ORDER NO. 80272

In the Matter of Default Service for Type II Standard Offer Service Customers. * * * * * Case No. 9037

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I. Introduction

This case involves the design of Standard Offer Service ("SOS") for Type II customers.[1] A number of proposals have been offered in this case, including: a non-unanimous "Type II Settlement" signed by numerous parties[2], a proposal from the Mid-Atlantic Power Supply Association ("MAPSA")[3], a joint proposal from Washington Gas Energy Services, Inc. ("WGES") and Ohms Energy, LLC ("Ohms"), and a separate proposal from Reliant Energy, Inc.[4] The Public Service Commission ("Commission") has considered the entire record in this proceeding and accepts the non-unanimous Type II Settlement with two modifications. First, the Commission will not move Type I-A customers to Type I-like service, but will instead continue the current Type II SOS procurement procedure for them.[5] This decision continues the Commission's policy of

[1] *See* Case No. 8908, Phase I Settlement Agreement. Type II customers are those from 25 kW to 600 kW, depending on the utility service territory.

[2] The Type II Settlement is Docket No. 29. The "Settling Parties" are: The Potomac Edison Company d/b/a Allegheny Power ("AP"), Apartment and Office Building Association of Metropolitan Washington ("AOBA"), Baltimore Gas and Electric Company ("BGE"), Conectiv Energy Supply, Inc., Constellation Energy Commodities Group, Inc., Constellation NewEnergy, Inc., Delmarva Power & Light Company ("Delmarva"), Maryland Energy Administration ("MEA"), Maryland Office of People's Counsel ("OPC") for a limited purpose, Maryland Retailers Association ("MRA"), Pepco Energy Services, Inc., Potomac Electric Power Company ("Pepco"), and the Staff of the Public Service Commission of Maryland ("Staff").

[3] The MAPSA proposal is supported by Strategic Energy, LLC, Direct Energy Services, LLC, Amerada Hess Corporation and Reliant Energy, Inc. (collectively "Joint Petitioners"). *See* Docket No. 413 in Case No. 8908.

[4] Select Energy, Inc. ("Select") submitted a proposal but did not file testimony in support of the proposal. However, in its brief, WGES notes that Select supports its (modified) position.

[5] In addition to SOS being based on a one-year contract for these customers, they shall be classified as Type II-B customers because they are still a segment of Type II accounts.

implementing an orderly transition to competitive retail electricity supply and electricity supply services markets.[6] Additionally, the Commission will implement the Type II Settlement for only a one-year period, from June 1, 2006 through May 31, 2007.[7]

The Commission encourages settlements and has accepted settlements without modification throughout the SOS proceedings, consistent with the statutory objective to create a competitive retail market. Those settlements that have been accepted have included parties from all market segments and thus represented a compromise among all adverse, competing interests. In this case, no unaffiliated retail provider, not associated with a Maryland investor-owned utility ("IOU"), has signed the Type II Settlement. Consequently, the base supporting the settlement in this proceeding is not as broad as those supporting previous SOS settlements in Maryland.

The Commission is receptive to broad-based settlements. As is shown by its decision in this proceeding, it also will consider settlements that lack support from one market segment or another. The changes to this settlement agreement adopted by the Commission are necessary, in the Commission's view, to better encompass the needs and requirements of all segments of Maryland's electricity industry: customers, suppliers, and utilities alike.[8]

Specifically, the Commission is concerned with the proposal to provide the newly-created Type I-A customer class with SOS based on blended (one and two-year) contracts. In our view, this represents a step away from market-based rates, and the

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[6] *See* Public Utility Companies Article ("PUC Article"), Sections 7-505(a)(1) and 7-504.
[7] For AP's Type II customers, the Type II SOS period shall be from January 1, 2007 through December 31, 2007.
[8] It is the Commission's statutory, non-delegable duty to act in the public interest. Consequently, there may arise instances when the Commission does not accept a settlement from parties representing adverse, competing interests because it is not in the public interest.

Commission finds this provision inconsistent with the statutory requirement that the Commission create competitive retail electricity markets. We note in this regard that § 7-504 of the Public Utility Companies Article sets forth a legislative purpose to create competitive retail electricity markets in Maryland. As discussed below, we find that the proposal to create a new Type I-A Standard Offer Service class, with SOS identical to Type I SOS, may interfere with and retard the development of a competitive retail market for those customers.

In addition to accepting a modified version of the Type II Settlement, the Commission will direct the parties to engage in further discussions on how to continue the orderly development of competitive electricity markets in the State. The parties should explore alternatives for different pricing intervals in the SOS model, successful alternatives adopted elsewhere, and innovative new proposals. The parties shall also explore metering issues. The parties are advised that any proposal must advance competitive markets, as the statute commands, for the Commission to accept a proposal. In this regard, the Commission's modified version of the Type II Settlement should be viewed as an interim measure.

II. Summary of Type II Standard Offer Service Proposals

On June 24, 2005, a settlement agreement ("Type II Settlement") was filed (including a revised Model RFP and Model FSA) on behalf of numerous parties, which sets forth the provision of Standard Offer Service for Type II SOS customers beginning June 1, 2006.[9] The Type II Settlement divides current Type II customers into two new groups, Type I-A and Type II-A. Type I-A customers are those not eligible for Type I

[9] The current Type II SOS period expires May 31, 2006, except for AP, which expires December 31, 2006.

SOS whose PJM capacity peak load contribution ("PLC") is 100 kW or less, excluding existing utility special generation contract customers, while Type II-A customers are all other Type II SOS customers (those with a PLC greater than 100 kW but less than 600 kW), excluding special generation contract customers.[10]

The Type II Settlement states that the utilities agree to provide Type I-A and Type II-A SOS from June 1, 2006 to May 31, 2008, except AP, which will provide the services from January 1, 2007 to May 31, 2008. Under the Type II Settlement, the utilities will provide Type I-A SOS in the same manner as Type I SOS is provided pursuant to Case No. 8908. Type II-A SOS will be provided in a similar manner to Type II SOS; however, service will be procured for two periods each year (summer/winter), no volumetric risk mechanism will be used, and some procedural details will be modified.[11] Finally, the utilities agree to provide interval meters to all customers with a PLC of 550 kW or greater and to standby service customers by June 1, 2007, and to customers with a PLC of 500 kW or greater by June 1, 2008.[12]

An alternative proposal was filed by a group of electricity suppliers, the "Joint Petitioners."[13] The Joint Petitioners have proposed adoption of hourly priced service ("HPS") as the only default electric service for those Type II customers who do not take electric supply from a competitive supplier upon the expiration of the current Type II SOS periods. They assert that this would be consistent with statutory requirements, the transitional nature of the Phase I and II Settlements in Case No. 8908, and the

[10] Type II Settlement at 2 and 4.
[11] *Id.* at 5-6.
[12] *Id*. at 6-7.
[13] Joint Petition for Declaratory Relief, or Alternatively, For Clarification Regarding Default Service for Type II Standard Offer Service Customers. The Petition was filed in Case No. 8908.

Commission's implementing orders in that case.[14] However, the Joint Petitioners have proposed that HPS be phased in for Type II customers. All Type II customers having a demand of 300 kW or greater would begin to receive (or more accurately be eligible for) HPS on June 1, 2006.[15] Type II customers having a demand of 100 kW or greater (but less than 300 kW) would receive HPS on June 1, 2008.[16] HPS would be provided to Type II customers in the same manner as HPS is provided to Type III SOS customers. The Joint Petitioners conclude by requesting a separate proceeding to determine the appropriateness of HPS for small commercial customers, those having a demand of less than 100 kW.[17]

Reliant offers a separate proposal if the Commission does not accept the Joint Petitioners' recommendation to transfer Type II customers to HPS.[18] For those non-hourly-priced SOS customers, Reliant proposes SOS based upon retail market rates, adjusted up to two times per year. Competitive electric suppliers will be invited to participate in a standard retail open offer program ("SCRS"). The marginal (i.e. highest) price accepted by customers in the open offer program will be used to determine the initial SOS energy price.[19] In addition to the fixed energy price, customers will pay all

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[14] In Case No. 8908, the Commission approved detailed rules for the provision of SOS for those electricity customers not served by a competitive electricity supplier.

[15] Docket No. 43. Direct Testimony of James A. Ajello at 6.

[16] *Id*. The Joint Petitioners recommend that non-hourly-priced Type II customers with a PLC of 100 kW up to 300 kW receive service from 2006-2008 pursuant to either Reliant's proposal, the Type II-A proposal, or pursuant to the existing Type II SOS structure. Docket No. 54, Rebuttal Testimony of James A. Ajello at 12.

[17] The Joint Petitioners recommend the same three options for Type II customers below 100 kW as discussed in the footnote above, but without a suggested ending date. Docket No. 54. Rebuttal Testimony of David A. Svanda at 25.

[18] Docket No. 39. Testimony of Lance S. Muckelroy.

[19] *Id*. at 15. Reliant later agreed to use the average price. Transcript at 437- 439.

non-bypassable charges assessed by transmission and distribution providers (including PJM network integration charges) based upon the existing tariffs of the applicable utility and PJM.[20] After the initial price determination, the SOS provider could then adjust the retail SOS price up to two times per year based upon changes in a known market index.[21] Reliant says an affiliated competitive electricity supplier of the incumbent utility, rather than the utility itself, should be the SOS provider.[22] Finally, Reliant says that the SOS provider would determine and execute its own SOS supply procurement strategy.[23]

Washington Gas Energy Services, Inc. and Ohms Energy, LLC also filed an alternative proposal.[24] They recommend extending Type II SOS for all Type II customers through May 31, 2008, based on the current procedures, except that wholesale bids would be conducted three times per year.[25] According to these parties, a trimester schedule "should adequately reflect market seasonality, offer price variability and provide appropriate price signals to end-use customers in this class."[26] Additionally, their proposal provides that: Allegheny Power would develop retail default service prices for Type II SOS based on actual retail bids, the same way the other three utilities do now; there would be no volumetric risk provisions; and there would be no switching restrictions.[27]

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[20] Docket No. 39 at 17-18.

[21] *Id*. at 15. Reliant suggests using the New York Mercantile Exchange ("NYMEX") PJM monthly financially settled on-peak and off-peak electricity futures contracts as indices. Docket No. 39 at 24-25.

[22] Docket No. 39 at 16. Reliant says that if the Commission decides to continue having utilities provide SOS, the remainder of its proposal could still be implemented. *Id*. at 16, footnote 7.

[23] Docket No. 39 at 16.

[24] Docket No. 27.

[25] *Id*. at 1. During the proceedings, WGES suggested that four bids per year would be preferable. Transcript at 387-388. It should also be noted that Select Energy, Inc. has recommended that Type II SOS bidding take place on a quarterly basis. Docket No. 26. In other respects, its proposal is essentially similar to that of WGES and Ohms. *Id*.

[26] Docket No. 27 at 1.

[27] *Id*. at 2.

Under the WGES/Ohms proposal, consideration would be given to transitioning the upper tier of Type II customers to HPS after May 31, 2008. WGES and Ohms recommend transitioning customers as follows: 450 kW and above in 2008; 400 kW and above in 2009; and 350 kW and above in 2010.[28] Customers below 350 kW would remain in Type II SOS and be subject to further Commission review and action in 2010.[29] WGES and Ohms also propose that AP fully synchronize with the default service periods of the other utilities. Further, the Administrative Charge would be increased if estimated bid procurement costs reach certain thresholds. Finally, these parties recommend that Staff convene a working group to explore non-utility, competitive default service options.[30]

Mirant Mid-Atlantic, LLC submitted comments regarding the Volumetric Risk Mechanism ("VRM"). Essentially, Mirant proposes narrowing the band for VRM price adjustments.[31] In the alternative, Mirant recommends retaining the current VRM for Type II SOS.[32]

III. Commission Decision

The Electric Customer Choice and Competition Act of 1999 ("Electric Act") establishes five purposes: to establish customer choice; create competitive retail electricity supply and electricity supply services markets; to deregulate the generation, supply and pricing of electricity; provide economic benefits for all customer classes; and ensure compliance with environmental standards.[33] Customer choice was established in

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[28] Docket No. 27 at 2.
[29] *Id*.
[30] *Id.* at 3.
[31] Docket No. 28.
[32] *Id*. at 9.
[33] PUC Article, Section 7-504. The Electric Act is contained in Sections 7-501 through 7-518.

2000 and the supply and pricing of electric generation was deregulated. Consequently, these SOS proceedings have focused upon how best to promote competitive retail markets in conjunction with an appropriate default service.

The purpose of the Standard Offer Service proceedings is to advance the orderly development of competitive retail electricity markets in Maryland, while maintaining reliable electric service and providing an appropriate default service option during the transition process.[34] In so doing, the Commission has deliberately balanced competing interests to achieve this goal. The Commission finds that the twice yearly procurement process proposed for Type II-A service will promote competition because it will allow retail competitive service providers an opportunity to offer products, particularly an annual contract, not otherwise available to these Type II customers. Conversely, the proposal to shift some Type II customers to Type I-like service, with its blended one and two-year SOS contracts, could potentially make it more difficult for retail providers to compete in the marketplace. Consequently, the Commission finds that it is more appropriate for the smaller Type II customers to have a SOS product based upon the current (one-year) procurement process. The Commission believes customers will benefit from competitive markets once providers have the opportunity to develop sustainable businesses and service offerings. Furthermore, this goal comports with the legislative requirement to develop competitive retail electricity markets in an orderly fashion.

The design of the SOS product can act as a barrier to entry into the Maryland market. Customers will be deprived of the multiplicity of contract terms that would be available to them in a market characterized by multiple providers, to the extent that entry

[34] PUC Article, Section 7-505.

does not occur. Therefore, the Commission must ensure that the SOS product developed in this proceeding does not act as a deterrent to entry. An SOS product that deterred entry in general or competition for particular classes of customers would neither be consistent with the intent of the Electric Customer Choice and Competition Act of 1999 to create a competitive retail market nor would it constitute good public policy. We find that an SOS product which is characterized by a price that remains unchanged for undue periods of time can deter entry and deprive customers of the varied contract terms which would be available with greater entry. The record establishes that there are costs associated with entry. The record further establishes that retailers will not choose to incur those costs if the SOS structure renders entry uneconomic for long stretches of time. In order for entry to occur, the opportunity to compete against the SOS product must be sustained and continuous, not intermittent.

We find that the treatment of the proposed Type I-A class of customers in the non-unanimous Type II Settlement will retard the development of competitive choices for the customers covered by that aspect of the settlement. Therefore, we do not accept that aspect of the settlement, as it is inconsistent with the legislative intent, expressed in Section 7-504(2), to create competitive retail markets.

While the Commission finds that seasonal (winter/summer) SOS procurements will provide pricing that is sufficiently market-based at this stage in the development of the retail market, the Commission is not convinced, based on this record, that an hourly-priced service (HPS) is an appropriate default service for most commercial customers. There was ample testimony regarding the current lack of interval metering for large numbers of Type II customers. Additionally, many parties, particularly customer representatives, convincingly demonstrated that even if the meters were available that many Type II customers could not reasonably make use of the data such meters can provide. Consequently, the Commission will not mandate broad-based hourly-priced SOS. However, the Commission does accept the investor-owned utilities offer to deploy interval meters as set forth in Paragraph 15 of the Settlement.

The Commission finds that the proposal of WGES and Ohms for three bids per year has merit, but represents too much of a change for the service year under discussion. Further, WGES now recommends bidding four times per year.[35] What bidding structure for SOS is best going forward is appropriately a matter for discussion and analysis in the workgroup process as discussed below. Therefore, the Commission will defer further consideration of the WGES proposal at this time.

Reliant has offered a proposal that essentially dismantles the basic SOS policy framework developed in the Case No. 8908 Phase I Settlement and establishes a new and very different default service paradigm for Type II customers. Reliant's proposal may or may not be a workable construct for provisioning default service. Nonetheless, the case has not been made that would lead the Commission to jettison the basic structure of SOS in Maryland. We decline the invitation to scrap a basic policy framework that appears to be working, and certainly has not been a failure, in favor of an alternative that is altogether unknown and untested in the Maryland market.

The Commission appreciates the continued efforts of the parties to promote the orderly transition to competitive electricity markets in Maryland. However, work still remains. Therefore, the Commission directs the Staff to convene the parties to address

[35] Transcript at 387-388. Select Energy also recommends that SOS be based on four bids per year.

proposals for expeditiously implementing customer choice. The workgroups shall not confine their proposals to Type II customers. Further, the Commission will require quarterly updates on the progress of proceedings, including the identification of issues, proposed resolutions and procedural requirements. The discussion among the parties should address all feasible program designs, including but not limited to, multiple procurements of SOS power per year by the utilities, various potential indexing methods for pricing SOS and the potential provision of SOS by a retail bidding regime.

For the reasons discussed herein, the Commission adopts the Type II Settlement, modified as follows: Type I-A customers (henceforth known as Type II-B customers) will be eligible for SOS based on current Type II procurement procedures and the Type II Settlement will expire May 31, 2007, except for AP customers, which shall expire December 31, 2007.

Since the Commission adopts a modified version of the Type II Settlement for one year, a technical issue must be addressed. The utilities have not agreed to the modified version of the Type II Settlement. Therefore, the Commission requests that AP, BGE, Delmarva, and Pepco respond within 10 days of this order whether they agree to be the Standard Offer Service provider in their respective service territory as set forth in the Type II Settlement and as modified herein. If any utility declines to be the SOS provider, the Commission will address alternatives at that time, including the possibility of soliciting retail offers for Type II Standard Offer Service.

IT IS, THEREFORE, this 20th day of September, in the year Two Thousand Five, by the Public Service Commission of Maryland,

ORDERED: (1) Standard Offer Service shall be provided to Type II SOS customers of The Potomac Edison Company d/b/a Allegheny Power for the period January 1, 2007 through December 31, 2007, according to the terms of the Type II Settlement, except that Type I-A SOS customers shall receive service in the manner currently provided for Type II customers;

(2) The Potomac Edison Company d/b/a Allegheny Power shall notify the Commission, in writing, within 10 days of this order whether it agrees to be the Type II SOS provider in its service territory according to the terms in Paragraph One;

(3) Standard Offer Service shall be provided to Type II SOS customers of the Baltimore Gas and Electric Company for the period June 1, 2006 through May 31, 2007, according to the terms of the Type II Settlement, except that Type I-A SOS customers shall receive service in the manner currently provided for Type II customers;

(4) Baltimore Gas and Electric Company shall notify the Commission, in writing, within 10 days of this order whether it agrees to be the Type II SOS provider in its service territory according to the terms in Paragraph Three;

(5) Standard Offer Service shall be provided to Type II SOS customers of Delmarva Power & Light Company for the period June 1, 2006 through May 31, 2007, according to the terms of the Type II Settlement, except that Type I-A SOS customers shall receive service in the manner currently provided for Type II customers;

(6) Delmarva Power & Light Company shall notify the Commission, in writing, within 10 days of this order whether it agrees to be the Type II SOS provider in its service territory according to the terms in Paragraph Five;

(7) Standard Offer Service shall be provided to Type II SOS customers of Potomac Electric Power Company for the period June 1, 2006 through May 31, 2007, according to the terms of the Type II Settlement, except that Type I-A SOS customers shall receive service in the manner currently provided for Type II customers;

(8) Potomac Electric Power Company shall notify the Commission, in writing, within 10 days of this order whether it agrees to be the Type II SOS provider in its service territory according to the terms in Paragraph Seven;

(9) The Public Service Commission Staff shall promptly convene working group meetings to explore the next phase in the provision of Standard Offer Service for residential and Type I and Type II commercial customers. Staff shall advise and report to the Commission on the progress of discussions as provided in this order;

(10) Each utility shall expand the deployment of interval meters as set forth in the non-unanimous Type II Settlement; and

(11) All outstanding motions not granted herein are denied.

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Commissioners