

DIRECT TESTIMONY OF JOHN R. HANGER

1 Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

2 A. My name is John R. Hanger. I operate Hanger Consulting LLC, and my
3 business address is 637 Zurich Drive, Hummelstown, PA 17036.

4 Q. PLEASE DESCRIBE YOUR PROFESSIONAL BACKGROUND.

5 A. My professional experience includes service in four (4) public positions or
6 offices. First, I was the Public Advocate for Philadelphia's 500,000
7 municipal gas as well as water and sewer customers from 1986-1988. My
8 duties included organizing testimony and trying cases before the
9 Philadelphia Gas Commission and Pennsylvania Public Utility
10 Commission. Cases included base rate cases, fuel cost proceedings, capital
11 budgets, customer service rules and regulations, and low-income
12 assistance programs, including conservation. Second, I was nominated to
13 the Pennsylvania Public Utility Commission and served as a commissioner
14 from 1993 to 1998, where I played a leading role in restructuring
15 Pennsylvania's electricity industry and initiating competitive retail electric
16 and gas markets. As a Commissioner, I wrote major electricity
17 restructuring motions that were the foundation of Commission
18 restructuring orders. In addition, I decided hundreds of electricity, gas,
19 water, sewer and telephone cases. Third, I also served as Secretary of the
20 Pennsylvania Department of Environmental Protection from 2008-2011.

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1 During this time, I promulgated major new regulations regulating gas
2 drilling in Pennsylvania and permitted shale gas wells and oversaw the
3 distribution of \$130 million of federal energy funding from the 2009
4 American Recovery and Reinvestment Act for energy efficiency and
5 renewable energy programs. From 2008 to 2011, I also served as the Chair
6 of Pennsylvania's Energy Development Authority, Chairman of
7 Pennsylvania's Board of Coal Mine Safety and Vice-Chair of
8 Pennsylvania's Infrastructure Investment Authority that made large
9 investments in especially water and sewer systems. I also advised
10 Governor Rendell concerning the drafting and adoption of Act 129,
11 Pennsylvania's electricity energy efficiency law. Fourth I served as the
12 Governor Wolf's Secretary of Policy and Planning from January 2015
13 until February 2016. My responsibilities included energy, utility and
14 environmental policy-making. I have also been employed as an attorney
15 by Community Legal Services in its Energy Project from 1984-88; as the
16 legal advisor to PAPUC Commissioner Joseph Rhodes from 1988-1993;
17 President of Citizens for Pennsylvania's Future from 1998 to 2008; and as
18 Special Counsel by the law firm of Eckert Seamans from 2011 to 2014. I
19 am currently President of Hanger Consulting LLC.

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1 Q. WHAT IS YOUR EDUCATION?

2 A. I graduated from Duke University in 1979, with an A.B. degree, majoring
3 in Public Policy Studies and History. I also graduated in 1984 from the
4 University of Pennsylvania School of Law. I am admitted to practice law
5 in Pennsylvania.

6 Q. ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS
7 PROCEEDING AND BY WHOM ARE YOU EMPLOYED AND IN
8 WHAT CAPACITY?

9 A. I am submitting this testimony on behalf of Direct Energy Services, LLC,
10 Direct Energy Business, LLC, Direct Energy Business Marketing, LLC,
11 and Gateway Energy Services Corporation (collectively, "Direct Energy").
12 Direct Energy is one of the largest competitive retail and wholesale
13 providers of electricity, natural gas, and home and business-related energy
14 efficiency services with over 4 million customers in North America. It
15 also provides commercial solar solutions and has provided residential
16 solar solutions across the Northeastern United States. Direct Energy
17 serves more than 240,000 residential, small commercial, large
18 commercial, and industrial electricity and natural gas customers in New
19 York.

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1 Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

2 A. My testimony provides recommendations for improving the residential
3 electricity and natural gas markets in New York, in response to the issues
4 noted in the December 2, 2016 Notice issued by the Secretary of the
5 Commission (“Notice”). These recommendations include actions to
6 implement stronger protections for residential consumers, improve the
7 retail competitive market to benefit consumers, and advance the clean
8 energy and other goals of New York’s Reforming the Energy Vision
9 (“REV”) initiative. The testimony also answers some of the questions
10 posed by the Commission in the Notice. The testimony supports reforming
11 and improving retail energy markets but opposes heavy-handed measures
12 that would effectively eliminate retail competition for mass-market
13 customers and deny consumers the ability to choose their own energy
14 future. Adopting the utility default rate as a cap on ESCO prices, either as
15 an explicit cap on the unit price of energy or as a cap on the amounts
16 ESCOs could bill to customers over time, is one such policy that would
17 destroy New York’s retail electricity and natural gas markets for
18 residential and small business customers. New York utilities’ default
19 service is a monthly-variable-rate product with, during the period of time
20 examined in this case, no green content beyond that provided by the
21 system generating mix, and with no price disclosure to consumers until

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1 after the consumer consumes the energy and receives a utility consolidated
2 bill. Using the rate for such a service as a cap on ESCO prices would be
3 poor public policy and would certainly harm consumers. The goal of this
4 proceeding should be to enact rules and policies that build the electricity
5 and natural gas marketplace of the future. Those marketplaces will be
6 driven by empowered consumers, who have data, technology, and the
7 power of choice to decide how best to consume energy services. Effective
8 markets that empower consumers will bring private investment to the task
9 of financing infrastructure deployment. New York has not yet created that
10 marketplace, but it has begun the journey by most importantly giving
11 consumers the legal right to choose their energy supplier and ending the
12 monopoly on generating electricity.

13 This journey is not without effort, but New York's clean energy and REV
14 goals cannot be achieved by dismantling retail energy markets and turning
15 back to a system that relied only on the monopoly utility to fulfill
16 important public policy goals. Well-meaning price intervention in markets
17 is a siren song always present that creates temptations in the moment.
18 Yielding to those temptations and having the Commission effectively set
19 prices will destroy efficiency, innovation, and the power of markets to
20 transform energy technology, products, and services. Caution about price
21 intervention is especially important and necessary given the Commission's

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1 desire to spur innovation and encourage more value-added products as
2 well as the need to implement REV and clean energy goals. This
3 testimony offers workable alternatives to banning ESCOs from offering
4 products, regulating them as though they were utilities with monopoly
5 power by requiring certificates of public convenience and necessity, or
6 setting pricing rules that will drive most or all ESCOs out of the market.

7 Q. YOU STATE THAT YOUR RECOMMENDATIONS ARE FOR
8 IMPROVEMENTS TO THE RESIDENTIAL MARKET. THE NOTICE
9 INCLUDES CONSIDERATION OF THE SMALL BUSINESS
10 MARKET AS WELL. DO YOU HAVE ANY RECOMMENDATIONS
11 FOR THAT MARKET?

12 A. Only one, which is to leave it alone. I was very disturbed by the Notice's
13 inclusion of the small business sector in this particular investigation.
14 From my review of the Commission's various actions over the past several
15 years, I can find absolutely no justification for concluding that the small
16 business market is not working effectively. Indeed, the Commission has
17 cited no evidence whatsoever specific to the small business sector in any
18 of the major orders on the retail market since the beginning of 2014 (and
19 here I have in mind the orders issued by the Commission in the current
20 dockets in February 2014, February 2015, and February 2016). This

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1 strikes me as an egregious example of regulatory over-reach that should
2 firmly be rejected by the Commission in this case.

3 There is a difference between residential consumers making purchasing
4 decisions for their homes and business people managing the various costs
5 of running a business. There is no evidence that small business people are
6 any less capable of making intelligent purchasing decisions with respect to
7 electricity and natural gas service than they are in making purchasing
8 decisions about rent, fixtures and other inputs into whatever product or
9 service they are selling. If the Commission should be wary about
10 excessive intervention in any market, it should be doubly wary of
11 intervening in markets where no evidence has been presented which would
12 prove that these customers do not have the sophistication and access to
13 resources such as brokers and trade organizations that might not be
14 available to residential customers. The prospect of eliminating fixed price
15 service for small business customers is of great concern. Small businesses
16 count on fixed price service to manage their energy costs with budgetary
17 constraints. Making the small business market a collateral victim of
18 concerns about the state of the residential market would be a terrible
19 mistake, and I urge the Commission in the strongest terms to avoid
20 making it.

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1 Q. HOW IS THE REMAINDER OF YOUR TESTIMONY ORGANIZED?

2 A. The rest of my testimony is divided into five sections:

3 **I. Strengthened Consumer Protections** – In this section I describe
4 several measures that would strengthen the protections available to
5 residential customers in New York and boost their confidence in the
6 competitive market. This confidence is critical for the creation and
7 maintenance of robust markets, and is especially important now in New
8 York where consumers have been hearing what I consider to be
9 misleading and unhelpful statements, to the effect that ESCOs are
10 supposedly harming customers and that customers would be better off not
11 shopping, which is definitely not the case.

12 **II. Improved Approach to Variable Pricing** – Monthly variable pricing,
13 whether it is provided by utilities through default service or by ESCOs,
14 poses certain challenges to residential customers when it comes to
15 transparency and notice. I make several recommendations for improving
16 the experience of New York residential customers served on monthly
17 variable products.

18 **III. Measures to Improve Customer Knowledge** – Despite the fact that
19 the New York market has been restructured for some time, I have
20 concluded that residential customers would benefit greatly from measures

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1 that would increase their level of knowledge about how the retail market
2 works and how they can use it to meet their individual energy needs. In
3 this section I describe several measures for achieving this goal.

4 **IV. Healthy Retail Energy Markets are Essential to Achieving New**
5 **York’s REV and CES Goals** – This investigation is not occurring in a
6 vacuum. It is taking place against the backdrop of Governor Cuomo’s
7 very ambitious energy agenda, which includes REV and the Clean Energy
8 Standard (“CES”), which has shifted, beginning in 2017. the obligation of
9 complying with the State’s clean energy portfolio standard to load-serving
10 entities. Meeting the goals of these initiatives will be very difficult, if not
11 impossible, if the Commission takes actions in this docket that effectively
12 drive competitive retailers out of the mass-market in New York.

13 **V. Answers to Certain Questions in the Notice** – In this section, I
14 respond to several of the specific questions posed in the Notice,
15 specifically those related to the regulatory framework around the ESCO
16 market and the idea of requiring ESCOs to provide certain kinds of
17 products as a condition of doing business in New York.

18

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1 **I. STRENGTHENED CONSUMER PROTECTIONS**

2 Q. WHAT NEW CONSUMER PROTECTIONS DO YOU RECOMMEND?

3 A. I have three broad recommendations for stronger consumer protections:

- 4 • Oversight of mass-market energy markets and enforcement of
- 5 consumer protections should be strengthened by annually assessing a
- 6 fee charged to ESCOs to pay for more staff to conduct oversight and
- 7 enforcement;
- 8 • The requirements for ESCO eligibility to serve customers and
- 9 participate in the market should be raised; and
- 10 • Improvements should be made in the oversight of residential door-to-
- 11 door and outbound telemarketing sales.

12 Q. YOUR FIRST CONSUMER PROTECTION RECOMMENDATION IS

13 TO INCREASE OVERSIGHT OF THE MARKET AND ENHANCE

14 ENFORCEMENT OF REGULATIONS PROTECTING CONSUMERS.

15 PLEASE DISCUSS.

16 A. Strong rules protecting consumers are vital. Just as important as adopting

17 such rules is insuring ESCOs comply with those rules. I discuss below the

18 recommendation that ESCOs demonstrate effective compliance programs

19 to insure implementation of consumer protection rules in the marketplace.

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1 Yet, more should be done. The Commission itself should increase staff
2 dedicated to the oversight of retail energy markets and enforcement of
3 consumer protection rules. I recommend that the Commission impose an
4 assessment to help pay for this effort. This assessment could be imposed
5 on a customer-count basis and collected from ESCOs as a condition of
6 obtaining and or maintaining one's eligibility to do business in New York.
7 An initial budget of \$500,000 to \$750,000 should allow for a significant
8 increase in oversight of the retail market and enforcement of regulations.
9 As this case has shown, there are billions of dollars of value at stake in the
10 New York electricity and natural gas markets, and requiring ESCOs to
11 make a small investment to improve the quality of ESCO performance and
12 boost confidence in those markets would be good for consumers and
13 ESCOs alike.

14 Q. YOUR SECOND RECOMMENDATION FOR STRONGER
15 CONSUMER PROTECTIONS IS THAT THE REQUIREMENTS FOR
16 ESCO ELIGIBILITY TO SERVE CUSTOMERS BE RAISED. PLEASE
17 DESCRIBE THE SPECIFIC CHANGES YOU RECOMMEND.

18 A. I recommend three specific ways in which eligibility requirements to serve
19 be raised: (1) posting financial security; (2) demonstrating necessary

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1 expertise; and (3) operating a robust compliance program to comply fully
2 with regulatory requirements.

3 Every ESCO should be required to demonstrate financial viability by
4 requiring each one to post financial security of up to \$5,000,000 and no
5 less than \$1,000,000, depending on the number of meters served. This
6 amount of financial assurance could be met through a performance bond,
7 letter of credit, or a corporate guarantee. Posting these amounts of
8 financial assurance would confirm compliance ability, provide customer
9 refunds, and deter dubious entrants or bad actors from entering the market
10 in the first place.

11 Q. PLEASE DISCUSS THE EXPERTISE DEMONSTRATION THAT YOU
12 RECOMMEND AS A REQUIREMENT FOR A COMPANY TO BE
13 ELIGIBLE TO SERVE CUSTOMERS.

14 A. It is important to never let into the market companies that don't have the
15 necessary expertise to effectively operate in New York's retail energy
16 markets. Consequently, in addition to posting financial assurance, every
17 ESCO should be required to demonstrate expertise necessary to serve
18 effectively energy customers. ESCOs should be required to demonstrate
19 expertise in energy operations like supervision of sales and marketing
20 activities, finance, supply hedging and customer service such as

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1 responding professionally to customer inquiries or complaints. I should
2 also be clear that by demonstrating expertise I mean more than simply
3 listing a name with a title that corresponds to one of the core areas of
4 expertise mentioned above. ESCOs seeking eligibility should be required
5 to provide background information showing the experience of those who
6 will hold positions of responsibility in the company, and make those
7 individuals available to answer questions from DPS Staff. To assist DPS
8 Staff in these efforts, I further recommend that the Commission consider
9 forming an ESCO Advisory Board composed of representatives from
10 stakeholders who have deep experience and expertise in the ESCO
11 industry. The Advisory Board would make itself available to Staff to
12 answer questions about the industry and to assist Staff in preparing a
13 protocol for reviewing ESCO applications and vetting the personnel of
14 prospective ESCOs.

15 Q. PLEASE DISCUSS YOUR RECOMMENDATION THAT A
16 COMPANY BE REQUIRED TO OPERATE A COMPLIANCE
17 PROGRAM TO PARTICIPATE IN NEW YORK'S RETAIL ENERGY
18 MARKETS.

19 A. The Commission rightly insists that rules written to protect consumers be
20 followed. While no company will operate error-free, every company

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1 should be fairly held accountable for its mistakes and be required to have a
2 compliance program to reduce or even eliminate mistakes. A robust,
3 effective compliance program within each ESCO to insure compliance
4 with applicable regulatory requirements is vital to protecting consumers.
5 Each ESCO should be required to describe its compliance program and
6 establish that it will adequately insure compliance with regulatory
7 requirements. ESCOs are currently required to provide a copy of their
8 Quality Assurance Program when applying for eligibility, but this
9 requirement must be strengthened to ensure that the ESCO has more than
10 just a written plan. The ability to implement such a plan effectively, using
11 processes that can be demonstrated to do what the ESCO claims they can,
12 overseen by personnel with experience and expertise in achieving
13 compliance in a complex regulatory environment is critical to protecting
14 customers and building trust in the market, and an ESCO should be
15 required to show that it can do these things in order to obtain or maintain
16 the ability to do business in New York.

17 Q. YOUR SECOND RECOMMENDATION FOR STRENGTHENING
18 CONSUMER PROTECTION IS TO IMPROVE THE OVERSIGHT OF
19 CERTAIN SALES CHANNELS. WHAT MEASURES DO YOU
20 PROPOSE IN THIS AREA?

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1 A. I recommend improvements in the oversight of door-to-door sales and
2 outbound telemarketing activities. Regarding door-to-door sale,
3 substandard practices in this sales channel can damage consumer
4 confidence in retail energy markets. While such in-person sales can
5 provide a very positive customer experience if done well, if done poorly,
6 the nature of the channel makes a bad customer experience extremely
7 damaging to the reputation of the ESCO involved in the sale and the
8 overall ESCO industry. Direct Energy and I support previous reforms like
9 requiring voice-recorded verification by either an independent Third Party
10 Verification (TPV) or Integrated Voice Response system of all sales
11 contracts initiated through door-to-door marketing. I recommend that the
12 compliance program of any ESCO engaged in door-to-door selling should
13 specifically address how all applicable regulations will be followed when
14 door-to-door marketing is conducted. I further recommend that (1) an
15 additional \$1,000,000 in financial assurance be required of any ESCO
16 engaged in door-to-door selling; and (2) the Commission issue twice a
17 year “Best Practice Guidelines” for door-to-door sales, such as regular
18 background checks for all sales agents, geo-location tracking of all sales
19 agents, and voice-recorded verification of all sales with updates to the
20 Uniform Business Practices (“UBPs”), to establish the most current and
21 best practices for door-to-door sales. Based on my understanding of the

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1 regulatory structure in New York, I believe it would be best if these
2 Guidelines were informal and voluntary so that they could be issued
3 quickly in response to the evolving understanding of DPS Staff and
4 ESCOs themselves about experiences with door-to-door sales in the field.
5 However, the UBPs should be clear, by amendment, if necessary, that an
6 ESCO that fails to meet minimum standards of conduct when using the
7 door-to-door sales channel will be subject to appropriately severe
8 consequences, such as the loss of the ability to post its prices on the DPS
9 rate board. Finally, I recommend that a collaborative discussion be
10 opened with the industry about door-to-door best practices and
11 compliance.

12 Q. WHAT IS YOUR RECOMMENDATION REGARDING OUTBOUND
13 TELEMARKETING?

14 A. While the total number of consumer inquiries or complaints that are not
15 resolved by ESCOs is a small number that represents a tiny fraction of
16 total energy customers in New York, or even of the customers served by
17 just ESCOs, the Commission identified telemarketing as a sales channel
18 that can be misused. The Commission rightly seeks to protect consumer
19 confidence in participating in retail energy markets. Direct Energy and I
20 share this goal of protecting consumer confidence. Requiring that all

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1 outbound telemarketing calls be recorded and that those recordings be
2 preserved for enough time to help solve any customer problems can serve
3 to insure regulations are being followed. Doing so can also help to resolve
4 some inquiries or complaints. Recording can increase the accuracy and
5 integrity of communications engaged in through outbound telemarketing
6 and build consumer confidence in market participation.

7 **II. IMPROVED APPROACH TO VARIABLE PRICING**

8 Q. PLEASE DISCUSS VARIABLE RATES AND THEIR ROLE IN THE
9 NEW YORK RESIDENTIAL ENERGY MARKET.

10 A. Variable rates play a central role in the New York energy marketplace.
11 Variable rates play this central role for two reasons: (1) the default product
12 offered by New York utilities is a variable rate product, and the great
13 majority of residential customers are on default service, paying monthly
14 variable rate bills, and (2) many ESCO customers are on variable rate
15 plans, either because the plan they purchased was variable from the
16 beginning of service with the ESCO or because they started off on a fixed
17 price and were transitioned to a monthly variable rate plan at the end of
18 the fixed price term, pursuant to the terms of their contract.

19

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1 Q. WHY DO UTILITY RATES MATTER IN THIS CASE?

2 They matter first and foremost because the Commission itself has, in its
3 previous orders, viewed the utility default service rate as the most
4 important, if not sole, benchmark of the health of the retail mass-market.
5 In its February 23, 2016 Order, the Commission adopted the utility default
6 rate as a de facto price cap on all ESCO service provided to residential and
7 small business customers unless, for electric service only, the power sold
8 included 30 percent renewable content. Thus, to explicate my
9 recommendations for improvements to variable pricing, it is necessary to
10 discuss the characteristics of utility default service in some detail, as my
11 recommendations **do not** include the suggestion the ESCO prices should
12 be in any way tied to, much less capped by, utility default service rates.

13 Q. IS IT REASONABLE TO COMPARE MONTHLY DEFAULT
14 PRODUCTS TO ESCO PRODUCTS OF ANY KIND?

15 A. No. Both the nature of the default service product and the cost structure of
16 the utilities' default service businesses makes such comparisons highly
17 inappropriate. The utilities' default products do not include basic costs
18 ESCOs incur when they operate in a competitive market. Utility default
19 service incurs no customer acquisition costs. This was true both at the
20 beginning of the market, when all customers were placed on default

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1 service at no cost to the utility, and on an ongoing basis, as when new and
2 moving customers are placed automatically on default service rather than
3 being given the option of starting service with an ESCO. Default service
4 rates do not include all the overhead costs that would be required to
5 operate a retail electricity or natural gas business on a stand-alone basis,
6 and default service earns no profit or return on its sales. Even for the cost
7 categories included in the utilities' default rates that might be similar to
8 costs incurred by ESCOs (e.g., customer service and billing), it is difficult
9 or impossible to determine if these services, which are shared with the
10 regulated delivery business, are being allocated pursuant to appropriate
11 transfer pricing principles. Furthermore, the Commission has, on
12 occasion, allowed or required utilities offering default service to defer
13 recovery of costs to soften increases in default rates in periods of sharp
14 increases in wholesale prices like those that occurred in the 2014 Polar
15 Vortex.

16 The Commission also allows utilities to true-up default revenues and costs
17 and recover any under-collection in subsequent months. This distorts any
18 comparison between utility default rates and ESCO prices, especially
19 where ESCOs are selling fixed price service as an alternative to volatile
20 default service rates and the Commission grants default service a reduction
21 in volatility on a post hoc basis and at less cost than the utility would have

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1 paid to reduce price volatility on a prospective basis, (The utilities were
2 allowed to recover carrying costs on the deferral but avoided the costs
3 of the hedges they would have had to acquire beforehand to smooth the
4 default service rate in the same manner.) Such regulatory interventions
5 undermine the reasonableness of comparing the default monthly variable
6 rate products to ESCO products, as DPS Staff and others have done,
7 without regard to the kind of service provided by the ESCO.

8 ESCOs have no such ability to shift costs so liberally from one time period
9 to another or from one group of customers to another. An ESCO must
10 recover the costs of providing service to customers solely from the
11 revenue earned from billing customers for the service provided in any
12 given period of time. Attempts to shift costs to other time periods or other
13 groups of customers will only increase prices during that later time period
14 or for that other group of customers, increasing the risk to the ESCO of
15 losing customers to price competition from other ESCOs and utility
16 default service, resulting in less total revenue rather than more. This is the
17 most fundamental difference between ESCOs and utility default service
18 and I hasten to emphasize that **this is a very good thing!** Looked at from
19 a customer's perspective, which is most appropriate here, the essential
20 difference between ESCOs and utility default service is that ESCOs make
21 commitments and deliver results to customers that utilities cannot. An

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1 ESCO can deliver a customer 12 or 18 or 24 or 36 months of fixed price
2 service, taking the risk of price fluctuations away from the customer. An
3 ESCO can deliver electricity with 100 percent renewable content. An
4 ESCO can deliver a smart thermostat as part of a price plan that also
5 provides a fixed price, helping the customer lower his or her energy
6 consumption while also being protected against price fluctuations. An
7 ESCO can deliver even non-energy related benefits to customers who
8 value those things, whether that be gift cards (which are like cash up front)
9 or airline miles or points in other loyalty programs. An ESCO can deliver
10 non-price related benefits, like information about the customer's energy
11 consumption and suggestions for how the customer can save on their
12 energy costs, or ease of service or more customer-friendly terms and
13 conditions.

14 So yes, in my view it is very poor public policy to focus solely on the
15 price of utility default service as the main or even an important measure of
16 the health of the retail market in New York. It is all trees, no forest,
17 especially where the forest is dominated by utility default service, which
18 currently enjoys an 80 percent market share among residential customers.
19 Instead of asking why the 20 percent of residential customers on ESCO
20 service aren't paying exactly what they would pay on default service – or
21 less – I would encourage the Commission to ask why the 80 percent of

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1 residential customers on default service aren't getting the benefits that the
2 20 percent have gotten through the free exercise of their ability to choose
3 among a broad range of ESCO offerings.

4 Q. IF YOU DO NOT BELIEVE ESCO PRICES SHOULD BE CAPPED BY
5 UTILITY DEFAULT RATES, WHAT RECOMMENDATIONS DO
6 YOU HAVE FOR REFORMING ESCO VARIABLE PRICING?

7 A. I have several recommendations. But first, to be clear, I do not
8 recommend having the Commission disallow consumers from buying or
9 taking service through a variable rate product supplied by an ESCO.
10 While some consumers may benefit from other products, it is critical to
11 maintain the flexibility for those consumers who see value in the variable
12 rate pricing product to continue to get this service type. As each consumer
13 is unique in their needs and wants, restricting an entire category of product
14 is detrimental to the market and to consumers. Here are some specific
15 recommendations.

16 • **The Commission should clarify that ESCOs are able to renew**
17 **customers who bought a fixed rate plan onto another fixed rate**
18 **plan.** The Commission notes that variable rate products supplied by
19 ESCOs have led to consumer complaints concerning high prices or no
20 savings. It should be recognized that many ESCO customers who are

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1 on monthly variable price products are on them because they did not
2 respond to notices informing them that their original fixed rate product
3 is expiring and it is time to renew to a subsequent fixed rate product.

4 To reduce the number of customers on variable rate products, I
5 recommend two actions.

- 6 ○ First, the Commission should clarify that the UBPs currently allow
7 ESCOs to renew customers from a fixed price plan to a subsequent
8 fixed price term at a new price, provided that all of the terms and
9 conditions of the service are the same. I believe the rules are fairly
10 clear in this regard. However, there appears to be some doubt about
11 this among the ESCO community, and it is possible that some ESCOs
12 are selling customers plans in which they roll from fixed to variable
13 price service under the mistaken belief that rolling from fixed to fixed
14 is not allowed by the UBPs.
- 15 ○ Second, the UBPs should be modified to also allow ESCOs to renew a
16 customer who is on a fixed rate product to a standard, reasonable fixed
17 price term that might be shorter than the initial term. A reasonable
18 term could be three to six months. This would provide ESCOs with an
19 incentive and a mechanism to auto-renew customers who may have
20 been on relatively long-term fixed price plans (and there are plans in

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1 the market that offer a fixed price for up to 36 months) to a fixed price
2 plan, even if its terms is shorter than the initial term.

3 • **The Commission should provide reasonable reforms to prevent**
4 **unforeseen consequences to customers who may not fully**
5 **understand the characteristics of variable service.** Reform options
6 for variable rate products in New York include:

- 7 ○ Requiring ESCOs to disclose the price of any variable rate product
8 before the beginning of the month in which the price applies;
- 9 ○ Establishing ESCO price “guardrails” for variable rate products
10 that limit how much an ESCO variable rate product can increase
11 from month-to-month;
- 12 ○ Banning the sale of variable rate products to customers who are
13 Assistance Program Participants (which has effectively occurred
14 already, with the Commission’s December 16, 2016 Order, unless
15 the variable products comes with a guarantee of savings versus
16 default service and the ESCO has received a waiver to provide it);
17 or
- 18 ○ Prohibiting their sale to any residential customer.

19 Again, restricting variable rate products in their entirety is a draconian and
20 ultimately harmful step, and should not be pursued. From the options
21 above, I would recommend enhanced education about variable rates and

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1 variable rate products, prior to sale, through Commission approved
2 marketing and consumer education materials. While my preference would
3 be to not intervene in any manner in ESCO pricing, if the Commission
4 disagrees, the Commission could impose, for a trial period, guardrails that
5 limit how much a rate can increase in any one month. A possible starting
6 point for the maximum amount a variable rate could increase in any one
7 month could be 30%, a potentially large substantial increase, but it is a
8 limiting guardrail; ESCOs could of course decide to limit any month-to-
9 month variation less than the 30%. Having a limit on month-to-month
10 adjustment provides time so that the consumer could receive a monthly
11 bill and could prevent any further increase by either switching to a fixed
12 rate product, or switching to another product offered by a competing
13 ESCO, or by returning to the utility default rate that is a variable rate
14 itself. If the Commission implements a variable rate guardrail or
15 monthly increase cap, the Commission should test that cap in the
16 marketplace. After testing in the marketplace a guardrail rule for perhaps
17 six to twelve months, the Commission should review whether the rule has
18 been effective in reducing complaints and increasing customer confidence
19 in the market.

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1 **III. MEASURES TO IMPROVE CUSTOMER KNOWLEDGE**

2 Q. YOUR RECOMMENDATIONS ABOUT VARIABLE RATES
3 PROVIDE REFORMS BUT SHOW CAUTION IN THE FORM AND
4 DEGREE OF INTERVENTION. WHY?

5 A. I recommend caution about intervening deeply in retail energy markets
6 and the pricing in those markets, as a general principle. Retail markets
7 already provide value-added products like renewable and fixed-term
8 products. They further provide a mechanism to bring additional private
9 capital to help reduce the ratepayer costs of decarbonization, distributed
10 generation, and energy efficiency. The rules of any markets determine
11 how they function and how well they advance consumer welfare and
12 environmental protection. The focus now should be on identifying
13 reforms that improve retail markets, while avoiding those changes (such as
14 adopting the utility default rate as a cap on ESCO prices) that predictably
15 or unintentionally destroy the value already created and the opportunity
16 for further value creation.

17 Q. ARE THERE ANY CHANGES THAT WOULD IMPROVE
18 COMPETITION IN RETAIL ENERGY MARKETS THAT YOU
19 WOULD RECOMMEND IN ADDITION TO THE ONES DISCUSSED
20 ABOVE IN SECTIONS I AND II?

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1 A. Yes. I recommend several further changes that focus on increasing
2 consumer knowledge. This is critical, as any well-functioning market is
3 the agglomeration of many decisions made by individual consumers
4 making their own choices about what is important to the among the things
5 offered in the market. The more consumers know about what the market
6 offers and how it works the better they will be able to use the market to get
7 more of what they want and less of what they don't want. That should be
8 the Commission's goal in this case, rather than second-guessing consumer
9 choices based on arbitrary benchmarks such as the utility default service
10 rate.

11 With that in mind, as I've already discussed above, more price information
12 would benefit consumers, competition, and innovation in the marketplace.
13 The transparency of ESCO residential pricing should be increased by the
14 Commission reporting monthly on its website the range of offered
15 electricity prices by utility service territory. The Pennsylvania Public
16 Utility Commission (PAPUC) does this at www.papowerswitch.com. Still
17 another shopping guide is operated by the Pennsylvania Office of
18 Consumer Advocate, an office within Pennsylvania's Attorney General, at
19 <http://www.oca.state.pa.us/Industry/Electric/elecomp/ElectricGuides.htm>.
20 The PAPUC and PAOCA shopping guides have features that alert
21 consumers to possible savings offered by ESCOs and that help consumers

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1 to compare ESCO products and to compare ESCO products to default
2 rates. For example, the PAOCA shopping guide tells consumers how
3 much every ESCO product and default product will cost on a monthly
4 basis, assuming usage of 500, 1,000, and 2000 kilowatt-hours. New York
5 has a shopping website maintained by DPS Staff already, which is a good
6 start, but it could be greatly improved to make shopping easier and more
7 efficient. For example, the Commission could consider having the website
8 list not only each competitive offer and its basic terms but also state the
9 lowest, median, highest and weighted-average price of ESCO products in
10 various categories like variable rates, fixed-term products, renewable
11 energy products, and other energy-related value-added services. The New
12 York Power To Choose website could also incorporate some of the
13 features in the PAPUC and PAOCA sites that help consumers identify
14 possible savings and make comparisons among product offerings. ESCOs
15 would be required to provide the Commission the information necessary to
16 publish this monthly report. These enhancements would allow customers
17 to compare like plans with like, and to more clearly understand the
18 differences in pricing not only among different ESCOs and different plans
19 but among different types of products. In this way, customers could more
20 easily see that, for example, comparing a variable-rate product to a fixed-
21 rate product is like comparing a heavy weight boxer to a bantam weight or

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1 comparing someone with the bare minimum auto or health insurance to
2 someone with policies that provide maximum protection. There are
3 fundamental differences in product type that drive differences in pricing,
4 and the more the Commission can do to help customers understand these
5 differences the better. My understanding is that DPS Staff have very
6 recently made changes to the Department's shopping website, which I
7 have not yet had a chance to review fully. I am hopeful that the changes
8 go in the direction I am recommending. But it is also important for the
9 Department to work closely with stakeholders with the goal of constantly
10 improving the resources available to consumers on the website and
11 elsewhere in response to trends observed in the market.

12 Q. DO YOU RECOMMEND ANY OTHER REFORMS TO IMPROVE
13 THE COMPETITIVE MARKET?

14 A. Yes. The Commission should increase consumer education about default
15 products, the right to choose, and how to make good energy choices. I
16 would urge the assessment of a fee to finance significant on-going,
17 consistent consumer education. If a fee of \$1 or \$1.50 per year was
18 assessed for every meter in the state or for every mass-market customer, a
19 substantial program of education could be created. Better informed
20 consumers are vital to healthy retail energy markets. A reasonably

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1 financed consumer education program is not a luxury. It is a necessity for
2 healthy retail energy markets. Consumers must be educated that they have
3 a responsibility to read the terms and conditions of their service so they
4 understand the nature and term of the ESCO service they are buying.
5 These education efforts, which are discussed further below, should include
6 guidance to customers in how to read their bills and the need to monitor
7 the price the customer is paying for electricity or natural gas, especially
8 when that service is being provided pursuant to a variable price plan,
9 whether with an ESCO or by utility default service.

10 Q. APART FROM CONSUMER EDUCATION, WOULD YOU
11 RECOMMEND ANY OTHER REFORMS TO IMPROVE
12 COMPETITION?

13 A. I do.

14 First, customers should be able to enroll with an ESCO, without having
15 immediate access to a utility account number or bill. Enrollment should be
16 made possible using other information to locate an account and to verify
17 where necessary. This alternative is sometimes called “Enroll with your
18 wallet.”

19 Second, true accelerated switching should be implemented. In
20 Pennsylvania, a customer can switch in three days. In Texas, a customer

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1 can switch the same day they make the switch request or self-select the
2 day of their switch.

3 Third, smart meters should be rolled out to facilitate better consumer
4 experience, more value-added products, and innovation. Real-time access
5 to consumption data is essential for companies to offer a variety of
6 products that allow customers to save more by conserving energy at times
7 of high demand or by moving consumption to lower demand periods.

8 Fourth, customers, who move into a service territory and begin service,
9 should not be just assigned to utility default service, without their explicit
10 consent. These customers should be given a list of ESCOs, in addition to
11 the default product, and the information necessary to make a good choice.
12 Customers should choose and have that choice implemented when they
13 initiate service.

14 Fifth, procedures should be developed to allow customers to have
15 seamless moves and instant connects to retain their competitive supplier,
16 rather than returning first to the utility.

17 Sixth, ESCO consolidated billing would enhance the ability of ESCOs to
18 develop customer relationships that allow the offering of new and
19 innovative products and services.

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1 I would further recommend the return to a collaborative process in New
2 York where further reforms to improve competition and consumer benefits
3 could be developed through a working process of stakeholders devoted to
4 this topic and issues. The goal should be to improve retail energy markets,
5 as opposed to adopting measures that would limit or even end them.

6 Q. YOU HAVE URGED CAUTION IN MAKING CHANGES TO THE
7 RETAIL MARKET. IS IT POSSIBLE THAT YOU ARE BEING TOO
8 CAUTIOUS IN YOUR RECOMMENDATIONS?

9 A. Regarding the possible remedies suggested in the Notice, no, I do not
10 believe I am being too cautious. As discussed above in Section II, it
11 appears that the Commission is focused primarily on the difference
12 between ESCO prices and utility default service rates, with the option of
13 setting the utility default rate as a cap on ESCO prices perhaps under
14 active consideration. Price caps and other artificial restraints on prices set
15 by a market should always be approached with great caution. The same
16 can be said of artificial requirements for product mix. Dictating prices
17 ESCOs can charge or the kinds of products ESCO can or cannot sell
18 would be treating only whatever symptoms the Commission perceives of
19 problems in the market. But the relationship between utility rates and
20 ESCO prices and the product mix sold by ESCOs are result of the choices

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1 the Commission has made about market design over the years, and not
2 some nefarious plot by ESCOs to deprive New York residential customers
3 of value in the energy market. That is why the measures I am
4 recommending address the underlying features of the market rather than
5 trying to regulate the outputs of the market, which almost always does
6 more harm than good. Taking this approach is prudent and reasonable
7 given the stakes at issue in this case.

8 **IV. HEALTHY RETAIL ENERGY MARKETS ARE ESSENTIAL**
9 **TO ACHIEVING NEW YORK'S REV AND CES GOALS**

10 Q. CAN RETAIL ENERGY MARKETS BENEFIT NEW YORK'S REV
11 AND CLEAN ENERGY GOALS?

12 A. They most certainly can. Indeed, they are indispensable for New York to
13 achieve these goals as fast as possible and at the lowest cost possible to
14 utility ratepayers and New York taxpayers. Those markets, with
15 appropriate rules and market design, offer tremendous resources and
16 synergies to implement REV and for CES. An informed, educated and
17 engaged consumer is the most important resource that healthy retail
18 energy markets create. The second most important resource created by
19 healthy retail energy markets is a range of companies and managers plus
20 investors who compete for customers by creating more value. Engaged

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1 consumers and competing companies can drive forward New York's
2 ambitious REV and CES. This is especially true now that the CES has
3 shifted to load-serving entities the obligation to comply with New York's
4 aggressive goals for renewable and other low-carbon content electricity.
5 Bringing competitive pressure to bear on compliance with the renewable
6 portion of the CES is a measure I strongly support, but residential load
7 represents about 37 percent of all the load being served in the investor-
8 owned utility service territories, and effectively turning all of that load
9 back to utility default service eliminates any of the positive effects of
10 competition in that sector. In fact, one of the ironies of adopting the utility
11 default service rate as a cap on ESCO prices is that it creates a huge
12 disincentive for ESCOs to offer renewable content beyond the bare
13 minimum required by law. This would deprive residential customers of
14 the ability, through their individual buying decisions, to help New York
15 achieve its ambitious 30 by 50 goals ahead of schedule.

16 Q. DO YOU HAVE ANY RECOMMENDATIONS ABOUT MARKET
17 RULES OR DESIGN THAT WOULD PROMOTE ACHIEVING NEW
18 YORK'S REV OR CLEAN ENERGY GOALS?

19 A. I do. ESCOs, utilities, and Community Choice Aggregations (CCAs), or
20 all retail electric load-serving entities, should be required to reduce overall

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1 energy consumption by 1.5% versus a baseline. They should also be
2 required to deliver cleaner energy by a minimum margin of 1.5% above
3 any other applicable state standard, using renewable energy credits from
4 facilities built within the most recent two-year period for their mass-
5 market customers. The Commission should convene a collaborative to
6 develop rules for establishing the baseline and methods of measuring
7 energy reduction and compliance. This initiative should allow ESCOs to
8 deliver and comply on a portfolio or total load basis and would not require
9 ESCOs to comply on a customer-by-customer basis. ESCOs should be
10 allowed to make alternative compliance payments instead of achieving
11 targets. If an ESCO over-complies in one area, that over-compliance
12 should be transferable to another area and count toward compliance there.
13 Utilities should include all costs of compliance with this initiative in
14 default rates, and specifically not in distribution rates, so as not to distort
15 even further comparisons between ESCO products and default rates. In
16 addition, a collaborative could be formed to recommend whether this
17 requirement should be extended to retail natural gas suppliers and natural
18 gas distribution companies.

19

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1 Q. DO YOU HAVE A RECOMMENDATION CONCERNING
2 CONSOLIDATED BILLING FOR ESCOS?

3 A. The Commission should begin a proceeding to consider allowing ESCOs
4 to provide consolidated billing. Consolidated billing can support the
5 provision of value-added products or non-commodity-only products by
6 ESCOs. It does so by allowing ESCOs to develop a deeper and broader
7 customer relationship with energy consumers. Such relationships are the
8 foundation needed for consumers to have the experience and confidence to
9 innovate and to purchase clean energy of distributed energy products and
10 service. Direct Energy has an industry-leading electric bill that provides
11 consumers with easy-to-understand graphics and data to inform consumers
12 about their energy usage. This is a valuable tool for any state wishing to
13 promote conservation and informed choices, and all it requires is a smart
14 meter. As such, consolidated billing would be an important reform that
15 improves the consumer experience, spurs competition, boosts innovation,
16 and advances New York's clean energy and REV goals.

17 Q. DO YOU HAVE AN OPINION ABOUT SMART METER
18 DEPLOYMENT?

19 A. The Commission should endorse full smart meter deployment in all utility
20 service territories in a timely manner. Smart meters and the data they

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1 provide are vital to innovation in a whole range of areas, including energy
2 product offerings, energy efficiency services, and energy management
3 services. The Commission should declare that customers own the data and
4 ESCOs have an equal right to access that data, with the consent of the
5 customer. Smart meter deployment and equal access to that data will help
6 to achieve New York's clean energy and REV goals. It will also help to
7 create more vibrant, healthy retail energy markets.

8 **V. RESPONSES TO CERTAIN QUESTIONS POSED IN THE**
9 **NOTICE**

10 Q. THE NOTICE POSES SEVERAL QUESTIONS REGARDING THE
11 FRAMEWORK WITHIN WHICH THE COMMISSION REGULATES
12 ESCOS, INCLUDING WHETHER ESCOS SHOULD BE REQUIRED
13 TO OBTAIN A CERTIFICATE OF PUBLIC CONVENIENCE,
14 WHETHER ESCOS SHOULD BE REQUIRED TO GUARANTEE ITS
15 PRODUCTS WILL OFFER SAVINGS COMPARED TO THE
16 MONTHLY VARIABLE RATE UTILITY DEFAULT PRODUCT,
17 WHETHER ARTICLE 4 SHOULD BE APPLIED TO ESCOS,
18 WHETHER ESCOS SHOULD BE REQUIRED TO PROVIDE
19 TARIFFS, AND MORE. DO YOU HAVE A RESPONSE?

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1 A. My testimony to this point offers stronger consumer protections and
2 resources to enforce them, better consumer education to improve
3 consumer knowledge and performance and resources to provide it,
4 competitive market reforms to increase competition and consumer
5 benefits, such as greater price transparency, and mechanisms for
6 harnessing retail energy markets to achieving New York's REV and clean
7 energy goals. These measures protect consumers and improve retail
8 energy market design and operation. They do so without taking steps of
9 questionable legality that would also cause investment to flee New York
10 like applying Article 4 to ESCOs or requiring ESCOs to obtain a
11 certificate of public necessity. My recommendations move New York
12 forward on its journey from the past of vertically-integrated generation,
13 transmission and distribution monopolies, where customers were captured
14 and without influence, to the energy marketplace of the future, where
15 consumers are at its center, and where consumer preferences drive
16 investment, technology and innovation. They do not turn back to a failed
17 past of no markets, no consumer choice, little clean energy, and a glacial
18 pace for innovation.

19 Q. WHAT IS YOUR RECOMMENDATION ABOUT THE FIRST
20 QUESTION IN THE NOTICE, WHERE THE COMMISSION ASKS
21 WHETHER ESCOS SHOULD BE BANNED FROM OFFERING

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1 PRODUCTS OR, ALTERNATIVELY, BE REQUIRED TO OFFER
2 VALUE-ADDED ENERGY MANAGEMENT AND ENERGY
3 EFFICIENCY SERVICES?

4 A. My answer is an emphatic “no” to the question of whether ESCOs should
5 be banned from offering any of their current products. A number of these
6 products, such as fixed price plans and renewable energy plans, are clearly
7 bringing value to New York consumers, and ESCOs should be allowed to
8 continue providing them. Banning all current products would also create
9 unintended consequences, including a rising risk that capital will flee New
10 York. Were the Commission to ban ESCOs from offering products, the
11 result could be the collapse of the retail electricity and natural gas markets
12 and, ironically, the transfer of all mass-market customers to monthly
13 variable rate default service as a remedy for perceived problems caused in
14 large part by variable rate practices. Renewable energy products would be
15 gone. Fixed-price products would be gone. Let us remember that
16 consumers have had the opportunity to lock-in a price for 12 months, 24
17 months and even 36 months. Those product offerings alone offer
18 tremendous additional value to every consumer, whether they purchase
19 them or not. In addition, mandating that ESCOs offer still more value-
20 added products to do business would limit consumer choice and market
21 segmentation around consumer preferences. As to efficiency services, I

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1 have indicated that all retail generation suppliers, including utilities, could
2 be directed to reduce electricity consumption by 1.5% below an agreed to
3 baseline, with the details worked out in a collaborative. Establishing such
4 a standard is quite different from mandating certain products or services
5 be provided. Building standards and appliance standards are among other
6 appropriate ways for insuring that markets achieve minimum levels of
7 required energy efficiency. Markets, with producers and consumers,
8 should then be allowed to innovate to develop further value.

9 **VI. CONCLUSION**

10 Q. DO YOU HAVE ANY CONCLUDING THOUGHTS?

11 A. Oscar Wilde said: “Nowadays everyone knows the price of everything and
12 the value of nothing.” The value of retail energy markets in New York are
13 already considerable but can be increased substantially with reforms. The
14 Commission should focus on implementing reasonable reforms for ESCO
15 products, increasing consumer information and education; improved
16 regulatory oversight to deter improper sales practices; and enhancing
17 ability of competitive energy suppliers to serve customers via ESCO
18 consolidated billing and deployment of smart meters. Informed, active
19 customers can bring substantial private investment to the electricity
20 marketplace, thereby helping New York achieve its REV and carbon

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1 reduction goals, at the lowest possible cost to homes and businesses in
2 New York State. Now is the time to increase the size and performance of
3 retail energy markets in New York. Doing so will cement New York's
4 leading position in clean energy and electricity innovation.

5 Q. DOES THIS CONCLUDE YOUR TESTIMONY?

6 A. Yes, it does.