

**NON-CONFIDENTIAL VERSION**

**STATE OF CONNECTICUT**

**DEPARTMENT OF PUBLIC UTILITY CONTROL**

RE: DPUC DEVELOPMENT AND : DOCKET NO. 06-01-08PH01  
REVIEW OF STANDARD :  
SERVICE AND SUPPLIER OF :  
LAST RESORT SERVICE : AUGUST 30, 2006

**THE UNITED ILLUMINATING COMPANY'S  
PROCUREMENT PROCESS AND RESULTS  
FOR STANDARD SERVICE AND LAST RESORT SERVICE:  
COMMENTS OF THE OFFICE OF CONSUMER COUNSEL**

## I. INTRODUCTION

### Summary

1. UI's conduct of its procurement effort for Standard Service (SS) and Last Resort Service (LRS) was satisfactory. UI's performance met the applicable statutory standards and the DPUC's basic criteria.
2. The prices UI obtained for its SS/LRS tranches appear to reflect current conditions in the wholesale market, judging by OCC's target price and otherwise.
3. OCC, having reviewed the joint UI/Levitan recommendations on what SS/LRS bids to accept, believes the DPUC should accept those recommendations as filed.
4. UI has been cooperative and open with OCC throughout this process. Levitan generally worked well with OCC.
5. This SS/LRS auction effort was made more difficult than necessary, due to delay in authorizing the start of this effort, and otherwise.

The Office of Consumer Counsel ("OCC") is a participant in this docket, which the Department of Public Utility Control ("DPUC" or "Department") established on its own initiative.

The initial phase of this docket approved a plan under which the state's two electric distribution companies, The Connecticut Light and Power Company ("CL&P") and The United Illuminating Company ("UI" or "the Company"), are to procure electric generation service contracts for two purposes. The first such purpose is to provide standard service under Connecticut General Statutes ("CGS") § 16-244c ("Standard Service" or "SS"), and the second such purpose is to provide supplier of last resort service under CGS § 16-244e ("Last Resort Service" or "LRS"). Under Public Act 03-135, An Act Concerning Revisions to the Electric Restructuring Legislation (the "Revised Restructuring Act" or "Act"), CL&P and UI will be required to offer both Standard Service and Last Resort Service to (separate) groups of customers from January 1, 2007 onward.

The DPUC issued its initial decision (the "Initial SS/LRS Procurement Decision" or "Initial Decision") in this docket on June 21, 2006. The Initial Decision (pp. 6-7) says that OCC should be afforded an opportunity to directly and fully participate in all aspects of the SS/LRS procurement process, for both distribution companies, and that OCC should have full access to all bidder information, subject to appropriate confidentiality provisions.

This invitation to OCC was something new in DPUC structuring of recent power procurements by CL&P or UI. For instance, during the Transitional Standard Offer procurements (2003-2005), OCC was essentially excluded from the process. OCC appreciates the DPUC's change of position on this issue, so vital to the state's electric ratepayers.

OCC, having reviewed the DPUC's Initial Decision, informed the DPUC on June 22, 2006 that it intended to accept this invitation to participate in the SS/LRS procurement process, for both distribution companies. The first step in that OCC participation was our agency's attendance at a June 23, 2006 "kick-off" meeting inside the DPUC, in which representatives of Levitan & Associates, Inc. ("Levitan"), the Department's<sup>1</sup> independent consultant, participated. Since then, OCC and its own chosen consultant have spent hundreds of person-hours on this effort (as will be recounted below, at least in some measure).

OCC herewith submits its Comments on UI's Procurement Process and Results in this docket.

## **II. DISCUSSION**

### **A. UI's Conduct of its SS/LRS Procurement was Satisfactory.**

Distribution company procurement of both Standard Service and Last Resort Service must meet a number of specific standards. In part, these standards are set out in the statute. In part, these standards have been established by the DPUC.

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<sup>1</sup> The DPUC's Initial Decision states, erroneously, that Levitan has been retained by both the Department and OCC. OCC has twice (7/10/06; 7/20/06) asked the DPUC to correct this clerical error. Inexplicably, the DPUC has twice (7/18/06; 8/18/06) declined to do so. While OCC has worked closely with Levitan in recent weeks, our agency retained its own consultant, per CGS § 16-18a, for the recent work in this docket.

### **The Statutory Standards**

The Revised Restructuring Act sets out the procurement process for Standard Service in considerable detail, in CGS §§ 16-244c(c)(3), 16-244c(c)(4) and 16-244c(c)(5). The DPUC must approve, for both distribution companies, a procurement plan that meets multiple standards. Among the standards that the Standard Service procurement process and the resulting “portfolio of [Standard Service] contracts” must meet are:

- (a) Distribution company mitigation of variation in the price of Standard Service;
- (b) Sufficiency to meet projected Standard Service load;
- (c) An overlapping pattern most likely to produce just, reasonable, and reasonably stable retail rates, while reflecting wholesale market prices over time;
- (d) Inviting competition, while guarding against favoritism, extravagance and fraud;
- (e) Securing reliable supply while avoiding unusual or excessive pricing;
- (f) Minimum six-month terms, though shorter terms are allowable under strict conditions prescribed by DPUC;
- (g) Bids from generation affiliates of distribution companies are allowed, with certain restrictions.

At the same time, the Revised Restructuring Act says very little about the procurement process for Last Resort Service (for which UI also sought bids in the present procurement effort). The Act does carefully define the (small) group of customers eligible for this service, and limits distribution-company risks related to customer switching (by setting a minimum one-year term on LRS for customers previously on competitive supply).

However, the Act sets out only two requirements regarding the energy supply for Last Resort Service. First, the distribution companies must procure such electricity. Second, the

DPUC must “determine a price for such customers that reflects the full cost of providing the electricity on a monthly basis.”

### **The DPUC’s Standards**

The Initial SS/LRS Procurement Decision (pp. 3-4) provides that distribution company procurement of both Standard Service and Last Resort Service is subject to a number of basic criteria, specifically:

- (a) The process must be fair and impartial to all participants.
- (b) The existing Code of Conduct (relating to distribution companies and generation affiliates) must be strictly observed.
- (c) The procurement effort must notify as broad a group of potential bidders as is practicable, through invitations issued in several available formats.
- (d) The procurement should cost-effectively promote price consistency/stability and minimization of revenue requirements. Criteria for evaluating competing bids must be well-defined, measurable and available to the suppliers in an open and fair manner.
- (e) Potential bidders should have clear opportunities for questions. Bidder access to relevant data should be complete, non-discriminatory and timely, so that the number of bidder responses is maximized.
- (f) The resulting contracts should not limit the pursuit, by multiple entities, of conservation or demand response initiatives.
- (g) Procurement participation should not be limited to bidders with their own fleet of power plants, but should include bidders that can offer supply by managing forward contracts and hedging instruments.

### **OCC’s Procurement Participation**

OCC, as the representative of electric ratepayers, participated closely in recent weeks in every aspect of the UI procurement process for Standard Service and Last Resort Service.

1. OCC staff and/or consultants attended approximately 36 meetings with UI and Levitan staff in person or by phone, including:
  - Meetings of UI staff, Levitan, and OCC on July 5, 11, 13, 18, 20, 21, 25, 27, 28, and 31; and August 2, 3, 4, 8, 9, 11, 15, 17, 22, 24, 25, 26, 27 and 29.
  - UI calls with individual bidders, monitored by Levitan and OCC: multiple calls on each of the following days: August 22, August 23, August 24, August 25, August 29.
2. OCC staff and consultants reviewed the following documents, each in several iterations, and proposed amendments and corrections:
  - Wholesale Power Supply Agreement for Standard Service
  - Wholesale Power Supply Agreement for Supplier of Last Resort
  - Term sheets
  - Bidder information form
  - Bidding worksheets
  - UI's closing statement to bidders
3. OCC consultants prepared mock bids in parallel with UI and Levitan staff, participated in the comparison of alternatives and the final selections of the mock bids, and reviewed Levitan's results.
4. OCC consultants reviewed draft responses to each of the bidder questions, and commented on approximately 33 such responses, sometimes in multiple rounds.
5. OCC consultants drafted, reviewed and suggested revisions to bid-evaluation tools, including linear-programming bid-choice models and comparison-price computations.
6. OCC was involved in essentially all discussions of employing the barrier-put option.
7. OCC staff and consultants were present at UI's offices on bid day, from 8:30 AM, before the first bids were received at 10 AM, until well after the selection of bidders was made,

and were involved in all aspects of the review of the bids and selection of the lowest-cost combination.

**OCC's comprehensive participation in the UI procurement effort, just described, has given our agency a sound basis upon which to evaluate the extent to which that UI effort meets the standards set out in the applicable statute and in the Initial Decision.**

### **UI's Procurement Effort**

1. The development of the request for proposals ("RFP"), term sheet, contracts, historical and projected data, questions, and other bid documents was undertaken seriously, with attention to detail, and in a commercially reasonable manner. The Company's management and technical staff, and its attorneys from outside law firms, along with Levitan staff and OCC consultants, reviewed and edited multiple versions of the RFP and contracts, prior to release of the RFP. The same parties completed additional rounds of RFP edits between the RFP release and bid date, in response to internal reviews, bidder questions, and discussions with bidders. This process culminated in the development of a final contract for each bidder, reflecting the specific issues of each bidder.

OCC believes that the development of the bid documents met the Department's standards and good utility practice. In particular, the RFP was consistent with the requirement in the Department's standard (d) that "Criteria for evaluating competing bids must be well-defined, measurable and available to the suppliers in an open and fair manner."

2. Notification of the RFP was widely distributed through ISO-NE to all the entities that would be eligible to participate in the procurement. The RFP itself was posted on the UI web site.

OCC believes that the distribution of the RFP meets the Department's standard (c), above.

3. The Company responded to questions, concerns and suggestions from Levitan and OCC seriously and cooperatively.

OCC believes that UI fulfilled its obligations with respect to cooperation with the Department's consultant and the OCC.

4. The Company responded to questions, requests and suggestions from potential bidders in a serious and diligent manner. The RFP web page clearly explained how potential bidders could pose questions to UI. Each question was forwarded to Levitan and OCC, as were draft responses prior to posting of the responses. The Company considered, and often incorporated, suggested improvements in responses proposed by Levitan and OCC. The Company continued to respond to questions after the formal deadline for questions. The Company solicited comments from potential bidders regarding the draft contract; with input from Levitan and OCC, revised the standard contract to reflect many of those comments; held teleconferences with each bidder to discuss remaining contract issues; and (again with input from Levitan and OCC) made additional changes to the contracts, both generically and to reflect bidder-specific issues.

OCC believes that this process meets the Department's standards (a) and (e), above.

5. One significant development in the development of the bid documents was the amendment of the draft contract to reduce bidder risk of delay in the DPUC's review process. The concern was that a selected bidder would have to purchase hedges to protect its position for up to ten days, and that the DPUC might fail to approve the contract within that period, potentially leaving the bidder with the costs of the hedges and no actual sale of power. To reduce the bidders' risk and the anticipated resulting cost to customers, UI agreed to assume the cost of the hedges<sup>2</sup> from the time that the Department might reasonably be expected to act until the date at which the Department rejected the contracts or the ten-day approval period lapsed.

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<sup>2</sup> It is not clear whether UI would ask ratepayers to bear this cost, if incurred. However, OCC believes that the probability that UI would have to pay anything to a successful bidder is quite low.

OCC believes that UI's willingness to accept this small risk is likely to reduce costs to customers and commends UI for this decision.

6. The Company, Levitan and OCC worked well together in developing and testing the bid spreadsheets. The bid spreadsheets went through several iterations, as well as testing by UI, Levitan and OCC and a round of indicative bids by potential bidders, to ensure that
  - The bid prices would be unambiguous.
  - Any mutually-exclusive bids would be clearly specified, which required careful wording and clear bid designations.
  - The bid prices could be exported easily to the evaluation worksheets, to allow the expeditious completion of the bid evaluation and selection of suppliers, to minimize bidder risks and costs.

OCC believes that the bid forms were well-designed to support the procurement and selection process, promoting minimization of revenue requirements, while clearly showing potential suppliers the "criteria for evaluating competing bids," as required by Department standard (d).

7. The Company, Levitan and OCC generally worked well together in developing and testing the linear-programming ("LP") bid-choice models. OCC's consultant developed a conceptual model to allow UI to compare bids for single blocks of power with bids for multiple periods. Levitan constructed comprehensive models, incorporating suggested refinements from OCC and UI. UI staff devoted the time and attention necessary to understand the approach, accept the feasibility of taking a variety of bids with a variety of limits on UI's ability to take combinations of bids, and master the use of the LP models.

OCC believes that the LP modeling approach was prudently pursued by UI to promote price stability and minimization of revenue requirements, as required by Department standard (d).

8. Levitan and OCC developed estimates of the prices we would expect suppliers to bid for the various terms, reflecting forward energy prices, congestion, load shape, ISO-NE

capacity-pricing rules, historical and expected uplift costs and ancillary prices, renewable-energy requirements and prices, distribution losses and an estimate of supplier mark-up for profit and risk. These values (called “proxy prices” by Levitan, and “target prices” by OCC) allowed the parties to determine whether bids were unexpectedly low, in which case the Company might take more SS supply than planned, or unexpectedly high, in which case the Company might not take all the tranches originally planned. So far as OCC is aware, the Company was interested in the results but did not contribute significantly to the computations. Levitan did not share with OCC the derivation of its inputs (e.g., the effects of congestion and load shape on energy prices, as well as uplift and ancillary-service costs as a percent of energy costs), despite several requests. The OCC consultant developed independent estimates of these values, and Levitan modified some inputs in response to OCC comments.

Ultimately, OCC believes that the resulting proxy prices are reasonable and adequate for the purposes of this procurement—namely, to determine whether the winning bids meet the statutory requirement of just and reasonable retail rates, reflecting wholesale market prices and avoiding unusual or excessive pricing, as well as the Department’s requirement of minimizing revenue requirements.

9. The Company selected the schedule for the procurement, which compressed to 25 days the time interval from the release of the RFP (August 4) to the receipt of final bids (August 29). In contrast, CL&P (which, unlike UI, had experience with power procurement over the last three years, including recent revision of its standard contract) provided 41 days for this process, from August 2 to September 12. The schedule UI chose limited the period for responding to bidder questions, revision of contracts, development of the bid worksheet, proxy prices, and the bid-selection models, requiring extensive last-minute efforts to meet tight deadlines. While it appears that these efforts have been successful, the opportunities for checking and feedback have been limited.
10. The test run of the bid-selection models using mock bids was helpful in improving the models and communication with bidders. The review of the indicative bids was similarly helpful in identifying potential problems in bid interpretation.

OCC believes that UI and Levitan used the mock-bid and indicative-bid processes well, to support compliance with the Department's standard (d), above.

11. On bid day, UI provided separate rooms for Levitan and OCC teams, in addition to UI's evaluation team, with internet access. The Company received the raw bids and copied them to the on-site Levitan and OCC teams, while redacting them for use off-site.

OCC believes that UI and Levitan were well prepared for bid day.

#### **OCC's Evaluation of the UI Effort**

Summarizing the above, OCC believes that UI's conduct of its Standard Service and Last Resort Service procurement was **satisfactory**. Just below, OCC explains the basis for its conclusion on UI's procurement conduct.

The DPUC's Initial Decision (p. 7) says that OCC should comment on "any prudence issues" arising during the procurement process. OCC did not observe any UI actions that, on their face, raise important prudence issues or appear to have directly resulted in excess costs to customers.

However, OCC is concerned that **UI did not establish any independent proxy price estimates** for use in evaluating the SS and LRS bids received. This concern is explained below.

OCC's Further Comments in this docket (4/3/06, at pp.11-12, 25-26) advocated the regular use in SS/LRS procurement of something we called "a range of target prices." We assumed that this target range would be developed by all procurement participants on a

careful and comprehensive basis.<sup>3</sup> This construct would serve several important purposes. Most vitally, the target range would enable procurement participants to evaluate whether the final bids in hand at the close of each RFP are demonstrably high or low, relative to actual market conditions. This evaluation would help inform the decision, which should be an integral part of every RFP for Standard Service<sup>4</sup>, on whether the bids in hand should be accepted at the scheduled acquisition quantities, or above or below those scheduled quantities instead. In simplest terms, the use of a proper target price range can lead a utility to buy, on a sound basis, more or less than was planned, or can confirm the initial intent to buy just the planned amount.

OCC believes that careful use of a comprehensively developed target price range is an essential component of each RFP for SS/LRS. This evaluation tool helps assure that these procurements meet the statutory standards for SS (e.g., just and reasonable retail rates, avoidance of unusual or excessive pricing). This tool also helps the distribution companies achieve maximum benefits from the SS requirement that they develop a portfolio of laddered contracts over time.

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<sup>3</sup> Also, the target range would be developed confidentially, to prevent bidders from gaming the system.

<sup>4</sup> And for Last Resort Service as well, for that matter.

Target prices are proxy prices by another name.<sup>5</sup> However labeled, such prices are a vital evaluation tool for electric power procurement. Each independent estimate of the target price and of the multiple inputs to the computation helps to test and improve the other estimates. In other words, UI could have helped both Levitan and OCC by preparing its own proxy/target estimate.

During the current procurement efforts, Levitan set out to develop a proxy price for each distribution company. After some delays, Levitan provided enough detail on its proxy analysis so that OCC consultants were able to propose corrections and improvements, based on their own analyses.

Of the two active buy-side participants in the present procurement process, only UI did not develop any estimates of its own of proxy prices or inputs. When OCC asked about this omission, UI management simply stated that it was unable to do such a thing, since the company is no longer active in the wholesale markets on a regular basis. It is true that UI has not had much need to buy or sell in the wholesale markets since its procurement in late 2003 of Transitional Standard Offer power for 2004–2006, and even since its procurement in 1999 of Standard Offer power for 2000–2003.

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<sup>5</sup> Except that OCC believes it is more reasonable for procurement participants to develop a range of such prices, reflecting (a) the bid price below which UI should seriously consider buying more power than planned, as well as (b) the price above which UI should seriously consider not buying as much power as planned, even if that meant (in the present time-constrained context) adding a later procurement to acquire power for the first half of 2007.

However, UI is familiar with, and is not indifferent to, the rules and operations of the ISO markets. In addition, Connecticut law requires UI to provide Standard Service and Last Resort Service, on a regular basis and for the indefinite future. Few if any UI customers are likely to be served by competitive suppliers, even though seeking such supply remains a customer right. Thus, both Standard Service and Last Resort Service will continue to be of critical importance to UI customers.

Under these circumstances, UI's development of its own target or proxy prices would have importantly assisted in the evaluation of the current RFP. For future RFP's, the Company could either acquire the internal staff capacity for this purpose, or obtain relevant expertise from independent contractors. For the future, UI should take this step as each SS procurement RFP is planned and executed.

**B. The Prices UI Obtained Appear to Reflect Current Market Conditions**

Within the limits of our available resources, OCC undertook to independently assess the results of UI's current SS/LRS procurement effort.

Confidential Appendix A describes in detail OCC's assessment of bidder interest and participation in the procurement process. OCC believes that the level of bidder activity was adequate to support DPUC approval of the recommended contracts.

Confidential Appendix B describes OCC's analysis of expected prices for UI's standard-service supply. OCC used this analysis to evaluate the final bids that UI received.

Based on our use of these analytic tools, OCC concluded that the prices UI obtained for both Standard Service and Last Resort Service, for the tranches the company accepted on August 29, 2006, reflect current wholesale market conditions.

**C. The DPUC Should Accept the Joint UI/Levitan Recommendations**

At the close of price day, August 29, 2006, OCC was able to review and evaluate the Joint UI/Levitan Report being filed contemporaneously with these OCC Comments. That report consists of three documents, each with attachments, as follows:

- Joint Recommendation of The United Illuminating Company and Levitan and Associates Inc., a document approximately 7 pages long, exclusive of attachments.
- Joint Affidavit of Ellen G. Cool and Richard L. Levitan, Levitan and Associates. Inc., a document approximately 9 pages long, exclusive of attachments.
- Affidavit of Michael A. Coretto, a document approximately 6 page long, exclusive of attachments.

OCC also has specifically reviewed the attachments to each of the aforementioned documents (some of which UI is filing as confidential).

The Initial Decision (on pp. 8-9) sets out the requirements for the Levitan-UI joint report. Those items are:

- (a) overview of all bids, plus a joint recommendation as to the preferred bidders;
- (b) projected system average rates resulting from the procurement;
- (c) redacted bids, with a motion for protected treatment;
- (d) natural gas and electric futures prices on the date of the procurement;
- (e) attestations from distribution company/Levitan that the procurement met the “basic criteria” set out in the Decision.
- (f) “conclusions and supporting reasoning” in any situations where discretion was exercised.

(g) the overview mentioned above should be filed as a “compilation”, with appropriate measures to keep it out of FOIA's reach, and should not include the names of the preferred bidders.

OCC believes that Levitan and UI have complied adequately with these requirements of the Initial Decision.

Given the analysis presented in Sections II-A and II-B of these Comments, supra, OCC states the following. We believe that **the DPUC should accept the Levitan-UI recommendations, in full, as filed.**

**D. Time Delays Made this SS/LRS Procurement Effort More Difficult Than Necessary**

Certain important dates relating to SS and LRS procurement have been known ever since June 26, 2003 (when the Revised Restructuring Act was signed into law). Specifically, both SS and LRS would take effect beginning January 1, 2007, and the DPUC had to establish the initial SS price no later than October 1, 2006. Further, of course, neither CL&P nor UI could begin the SS/LRS procurement process for 2007 and beyond until the DPUC had approved their plans to do so.

**The DPUC's Timing**

The DPUC initiated the docket to approve the distribution companies' SS/LRS procurement plans in an order dated January 25, 2006. Manifestly, the DPUC could have initiated this docket many weeks or months prior to that time.

The DPUC completed that docket on June 21, 2006. This was considerably later than the distribution companies had requested.

For instance, CL&P asked the Department to issue its pertinent decision by the end of March 2006. See CL&P Proposal, 2/22/06, pp. 2-3. CL&P's stated rationale for this recommendation was that it would enable the company (a) to issue more than one RFP prior to the 10/1/06 deadline, and (b) to avoid testing the wholesale markets during hurricane season.

UI observed, more mildly, that the multiple RFPs (before 10/1/06) contemplated by the Department's 1/25/06 procedural order might be impossible. See UI Proposed Plan, 2/22/06, p. 3. UI observed, for instance that its prior transitional standard offer ("TSO") procurement had taken 95 days from the development of the company's term sheet to the DPUC's final decision.

During the first phase of this proceeding, OCC did not request any particular docket timing of the Department.<sup>6</sup> However, we shared the general concern that time was (and is) of the essence in this matter. Further, now that OCC has participated closely in the initial SS/LRS procurement effort, as conducted by both CL&P and UI, we have the following observation to offer.

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<sup>6</sup> OCC did observe that, given the timing which actually was unfolding in the docket, it was likely that only one RFP would be possible prior to 10/1/06. See OCC's Further Comments, 4/3/06, p. 8; OCC's Brief, 4/26/06, p. 9.

### **Implications of Time Delay**

The delay in issuing the Initial SS/LRS Procurement Decision made this SS/LRS procurement effort more difficult than it had to be, for both distribution companies.

During recent weeks (i.e., since 6/21/06), substantial employee teams at both CL&P and UI have worked on the current SS/LR procurement on an intense and continuous basis, with a diligent and conscientious focus on the many tasks at hand. Both company teams have been acutely aware of the numerous steps necessary to any such procurement effort, and of the need to complete all such steps within a time frame that has been severely (and unnecessarily) compressed.<sup>7</sup>

It appears to OCC that these limits on the time available to complete the initial SS/LRS procurements have had at least two deleterious effects on the process. One such effect relates to the possibility of multiple RFPs, and the other relates to distribution company use of the so-called barrier put option. Each of these is discussed below.

### **Multiple RFPs**

Clearly, it is highly desirable for both UI and CL&P to be able to issue multiple RFPs to obtain SS/LRS power for given periods of time, for at least two reasons. First, the applicable statute specifically favors this option. That statute empowers the DPUC to reject

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<sup>7</sup> For instance, if the DPUC had followed CL&P's suggestion, and issued its final decision in the docket at the end of March, the time available for the first round(s) of SS/LRS procurement would almost have doubled --- from three months (that is, July through September) to six months (that is, April through September).

the results of given RFP efforts, and it also requires the development of “laddering” among SS contracts (that is, securing contracts at different times, so that the utility achieves a price result resembling dollar-cost-averaging). Second, sound economic thinking supports this option. When seeking a necessity (e.g., electrical energy for a service the utility is required to provide), the flexibility of being able to go into the relevant market at more than one time is a substantial tool for moderation of possible price shocks.

The delay in the issuance of the Initial Decision in this docket substantially eliminated the possibility that either CL&P or UI could issue multiple RFPs in the present context. On the one hand, the companies would have to act in time to present auction results that allowed the Department to meet the 10/1/06 statutory deadline. On the other hand, multiple RFPs test the market more effectively when they are meaningfully separated in time. As of 6/21/06, there was insufficient time remaining for the distribution companies to meet both criteria.

### **The Barrier Put Option**

The barrier put option is a financial instrument that potentially could lower the cost to customers of SS/LRS energy. Levitan suggested this concept to both CL&P and UI very early in the working sessions associated with these initial SS/LRS auctions. The specific variety of barrier put option under discussion within the working groups is described specifically in the letter that CL&P and UI jointly filed with the DPUC on August 11, 2006. As that letter suggested, use of such an option could enable customers to share in the benefits of downward

movements (if any) in major components of wholesale energy prices during the last three or four months of 2006.

So far as OCC can tell, the barrier put option was a new idea to both CL&P and UI when Levitan first brought it up. It took some time for Levitan to explain this concept sufficiently that procurement participants developed the comfort to pursue it further. Also, it took further time for Levitan to provide the supporting information necessary to include this new concept in the current RFPs (e.g., financial calculations, term sheet language, contract language). At this writing, these latter requested inputs from Levitan remain incomplete.

The barrier put option, if available and if working as designed, could be a valuable tool, serving as a partial substitute for the contract laddering that Connecticut law so strongly favors for procurement of Standard Service. So far as OCC is aware, this particular financial device has not yet been used in regulated energy procurements comparable to the SS/LRS procurement effort now beginning in Connecticut. OCC expects that recommendations will be forthcoming on distribution company use of the barrier option in the SS/LRS context. More generally, the DPUC should see that all possible tools, for hedging and otherwise, are explored and vetted for current and forthcoming SS/LRS procurement efforts.

### **Other Unnecessary Difficulties**

In addition to time delays, the Initial SS/LRS Procurement Decision also was unduly complex in a number of its particulars, and this led to further problems in the procurement process. Three specific points can be mentioned in this context.

**Time-of-Use (“TOU”) Rates.** The Initial Decision (pp. 15-16) requires CL&P and UI to incorporate a distinction between on-peak and off-peak time periods into SS procurement. The apparent reason for this was to facilitate future implementation of the optional TOU rates referenced in § 13 of the Energy Independence Act. However, the Initial Decision (p. 15) also warned that the Department conceivably would modify the current on-peak/off-peak definitions for SS purposes.

This warning was completely irrelevant to the current SS solicitation, for two reasons. First, such an unknown future event could not possibly be incorporated into RFP efforts that necessarily had to “go live” into the market within a very few weeks of the DPUC’s issuance of the Initial Decision.<sup>8</sup> Second, the DPUC in any case had long since missed several EIA, § 13 deadlines.<sup>9</sup>

**Bids by Rate Class.** The Initial Decision (at pp. 15-16) required CL&P and UI to solicit SS bids reflecting “the cost to serve” four separate categories of potential SS

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<sup>8</sup> In the event, CL&P issued its current RFP on 8/2/06, and UI did so on 8/4/06. Neither of the Department’s “EIA, §13” decisions has been issued in final form at this writing.

<sup>9</sup> Most notably, the § 13(g) requirement to issue appropriate final decisions by 1/1/06.

customers. This requirement was somewhat oddly framed, since it was not clear whether the companies were required to accept any bids of this type (that is, whether the companies also could solicit bids for SS service not differentiated by rate class). This requirement so troubled CL&P that the company promptly (7/6/06) asked the DPUC to reconsider it. In any case, this part of the Decision, which was not required by the statute, introduced an unnecessary complexity into the current time-pressured RFP solicitations. OCC is not necessarily opposed to these class-specific prices. However, the DPUC should have been clearer about its intentions regarding this subject.

**LRS Deadline.** The Initial Decision (p. 17) requires CL&P and UI to obtain their initial LRS power by October 1, 2006. However, this deadline is not found in the statute (as is true for SS). This requirement may well have injected extra pressure into a procurement process that participants already experienced as a “pressure-cooker”. OCC had recommended an initial LRS deadline of December 1, 2006<sup>10</sup>; use of such a deadline could have allowed for a more reasonable RFP process in this round.

Curiously, the Initial Decision (p. 17) says that, going forward, LRS prices must be posted by May 1 and October 1. This is two months in advance of the indicated LRS service period in one case, and three months in advance in the other. OCC recommends that the DPUC set these deadlines at November 1 and May 1 (i.e., two months in advance for both LRS service periods).

**III. CONCLUSION**

OCC respectfully urges the Department to take full account of our agency's views as expressed above, and looks forward to further participation in this important proceeding.

Respectfully submitted,

MARY J. HEALEY  
CONSUMER COUNSEL

By: \_\_\_\_\_  
Bruce C. Johnson  
Principal Attorney

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<sup>10</sup> See OCC Brief, 4/26/06, p.10.

**CERTIFICATION**

I hereby certify that a copy of the foregoing has been mailed and/or hand-delivered to all known parties and intervenors of record this 30<sup>th</sup> of August 2006.

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Bruce C. Johnson  
Commissioner of the Superior Court