



State of New Jersey
DIVISION OF RATE COUNSEL
31 CLINTON STREET, 11TH FL
P. O. Box 46005
NEWARK, NEW JERSEY 07101

CHRIS CHRISTIE
Governor

KIM GUADAGNO
Lt. Governor

STEFANIE A. BRAND
Director

**I/M/O the Provision of Basic Generation Service (“BGS”) for
the Period Beginning June 1, 2011
BPU Docket No. ER10040287**

**Comments of Stefanie A. Brand,
Director of the Division of Rate Counsel
at a Legislative-Type Hearing
Before the Board of Public Utilities
September 21, 2010**

Good afternoon, my name is Stefanie A. Brand and I am the Director of the New Jersey Division of Rate Counsel. Rate Counsel’s consultant, Mr. Robert Fagan of Synapse Consulting, is here with me. I want to thank you for the opportunity to appear before you today on behalf of the state’s ratepayers. I would like to offer some ideas, that I hope the Board will consider, of ways to improve our procurement of Basic Generation Service – or BGS.

While there has been an increase in residential use of third party suppliers in recent months, New Jersey still relies on an auction process to procure Basic Generation Service Fixed Price (BGS-FP) supply that has essentially remained the same since 2003. For example, between June 1, 2009 and May 31, 2010, BGS-FP

ratepayers bought just over 51 million MWh of energy and capacity at a supply cost of roughly \$5.4 billion¹.

While the electric industry and our understanding of the restructured industry environment has evolved, the procurement process for BGS-FP supply has remained essentially static since 2003. Rate Counsel submits, and has previously submitted, that New Jersey requires a more flexible, forward-looking approach that recognizes the importance of establishing procurement vehicles in addition to the limited procurement option currently exercised each winter with the BGS-FP auction.

Rate Counsel has consistently taken the position that New Jersey BGS-FP ratepayers would benefit from the establishment of a Portfolio Manager approach to BGS-FP supply procurement. We believe a reasonable response to the continually evolving energy markets is the creation of a Portfolio Manager with the ability to investigate potential ratepayer cost savings available through these evolving markets and the flexibility to secure resources outside the BGS auction process. The current approach limits potential suppliers to only those who can provide a “full requirements” product. An expanded supply marketplace would allow for other products which would place additional competitive pressure on prices for BGS-FP supply and maximize the benefits of competition for ratepayers. As noted in our earlier filed comments, the creation of a statewide Portfolio Manager could expand BGS-FP service to include, if economically attractive, a wider range of resource options than is currently available.

¹ Includes energy, capacity, ancillary services, RECs and transmission costs. Excludes distribution, retail margin, SBC, etc. Assumes 10.5 cents/kWh laddered rate. Consumption from BGS auction website; laddered rate from Synapse computation using auction results.

For example, a Portfolio Manager procurement approach might be more conducive to capturing the benefit of the current lower wholesale energy rates in PJM than the BGS-FP auction approach.² A Portfolio Manager could also consider a purchase of other products – such as fixed volume energy blocks coupled with “hedges” to protect against fuel cost variation - or consider a procurement of energy for different time durations or at different intervals than the current process, which is limited to a single annual purchase of a three-year term product. A Portfolio Manager might also be able to enter separate contracts for capacity resources to help place downward pressure on capacity prices in New Jersey if found to be economically feasible. The key point is that unlike the rigid structure of the current BGS auction process, a Portfolio Manager would have the ability to explore and recommend economically attractive options for BGS supply in response to market conditions and as opportunities arose. To provide increased opportunity for lower prices while maintaining appropriate levels of price stability for customers, the BGS-FP supply portfolio could include resources, such as fossil, wind, solar, or even demand response, and contracts of varying terms such as long-term contracts for ten to twenty-five years, or even “Life of Plant” contracts. For example, solar PV and wind resources both lend themselves to long-term contracting mechanisms given their high capital cost and zero going-forward fuel costs. The financial realities of developing renewable resources usually require longer-term contracts than three years, and thus coupling this purchase requirement with the current

² PJM wholesale market prices in the first half of 2010 were higher than the prices seen in 2009, but still much lower than the historically high average prices seen between 2005-2008. *2010 Quarterly State of the Market Report for PJM*, January through June, August 12, 2010, page 30 Table 2-52 PJM real-time, annual, load-weighted, average LMP (Dollars per MWh): Calendar years 1998 through June 2010 (See 2009 SOM, Table 2-59).

Available at http://www.monitoringanalytics.com/reports/PJM_State_of_the_Market/2010/2010q2-som-pjm-sec2.pdf.

3-year term associated with BGS supply does not necessarily achieve the economies that could be obtained with longer-term renewable resource contracting.

Portfolio Manager could also include three-year contracts procured through the auction, and shorter-term resources to balance out the portfolio, and financial “hedge” products as appropriate to protect against fuel price increases. In turn, the size and/or number of tranches sold at the auction would be based on load needed after subtracting the contribution from the other resources in the portfolio. Thus, if 10 percent of the BGS-FP supply were procured through the portfolio management approach, the auction could procure the remaining 90 percent of the load. As a spillover benefit, the reduced electricity volume in the BGS-FP auction would place additional competitive pressures on BGS-FP auction bidders.

A Portfolio Manager approach could be implemented in a number of ways. We would encourage the Board to implement a portfolio management approach for BGS-FP supply by exploring the feasibility of retaining the services of a professional Electricity Portfolio Manager through an RFP process. The scope of work sought through the RFP could be defined by a working group. The Portfolio Manager should have extensive expertise in mid-Atlantic electric markets, specifically PJM. The Portfolio Manager should also be independent, with no ties to existing BGS-FP suppliers and no financial interest in the outcome of the procurement.

I would also like to point out that alternative approaches to supply procurement for New Jersey electric customers are not without precedent. Notably, one New Jersey EDC - RECO – already procures supply for two of its service territories through an RFP

approach.³ Also, current EDC programs for solar and demand response resources are but two examples of the forms of procurement expansion that is required to ensure the most cost-effective supply purchase for BGS-FP customers. We note that New Jersey's EDECA statute requires a market based procurement for BGS-FP load – but there are a number of methods that would satisfy the statute. While the current auction process using a 3-year full-requirements product meets the intent of EDECA, it is not the only way to meet the intent of the statute.

Procurement practices in other States illustrate a varied mix of competitive-market-based purchase practices for residential and small customer fixed-price “standard offer” service supply, and for renewable energy supplies. For example, Connecticut utilities have secured peaking power supplies for 20-year year terms from three separate generating resources to complement standard service energy supplied under shorter-term contracts. The Illinois Power Agency has completed fixed-volume energy procurements using competitive RFPs, on behalf of Illinois EDCs; and it directly purchases capacity and ancillary service requirements through PJM. It also has received approval from the Illinois Commerce Commission for 20-year PPAs for renewable energy and the associated RECs. Three, 12, and 24-month contracts have been approved in Maryland. For residential customers, Rhode Island has used and is proposing to continue use of a small level of spot market purchases, mixed with full-requirements service, with bi-annual purchases of contracts with six and 12 month terms. For larger industrial customers, Rhode Island purchases standard offer supply on a quarterly basis. Rhode Island and Massachusetts have secured or are in the

³ See RECO Company Specific Addendum, response to RCR-73.

process of securing long-term PPAs for offshore wind energy to meet a portion of RPS requirements. And as we have previously noted, Delaware has both onshore (170 MW total) and offshore (200 MW total) long term wind contracts in place between developers and utilities. This sampling of standard offer and renewable energy procurement activity in other states illustrates that there are a multitude of alternative arrangements being used by “deregulated” states to secure energy and renewable supplies for BGS or standard offer service customers, and they are all based on competitive market procurement mechanisms.

In sum, we believe that the creation of a Portfolio Manager could expand BGS-FP service to include, if economically attractive, a wider range of resource options than is currently available. A Portfolio Manager could take advantage of opportunities in the evolving energy markets and leverage the market to, hopefully, mitigate price increases and volatility for New Jersey’s BGS ratepayers. If the Board elects not to adopt the Portfolio Manager approach at this time, Rate Counsel submits that a formal stakeholder process be established to consider this issue.

Thank you for allowing me to present this testimony and in the interest of New Jersey’s ratepayers, I strongly urge the BPU to seriously consider our recommendations. Further details of our recommendations can be found in our written comments filed on August 27, 2010 and in the comments we will be filing later this month. We are, of course happy to take any questions you may have regarding our testimony.