STATE OF NEW YORK
PUBLIC SERVICE COMMISSION

At a session of the Public Service Commission held in the City of Albany on April 18, 2007

COMMISSIONERS PRESENT:

Patricia L. Acampora, Chairwoman
Maureen F. Harris
Robert E. Curry, Jr.
Cheryl A. Buley

CASE 06-M-1017 – Proceeding on Motion of the Commission as to the Policies, Practices and Procedures For Utility Commodity Supply Service to Residential and Small Commercial and Industrial Customers.

ORDER REQUIRING DEVELOPMENT OF UTILITY-SPECIFIC GUIDELINES FOR ELECTRIC COMMODITY SUPPLY PORTFOLIOS AND INSTITUTING A PHASE II TO ADDRESS LONGER-TERM ISSUES

(Issued and Effective April 19, 2007)

BY THE COMMISSION:

BACKGROUND

In an Order Instituting Proceeding and Notice Soliciting Comments (Order Instituting Proceeding) issued August 28, 2006 in this proceeding, it was noted that electric utility hedging practices varied in their impacts on customers and on the development of wholesale and retail competitive markets. To address those impacts, it was determined that electric utility supply portfolio management practices would be considered further.

Electric utilities have been expected to manage their electric supply portfolios in conformance with the principles

established in the Retail Market Policy Statement,[1] where it was determined that electric utilities should maintain balanced commodity supply portfolios -- characterized as neither 0% nor 100% hedged -- for serving residential and small commercial and industrial (C&I) (collectively, mass market) customers. The Policy Statement also provided that larger C&I customers would be increasingly exposed to wholesale spot market pricing, a policy subsequently further developed for electric customers through the tariffing of hourly pricing mechanisms.[2] The demarcation separating the mass market customers requiring hedging protection from the larger C&I customers exposed to real-time pricing is individual to each electric utility, and is established for each of a utility's customer classifications in rate or other proceedings.

Besides addressing issues related to the various practices electric utilities have followed in complying with the Retail Market Policy Statement, the Order Instituting Proceeding noted that, in recent rate proceedings, parties have disputed the proper approach to formulating mechanisms for the recovery of commodity-related costs, including the cost and value of hedging arrangements. Disagreements have also arisen over disclosure of utility supply portfolio price information.

Although it was reported in the Order Instituting Proceeding that hedging practices adopted under the Gas Purchasing Policy Statement have generally worked well,[3] it was

---

[1] Case 00-M-0504, Development of Retail Competitive Opportunities, Statement of Policy on Further Steps Towards Competition in Retail Energy Markets (issued August 25, 2004).

[2] Case 03-E-0641, Mandatory Hourly Pricing, Order Denying Petitions for Rehearing and Clarification in Part and Adopting Mandatory Hourly Pricing Requirements (issued April 24, 2006).

[3] Case 97-G-0932, Gas Cost Volatility, Statement of Policy Regarding Gas Purchasing Practices (issued April 28, 1998).

determined a few issues affect gas utilities as well as electric utilities, and that those issues should be resolved for gas utilities at the same time they were resolved for electric utilities.[4]

Interested parties were invited to submit comments on the issues raised in the Order Instituting Proceeding by October 30, 2006, with replies due November 20, 2006. Those deadlines were later extended to November 17, 2006 and December 11, 2006, respectively. Moreover, Notice of the Order Instituting Proceeding was published in the State Register on September 20, 2006, in conformance with State Administrative Procedure Act (SAPA) §202(1). The period prescribed for submitting comments to that notice under SAPA §202(1)(a) expired on November 6, 2006. Consumer advocates, generators and generator affiliates, electric and gas utilities, and energy service companies (ESCO) filed comments in response to the notices. The parties are listed, with abbreviations, and their comments are summarized, at Appendix A.

DISCUSSION

To frame the issues that utility hedging practices raise, the Order Instituting Proceeding listed seven questions and asked parties to respond to them. Some parties went beyond the scope of the Order Instituting Proceeding and its questions by raising additional issues or proposing new policies. Consequently, the scope of this proceeding must be established before the questions presented in the Order Instituting Proceeding can be resolved.

[4] The two questions affecting gas as well as electric utilities are: first, what limitation, if any, should be imposed on the length of the term of a hedging instrument deemed appropriate for inclusion in a utility supply portfolio, and, second what level of disclosure of utility supply portfolio price information is appropriate.

In analyzing the seven questions presented in the Order Instituting Proceeding, parties took a variety of positions, sometimes directly contradictory to each other. Many parties based arguments on their perception of the effect utility hedging activities would have on the operation of retail competitive markets. Those arguments are best considered before turning to the issues raised by the seven questions.

Scope of the Proceeding

Some consumer advocates argue that deficiencies in the structuring of competitive markets require solutions that go beyond developing guidelines for utility hedging practices. In particular, Assemblyman Tonko and NYC maintain that electric utilities should be required to engage in integrated portfolio management planning, with each utility forecasting its energy supply needs and devising plans to meet those needs. In addition to methods for constraining price volatility, the plans would address issues such as reducing emissions of air pollutants and greenhouse gases, promoting renewable resources and encouraging energy efficiency.

NYC adds that long-term contracts for the purchase of electric supply should form one component of the integrated portfolio management plans. In the absence of long-term contracting, NYC asserts, new sources of generation supply cannot be developed, and the long-term system reliability dependent upon adequate generation resources cannot be achieved. Other parties also propose solutions to long-term resource adequacy concerns.

In opposing consideration of long-term planning issues here, some parties maintain that those issues are beyond the scope of this proceeding. Others argue that the proposals to address long-term planning are in conflict with the Retail Access Policy Statement.

The resource adequacy, environmental, and energy efficiency issues NYC and other consumer advocates raise in the context of integrated planning are of crucial importance. These questions, and the use of long-term contracts as a tool for the acquisition of new generation resources, require careful consideration. Those issues are, however, beyond the scope of this phase of the proceeding.

The Order Instituting Proceeding defined the issues under consideration here as the hedging practices needed to constrain price volatility, and did not go further to address the practices needed to ensure resource adequacy or advance other public policies. The Retail Access Policy Statement draws the same distinction, by acknowledging that utilities should make available to mass market customers prices supported by a balanced hedging portfolio consisting of instruments and arrangements that mitigate volatility, but treating long-term contracts entered into for purposes other than restraining volatility as devices separate from the proper content of a hedging portfolio.[5] This phase of this proceeding is therefore best restricted to those hedging practices needed to protect against price volatility without addressing resource adequacy, source of supply, or public policy issues.

Those issues, however, are of paramount importance in protecting utility ratepayers from shortages of supply or adverse environmental impacts. Consequently, the long-term contracting, resource planning, energy efficiency, and environmental issues the consumer advocates and some other parties raise will be addressed in a Phase II of this proceeding that will be instituted in accordance with the discussion below.

[5] Retail Access Policy Statement, pp. 29-35.

Consumer Benefits and
Competitive Market Impacts

Some parties contend that utility hedging practices do not benefit consumers, because hedging does not reduce price volatility and is overly expensive, thereby imposing excessive costs on ratepayers. Those parties claim that utility hedging is inherently inconsistent with the operation of competitive retail markets for energy supply, and suggest that the transition of utilities out of the hedging function should be accomplished in this proceeding, in conformance with their interpretation of the Retail Access Policy Statement as providing for the exit of utilities from the hedging function as the competitive marketplace develops. In support of their contentions, these parties present arguments drawn from decisions on the fixed price energy supply offers utilities have been allowed to tariff.

In opposition to those views, some parties respond by arguing that utility hedging is an essential consumer protection measure. These parties assert that mass market customers are risk averse and desire protection, through utility hedging, from the flow-through of wholesale spot market price variations. They add that competitive markets should not be promoted by preventing the utilities from delivering a service customers desire to obtain from them. They also assert that, with fixed-price service offers unavailable from most utilities, utility hedging is a necessary function.

In addressing utility hedging practices, we will first ensure ratepayers are charged just and reasonable rates, and then balance the benefits of hedging against the potential impediments to retail energy market development. As noted in the Retail Market Policy Statement, this balancing is an ongoing effort that depends upon the needs of consumers and the particular state of retail markets at any particular time.

A. Benefits of Hedging

Utility hedging of supply, if properly implemented, reduces the price volatility mass market customers would experience in the absence of hedging. Most utilities already enter into hedging arrangements for the purpose of stabilizing prices, and, as a result, have been able to charge mass market customers end-use prices that are less volatile than wholesale spot market prices. That volatility can be constrained is also demonstrated by the fact that averaging Independent System Operator (NYISO) hourly prices on a monthly basis yields a monthly price that is less volatile than the hourly prices. The same effect can be seen over longer time periods.

ESCOs maintain that volatility can increase suddenly upon the termination of a particularly effective hedge. That effect, generally experienced in moving from one fixed price period to the next, can be avoided by structuring diverse portfolios that consist of a variety of hedges that run for differing time periods, instead of relying on a fixed price that expires as of a specified date.[6] Therefore, we reject ESCO assertions that utility hedging practices do not successfully moderate price volatility, and we find that utility hedging practices can continue to yield prices that are more stable than those that can be obtained in wholesale spot markets. We will, however, continue our inquiry into improvements that might be made to existing hedging practices.

Mass market customers generally find beneficial the restraints on price volatility that the utilities are able to achieve, notwithstanding that cost premiums might be incurred in

[6] For example, the fixed commodity price offered by NYSEG to its residential customers went from 6.21¢ per kWh for the 24-month period ending December 2004 to 7.48¢ per kWh for the 24-month period beginning January 2005, an increase of 1.27¢ or approximately 21%, and the price increased again by approximately 17% for the period beginning January 2007.

procuring the restraints. As consumer advocates point out, mass market customers taking service under broad rate classification tariffs are generally risk-averse, and many of the customers in those classifications prefer price stability over unexpected price spikes. As a result, hedging is a form of insurance that many such customers would find worth purchasing if the price is reasonable and the risk that is insured against is successfully ameliorated. That hedging practices may over time cost somewhat more than the average of wholesale spot market prices is not a reason to forgo hedging, so long as the price incurred in obtaining the hedge is not more costly than the benefit of the volatility reductions that are achieved. To ensure that utilities are in fact properly obtaining the benefits of hedging at appropriate costs is one of the purposes of this proceeding.

Consumer advocates note that most electric utilities do not offer mass market customers fixed price service, which would stabilize rates for a pre-established period of time. Disputes over the efficacy of fixed price service, however, have been addressed elsewhere.[7] As decided in the NYSEG Rate Order, where a utility offers more than one rate, the hedged offering serves as the default option for those customers that decline to affirmatively select an option. Moreover, the SCMC Order and the NYSEG Rate Order establish that the issue of utility rate offerings to mass market customers in addition to the hedged offering is best addressed in utility-specific proceedings.

Since hedged rates will serve as the default rate for mass market customers, even where a fixed price service is offered, it is necessary in this proceeding to arrive at the

[7] Case 05-E-1222, New York State Electric & Gas Corporation, Order Adopting Recommended Decision With Modifications (issued August 23, 2006)(NYSEG Rate Order); Case 05-G-0311, Small Customer Marketer Coalition, Order Directing the Future Termination, Subject to Conditions, of a Fixed-Price Offer (issued July 22, 2005)(SCMC Order).

hedging guidelines that will result in the utility commodity rates that best advance the public interest. The desire of consumers for price stability and the role utility hedging efforts can play in furnishing that price stability are factors that may be considered in guiding the utility hedging activities that support just and reasonable rates. Those factors may then be balanced against the impacts of utility hedging activities on the development of competitive retail energy commodity markets.

B. Effect of Hedging on Competition

ESCOs maintain that utility hedging activities can be anti-competitive. Some ESCOs argue that utilities possess inherent advantages over ESCOs in engaging in hedging, and that ESCOs cannot avail themselves of all the hedging opportunities utilities can access. Among the alleged utility advantages are supposedly superior credit ratings ESCOs cannot achieve because they lack the customer base the utility can rely upon as the monopoly delivery service provider in a geographic service territory. Utilities, however, deny that they possess inherent advantages over competitors in pursuing hedging strategies and claim that ESCOs can achieve the same credit ratings as are available to them.

Opponents of utility hedging have failed to demonstrate that the practice is anti-competitive. Other than existing legacy hedges, hedging opponents have not demonstrated that hedging instruments are uniquely available to utilities or that utility hedging denies them sources of supply.[8] Moreover, as utilities contend, hedging is a practice consistent with the operations of competitive markets generally.

[8] Legacy hedges were generally entered into with the new owners of generation plants after utilities divested those plants, or in conformance with past regulatory practices; in both cases, the general body of ratepayers was responsible for meeting the costs underlying the hedge.

The opponents of utility hedging also argue, in effect, that hedging is a barrier to competitive market development because it enables utilities to retain customers. For example, ESCOs entering into hedges that become unattractive may face greater risks than utilities entering into equivalent hedges. The utilities, with their larger customer bases, can better adapt to the financial losses unattractive hedges pose than ESCOs, which are more adversely affected by a loss because of their smaller customer bases. Utilities can recover the costs of disadvantageous hedges from their larger customer bases, while ESCOs may find cost recovery more difficult if their customers decide to switch to other providers. To neutralize these advantages, the opponents of utility hedging claim, utilities should cease hedging as soon as possible and should instead flow through spot market prices to their mass market supply customers.

Taking that step, however, would expose mass market customers to greater price volatility. Under current utility commodity charge mechanisms, the commodity rates billed to mass market customers are monthly average prices. If the source of supply were unhedged market prices, these customers would face the excessive price volatility that they generally wish to avoid and would insure against, even though that volatility would be experienced on a monthly basis.[9] It would be unreasonable to expose mass market customers to such an overly-volatile rate.

As proponents of hedging point out, competitive markets should not be developed by restricting utility efforts to serve customers at regulated rates that are just and

[9] For example, the unhedged 30-day load weighted market price for National Grid customers in the Capital District region went from 7.093¢ per kWh on January 21, 2007 to 10.976¢ per kWh on February 21, 2007, an increase of 3.883¢ per kWh, or approximately 55%.

reasonable. If the market is open to competition and barriers to entry have been removed, competitive providers should succeed or fail based on whether they can offer energy products on terms that consumers find preferable to regulated utility commodity rates. With the implementation of the policies prescribed in the Retail Access Policy Statement, barriers to market development growing out of the utilities' status as the incumbent providers to large bodies of customers have been ameliorated. In light of those policies, compelling utilities to exit the hedging function in order to promote competitive markets would not yield benefits commensurate with the harm mass market customers could experience upon the attendant increase in price volatility.[10]

Nor does utility hedging prevent ESCOs from successfully competing. ESCOs can offer prices different from the regulated and hedged rate the utilities tariff for various mass market customer classifications, allowing ESCOs to seek out market opportunities the utility does not meet with its hedged rate offering. Moreover, hedging of commodity prices is a practice typical of competitive markets and offering a hedged price is a feature of those markets that competitors must successfully confront if they desire to expand upon their market share.

Nor, as some ESCOs claim, is utility hedging analogous, in its effects on competitive markets, to the fixed price offerings recently considered in the NYSEG Rate Order and the SCMC Order. Those offerings fixed a rate for a pre-set period of time, unlike a hedging approach, where a utility seeks to smooth out volatility on an ongoing basis. Such fixed price

[10] The role of retail access policies in promoting the further market development of competitive markets is discussed in the Order on Review of Retail Access Policies and Notice Soliciting Comments issued today in Case 07-M-XXXX.

offerings can sometimes be subsidized by customers who do not participate in them,[11] or can be viewed by some utilities as potential profit centers, creating an incentive to engage in anti-competitive behavior.[12] In contrast to those fixed price offerings, utility hedging practices, if implemented properly, do not raise improper subsidization concerns, and utilities do not treat hedging as a profit center, because the costs and benefits of hedging are passed through to the ratepayers that take the hedged commodity service from a utility. Therefore, utility hedging is not analogous to the recently-considered fixed price offerings in its impacts on competitive markets.

C. The Retail Access Policy Statement

Some ESCOs argue that the Retail Access Policy Statement requires utilities to exit the hedging function. The Policy Statement, however, explicitly provides for the continuation of utility hedging for the benefit of mass market customers. The hedging practices at issue in this proceeding are those needed to protect those customers. Nor did the Retail Access Policy Statement provide any timetable for utility exit from the hedging functions performed on behalf of mass market customers. The principles set out in the Retail Access Policy Statement do not conflict with a policy of continuing utility hedging under the guidelines discussed below.

D. Conclusion

Utility hedging of price volatility for the benefit of mass market customers shall continue. Most mass market customers expect and desire that utilities will offer a regulated product that limits volatility, and charging a stabilized rate to mass market customer service classifications is a traditional utility rate offering. In the past, when New

[11] SCMC Order, p. 7.

[12] NYSEG Rate Order, pp. 3-11.

York electric utilities owned generation, the costs they incurred in supplying energy were generally more stable than the costs they currently incur when purchasing energy in today's wholesale spot markets.[13]

The impact of a hedged utility commodity rate on the competitive market is not anti-competitive and does not significantly disadvantage competitors. Instead, the utility offering challenges competitors to devise products that consumers will find more beneficial than the utility hedged product. There is nothing improper in such an outcome, which is typical of competitive markets. Balancing the extensive benefits of utility hedging to mass market customers generally against the minimal adverse impacts on competitive markets justifies a finding that utilities should continue to hedge for the benefit of their mass market customers, subject to the appropriate guidelines needed to ensure the hedged rate is just and reasonable.

The Order Instituting Proceeding Issues

With the preliminary issues addressed, the questions raised in the Order Instituting Proceeding may be considered. The questions are listed below.

Question 1: the extent to which guidelines for electric utilities should constrain their discretion, or allow them to exercise flexibility, in structuring their supply portfolios, while recognizing the impact that utility purchasing activities might have on the functioning of competitive electric markets?

In addressing Question 1, parties made proposals running the gamut from allowing electric utilities to freely

[13] When the utilities owned generation, the fuel diversity of their generation portfolio provided price stability. In contrast, the wholesale market clearing price generally reflects the impact of the fuel price of the marginal generation unit.

exercise their discretion in structuring their hedging supply portfolios to directing them to engage in a process for obtaining supply prescribed to a level of detail intended to prevent the exercise of discretion. Proponents of utility discretion argue that utilities should be left free to act in the best interest of their customers without the constraint of artificial guidelines that might restrict their ability to obtain the most advantageous hedging arrangements for the benefit of their customers.

Other parties would limit discretion, by establishing guidelines that would require electric utilities to take steps believed to more fully and properly protect consumers against price volatility. ESCOs generally would constrain utility hedging to circumscribed activities they say would not harm the competitive market. Generators, for their part, propose that utilities obtain their supply through an auction process of some sort. ESCOs counter that these auctions would destroy retail markets, as the utility would eventually become the supplier to all mass market customers at the auction price.

The restrictions on utility procurement practices that ESCOs and generators propose will not be adopted. ESCOs would limit procurement to artificially-short time periods, such as no longer than one month. Those constraints would not enable utilities to make the longer-term purchases that may be in the best interest of their customers, or to smooth out price variations by structuring portfolios with hedging instruments of different lengths.

The auction processes the generators propose, even those that yield hedging instruments with longer terms than the ESCOs propose, are similarly overly-constraining. Requiring a rigid auction approach, with utilities able to obtain supply only in prescribed forms at pre-established time intervals, might force utilities to miss advantageous hedging opportunities

as they arise. Utilities should be able to approach such opportunities with the flexibility necessary to act in the best interests of ratepayers. Rigid constraints or overly prescriptive guidelines could preclude utilities from acting on those opportunities, to the detriment of ratepayers.

Moreover, the auction processes undertaken in other states that the generators reference are not relevant to New York. Unlike the circumstances in those other states, most New York utilities have continued to hedge since the inception of competitive markets, and so a substantial amount of the supply they already purchase acts as a partial shield against volatility. New York utilities also have largely divested their generation, preventing the potential for abuses that arise in states where delivery utilities might purchase from their generation affiliates. Therefore, the constraints on hedging activity ESCOs and generators propose are rejected.

Consumer advocates present a variety of proposed constraints they say will better protect consumers. For example, CPB suggests that electric utilities should hedge no more than 60% of their mass market loads. PULP urges hedging to the level needed to eliminate volatility.

These standards are unlikely to advance consumer welfare. If utility discretion is overly constrained, their flexibility to seek out and obtain the most advantageous hedges may be lost and ratepayers could suffer as a result. Therefore, the constraints consumer advocates propose will not be adopted.

As a result, no one particular procurement approach yet proposed is optimal for all New York electric utilities. Utility service territories differ substantially in the price volatility they have experienced, and in the means available for constraining that volatility. A utility-specific approach is necessary.

In order to adequately constrain volatility, however, volatility itself must first be adequately defined. To achieve such a definition, a means of measuring volatility must be devised. This requires that a standard for measuring volatility be established for each utility. Once volatility measurement standards are selected, goals for the levels of price volatility that are acceptable can be determined.

Arriving at those standards and goals, which would then comprise the utility-specific volatility mitigation guidelines, will be undertaken in a collaborative or other administrative process for each utility. Such a process will encourage interested parties to participate, assisting in assuring that the guidelines that are developed satisfy the public interest and adequately protect consumers. Where a utility rate case is ongoing, or a rate case filing is expected soon, the process of developing the guidelines can be conducted in the context of such a proceeding. Where utilities are in the midst of rate plans, it may be necessary to proceed without awaiting a new rate filing.[14]

Once the measurement standards and volatility goals are in place, utilities shall meet with Staff annually on the portfolio management strategies it will implement, and the commodity supply instruments and hedging arrangements it will deploy, to achieve its goals. This will enable Staff to monitor volatility and review and compare utility performance in managing that volatility.

This approach to structuring utility supply portfolios should enable interested parties to participate in that

[14] We direct Department of Public Service Staff (Staff) to supervise procedures for conducting the collaborative processes for the major electric utilities, in coordination with ongoing or imminently anticipated electric rate proceedings or otherwise.

structuring to the extent appropriate, and should result in portfolios that enhance benefits to consumers. The development of the standards and goals, and the subsequent Staff review of the strategies for achieving the goals, will also help to ensure that utilities do not unduly interfere with the operation of competitive markets, and instead engage in the hedging activities that are typical of those markets. Therefore, the guidelines adopted here shall consist of a directive that each electric utility develop standards and goals for measuring and constraining volatility in a collaborative or other administrative process, subject to annual Staff review of the strategies for achieving the goals.

Question 2: the balance between the level of electric commodity price mitigation needed to appropriately protect customers from volatility and the level of exposure to volatility needed to appropriately send reasonably-accurate price signals to those customers?

The positions of the parties on minimizing volatility while sending accurate price signals mirror their positions on the level of guidance that should be imposed on utilities in structuring their supply portfolios. Electric utilities oppose specific guidelines on achieving a balance between volatility minimization and price signal transparency; consumer advocates prefer that volatility be constrained to the greatest extent feasible, and ESCOs would impose strict guidelines constraining utility hedging activities.

The appropriate balance between minimizing volatility and sending accurate price signals can be better achieved, at least in the short run, through the proper development of utility-specific standards, goals and portfolio strategies. After the standards for measuring volatility and the goals for limiting that volatility are established, each utility will develop its portfolio management strategies, subject to Staff

review. Once the portfolio management strategies are in place, the appropriate balance between volatility and price signal accuracy can be best achieved through the implementation of those strategies.

Nonetheless, utility hedging portfolio practices can mask price signals based on wholesale market spot prices, which can be beneficial. Where a utility confronts a supply or demand problem that persists for a period of several months to a year, wholesale market spot price signals, even though they occur in the form of simple average monthly prices for mass market customers, can successfully cause customers to alter their aggregate consumption. In doing so, they would contribute to solving a shortage problem. To the extent a utility hedges a portfolio, the strength of the monthly prices as signals of supply or demand imbalances is weakened.

This effect, however, does not prevent utilities from protecting vulnerable mass market customers from price volatility through their individual portfolio decisions. Each electric utility's hedging portfolio, arrived at through execution of its strategies, will encompass a variety of supply instruments and hedging arrangements that are intended to appropriately limit volatility in conformance with the utility-specific measurement standards and volatility mitigation goals. Included among portfolio instruments and arrangements is expected to be some level of wholesale spot market purchases, needed both to meet load fluctuations as they occur and because attempting to hedge all load would likely be unduly expensive. Depending to some extent on spot market purchases will result in a portfolio price that reflects some shorter-term price signals. As utilities periodically re-balance their portfolios to best achieve volatility mitigation, the re-balanced price will also send appropriate signals. As a result, mass market customers will see incentives to respond to price trends over time.

Dampening volatility will smooth out those trends, but will not eliminate them.

To the extent this effect is inadequate to transmit all the price signals desired, rate design mechanisms for sending additional price signals already exist or can be developed in individual rate cases. Indeed, some parties point out that regulatory mechanisms other than utility portfolio hedging might be useful in mitigating price volatility or in sending the price signals that alter consumer behavior. Direct Energy in particular proposes that volatility is best constrained through bill averaging methodologies instead of relying on utility hedging. Other parties contend that rate design mechanisms can be devised to properly transmit price signals notwithstanding utility hedging activities.

These methodologies and mechanisms, which can be useful volatility mitigation tools, are best addressed elsewhere than in this proceeding. The purpose of this proceeding is to undertake a review of utility hedging practices and their effects on consumers and competitive markets. As the Retail Access Policy Statement acknowledges, the continuation of hedging practices is necessary, at least in the short-term, because utility hedging can successfully constrain the price volatility that many mass market customers find undesirable. As a result, the effects of hedging must be properly assessed notwithstanding the availability of other mechanisms for accomplishing bill mitigation and transmitting proper price signals. Given that availability, however, it is not necessary to take specific steps for ensuring that measures undertaken here to limit the volatility mass market customers experience do not unduly mask prices signals.

Question 3: whether an index is needed to measure electric price volatility, how to establish an index if one is needed, and how to guide electric utilities in the structuring of their supply portfolios to comport with the limits indicated by the index?

For a variety of reasons, nearly all parties opposed the indexing of electric utility performance in limiting volatility. Many parties pointed out that utility efforts to meet a pre-established indexing requirement could induce utilities to engage in overly-expensive hedging practices in order to satisfy the index, thereby saddling ratepayers with excessive costs. As with other constraints on utility hedging activity, use of a single index would overly hobble utility management discretion in executing hedging strategies, to the eventual detriment of ratepayers. Moreover, no party succeeded in proposing a single index that might properly be imposed on all utilities.

For those reasons, a generally-applicable volatility index will not be established at this time. The utility-specific volatility measurement standards, goals and portfolio management strategies that will be developed are expected to be sufficient, in the short run, to yield appropriate portfolios that best protect ratepayers without the imposition of a mandatory index.

Nor is it necessary for regulatory purposes to adopt a single index applicable to all electric utilities. The utility-specific measurement standards and goals that will be developed will adequately facilitate the monitoring of electric utility performance in executing their hedging strategies. The information obtained from that monitoring will enable Staff to compare utilities' approaches to the extent appropriate, and to evaluate the extent to which greater consistency among utility approaches might become beneficial. As a result, applying a

single index to all electric utilities would not advance the public interest at this time.

Question 4: whether electric hedging costs and the values achieved through the hedges, above or below spot market prices, should be recovered through commodity mechanisms from only those customers taking commodity from the electric utility, or should be recovered through delivery mechanisms from all customers?

Most parties favor recovering the costs of hedging conducted for the purpose of constraining volatility through electric commodity charge mechanisms. Those parties agree that this approach to recovery sends the most accurate price signals and properly allocates responsibility for hedging costs. Some parties also contend that recovering the cost of hedges through delivery rates would dilute the effect of the hedge on volatility, because its cost-ameliorating impact is spread over a larger number of customers. As an exception to the general rule of commodity charge recovery,[15] some parties caution that legacy hedges are sometimes appropriately recovered through delivery rates, because utility competitors cannot obtain these legacy hedges in the existing market.

Some ESCOs, however, oppose achieving commodity cost recovery entirely through commodity charges. They argue that delivery customers support utility hedging because they support the financial viability of the utility, and so some hedging costs are properly imposed on them even under traditional cost causation principles. They dismiss the concern that delivery rate recovery will dilute the value of the hedges, because most customers in mass market customer classes remain utility

[15] Some parties propose that a portion of the costs of long-term contracts entered into to obtain new generation resources instead of to constrain price volatility should be recovered at least in part through delivery rates; that issue will be addressed in the Phase II proceeding discussed below.

customers and are therefore properly charged the value of the hedge in any event. The ESCOs also contend that utilities gain competitive advantage if all hedging costs are flowed through commodity charges, because prospective ESCO customers compare the price the ESCOs offer to those utility charges. If the utility charge is reduced because of hedging, the ESCOs must reduce their prices in response if they are to maximize their market share.

Proper cost causation principles require that commodity costs like hedging be recovered through commodity charges imposed on the ratepayers that subscribe to the commodity service. Recovering commodity costs in delivery rates disguises the value of both the commodity and the delivery services and should be avoided. As some parties point out, however, continuing recovery of legacy hedges through delivery rates is appropriate. Not only are those hedges no longer obtainable in the market, but generally all ratepayers supported the costs that resulted in the legacy hedges. As a result, all ratepayers should bear their costs or receive their benefits through delivery rates.

The arguments of those ESCOs proposing that a portion of volatility-related hedging costs be recovered through delivery rates are rejected. This approach dilutes the value of the hedge. Spreading the benefit of the hedge over a larger number of customers through delivery rates necessarily means the benefit will have a smaller impact on constraining price volatility for the lesser number of customers that take utility commodity service.

ESCOs argue that, given existing mass market customer migration rates at most utilities, the difference between the number of customers taking utility commodity and delivery, and those customers taking only utility delivery, is not large enough to result in a dilution value that is significant.

Notwithstanding that argument, any dilution harms the regulated ratepayers who bear the additional cost, and recovery through delivery rates improperly impacts delivery-only customers, who would pay the utility for a hedged service they did not ask to receive. More importantly, proper cost recovery principles should not be ignored merely because utility competitors will benefit. Competitors should succeed based on the value they create in the marketplace, not by imposing artificial restrictions, like recovery of commodity costs in delivery rates, on their competitors.

Finally, recovery of electric commodity costs through commodity charges results in consistent treatment of the electric and gas industries, because gas commodity charges have previously been recovered solely from gas commodity customers, and not through delivery rates. Therefore, electric utilities shall, in future rate cases, present electric commodity charges that fully recover commodity costs (except for legacy hedges).

Question 5: the cost elements that should comprise electric commodity charges to customers?

Most parties believe that the commodity-related costs best recovered through electric commodity charges can be adequately identified. These cost elements include NYISO energy prices, capacity costs, ancillary service costs (including the NYISO's collection of the NTAC charge), and re-billing costs.[16] Besides the NYISO costs, utilities say they incur line loss and unaccounted-for energy costs, the costs of procuring the hedges and the risk of gain or loss on the hedges. These types of costs are appropriately recovered through commodity charges, as determined with specificity in utility rate cases.

[16] NYISO rebilling adjustments can raise difficult issues, which may sometimes require fact-specific resolution.

Question 6: for both gas and electric utilities, the length of the time period over which utilities should execute longer-term supply portfolio management strategies to mitigate volatility?

Parties presented a wide variety of proposals on the length of time over which hedging is deemed appropriate. Some parties would constrain utility hedging to periods as short as a month. Others suggest three months, one year, three years, or up to five years. Gas utilities, for their part, argue that existing gas hedging policy, providing for instruments and arrangements of about a year in length, is working well and should not be changed.

No particular limitation on the length of a hedging arrangement will be imposed on electric utilities as a requirement for the structuring of the portfolios supporting hedged service to mass market customers. Artificially restricting the length of the term of an electric hedging arrangement could be a disadvantageous constraint that would reduce the flexibility utilities need to act in the best interest of their mass market customers. It is expected, however, that utilities will properly develop and prudently manage their resource portfolios, and nothing here relieves utilities of that responsibility.

Instead of adopting a proscriptive limitation on the length of electric hedging arrangements, electric utilities are advised that they may enter into hedges of the appropriate length for the purpose of constraining volatility. For example, a utility might find an opportunity to make longer-term purchases at an attractive price from a generator whose variable costs of production are predictable and comparatively low, like an owner of a hydro or nuclear facility. Electric utilities, however, would also be expected to avoid hedges that are unduly expensive or risky because of their length or other unfavorable

characteristics. This expectation will constrain hedging activities to instruments and arrangements of the proper length without adopting a specific limitation on the length of time deemed acceptable.

A long-term contract entered into for the purpose of encouraging the development of new resources, however, would be outside the scope of this hedging policy. As a result, the approach discussed above will enable electric utilities to avail themselves of longer-term hedges if opportunities arise for them to constrain volatility over a longer period of time, but will not promote activities, or raise cost recovery issues, that should be decided in the Phase II proceeding discussed below.

As to gas utilities, existing hedging practices are working well. No party has been able to direct a specific criticism against the success of those policies, or propose a compelling case for improvement. Moreover, allowing gas hedging arrangements of more than about a year could raise risks to ratepayers. Existing experience with gas futures markets indicates that liquidity for longer periods of time is not robust. The risk of entering into longer arrangements, in view of the volatility gas markets have experienced in recent years, seems not worth the price. As a result, the existing policies, including limiting hedging arrangements to a term of about a year in length, shall remain in place.

Question 7: the appropriate levels of gas and electric utility supply portfolio information that should be revealed to the public to promote price transparency and the timing, process and procedures for doing so?

The views of the parties on making public supply portfolio information diverged widely. Some utilities, especially gas utilities, adamantly opposed making any supply portfolio information public, arguing that publicizing the information would redound to the detriment of ratepayers as non-

utility parties would use the information to drive the price of future hedging activities upward. Other utilities, however, were willing to publicize some data on an aggregate basis after the fact.

Taking a directly contradictory position, ESCOs ask that utilities be required to reveal information on hedging strategies in advance of executing those strategies. Most ESCOs suggest some form of detailed reporting of hedging information after the hedges are entered into, and some ESCOs would go as far as to open hedging instruments themselves to public scrutiny after they have been executed. Generators generally rely on the auction processes they propose as the source of information that can be made public after the auctions are conducted and the hedges are entered into.

Consumer advocates are interested in placing utility and ESCO price offers on a comparable basis. To achieve that goal, PULP and CPB suggest that utilities could furnish current and forecasted price information that could be posted on websites in a format comparable to ESCO price information. Responding to the consumer advocates, Central Hudson argues that comparability of utility and ESCO prices is not a proper issue for consideration in this proceeding.

Approaches to publicizing utility supply portfolio information fall into two categories. First, information on utility strategies for obtaining hedges is desired in advance of entry into the hedges themselves. Second, the reporting of information on the hedges after they are executed is proposed.

Under the process described above, electric utilities will collaborate with other parties on the development of guidelines consisting of hedging measurement standards and volatility limitation goals, either in rate cases or in proceedings dedicated to that purpose. Once the standards and goals are in place, utilities will report annually on their

proposed implementation of their portfolio management strategies to Staff.

This approach properly provides for any needed reporting on hedging portfolio strategies prior to their implementation. Public input is solicited on standards and goals so the public interest in ascertaining those matters is satisfied. More detailed information on the execution of the strategies is provided to Staff, enabling it to monitor and review each electric utility's performance.

Making the annual information provided to Staff publicly available, however, could impede utility efforts to execute their hedging strategies at least cost. If competitors were to possess more detailed knowledge of the utilities' plans, especially prior to their execution, they might be able to drive up prices in the market or execute maneuvers that would detract from the utilities' ability to hedge at least cost. As a result, more information will not be revealed on hedging strategies.

ESCOs argue that they require more detailed information on hedging strategies in order to compete effectively with electric utilities. Obtaining knowledge of a competitors' plan before the competitor executes them, however, is not a characteristic of competitive markets. ESCOs should be expected to compete without by obtaining information that would normally remain in the competitor's possession in competitive markets. The ESCOs' position is therefore rejected.

As to the issue of post-hedging reporting, most parties agree that some after-the-fact reporting on the outcome of electric hedging strategies is appropriate. This reporting would open electric utility performance to public scrutiny and enable competitors to obtain information on utility efforts after the fact, when discovery of the price impacts would generally become available in any event in most competitive

markets. But excessive disclosure, such as releasing the content of specific hedging instruments after their execution and identifying the names of hedging counterparties, might allow competitors to gain access to information they could use to distort the operation of markets in the future. Even after-the-fact disclosure must be appropriately bounded.

Therefore, methods for after-the-fact reporting of electric utility hedge prices shall be developed, in the proceedings for developing hedging standards and goals discussed above. Reporting requirements should provide for the release, at least quarterly, of price information in an aggregate form, while masking the identity of the individual market participants. The furnishing of information subject to these practical safeguards should enable consumers and competitors to adequately protect their interests while preventing competitors from obtaining information which might enable them to manipulate markets and drive prices upward.

As to the comparability of utility and ESCO prices, the steps taken in this proceeding advance that comparability. As discussed in the ESCO Price Reporting Order,[17] establishing the proper content of utility commodity charges, and requiring utilities to report the outcome of their hedging portfolio activities, will enhance the comparability of ESCO and utility offers. Additional steps to achieve more improvements to comparability, and to devise Web site comparison tools, are left to other proceedings.

As to gas utilities, adequate after-the-fact reporting is already required. Gas utilities submit aggregate price data on a monthly basis as required by our regulations.[18] Moreover,

[17] Case 06-M-0647, Energy Service Company Price Reporting Requirements, Order Adopting ESCO Price Reporting Requirements and Enforcement Mechanisms (issued November 8, 2006).

[18] 16 NYCRR §720-6.5.

gas utilities already share their hedging plans annually with Staff in advance of executing their hedging strategies, as in the process suggested above for electric utilities. Therefore, no changes to gas utility information reporting requirements are necessary.

Long Term Contract Issues

In addition to the hedging policies discussed above, the filings of some parties addressed two additional topics. First and most broadly, New York City urged the adoption of a statewide integrated resource planning process to help guide the overall development of electricity infrastructure.[19] Second, a few parties urged the use of long term supply contracts for diversified supply portfolio management (e.g., to maintain appropriate generating fuel diversity) or to provide a financial basis to support the provision of new capacity.[20] Issues concerning the use of long term contracts for these purposes were not addressed by every party because some believed the issues were beyond the scope of our initial inquiry. In our view, these are important issues that need to be addressed expeditiously. Accordingly, we are issuing a further set of questions to examine these topics as set forth below.

Before discussing the details, it is important to note that this Commission has consistently found that the development of competitive markets, where feasible, will assist in assuring the provision of safe and adequate utility services at just and

[19] NRG also urged action to ensure future resource adequacy in New York, Initial Comments, p. 3. Those companies express the opinion that the need is "acute" to take decisive action to ensure adequate resources and to remove regulatory uncertainty. Id., p. 5.

[20] New York City uses the term of five years or greater to define long term contracts. New York City Comments, p. 2. For the purpose of this order, we will assume here that long term contracts are five years or longer.

reasonable costs.[21] We have consistently endorsed competition where it is more effective than regulation, but also realize that markets alone may not automatically satisfy a broad range of public policy needs and goals.[22]

The existing wholesale electricity market structure in New York City has not led to much merchant driven supply nor shown much promise for new merchant driven market entry. It appears that merchant wholesale market participants in New York City have been unwilling or unable to invest in needed new infrastructure, despite the fact that New York City's wholesale electric market prices are some of the highest in the country and the latest Reliability Needs Assessment (RNA) of the NYISO forecasts a need for additional capacity as soon as 2011. A number of matters appear to be influencing this result, all of which affect the risks and returns of infrastructure investment.

Regulatory uncertainty could have a substantial impact on investment decisions, and those uncertainties may arise in

[21] Retail Access Policy Statement, pp. 18-19; Case 94-E-0952, Competitive Opportunities Regarding Electric Service, Opinion No. 96-12 (issued May 20, 1996), pp. 24-26; Case 94-C-0095, Transition to Competition in the Local Exchange Market, Opinion No. 96-13 (issued May 22, 1996), pp. 3-6; Case 93-G-0932, The Emerging Competitive Natural Gas Market, Policy Statement Concerning the Natural Gas Industry in New York State and Order Terminating Capacity Assignment (issued November 3, 1998), pp. 3-5.

[22] Case 03-E-0188, Retail Renewable Portfolio Standards, Order Approving Implementation Plan Adopting Clarifications, and Modifying Environmental Disclosure Program (issued April 14, 2005) and Order Regarding Retail Renewable Portfolio Standard (issued September 24, 2004).

new state[23] or federal legislation,[24] new policies of regulatory agencies, or new practices at the NYISO. For example, market rules the NYISO has developed and amended since 2000 continue to evolve, as needed, to constrain the exercise of market power. Further, a new generation of forward capacity market approaches is being implemented in New England, and new rules may be proposed for New York.[25] Changing market rules, and the consequences such changes can sometimes bring, provide continuing risks and uncertainties for investors in new generating, demand side management (DSM), and transmission facilities.

Another risk-related issue is the affect on wholesale prices of substantial capacity increases. If capacity additions create a significant surplus, prices could decline especially in

[23] One uncertainty in New York is based on the absence of a specific generator siting statute, following the expiration of Public Service Law, Article X, and whether a new statute will be passed.

[24] For example, the Federal Energy Policy Act of 2005 allows FERC to authorize the construction of new transmission lines into locations, such as New York City, if the Department of Energy finds the existence of a National Interest Electric Transmission corridor and state authorities fail to timely act on siting applications within that corridor. Were that to occur, the wholesale price for electricity in the City could fall, as could the value of the existing generating plants.

[25] The ISO New England (ISONE) “Forward Capacity Market” approach is to create a longer-term capacity market (5 years) using an auction approach and providing up to a five year guaranteed revenue stream for new entrants and a one year revenue stream for existing generators. While the diversified forward contracting approach discussed in this memorandum varies significantly from New England’s, both approaches recognize the value of creating longer-term markets to benefit wholesale competition and resource adequacy.

smaller-sized markets.[26] This result could occur if new generation were built or if electricity demand were reduced. It thus appears that existing New York City generators might face a reduced market price should new transmission, generation, and/or DSM projects be undertaken. Therefore, existing owners of generators might have little interest in building, and potential new generators may hesitate to invest in a market where new entry could substantially reduce prices. Again, the risks of investing could be significant.

Another difficulty that arises in considering public policy interests is deciding among several competing projects or competing types of projects (generation vs. transmission vs. DSM). If we have a need for more capacity: should it be served with generation, and, if so, what type (renewables, low-carbon, distributed, central station, gas, coal, nuclear, fuel cells, etc.); should transmission be chosen, and at what environmental cost along its route; or should efficiency improvements or other DSM approaches be used, and at what cost? These issues are not addressed by the existing NYISO planning process, yet they are of substantial interest to the public. How those questions will be answered is another risk market investors face.

NYISO has established a planning approach to identify system reliability needs. It has relied on the market, in the first instance, to decide which reliability project should go forward, but in that process it does not address other potential

[26] While lower prices in the short term are appealing, the potential long term impact on electricity prices of substantial excess capacity may overwhelm any short term benefits.

public policy concerns.[27] If it were determined, for example, that the public interest would best be served by choosing a nuclear-powered plant rather than a gas or coal fueled plant in order to maintain supply diversity, or that restricting new contracts to low-carbon sources would be in the public interest, it is unlikely that these interests would be comprehensively addressed by the NYISO market structure in its current state. Further, it is our understanding that the NYISO participants would prefer to have public policy issues addressed by the State rather than by NYISO.

Accordingly, there may be a growing need for a rational and comprehensive decision-making approach to guide the future of New York's electricity infrastructure. The NYISO's approach maintains the reliability of the system, but investment in new resources, whether demand or supply, may be advisable and in the public interest long before similar additions would be required by the NYISO to maintain reliability. In the past, this type of public policy planning has been incorporated into state or utility integrated resource planning efforts, but today, there is no comprehensive planning regarding electric system infrastructure that addresses such economic and public policy goals.

We conclude that integrated planning for public policy purposes needs to be further considered in an expedited manner. Whatever planning approach the parties might suggest in response to our questions, it is essential that the process and plan be flexible and capable of responding adequately to rapidly changing circumstances.

[27] A diverse mix of peaking, intermediate, and base-load generators, distributed generation, and DSM could be in the public interest, but such issues are not addressed in the ISO process.

In addition, it appears that the use of long term contracts could facilitate entry of new supply. The arguments made by NYC and others, and the observations we made in the Retail Access Policy Statement, suggest that long term contracts could reduce the risk of financing new infrastructure. Moreover, new capacity might not be built in the absence of long term agreements between a new entrant and one or more load serving entities (LSEs). Thus, a more detailed inquiry is needed regarding long term contracts. Besides assisting in the financing of new infrastructure, if all LSEs purchased (or continued to purchase) a portion of their supply needs through longer-term contracts, retail price volatility might be moderated. Longer-term contracts for that and other purposes could be entered into with existing wholesale generators.

While there are a number of benefits that contracts of various lengths might provide to the wholesale and retail markets, we also recognize that such contracts provide the opportunity for utilities to undertake anticompetitive activities to disadvantage ESCOs. For example, if a utility entered into contracts for future energy supply well in excess of its own needs, ESCOs might thereafter be required to pay a higher price due to the reduced supply available in the market. While anticompetitive actions are possible, we intend to closely monitor this market to ensure that such behavior is prevented.[28] The means for effectuating this result, however, is also an important topic for further inquiry.

We have no direct information on ESCO hedging practices, but assume that ESCOs enter into at least some

[28] In the Retail Access Policy Statement, p. 43, we set as our goal "a level playing field for ESCOs, free of antitrust abuses." If a utility were to enter into a contract to impede the development of a competitive market, "the cost of those contracts may not be recoverable from ratepayers." Id., p. 34.

contracts for future supply in order to support fixed price offerings. We reiterate our expectation that ESCOs who have acquired a significant level of customer load, will enter into longer term contracts.[29]

In addition to using long term contracts for future supply, there are a number of additional public policy issues regarding additional capacity (generation, transmission, and/or DSM) that need to be addressed. For example, the NYISO announced on March 19, 2007 that additional capacity will be needed in New York City to maintain reliability. [30] Additional capacity can also help moderate prices, reduce air pollution, and create greater fuel diversity. Consideration should be given, however, to the possible adverse effects new capacity could have on the economics and operation of existing facilities that support system reliability.[31]

For all the above reasons, an examination will be undertaken of the use of long term contracts and other means to facilitate the entry of new resources that would further the

[29] The Retail Access Policy Statement, p. 37, notes our expectation that "non-utility entities should increasingly be taking over this responsibility [long term contracting for supply] from the utilities." As of February 2007 about 40% of the State's MWh are being sold to customers by ESCOs. This magnitude of usage should enable the ESCOs to engage in long term contracting.

[30] The NYISO found that 250-500 MW of capacity was needed downstate by 2011 and 1500-2000 MW was needed on a statewide basis by 2016 to satisfy reliability criteria. The upstate and downstate electricity markets are significantly different.

[31] As discussed previously, the development of additional capacity would likely reduce electric market prices, possibly rendering it uneconomic to continue the operation of some existing capacity. If that uneconomic capacity is needed for reliability and is not replaced by new capacity, appropriate steps could be required to ensure the integrity of the system.

public policy goals of the State regarding electric infrastructure.

Accordingly, interested parties are invited to address the following questions.

1. Should there be a statewide integrated resource planning process to examine long term electricity resource needs? To what extent or in what manner would a statewide integrated resource planning process build on or parallel existing reliability planning processes? What time frame should be examined in such a process and what issues should be considered? What is the role of the utilities and other interested parties in the process? How should the process differ from any previous integrated resource planning processes? What processes should be adopted, if any, to ensure that resource portfolios at the utility and statewide level, satisfy overall planning objectives and public policy considerations? How should immediate concerns and long range considerations be addressed?

2. Should major regulated electric utilities be required or encouraged to enter into long-term contracts, with existing generators, proposed generators, and other entities, that facilitate the construction of new generation, the development of additional energy efficiency, the development of additional renewable generation resources, the re-powering of existing generation, or the relief of transmission congestion? Should such contracts be entered into for the purposes of improving fuel diversity, mitigating market power, or furthering environmental policies?

3. Should Load Serving Entities other than utilities, including the New York Power Authority and the Long Island Power Authority, be required or encouraged to enter into long-term contracts as described above? What role, if any, might entities other than Load Serving Entities play in such resource procurement?

4. Should resource procurement, as described in Question 1, be coordinated on a statewide basis? What regulatory oversight, if any, would be appropriate?

5. What barriers, if any, exist that discourage long-term contracts for development of new electricity resources? What other barriers exist, if any, for the

development of new electricity resources? Should incentives beyond what exist today be created to encourage entry into long-term contracts generally, or to foster the development of any particular type of resource? How could those incentives be structured consistent with the goal of acquiring the most cost-effective resources?

6. Should constraints be imposed that would, under certain circumstances, restrict the resource types eligible for long-term contracts, limit the length of contract terms or establish the content of other contract conditions? What steps should be taken to limit any anti-competitive impacts long-term contracts might create?

7. Should restrictions or guidelines be imposed on the resource procurement practices employed in selecting the resources that would be acquired under the long-term contracts?

8. How should long-term contract costs be recovered from customers, and should different recovery mechanisms be developed based on the type of resource that is acquired under the contract, the length of the contract, or other factors?

9. What procedures should be followed in reviewing a long-term contract and in establishing its qualification for cost recovery? Under what circumstances, if any, should recovery of contract costs be pre-approved?

10. Can long-term contracts (energy and/or capacity) be harmonized with existing NYISO rules for energy and capacity markets, and with potential NYISO forward capacity markets? If so, how can they best be harmonized? What changes to NYISO market rules, if any, would be necessary or appropriate for the purpose of accommodating long-term contracts? Should NYISO market rules recognize or ameliorate the impact, if any, of long-term contracting on the NYISO capacity prices paid existing generators, or, if amelioration is appropriate, should it be accomplished through non-NYISO mechanisms?
11. Are there any other creative solutions that might be considered to address the issues identified herein?

Interested parties are invited to serve an original and ten copies of their comments on the above questions on the Secretary and serve a copy of the comments on the Active Party List in this proceeding by June 5, 2007. Reply comments may be similarly served by June 25, 2007. Initial comments shall be limited to 70 pages and reply comments to 25 pages. An Administrative Law Judge (ALJ) will be assigned to this matter, and the ALJ will schedule a conference to establish any further processes necessary to fully develop a record on the issues in this proceeding. It is expected that proceedings conducted on this matter will be expedited, so that we may consider its resolution as soon as reasonably possible.

CONCLUSION

The utility-specific guidelines developed in accordance with the process described above will enable electric utilities to engage in the hedging activities needed to protect mass market customers from excessive price volatility. Accordingly, that approach to electric utility hedging is adopted. In addition, a Phase II of this proceeding is instituted to examine the use of long-term contracts and whether an integrated planning process should be established in New York.

The Commission orders:

1. New York's six major electric utilities are directed to participate in collaborative discussions supervised by the Department of Public Service Staff for the purpose of developing standards for measuring price volatility, goals for limiting price volatility, and mechanisms for reporting, on a quarterly basis, utility supply portfolio price information in an aggregate form.

2. A Phase II of this proceeding is commenced in accordance with the discussion in the body of this Order.

3. Parties interested in Phase II shall submit an original and ten copies of their comments on the questions and issues described in the body of this Order by June 5, 2007, to Jaclyn A. Brilling, Secretary, Public Service Commission, Three Empire State Plaza, Albany, New York 12223-1350 and shall serve a copy on all parties on the active party list. An original and ten copies of reply comments may be filed and served by June 25, 2007.

4. This proceeding is continued.

By the Commission,

(SIGNED) JACLYN A. BRILLING
Secretary

APPENDIX A

POSITIONS OF THE PARTIES

Initial Comments

I. Consumer Advocates

A. Assemblyman Tonko

Assemblyman Paul Tonko reports that, in conformance with the longstanding position of the New York State Assembly, Assembly Bill No. 10370, introduced in the 2005-2006 Legislative Session, would require electric utilities to engage in portfolio management services. To conform to the proposed statute, electric utilities would devise portfolio management plans for obtaining the supply-side and demand-side resources needed to meet the forecasted load requirements of those customers that choose to obtain electric commodity supply from them instead of from other suppliers. According to Assemblyman Tonko, the portfolio management approach is intended to create a market structure that, by sharing the risk of price volatility between customers and the utilities, better serves small customer classes than the current competitive services model, while recognizing that larger customers, better able to respond to market prices, should remain more responsible for their energy costs and usage.

Proposed plans for managing the portfolios would be submitted to the Commission for approval after a public review process. To the extent the utilities' plans are successful in moderating volatility, utilities could be rewarded or penalized.

Assemblyman Tonko also notes that pre-existing contracts, entered into in conformance with earlier policies, should not be viewed as hedging instruments. Those contracts, he explains, were not selected as a component of a strategic plan for power procurement and so are outside the types of hedging devices that could become a choice under the portfolio management approach. Assemblyman Tonko adds that,

notwithstanding the apparent success of current gas utility hedging practices, additional strategic planning could benefit small gas customers as well.

B. CPB

The Consumer Protection Board (CPB) believes that utilities should be required to structure their commodity portfolios so that price risk is mitigated for smaller customers, which it describes as risk-adverse. While CPB would require utilities to maintain a diverse and balanced portfolio of supply arrangements for residential and small commercial customers, it cautions that utilities should retain broad discretion to structure those portfolios in order to meet changing conditions.

To achieve these goals, CPB recommends that the Commission adopt three guidelines. First, utilities should rely upon spot market purchases for no more than 60% of their supply requirements. Excessive reliance on the spot market, CPB contends, exposes small customers to price risks they do not willingly accept, as indicated by their preference for fixed price alternatives. CPB opposes artificially disadvantaging utility offerings by compelling reliance on spot purchases as the basis for those offers, in order to enhance the attractiveness of non-utility provider offers. It describes that approach as an inappropriate means of promoting the development of retail competition.

For its second guideline, CPB would restrict utility hedging arrangements to devices readily available to all market participants. As a result, CPB would not treat advantageous legacy contracts as hedging devices, because they cannot be duplicated by other market participants. Other types of physical and financial supply arrangements, it believes, are available to all market participants on a going-forward basis.

As its third guideline, CPB would limit price mitigation arrangements to terms of three years or less. CPB argues this limitation appropriately balances the interest in mitigating price volatility with the interest in preventing utilities from exercising undue influence in competitive markets. Utilities, CPB explains, can gain competitive advantage because they can enter into longer-term contracts than other market participants, by relying on their ability to recover the costs of those contracts from their ratepayers. Limiting the length of a contract to three years, says CPB, prevents utilities from deploying unduly lengthy contracts to the disadvantage of other competitors, while still adequately protecting consumers against price volatility.

Turning to the structuring of commodity charges, CPB maintains current supply portfolio management costs should be recovered through commodity charges, as this approach enhances price transparency and comparability. CPB points out, however, that utilities have entered into legacy hedges that are the product of past utility practices for which all ratepayers are financially responsible. Consequently, CPB discerns, recovering the costs of those hedges independently from other commodity costs is appropriate.

CPB also asserts that utilities should be required to present current and forecast retail price information in formats that facilitate comparison with competitive ESCO formats. CPB is skeptical that revealing the information necessary to the development of those utility formats would be detrimental to utility or ratepayer interests.

C. CPA

Consumer Power Advocates (CPA) points out that the extremes of no hedging and complete hedging yield different disadvantages. Exposing small customers to volatile hourly

prices, CPA suggests, would not necessarily improve their choices in the market, while fully hedging supply could create stranded costs if, for any reason, customers migrate from the utility. As a result, CPA would accord utilities broad discretion in developing supply portfolios.

CPA finds it obvious, however, that hedging costs should be recovered only from commodity customers, and that commodity cost elements should include all costs allocable to supply, such as those costs attached to commodity by the New York Independent System Operator (NYISO). It also contends that some disclosure of utility supply portfolio practices would be warranted, subject to the trade secret protection from disclosure needed to prevent the undermining of utility bargaining positions in negotiating future supply contracts.

D. MI

Multiple Intervenors (MI), an unincorporated association of large energy consumers, argues that hedging costs should be recovered through commodity cost mechanisms. MI asserts, however, that large customers should not be required to fund the costs of hedges intended exclusively for the benefit of small customers. MI cautions that policies intended to ensure that large customers see accurate price signals would be defeated if the costs of hedges negotiated for the benefit of other customers were imposed on them. As a result, MI would not allow recovery of hedging costs through utility delivery rates.

If, however, large customers are forced to bear the costs of utility hedges, MI argues they should be allowed to opt to participate in a hedge and obtain its benefits. Even that participation, MI emphasizes, should be accomplished through commodity charge mechanisms rather than through delivery rates.

E. NYC

The City of New York (NYC, the City) argues that an integrated portfolio management approach to utility supply is needed, with longer-term contracts included in the portfolios in order to reduce the City's vulnerability to capacity shortages and price volatility. Without those contracts, it cautions, consumers may again be exposed to sharp price spikes, such as the 40% increase in 2005 over 2004 that occurred in NYISO Zone J (which includes much of the City).

According to NYC, a portfolio should include contracts of more than ten years in length, for supply from strategic long-term resources, mid-term contracts of five to ten years, short-term contracts of one to five years, and spot purchases. For each type of resource, the City continues, utilities would be expected to leverage their buying power by inducing suppliers to compete for the bi-lateral contracts the utilities would make available.

NYC reports that the generation capacity situation within its boundaries is tenuous at best and that very little merchant generation resource development has occurred in the absence of long-term contracts. Its capacity difficulties, the City asserts, are exacerbated because current generators possess significant market power and can consequently realize financial gains by withholding capacity from market. As a result, the City concludes the competitive market is not working well within Zone J.

Long-term contracts, NYC asserts, are needed to support the development of new generation resources while avoiding multi-year boom-and-bust cycles, when excess generation capacity is over-built in response to short-term upward price volatility, followed by capacity shortages after new construction ceases for an extended period of time. Emphasizing

the function of long-term contracts in the development of new generation resources, NYC declares that proposed resource additions have been unable to move forward without those contracts. ESCOs, it continues, are not in a position to commit to the long-term arrangements that would support resource additions. Moreover, to date, the NYISO has been unable to enhance supply through promoting the construction of new capacity, because the City asserts, the NYISO's demand curve has failed to attract new generation market entrants, despite the higher costs consumers have borne as a result.

Merchant transmission, NYC complains, is not an answer either. The NYISO, it says, has been unable to develop a market mechanism that will attract developers of alternating current transmission, even in theory. The building of direct current transmission, the City explains, cannot be properly compensated, since the value of such a line would depend upon the difference in price between two transmission zones, a mechanism that is too risky to entice a developer. The City claims transmission capacity additions, like generation additions, are feasible only with the encouragement of a long-term contract.

Only entities like the distribution utilities or the New York Power Authority (NYPA), the City stresses, can bear the cost of the long-term contracts needed to promote additional generation development. Analyzing Con Edison's current supply portfolio, however, NYC finds it deficient in mid-term and long-term supply arrangements. In comparison, the City asserts, NYPA plans to meet all of its capacity requirements through supply resources it owns or through long-term contracts, as evidenced by its procurement efforts to replace the anticipated retirement of older units at its Poletti site.

Long-term utility contracts, the City posits, should be entered into in conformance with an integrated portfolio

management strategy. Besides capacity additions, the City continues, portfolio management would yield lower prices, constrain price volatility, reduce emissions of air pollutants and greenhouse gases, promote renewable resources, and effectuate other planning goals (including prioritizing land use). The City notes, however, that mechanisms must be developed to ameliorate the effect of long-term contracting on utility credit ratings.

Once an integrated resource plan is in place, the City maintains, capacity may be procured through a series of requests for proposals (RFP). RFP solicitations would be issued for different products over terms of varying lengths, enabling the utility to mitigate price volatility while meeting the goals of the planning process. Utility planning could also be coordinated with that of other agencies, such as NYPA. The planning process would be competitively neutral, neither encouraging nor discouraging retail customers from selecting competitive suppliers for commodity service. Those suppliers, the City asserts, can still compete with the utility's hedged product, because many customers may desire alternatives to the one utility rate offering supported by the portfolio prices.

Two factors, the City asserts, may discourage utilities from participating in the needed long-term contracts. First, if they are under pressure to reduce their share of the retail market, they will be understandably reluctant to incur long-term obligations. Second, the utilities have not been assured they will recover the costs of long-term contracts. The City would therefore allow utilities to fully recover the costs of prudently executed long-term contracts.

To properly charge long-term contract expenses to ratepayers, the City would divide those costs into two components -- a short-term market equivalent and a long-term

resource differential. The market equivalent costs would be recovered in utility commodity charges, while the resource differential would be recovered from all ratepayers through delivery rates. The City maintains this approach is appropriate, because all customers will benefit from the supply additions the long-term contracts will support.

While the City agrees that utilities cannot be assured with certainty that they will recover the costs of all long-term contracts, it argues that "the standard for denying cost recovery should be very high."[1] Increasing the assurance of cost recovery could be accomplished, it theorizes, through the resource planning process; a utility would be awarded a greater degree of cost recovery certainty if it could establish it had complied with the plan developed in that process.

F. PULP

The commencement of this proceeding, the Public Utility Law Project (PULP) complains, is already belated, in that this inquiry into the means for protecting consumers from price volatility was launched after customers were deprived of hedged fixed-price offers (FPO) previously provided by utilities. PULP adds that the procedural course taken in this proceeding is unlikely to generate the analyses needed to achieve its goals. PULP believes a better process would be to gather a factual record and then proceed through a series of collaborative meetings in a search for consensus, if feasible. The guidance of an Administrative Law Judge (ALJ) in this process, PULP maintains, would be useful.

Responding to the questions raised in the Notice, PULP argues that the functioning of competitive markets is not a factor which would justify restricting utility discretion to

[1] NYC Initial Comment, p. 22.

manage supply portfolios to the best advantage of their customers. PULP also asserts hedging should eliminate all or virtually all price volatility for residential customers over the short-term, when demand for energy is relatively inelastic. Over the longer term, PULP suggests, customers would be expected to reduce usage irrespective of price mitigation, in response to upward energy price trends. As a result, PULP claims, hedging would not interfere with the price signals that encourage customers to control energy consumption.

PULP would not apply an index to the management of utility portfolios, because the index's workings would be obscure and would only indirectly affect the price the customer is eventually charged. On the other hand, PULP sees value if the index is intended to quantify the effect of the hedge in constraining price volatility. The public, it believes, would be better informed if all providers are required to quote and substantiate the relationship between their fixed price products and an index.

PULP dismisses limitations on the length of time over which utilities would execute portfolio management strategies as insignificant in comparison to the issue of the price and benefits a utility can obtain from an arrangement, whatever its term. PULP would recover hedging costs through commodity charges, with the cost elements comprising those charges best arrived at in utility-specific proceedings.

As to the publication of utility commodity supply portfolio information, PULP declares that consumers desire the disclosure of complete and accurate utility prices at a time contemporaneous with the customer's usage. As a result, PULP asserts, customers should be able to learn the cost of their usage, forecast over a coming month and also longer periods, through an interactive calculator the utilities should make

available at their Websites. The content of the supply portfolio underlying this forecast cost, PULP contends, is of little or no use to residential consumers, and so its disclosure would be of little benefit.

II. Generators

A. Overview

In general, generators and generator affiliates support including long-term contracts within utility supply portfolios. Contract terms of at least one to three years in length are favored. To select among these options, the generators propose a variety of auction processes, based on the auctions conducted by individual utilities in Connecticut, the Basic Generation Service (BGS) auction supervised by the State of New Jersey, or other models. Most suggest a blended auction approach, with RFPs issued for different contract timeframes, between one and three years, to stabilize prices. Some suggest that the auction process be developed through a collaborative with the Commission approving and supervising the process that is selected.

The generators generally support price reporting, but would delay announcement of the prices obtained in auctions until the winners have the opportunity to make final arrangements for procurement of their supply. Once commodity costs are established in the auction, the generators explain, the costs can then be allocated to commodity charges that are readily quantified. Most generators believe an auction approach obviates the need for an index, because the auction's process can be devised to yield the optimal portfolio structure.

B. Constellation

Constellation Energy Commodities Group, Inc. and Constellation New Energy, Inc. (Constellation) states that the problem confronting the Commission is how to protect smaller

customers from volatility without potentially creating new stranded costs. The portfolio management techniques needed to achieve both goals, Constellation claims, are already offered by firms active in the field that can conduct auctions for obtaining the necessary hedging products, supervised by either regulatory commissions or the utilities themselves.

Constellation contends the auction approach answers questions over the flexibility utilities should be afforded in managing their portfolios, as that flexibility is achieved through the auction model that is implemented. According to Constellation, returning to the wholesale market periodically through an auction process also will yield the proper adjustments to retail rates that balance the mitigation of volatility with price transparency.

As to disclosure, Constellation would promptly publish the rate schedule that results from the auction process. The identity of winning bidders and contract length would be disclosed only after a reasonable amount of time has passed, allowing the suppliers to avoid impediments in arranging for their supply. Constellation maintains that other contract information, especially credit terms, should never be disclosed, as disclosure might chill the willingness of bidders to participate in further auctions.

C. Entergy NPM

Entergy Nuclear Power Marketing, LLC (Entergy NPM) believes utilities should devise portfolios of short, medium and long-term contracts to protect against price volatility. Such a portfolio is needed to protect small customers, says Entergy NPM, because those customers lack the resources to protect themselves by installing the advanced metering necessary to take advantage of hourly pricing.

Long-term contracts, Entergy NPM insists, are also needed to facilitate investment in new generation facility construction. The contracts, Entergy NPM claims, are critical to effectively reducing price volatility over time. For example, it posits, over contractual periods of one to three years, price volatility falls precipitously, with annual deployment of contracts for periods of two years forward reducing volatility to only approximately 15%.

D. IPPNY

The Independent Power Producers of New York, Inc. (IPPNY) supports auction approaches because, it claims, otherwise portfolio management can be accomplished only through promulgation of complex risk management guidelines. In contrast, says IPPNY, an auction process will properly protect ratepayers while affording utilities sufficient flexibility to properly structure their supply portfolios. IPPNY would allow each utility to structure its auctions independently, but, to ensure that the auctions are conducted efficiently and fairly, IPPNY would require utilities to hire independent firms to manage the auctions.

E. FPL

FPL Energy LLC (FPL) would encourage utilities to select from a designated menu of options in developing supply portfolios to protect against price volatility. FPL lists the types of auction approaches implemented elsewhere in the nation, saying that it would participate in any of them, so long as fairly administered, because auction pricing sends proper price signals to customers.

F. Ravenswood

KeySpan-Ravenswood LLC (Ravenswood) argues that effective and efficient wholesale markets create better price signals than uneconomic utility hedging practices. It favors an

auction process as the means for better developing wholesale markets. Deviating somewhat from other generators, Ravenswood cautions that long-term contracts that impede the development of competitive wholesale markets should be discouraged.

Ravenswood would, however, allow parties to continue existing hedging practices, to the extent those practices do not harm competitive retail or wholesale markets. Where hedges are entered into, Ravenswood would require utilities to describe the purpose of the hedge and its effect on reliability, the environment, fuel diversity and market power mitigation. To allow ESCOs to compete effectively with the utilities, Ravenswood would permit them to participate in the auctions.

G. NRG

NRG Power Marketing, Inc., and its five generating affiliates operating in New York (collectively, NRG), favor a BGS-style approach over what it describes as the short term of one to three years, which would, it claims, diversify utility portfolios and assist in creating the forward price signals necessary for continued investment in generating resources. Beyond the BGS auctions, NRG would include in utility portfolios a mixture of contracts with terms of one to twenty years. The longer contracts, it declares, would permit investors to finance new generation additions. NRG notes that this approach would be facilitated if the NYISO were to modify its tariff to allow the owners of generation divested by the utilities to enter into bilateral contracts. It cautions, however, that bilateral contracts should not be permitted to undermine the existing NYISO capacity market, which it believes is critical to the financial viability of existing generation facilities.

NRG deviates somewhat from the other generators in joining NYC in proposing recovery of a portion of long-term contract costs through delivery charges. It believes that such

recovery would recognize the benefit of ensuring resource adequacy to all customers.

H. PSEG

PSEG Energy Resources and Trade LLC and PSEG Power New York, Inc. (PSEG) support use of a BGS process. It believes that the auction process eliminates risks that would otherwise attend the structuring of utility-specific supply portfolios; properly transmits price signals; and, has been successfully implemented in other states. PSEG notes that, in New Jersey, a regulatory commission approves the results of the auction, after retaining an independent consultant to conduct it.

III. ESCO PARTIES

A. Overview

Expressing their concern that utility hedging practices could enable utilities to gain competitive advantages that would impede the development of competitive retail markets for energy supply, the ESCOs generally recommended that restrictions be imposed on utility hedging practices. They also argue that long-term utility hedging is inconsistent with the Retail Market Policy Statement and contend that hedging could improperly insulate customers from the price signals needed to encourage the most efficient use of energy.

ESCOs oppose the use of an index to measure electric price volatility, asserting that selection of an index, for the purpose of guiding regulatory oversight, would inevitably require a determination on the level of price volatility that is acceptable. Competitive markets would then be disrupted as utilities struggle to achieve the level deemed appropriate. They also claim that no index can measure the relationship between bill volatility and consumer welfare.

ESCOs set forth a variety of proposals on cost recovery and capacity charge cost elements. While agreeing that

utilities should be required to report more and better pricing information, the ESCOs propose differing mechanisms for accomplishing that goal.

B. Direct Energy

According to Direct Energy Services LLC (Direct Energy), long-term contracting by utilities is unlikely to reduce either price volatility generally or the bill volatility that small customers might experience. Direct Energy argues that, because all hedges must eventually expire, the rate volatility that occurs in the presence of such arrangements is not substantially different from the volatility occurring in their absence.

Claiming that bill volatility is inextricably intertwined with the customer volume volatility resulting from seasonal differences in energy use, Direct Energy maintains small customer bill volatility is best addressed through bill levelization methods. Criticizing existing budget billing methodologies as failing to prevent substantial increases in customer bills from one year to the next, Direct Energy proposes a detailed methodology it says would effectuate bill levelization properly. That methodology is based on averaging bills over a rolling twelve-month period, coupled with a monthly adjustment charge of one-twelfth of the outstanding over-collection or under-collection.

Direct Energy would supplement its budget billing methodology with utility purchases consisting of one-month forward arrangements, obtained through an auction process. The price of the utility's default service would be based on the overall price of the supply obtained in the monthly auctions. Direct Energy asserts this approach will remove barriers to the development of competitive markets, inherent in any utility default service that is based on long-term contracts, while

limiting price volatility to the extent feasible in a competitive market.

The monthly hedging costs, Direct Energy explains, are readily recovered through commodity pricing mechanisms, along with the NYISO costs embedded in the pricing of wholesale commodity at the delivery point. Its monthly pricing system, says Direct Energy, also simplifies price reporting, because the monthly price is readily reported and compared to other prices. If hedging mechanisms of more than one month are adopted, Direct Energy cautions, a balance must be achieved between two equally important objectives of disclosure policy: ensuring transparency of utility commitments and preventing disclosure of information that market participants might use to drive up the costs of future hedging arrangements.

C. Hess

If utilities are allowed to engage in hedging, Hess Corporation (Hess) would limit the term of the hedging arrangements to no more than three months. It notes that a three-month limitation on hedging transactions is consistent with the approach to default service taken in other states, for customer classes with peak demands as low as 25 kW.

Complaining that utilities, unlike ESCOs, are insulated from hedging risks because those risks are subsidized by regulated delivery customers, Hess maintains that hedging costs should not be recovered from ratepayers. Instead, it argues that utility shareholders should bear the costs of hedging risk. Hess maintains that this approach is consistent with what should be a brief and transitional utility foray into the commodity supply business.

Arguing that utility commodity charges must fully disclose the cost of commodity, Hess would establish the components of the commodity charge in considerably greater

detail than utility tariffs currently provide. Hess would reflect in the commodity charge all NYISO costs, localized by NYISO zone and allocated to the proper customer class to the extent feasible. For some NYISO cost components like UCAP, Hess continues, costs might be assigned on a customer-specific basis.

In order to better promote price transparency, Hess would require utilities to file, every six months, a plan that fully describes hedging methods and volumes. Hess contends that the plans should also identify the generation sources the utility currently relies upon to meet its full service load. According to Hess, this level of disclosure already exists in other states, such as New Jersey.

D. Intelligent

Infinite Energy, Inc. d/b/a Intelligent Energy (Intelligent) adamantly opposes utility hedging, characterizing the practice as a form of gambling with ratepayer money. It describes historic gas futures contract prices it says support its characterization.

If the utilities are permitted to hedge, Intelligent would limit hedging to no more than one heating season, and would restrict hedging volumes. Intelligent would also require utilities to report their hedging activities on a monthly basis, identifying prices after the execution of hedging transactions.

E. Energetix

Energetix, Inc. and NYSEG Solutions, Inc. (Energetix) voices its expectation that utility commodity service will eventually be tied exclusively to short-term spot market prices. During the transition to that end state, Energetix would restrict utilities to hedging no more than 40% of their small customer retail load. Energetix believes hedges should be structured into four packages, each for a two-year time period, entered into at the beginning of an electric capability period.

Energetix would set commodity charges in conformance with the Strategic Power Order.[2] It interprets that Order as requiring the unbundling of a market supply charge to separately identify actual market costs, hedging gains and losses, and other reconciliations. Energetix notes that the Order did not provide for the recovery of any commodity costs through delivery rates, because that would dilute the value of the hedges.

Under its approach, Energetix claims, reporting requirements are simplified. The semi-annual hedge purchase and rolling average costs are readily reported after the hedges are procured, without identifying the vendors that provide them. This reporting, Energetix maintains, would yield the price transparency critical to the success of competitive markets.

F. NEM

Cautioning that, in falling markets, hedging activities may result in higher prices for consumers, National Energy Marketers Association (NEM) would analyze each utility's hedging activities to determine if its efforts are in the best interest of its customers or are instead intended to maintain utility market share. One indicator of that intent, NEM claims, is if a utility conducts marketing through an affiliate that bears the same name as the utility.

NEM supports restricting utility hedging to a monthly timeframe. To the extent that customers desire additional protection from price volatility, NEM asserts, they should be expected to obtain that protection in the market. Otherwise, NEM warns, utilities might charge premiums for hedged services, and it claims that those premiums, for some New York utilities,

[2] Case 06-M-0003, Strategic Power and Management, Inc., Order Denying Complaint in Part and Directing Tariff Filing (issued August 2, 2006).

have amounted to as much as 25% above the cost of variable price offerings.

NEM believes that cost causation principles dictate that hedging costs be recovered only through commodity rates. Recovery through delivery rates, it asserts, might double-charge delivery customers that take service from competitive providers, who must recover all of their costs in a commodity charge.

More comprehensive utility price reporting is also needed, NEM argues, to enable consumers to accurately compare ESCO and utility prices. NEM recommends submission, on a continuing basis, of periodic reports detailing the strategies and methods used to hedge prices; the implementation of the hedging strategies; and, the status of each hedge and its role in the overall price charged. If this hedging reporting is restricted to retrospective prices, NEM claims, confidentiality concerns are avoided.

G. NYSEMC

The New York State Energy Marketers Coalition (NYSEMC) would restrict utility hedging practices, but would enable competitive providers to participate in the hedges, to prevent utilities from gaining an unfair competitive advantage over competitors. NYSEMC would provide for the phasing out of utility hedging activities over a period of three to five years, by slowly reducing the volume of load a utility could hedge until each utility has exited the hedging function.

NYSEMC also believes that a more extensive inquiry is needed into the role gas storage plays in competitive markets. That gas utilities are virtually guaranteed they will recover their gas storage costs, NYSEMC claims, affords them a significant competitive advantage over ESCOs that are at risk for recovery of such costs. As a result, NYSEMC would require

utilities to withdraw from the gas storage business, after a transition period.

All properly allocated commodity costs, says NYSEMC, should be recovered through commodity charges, because recovery through delivery charges distorts price signals. Better price reporting, NYSEMC contends, is best accomplished through restricting hedging to short-term mechanisms, which NYSEMC believes are more readily transparent to customers and competitors than long-term arrangements.

H. Shell

Shell Trading Gas and Power Company (Shell) maintains that, while utilities require flexibility in structuring their supply portfolios, some guidance is required. Shell would establish, through a collaborative, a procurement process for each utility. That process would, in turn, drive the structure of the utility's hedging portfolio.

While opposing indexing for the purpose of measuring utility success in dampening volatility, Shell would establish standards for determining the level of volatility that is acceptable. Shell maintains use of a standard would reveal the effect wholesale price movements have on retail price volatility, and could assist utilities in selecting the best tools for constraining volatility. Shell cautions, however, against allowing hedging contracts to run for more than three years. It asserts that overly long contract terms can exacerbate volatility, if prices rise substantially after a hedge expires.

After a procurement process is implemented, Shell asserts, winning bidders and the average prices obtained for each solicitation can be reported. According to Shell, this approach avoids the disclosure of the specific price each bidder offered.

I. UGI

UGI Energy Services, Inc. (UGI) would restrict utility hedging practices to hedging instruments of no more than one month in duration. UGI believes hedging costs should be recovered through commodity charges instead of delivery charges, but that the financial risk of liquidating excess gas purchases should be born by utility shareholders.

UGI sees no reason why information on the commodity a regulated utility purchases should not be public. UGI would require utilities to describe their methods of obtaining commodity and to translate the cost of their commodity purchases into the prices charged customers.

J. SCMC

The Small Customer Marketer Coalition and Retail Energy Supply Association (SCMC) would limit the length of hedging arrangements to no more than three to six months, with even shorter periods perhaps suitable for gas hedging. SCMC contends that this approach would address volatility while avoiding saddling utilities with long-term obligations that would intrude upon the functioning of competitive markets.

If more extensive hedging is allowed, SCMC asks that its anti-competitive aspects be constrained. Utilities, SCMC contends, can gain competitive advantage because they rely upon investment grade credit ratings obtained as a result of their regulated delivery service activities, making it less costly for them to engage in hedging than ESCOs whose credit ratings are not as robust. Utilities are also held harmless against hedging risks, SCMC argues, because they can recover hedging costs from regulated ratepayers. SCMC also compares the impact of utility hedging practices to the impact of utility-provided FPOs, which have been declared anti-competitive and a barrier to market entry.

Allowing utilities to recover the costs of hedges in commodity charges, SCMC claims, improperly embeds their competitive advantage in the utility price customers compare ESCO offerings against. As a result, SCMC believes that some hedging costs should be recovered through delivery rates. Since delivery customers support utility hedging in any event, SCMC theorizes, hedging costs are properly imposed on them, even under traditional cost causation principles. Dismissing the concern that delivery rate recovery will dilute the value of hedges, SCMC points out that because mass market customer migration rates are low, most customers in those customer classes remain utility customers and therefore are properly charged the value of the hedge in any event. SCMC also asserts that hedging often increases costs, and that adverse impact can be mitigated if cost recovery is spread over the broader base of all delivery customers. As an alternative, SCMC suggests that utility shareholders could bear the risk of hedging costs.

With hedging costs recovered through the delivery rate, SCMC contends that the cost elements comprising commodity charges are properly limited to the NYISO cost components. It is possible, SCMC theorizes, that customer-specific capacity costs might be developed for larger customers.

SCMC would require utilities to report supply portfolio information every six months. Utilities would include in their reports the level of full service load; the sources relied upon to serve that load; the hedging anticipated during the upcoming capability period; and, a description of the hedging strategy and instruments that would be deployed. SCMC contends that furnishing this information would not impair the utilities' negotiating position with prospective suppliers, while its availability would enable ESCOs to properly structure their products in competition with the utility.

SCMC would also require reporting of actual hedging instrument types, quantities and costs. SCMC maintains that submittal of this information will assist the Commission in assessing the prudence of utility hedging decisions.

III. DELIVERY UTILITIES

A. Overview

Utilities generally opposed the promulgation of guidelines that would constrain their flexibility in structuring their supply portfolios, maintaining that other forms of review are sufficient to protect ratepayers against unreasonable hedging activities. Most utilities believe that guidelines will likely be either too vague, rendering them ineffective, or unduly prescriptive, preventing them from adequately hedging at least cost. They claim they should be left free to devise the degree of price mitigation that best protects customers, without the hindrance of guidelines.

If guidelines are adopted, utilities would limit them to broad statements of principle. They add that regulatory oversight functions can be adequately performed if utilities meet with Staff on approaches to their supply portfolios.

The utilities argue that an index measuring price volatility is not needed, because indexing is unlikely to yield benefits to ratepayers and could instead overly constrain utility discretion to the detriment of ratepayers. An index, they claim, could also entice utilities into over-hedging for the purpose of ensuring a margin of compliance with the index's requirements, thereby imposing excessive costs on ratepayers.

Most utilities believe commodity costs, including hedging costs, are best recovered through commodity charges. As migration increases, they point out, the value of a hedge is diluted if it is spread over all delivery customers. Customers that purchase a hedged product from a competitor could also pay

twice for the same service, once through the competitor's charge and again through the utility's delivery charge.

Utilities insist that publishing information about their wholesale supply portfolio could impede their ability to negotiate the best prices on behalf of their ratepayers. They also generally contend they already make price information available through their tariffs or otherwise. As a result, they either oppose additional disclosure altogether or would limit the scope of that disclosure to historic and aggregate data.

B. Central Hudson

Central Hudson Gas & Electric Corporation (Central Hudson) asserts that its hedging activities do not disrupt competitive markets and are instead a feature typical of those markets. Central Hudson also finds the promulgation of guidelines inconsistent with the Commission's pronouncements rejecting continuation of FPOs by utilities, because if customers do not need the protection of FPOs, they do not need the protection of guidelines either.

Central Hudson opposes any guideline requiring it to enter into contracts of more than two to three years in length. It asserts longer-term contracts create credit risk, because credit rating agencies treat them as debt equivalents. That credit risk, it declares, translate into higher borrowing costs that could increase rates for captive customers.

C. Con Ed/O&R

Consolidated Edison Company of New York, Inc. (Con Edison) and Orange and Rockland Utilities, Inc. (O&R) (Con Ed/O&R) caution that guidelines should be structured to avoid impediments to the development of competitive energy markets. Con Ed/O&R would restrict guidelines to the statement of broad principles, allowing each utility to structure an approach to hedging that best benefits its service territory.

Noting that Con Edison still recovers some hedging costs in its delivery rates, Con Ed/O&R report that changes to that approach will be considered in the utility's next rate case. As a result, they believe a commodity charge should include all energy costs, all related NYISO costs and the cost of hedging transactions.

Con Ed/O&R contend that hedging should be restricted to arrangements of no more than three years in length. The utilities find that period sufficient to smooth out seasonal cycles, while protecting ratepayers from the excessive costs that might be incurred over a longer period of time. The utilities add that hedging is an insurance transaction, and so purchasing price stability will not always result in prices lower than for unhedged transactions. They also believe that hedging activity should be phased out as competitive markets develop, with the level of hedging deemed appropriate for each customer class decided in rate cases.

D. KeySpan Delivery

The Brooklyn Union Gas Company d/b/a KeySpan Energy Delivery New York and KeySpan Gas East Corporation d/b/a KeySpan Energy Delivery Long Island (KeySpan Delivery) emphasized that existing gas utility hedging practices are working well. As a result, the utility would not constrain the length of hedging arrangements to a particular period, would allow each utility to judge which longer-term arrangements, with their attendant risks, would best protect ratepayers.

While KeySpan Delivery concedes that price transparency is important, it cautions that the disclosure of even historical purchase prices and volumes could disadvantage ratepayers, by encouraging suppliers to seek to replicate the highest prices paid in the past. Excessive disclosure, the utility posits, might also increase price volatility, by

encouraging market participants to speculate based on the data they have obtained.

E. NFGD

National Fuel Gas Distribution Corporation (NFGD) points out that, while approximately 88% of its residential customers select it as their commodity supplier, nearly 100% of its large commercial and industrial customers choose to purchase commodity in the market. A portfolio of arrangements of less than two years in length, NFGD claims, is adequate to protect consumers because that period adequately reflects changing market prices while avoiding excessive price volatility.

NFGD reports that it posts its gas supply prices monthly, as specified by its tariff. This disclosure, it argues, adequately informs customers and is sufficient to promote the development of competitive markets.

Opposing more extensive disclosure, NFGD points out that specific price and other contract terms have long been treated as confidential trade secrets, and there is no justification for reversing that long-standing policy. Allowing ESCOs and suppliers to gain access to the prices it has paid in the past, NFGD concludes, would encourage ESCOs to charge more, in order to maximize their profit margins.

F. NYSEG/RG&E

New York State Electric & Gas Corporation and Rochester Gas and Electric Corporation (NYSEG/RG&E) maintain that hedging guidelines should recognize that utilities are experienced in supply portfolio management, and should be structured to achieve price transparency, to promote customer choice, and to enable customers to respond to price changes. The utilities also argue the Commission should not attempt to dictate the optimal balance between protection from price volatility and the dissemination of accurate price signals.

Differing with most other utilities, NYSEG/RG&E would recover hedging costs through a transition charge collected from all delivery customers. The utilities believe this approach results in a level playing field for competitors and sends efficient price signals to consumers. The commodity charge would then be structured to recover commodity purchase costs and administrative costs.

Contending that no new price reporting requirements are needed, NYSEG/RG&E point out that the NYISO already posts electric prices and utilities already file natural gas costs with the Commission. Any further disclosure, they argue, would compromise the ability of utilities to comply with confidentiality requirements imposed under their supply contracts.

G. National Grid

After expressing its support for competitive markets and the Retail Market Policy Statement, Niagara Mohawk Power Corporation d/b/a National Grid (National Grid) states that, in conformance with its Merger Rate Plan,[3] it has ended hedging for the benefit of its larger customers and is ceasing hedging for the benefit of medium-sized customers in 2008. It will, however, continue hedging for the benefit of residential and small business customers, with more than 50% of that load hedged through 2011.

National Grid asserts its approach to hedging is working well, and that additional hedging requirements should not be imposed at this time. In particular, the utility opposes mandating entry into long-term commodity supply contracts, which it claims would distort the wholesale supply market. It adds

[3] Case 01-M-0075, Niagara Mohawk Holdings, Inc., Opinion and Order Authorizing Merger and Adopting Rate Plan (issued December 3, 2001).

that it cannot make long-term commitments to suppliers, when its customers no longer make long-term commitments to it. If a long-term supply requirement is adopted, National Grid argues such commitments should be limited to a length of no more than two years, because arrangements of that duration have only a limited impact on retail market development.

While National Grid contends that the cost of legacy hedges should be allocated to all delivery customers, it believes hedging and other commodity costs are otherwise best recovered through commodity charges. It also asserts its tariffed commodity charges yield a price that can be used as a market benchmark.

Reply Comments

I. Consumer Advocates

A. NYC

Maintaining that there is significant support for requiring utilities to engage in long-term planning, NYC lists a variety of topics the utilities should be required to address in those plans. It also urges that planning commence promptly, so that the need for new resources in southeast New York, which is expected to arrive at about 2011, can be met.

According to NYC, parties generally believe that some form of hedging is necessary to protect consumer interests. Long-term contracts, the City insists, are an appropriate form of hedging that should be a component of utility supply portfolios. The City therefore agrees with those generators that propose using long-term contracts as a tool for promoting the development of new generation facilities, and with the general approach of developing auctions as the means for obtaining those contracts.

NYC, however, finds some of the restrictions generators would impose upon an auction process unreasonable.

For example, the City disputes IPPNY's proposal to open competitive solicitations to all resources on a non-discriminatory basis, and contends instead that auctions can be tailored to specific purposes. The City also prefers utility-specific procurement approaches to BGS-style auctions, which it believes are expensive to administer and review and may be open to gaming by bidders.

Dismissing objections to long-term contracting, the City argues that opponents premise their positions on mistaken assumptions. For example, it asserts, Central Hudson seems to believe generation markets in New York City are competitive, when they are not.

Utilities, the City maintains, are qualified to assume the role of purchasers under long-term contracts. Addressing Central Hudson's complaint that entry into long-term contracts can push credit ratings downward, the City asserts appropriate regulatory mechanisms can be developed to counteract that effect. It also suggests that alternatives to utility purchasers, like NYPA, can be deployed if utilities fail to enter into long-term contracts.

Advocating short-term hedging as a component of utility portfolios, NYC asserts opponents of short-term hedging take the contradictory position of acknowledging that utilities are inherently superior to competitive suppliers at hedging activities, but opposing hedging because of its alleged effect on the development of competitive markets. Those markets, the utility asserts, should be developed only upon principles that are not disadvantageous to consumers. The City expects that utilities will remain the primary source of commodity for small customers, because it doubts that "competitive suppliers will

ever be able to serve those small customers as efficiently as the utilities can."[4]

Responding to utility objections to hedging portfolio disclosure, the City asserts utilities should provide two types of information on hedging strategy. First, a utility should detail the level of supply it has procured and the prices it expects to charge for a coming year, so that competitive suppliers can market against that price. Second, information on the type and length of long-term contracts the utility has entered into should be made available to competitive suppliers and other market participants. The current Con Edison variable commodity charge, the City claims, is not an acceptable means of reporting because it is unpredictable and uninformative.

NYC believes further collaborative efforts are needed to develop strategies and mechanisms for accomplishing its goals. The collaboratives would result in joint filings, supplemented by filings of individual parties where a consensus cannot be reached.

B. PULP

According to PULP, if hedging strategies benefit consumers, they should be implemented whatever the impact on the operations of competitive markets. It also stresses that hedging cannot be deemed to interfere with effective price signals, because hedging dampens volatility without disguising other price impacts. Volatility, PULP asserts, is not itself a useful signal because energy investment and usage decisions made in response to volatility are not efficient. Responding to arguments that hedging raises prices, PULP finds value in the price stability hedges bring and so dismisses the price comparison as inapposite.

[4] Reply Comment, p. 17.

Responding to other points parties raised, PULP maintains that the transition from one hedge to another could be managed through designing the hedges to allow for some price fluctuation. PULP also argues that long-term contracts priced under prevailing market levels are not detrimental to consumers merely because they will induce consumers to move to the lowest-price provider. That, says PULP, is a proper outcome of competitive markets, even if the impact on a particular competitor may be adverse.

PULP disputes Direct Energy's claim that budget billing is a tool for reducing price volatility. According to PULP, budget billing smoothes fluctuations in customer usage, but is not intended, and is ineffective, in eliminating fluctuations caused by month-to-month price changes. PULP points out that budget billing, as defined in PSL Article 2 and the Commission's regulations, is not tied to price variations and so is unlikely to yield bill stability under circumstances when price volatility is experienced. PULP also maintains that hedges shift risk away from consumers, an outcome budget billing cannot accomplish.

II. Generators

A. Entergy NPM

Entergy NPM opposes ESCO proposals to restrict hedging arrangements to terms of one month or less, arguing that such a limited time period would make it impossible to protect consumers from price volatility. Entergy NPM instead favors flexible utility procurement mechanisms, which would permit utilities to obtain supply through competitive solicitations over a variety of time periods.

B. IPPNY

IPPNY joins Entergy NPM in opposing restrictions on the length of hedging arrangements. Responding to Direct

Energy's argument that long-term contracts are unlikely to reduce volatility, IPPNY argues that a portfolio comprised of long-term hedges will, by definition, be less volatile than a portfolio comprised of short-term hedges, because short-term price swings will be avoided.

IPPNY also claims that Direct Energy has failed to demonstrate that long-term contracts harm competitive retail markets, and asserts that the ESCO undermines its position by conceding that New York's markets are generally competitive even though utilities currently enter into long-term contracts. Moreover, IPPNY posits, as utilities compete to obtain long-term supplies, they will obtain information that will indicate when it is necessary to develop new supply resources.

III. ESCOs

A. Direct Energy

Although Direct Energy believes that properly-structured long-term contracts can be consistent with competitive markets, it opposes the proposals of generators and some consumer advocates to require utilities to enter into long-term contracts, through an auction process or otherwise. Such a requirement, it asserts, would displace the functioning of the competitive market, in deciding which hedging devices are the most efficacious, with regulatory fiat, which would disrupt competitive markets and deprive consumers of market efficiency. Direct Energy points to the Electric Reliability Council of Texas as an example of a market that functions well without requiring utilities to enter into long-term contracts, but where such contracts exist as a result of market forces.

Direct Energy also maintains that BGS-type auction processes are unsuccessful in constraining bill volatility. It reiterates that bill levelization accomplished through its

proposed budget billing method will better protect consumers from bill volatility than hedging would.

B. Hess

Like Direct Energy, Hess opposes BGS or other auction-type structures. Use of the BGS approach in New Jersey, it claims, has resulted in a market where no residential customers are currently served by competitive suppliers. Similar flaws, Hess protests, afflict all long-term contract models and integrated resource planning processes.

C. SCMC

SCMC joins other ESCOs in opposing BGS or other auction approaches, claiming that auctions have failed to reduce price volatility, have yielded electric prices in excess of those available in hourly markets, and have stymied the development of residential competition. SCMC also points out that the BGS approach was rejected in the Retail Market Policy Statement. If the approach were adopted, SCMC warns, the considerable investment ESCOs have made in developing a robust and sophisticated market presence in New York will be lost.

IV. Utility Replies

A. Central Hudson

According to Central Hudson, most customers are unconcerned with the price volatility they have experienced, as opposed to the magnitude of the price increases themselves. Those price increases, Central Hudson asserts, are not caused by volatility, but by the failure of the market to attract sufficient new generation resources to New York, especially within NYISO Zone J. The ill effects of resource inadequacy in Zone J, Central Hudson theorizes, then radiates outward to create pricing problems in nearby zones, like Zone G, where most of its service territory is located.

An integrated resource management approach, Central Hudson maintains, will not resolve this resource inadequacy. Instead, large-scale capital formation, on the order of billions of dollars, is needed to support the construction of new generation resources. To Central Hudson, the solution is obvious -- utilities must build new coal-fired generation in or near to Zone J to reduce the present over-dependence on natural gas as a fuel.[5] The costs of its coal-fired facilities, says Central Hudson, could be recovered through an assessment charged to the customers that benefit.

Central Hudson opposes generator and ESCO proposals to constrain utility discretion in structuring their hedging portfolios. These proposals, the utility asserts, would dangerously deny customers the benefits of utility experience to their detriment, and to the benefit of only the generators and ESCOs that would gain competitive advantage as a result. It claims that the ESCO proposals would cause a "deterioration in utility-delivered services, in the hope that customers will then turn to ESCOs for improvement."[6] Voicing doubts about the viability of mass market competition, the utility believes a re-evaluation of whether competitive alternatives are workable for those customers is needed.

Responding to ESCO proposals to require utilities to bear the risks of hedging, Central Hudson notes that such an approach would necessarily entail allowing utilities to retain gains as well as to absorb losses. It claims, however, that the

[5] While nuclear plants might also serve the same purpose, Central Hudson describes their construction as a relatively low probability event, feasible only somewhere upstate too remote from Zone J to resolve its problems.

[6] Central Hudson Reply, pp. 24-25.

proposals are too lacking in detail to allow for meaningful calibration of the risks that would arise under them.

Like the ESCOs, however, Central Hudson criticizes BGS and auction approaches. The utility maintains that recent BGS auctions may have locked in prices well above those available in short-term markets. Mandated long-term contracts, the utility asserts, are also disadvantageous, albeit those contracts can be useful in certain circumstances if not mandated.

PULP's goal of deploying hedging to eliminate all or virtually all price volatility, is, Central Hudson asserts, unrealistic. Moreover, the utility argues that PULP's objective would insulate customers from price signals, thereby adversely affecting efforts to promote energy efficiency.

Disagreeing with SCMC, Central Hudson argues that the ESCO's proposal to recover capacity costs through delivery rates is inappropriate. The utility also dismisses the claim that it can rely upon monopoly revenues to support its credit rating when purchasing hedges, because, it asserts, its delivery revenues are less than its commodity revenues, which are the revenues at risk when it hedges. Large ESCOs, the utility adds, have revenue streams equivalent to its delivery revenues.

Central Hudson discerns in ESCO proposals to impose reporting requirements an effort to compel utilities to publish a utility "price to beat" that, the ESCOs seem to believe, would facilitate their marketing efforts. Central Hudson finds no connection between publication of a "price to beat" and the utility commodity supply and hedging issues raised in this proceeding. As a result, it would not address "price to beat" issues here.

B. Con Ed/O&R

Con Ed/O&R asserts flexible electric hedging policies similar to those in place for gas price hedging would result in

adequate mitigation of volatility for customers while allowing for some exposure to price signals and encouraging continued retail migration. As a result, the utilities oppose proposals to constrain utility hedging discretion.

Con Ed/O&R declare that integrated portfolio management proposals are beyond the scope of this proceeding. According to the utilities, adequate resource planning is taking place under the NYISO's Comprehensive Reliability Planning Process (CRPP). The utilities also claim that long-term contracting inherent in the planning approaches NYC and others propose risks repeating the experience with mandated long-term contracts in the 1980's and 1990's, when many contracts proved substantially overpriced. The utilities raise similar objections to the BGS and other auction proposals.

Arguing there is no basis to proposals to shift the risk of hedging costs to shareholders, Con Ed/O&R point out that hedging costs are costs incurred in serving retail customers. Those costs, whether they result in gains or losses, should therefore be flowed through to those customers. There is no comparison between utility investors and ESCO investors, the utilities continue, because utilities must supply all customers that request service, while ESCOs can choose their customers and can earn an unregulated return, adequately compensating them for the risk of their investment.

Finally, Con Ed/O&R dismiss criticisms that they have made their commodity service intentionally less palatable to consumers. The utilities state they have complied with Commission policies on the implementation of retail access, and that the Commission adequately monitors those policies.

C. NFGD

Arguing against ESCO price reporting proposals, NFGD claims allowing access to data the ESCOs request would cripple

its ability to negotiate gas purchases in the best interests of its ratepayers. NFGD also accuses ESCOs of pursuing the data so that they may, in effect, engage in price fixing arrangements by more closely tying their prices to utility prices instead of competing with the utility.

D. National Grid

Stating its continued support for the Retail Market Policy Statement, National Grid asserts that mandating long-term contracts would obstruct the development of competitive markets and could lead to a new wave of stranded costs. The utility believes that fostering new entry into generation markets is best left to the NYISO, which, it asserts, is addressing the issue through its demand curve and forward capacity markets.

Agreeing with other utilities, however, National Grid states that the costs of hedging should be recovered from the customers who benefit and should not be imposed on utility shareholders. It also joins with other utilities in opposing proposals to require disclosure of commodity supply contract price information and to constrain utility discretion in structuring hedging portfolios.

E. NYSEG/RG&E

NYSEG/RG&E oppose expanding the scope of this proceeding to include resource planning issues. They also argue that BGS and auction type approaches are unlikely to substantially benefit consumers and so should be rejected. They join with Niagara Mohawk in criticizing proposals to require greater disclosure of hedging contract prices and with Central Hudson in contradicting ESCO claims that utilities possess an inherent competitive advantage in their superior credit ratings. The utilities also defend the FPOs they formerly or currently offer.

Opposing Direct Energy, NYSEG/RG&E reject the ESCO's claim that its budget billing proposal would protect consumers from price volatility. The utilities are also concerned that the ESCOs' levelization approach could expose a customer to a large one-time cost upon its exit from the utility's service territory, and could make it difficult for the utility to collect that cost.