



Agenda Date: 11/20/02
Agenda Item: 2E

STATE OF NEW JERSEY
Board of Public Utilities
Two Gateway Center
Newark, NJ 07102
www.bpu.state.nj.us

ENERGY

I/M/O THE PROVISION OF BASIC)
GENERATION SERVICE PURSUANT) DECISION AND ORDER
TO THE ELECTRIC DISCOUNT AND)
ENERGY COMPETITION ACT,) DOCKET NO. EX01110754
N.J.S.A. 48:3-49 ET SEQ.)

(SERVICE LIST ATTACHED)

BY THE BOARD:

PROCEDURAL HISTORY

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 New Jersey Board of Public Utilities ("Board") finds it to be no longer necessary and in the public interest, electric public utilities shall provide basic generation service ("BGS"). N.J.S.A. 48:3-57(a).

After an extensive proceeding, the Board, by Order dated December 11, 2001, determined that for Year 4 of the Transition Period (August 1, 2002-July 31, 2003), the electric utilities should continue to provide basic generation service ("BGS"), with the procurement of supply to meet the full electricity requirements of BGS customers to be achieved via an auction process.

By Order dated June 6, 2002, the Board ordered the electric utilities and other interested parties to file formal proposals by July 1, 2002, on how BGS should be procured for the post-Transition Period. The Board also adopted a procedural schedule, which would enable a Board decision on this issue in the fourth quarter of 2002. Among other things, the procedural schedule provided for discovery, public hearings, and the filing of comments and reply comments by all interested parties.

On July 1, 2002, the Board received numerous proposals on how to proceed with the BGS procurement process for the post-Transition Period, from interested parties. A joint proposal and company specific addenda was received from the electric distribution companies (“EDCs”), including Public Service Electric & Gas Co. (“PSE&G”), Jersey Central Power & Light Co. (“JCP&L”), Conectiv Power Delivery (“Conectiv”), and Rockland Electric Co. (“Rockland”) (“Joint EDC Proposal”). In addition, proposals were filed by the Division of the Ratepayer Advocate (“RPA”), Mid-Atlantic Power Supply Assoc. (“MAPSA”), Williams Energy Marketing & Trading Co. (“Williams”), Consolidated Edison Solutions, Inc. (“CESI”) and Consolidated Edison Energy, Inc. (“CEEI”), Constellation NewEnergy, Inc., formerly AES NewEnergy, Inc. (“Constellation”), Pepco Energy Services, Inc. (“Pepco”), New Jersey Large Energy Users Coalition (“NJLEUC”), Independent Energy Producers of New Jersey (“IEPNJ”), Reliant Resources, Inc (“Reliant”), Select Energy, Inc. (“Select”), Duke Energy Trading and Marketing, LLC (“Duke”), and the New Jersey Food Council (“NJFC”).

The joint proposal from the EDCs included the BGS Supplier Master Agreement (“BGS Agreement”) used in last year’s auction. However, in response to comments made by participants in last year’s auction process, the EDCs indicated that a new draft agreement addressing some of the participants’ concerns would be forthcoming.

On September 12, 2002, the EDCs posted the new draft BGS Agreement on the auction website, for review and comment by all parties. On September 16, 2002, the EDCs posted a revised draft that reflected initial changes requested by certain suppliers. Comments on the draft BGS Agreement were filed on or about October 2, 2002. The EDCs responded to the comments on October 25, 2002 and supplied a further revised draft of the BGS Agreement on October 29, 2002. The new draft incorporated some of the participants’ comments, but did not address all of them. Because the remaining concerns were of a serious enough nature to possibly deter some potential bidders from participating in the auction, Staff proposed a meeting of all parties to attempt to reach a settlement on the outstanding issues.

At its November 6, 2002, public agenda meeting, the Board approved the EDCs’ BGS procurement proposal and EDC-specific addenda, with certain modifications. However, the Board deferred consideration of the BGS Agreement to its November 20, 2002 regularly scheduled public agenda meeting, in order to allow Staff to convene a settlement meeting on November 8, 2002.

On November 7, 2002, the EDCs posted, on the BGS auction website, a revised policy on the requirements for guaranty forms submitted by potential bidders. The proposed revision allows potential bidders to request an alternative form of financial guarantee, and specifically states the minimum requirements that must be considered.

On November 8, 2002, a settlement meeting was held. Participants included BPU Staff, the Ratepayer Advocate, PSE&G, JCP&L, Conectiv, Rockland, Reliant, Constellation, Conectiv Energy, Goldman Sachs/J. Aron & Co. (“J. Aron”), PSEG Service Corp., Sempra Energy Trading, Consolidated Edison Energy, IEPNJ, Select Energy, Morgan

Stanley Capital Group, Inc. (“Morgan Stanley”), PSEG Energy Resources, Duke, Coral Energy, National Economics Research Assoc. (“NERA”), Amerada Hess, Geophonics, and Element Re Capital Products, Inc. (“Element Re”). Many issues were resolved and were incorporated into the latest draft BGS Agreement, which was released to all interested parties via the Board’s electronic list-server on November 13, 2002. However, as not all of the issues were resolved, a comment period was proposed for major issues still in dispute, including reciprocal utility creditworthiness standards, with initial comments due November 13, 2002, and reply comments due November 15, 2002.

COMMENTS AND REPLY COMMENTS

On November 13, 2002, initial comments were received from the following companies: Element Re, Morgan Stanley, Consolidated Edison Energy, Inc., J. Aron, Reliant, Duke, and Constellation. NRG Energy, Inc. (“NRG”) also filed initial comments, which were distributed to the parties on November 19, 2002. NRG asserts that it attempted to file initial comments on November 13, 2002, via the Board’s electronic list server, but due to a problem with the list server it was not successful. NRG contacted Board Staff on November 19, 2002, to explain what happened and to resubmit its filing. Staff successfully distributed NRG’s filing to all parties at that time, via the list server. The EDCs filed reply comments on November 15, 2002.

Although a number of issues were raised in the comments, the issue of overwhelming importance to the majority of parties who submitted comments was the issue of reciprocal creditworthiness assurances. The BGS Agreement contains a number of clauses pertaining to the creditworthiness of the BGS suppliers, and the suppliers, in turn, have requested reciprocal assurances from the EDCs. The issue is not a frivolous one, as over the past few years there has been a great deal of turmoil in the energy industry, with several utilities in other jurisdictions filing for bankruptcy. The BGS suppliers would like to see assurances, in the form of letters of credits or cash, that in the event of defaults or EDC credit impairment, the BGS suppliers would still be paid. The EDCs have been reluctant to provide these types of assurances, since these would be costly and would, in turn, be reflected in the BGS price. On the other hand, without such assurances, the additional risk could be reflected in the BGS bid price, or might result in a number of bidders choosing not to participate in the auction. At the November 8 meeting, Staff proposed a process to commence in the event of an EDC credit impairment, which would result in a Board decision to assure payments to BGS suppliers.

The parties addressed the creditworthiness issue in their initial comments. The proposed remedies in the event of default or an impairment of the EDCs’ credit included: letters of credit, standby letters of credit, cash, or a Board process that would provide assurances to BGS suppliers that they would continue to be paid.

DISCUSSION AND FINDINGS

Upon review of the comments provide by the parties, it is clear that the issue of reciprocal creditworthiness standards is of concern to a number of potential bidders. Accordingly, the Board will address this concern herein. It should be noted that there are other issues, of a more minor nature, which will not be addressed at this time, but will be reviewed again before the next auction. On the creditworthiness issue, the Board believes that the best and most cost-effective approach at this time is to develop a clear Board process for dealing with a utility default or credit impairment as it affects the BGS suppliers. By announcing the process to be followed before any such occurrence happens, the Board will be providing certain assurances to potential BGS suppliers, which, in turn, should assist in providing for maximum supplier participation in the BGS auction.

The process that will be followed is described below:

If one of the nationally recognized statistical rating organizations (Fitch, S&P, or Moody's) issues a report indicating a prospect of downgrading a rating of an EDC or its parent holding company below investment grade, the EDC shall, within 3 business days, file with the Board a plan to mitigate or remove the threat of such downgrade. Included therein should be an assessment of its present and future sources of liquidity necessary to assure continued payments for the BGS supply for its customers. The Board, within 10 days after such filing, shall hold a public hearing to review the plan and consider the available options, including assurances to the BGS suppliers of the affected EDC that their payments will continue. The affected suppliers may present their recommendations to the Board at this time by filing their positions no later than 3 business days prior to such hearing.

No later than 30 days after the public issuance of the negative report of the rating agency, the Board shall issue an Order, which shall include assurances, in such form as shall be determined by the Board, to the suppliers of BGS to the affected EDC that their payments will continue in a prompt and timely manner.

The Board hereby FINDS that the above-described process is fair and reasonable and should be adopted. The Board DIRECTS the EDCs to reference this process in the BGS Supplier Master Agreement.

The Board ACCEPTS the EDCs' proposed form of financial guaranty from the BGS bidders or any such guaranties approved through the revised policy on alternative forms of guaranty announced by the EDCs on November 7, 2002.

The Board HEREBY APPROVES the EDCs' BGS Supplier Master Agreement released on November 13, 2002, with the aforementioned changes. A final copy of the BGS Supplier Master Agreement with these changes shall be filed with the Board and posted on the BGS Auction website no later than three business days from the date of this Order

DATED: 12/04/02

BOARD OF PUBLIC UTILITIES
BY:

(SIGNED)

JEANNE M. FOX
PRESIDENT

(SIGNED)

FREDERICK F. BUTLER
COMMISSIONER

(SIGNED)

CAROL J. MURPHY
COMMISSIONER

(SIGNED)

CONNIE O. HUGHES
COMMISSIONER

(SIGNED)

JACK ALTER
COMMISSIONER

ATTEST:

(SIGNED)
KRISTI IZZO
SECRETARY