TESTIMONY OF THE RETAIL ENERGY SUPPLY ASSOCIATION

BEFORE THE

PENNSYLVANIA HOUSE CONSUMER AFFAIRS COMMITTEE

February 5, 2009

Good morning Chairman Preston, Chairman Godshall and members of the Committee.

My name is Richard Hudson and I'm the Pennsylvania Chairman of the Retail Energy Supply Association (RESA). RESA is a trade association of competitive electricity suppliers serving residential, commercial and industrial and institutional customers in the Commonwealth and in other states that have enacted retail choice. [1]

Since there are several new members on the Committee, I'd like to start by briefly describing the retail electricity business that our members compete in. Historically, customers had no choice in their electricity supplier. They were captive to the local utility company which was a monopoly that generated, transmitted and delivered the electricity that everyone used. After the Electric Choice Act was passed in 1996, the generation side of the electricity industry became competitive, or as some people say, was deregulated. Today, the local utility still operates the transmission and distribution lines, but separate, competitive generation companies generate the power that is delivered. Power is bought and sold at the wholesale level in organized electric markets and through one on one contractual agreement between buyers and sellers. At the retail level, customers can shop around and choose their electricity supplier. However, the utility still has the obligation to provide backstop (default) generation service to customers that cannot or choose not to take service from a competitive retail provider.

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[1] RESA's members include Commerce Energy, Inc; Consolidated Edison Solutions, Inc; Direct Energy Services, LLC; Gexa Energy; Hess Corporation; Integrys Energy Services, Inc.; Liberty Power Corp.; Reliant Energy Retail Services, LLC; Sempra Energy Solutions; SUEZ Energy Resources NA, Inc. and US Energy Savings Corp. The comments expressed in this testimony represent the position of RESA as an organization but may not represent the views of any particular member of RESA.

The utilities procure the supply needed to provide this “default servie” from the competitive market. The companies that I represent are competitive retail suppliers, meaning that we compete against the utility and against each other to attract customers. Many of our members already serve customers in parts of Pennsylvania where rate caps have already expired.

Next I’d like to talk a little about what has already happened in Pennsylvania with the transition to competition. You may have read articles or other reports that claim that competition has failed or is non-existent. Quite frankly, this is simply not true. Competition at the retail level has not developed in many parts of Pennsylvania because of rate caps that were put in place over a decade ago that have kept prices at below market levels which prevents competitors from offering service. However, there are some examples of how competition is indeed already working for the benefit of the Commonwealth:

- Rate caps have already expired for three major utilities and competitive suppliers are serving customers in those service territories
    - 22 percent of Duquesne’s, and 12% of Penn Power’s residential customers are served by competitive suppliers
    - Over 90% of large commercial and industrial load in both Duquesne and Penn Power is served by competitive providers
    - In Pike County, residential customers have three generation supply options (the default rate, a competitive retail aggregation option, and a fixed price rate from a competitive supplier)
- Retail competition is delivering savings to Pennsylvania customers
    - A RESA member company that has been working with Western Pennsylvania schools since 1997 estimates over $30 million in savings—money that can be reinvested in the classroom instead of going to electric bills.
    - Last year, the City of Pittsburgh and Allegheny County created an energy-buying consortium with other area organizations and chose a competitive supplier to save an estimated $1.4 million (as reported in the Pittsburgh Business Times in February).
- Retail competition is promoting alternative energy, energy efficiency and conservation
    - Last year, a RESA member company recently helped Duquesne University go 100% green through the purchase of renewable energy credits associated with energy from non-depleting sources like wind, hydropower, and solar – an option simply not available through most electric utilities.
    - Competitive markets provide customers with the price signals and economic incentive to reduce consumption and demand and invest in energy efficiency. For example, a recent study found in Texas average residential customer consumption fell by 10% from 1998-2006. Texas is widely considered to have the most successful competitive retail market.

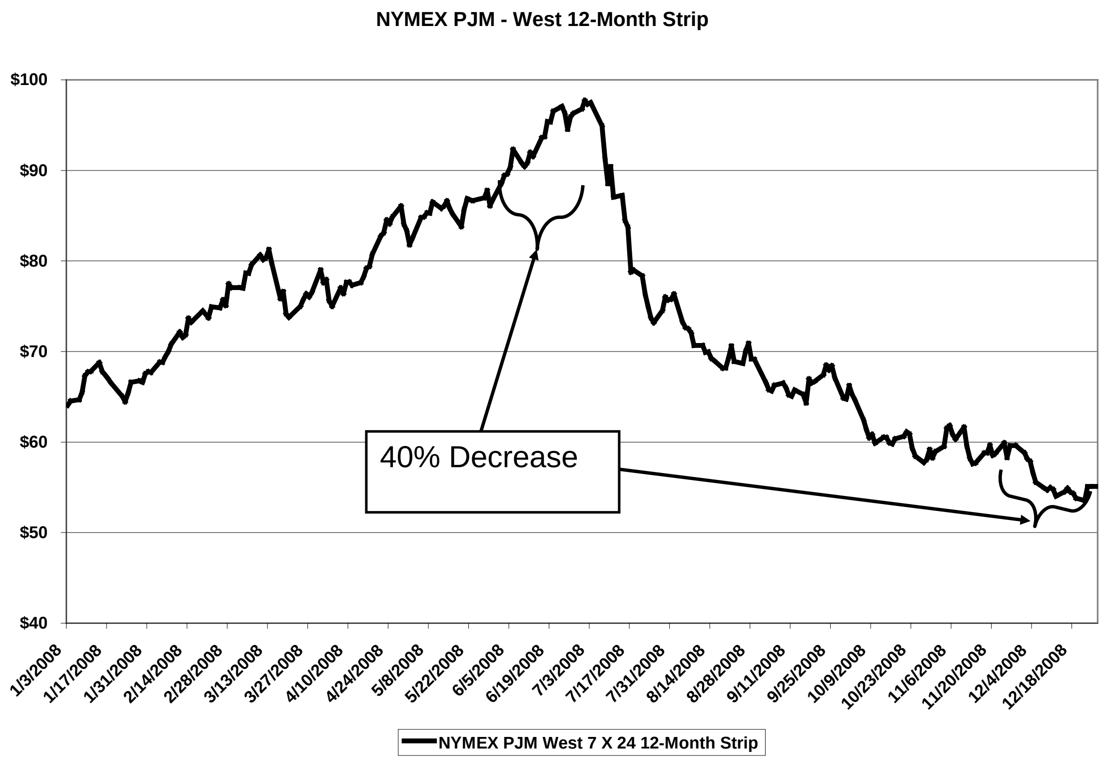
Now, turning to the more complex and controversial issue of electricity prices. Over the last two years, I have testified several times before this and other Committees. Those previous times, the news about electricity prices wasn't good—we were seeing continually escalating prices driven by continually rising fuel costs. Today, the story is different--fuel prices are falling and market prices for electricity are falling. This turn of events doesn't change what, in our opinion, constitutes smart energy policy. Competition and customer choice is the best policy regardless of whether market prices are rising or falling. However, it is important reexamine the situation with this new reality in mind.

You've likely heard the claims that competition has failed because customers may face skyrocketing rate increases as rate caps expire. These claims were unfounded when prices were rising, and are even more inaccurate now. Last year, the Commission began publishing quarterly estimates of post-rate cap price increases. The Commission's analysis compares the current capped rates to current market prices. Because market prices change, the Commission has updated this analysis each quarter based on new market price information.

RESIDENTIAL RATE INCREASES						
	MetEd	PECO	Penelec	PPL	West Penn	Average
12/30/2008	36.9%	1.0%	29.3%	22.8%	36.0%	25.2%

The most recent results for residential customers range from practically no increase (1% in the case of PECO) to a 37% increase for MetEd and West Penn. Now, wait a minute, you might be saying, this still shows a rate increase for most utilities. That is true. However, you must put this in context. Rates have been capped for over a decade. So, even after years of inflationary pressure and dramatic increases in production and fuel costs, post-rate cap increases based on today's market prices are in the 1-37% range. Let's contrast this with price increases for the last ten years for several other everyday products: eggs --90%, ground beef—66%, bread—52%, potatoes—49%.

The recent decline in electricity prices also raises another point worth considering. Over the last couple of years there has been a lot of discussion about long-term contracts. Act 129, which was passed last fall, modified the procurement standard to allow the PUC to consider the use of long-term contracts as part of a supply portfolio. The recent dramatic decline in prices demonstrates the risks associated with long-term contracts. When prices are rising, just as they were in the first half of 2008, it may be very tempting for a utility to lock in prices in the hope of avoiding continued increases. But, as we've seen in the last few months, market price trends can and do change. For example, as seen in this chart, prices dropped by around 40% from June to December. If a long-term contract had been purchased in June, customers would be locked into prices much higher than current market prices.



Now, turning to my final point. Although the magnitude of rate increases may be less than previously expected, we do recognize the need to help customers manage the transition from capped rates to market based rates. As you know there was considerable debate about various rate mitigation options last year. RESA continues to support properly structured policies that will help customers manage expected rate increases. But it is critical that any form of rate mitigation be structured in a competitively neutral manner. This means that customers should receive the rate mitigation or be allowed to participate in the phase-in plan regardless of whether they choose to take the utility's default service or whether they choose service from a competitive supplier. This is a win-win for customers because they receive the benefit of the phase-in or pre-payment plan and can take advantage of potentially lower prices from a competitive supplier. Attached to my testimony is additional information on this issue.

Thank you for the opportunity to testify and I'm available for any questions.