 9, 2006 public hearing in Docket No. 05-11-05 (the "January 9 hearing"), Connecticut's investor-owned electric utilities touted the merits of long-term procurements, arguing that they were good for customers. UI, in particular, claimed that the existing TSO paradigm has allowed the utilities to enter into favorable long-term supply contracts when the market appears to be at a low point, thereby saving customers millions of dollars. RESA urges the Department not to be swayed by that earlier argument because it is short-sighted and inconsistent with the statutory mandate.

Although, in hindsight, UI's last procurement cycle created prices that were temporarily below market, that result was based largely on good fortune. UI could just have easily guessed wrong. Because the utilities are not clairvoyant, attempting to lock into contracts whenever they perceive that the market is at a low point is not the way to achieve the lowest possible energy prices. That goal should be attained by developing a competitive retail market that will consistently provide choice and favorable prices over the long term.

At the January 9 hearing, Mr. Michael Coretto testified that bringing the standard offer of UI to then-current market levels would *double* the generation component of UI's rates. Surely,

any structure that creates the potential for rate hikes of this magnitude and deprives customers of retail choice at precisely the same time when they could be forced to swallow a doubling of their generation charges cannot be a sound model. Long-term supply contracts can be equally problematic in a declining market. If the market drops unexpectedly during the term of basic service contracts, customers will not be allowed to timely capture the benefits of lower prices because long-term contracts prevent retail markets from developing. Hence, customers will be locked into the rigid, one-size-fits-all utility model until the long-term contracts expire.

As the Department proceeds with the implementation of both SOLR and standard service, it is crucial that it recognize the value of retail choice. As Mr. Bessette explained at the January 9 hearing, all electricity consumers do not think alike. RESA members can offer Connecticut businesses literally hundreds of products that can be tailored to meet their particular needs for budget certainty and flexibility and their tolerance for risk. By contrast, the existing TSO offers virtually no choice, exposes customers to the risk of unacceptable rate shocks in rising markets, and precludes them from escaping high energy prices in declining markets. In the end, however, long-term procurements, particularly for SOLR service, must be rejected on legal grounds because they cannot be squared with the statutory requirements discussed in the preceding sections.

**D. CL&P Agrees That the Statute Requires Shorter-Term Procurements of Standard Service and SOLR Service Wholesale Power Supply**

On October 3, 2005, CL&P filed an application in Docket No. 05-10-03 to implement time-of-use, interruptible or load response, and seasonal rates (the “Application”) as required by the Energy Independence Act (the “Act”).<sup>7</sup> In that application, CL&P properly acknowledged that the standard service and SOLR statutes require more frequent pricing and procurement of power

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<sup>7</sup> Public Act 05-01 (June Special Session).

