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VIA EMAIL (luly.massaro@puc.ri.gov) and
FEDERAL EXPRESS

May 1, 2017

Division Clerk
Rhode Island Division of Public Utilities and Carriers
89 Jefferson Boulevard
Warwick, RI 02888

Re: D-16-113 Rulemaking To Establish Nonregulated Power Producer Evidence Of Financial Security - Comments of Retail Energy Supply Association

Dear Sir or Madam:

Enclosed please find Comments of Retail Energy Supply Association ("RESA") regarding the above-captioned Proposed Rulemaking.

If there are any questions regarding this matter, or if any additional information is required, please contact undersigned counsel.

Sincerely,

Robert J. Munnelly, Jr.

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STATE OF RHODE ISLAND

DIVISION OF PUBLIC UTILITIES AND CARRIERS

RULEMAKING TO ESTABLISH NONREGULATED POWER PRODUCER EVIDENCE OF FINANCIAL SECURITY	D-16-113

COMMENTS OF THE RETAIL ENERGY SUPPLY ASSOCIATION ON PROPOSED RULE AMENDMENTS ADDRESSING FINANCIAL SECURITY REQUIREMENTS OF NONREGULATED POWER PRODUCERS

Introduction and Summary of Comments

The Retail Energy Supply Association ("RESA")[1] offers the following comments on behalf of its members concerning proposed amendments to the 815-RICR-40-05-1 Regulations for Nonregulated Powers ("NPPs" or "suppliers") to establish new financial security requirements ("Draft Financial Security Rules"). The Division of Public Utilities and Carriers ("Division") circulated the Draft Financial Security Rules and an accompanying Public Notice of Proposed Rulemaking on March 28, 2017. The Division, through its hearing officer, conducted an April 20, 2017 hearing at which undersigned counsel and Mr. Marc Hanks, Senior Manager of Corporate and Regulatory Affairs of RESA member Direct Energy, attended and offered public comment. Division Advocacy Staff and Mr. Andy Mitrey, President of Archer Energy, also provided public comment at the April 20 hearing.

[1] The comments expressed in this filing represent the position of the Retail Energy Supply Association (RESA) as an organization but may not represent the views of any particular member of the Association. Founded in 1990, RESA is a broad and diverse group of more than twenty retail energy suppliers dedicated to promoting efficient, sustainable and customer-oriented competitive retail energy markets. RESA members operate throughout the United States delivering value-added electricity and natural gas service at retail to residential, commercial and industrial energy customers. More information on RESA can be found at www.resausa.org.

RESA commends the Division for its thoughtful efforts to implement a recent statutory directive to establish a financial security requirement for NPPs within a range of between $25,000 and $500,000. See Rhode Island General Laws ("RIGL") chapter 39-1-27.1(c)(9) (as amended in 2016). The Division informally consulted with certain NPPs, prepared a cost-benefit analysis, and commissioned an April 14, 2017 memorandum from Daymark Energy Advisors entitled "Financial Surety Development Process Summary" ("Daymark Memorandum") that initially proposed a two-step security of $250,000 or $500,000 based on annual sales volumes (with the higher security applicable to suppliers with greater than 100,000 MWh in annual sales) and later settled on a single security amount for all NPPs of $250,000. The single security of $250,000 that could be maintained using any of three financial instruments, plus an alternative option of a corporate guarantee for a supplier with not less than $10 million in "investment-grade" assets, are proposed in the instant rulemaking. See Draft Financial Security Rules at section 1.3A(9) (Evidence of Financial Soundness). Section 1.3A(9), as proposed to be amended, would read in full as follows:

9. Evidence of financial soundness:

   a. Evidence of financial soundness such as surety bonds, a recent financial statement, or other mechanism as specified by the Division, except those nonregulated power producers who may be obligated entities shall provide financial security showing evidence of liquid funds, such as:

      (1) a surety bond;

      (2) a certificate of deposit;

      (3) an irrevocable standby letter of credit from an ISO New England Eligible Letter of Credit Bank, a New York Mercantile Exchange ("NYMEX") or a Chicago Mercantile Exchange ("CME") approved letter of credit bank, or;

(4) a corporate guarantee from an investment-grade entity with a Tangible Net Worth of at least ten million dollars ($10,000,000.00).

The financial security shall be in an amount of not less than two hundred fifty thousand dollars ($250,000.00). All financial security provided in satisfaction of this provision shall name the Commission and the Division as obligees;

b. Financial security shall be reviewed each year at the time a nonregulated power producer makes its annual filing. The above notwithstanding, each obligated entity is responsible for informing the Division in writing within five (5) business days of any material adverse change in its financial status. The financial security shall be available to satisfy penalties assessed by the Division for violations of any consumer protection rules or laws related to nonregulated power producers, refunds ordered by the Division, or failure to comply with the provisions of R.I. Gen. Laws Chapter 39-26 as determined by the Public Utilities Commission. Payments made pursuant to this subsection for violation of the provisions of R.I. Gen. Laws § 39-26-4 shall be forfeited, and shall be remitted to the renewable energy development fund established in R.I. Gen. Laws § 39-26-7, or any successor funds, and all other forfeitures will be remitted to the state's general fund; and

c. All financial security provided in satisfaction of this provision, in addition to naming both the Commission and the Division as obligees, shall meet the language and form requirements of the Commission and Division as such direction may be provided from time to time.

For the reasons discussed below, RESA supports the thoughtful and flexible approach of allowing four different mechanisms for establishing statutory financial security requirements that are well below the permitted $500,000 statutory maximum. Nevertheless, RESA recommends the following proposed two options for consideration by the Division: 1.) reduce the proposed fixed financial security amount of two hundred fifty thousand dollars ($250,000) to a fixed one hundred thousand dollars ($100,000) amount as an incremental step to institute this requirement. This simplified approach meets the statutory requirements while reducing the associated administrative burdens for both the Division and NPPs alike. Should the Division determine the

proposed $100,000 financial security amount is insufficient, it retains the right to re-evaluate and amend the regulations to increase the amount within the statutory limits in the future; or 2.) eliminate the proposed fixed amount of financial security in the amount of $250,000 and replaced it by a sliding scale approach for NPP financial security of between $100,000 and $250,000. RESA notes that a similar incremental or reduced security approach to establishing financial security requirements has been adopted in many of the smaller restructured states comparable to Rhode Island's market size, including Delaware, District of Columbia, Maine and New Hampshire. These two approaches also account for needs and risks associated with smaller NPPs and will encourage, rather than impede, new market entrants. Larger NPPs (or those not interested in pursuing an annual filing to justify a reduced bond amount) would retain the option of maintaining the maximum $250,000 security.

This more reasonable approach to financial security, acting in conjunction with the establishment of reasonable consumer protection rules in the ongoing Docket No. D-16-112 rulemaking, will help to stimulate the participation by a full range of NPPs in Rhode Island's emerging competitive generation market, without imposing undue administrative burdens on the Division. Additionally, RESA recommends use of either five or, at most, ten percent of estimated gross annual receipts as the mechanism for determining the size of the security as between the $100,000 minimum and $250,000 maximum. Moreover, RESA objects to the use of the term "investment-grade" in the definition of the corporate guarantee alternative to a bond or other financial security. "Investment-grade" is not a necessary or reasonable requirement when seeking to confirm that a large corporation is sufficiently creditworthy not to require submission of a Rhode Island-specific bond, and it is likely to raise definitional and administrative problems that will complicate use of this otherwise attractive option for larger suppliers. Finally, RESA

requests that the five (5) business day period for providing notice of a material adverse change be extended to fifteen (15) business days, or not less than ten (10) business days.

RESA Comments

I. A $250,000 Security for all Suppliers is Unreasonably High for a Smaller State Market and Should be Replaced by a $100,000-$250,000 Sliding Scale Based on Revenues.

A. A Fixed $250,000 Security is Excessive Compared to Similar Smaller States.

The Division's analysis supporting a fixed security amount of $250,000, including the Daymark Memorandum, relied principally on similar requirements established for states considerably larger than Rhode Island. See Daymark Memorandum, pp. 2-3 (citing fixed security amounts of $250,000 used in Maryland, New Jersey, Pennsylvania and Texas and an amount of $250,000 or five percent (5%) of estimated revenues in Connecticut). The only smaller state comparable to Rhode Island mentioned in the Daymark Memorandum is Delaware, which has a much lower security requirement. Id., p. 3 (citing Delaware requirement of $50,000 or one hundred fifty percent (150%) of customer deposits and similar funds held by the supplier, whichever is greater). The analysis wholly omitted references to other neighboring states in New England, including New Hampshire and Maine which both have sliding scale financial security requirements starting at $100,000,[2] as well as the District of Columbia, another state with a much lower fixed financial security requirement of $50,000).[3]

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[2] See NH Rule Puc 2003.03; Maine ch. 305 Rules at § 2B.3.c; see also NH Docket No. 16-853 (maintaining $100,000 minimum bond for sliding scale rule in revised proposed rules under consideration by New Hampshire Commission). The Daymark Memorandum also omitted any mention of Massachusetts which, akin to the longstanding Rhode Island rule under review in this proceeding, has no security requirement at all. Furthermore, the Massachusetts Department of Public Utilities has not proposed adding a security requirement at any point in its longstanding (since December 2014) multi-issue proceeding to propose changes to its existing supplier rules. See DPU Docket No. 14-140 (docket filings are available at the following link: <http://170.63.40.34/DPU/Fileroom/dockets/bynumber> (last accessed April 24, 2017)).

[3] See District of Columbia Public Service Commission Interim Application for License to Supply Electricity, p. 14, link available at <http://www.dcpsc.org/PSCDC/media/PDFFiles/Electric/ea_application.pdf> (last accessed April 24, 2017)

As discussed by the RESA presentations during the April 20, 2017 hearing, and supported by the Archer Energy hearing statements, most (if not all) smaller states have used either smaller fixed security amounts or sliding scale requirements in order to avoid creating unintended entry barriers that may dissuade entry by smaller retail suppliers. Financial security can be relatively costly to a smaller supplier,[4] and an excessive requirement would harm consumers by limiting the extent of customer-beneficial choice and competition. The Division should hesitate, in these evolving days of retail electricity competition, especially for the residential and small commercial market segments, to create an above-average financial security amount that could, in combination with the relatively small Rhode Island market size and local regulatory factors, dissuade smaller suppliers from focusing their marketing efforts on Rhode Island and lead them to consider alternative state markets that have lower financial and operational barriers. To the extent that subsequent bankruptcies demonstrate that the above $100,000 fixed security or sliding scale approach are insufficient to protect consumers, the Division can review and revise these rules at such future time.

Finally, as noted during the April 20, 2017 public hearing by Division Advocacy Staff, the legislative impetus for the establishment of new financial security requirements was attributed to one (1) NPP that did not fulfill its Alternative Compliance Payments ("ACP") to the State of Rhode Island associated with its annual Renewal Portfolio Standards ("RPS") compliance requirements. While RESA fully appreciates and supports the need to enhance the financial security requirements, it is important to place into proper context that the vast majority of registered NPPs in over 20 years of a restructured retail electricity market have been

[4]According to RESA members, costs would vary among the proposed instruments, with a surety bond being least costly. RESA member finance personnel indicated that, depending on the size and creditworthiness of the company, a surety bond would typically cost between one and two percent of the face value of the security, or $2,500 to $5,000, exclusive of staff resources devoted to applying for or securing issuance of the bond. Other options could cost as much as the full face value of the instrument.

responsible market participants.[5] Therefore, RESA urges to the Division to consider a gradual transition or measured step when instituting the proposed new security requirements.

B. The Sliding Scale Should Start at $100,000 and Increase at Five or, at most, Ten Percent of Revenues Up to the $250,000 Maximum Security.

The Hearing Officer requested that RESA's comments offer a methodology for determining the sliding scale that would apply to increments between the recommended $100,000 to $250,000 parameters for the financial security requirement. RESA recommends the approach of either five percent (5%) of estimated annual gross receipts (as in Connecticut and Pennsylvania) or, at most, ten percent (10%) (as in Maine).[6] This approach balances the opportunity for a supplier to grow its customer base and revenues within a state with the need to provide a reasonable level of financial protection to cover potential losses resulting from bankruptcy or financial distress.

C. A Sliding Scale Should be Straightforward for the Division to Implement.

Contrary to some concerns expressed by the Division, RESA does not believe that a sliding scale financial security approach will be difficult or costly to implement from the Division's standpoint in the event the Division does not accept the recommendation for a reduced $100,000 fixed security amount. As acknowledged in the Draft Financial Security Rule itself (at Section 9.b), creation of a security requirement necessarily will lead to at least some new Division administrative work to confirm that each NPP or retail supplier has a requisite security in place, whether during initial registration, during the annual reporting process and as suppliers periodically change the issuer of bond due to changing business considerations. Use of a standardized annual revenues form, which would require self-reporting of estimated annual

[5] Furthermore, as the Archer Energy representative pointed out during the hearing, the ACP may not represent the proper measure of financial loss to the State, and that the cost of purchasing replacement RECs – at a far lower cost than a full ACP – may be a more suitable measure, and would support a somewhat reduced bond amount.
[6] See, e.g., Conn. Agency Regs. § 16-245-4 (Security); Maine ch. 305 Rules at § 2B.3.c.

receipts and a mathematical calculation of the corresponding bond amount, should require minimal additional Division attention during a limited period following the mandated once per year filing due date. RESA does note that the existing Draft Financial Security Rules would need to be modified to add an annual financial security form filing requirement for those suppliers seeking to make use of a sliding scale financial security, likely by means of a new second sentence in Section 9b of the Draft Financial Security Rules..

Additionally, the Division could further minimize administrative work by adopting three procedural requirements. First, the Division should make clear that the annual revenue filing requirement only applies to those NPPs that choose not to maintain the maximum $250,000 security. Many suppliers will have a customer base that justifies a $250,000 security and others will decide, as a business matter, that the potential cost savings associated with a reduced sliding scale security will not offset the time and resources associated with making an annual regulatory filing. The Division should make clear that such suppliers are exempt from the annual filing of Rhode Island gross receipts under the new Financial Security Rule. Second, RESA urges that the Division adopt the Connecticut security policy that a bond amount need not be changed at all unless estimated annual receipts change up or down by more than ten (10) percent from the amount on file.[7] Thirdly and finally, from the standpoint of avoiding unnecessary work by both Division and NPPs, the Division should issue a standing order that commercially-sensitive NPP revenue information for Rhode Island be submitted on a confidential basis or will receive protected treatment. It should not require a motion for confidential treatment to be filed by each

[7] See Conn. Agency Regs. § 16-245-4(b) (providing that "[s]ecurity based on an electric supplier's gross receipts shall be subject to annual adjustment. The department may require an increase in the amount of the security if the electric supplier's annual gross receipts increase more than ten percent from the gross receipts amount previously used by the department to determine the level of security required, except in no event shall the department require security in excess of $250,000").

supplier on each filing due date that would need to be reviewed and acted on by the Division with respect to every filing of confidential business information to support bond issuance.

II. The Division Should Delete the Reference to "Investment-Grade" in the Corporate Guarantee Alternative to a Financial Security.

In addition to the requirement of a minimum security requirement in any of three permitted forms (i.e., surety bond, certificate of deposit, or irrevocable standby letter of credit), the Draft Financial Security Rules permit "a corporate guarantee from an investment-grade entity with a Tangible Net Worth of at least ten million dollars ($10,000,000.00)." See Proposed Rule 1.3A.9.a(4). RESA requests that the "investment-grade" qualifier be deleted as unnecessary, inappropriate and likely to adversely affect use of this attractive financial security bypass option for larger NPPs.

"Investment-grade" is a term of art that allows larger companies to choose the option of establishing financial instruments that can be rated in precise ways by agencies such as Moody's for the information and benefit of institutional and individual investors. Some very large companies, especially those which are privately held and/or do not issue investment-grade bonds or securities, do not choose to seek an "investment-grade" designation. Some also have potentially volatile risk profiles that render infeasible an investment-grade qualification. These very substantial companies would be cut off from this otherwise attractive corporate guarantee compliance option even if they have assets at or even far in excess of the already-high threshold of $10 million in tangible net worth and have very substantial operational cash flows that can easily backstop the NPP's operations in Rhode Island.[8] As a practical matter, such a larger

[8] For example, many larger energy companies operate in the merchant power sector and currently face investment-grade rating challenges because natural gas prices are trading at historic lows. Nevertheless, many such companies in the energy sector are cash flow rich. In such cases, the credit rating may not accurately reflect the company's liquidity profile. The "investment-grade" requirement is unreasonable and potentially discriminatory because it would reach and harm companies with a very low probability of default, but are not "investment-grade."

company is going to have sufficient resources to meet obligations in the event of a business reversal of an NPP business in Rhode Island. Instead, RESA requests that the Division rely on the remainder of the subsection (4) option as stated – that an NPP with a corporate guarantee from an entity with a tangible net worth of at least $10 million dollars need not be forced to submit a surety bond or other instrument available under subsections (1) to (3) of Proposed Rule 1.3A.9.a.

III. The Division Should Give More than Five Business Days to Report on Material Adverse Changes in Financial Status.

RESA appreciates the importance of requesting that NPPs provide notice to the Division shortly after the occurrence of a material adverse change, as proposed in Draft Financial Security Rule 9.b. Nevertheless, it is not reasonable to expect an NPP to sustain such an event, identify all business and regulatory actions resulting from such an event, and specifically identify, draft and complete filing of a Rhode Island-specific notice to the Division within only five (5) business days. As a practical matter, this is a recipe for noncompliance by any and all Rhode Island NPPs. The Division should modify this to a more reasonable but still prompt time period, such as fifteen (15) business days or, at minimum, ten (10) business days after the event.

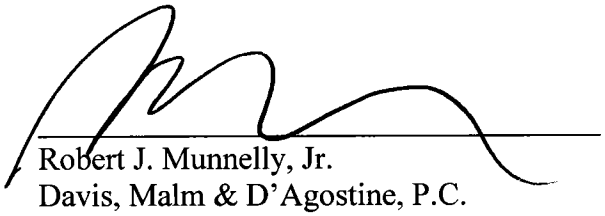
Conclusion

RESA appreciates the opportunity to provide comments on this topic of importance to the development of robust electric competition in the State of Rhode Island. For the reasons discussed above, RESA recommends that (1) the proposed fixed $250,000 security be changed to a fixed $100,000 security amount or, alternatively, should the Division deem that amount to be insufficient, to a $100,000 to $250,000 sliding scale; (2) the revenues for the sliding scale be based on five percent (5%) or, at most, ten percent (10%), of the NPP's estimated annual gross receipts for the upcoming year; (3) procedural requirements should be adopted that would

minimize administrative work by NPPs and the Division; (4) the "investment-grade" requirement be deleted from the corporate guarantee alternative to the financial security requirement; and (5) the material change notice be extended from five business days to a more reasonable fifteen (15) business days, or alternatively not less than ten (10) business days.

RETAIL ENERGY SUPPLY ASSOCIATION

By its Attorney



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