STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

CASE 15-M-0127 – IN THE MATTER OF ELIGIBILITY CRITERIA FOR ENERGY SERVICE COMPANIES.

CASE 12-M-0476 – PROCEEDING ON MOTION OF THE COMMISSION TO ASSESS CERTAIN ASPECTS OF THE RESIDENTIAL AND SMALL NON-RESIDENTIAL RETAIL ENERGY MARKETS IN NEW YORK STATE.

CASE 98-M-1343 – IN THE MATTER OF RETAIL ACCESS BUSINESS RULES.

CASE 14-M-0101 – PROCEEDING ON MOTION OF THE COMMISSION IN REGARD TO REFORMING THE ENERGY VISION.

RESPONSE TO THE COMMISSION'S NOTICE SEEKING COMMENTS ISSUED MAY 10, 2016 BY INFINITE ENERGY

Infinite Energy, Inc. DBA Intelligent Energy ("Infinite Energy") appreciates the efforts of the New York Public Service Commission ("Commission") and its Staff to address the issues plaguing the New York retail energy market. As a natural gas ESCO serving New York since 2004 and an energy services provider serving customers throughout the country for over two decades, Infinite Energy appreciates the opportunity to participate and assist in these proceedings.[1]

As a preliminary matter, Infinite Energy respectfully asserts that the three areas of concern addressed in the white papers issued by the Staff of the Commission are merely symptoms of the fundamental flaws in the structure of the New York retail energy market. Untenable issues will persist, whether in their current or different forms, until the fundamental flaws are addressed.

Infinite Energy proposes that the Commission pursue whatever action is necessary to require the New York utilities to create arms' length regulated affiliates to manage all commodity-related functions for customers who have not chosen a competitive ESCO. These "Regulated Providers" would continue to operate under an obligation to serve and offer month-to-month rates regulated by the Commission, ensuring that the Commission's concerns regarding utility service are addressed. By separating the accounting that underlies utility ratemaking, the Commission can ensure that its ratemaking responsibility is properly applied to utility delivery rates and, on a fully unbundled basis, utility commodity rates. Such Regulated Providers would be required to operate on the utility's system in the same manner as ESCOs, fully unbundling commodity costs from delivery charges, thus ensuring that New York customers are paying no more or less for either service than is appropriate, thereby providing a level playing field for all suppliers.[2]

This action would solve outright many of the issues affecting the New York market, and would immediately address the concerns of consumers, market participants, and the Commission. Moreover, the complete unbundling of delivery from supply and the appropriate allocation of costs will reveal that ESCO rates already are competitive against utility rates, and can be more competitive.

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[1] At this time, Infinite Energy focuses its comments on the New York natural gas market. We note, however, that many of the concerns and proposed solutions translate to the New York electric market.

[2] It also comports with Commission precedent and practice that, "it is well understood that we [the Commission] lack authority to regulate the rates that an ESCO charges any customer (residential or nonresidential). Therefore, neither an informal hearing officer nor the Commission may determine that an ESCO's charges to its customer is improper." Case 09-G-0289, Commission Determination, issued August 23, 2010, at 7.

New York utilities currently act as both regulated commodity suppliers and local distribution providers. These conflicting roles introduce confusion at all levels of the market, create "information asymmetry" in rate cases,[3] confound the appropriate allocation of costs and charges, and contribute to tension within and without the utilities themselves. It is difficult, if not impossible, for any organization, let alone an integrated monopoly, to simultaneously act as a competitive commodity supplier and as a neutral platform provider without these negative effects.

Creating arms' length affiliates for regulated commodity supply functions would mirror the divestiture of wholesale electric generation assets that necessarily preceded the opening of the retail energy market. It is a natural evolution for a restructured state and would address several longstanding problems.

- Market power at the operational, scheduling, and balancing level would be eliminated. The Commission easily could ensure that Regulated Providers are assigned capacity and other upstream assets on a pro rata basis, equal to the assignments and releases ESCOs are granted. Each utility's Regulated Provider would pay imbalance and other operational charges in the same manner as other suppliers operating on the LDC's system. As in other competitive markets, simple processes and safeguards would ensure that the LDC could maintain system reliability. As currently structured, the same LDC operations team that secures supply and vies for off-system sales is responsible for releasing capacity and providing the scheduling and balancing platform used by ESCOs – in any other industry this inherent conflict of interest, which harms consumers by distorting the market, would be scrutinized as a potential antitrust matter.
- The longstanding issue of incomplete unbundling would be automatically addressed – all credits and charges applicable to acquiring and transporting commodity[4] would be appropriately levied by the Regulated Provider while all charges and credits applicable to maintaining, operating, and improving the delivery system would be appropriately levied by the distribution utility. As LDC charges are currently structured, New York ratepayers cannot compare their delivery or commodity charges against those of consumers in neighboring service areas or other states; those responsible for ensuring fair and just rates cannot perform full analyses or audits of utility charges; those who compete are accused of over-charging customers despite the clear and present concern that New York customers are underpaying for commodity while overpaying for delivery.
- The Commission, ratepayer advocates, customers, and other market participants would be able to easily monitor the activities of the LDCs and their unbundled affiliates to ensure just and fair rates, equitable assignment of costs, fair market dealing, and an even playing field for all parties. This is especially important in light of the Commission's Ratemaking Order; separating supply-side from delivery-side operations will ensure that each of the Commission's four new ratemaking principles can reach fruition, as each entity will be incented to focus on cost-effective and value-added initiatives within its respective domain.

While Infinite Energy believes that the best solution to New York's retail market issues is the complete exit of the utilities from all competitive functions, both the Commission and its Staff have made it clear that there is little possibility of such occurring in the near future. Our current proposal for the creation

[3] Order Adopting a Ratemaking and Utility Revenue Model Policy Framework issued May 19 ("Ratemaking Order").
[4] It cannot be stressed enough that a gross unfairness is done to ESCO customers in New York under the current ratemaking that applies significant credits to LDC commodity rates. All New York customers have contributed to the LDC charges, systems, and assets that earn those credits; therefore, all New York customers deserve to receive those credits.

of arms' length Regulated Providers addresses all of the issues in question while, we believe, remaining within the realm of the Commission's authority. Solutions such as those proposed in the white papers that do not address the underlying inequities addressed above will only push the market issues and complaints back a level of abstraction. Therefore, to the extent that the proposals presented in the white papers are considered as immediate-term stopgaps, we respectfully submit the following comments.

Express Consent

Infinite Energy recommends that customers be allowed to select electronic service to receive the three expiration notices by email or text. Customers should be allowed to change between paper and electronic options at any time.

Performance Bonds

Infinite Energy supports the imposition of reasonable performance bonds, similar security, or proof of financial capability ("Security") for ESCOs operating in the New York retail energy market. Infinite Energy agrees with the several parties who argued that the Commission itself, not the utilities, should hold any Security requirements.

Such Security should not be exclusively scaled based on the number of customers served and volumes supplied by the ESCO. All ESCOs should meet a minimum threshold, whether by posting a bond, some other security, or proof of equity. ESCOs that cannot meet minimum qualifications should be excluded from the New York market. The purpose of this Security should be not only to ensure ESCO performance and ability to pay fines, but to proactively identify ESCOs which do not meet a sufficient standard of financial and operational integrity to operate in markets as demanding as New York's market.

As stated in previous comments,[5] Infinite Energy believes that a significant number of the many ESCOs operating in New York do not possess the financial, operational, or technical qualifications to properly serve the New York market. At least some of these operations are designed to sign up customers using aggressive techniques and teaser rates, as they have neither the operational or financial backing to provide long-term, consistent value. Appropriate Security, as well as standardized technical and managerial requirements, will do much to remove unqualified ESCOs from the market.

It must be stressed, however, that removing these unqualified ESCOs will not have a complete curative effect on the complaints and pricing issues that have spurred the Commission to action in these proceedings. The aforementioned comments detail the much greater roles played by the direct presence of monopoly utilities in commodity supply, the continuation of Utility Consolidated Billing and the Purchase of Receivables program, the ongoing issue of incompletely unbundled LDC charges, and the lack of effective oversight and effective penalties for misbehavior.

Reference Prices

For ESCO variable rate products, Staff proposes that the "Reference Price" would remain the LDC's posted monthly commodity price. For ESCO fixed rate product offerings, Staff proposes a calculated "Reference Prices" against which ESCOs would compete. Infinite Energy strongly disagrees with the presumption that the Commission possesses the authority to regulate ESCO prices. We also strongly

[5] Comments on the Commission's Efforts to Improve the New York State Retail Energy Markets of Infinite Energy, Inc., dated June 2, 2014.

disagree with the presumption that most ESCO prices are "uncompetitive" – the question is not whether ESCO prices are competitive with utility charges but whether utility charges are properly designed. As discussed in detail below, there are serious concerns with the current assignment and allocation of costs between utility commodity charges – against which ESCOs are expected to compete – and utility delivery charges, which all ratepayers pay.

Respectfully, it is not clear what advantage there is to creating an artificial "reference price" structure for 12 month fixed rates[6] if the LDC's monthly rate calculation remains unchanged. The proposed formulas are themselves a testament to the flaws in current LDC commodity rates. Were those rates market-based and aligned with the true cost to supply commodity to customers, there would be no need to create a formula for an apples-to-apples reference price.

Customers will find no solace in the fact that their ESCO rate is lower than the reference price but nonetheless higher than the LDC's rate. ESCO rates will likely remain higher than LDC charges in the majority of cases for the simple reason that LDC charges are themselves artificially low inventions that do not reflect the actual cost of gas delivered to the LDC's citygate. The "reference price" proposal does nothing to address price comparisons insofar as variable rates are concerned. ESCO variable rates especially are forced upwards by inequitable capacity releases and related issues afore-mentioned, making any comparison to the LDC commodity charges even more distorted.

The only effective solution, aside from removing the LDCs from commodity supply and merchant functions entirely, is to fix the underlying problems with LDC commodity rates. Reference prices – indeed, the entire question of the competitiveness of ESCO rates – would be moot if LDC and ESCO commodity prices reflected the true and equitable costs of securing, transporting, and managing the commodity.

Current LDC charges are such that no party – neither the LDCs nor those tasked with regulating them – can prove that ratepayers aren't significantly overpaying for delivery while underpaying for LDC-supplied commodity. Unfortunately, due to the fact that the LDC ratemaking has bundled delivery and commodity costs and cross-subsidized charges in a complex manner, it is nearly impossible for anyone to perform a thorough analysis of LDC charges. For this reason, it is crucial that all LDC charges be transparent, audited, and objectively allocated. Until this occurs, all other proposals are built on a foundation that is both uncertain and unsteady. The ratepayers of New York deserve an unwavering commitment to just and reasonable rates – and transparent, accessible proof of the same.

Three major elements contribute to the lack of apparent competitiveness in ESCO product offerings:

- Despite being paid for equally by all ratepayers, access to upstream assets controlled by the LDCs is not shared equally with the ESCOs serving customers. Pipeline capacity, storage, and other upstream assets that then can be optimized to reduce a customer's commodity price is not fully and equitably released to the ESCO when that customer switches. ESCOs thus pay more to acquire and transport gas to their customers, while those customers that remain on system supply receive more and more of their commodity from the most economical sources.
- Imbalance charges and other gas scheduling and nomination practices are not based on a cost-to-serve or cost-incurred model, and instead are punitive even in the vast majority of cases where minor imbalances cause no damage or even the possibility of risk to the utility system. Each LDC maintains separate rules, requirements, and schedule of charges, effectively

[6] Infinite Energy's comments regarding the issues with the specific Reference Price formula proposed for 12 month fixed rates are included as Appendix A.

unregulated by the Commission. These requirements and charges are not only arbitrary but severely limit ESCOs' flexibility in the wholesale market and burden them with arbitrary costs to do business far in excess of the LDCs' cost or risk incurred. The LDCs themselves, in their role of commodity supplier, are themselves not subject to either the limitations or the charges to which ESCOs are subjected. Moreover, at least some of the profit derived from this rent-setting is applied to LDC commodity charges, further reducing the LDC's apparent rates.

- In addition to the inequitable allocation of upstream assets and the application of specious credits by LDCs, LDC charges have never been fully unbundled, resulting in a significant number of issues that affect not only ESCOs and their customers but all market participants.

As many market participants have said, both during these proceedings and for the preceding two decades, the New York retail energy market suffers due to the fact that commodity prices are not fully unbundled from delivery prices. <u>The delivery charges paid by all ratepayers subsidize the commodity prices for those LDC customers who choose not to shop.</u> Furthermore:

- Lack of complete unbundling also results in ratepayers, their advocates, regulators, and other market participants being unable to evaluate, let alone assess, LDC charges. As made clear by its statements regarding information asymmetry in its Ratemaking Order, <u>not even the Commission can determine whether rates charged for *either* commodity or delivery are just and reasonable.</u> *This would be a problem worthy of Commission action even if New York had never opened to retail competition.*
- Profits from off-system sales, services provided to ESCOs, and other sources are shared with ratepayers primarily or exclusively as commodity credits. <u>Shopping customers are denied their share of credits and profit-sharing, despite the fact that their delivery charges contribute just as much to building the system and acquiring the assets that resulted in the profits.</u>
- Because LDCs can shift costs to delivery charges and credits to commodity charges, as well as profit from punitive imbalance penalties on ESCOs, LDCs are not the efficient, neutral, outcome-based "platform providers" envisioned by the Commission in its Ratemaking Order. Instead, <u>LDCs are incented to retain upstream assets and achieve earnings at the expense of ESCOs and shopping customers in any way possible.</u> This parallels the very policies that led to unbundling in most states and at the federal level, as well as to the prohibition on utilities making any profit on the commodity portion of their utility bills.
- As more system supply volume migrates to ESCO supply, credits and other price reductions applied to LDC commodity rates are divided across smaller and smaller volumes of gas. <u>LDC commodity prices thus reflect an artificial drop over time – a drop which today punishes ESCOs and their customers for moving toward the Commission's goal of voluntary migration from LDCs.</u>

As stated by the Commission in its Ratemaking Order, "the Commission has concluded that its core statutory duties can no longer be met with the utility regulatory model of the previous century." Infinite Energy wholeheartedly agrees, but respectfully asserts that the bold changes proposed by the Commission cannot hope to succeed so long as utility rates are left incompletely unbundled. If current LDC practices which allow LDCs to profit at the expense of third parties are allowed to continue, it is inevitable that those business practices and the problems they create will creep into the new model.

Neither the Commission, the LDCs, the consumers, nor third-party service providers can hope to find or create value, make or encourage effective choices, ensure efficiency, or address the question of information asymmetry if the two core elements of utility service – the platform costs that apply to all ratepayers, and the commodity costs that apply only to sedentary LDC customers – remain unbundled.

This is true whether the "platform" is the distributed electric grid of the Reformed Energy Vision or the pipes and distribution system of the natural gas sector. Likewise, it is just as true whether the "service costs" are commodity-only energy supply or the value-added services and other benefits pursued by the Commission.

Concluding Remarks

The New York energy market is one of the most complex of its kind. The Commission and its Staff have undertaken the arduous and often thankless task of righting a ship that set sail over twenty years ago. Infinite Energy respectfully submits that the Commission's retail market policy goals – as well as its mission to ensure affordable, safe, secure, and reliable access to electric and gas services for New York State's residential and business consumers – will be best met by truly leveling the playing field of the retail market. This can only be achieved by taking the step suggested, but not fully developed, in the Commission's Ratemaking Order – namely, creating an arm's length separation between the utility in its role as platform provider and the utility's operations team in its role as provider of commodity supply.

Infinite Energy appreciates this opportunity to address the Commission's concerns and to contribute to the latest and, ultimately, greatest effort to improve the New York retail energy market since its inception. Additional information and research will be provided in future filings in these proceedings, and will also be made available to the Commission and Staff upon request.

On Behalf of Infinite Energy,

Respectfully Signed,

Richard F. Paez

Infinite Energy, Inc. | Manager, Regulatory Affairs
7001 SW 24 Avenue | Gainesville, Florida 32607-3704
Phone: 352-331-1654 | Fax: (352) 313-6925
Regulatory@InfiniteEnergy.com | www.InfiniteEnergy.com

Dated: Wednesday, May 25, 2016

Appendix A – Comments on Proposed Reference Price Formula for 12 Month Fixed Rates

To the extent that reference prices are established as a stop-gap until utility prices can be fully unbundled and appropriately allocated, Infinite Energy respectfully shares the following suggestions and concerns regarding Staff's proposal.

- Future start dates must be taken into account. For example, the NYMEX futures are different for the 12 month period beginning in July 2016 and for the 12 month period beginning August 2016. Customers should not be limited to reference prices approved only for service start dates occurring six to ten weeks in the future. In theory, for each LDC and service class, Staff should compute a reference price for each 12 month period starting every month for the next 12 months, otherwise customers and ESCOs will be forced to do business only on the shortest of timeframes – a significant impediment to customer choice and the competitive market.
- While residential customers, in aggregate, are sufficiently similar within a given LDC's service area to be treated identically[7], this cannot be said of commercial customers. One of the key reasons that ESCO rates have been competitive in the commercial market segment even against the problematic LDC rates is because ESCOs have been able to individually price those customers based on their individual usage patterns, load factors, location, and other unique characteristics. These individual characteristics have a direct impact on how the ESCO can source the customer's natural gas, manage upstream assets, and thus price the customer.
- For similar reasons, limiting ESCOs to 12 month fixed rates is highly problematic, especially in the commercial market segment. Frequently, ESCOs will be able to structure fixed rates that, by virtue of being shorter or longer than one year, position the customer's usage and capacity releases in a manner that allows the ESCO to pass significant savings to the customer.
- Basis must account for the fact that ESCOs are required to source gas from different receipt points. An ESCO may be required, for example, to source gas from multiple receipt points, each with its own basis.
- Capacity, as much as commodity and basis, must be load-weighted. ESCOs assume the cost of all unused capacity that is released to them, with no guarantee of cost recovery on the excess capacity. This is one of the core reasons why commercial customers are individually priced in the competitive market – whether an ESCO prices some or all of the cost of the excess capacity into the customer's rate, takes the risk of assuming the cost based on the ESCOs predictions of wholesale market opportunities, or takes some other action is a key component of an ESCO's proprietary treatment of each individually priced customer.
- Example: Customer A is assigned 1,500 dekatherms of capacity but has a load factor of 50%. Assuming a weighted average cost of capacity ("WACOC") of $0.50 per dekatherm, the ESCO serving Customer A would be charged $750 for the released capacity. However, they would only be allowed to charge the customer the $0.50 WACOC for the 750 dekatherms of gas the customer actually used. The *effective* cost of the capacity released to the ESCO for that specific customer is actually $1.00 per dekatherm. The ESCO would be unable to make market-based decisions whether to negotiate a price with the customer that included some or all of the excess $0.50 per dekatherm. No matter the potential market value (or lack thereof) of the specific excess capacity (i.e., geographical location, time of year during which excess capacity is available, market conditions, etc), the ESCO will have no choice but to take an unhedgeable

[7] We note, however, that many LDC's tariff rates differentiate even within the residential class, treating heating and non-heating customers as different service classifications that are served at different rates.

gamble that the excess capacity in question can be positioned to recoup the ESCO's costs. And unlike the utility against which the ESCO is supposedly competing, the ESCO which takes a loss on unprofitable excess capacity cannot petition the Commission for a prior-period adjustment to recoup its losses.

Infinite Energy stresses that the proposed formula, especially for commercial customers, will result in reference prices which are either so high as to be meaningless or so low as to make ESCOs incur an untenable degree of risk – especially if the assumption is made that ESCOs are guaranteed wholesale market returns in a manner that is in any way comparable to how utilities are guaranteed administrative cost recovery.

Appendix A.1 – Proposed Reference Price Formula for 12 Month Fixed Rates

REFERENCE PRICE ($R_{U,M}$) = $D_U + (C + B_U)*F_U*W_U + P + M + Y$.

$R_{U,M}$	=	Reference price at Local Distribution Company (LDC) U's franchise area for the 12-month period beginning in month M.
D_U	=	Weighted average Cost of pipeline capacity for LDC U, including fuel/line loss factor.
C	=	NYMEX or ICE Futures commodity price.
B_U	=	Basis forecast from CME Group.
F_U	=	LDC Fuel and Line Loss Factors.
W_U	=	Weather Risk at LDC U's franchise area.
Y	=	charges to ESCOs for balancing services and applicable managed storage services.
P	=	Premium includes supplier margin and MFC related costs, including purchase of receivables and billing.
M	=	Cushion to limit price gouging.

- The cost of capacity that is released to the ESCOs can be obtained from each LDC's tariffs/statements or pipeline tariffs.
- The commodity price and the basis forecast are load weighted to reflect higher consumption and higher costs in the winter.
- Fu Factor reflects losses in the LDC's distribution system. Fuel and Line Loss factors can be found in the LDCs' tariffs.
- Factor P will be decided periodically by the PSC, based on need. The other factors will be updated as shown. Update periods may change based on circumstances.
- Weather Risk Premium Factor varies by area. Weather Risk factor ranges from 1.05 to 1.10 (or 5-10% of the commodity cost).