

## State of New Jersey

### *Board of Public Utilities*

*Two Gateway Center  
Newark, NJ 07102*

I/M/O The Provision Of Basic )  
Generation Service Pursuant )  
To The Electric Discount And )  
Energy Competition Act, )  
N.J.S.A. 48:3-49 et seq. )

ENERGY

DECISION AND ORDER

Docket No. EX01050303, EO01100654,  
EO01100655, EO01100656 and EO01100657

(Service List Attached)

BY THE BOARD:

The Electric Discount and Energy Competition Act of 1999 (“EDECA” or “Act”), N.J.S.A. 48:3-49 et seq., provides that for at least three years from the starting date of electric retail choice and until the Board finds it to be no longer necessary and in the public interest, electric public utilities shall provide basic generation service. N.J.S.A. 48:3-57(a).

In the rate unbundling, stranded costs and restructuring Final Orders (“Final Orders”) for Atlantic City Electric Company d/b/a Conectiv Power Delivery<sup>1</sup> (“Conectiv”), Jersey Central Power & Light Company d/b/a GPU Energy<sup>2</sup> (“GPU”), and Public Service Electric and Gas Company<sup>3</sup> (“PSE&G”), the Board directed each of the electric utilities to file, by August 1, 2001, specific proposals to implement a Request for Proposal (“RFP”) process for Basic Generation Service (“BGS”) for Year 4 of the Transition Period, consisting of August 1, 2002 through July 31, 2003 (“Year 4” or “Year 4 of the Transition Period”), subject to public comment and Board review and approval. In addition, in the Summary Order for Rockland Electric Company (“Rockland” or “RECO”)<sup>4</sup>, the Board indicated that it will undertake a review at the beginning of Year 3 of the Transition Period (August 1, 2001), with an opportunity for participation by the parties, to determine whether, and if so in what manner, Rockland should be permitted to bid out BGS responsibility for Year 4 of the Transition Period.

By Order dated June 6, 2001, the Board directed the four electric distribution companies (“EDCs”) to each file, by June 29, 2001, specific proposals to implement an RFP process for BGS for Year 4 of the Transition Period. In the same Order, the Board established a preliminary procedural schedule, which would enable a Board decision, on this issue, in the

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<sup>1</sup> In The Matter of Atlantic City Electric Company’s Rate Unbundling, Stranded Costs and Restructuring Filing, Docket Nos. EO9707455, EO9707456 and EO9707457, Final Order, dated March 30, 2001.

<sup>2</sup> In the Matter of Jersey Central Power & Light Company d/b/a GPU Energy – Rate Unbundling, Stranded Cost and Restructuring Filings, Docket Nos. EO97070458, EO97070459 and EO97070460, Final Order, dated March 7, 2001.

<sup>3</sup> In the Matter of Public Service Electric and Gas Company’s Rate Unbundling, Stranded Costs and Restructuring Filings, Docket Nos. EO97070461, EO97070462 and EO97070463, Final Order, dated August 24, 1999.

<sup>4</sup> In the Matter of Rockland Electric Rate Unbundling, Stranded Costs and Restructuring Filings, Docket Nos. EO97070464, EO97070465 and EO97070466, Summary Order, dated July 28, 1999.

fourth quarter of 2001. Among other things, the preliminary procedural schedule provided for discovery, the filing of non-EDC positions, public hearings, and the filing by all interested parties of final comments and reply comments. The Board directed Staff and the Advising Deputy Attorney General (“DAG”) to schedule a procedural conference after the filing of the EDCs’ proposals and to develop a final procedural schedule.

On June 29, 2001, the four EDCs filed a generic proposal for Basic Generation Service (“EDCs’ Proposal”). The generic submission consists of three parts: EDCs’ Proposal Objectives, the EDCs’ Proposal and a Master Service Agreement. In addition, each EDC filed an addendum to the generic proposal dealing with utility-specific issues. The generic proposal recommends a simultaneous, multi-round, descending clock auction (“Auction”) format.

On July 12, 2001, a procedural conference was held and a procedural schedule was established, which DAG Wallenstein memorialized by letter dated July 16, 2001. Public legislative-type hearings were scheduled for October 3 and 4, 2001. The letter noted that if, after review of the discovery responses, the Division of the Ratepayer Advocate (“RPA” or “Ratepayer Advocate”) or the marketers identify specific factual issues in dispute which, in their view, require their cross-examination, they may make a prompt application to the Board for permission to cross-examine on such issues. The letter further noted that any such application should set forth the disputed factual issue(s) with specificity.

At the July 12, 2001 Board agenda meeting, Staff recommended and received Board approval to obtain the services of a consulting firm to provide advice to the Board and its Staff on the auction proposal.

By letter dated July 24, 2001, the RPA filed a motion to reconsider the procedural schedule and to permit full evidentiary hearings.

At the August 29, 2001 Board agenda meeting, Staff recommended and received Board approval to engage the consulting firm of Charles River Associates (“CRA”) to perform a review of the EDCs’ Proposal, and provide oversight of any auction process approved by the Board. CRA is a multinational consulting firm, with vast energy and auction experience.

On August 29, 2001, the RPA, Williams Energy Marketing and Trading Co. (“Williams”), Enron Corp. (“Enron”) and Shell Energy Services Co., LLC (“Shell”) filed comments and proposals (“Initial Comments”).

At its agenda meeting of September 26, 2001, the Board determined to deny the RPA’s request for reconsideration and for full evidentiary hearings. The Board determined, however, to allow the RPA to depose utility representatives on October 3, 2001, with the public legislative hearing to be held on October 4, 2001. The Advocate, by letter dated September 28, 2001, indicated that it did not intend to conduct depositions.

On October 4, 2001, consistent with the procedural schedule established by the Board, a public legislative-type hearing was held before President Hughes and Commissioner Murphy. Any party wishing to do so was afforded the opportunity to participate and present comments. Those testifying included an EDC sponsored panel of witnesses, including witnesses from National Economics Research Association (“NERA”) and the four EDCs, the RPA, Enron, Green Mountain Power (“Green Mountain”) and Geophonic Networks, Inc. (“Geophonics”). At the hearing, the discovery which had been propounded during the proceedings and the responses thereto were entered into the record. Hearing Transcript at 128-129.

Consistent with the Board's procedural schedule, on October 17, 2001, final comments concerning this matter were filed by the EDCs in a joint filing<sup>5</sup> as well as supplemental letters from GPU and RECO, and by Enron, the Mid-Atlantic Power Supply Association ("MAPSA"), the New Power Company ("New Power"), RPA and Shell ("Final Comments"). On October 24, 2001, Enron, Shell, the RPA and the EDCs in a joint filing submitted reply comments ("Final Reply Comments").

On November 20, 2001, counsel for Enron clarified Enron's position and indicated that while not withdrawing its own proposal, Enron will not oppose the EDCs' Proposal.

By letter dated December 6, 2001, the RPA requested that in light of recent events pertaining to the bankruptcy filing by Enron and issuance of certain guidelines by the Federal Energy Regulatory Commission ("FERC"), the Board should delay its decision in this matter and/or adopt the RPA position. By letter dated December 7, 2001, the EDCs submitted a response opposing the RPA's December 6, 2001 submission. GPU also submitted a separate letter in opposition to the RPA's request.

### EDCS' PROPOSAL

The EDCs' Proposal consists of three parts; EDCs' Proposal Objectives ("Part I"), EDCs' Proposal, with company-specific addendums ("Part II"), and BGS Master Service Agreement (filed July 11, 2001) ("Part III"). The EDCs jointly propose a single Auction Process for the procurement of supply to meet the full electricity requirements (*i.e.*, energy, capacity, ancillary services, transmission, etc.) of retail customers that have not chosen a Third Party Supplier ("TPS"). Rockland Electric Company joined in the EDCs' Proposal although it is currently a member of the New York Power Pool and subject to operating requirements of the New York Independent System Operator ("NYISO"), while the other EDCs are members of the PJM Interconnection, L.L.C. ("PJM"). In its utility-specific addendum to the EDCs' Proposal, Rockland indicates that it would be requesting permission to become a PJM member. On October 2, 2001 Rockland received approval from the PJM Board of Directors to join PJM subject to FERC approval. On October 17, 2001 Rockland and PJM jointly filed with FERC for expedited approval of its request for Rockland to be admitted to PJM. In its filing, Rockland and PJM requested FERC approval for PJM tariffs to become effective February 1, 2002.<sup>6</sup>

### AUCTION STRUCTURE

The competitive process by which the EDCs propose to procure their supply for BGS Load for the period August 1, 2002 to July 31, 2003 is called a "simultaneous descending clock auction." Under the proposal, the BGS Loads of all EDCs would be bid out in the same auction. The total load for all EDCs may be as large as 18,000 MW. Under the EDCs' Proposal, the annual BGS retail load of each EDC is considered a separate "product." A participant may bid to supply a portion of the BGS load of one or more of the EDCs ("tranche"). A tranche of one product (*i.e.*, a tranche of the BGS Load for one EDC) is a full requirements tranche. A tranche for an EDC is a fixed percentage share of the BGS Load. The percentage is determined so that the portion of BGS Peak Load Share represented by one tranche is approximately 100 MW for all EDCs. "BGS Peak Load Share" is defined as the portion attributable to those customers on BGS service of PJM-determined EDC zonal peak load on a proxy day. When a participant bids in this auction, that participant would be stating the number of tranches that it is willing to serve for

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<sup>5</sup> GPU did not join in Section III of the comments.

<sup>6</sup> Rockland Electric has requested FERC approval to transfer its "Eastern Division" to PJM operations. This is the only territory that would be included in the BGS auction if its FERC application is approved.

each EDC at the prices in force at that point in the auction. A price for an EDC is an amount in ¢/kWh paid for each kWh of BGS Load served. The “BGS Load Served” for each EDC is determined as the BGS Load less the Committed Supply of the EDC and is measured in kWh. Potentially, at the end of the auction, the final prices for the EDCs’ tranches may be different because of differences in the products due to EDC load factor, delivery location and other factors.

The auction is called “simultaneous” because tranches for all EDCs are offered through the same sale. The auction volume will be set after receipt of the first round bids. The auction is “descending” because the going prices are reduced gradually throughout the auction. Participants reduce the number of tranches they wish to serve as the going prices decrease. The auction ends when the total number of tranches bid equals the number of tranches that the Auction Manager, acting on behalf of the EDCs, and the Board have set as the auction volume. The prices as the auction closes are the clearing or final auction prices. The bidders that hold the final bids when the auction closes are the winning bidders. The auction is characterized as being a “clock auction” because the prices of the various products “tick” down in a sequence of steps controlled by the Auction Manager.

In the EDCs’ Proposal, the Auction Manager, the EDCs and the Board will determine a single maximum starting price and a single minimum starting price for all the EDC products. Twenty-one days before the auction, the Auction Manager will announce the single maximum starting price and the single minimum starting price for all EDCs and any Load Caps that the EDCs wish to impose. A Load Cap limits the number of tranches of a particular EDC for which any participant can bid. Under the proposal, such a limit may be imposed by an EDC to diversify default risk or for other business reasons. To qualify for the auction, interested parties will be required to submit an application within three days after this announcement of minimum and maximum starting prices. The EDCs’ Proposal specifies that applicants must meet PJM Load Serving Entity (“LSE”) requirements (or NYISO if applicable), Board licensing requirements, credit worthiness requirements and other criteria as specified in the BGS Master Agreement

Under the EDCs’ Proposal, ten days before the start of the auction, qualified bidders must submit indicative offers and bid bonds. An indicative offer must indicate the total number of tranches that the participant is willing to serve at the single maximum starting price and the total number of tranches that the participant is willing to serve at the single minimum starting price. The number of tranches that the participant is willing to serve at the maximum starting price is called the “participant’s initial eligibility” in the auction. Since eligibility can never increase, the participant is encouraged to state the maximum number of tranches that it would be willing to serve. The participant must post a bid bond that is proportional to its initial eligibility. As part of the indicative offer, the participant will also be asked to indicate its maximum interest in each EDC at the maximum and at the minimum starting prices.

In the first round of the auction, there will be a potentially different starting price for each EDC. The EDCs propose that the Auction Manager, the EDCs and the Board agree on a starting price for each EDC. Each starting price in the first round of the auction will be set no higher than the single maximum starting price and no lower than the single minimum starting price. Three days before the start of the auction, the Auction Manager will announce to the qualified participants a starting price for each EDC’s tranches. Indicative offers will be considered in setting the starting prices. In the first round of bidding, the bidders state the number of tranches of each EDC to which they want to subscribe at these starting prices. After the first round of bidding, if, to ensure the competitiveness of the auction, the Auction Manager must revise the auction volume to be less than the full BGS Load for all EDCs, the Auction Manager will declare the auction in recess. At that time, the Auction Manager may also revise any Load Caps based, among other factors, on the revised auction

volume and the sum of the first round bids. After the recess, the Auction Manager will announce a target auction volume that will be purchased through the auction and any revised Load Caps. In setting the auction volume, the EDCs propose that the Auction Manager use a set of Board-approved guidelines regarding competitiveness of the auction and a desired maximum percentage of the BGS Load that can be procured through a Contingency Plan of each EDC. Under the Contingency Plan, the EDCs would purchase through PJM-administered markets. The Board will have final authority over auction volume.

## DESCRIPTION OF AUCTION PROCESS

The simultaneous descending clock auction proceeds in a series of rounds. Prior to the start of bidding in each round, the Auction Manager announces a price for each EDC's tranches. During the bidding of each round, each bidder indicates how many tranches of each EDC the bidder wishes to serve at the prices announced by the Auction Manager. A "bid" is the number of tranches of each EDC to which a bidder wants to subscribe. At the end of the bidding of a round, the Auction Manager reduces the price for the tranches of an EDC by a decrement if the bidders together subscribe to more tranches for that EDC than are available in the auction. If the tranches of an EDC are just subscribed or are under-subscribed, the announced price of a tranche for that EDC does not change. The auction continues and the price continues to tick down until, for each EDC's product, the total number of tranches subscribed falls to the point where it equals the number of tranches available. When the auction ends, the bidders holding the tranches at the final auction prices are the auction winners.

During the auction, bidders can switch from one EDC's product to another. At the start of the auction, one product may be oversubscribed while the others are under-subscribed. The Auction Manager will tick down the prices only for the oversubscribed products. This will lead to switching from the oversubscribed products to other products. As a result, there is not a need for each product to be fully subscribed at the auction starting prices. The auction normally stops when all products are just subscribed. For an EDC's tranches to be under-subscribed at the end of the auction, the EDC's tranches must have been under-subscribed at the starting price and must have remained under-subscribed throughout the auction.

The auction ends when the number of tranches to which bidders subscribe is equal to, or smaller than, the number of tranches available for each EDC. As offers made at the auction are binding, there will be no post-auction negotiations. The proposal is for the Board to confer with its Advisor immediately at the conclusion of the auction to determine that the auction was conducted according to Board-approved auction rules and procedures, and to certify the auction results by the start of the next business day. Upon approval by the Board, all parties will be bound by the auction results.

The EDCs' Proposal includes numerous other auction details, which are explained in the EDCs' Proposal, Part II and Part III. The more significant of these include the following:

- Each winning bidder assumes the responsibilities of a PJM LSE for their portion of BGS Load, including capacity, energy, ancillary services and transmission, and other services as may be required by PJM.
- Each winner is allocated a pro-rated share of the Committed Supply of an EDC, proportional to the share of the BGS Load that they have won for the EDC.
- Each winner receives, for each product, the final auction price times the amount of BGS Load Served. The BGS Load Served for each EDC is determined as the BGS Load less

the Committed Supply of the EDC.

- BGS suppliers must meet all New Jersey Renewable Portfolio Standards requirements, including the reporting standards as prescribed by Board Order dated June 12, 2001, Docket No. EX 99030182, in addition to all requirements of N.J.A.C. 14:4-8.1 et seq.
- The EDCs will make data regarding BGS from the start of retail choice in November 1999 to June 2001 available to market participants on an auction website.
- As conditions of qualification, applicants must: meet pre-bidding credit worthiness requirements; agree to comply with all rules of the auction; and agree that if they become auction winners, they will execute the BGS Master Service Agreement within two days of Board certification of the results and they will demonstrate compliance with the credit worthiness requirements set forth in that agreement.
- Each EDC can specify a different Load Cap subject to the Board's approval.
- To qualify, applicants will disclose ownership information that will be used to determine if associations with other bidders exist. The Auction Manager, under guidelines set by the EDCs in advance of the auction and approved by the Board, will have the authority to require disclosure of additional information directly relevant to determining whether such associations exist. The Auction Manager and the Board will resolve any issues arising from associations based on the approved guidelines and may at that time require additional information from bidders. Associations may be considered in setting the target auction volume and may be used in the application of Load Caps.
- The Auction Manager, the EDCs and the Board will agree on a single maximum starting price and a single minimum starting price for all EDCs.
- Qualified bidders are required to post a bid bond of \$1 million per tranche.

## CONTINGENCY PLANS

In the utility-specific addendums to the EDCs' Proposal, each EDC describes a Contingency Plan in the event that the auction volume is adjusted to less than 100% of the BGS Load for all EDCs. The EDCs propose that the Auction Manager, subject to BPU approval, decide the final auction volume after the first round of the auction.

The EDCs each identify three contingencies:

1. Insufficient number of bids to provide for a fully subscribed auction volume – The EDCs propose to secure services for unsubscribed tranches through PJM-administered markets, or in the case of RECO, if it has not become a member of PJM, through NYISO-administered markets.
2. Default by a winning bidder prior to August 1, 2002 – Open tranches may be offered to other winning bidders or bid out as quickly as possible, with additional costs assessed against the defaulting company's BGS security.

3. Default during Year 4 – Open tranches may be offered to other winning bidders, bid out or obtained from PJM-administered markets, with additional costs assessed against the defaulting company's BGS security.

## ACCOUNTING

In the utility-specific addendums to the EDCs' Proposal, each EDC describes a proposed accounting process for Year 4, and a process for BGS cost recovery. Each EDC is requesting that the Board approve its proposed accounting for BGS for Year 4.

In its utility-specific addendum to the EDCs' Proposal, Rockland also requested approval of all costs associated with its request to become a PJM member, whether the request is successful or not. Rockland estimates that the installation of revenue grade metering equipment at various locations along the Rockland-Orange & Rockland border will cost \$1 million. In addition, there will be legal fees, consulting fees and other costs associated with the Rockland request to join PJM.

## NON-EDC POSITIONS AND PROPOSALS

Following is a summary of the positions of non-EDC parties.

### RPA

The RPA submitted Initial, Final and Final Reply Comments and appeared at the public legislative-type hearing.

The RPA submitted the direct testimonies of Paul Chernick and Scott Hempling as their initial written comments. Chernick asserts that the form of proposed auction has risks, including that: the simultaneous-descending-clock-auction appears to have never been used before; the broader simultaneous multi-round ("SMR") auction format has only been used for sales, not for purchases; that the size of the auction is a very large scale for an "experimental" procurement method and could distort an already tight capacity market in PJM; the Contingency Plan would mandate reliance on purchases from spot markets that are highly volatile, raising California-like concerns; there would be no test of bid prices against the costs of other BGS supply approaches; no proposals have been submitted by the EDCs for determining the relationship between the initial level of interest by bidders and the amount of BGS to be purchased, and the rules for determining whether all BGS or some smaller fraction will be acquired through the auction; and that the proposed acquisition period (August 2002 through July 2003) does not match the PJM capacity-responsibility period. Chernick asserts that the proposed auction format is subject to manipulation in several ways, including that generators or marketers could exercise market power; bidders could overstate the apparent level of competition, or bidders could collude. He argues that the market power issue is further complicated by the need for bidders to bundle a variety of generation services as part of full-requirements service, that the EDCs have not assessed the level of generation market concentration, and that the amount of excess capacity in PJM appears to be relatively small. Chernick also argues that the imposition of full-requirements obligations on suppliers would require the assumption of a range of risks that require the addition of a margin to the expected cost of generation services. In addition, Chernick asserts that the EDCs' Proposal will not promote retail competition because suppliers will have no visibility to customers. Chernick recommends that the Board delay the auction by several months to resolve the issues he has raised, and order the EDCs to acquire generation services to meet BGS supply through September 2002. Finally, Chernick recommends that BGS supply be acquired in smaller increments, and that the EDCs Contingency Plan require

utility procurement of bilateral energy and capacity contracts similar to the approach taken by Atlantic Electric to supply BGS during the first three years of the Transition Period.

The RPA's witness Hempling, citing EDECA, concludes that a BGS supplier could replace the utility as the retail provider of the traditional package of retail electric services, including energy and capacity, delivery of energy, and customer account services, and that while the BGS supplier may not produce all such services itself, it would have the retail relationship with the customer and could purchase certain services from the utility. Alternatively, Hempling states, if the Board views BGS as confined to wholesale generation service, it should add a retail version of BGS to give non-shopping customers the benefits of competition. Hempling notes that EDECA assigns the incumbent utility the task of serving as BGS provider for three years and that thereafter, Section 9(c) of EDECA (N.J.S.A. 48:3-57(c)) permits the Board to hold a bidding process to allow competitive suppliers to be BGS providers. Hempling further notes that, assuming the incumbent utility continues to provide transmission and distribution services and that the BGS supplier provides some or all of the remaining retail services, there are various options which can govern the relationship, if any, that the incumbent utility and BGS supplier should have with retail customers, including the BGS supplier having the exclusive relationship with the retail customer, the utility having the exclusive relationship with the retail customer, and the BGS supplier and the utility each having an independent relationship with the retail customer for the services it is providing. The decision as to which option will work best in New Jersey requires a factual analysis, according to Hempling, which considers questions like the importance to the development of retail competition of having a direct relationship with the customer, the potential for customer confusion under each option, and the costs of separate versus bundled billing. Hempling asserts that bidding out BGS to third party suppliers can permit winning suppliers to overcome barriers to entry and acquire large numbers of customers at much lower acquisition costs. He states that the competitive process may also promote new efficiencies and innovation. Hempling states that competitively-bid BGS is not inherently less reliable than utility-provided BGS, since the Board can impose the same standards and impose minimum terms and conditions. He argues that assignment of non-shopping customers to non-utility BGS suppliers does not constitute "slamming" because, among other reasons, the substitution of a legally authorized service provider, in accordance with a Board-conducted or supervised bidding process is not an unlawful transfer of a customer from one supplier to another as is the case with slamming, but rather is a lawful transfer. He further notes that the Board should provide notice of such a switch, and that customers may be given the option to switch to a competitive supplier of their choice before being assigned.

Hempling points out that the two issues which must be decided to determine whether competitively-procured BGS is consistent with the goals of retail competition are: (1) which elements of service should be produced or procured by the BGS supplier and which by the utility and (2) determining the scope of the utility and the non-utility's commercial relationship with the retail customer. Hempling argues that the pre-existing commercial relationships the utility has with customers may give a competitive advantage to utility affiliates competing in retail markets, and that denying non-utility suppliers the ability to establish their own commercial relationships with customers is the model least consistent with retail competition. If the Board allows suppliers to establish commercial relationships with customers, it could also decide or leave the choice to BGS suppliers as to the scope of its customer relationship (i.e whether the utility would maintain a commercial relationship with customers for certain services such as delivery service). Hempling asserts that the EDCs' Proposal would restrict non-EDCs to producing only one element of the BGS package and deny non-EDCs the benefits of having a



commercial relationship with the retail customer. Therefore, Hempling concludes that the EDC proposed model for BGS is the least consistent with retail competition.

Hempling identifies a number of questions concerning the shape of the final program that he maintains must be answered and, rather than making specific recommendations on each, describes some of the options available to the Board that require further study. He recommends that utilities and their affiliates not be permitted to participate in the bid or, in the alternative, that the Board adopt rules to preclude affiliates from gaining an unfair advantage. Hempling states that the bid could be designed such that suppliers are bidding either on fixed numbers of customers, a fixed percentage of BGS Load, or any increment of their choosing. Hempling states that the bid can be designed to require or encourage multiple winners rather than a single winner, and to recognize or limit the potential cost-increasing effect of having multiple winners. He identifies three options if bidders offer less supply than the total actual load: require each winning bidder to take on a pro rata share of the unsubscribed load; conduct a new bid or succeeding bids until all load is covered; or order utilities to provide BGS services through affiliates. Hempling asserts that the Board will need to create standard contracts to establish the relationships between and among customers, BGS suppliers and the utilities. Hempling discusses three possible options for determining the winning bidders: on the basis of price; on the basis of services or other benefits offered; or a combination of price and services. He asserts that the Board can establish a price cap on bidders in advance of the bid. He claims that the Board could establish a single category of BGS at a single price, or it could establish rate class-specific BGS rates, in which case bidding increments could be either cross-sectional or rate class-specific. Finally, Hempling recommends that under a BGS competitive procurement program, the EDC should be required to provide the elements of the BGS package that the Board determines are not subject to competitive procurement, and if the Board provides non-EDCs with a choice of bidding on certain elements, the EDC may have to provide other elements which winning bidders opt not to provide. Hempling also submits that the Board should require EDCs to create a statistically representative load profile for the bidding increment, and possibly prepare other bid documents.

In its Final and Final Reply comments, the RPA argues that the EDCs' Proposal is contrary to the requirements of EDECA for competitive BGS. The RPA asserts, among other things, that the Act's provisions contemplate a BGS program that provides non-utility suppliers with the opportunity to enter New Jersey's retail market and requires the elimination of the incumbent utilities' traditional monopolies over electric retail service. The RPA further asserts that the Board's Orders in the four EDCs' rate unbundling, stranded costs and restructuring proceedings reflect the dual objectives for BGS in Year 4 of reasonable prices for consumers and encouragement of retail competition. The RPA asserts that the EDC Proposal promotes neither of these objectives and should therefore be rejected.

Citing the risks associated with the EDCs' auction proposal discussed in its witness Chernick's testimony and summarized above, the RPA concludes that the proposal subjects ratepayers to the risk of high and volatile BGS prices and therefore does not meet EDECA's requirements that ratepayers have access to reasonably priced BGS. It states that the EDCs' Proposal provides no opportunity for suppliers to establish direct relationships with consumers, and therefore does not meet the EDECA's objective of promoting the development of a retail electric marketplace and allowing competition for the opportunity to provide BGS at the retail level. The RPA argues that the present energy marketplace is devoid of choice, and that, if approved by the Board, the EDCs' Proposal will continue to be a roadblock to competition.

The RPA recommends minimizing risks inherent in the EDCs' Proposal by adopting a diversified approach to procurement which uses a variety of methods over a longer period of time,

including: procurement of BGS for at least 30% of residential and small commercial customers through a retail Request for Proposals process; an auction to procure no more than 10% of the State's BGS requirements, with additional auctions to be conducted only if the first one is successful; and procurement of the remaining BGS supply requirements through a wholesale RFP process. The RPA cites to the support of three energy marketers in the proceeding (Enron, Shell and Green Mountain) for a program similar to that being utilized in the Philadelphia Electric Company ("PECO") territory, whereby approximately 245,000 residential customers have been assigned third party suppliers, and asserts that the program provides a model for a retail program in New Jersey. The RPA also refutes the EDCs' assertion that a retail BGS program would create customer confusion, and cites to the asserted successful program implemented in Pennsylvania. The RPA recommends that the Board reject the EDCs' Proposal, and instead adopt a diversified approach that includes a retail component.

## ENRON

Enron filed Initial, Final and Final Reply comments and appeared at the public legislative-type hearing. It also submitted a letter dated November 20, 2001.

In its comments, Enron asserts that it is no longer necessary, and it is contrary to the public interest, for the EDCs to provide 100% of the State's BGS. It recognizes that Year 4 of the Transition Period can be a critical first step in the move toward a fully competitive BGS market and notes that while the Legislature and others recognized the danger of an abrupt shift to a competitive BGS program, they saw the dangers in proceeding too slowly during the transition period. Enron argues that a competitive BGS program will enable all stakeholders to realize the benefits of a competitive market, in accordance with EDECA. It asserts that EDECA requires a "true retail" program. Citing the definitions of "basic generation service" and "electric generation service" and the provisions of section 9 of EDECA, Enron asserts that the plain language of the Act requires any competitive BGS program to provide retail access directly to customers. It also asserts that the Board's rate unbundling, stranded costs and restructuring Final Orders recognized that EDECA required a competitive BGS program that affords suppliers retail access. It argues that the EDCs' Proposal provides for a competitive procurement of wholesale supply only, which it asserts is not contemplated in EDECA. Enron asserts that the EDCs' Proposal maintains the status quo, and that contrary to the EDCs' assertion, no drastic changes have occurred in the industry, as reflected by the fact that only one percent of customers have switched suppliers. It asserts that the competitive market in the State will suffer because suppliers will be denied the opportunity to compete to provide BGS directly to retail customers. Enron argues that given the status of competitive markets in New Jersey, there is a great need for a direct retail access program, and that its proposal will provide an incentive for suppliers to re-establish or maintain their presence in the New Jersey market.

Enron proposes that the Board establish a framework to make available on a competitive bid basis the provision of BGS starting on August 1, 2002 by electric power suppliers to at least 30% of the EDCs' customers in each rate class, except for certain commercial and industrial ("C&I") customers with a peak load demand to be determined by the Board. It asserts that only electric power suppliers with a Board license in good standing should be allowed to submit bids. Enron proposes a random selection process that would be intended to ensure that customers assigned to electric power suppliers are a representative cross-section of the EDCs' overall customer base. The customer pool would be derived through random selection from a list of all "non-shopping" customers prepared by each EDC. The Board would employ a neutral, independent third party "Statistical Expert" to assist in the selection process. Enron proposes

that winning suppliers be required to notify assigned customers within a determined period of time, and that subsequent to such notification, customers designated to receive BGS from third party suppliers be allowed within a designated period of time to choose to remain with the incumbent EDC, a process commonly referred to as “opt-out.” Suppliers would be permitted to establish retail Customer Account Services (“CAS”) relationships with customers.

Enron argues there is nothing in EDECA that prohibits the Board from employing a random selection process for customers to be supplied BGS by an electric power supplier and asserts that the Board has express authority to implement any process it deems necessary to institute a competitive BGS program, and broad and discretionary authority under Title 48 and as afforded by the New Jersey Courts. Enron further argues that the Board’s consumer protection standards and the municipal aggregation sections of EDECA are unique to the competitive retail market in order to protect customers against unauthorized switching, and are not applicable in connection with Board-authorized competitive BGS. However, because it recognizes the sensitivity of the issue, it supports allowing consumers to opt-out of a random assignment. Enron also argues that its proposal for random selection of customers is clearly distinguishable from the experience in the long-distance telecommunications market in the 1980’s after the break-up of AT&T, since customers would be notified prior to the switch, and would be able to “opt-out.”

Enron argues that its proposal will minimize customer confusion because it does not place a utility agent between the retail customer and the supplier and allows questions and complaints to be handled directly by the supplier of BGS, and that it will protect customers because they will be given the option to shop for another supplier or remain with the incumbent EDC if they so choose. Enron asserts that the direct relationship between the consumer and the BGS supplier established through its proposal is required by EDECA. Enron further asserts that its proposal is consistent with the Board’s Order in the CAS proceeding because customers will have the opportunity to receive a bill from an electric power supplier.

Enron proposes that the bid specifications for BGS supply be developed by the Board in consultation with the electric power suppliers and utilities, but offers no specific proposals in this regard. The Board would oversee and administer the bid process, and would select up to three suppliers to supply BGS for each EDC service territory. Each winning BGS supplier would be required to provide a corporate guarantee from a creditworthy party or other financial assurances. The terms and conditions governing the relationship between the winning suppliers and customers, as well as the rights and obligations of the winning suppliers and the EDCs, would be determined by the Board; however no specific proposed conditions are included in the proposal. Enron proposes that affiliates of the EDCs not be permitted to bid for customers in their respective affiliated utility’s BGS bid pool.

By letter dated November 20, 2001, counsel for Enron clarified Enron’s position on the EDCs’ Proposal. Enron explained that although EDECA makes clear that the Legislature contemplated a retail relationship between the BGS supplier and customer, EDECA also grants the Board “full authority over the provision of BGS for Year Four of the Transition Period.” While not withdrawing its own proposal, Enron clarified that it will not oppose the EDCs’ Proposal. It indicated an intent to be an active participant in the BGS auction and that it would gain important PJM experience on pricing, capacity and ancillary services. It also noted that the descending clock auction would be conducted under Board supervision and result in competitive pricing reflecting market conditions. Although Enron prefers adoption of its “true retail BGS program,” it stated that the EDCs’ Proposal would continue the State’s movement towards competitive wholesale and retail markets and allow non-utility suppliers to serve BGS load.

## SHELL

Shell filed Initial and Final Reply comments.

Shell asserts that the EDCs' Proposal provides for a wholesale procurement that violates both the letter and spirit of EDECA, and would further delay and inhibit the development of a competitive market. Shell argues that EDECA defines BGS as a retail service provided directly to end-use customers, and that under the EDCs' Proposal, the EDCs would continue to have all customer interface and that nothing would change in the existing relationship between customers and the utilities. Shell also asserts that the EDCs' Proposal is anti-competitive insofar as it would include a blanket prohibition against switching by all C&I customers, including "mom and pop" sized businesses. Shell indicates that an opportunity to provide BGS directly to at least a portion of residential and small commercial customers was viewed as an important opportunity to demonstrate suppliers' ability to provide BGS service. It further argues that the "multi-year alternative" proposal in PSE&G's company-specific addendum, which could extend the auction supply beyond Year 4, would have the most chilling effect on competition, because it would shut-out smaller suppliers without wholesale capabilities on a going forward basis. Moreover, Shell interprets PSE&G's proposal as requiring suppliers to compete against a wholesale price in Year 5, after the price-freeze is lifted, and argues that the price to compare must fully reflect all retail costs. Shell asserts that the EDCs' Contingency Plan, which relies on PJM spot market purchases, will introduce price volatility that could negatively impact the level of cost deferrals.

Shell argues that the Legislature likely did not envision when it passed EDECA that nearly three years later virtually all residential customers would still be taking BGS from the utilities. Citing the definitions of "BGS," "electric generation service," "customer" and "electric power supplier" set forth in section 3 of EDECA (N.J.S.A. 48:3-51), Shell states that the Act clearly provides for the services subject to potential bid-out in Year 4 to encompass retail sales of electric generation and related services to end-use customers. Shell also cites the Board's Final Order in PSE&G's rate unbundling, stranded costs and restructuring proceeding as allegedly demonstrating the Board's view that BGS to be bid-out in Year 4 should be provided directly to end-use customers by third party suppliers. Shell asserts that the EDCs' Proposal is akin to the wholesale procurement of gas supplies that the State's gas utilities have been engaged in for many years, as well as the wholesale parting contracts that the electric utilities entered in conjunction with generation asset divestiture, and would not provide any new opportunity or benefit to suppliers. Shell argues that the value of BGS to suppliers is the right to obtain aggregated groups of retail end-use customers without incurring high acquisition costs, and to help overcome consumer inertia of nearly a century of utility incumbency.

Shell also states that, given current market conditions, it is critical that markets be given the opportunity to serve at least a portion of BGS customers, as contemplated in EDECA. Shell rejects the assertion that marketers should wait for major changes until Year 5 when the rate caps expire and market-based pricing is put into effect, indicating that if marketers are denied the ability at this time to provide default service to a portion of BGS customers, they may not be able to wait another year to participate meaningfully in the New Jersey market. Shell asserts that a customer assignment proposal does not violate consumer protection and anti-slamming standards, since BGS is a regulated service and the Board has broad regulatory authority to craft a program that will insure necessary protections for customers who receive BGS. It argues that subsection 9(c) of the Act (N.J.S.A. 48:3-57(c)) contemplates the potential substitution of third party suppliers for the EDCs as the provider of regulated default service, rather than a transfer of customers. Shell maintains that any assignment of customers through an approved BGS program would, by definition, be "authorized" and therefore would not constitute slamming,

and approved education materials would provide further protection. Shell urges the Board to adopt Enron's proposed retail BGS program.

## WILLIAMS

Williams filed Initial comments.

Williams applauds the State's efforts towards the establishment of a competitive market. It particularly cites the capping of rates only through 2003 and the decision to require utilities to exit the BGS role within a relatively short period of time. Williams neither supports nor opposes the EDCs' proposal, but identifies four principal areas of concern which it states are not "fatal flaws" in the auction design but which could "militate against obtaining the most efficient prices competition could otherwise produce." Williams expresses concern over the 18,000 MW size of the auction, considering that supply and demand are fairly closely matched in PJM, and recommends separation of the auction into three or more parcels of 6,000 MW or less, spread over 6 to 12 months. Williams argues that this will: allow any portions unable to be successfully awarded to be placed in the next parcel auction and thus reduce the necessary effective period for each Contingency Plan to only a few months, rather than a full year, thereby reducing risk and cost; allow bidders and auctioneers to refine the process and work out problems; and provide better price discipline to potential bidders.

Williams argues that placing full requirements obligations on auction winners is a major step, and servicing full requirements service is beyond the capabilities of many market participants who are financially or physically unequipped to manage volume risk associated with full requirements service, and who may not be capable of understanding the obligations of a LSE, including all related PJM rules. These factors may limit the number of potential qualified bidders, and necessitate that the Board provide for an evaluation of the qualification and experience of bidders. Williams asserts that the one-year term of the BGS product being offered creates several concerns, including that such a short term will limit opportunity for bid differentiation, and that it eliminates creative longer-term options such as building a plant. Williams recommends that the Board consider modifying the auction design by allowing each bidder to place a 1-year, 3-year and 5-year bid on each 100MW tranche to be auctioned.

Finally, Williams strongly recommends that in approving the final form of auction, the Board make a strong statement of its commitment to the outcome of the auction, particularly the resultant pricing, absent any provable allegations or strong indications of rule violation. Williams asserts that, because of the complexity and size of the auction participation on the part of suppliers is neither simple nor inexpensive, and potential participants will have strong reservations and in fact may not participate if they perceive that the Board will not stand behind the final prices.

## MAPSA

MAPSA filed Final comments.

MAPSA supports the Initial comments and public testimony of the Ratepayer Advocate and the testimony of Enron and Green Mountain at the public hearing. MAPSA is critical of the status of electric retail competition in New Jersey. MAPSA also includes comments concerning its view of post-Transition BGS.

## GEOPHONIC NETWORKS INC.

Geophonics appeared at the public hearing.

Geophonics indicated that it has a patent, issued on April 4, 2000, called "Bidding for Energy Supply." Geophonics claims that the patent covers the use of computers and other telecommunications means to procure power and natural gas for end users. Geophonics also claims that the patent includes the running of an energy auction by a Local Distribution Company. Geophonics requested that the EDCs review the patent and begin a discussion with it over the relevance of its patent to the proposed auction process.

## NEW POWER

New Power filed Final comments

New Power cites to the definitions of "basic generation service" and "electric generation service" contained in EDECA as demonstrating the Act's intent that BGS is a retail service. New Power states the EDCs' Proposal imposes all of the obligations and burdens of a LSE, but withholds all of the value and benefits of a commercial relationship with a retail customer, and thereby blocks the asserted primary meaning and purpose of the Act to establish vibrant, competitive retail electric and gas markets in the State. New Power states that the Enron proposal is consistent with the requirements of EDECA, and supports the proposal. New Power indicates that the Enron proposal to start with an assignment of 30% of customers is a reasonable first step given the start-up and ongoing costs of a supplier coming into the residential market, but should be regarded as a minimum. It also supports the collaborative development of bid specifications and the terms and conditions of supplier/customer and supplier/EDC relationships, and supports the proposal to ban utility affiliates from bidding in their related EDC's service territory. New Power states its support for the concerns with the EDCs' Proposal expressed by RPA witness Chernick, and asserts that the Texas capacity auction cited by the EDCs is much different than the auction proposal of the utilities herein.

New Power notes that it is the default provider of natural gas service in Atlanta Gas Light's service territory and provides competitive default service to 200,000 plus residential customers in the PECO franchise territory, and supports the comments submitted by Green Mountain. New Power states that approximately 10 percent of the 299,000 customers randomly assigned in PECO territory "opted-out" and, after accounting for other drop-outs for a number of reasons, approximately 250,000 were enrolled with New Power. New Power cites to the low level of complaints in PECO, and states the importance of customer education and call center training, emphasizing the importance of the suppliers being involved in that training process. Finally, it states the importance of having the EDC and supplier charges clearly stated and explained on the bill.

## GREEN MOUNTAIN

Green Mountain presented comments at the October 4, 2001 hearing.

Green Mountain asserts that EDECA defines BGS as a retail service, and that the EDCs' wholesale auction proposal is contrary to the direction provided in EDECA for Year 4 BGS. Green Mountain describes what it regards as a successful default service model being used in the PECO service territory in eastern Pennsylvania, in which residential customers were randomly selected to participate. Specially selected customers could opt-out of the program within a specified period of time after notification, and can switch

out at any time. Green Mountain asserts that virtually no complaints were received, and “opt-outs” were in an expected range of 10 percent. Green Mountain asserts that the BGS process envisioned in EDECA can provide a similar opportunity for non-shopping customers, and urges consideration of the Enron proposal. It asserts further that such a program, if extended beyond Year 4, could provide customer protection against price fluctuations.

Green Mountain further recommends consideration of the following elements of a BGS program: it should be a retail, not a wholesale auction; tranches should be for a term longer than one year; suppliers should have the opportunity to directly serve residential customers; selected customers should be able to opt-out within a specified period of time; additional customers should be assigned to replace those who opt-out; a limited number of tranches should be set aside to help promote “green power”; adequate customer communications must be provided; and new customers connected in the EDCs’ service territories should be required to affirmatively select a generation supplier.

## EDCs

In addition to their generic and utility specific proposals, the EDCs filed Final and Final Reply comments and appeared at the hearing.

The EDCs state that EDECA provides a blueprint for a smooth transition from a regulated monopoly to a competitive market, and note that the provision of retail choice to customers and the establishment of BGS for customers who do not switch suppliers are principal elements of that transition blueprint. The EDCs emphasize that the Act envisions competitive electric supply provided through retail choice as an inherently different product than BGS. They assert that BGS is a “plain vanilla” service intended as a backstop only, the price of which is fixed through the end of the Transition Period, and which cannot be marketed to customers. The EDCs emphasize that BGS supply must be procured from the competitive market commencing in August 2002, as the utilities have exited or are in the process of exiting the generation business, and have entered into various supply arrangements to meet their State-mandated BGS responsibilities at least through July 2002, with the expectation that BGS would be bid-out for service beginning August 2002.

The EDCs assert that their proposal would result in suppliers shouldering responsibility for BGS Load for the first time, will constitute the State’s initial attempt to bid-out BGS, and will further the orderly transition to a competitive power supply market. Given this, and given the time constraints associated with the August 2002 implementation date, the EDCs assert that any auction proposal accepted by the Board will serve as a transitional tool rather than embody the competitive “end-state.” They maintain that their proposal is the only one presented in the proceeding that is well developed and would not require lengthy collaborative sessions to work out basic fundamentals, and will provide experience to winning suppliers in supplying full-requirements service on a large-scale in the State.

The EDCs emphasize that no matter what method is used there will have to be 18,000 MW of supply procured commencing August 2002, and that the realities of supply and demand in PJM are unaffected by the process by which this power is procured. The EDCs’ contend that their proposed auction format would create an open and transparent process that would lead to an efficient and cost-effective procurement within the existing PJM supply and demand realities.

The EDCs explain the mechanics and advantages of the proposed Auction, claiming that the open and transparent system generates information that dispels the uncertainty faced by

suppliers regarding the likely success of their bids and thus encourages them to bid more aggressively. They argue that the inherent flexibility and efficiency of the auction and equitable treatment of all bidders will encourage participation and produce competitive pressure that will reduce overall procurement costs. Citing criticisms leveled by some concerning the request that the Board approve the auction results within one business day, the EDCs point to the testimony of their witness Meehan that the sole reason for this request is to reduce the cost associated with bidders having to otherwise include the cost of an “open option” in their price bids in the face of a volatile energy market. The EDCs cite to a similar expedited process employed by the Board for refinancing via securitization. They further state that such criticisms fail to recognize that the auction decision will not be a one-day approval, but rather a culmination of a process of numerous checks and balances in which the Board, its Staff and consultant, will have active involvement and will have agreed to interim decisions. The EDCs assert that this process will provide the Board with far more information than the simple forward price yardstick applied to a sealed bid process that the RPA’s witness Chernick advocates.

The EDCs argue that their proposal recognizes the unalterable, drastic changes that have taken place in the industry, including the EDCs’ divestiture of generation assets and deregulation of energy prices in PJM. Since the EDCs no longer have generation to hedge the risks involved in providing fixed price full-requirements service, a process that requires PJM generators and marketers to compete to provide fixed annual price BGS service is now appropriate, according to the EDCs.

The EDCs further assert that the proposed auction process is tried and true, having been used for years by the Federal Communications Commission and other agencies throughout the world to sell and allocate radio spectrum licenses, and in the energy industry such auctions have been successfully implemented in Texas, Canada, and France. They add that numerous refinements have been implemented over the years to improve the auction process. The EDCs rebut the criticism leveled by RPA witness Chernick that all previous SMR auctions involved a sale, rather than a purchase, pointing out that buyers can mirror strategies used by sellers. They also rebut RPA criticisms by pointing out that post-auction performance issues have been addressed through qualification criteria and rigorous contract protections, and by pointing out that preliminary interest on the part of prospective bidders is high, and that if actual interest is insufficient, auction volume can be modified accordingly. Rebutting the assertion that a single auction is somehow more risky or produces worse results than several, smaller-sized auctions, the EDCs argue that in fact several, smaller-sized auctions can lead to gaming opportunities and inefficiencies that are mitigated with a single auction. The EDCs assert that the likely case would be that suppliers would simply stay out or not bid aggressively in early auctions. Similarly, they assert that the RPA’s proposal to use a combination of approaches, including an auction, long-term purchases and short term purchases creates opportunities for gaming by bidders leading to both higher prices and inefficiencies. The EDCs contend that no other party in the proceeding has offered a viable, comprehensive alternative to their proposal, but offer instead only pilot programs for smaller quantities, criticisms, distortions or proposals to delay decisions for some unspecified period of time.

The EDCs state that others have mischaracterized their proposed Contingency Plan, in the event the BGS tranches are not fully subscribed as relying exclusively on “spot” purchases, and thereby, by implication, raising unfounded specters of California-like problems. They state that, in fact, they recommend using purchases from PJM-administered markets and various financial instruments that provide much more flexibility and risk management tools than reliance on the “spot” market. The EDCs also re-emphasize that the limited restrictions in the Contingency Plan preventing post-auction fixed-price, bilateral agreement contracts are solely intended to induce suppliers to bid and to ensure maximum participation in the auction. The EDCs also refute



suggestions that EDC affiliates should be prevented from bidding by arguing that numerous affiliate standards and other protections have been implemented and that such an artificial restriction on the sources of supply, particularly without any evidence of any wrongdoing, will only serve to reduce competition and increase the price of BGS service.

The EDCs refute the claim that EDECA requires that the Board must establish a “retail” program for BGS that assigns customers to suppliers and argue that such claims evidence a misunderstanding of EDECA. They assert that BGS is a regulated service separate and distinct from competitive service marketed by alternative suppliers. They note that subsection 9(c) of EDECA (N.J.S.A. 48:3-57(c)) does not direct the Board as to the manner in which the opportunity to provide BGS is to be bid-out or structured, nor does it mandate that such an opportunity include an electric power supplier becoming the “third party supplier” for those customers. The EDCs assert that their proposal will require winning bidders to be the providers of electric generation service to non-switching customers, and will result in suppliers being compensated based upon actual usage of supply by customers. This, the utilities assert, is different than a wholesale supply arrangement, in which suppliers contract to sell energy and capacity to the EDC without regard to what is actually used by customers. The EDCs point out that there is no mandate in EDECA that the provision of third party-supplied BGS include customer account services, or that BGS suppliers be given the type of customer-specific information, which a licensed supplier would normally obtain. They argue that proposals such as Enron’s would not constitute a true BGS proposal. They point out that the supplier in such a program would not act as a “provider of last resort” which is the primary function of BGS. They argue that under Enron’s plan, customers may opt-out, and the proposed “retail” program does not allow for the acceptance of new customers or customers who lose their competitive supply. The EDCs assert that the proposal by Enron should be called instead a “marketing through customer assignment” plan rather than a BGS plan.

The EDCs argue that the goals of developing a BGS proposal should not be confused with the goal of introducing competition, and maintain that the competitive retail market offers suppliers opportunities to market their services to customers and that BGS should not be used as a vehicle for mass marketing. They reiterate that EDECA leaves to the Board’s discretion the manner in which the opportunity to provide BGS is to be structured, and that a decision to adopt the EDCs’ proposal would therefore be consistent with the Act.

## GPU

GPU filed a supplement to the Joint EDC Final Comments. GPU states that it does not agree that EDECA mandates that customers be assigned to the winning bidder in the BGS auction; however, it indicates its belief that the EDECA permits an EDC to volunteer to undertake such an approach for a portion of its BGS Load<sup>6</sup>.

## **DISCUSSION**

As a preliminary matter, the Board has considered the RPA’s request of December 6, 2001 and the EDCs’ response dates December 7, 2001 and finds no reason to delay its decision in this matter. The Board agrees with the EDCs that notwithstanding the Enron situation, the electric and gas marketplace is currently operating in a robust, liquid, competitive and reliable fashion, and the natural gas supply marketplace is currently extremely robust, liquid, and quite competitive. Regarding the RPA claim that FERC’s issuance of new guidelines for determining

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<sup>6</sup> By letter dated November 19, 2001, GPU filed a petition seeking expedited approval of a retail pilot program for the provision of BGS. The Board will consider this petition in Docket No. EE01110784.

whether generation market power exists, the Board has reviewed the FERC Order and agrees with the EDCs that it does not apply to the PJM marketplace and the EDCs proposed auction. As for the RPA's request that the Board adopt the RPA position, the Board will discuss the issues related thereto below in rendering its decision in this matter.

The Board has very carefully considered the EDCs' Proposal and their comments and arguments in support thereof, and has very carefully considered the proposals, comments and arguments of the Ratepayer Advocate and all of the other parties who have participated in this proceeding. In conducting its review and consideration of the record in this matter, the Board, most importantly is ever mindful of EDECA and its responsibilities thereunder. Section 9(a) of EDECA, N.J.S.A. 48:3-57(a), provides that for at least three years after the starting date for the implementation of retail choice and thereafter until the Board "specifically finds it to be no longer necessary and in the public interest," each electric public utility shall provide basic generation service. Accordingly, pursuant to N.J.S.A. 48:3-57(a), with retail choice having been implemented on August 1, 1999, the Board must consider whether, as of the beginning of Year 4, or August 1, 2002, it is no longer necessary and in the public interest for the utilities to provide BGS. The Board also is cognizant that, as parties to this proceeding have pointed out, Section 9(c) of EDECA, N.J.S.A. 48:3-57(c), requires that no later than three years after the starting date of retail competition, the Board must issue a decision as to whether to make available on a competitive basis the opportunity to provide BGS to any electric power supplier, any electric public utility, or both. Thus the decision to be rendered under N.J.S.A. 48:3-57(c) must be issued by August 1, 2002.

In evaluating the proposals which have been presented in this matter, the Board also must recognize, as indeed a number of parties in addition to the EDCs do, that any decision rendered herein must be able to be implemented in a timely fashion so as to ensure the continuity of 18,000 megawatts of BGS service on and after August 1, 2002. The EDCs' Proposal can be implemented in a timely fashion so as to provide BGS service for Year 4 of the Transition Period, and moreover, rather than maintaining the status quo, the EDCs' Proposal represents a step in the smooth and orderly transition of the State's electric industry from a regulated monopoly to a competitive power marketplace. The EDCs' Proposal will diversify the supply for BGS service by seeking multiple competitive suppliers to serve "tranches" of the BGS retail load.

On the other hand, however, before determining whether the EDCs' Proposal represents a reasonable and appropriate measure for the provision of BGS, the Board has considered arguments of the parties opposed to the EDCs' proposal, including that the EDCs' Proposal is inconsistent with EDECA insofar as it does not allow for electric power suppliers to provide BGS on a retail basis directly to end-use consumers. Further, the Board has carefully considered whether there is any other proposal before it which can be implemented to provide for BGS on and after August 1, 2002, and if so, whether such a proposal is reasonable and appropriate.

Turning first to whether there are any other viable proposals before the Board, the only other proposal before the Board is that of Enron which provided what can be characterized at best as an outline of a proposal to bid out at least 30% of the EDCs' customers in each rate class to Board-licensed electric power suppliers. Shell, New Power, MAPSA, Green Mountain and the RPA have all, in varying degrees, endorsed the Enron approach. The Enron proposal requires numerous aspects to be developed: the development of bid specifications, creditworthiness standards, and supplier/customer agreements, the development of a random selection process to select from a list of all "non-shopping" customers, the employment of an independent third party "Statistical Expert" to assist in the selection process, the notification of assigned customers and an "opt-out" period for selected customers. In effect, the Enron proposal

requires the Board and parties to start almost from scratch in developing a process for Year 4. Even then, the Enron proposal would still leave the responsibility for procuring the majority (70%) of BGS supply with the EDCs. The Enron proposal entails numerous activities that need to be developed and as a practical matter could not be implemented so as to ensure the provision of BGS for Year 4.

Furthermore, in a related vein, the decision to be issued under N.J.S.A. 48:3-57(c) as to whether to make available on a competitive basis the opportunity to provide BGS, is a complex question with many significant implications particularly with respect to the pricing of BGS and the impact on retail choice. Among the many issues that need to be carefully considered by the Board before it makes its determination are: the percentage of BGS load which should be made competitive; what process should be used to make BGS available on a competitive basis; who should be the supplier if a BGS supplier defaults; what customer services should be included in BGS on a competitive basis; will reliability be maintained; how should customers be switched to different BGS suppliers; does competitive BGS pricing have to be uniform for all customers and should it be; what should be the role of the distribution companies and should they have any remaining supply responsibilities; should there be a specific licensing requirement for BGS suppliers; and, should utility affiliates be permitted to supply BGS in a competitive environment. Also to be considered must be the requirements of N.J.S.A. 48:3-57 (d) and (e) for BGS pricing consistent with market conditions and for cost recovery. Indeed, the RPA's witness Hempling described various options and questions that the Board will need to consider in deciding how to design a competitive BGS system and noted that in choosing from among the many options, the Board will have to determine which products and services BGS providers should produce or procure and the scope of their relationship with retail customers. Hempling Direct Testimony at 4, 17.

The record in the current proceeding does not fully address the many complex issues that need to be considered in rendering an informed decision under N.J.S.A. 48:3-57(c). Accordingly, by an Order being issued concurrently with the within Order, the Board will be providing an opportunity to more fully explore and consider the vital issues which must be determined in deciding whether to make available on a competitive basis the opportunity to provide BGS to any electric power supplier, any public utility, or both.

Pending the undertaking of this more comprehensive review and issuance of a decision, which, pursuant to N.J.S.A. 48:3-57(c), must be rendered by August 1, 2002, the Board, pursuant to N.J.S.A. 48:3-57(a), cannot, at this juncture, find it to be no longer necessary and in the public interest for the electric utilities to provide BGS. The Board recognizes that there are time constraints associated with ensuring the provision of BGS for the August 1, 2002 through July 31, 2003 period. The EDCs' Proposal, besides being the only fully developed proposal before the Board, will provide the greatest possibility for obtaining Year 4 BGS supplies at minimum cost to customers. It also provides for greater reliance on competitive markets by taking electric supplies out of the exclusive two party/bilateral contract arena and places BGS requirements open to all comers on an equal basis.

In reaching this decision, the Board also has considered the RPA's arguments that the Board's Final Orders in the EDCs' rate unbundling, stranded costs and restructuring proceedings reflect the objective of increased retail competition for BGS in Year 4. RPA Final Comments at 4-5. In particular the RPA cites " We expect that the bidding out of BGS for year four as provided in the Stipulation will have the added benefit of creating substantial competition among third party suppliers for the right to provide this service at the pre-established BGS rate/shopping credit price, thereby potentially producing added benefits to customers consistent with paragraph 17 of the proposed Stipulation. PSE&G Final Order at 111." The RPA also cites to similar terms in

the GPU and Conectiv Final Orders, while recognizing a distinction for Rockland. However, the Board believes that the RPA argument is flawed and does not preclude the Board from approving the EDCs' proposal herein. The reference in the Board Order to "potentially producing added benefits to customers consistent with paragraph 17 of the proposed Stipulation," is a reference to reduced costs/increased credits post-Year 4. Specifically, it was the intent of the Board that the Year 4 bid be designed to mitigate the aggregate level of deferred balances at the conclusion of the Transition Period. In fact, in the GPU Final Order the Board specifically indicated that the benefit of a competitive process would be of "potentially producing added benefits to customers in terms of a reduction to the Deferred Balance consistent with provisions of paragraph 6 of Stipulation I "GPU Final Order at 96. The EDCs' Proposal is consistent with that intention i.e. to minimize the cost of BGS in Year 4 and thereby, reduce deferred balances. The fact that the Board used the terminology "...creating substantial competition among third party-suppliers" if that is the focus of the Advocate's retail competition claim, is not contrary to the current proposal, and the use of "third-party suppliers" rather than "electric power suppliers" in the Final Orders allows for BGS proposals that provide for participation of a broad array of potential market participants. Thus, the Board concludes that the EDCs' Proposal is not inconsistent with the Board's prior Orders.

### AUCTION PROCESS

The RPA raises several concerns with the proposed auction process without offering any viable solutions. The RPA's concerns appear to be summarized by its remarks that the EDCs' Proposal is "fundamentally at odds with EDECA's objective of providing reliable and reasonably priced BGS subject to oversight by the Board" and "the utilities proposal would subject ratepayers to many dimensions of risk." RPA Final Comments at 6-8. Because the EDCs' Proposal would require successful bidders to be Load Serving Entities subject to PJM reliability rules as administered through the Reliability Assurance Agreement, the Board is convinced that the EDCs' Proposal in no way compromises reliability of BGS supply. As such, we must assume that the Advocate's emphasis is on reasonable pricing and minimal risk. In this context, the RPA fails to realize two basic fundamentals of not just the EDCs' Proposal but of any RFP process for Year 4. First, load requirements and the amount of supply available in the marketplace for Year 4 are not a function of the specific BGS procurement process that is utilized. Therefore, the RPA's criticisms that available supplies are not sufficient to create price competition, that a few generation owners dominate uncommitted generation and that the operation of the generation market would be hidden from the Board are concerns that could be raised for any RFP process. Second, the Board has the ultimate authority to accept or reject the results of the auction. The Board will direct its Energy Division Director and Chief Economist to observe the BGS auction, along with its consultant CRA. After the auction, the Board will be briefed by Staff and its consultant and receive input from the Auction Manager on the conduct of the auction and its results. At that point the Board would know if any national or industry event occurred which might have skewed the results. It would also know whether any questionable activity occurred during the auction to raise concerns about the validity of the outcome. The Board retains authority to not certify the auction results and to determine the manner to be used to secure Year 4 supplies. Therefore, the Board's final certification authority will sufficiently address the RPA comments regarding risk.

The RPA also indicates that this type of auction has never been tried for purchases. Although this is not entirely accurate, the fact is that there is no fundamental difference between using this auction for sales, which the Federal Communications Commission and many other government agencies have done, and using it to purchase electricity.<sup>7</sup>

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<sup>7</sup> See discovery requests/responses S-18 and RAR-BGS-7.

The RPA also comments on the EDCs not proposing benchmarks with which to evaluate the results of the auction. While benchmarks can, at times, be useful evaluation tools, because of the volatile nature of the wholesale electric market, and because it is not just commodity but capacity, ancillary services, load factors, weather risk and profit margin which must be factored into overall bids, it is difficult to predict results in a precise manner. The Board believes that an evaluation can be made to assure that the auction was conducted in a fair manner, in accordance with the auction rules and that the process was not circumvented in a way that would harm the results. The Board believes that a post-auction evaluation form, to be completed by the Auction Manager, is necessary and will order that the Auction Manager complete the Post-Auction Assessment annexed to this Order as Attachment B. The Board also will request its consultant CRA to complete this form.

As for the RPA's suggestion to rely in part on the RFP process previously utilized by Conectiv to procure BGS wholesale supply, the EDCs properly note that the Conectiv process had different goals and served different ends than the instant EDCs' Proposal. Conectiv was the LSE responsible for procuring supply to meet obligations, and was cautioned by the Board against locking up too much supply. However, for Year 4 the BGS suppliers will be LSEs, and will have the responsibility of planning and assuming risk associated with having sufficient supplies at all times to meet the BGS Load assigned to them.

The Board notes that the RPA has raised a series of concerns but has proposed no viable alternatives and has in fact advocated a delay in the Year 4 BGS procurement process. In fact, a number of the RPA's recommendations would actually detract from the competitiveness of the auction process and likely result in higher prices to ratepayers. For example, the RPA takes issue with the EDCs' Contingency Plan Proposal to obtain any unsecured supply through PJM-administered markets, and focuses on the spot market. RPA Final Comments at 8. In fact, as described in the EDC comments, the term "PJM-administered markets" does not foreclose the opportunity to use financial hedging tools to reduce spot market risks in the event that the Contingency Plans must be implemented. The purpose of this provision is to ensure maximum participation in the auction process. If suppliers think that there is an alternative way to supply New Jersey on an annual basis to participating in the auction, some would likely bypass the opportunity to participate in the auction in favor of negotiating with the EDCs post-auction. Power suppliers need to know that if they want to serve on an annual basis, New Jersey in Year 4, they need to participate actively in the auction process. It is for this reason that the Board rejects the RPA's proposal that exclusive two party/bilateral contracts remain an option, which could cause potential bidders to bypass the auction.

The RPA also suggests that to reduce risk, BGS Load should be auctioned in phases. RPA Final Comments at 14. As the EDCs indicate, however, the risks of a free and volatile marketplace do not disappear because the auction is spread out over a period of time. In fact, with the RPA's proposal, the chances are increased of conducting at least one phase of the auction during unfavorable market conditions. Furthermore, as described above, the Board's, final certification authority protects against the risks with which the RPA is concerned. Moreover, the RPA proposal also would involve increased time required to conduct the additional auctions and the potential for gaming by bidders. As additional time is added to the procurement schedule, the EDCs would be conducting the final phases of their auction closer to the peak summer pricing period. As time goes on, the available generation begins to become committed thereby reducing the amount available to participate in the auction and increasing prices. While the RPA raised a concern about the amount of available generation, the RPA proposal to address that concern will reduce that supply even further. Under this RPA recommendation, the Board also has a concern with supplier gaming. As proposed by the RPA,

several auctions would give suppliers “multiple bites at the apple.” There would be no incentive for suppliers to make their best offers in the first or even second auction if they know that if unsuccessful at a higher price, there will be additional opportunities to secure a portion of the load responsibility at a future time.

Based upon its review, and subject to certain qualifications discussed below, the Board believes that the EDCs’ proposed auction design is appropriate. If implemented effectively, the auction design should facilitate bidders’ expressions of economic value, mitigate the “winner’s curse,” and provide an efficient price discovery mechanism. Further, given the information currently available to the Board, the Board considers the EDCs’ Proposal for a simultaneous statewide auction as the best approach for procuring Year 4 BGS supply for electricity consumers in New Jersey; any other process is likely to present equal or greater risks and uncertainties for prospective bidders and would likely result in a less successful outcome relative to the objectives established for the auction. In reviewing the auction mechanics, the Board has identified a number of details concerning the auction process, auction marketing and promotion, auction design and other issues related to the auction that should be clarified and/or modified in order to proceed with the most efficient auction process with the greatest clarity for bidders. These clarifications and modifications will enhance the auction process, and are included and attached to this Order as Attachment C.

## BIDDER LICENSING

The EDCs’ Proposal includes a requirement that bidders be licensed by the Board as retail suppliers for the provision of BGS. EDCs’ Proposal, Part III, pg. 13. The EDCs’ licensing requirement is apparently premised upon the presentation of the EDCs’ Proposal as an auction to serve the full electricity requirements of retail customers. EDCs’ Proposal, Part II, pg. 1.

As the EDCs properly recognize, any party providing electric generation service to retail customers must be licensed. N.J.S.A. 48:3-78. , The Board, consistent with the requirements of EDECA, has adopted Interim Licensing and Registration Standards. N.J.A.C. 14:4-2.1 et seq. The interim standards were adopted specifically for the purpose of implementing retail choice, consistent with the Act, and specifically to enable and to establish the conditions for suppliers to offer electric generation service to individual retail customers. The interim licensing standards do not apply to EDCs engaged in the provision of BGS pursuant to section 9 of EDECA, N.J.S.A. 48:3-57. N.J. A.C. 14:4-2.2.

The Board has carefully considered but does not concur with the EDCs that their proposal requires licensing. EDECA requires licensing, consumer protection and anti-slamming standards in order to define and safeguard the relationship between electric power suppliers and those customers that they directly serve. EDECA further requires the Board to consider which customer account services can be provided by licensed suppliers. N.J.S.A. 48:3-54. In these and other instances EDECA envisions that licensing is required because retail suppliers would have direct contact with and sensitive information concerning its customers. The EDCs’ Proposal does not provide for this type of relationship. Rather than serving specific customers, the successful bidders will enter into contracts with EDCs acting on behalf of retail customers as a group such that the BGS suppliers will become responsible for a percentage share of total BGS Load, or a “tranche” of an EDC’s system. There will be no specific customers attached to specific suppliers and no bidder will have access to any customer names, addresses, phone numbers, account numbers, etc. The EDCs shall continue to be responsible for billing BGS customers and for responding to customer inquiries; BGS suppliers will have no direct contact or direct relationship with individual customers. Therefore, the EDCs’ Proposal cannot properly be categorized as “serving retail customers” in the manner that EDECA envisioned as

necessary for Board licensing. The Board FINDS that fulfillment of their auction obligations will not cause successful bidders to be “Electric Power Suppliers” as defined in N.J.S.A. 48:3-51 and N.J.A.C. 14:4-2.2 and thus successful bidders do not need to obtain a New Jersey electric supplier license.

Moreover, while the interim licensing and registration standards are not applicable to suppliers under the EDCs’ BGS auction proposal, since they will not be directly interacting with individual retail customers, the Board has reviewed each of the provisions of the standards and notes that those provisions are met or are rendered moot by the EDCs’ Proposal. The relevant provisions of the interim standards are set forth in Section 2.5- Application Requirements, and Section 2.6 – Conditions for Maintaining a License in Good Standing. N.J.A.C. 14:4-2.5; N.J.A.C. 14:4-2.6.

Specifically, background information on the supplier as required to be submitted by prospective electric power suppliers in subsections 2.5(a) 1. through 4. of the interim licensing standards will be submitted by prospective BGS suppliers as provided in Part 1 of the auction Application Form. Subsection 2.5(a) 5. of the licensing standards, requiring a list of all types of services and/or products which the supplier intends to offer to customers, is rendered moot by the nature of the BGS proposal. The required information set forth in subsections 2.5(a) 6. through 9. of the licensing standards, dealing with evidence of financial integrity, ownership interests, and any past adverse rulings and criminal activities, is also provided for in Part 1 of the auction Application Form. While the provisions of subsection 2.5(a) 10. concerning an in-state agent for service of process and customer service agent purposes are rendered largely moot since BGS suppliers in Year 4 will not be serving individual customers, Part 1.3 of the auction Application Form nonetheless requires identification of a supplier’s in-state legal representative or agent. Subsection 2.5(a) 11 of the licensing standards requiring retail sales information broken down by customer class is rendered moot by the nature of Year 4 BGS supply. The requirements of subsections 2.5(a) 12. and 2.6(e) concerning the maintenance of a surety bond or equivalent financial instrument, to insure against a failure on the part of a supplier to pay taxes or assessments, or a failure to meet contractual commitments to customers, is superseded and/or rendered moot by the credit application procedures and posting of bid bonds in the auction Application Form, and the Creditworthiness provisions in Article 6 of the BGS Master Service Agreement. Moreover, it should be noted that in Year 4 the EDC will be responsible for collecting and remitting sales tax on BGS sales to customers.

The provision of subsection 2.6(a) of the licensing standards requiring that the supplier meet the requirements of a PJM LSE will be directly satisfied, as it is a condition of eligibility for a BGS supplier under the EDCs’ Proposal. Subsections 2.6 (b) and (c) apply only to gas suppliers, and are therefore moot. Subsection 2.6(d) of the licensing standards, requiring an in-state office, is rendered moot since a BGS supplier in Year 4 will not have direct customer contact therefore will not need a customer service function (as noted previously this function will be provided by the EDCs), will not need to maintain records related to contracts entered with New Jersey customers since no contracts with individual customers will be entered into, and will not be responsible for collection or remittance of sales tax. Moreover, as discussed above, BGS suppliers will be required to identify in the auction Application Form an in-state legal representative or agent upon whom legal process may be served. The provisions of subsection 2.6(e) of the licensing standards are addressed above. With respect to the provisions of subsection 2.6(f) of the licensing standards, requiring compliance with specific electric power supplier standards, the Board’s consumer protection and anti-slamming standards are clearly not applicable to BGS suppliers in Year 4 since such suppliers will not be marketing to,

assigned to, contracting with or otherwise interacting directly with individual retail customers.<sup>8</sup> Subsection 2.6(g) of the licensing standards requiring Zip plus 4 information on residential customers served by each supplier is rendered moot by the nature of BGS supply in Year 4, and subsection 2.6(h) requiring assistance in investigating customer complaints against supplier is also rendered moot, since suppliers will not have direct contact with individual retail customers, and since customer complaints concerning BGS supply will continue to be handled by the EDCs which are subject to the Board's jurisdiction through existing regulations.

In addition to concluding that an electric power supplier license is not required for bidders under the EDCs' Proposal, the Board notes that such a requirement might potentially eliminate a number of market participants in the auction and not requiring licensure which is not otherwise mandated will enable the auction be open to the broadest possible array of participants.

It should also be emphasized that the proposed auction represents a transitional mechanism that will be in effect for one year. In the event the Board adopts a different model for the procurement of BGS for Year 5 and/or beyond, by which individual retail customers are served directly by individual non-utility BGS suppliers, it may be necessary and appropriate to require licensing of BGS suppliers at that time. Moreover, given the unique nature of BGS, as compared to competitive electric generation service offered through retail choice, it may be necessary in that event for the Board to adopt a specialized set of licensing standards applicable to BGS suppliers only.

## CUSTOMER SWITCHING

The EDC filing proposes that commercial and industrial customers ("C&I") on BGS as of August 1, 2002 be required to stay on BGS through the term of this supply period (through July 31, 2003). EDCs' Proposal, Part I, pg. 3. The EDCs' Proposal recognizes that C&I customers represent a larger load per customer than do residential customers, and that even a few C&I customers leaving BGS can affect the amount of load and the load profiles being served. As a result, the prospect of switching by C&I customers during Year 4 can introduce an additional element of risk for a fixed price offering, thereby necessitating a larger risk premium in the bid prices. Accordingly, the more certainty in the load that will be served by prospective bidders, the lower the bids should be. Therefore, to the extent C&I customers can remain committed to being served via BGS, all BGS customers would be better off.

This auction provision is similar to current EDC tariff provisions that, in order to reduce gaming, require C&I customers returning to BGS during the summer months to stay on BGS for one year and during other months provides a thirty day window to find a new supplier before the one year commitment takes effect. An issue arises however when the current tariff requirements are combined with the proposed auction provision. If a C&I customer returned to BGS in September of this year, for example, and did not find a supplier within thirty days it would have to stay on BGS until September 2002. Currently, the C&I customer has ample opportunity to be aware of this tariff provision and would act accordingly. However, the EDCs are now proposing that the requirements change, in effect tying this sample customer to BGS for 23 months (September 2001 through July 2003).

The Board agrees with the desired effect of reducing bidder uncertainty and lowering costs to BGS customers. However, the Board believes that this provision should be modified to require ample notice to C&I customers and an opportunity prior to the beginning of Year 4 for C&I

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<sup>8</sup> The Board is not deciding herein whether the "anti-slamming" provisions of EDECA apply at all to changes in the identity of BGS Suppliers that have been approved by the Board. Our finding here is limited to the facts as set forth in the current EDCs' Proposal.



customers to switch to a licensed supplier. Specifically, the Board believes that EDCs should provide C&I customers that have, or will, return to BGS service beginning July 2001 through June 2002 with the opportunity to switch to a TPS on their April, May, June or July 2002 meter read dates, providing the meter read date is before August 1, 2002. C&I customers on BGS as of August 1, 2002 would be committed to stay on BGS through July 31, 2003. C&I customers who returned to BGS service up to and including their June 2001 meter read date or return on or after August 1, 2002 will be subject to existing tariff switching requirements. In addition, EDCs must notify all C&I customers of the changes in this BGS requirement twice between the date of this Order and June 1, 2002.

## COMMITTED SUPPLY

The filings of the EDCs would assign to winning BGS bidders a proportional share of Committed Supply capacity, energy and ancillary services, if any. "Committed Supply" is defined, in part, as "certain power supplies to which the Company has a physical or financial entitlement." EDCs' Proposal, Part III, pg. 4-5. While there is some merit in this methodology, it requires bidders to understand and evaluate the risks of energy and ancillary service deliveries from Committed Supply. In order to avoid a situation where bidders are asked to price risks, which they may believe to be difficult for them to fully evaluate, the Board will modify the EDCs' Proposal with respect to Committed Supply. Specifically the EDCs shall make available to bidders a proportional share of only the PJM capacity credits associated with Committed Supply. Capacity credits are subject to less uncertainty and will help bidders prepare attractive bids. Committed Supply energy and ancillary services, if any, should be sold by the EDCs in the wholesale market and revenues from such sales should be credited against the corresponding costs of Committed Supply, consistent with each EDC's deferred accounting. There should be two exceptions to this modified procedure. First, due to the small amount of Committed Supply available to Rockland and the fact that none has historically been used for PJM capacity credits, Rockland shall exclude all Committed Supply products, including capacity credits, from the BGS auction and recover these costs as authorized in past Orders. Second, recognizing that Conectiv has a Final Order which calls for it to use the power from its non-utility generation ("NUG") contracts to serve BGS load, Conectiv should reserve a fixed percentage of BGS load and to serve that load by applying its NUG related power (capacity, energy and ancillary services), using as necessary the procedures previously approved by the Board, to serve that percentage of the BGS load; thus Conectiv would provide full requirements service to a fixed percentage of its BGS load.

## AUCTION PROMOTION/DEVELOPMENT

A successful BGS procurement can be achieved with a well-designed simultaneous descending clock auction provided that the rules and details are specified and implemented correctly, and provided that the auction process provides sufficient awareness among qualified potential bidders so that a competitive procurement takes place. To maximize participation and competition, the BGS auction process requires a marketing and promotion plan aimed at ensuring exposure and awareness among qualified potential bidders. In anticipation of Board approval, the EDCs have attempted to facilitate the auction process and increase the number of prospective bidders by educating potential bidders about the auction proposal. Among the steps taken by the EDCs are:

- Bidder Information Sessions in Philadelphia and Houston;
- Auction web site at [www.bgs-auction.com](http://www.bgs-auction.com) which publicizes new developments, allows interested parties to download documents related to the auction, has FAQs (Frequently

Asked Questions with answers) so all bidders are similarly informed; and has links to PJM and other useful sites;

- Virtual data room for potential bidders with data relevant to the bid and answers to questions posed by bidders about the data in virtual data room;
- Bidder information packets including the background information and information about the auction process;
- Press releases to newspapers and trade publications;
- Direct emails to interested parties to inform them of any new developments or any new documents posted to the website; and
- Comments solicited on the draft auction rules, the draft Master Service Agreement and the draft application materials.

The Board believes that the foregoing marketing effort by the EDCs increases the chances that a successful BGS procurement can be achieved.

#### ROCKLAND ELECTRIC COMPANY

The Board recognizes that the Rockland request to join PJM is pending at FERC and that at the present time Rockland is still affiliated with the New York ISO. This membership issue is addressed by Rockland in its addendum to Part II of the EDCs' Proposal, but not in the BGS Master Service Agreement. Should PJM membership not be determined by the time of this Order, Rockland needs to prepare and file a separate BGS Master Service Agreement to reflect the obligations and responsibilities of bidders as a result of possibly operating through the New York ISO, and the EDCs' Proposal needs to reflect Rockland's possible participation in the auction as a member of the New York ISO.

In addition, the Board does not believe that this is the appropriate forum to consider Rockland's request for approval of all costs associated with its request to become a PJM member, whether the PJM request is successful or not. This proceeding is focused on the RFP process and alternatives thereto, not recovery of costs not previously addressed by the Board. Rockland will have the opportunity in a future proceeding to request recovery of its PJM-related application costs, at which time the Board and participating parties will be able to consider the appropriateness and prudence of those costs.

#### PJM

There are several areas in which close coordination between the EDCs and PJM is required to qualify BGS suppliers to serve load within PJM, and to ensure that potential BGS suppliers are not at a disadvantage relative to other suppliers in PJM. The specific areas where such coordination is required include:

- o Timing of Fixed Transmission Rights.
- o Credit requirements for PJM membership.
- o Capacity obligations and credits.
- o Network Service Agreement for BGS suppliers.

PJM has been very receptive to accommodating a BGS auction process for New Jersey within their administrative and operational framework, including providing information about the Auction on its own website. By working with the representatives from PJM, these key issues have been addressed, and any necessary changes at PJM have been implemented. In fact, on December 6, 2001, PJM approved changes to the Network Service Tariff and agreed to a second Firm Transmission Rights ("FTR") "Open Season" to specifically accommodate the BGS auction process. These changes will be filed with FERC.

## YEAR 5

Each of the EDC's Company Specific Addendums discusses BGS "post Year 4." While not making specific requests, each indicates a pricing structure "after the transition period" and the possibility of extending the term of the current auction proposal beyond Year 4. The Board concludes that the BGS auction should be confined to Year 4 only, as envisioned in the Final Orders. As emphasized above, the EDCs' proposed auction is an appropriate transition mechanism, in keeping with the intent of EDECA that there be a smooth transition to a fully competitive electric power industry. It may be appropriate to consider refinements or alternatives to the BGS auction mechanism for implementation after the conclusion of Transition Period, in Year 5 and beyond, to address some of the issues raised in this proceeding by retail suppliers and the RPA. The Board is concurrently issuing an Order establishing a proceeding by which post-Transition Period BGS issues will be further reviewed. Many of the issues raised herein by the RPA, as well as rate structure design raised by the EDCs, will be included as subjects for further investigation as part of this proceeding.

## GEOPHONICS

Although Geophonics presented its concerns as to the applicability of its patent, Geophonics indicated at the hearing that it did not intend to "get in the way" of the auction process. By issuing this Order and authorizing the utilities' use of their proposed auction process to provide for BGS for Year 4, the Board is not ruling upon patent matters as between Geophonics and the utilities, which matters are not within the Board's jurisdiction. See 28 U.S.C.A. §1338; 35 U.S.C.A. §281.

## BOARD APPROVAL PROCESS

The Board believes that a successful BGS procurement can be achieved with a well-designed simultaneous descending clock auction provided that the rules and details are specified and implemented correctly. An overriding fundamental, which the Board has concluded from reviewing the EDCs' Proposal and the record in this proceeding, is that bidders are averse to uncertainty. Uncertainty results in bidders either not participating or in factoring their discomfort, as "risk premiums" into their bids. In addition to other risk elements discussed above, uncertainty or delay concerning the period between the submission of bids and the approval of the bid results by the Board is of substantial concern. Therefore, if the Board approves an auction process, barring some national or industry emergency, the timing of the auction process, including certification of the auction results, needs to take place according to a pre-approved schedule. As indicated in Attachment A, Tentative Approvals and Process, there are a number of decisions/actions that would need to be made after Board approval of the auction process. Each of these decisions/actions needs to take place according to schedule in order that the bidders are prepared and comfortable with participating and the auction results in the

best BGS price possible. Attachment A is labelled "Tentative" only to indicate that the Auction Manager has some discretion with implementation dates, not to indicate that the Board anticipates any changes to this schedule.

Paramount among the actions that need to be taken is prompt certification of the auction results. Because of the volatility of the electric markets, bids cannot remain valid for any prolonged period of time. If bidders perceive that there may be a delay in certifying the results the additional risk to bidders will show itself through higher prices. Therefore the Board will commit to addressing the auction results by the end of the second full calendar day after the calendar day on which the auction closes.

Furthermore, the auction has been designed to secure supply for all four EDCs at the same time. The structure of the auction that permits and encourages bidder movement between EDCs implies to the bidder that, while being different products, tranches will be viewed on equal terms by the Board. It is important to the efficiency and economy of the process that bidders do not impute unwarranted uncertainty into the auction results of any EDC. Therefore, the Board will consider the results of the auction in its entirety and certify the results of all of the EDCs or for none of them.

For the final certification of the auction results, the Board will schedule a special agenda meeting for the first day of the auction, as a forum to consider unforeseen circumstance, should any develop. The Board will schedule and convene this meeting and then recess until the auction is complete and the Commissioners each have an opportunity to review and consider the auction results. It is envisioned that the process will take a minimum of three days, *i.e.*, at least a day for the auction, a day for Commissioners to review and consider the results, and certification on the third day.

In addition to the auction certification, the only other decision, identified in Attachment A that requires full Board approval is acceptance of the EDCs' Compliance Filing. As indicated above, the Board believes that certain clarifications to the EDCs' Proposal are required pertaining to the details of the auction design. Because of the significance of this proceeding the Board will direct that the EDCs make a Compliance Filing within two days of this Board Order. The Board will consider approval of the Compliance Filing at a special Board meeting two days thereafter.

Either the EDCs or the Auction Manager, in consultation with Staff and CRA as may be necessary, will make other Auction decisions, identified in Attachment A. These decisions include determination of Contingency Plan levels, establishing minimum and maximum starting prices, establishing specific starting prices, the resolution of association issues, specific bidder application and credit issues, load cap and volume adjustment decisions, auction price decrements and other unknown lesser decisions which might be required throughout the implementation process. Some of the aforementioned areas, such as bidder application and credit issues, are subject to rules spelled out in the EDCs' Proposal. Other areas, such as load caps and volume adjustment decisions, determination of Contingency Plan levels, establishing minimum and maximum starting prices, establishing specific starting prices, the resolution of association issues, and auction price decrements are either utility-specific concerns, are determined directly from algorithms included in and approved as part of the EDCs' Proposal or

are areas that need to be addressed by the Auction Manager based on its experience in this field.

## FINDINGS AND CONCLUSIONS

Based on the foregoing and after carefully reviewing the record in this proceeding, the Board FINDS that:

this has been an open proceeding, with all parties desiring to present written or oral comments on the record able to do so;

the EDCs' Proposal, as modified herein, is consistent with EDECA and the EDCs' Final Orders;

the EDCs' Proposal does not exclude participation by electric power suppliers;

the EDCs' Proposal can be implemented in a timely fashion so as to provide BGS service for Year 4 of the Transition Period;

the EDCs' Proposal represents a step in the smooth and orderly transition of the State's electric industry from a regulated monopoly to a competitive power marketplace;

the EDCs' Proposal will diversify the supply for BGS service by seeking multiple competitive suppliers to serve "tranches" of the BGS retail load;

the proposal to obtain any unsecured supply through ISO-administered markets will ensure the maximum participation in the auction process;

conducting one auction for all BGS Load, rather than multiple auctions, reduces risk and the opportunity for gaming by bidders;

besides Enron, no other party has proposed more than an outline of an alternative to the EDC approach, and the alternatives that have been outlined all provide greater risks and uncertainties than the EDC's proposed auction;

the RFP proposal submitted by Enron does not provide sufficient detail to be implemented in time to secure economical supplies for Year 4 and does not address the electric supply for 70% of the BGS Load;

the record in this proceeding does not fully address the issues that need to be considered in rendering a decision under N.J.S.A. 48:3-57(c) as to whether to make available on a competitive basis the opportunity to provide BGS directly to end-use customers to any electric power supplier, any public utility, or both, and these issues will be considered in the proceeding being established pursuant to an Order being issued concurrently with the within Order;

the Board is making no ruling herein as to Year 5 and beyond and will consider issues related thereto in the further proceedings being established by concurrent Order;

it is necessary and in the public interest for the electric public utilities to provide BGS in Year 4 of the Transition Period;

the EDCs' Proposal, as modified herein, is the best means to secure electricity for Year 4 with the least cost to consumers and with a minimum of risk;

modifications identified by Staff concerning the details of the auction process, auction marketing and promotion, auction design and other auction issues set forth in Attachment C, are appropriate and should be implemented;

in order to avoid situations where bidders are asked to price risks, which they may believe to be difficult for them to fully evaluate, the Committed Supply methodology should be modified as described herein;

the EDCs' Proposal, and particularly the BGS Master Service Agreement, must specifically recognize that Rockland is not currently a member of PJM;

this is not the appropriate forum to consider Rockland's request for approval of costs associated with its request to become a PJM member which request for approval and recovery of costs may be renewed at a future time, subject to review for appropriateness and prudence of those costs;

the EDC Proposal, as modified herein, is consistent with PJM rules, procedures and operations and can be accommodated by existing PJM rules or procedures;

fulfillment of their auction obligations will not cause successful bidders in the BGS auction to be "Electric Power Suppliers" as defined in N.J.S.A. 48:3-51 and N.J.A.C. 14:4-2.2 and thus successful bidders do not need to obtain a New Jersey electric power supplier license;

it is consistent with the goals of the RFP proceeding to require that C&I customers on BGS as of August 1, 2002 be required to stay on BGS through July 31, 2003;

that EDCs must provide C&I customers that have, or will, return to BGS service beginning July 2001 through June 2002 with the opportunity to switch to a TPS on their April, May, June or July 2002 meter read dates, providing the meter read date is before August 1, 2002;

C&I customers who returned to BGS service prior to their June 2001 meter read date or return on or after August 1, 2002 will be subject to existing tariff switching requirements;

EDCs must individually notify all C&I customers of the changes in the BGS switching requirement and conditions a minimum of two times between the date of this Order and June 1, 2002;

the accounting and cost recovery processes identified in the utility-specific addendums to the EDCs' Proposal are reasonable and consistent with the Board's Final and Summary Unbundling Orders;

the utility-specific Contingency Plans are reasonable;

the Board's Energy Division Director and Chief Economist and CRA shall observe the auction for the Board;

EDCs and the Auction Manager will provide final comments to the Board on the results of the auction and how the auction was conducted, including the post-auction evaluation form in

Attachment B, prior to Board certification of the results, with copies provided to the RPA.

CRA shall provide final comments to the Board, including a completed post-auction evaluation form in Attachment B, prior to Board certification of the results;

the Tentative Approvals and Process schedule in Attachment A balances process efficiency with Board oversight; and

the Board will consider the results of the auction in its entirety and certify the results of all of the EDCs or for none of them.

For the foregoing reasons, the Board APPROVES the EDCs' Proposal and EDC-specific addendums, with modifications as indicated herein. The Board FURTHER APPROVES the tentative decision schedule included as Attachment A, including Board certification of the auction results by the end of the second calendar day following the calendar day on which the auction closes. The Board reserves the right, at the certification meeting, to reject the auction results and to provide direction on an alternate means for the EDCs to procure its BGS supply requirements for Year 4. In addition, the Board DIRECTS that the EDCs' Proposal be modified consistent with the foregoing, including:

the decision-making process and auction timetable are consistent with Attachment A;

EDCs will provide C&I customers that have, or will, return to BGS service beginning July 2001 through June 2002 with the opportunity to switch to a TPS on their April, May, June or July 2002 meter read dates, providing the meter read date is before August 1, 2002;

C&I customers who returned to BGS service prior to their June 2001 meter read date or return on or after August 1, 2002 will be subject to existing tariff switching requirements;

EDCs will notify all C&I customers of the changes in the BGS switching requirement twice between the date of this Order and June 1, 2002;

bidders, potential and/or successful, shall not be required to obtain an electric power supplier license;

modifications identified in Attachment C, concerning the details of the auction process, auction marketing and promotion, auction design and other auction issues, are implemented;

the changes necessary to effect the Committed Supply modifications, described herein, including changes to the BGS Master Agreement and clarifications to each EDC's proposed accounting and cost recovery provisions;

Rockland should prepare and file a separate BGS Master Service Agreement to reflect its status as a member of the New York ISO and the obligations and responsibilities of bidders as a result of possibly operating through the New York ISO; and

the EDCs' Proposal should reflect Rockland's possible participation in the auction as a member of the New York ISO.

Furthermore, the Board DIRECTS the EDCs to make compliance filings, including any changes consistent with this decision, by Wednesday, December 12, 2001. The Board FURTHER DIRECTS the EDCs to work with Staff and CRA to ensure that any supplemental documents, such as application forms, are fair and developed consistent with this decision and that the review procedures for such documents are applied in a consistent and non-discriminatory manner.

DATED: December 11, 2001

BOARD OF PUBLIC UTILITIES

BY:

(Signed)

CONNIE O. HUGHES  
PRESIDENT

(Signed)

CAROL J. MURPHY  
COMMISSIONER

(Signed)

FREDERICK F. BUTLER  
COMMISSIONER

ATTEST: (Signed)

HENRY M. OGDEN  
ACTING BOARD SECRETARY