

STATE OF CONNECTICUT

DEPARTMENT OF PUBLIC UTILITY CONTROL

DEPARTMENT OF PUBLIC UTILITY : Docket No. 05-11-05
CONTROL REPORT ON THE STATE :
OF RETAIL ELECTRIC COMPETITION : February 16, 2006

WRITTEN EXCEPTIONS OF RETAIL ENERGY SUPPLY ASSOCIATION

The Retail Energy Supply Association (“RESA”) offers these written exceptions to the Department’s February 10, 2006 Draft Decision to assist the Department in making its final decision a useful document to frame the discussion of evolving retail markets in Connecticut. The Draft Decision falls short of this goal both because it ignores the fact that there is no one universal “best price” for our state’s diverse electricity consumers and because it misses several other fundamental points about electric markets.

I. THE DRAFT DECISION INCORRECTLY ASSUMES THAT THERE IS A UNIVERSAL BEST PRICING MODEL AND PLACES NO VALUE ON RETAIL CHOICE

As it pertains to retail competition, the Draft Decision makes a fundamental error that pervades much of the document: it presumes that there is one best pricing model for every electricity consumer – that is, a long-term, fixed price option like that provided by the transitional standard offer (“TSO”). The Draft Decision then questions the value of competitive retail markets to customers because retail suppliers have not demonstrated that they can beat the TSO price. The Draft Decision views the state’s role in structuring energy markets as seeking the market model that can deliver that lowest price.

This perspective ignores the fact that consumers have a wide range of preferences for electricity pricing models that differ from the “one-size-fits-all” TSO construct. Some seek fixed

prices and are willing to pay a premium for them. Others can tolerate volatility if it means a lower overall price. Still others seek multi-year contracts. The key question, therefore, in evaluating the benefits of retail competition is not whether competitive suppliers can beat the utility price; rather, it is whether customers can benefit from a broad array of innovative retail products that will enable them to manage their energy costs in a way that best fits their needs – whether business or personal. Until the Department acknowledges this fundamental point and recognizes the extraordinary value of retail choice, no full and fair deliberations about retail competition in Connecticut are likely.

In the Draft Decision, the Department first posits that the “business mode” of retail suppliers is to “[provide] savings to customers by procuring power in the wholesale market at lower cost than the utilities.” Draft Decision at 18. The Department then states that retail suppliers have been unable to match the utility generation prices because (1) they do not have a sufficient customer load, and (2) problems in the wholesale market render suppliers unable to compete with the TSO generation service. *Id.* at 20, 25. Thus, the Department reports, only a miniscule percentage of Connecticut consumers have migrated to competitive supply. *Id.* at 24. Although the Department recognizes that shorter-term wholesale supply contracts for utility offerings could spawn retail competition, it questions whether the end result would yield material benefits to customers. *Id.* at 19-20. In particular, the Draft Decision states:

The Department is concerned that competition may deteriorate into merely a timing game. If the TSO pricing is changed more frequently, it is uncertain whether suppliers will actually offer long term fixed options. Instead, shorter term TSO pricing could result in shorter term supplier offerings. This could result in more price volatility for consumers. If this scenario occurs, more customers might switch to retail suppliers; however, there could be negligible resulting benefit. If all suppliers are procuring the same generation, they would basically be competing with one another via measures to reduce their

administrative costs. This would provide inconsequential potential benefits to electric customers.

Id. at 19.

This reasoning is unsound for several reasons. First, it improperly assumes that all electricity customers want the same thing – long-term, fixed-priced contracts with low volatility. Second, it places no value on retail choice and fails to consider that retail suppliers routinely offer consumers long-term, fixed-price contracts within their broad suite of products. Third, it does not recognize that the new standard service and supplier of last resort (“SOLR”) service models, if properly implemented, will quickly spur retail competition. Finally, it completely ignores the experiences of neighboring states that have developed thriving retail markets.

A. There is no Single Best Pricing Model for all Customers

Connecticut, like Massachusetts, Maine and other states with vibrant retail markets, has an eclectic mix of businesses that vary dramatically in terms of energy consumption, financial resources, tolerance for risk and need for budget certainty and flexibility. These variations lead businesses to have a broad range of preferences with respect to the optimal pricing structure of electricity products. Put simply, all business electricity consumers do not think alike.

For example, RESA members have learned from their vast marketing experiences that some large commercial and industrial (“C&I”) customers that have a high tolerance for risk and a need for business flexibility, coupled with the financial means to sustain fluctuations in energy costs, *often prefer* real-time pricing or short-term retail contracts, believing that such products will offer the lowest possible energy costs (because of the absence of any risk premium). Conversely, some other customers prefer fixed-priced contracts for extended periods. Other retail customers fall in between these two extremes. They purchase a broad array of retail

products that seek to obtain what the customers perceive to be the optimal balance between volatility and the lowest possible energy costs. This real world experience of RESA members demonstrates that the Draft Decision's implicit assertion that fixed pricing is the only proper pricing model for all customers is inconsistent with the actual choices made by customers in New York, Massachusetts and Maine.

Based on the marketing experiences of its members, RESA maintains that the Department's attempt to measure the potential success of retail markets based on whether retail suppliers can beat the utility offering price misses the mark because it fails to recognize that there is no best pricing model for all electricity consumers. It presumes, moreover, that the Department knows what is best for all electricity consumers, rather than allowing individual customers to make that decision themselves. What's more, it does not comprehend the value that retail choice can bring to Connecticut consumers.

B. Retail Suppliers Can Offer A Broad Range of Products Including Long-Term Contracts

Competitive retail suppliers can offer Connecticut businesses an incredible array of retail products as an alternative to utility offerings. Indeed, the Department acknowledges that point in the Draft Decision:

The Retail Energy Supply Association (RESA) states that its members can offer C&I customers literally hundreds of products including, among others, fixed price products for various terms, real-time products, block products and green products, all of which can be tailored to meet a customer's particular risk tolerance and need for flexibility and budget certainty. RESA brief at 8.

Id. at 17. The Department, however, does not evaluate how retail choice could bring substantial benefits to business customers by offering innovative solutions to rising energy costs or fostering participation in demand response programs and other conservation measures. Rather, the

Department speculates that retail competition can actually harm customers because it may dampen the availability of long-term, fixed-priced contracts. *Id.* at 20.

Although RESA rejects the view that all customers desire such a fixed-priced model for the reasons set forth above, the record evidence in this case suggests that the Department's concerns are wholly unsubstantiated. RESA testified at the January 9 public hearing that its members routinely offer a broad range of products, including long-term, fixed-price contracts, to customers in Maine, Massachusetts and other states with robust retail markets. RESA members stand poised to offer such contracts to Connecticut consumers, too, if that is what they want.

On January 20, 2006, Constellation New Energy, Inc. ("Constellation") filed a letter in this proceeding (the "Constellation letter"), stating that it already had entered into multi-year contracts with large Connecticut electricity consumers in anticipation of the transition to standard service and supplier of last resort ("SOLR") service on January 1, 2007. These include an agreement with Connecticut Consortium Cooperative Purchasing to provide 70 megawatts of energy to 65 schools and municipalities for multi-year, fixed-priced contracts beginning January 1, 2007, as well as an agreement with the Manufacturers Alliance of Connecticut to provide 16 megawatts of energy to 33 manufacturing companies for multi-year, fixed-price contracts also commencing on January 1, 2007. Thus, there is no evidence to support the notion that retail competition will harm customers by depriving them of the availability of long-term, fixed-price contracts. In fact, the only record evidence on this point directly contradicts the unsupported statement in the Draft Decision.¹

¹ There also is no evidence to support the Department's related assertion that "Suppliers will not commit to long-term contracts with generators because their load is small and it is uncertain how many customers they will have in the future." Draft Decision at 24. Irrespective of the contracting relationships of retail and wholesale suppliers, the record unequivocally demonstrates that retail suppliers routinely enter into long-term, fixed-price contracts with their customers, including those located in Connecticut. See Constellation letter.

C. The New Service Models Scheduled for 2007 Will Spur Competition

The Draft Decision is dedicated largely to the present state of retail competition in Connecticut and observes that “currently there is very little incentive for customers to switch to a competitive supplier” under the TSO regime. *Id.* at 24. The Department does state, however, that the new standard service and SOLR service models that are scheduled for 2007 will reveal whether retail suppliers can compete in Connecticut and “bring real benefits to Connecticut ratepayers.” Draft Decision at 21. The Draft Decision, however, fails to acknowledge that this new statutory regime *already* has allowed competition to gain traction in Connecticut for the very first time, as evidenced by the contracts described in the Constellation letter. RESA urges the Department to incorporate that point into its Final Decision and note that the reason Connecticut consumers are contracting with retail suppliers now is that SOLR will finally be structured properly on January 1, 2007 to be a short-term, market-priced service of last resort. In light of this demonstrated progress, RESA further urges the Department to explicitly recommend that the legislature stay the course toward the adoption of standard service and SOLR models so that retail competition will have the opportunity to flourish in Connecticut, as it has in Maine, Massachusetts, New York and other jurisdictions.

D. The Department Should Recognize the Positive Retail Experiences of Neighboring States in its Final Report

The standard service and SOLR service designs scheduled for 2007, if properly implemented, will resemble the basic service models embraced by Massachusetts, Maine and other neighboring states. In light of that fact, RESA finds it perplexing that the Draft Decision makes no mention of the positive retail marketing experiences of those jurisdictions. For example, in Massachusetts, nearly 43 percent of the customer load is served by competitive

suppliers.² The comparable number in Maine is 39 percent for all customers, with 53 percent to 90 percent of the large customer load on competitive supply across Maine's three largest service territories.³ RESA believes that these impressive statistics would be highly relevant to the legislature particularly since they were achieved (1) within the context of basic service models that resemble Connecticut's 2007 statutory regime, and (2) in the face of the very same purported wholesale market problems in New England ISO that the Department believes hinder retail competition. *See* Draft Decision at 24. RESA urges the Department to address the positive retail experiences of other states because they demonstrate that retail competition can succeed in Connecticut and that customers place a high value on retail choice.

II. RESA RESPECTFULLY REQUESTS THAT THE DEPARTMENT MODIFY CERTAIN PARTS OF THE DRAFT DECISION

In RESA's review of the Draft decision, it noted several points that would benefit from clarification or modification as recommended below.

"Prices are higher than they would be under regulation." The Department writes, on page 14, of the Decision that "[p]rices are higher today than they would have been under regulation." There is absolutely no evidence in the record to support that bald assertion. Indeed, the evidence of record, namely, studies conducted by ISO New England, Inc., Cambridge Energy Research Associates, Inc. and Global Energy Systems, Inc., which were cited by RESA in its brief, overwhelmingly supports the opposite conclusion. RESA therefore requests that the Department eliminate that speculative assertion.

"Deregulation has compromised fuel diversity." The Draft Decision also states that deregulation has compromised fuel diversity because the current marginal pricing system treats

² *See* Customer Switching Data at <http://www.mass.gov/dte/restruct/competition/index.htm>.

³ *See* Customer Migration Statistics at <http://www.state.me.mpuc/industries/electricity/index.html>.

all generators identically and, therefore, they naturally gravitate towards natural gas as the fuel of choice. *Id.* at 15. The Department further posits that, even if fuel diversity could be enhanced in the deregulated arena, it will “exert insignificant price benefits as long as gas units are on the margin and set the price.” *Id.* What the Decision fails to recognize, however, is that fuel diversity can be readily obtained by adhering to the requirements of Section 12(c) of the Energy Independence Act.⁴ That section requires the Department to “encourage diversity in the fuel mix used in generation” when awarding long-term capacity contracts. Furthermore, generators and utilities can contract for the energy output of these projects in a way that will allow ratepayers to reap the benefits of fuel diversity.

“TSO Prices are Artificial.” Page 19 of the Draft Decision states:

Suppliers claim that the TSO generation prices are artificial, that these prices do not reflect current market prices. These prices, however, are not artificial. While the procurement and pricing period may be longer term than suppliers would prefer, it is unfair to characterize the pricing as artificial. Generation service is competitively bid and the full cost is reflected in rates.”

To clarify, RESA does not claim that the TSO price is artificial in the sense that it does not reflect the actual cost of the wholesale supply at the time it was bid. Rather, RESA has consistently maintained that the TSO rates do not provide timely and accurate market signals, which is a crucial feature for any successful retail environment. This distinction is subtle but crucial.

“Suppliers Want Extended Notice of TSO Contracts.” The Decision maintains that “Suppliers recommend that the TSO contracts be approved several months in advance of implementation to allow suppliers time to arrange contracting.” *Id.* at 20. Although it is true that Dominion indicated that the short notice of the results of CL&P’s most recent TSO

⁴ Public Act 05-01 (June Special Session)

