National Energy Marketers Association

I/M/O THE PROVISION OF BASIC GAS	)	
SUPPLY SERVICE PURSUANT TO THE	)	
ELECTRIC DISCOUNT AND ENERGY	)	Docket No. GX01050304
AND COMPETITION ACT OF	)	
1999, N.J.S.A. 48:3-49 et. seq.	)	

COMMENTS OF THE NATIONAL ENERGY MARKETERS ASSOCIATION ON BASIC GAS SUPPLY SERVICE

The National Energy Marketers Association (NEM) hereby submits Comments in response to the Order Establishing Procedural Schedule issued in the above-referenced proceeding on June 6, 2001, pertaining to Basic Gas Supply Service (BGSS) being rendered on a competitive basis.

The National Energy Marketers Association (NEM) is a national, non-profit trade association representing both wholesale and retail marketers of energy and energy-related products, services, information and technologies throughout the United States. NEM's membership includes: small regional marketers, large traditional international wholesale and retail energy suppliers (as well as wind and solar power), billing and metering firms, Internet energy providers, energy-related software developers, risk managers, energy brokerage firms, information technology providers and both manufacturers and suppliers of advanced distributed generation. Our membership has both affiliated and unaffiliated companies.

This regionally diverse, broad-based coalition of energy and technology firms have come together under the NEM auspices to forge consensus and to help eliminate as many issues as possible that would delay competition. NEM is committed to working with representatives of state and federal governments, large and small consumer groups and utilities to devise fair and effective ways to implement restructuring of natural gas markets.

NEM has developed "***National Guidelines for Designing and Pricing Default Energy and Related Services***," and "***National Guidelines for Unbundling and Restructuring the Natural Gas Distribution Function***," copies of which are attached hereto and incorporated by reference. NEM submits that in a restructured environment the utilities' historical obligation to serve should be converted into an obligation to connect and deliver. Therefore, while the utilities should and will continue to provide transportation or distribution service for all customers, it is not necessary or desirable to establish the utilities, on a long-term basis at least, as the default provider of energy supply services. Indeed, the sooner the competitive market can super-aggregate small customers the sooner true price competition can begin. It is from this perspective that the questions included in the June 6 Order are addressed below.

A. SHOULD BGSS BE COMPETITIVE

1. What benefit would customers see if BGSS were made available on a competitive basis?

State economic regulation of the true distribution monopoly function reduces costs to society by eliminating duplication and by regulating monopoly profits. Therefore by definition, limiting regulation to the natural monopoly function, while permitting robust competition on all other functions, products, services, information and technology, should maximize benefits of innovation, reduce prices and provide higher quality service, while minimizing the economic distortions inherent in monopoly economics. Clearly the public interest is not served by charging monopoly prices for competitive services. Additionally, as regulated utilities fully unbundle energy supply and service functions, the provider-of-last-resort function can be provided by qualified suppliers and the obligation to serve can be modified into an obligation to connect and deliver.

Retaining the utility as the default provider of energy supply and other competitive services long term in a restructured environment will present a major barrier to the development of competitive markets. The structure and pricing of default service are critically important issues in determining whether consumers will receive the benefits of meaningful price competition. When states mandate the selection of incumbent utilities for all consumers who fail to make timely supplier elections and set a non-competitive price for default service, it perpetuates the same non-competitive energy services that restructuring is designed to replace.

2. Would benefits accrue uniformly to all classes?

It is imperative that default pricing mechanisms not hide the true costs of providing retail energy services. Correct price signals are critical to both lower prices and conservation. Merely showing the "price to compare" as wholesale cost of power does not benefit default service customers because they are sent a false price signal and are still paying other costs to provide gas sales service in the distribution component of the bill. Default service pricing must be designed to reflect retail costs to avoid producing artificial or cross-subsidized price signals. Suppliers of competitive BGSS service will incur costs in addition to the wholesale cost of the energy commodity including no notice service, pipeline capacity charges, city-gate delivery requirements, and related-commodity charges, a share of pool operating expenses, risk management premiums, load shape costs, commodity acquisition and portfolio management, working capital, taxes, administrative and general expenses, the costs of metering, billing, collections, bad debt, information exchange, compliance with consumer protection regulations, and customer care. These costs must be reflected in the default service rate.

When utilities are limited to performing solely monopoly functions and all other competitive services are offered by the marketplace, all consumers will receive the benefits including the potential to receive innovative product, service, information and technology offerings and to benefit from lower prices engendered by competitive market forces.

3. **Would reliability be maintained? How?**

With respect to reliability concerns, NEM submits that risk management is a core competency for competitive suppliers. Utilities have relied primarily on the BPU to manage risks. The sooner market forces can monetize supply risk, the sooner price competition can occur. Additionally, if the political demands of the state require extra reliability then specific reserve margins can be specified in an RFP for the default supplier so that qualified suppliers can competitively bid for the extra reliability required. Marketers have long been involved in developing and aggregating natural gas supply and managing supply risks. Indeed, in many cases, marketers have supplied utilities with energy and related services on an outsourced basis for years. Competitive suppliers have extremely sophisticated trading operations unparalleled in the regulated paradigm.

4. **If the Board were to make BGSS competitive, should the Board allow 100% of utility customers to be eligible, or should there be a transition program?**

Basic Gas Supply Service should be a last resort service and not a standard service option. It should be used in emergency or special circumstances. Customers should be eligible to receive BGSS when they are no longer being served by a competitive provider, i.e., if the customer's provider stopped doing business in the state.

BGSS should be structured to encourage minimum stays not mandated minimum terms. There should not be an incentive for any class of customer to use the BGSS option as a long-term standard service option. Accordingly, it is important to prohibit the BGSS entity from mandating that a customer enroll for a minimum term as a condition of service in the competitive market. If customers are required to enroll for minimum service terms, the customers will be unable to shop for other competitively priced services or switch to take advantage of other types of services. As ridiculous as it seems, there are still customers renting their telephones.

In the long term all consumers in restructured energy markets should be served by competitive energy service providers at competitive prices. It is desirable to get to that end state as quickly as possible following the opening of the market. An example of an approach that holds promise for accomplishing a quick transition to a fully competitive market is to assign customers to competitive providers after a limited period of time. Utilizing this approach, customers who have not selected a competitive supplier during a specified enrollment period are assigned to reliable suppliers based on the market shares of those suppliers. Although there may be some regulatory restrictions and requirements, the price and non-price attributes of the default service offer under this model are determined by individual suppliers and reflect efficient and true market conditions. See also Response to Question B.8.

B. If BGSS were to be made available on a competitive basis - GENERAL

1. **What is the role of the regulated gas distribution company if BGSS becomes available competitively?**

If BGSS becomes available competitively, the role of the regulated gas distribution company will be limited to an obligation to connect and deliver. Qualified suppliers can bid on emergency supplies at competitive prices.

2. **How do you envision BGSS being supplied?**

3. **Is it necessary that one supplier provide BGSS to all customers?**
    a. **If not, is it necessary that all similar customers be priced the same?**
    b. **Would BGSS be divided as a "slice of the system", or on some other basis?**

The costs to provide default service vary by customer group. Properly designed default service prices should reflect these differences to encourage competition for all customer classes. NEM supports the proposition that the BGSS entity could be different by customer group. Inasmuch as the costs to provide services varies by customer class, the BGSS entity and BGSS pricing should be structured to reflect those real price differences, and as a result, will encourage competition for all customer classes. Furthermore, NEM asserts that the BGSS function should reflect all of the political, social and reliability concerns of providing last resort service. The BGSS function can include a hedging requirement as well as a reserve requirement as part of the request for competitive proposals.

NEM also urges that specific programs be designed to address low-income needs rather than trying to utilize default service for this purpose. Often, concerns that low-income individuals will be unwelcome in the competitive market drives, explicitly or implicitly, the design and pricing of default service. This approach serves neither low income customers nor the development of a competitive market well. Specific programs should be designed to serve low-income needs and to facilitate the targeting of public benefits funds. Such programs might include aggregation of low- income customers to access lower prices in the competitive market, perhaps with subsidies or guarantees of payment that would ensure the lowest-cost supply for these customers.

4. Should there be any restriction on affiliates competing for BGSS service?

Automatically presuming that an entity affiliated with the incumbent utility should act as the default supplier in lieu of the utility itself grants that entity an unfair competitive advantage and violates the important principle that all market participants should be treated in a competitively neutral fashion. In contrast, the representative assignment of default service customers to competitive suppliers, or the award of default service to one or more suppliers through a bidding process, will result in increased market diffusion and an improved ability on the part of suppliers to aggregate customers, spread costs and compete on the basis of price.

5. Would billing and metering be a part of BGSS service?

NEM submits that all metering services, including ownership, installation, servicing of equipment, maintenance, testing, reading, data management, validation, editing, estimations, providing pulse output and billing are services that should be rendered by the competitive marketplace. As such, competitive suppliers, and not the regulated monopoly, should be responsible for rendering these services.

6. What creditworthiness provisions need to be applied?

NEM submits that unreasonable creditworthiness standards represent an artificial barrier to competition and as such should be prohibited. Companies with certain S&P or Moody ratings should already meet reasonable standards. Others should be able to meet a creditworthiness standard with a reasonable bonding requirement. Excessive creditworthiness requirements will increase the costs associated with energy delivery and limit competition.

7. How often would the Board reconsider BGSS?

NEM asserts that default service pricing mechanisms must be designed to account for changing market conditions. There is a huge inherent risk for the State and the market if a "price to compare" is fixed and does not change over time in response to changes in wholesale markets. Such set prices put tremendous pressure on retail suppliers during periods of wholesale price volatility and provide opportunity and motivation for entities to game the wholesale market for competitive advantage. Default service pricing mechanisms that allow prices to change over time in response to wholesale market conditions better reflects real competitive markets, provides more accurate price signals, and helps consumers better manage their energy consumption decisions. If, for example. BGSS is awarded based on revenue bids, BGSS should be reconsidered frequently enough such that the Board can reset the default service price and rebid the service periodically due to the difficulty and risk of forecasting prices into the future.

8. How would customers participate (voluntary sign-up or assignment)?

NEM believes that the assignment alternative to default service holds promise for customers and the competitive market. We also recognize that other methods will be considered. Regulatory bodies may not be prepared to implement such an approach at the opening of the market and will evaluate other alternatives to satisfying their own state's unique set of circumstances regarding default service. Other options for approaching default service fall into four general models and may be used in varying combinations and permutations, preferably for a brief interim period of time before all customers make the transition to a competitive market.

- **Default service awarded based on price bids.** This approach can represent significant progress toward establishing default service charges that reflect the competitive market for energy supply services. If it is utilized, however, it is important to ensure that the default service provider is responsible to the maximum extent possible for all of the retail functions and costs that impact competitive suppliers. Since a default service provider can avoid certain costs (such as marketing costs) and enjoy certain advantages (such as instant economies of scale), it is important to ensure that these advantages are minimized in order to allow a competitive market to flourish.
- **Default service awarded based on revenue bids.** This option puts the responsibility on the Commission to set the default service price. Suppliers then bid a dollar amount for the right to serve default customers at the price established by the commission. This revenue bid amount is then available to reduce stranded costs or offer other benefits to all distribution customers. While there are a number of benefits to this approach, an inherent problem with this option is the difficulty and risk of forecasting prices into the future. From a competitive market perspective, the greatest risk is that the price will be set too low, presenting substantial risk to potential default service providers and limiting opportunities for the competitive market to offer pricing benefits to customers. If this approach is utilized, it is important that these dynamics are considered and that Commissions provide themselves with opportunities to reset the default service price (and rebid the service) periodically.
- **Default customers transferred to another supplier.** Under this approach default service is granted to an entity other than the utility, such as an affiliate or the buyer of the utility's generation assets. An automatic non-competitive transfer of customers to any other single entity (affiliated or unaffiliated) grants a substantial and unfair competitive advantage to one market participant and violates the concept of competitive neutrality. In addition, automatic transfer

to a utility affiliate offers few, if any, advantages to the competitive market over leaving customers with the incumbent utility itself.

- **Utility retains default customers:** From a default service customer's perspective, competition has changed nothing. Customers continue to deal with the utility for all aspects of service. As indicated above, this approach is not a long term solution. When it is employed on a transitional basis, Commissions should insure that the transition plan:
  - **maximizes** appropriate incentives for customers to choose competitive suppliers by allocating retail costs appropriately between the distribution rate and the energy supply service (i.e., default service) rate, thereby preventing customers who switch to competitive suppliers from paying the retail cost component twice.
  - **minimizes** incentives for utilities to retain default service customers by ensuring that revenues in excess of commodity costs benefit all customers via lower stranded costs or distribution rates.
  - **educates** consumers on the benefits of competitive energy supply service options, including the potential for: innovative product offerings, including flexible pricing, billing and delivery options, and cleaner and renewable energy resources; multiple supply and purchase alternatives; and lower costs as the result of price competition among suppliers.

9. **Should BGSS be structured to provide multiple pricing options for customers?**
10. **Should each gas utility implement the same type of competitive BGSS program, or do unique utility situations lead to different BGSS programs?**

Regardless of whether there are separate programs, each program should be designed to incorporate the above principles.

11. **Should the Board regulate BGSS providers?**

All of the social and political considerations that the BPU requires should be set forth in the RFP and allow the competitive marketplace to determine the costs associated with these requirements. Competitive suppliers cannot be regulated like utilities. In fact, onerous rules and regulations discourage market entry and increase the costs of doing business.

12. **Should BGSS suppliers be licensed similar to third party suppliers, or should there be a separate BGSS license?**
    a. **If a separate BGSS license is required, what standards should the Board establish?**

A potential BGSS supplier should demonstrate compliance with whatever political or social requirements that are necessary to be a BGSS and those requirements should be spelled out in the RFP. There are no default suppliers of food or gasoline or other essentials of American life. The regulation of what can be added to food or gasoline is established and then competitive suppliers meet those standards or they don't sell the product.

13. **What additional consumer protections should be adopted by the Board, if any, for customers served by competitive BGSS providers?**

In the marketplace, there are numerous laws and regulations that are designed to protect consumers from invasion of privacy, fraud and all manner of improper commercial practices. These laws provide reasonable protection. Reference to the Uniform Commercial Code (UCC), state privacy laws and local laws against unfair trade practices imbues the marketplace with meaningful and enforceable guidelines to implement the final unbundling of the natural gas industry. Incorporating these laws and the years of court cases interpreting these laws protects all purchasers of energy without imposing new and costly regulations, licensing requirements, paperwork and administrative burdens. In addition, NEM strongly endorses standards of conduct and self-policing rules to protect customers against unwanted sales tactics.

C. If BGSS were to be made available on a competitive basis - RELIABILITY

1. **Would the Board have jurisdiction to oversee the capacity arrangements of providers?**
2. **How would the Board monitor the capacity arrangements of BGSS providers?**
3. **How would system balancing be accomplished?**
4. **How would BGSS customers be served if a supplier(s) defaults?**

NEM submits that if BGSS is properly designed and priced as gold-plated, no notice, reliability service, that market participants will be enabled to render service to customers when needed. Each of these requirements if deemed necessary should be part of the RFP. If no one bids on the service the BPU will know that the restrictions are not realistic or competitive.

5. **Who should perform long-term planning regarding additional supply and capacity?**

This question requires significant additional information. If properly designed, a competitive supplier, expert in risk management should be able to plan for additional supplies most efficiently. Expansion of monopoly functions must be coordinated with the expansion in expected demand. Perhaps, this is a coordination role of the BPU, the utility and the competitive suppliers.

NEM appreciates the opportunity to submit comments on this vital issue and reiterates its commitment to working with regulators and other stakeholders on the development of competitive natural gas markets in New Jersey.

Sincerely,

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