



USAID
FROM THE AMERICAN PEOPLE

Regulatory and Energy Assistance

SOLR/Default Supplier Market Contracts Regulatory Issues

November 2010

John Gulliver/Deborah Shaw
REAP/Pierce Atwood LLP

This presentation is made possible by support from the American People sponsored by the United States Agency for International Development (USAID). The contents are the sole responsibility of the author/s and do not necessarily reflect the views of USAID or the United States Government.

Bosnia and Herzegovina (BiH) Regulatory and Energy Assistance Project (REAP)
USAID Contract No. EPP-I-00-03-00004-00, Task Order 5
Implemented by Advanced Engineering Associates International, Inc. as USAID Contractor



FERC and RSERC

- Regulatory Commission has jurisdiction “to supervise and regulate relations between generation, distribution, and buyers of electric power, including electric power traders” (Fed. Law § 14; RS Law § 23)
- Regulatory Commission has authority to, *inter alia*,
 - “regulate the electric power system in such a manner as to ensure transparent and fair relations between all participants” (Fed. Law § 15)
 - “ensure fairness in the supplying of electric power” (RS Law § 24)

SERC

- Jurisdiction over, *inter alia*, transmission access, monitoring and enforcing conditions for international trade, consumer protection to ensure fair and non-discriminatory treatment, ISO market rules, creation and maintenance of competitive markets “when practicable” and resolution of disputes among system users
- Cooperation with competent State and Entity authorities with respect to scope of law

(Law on Transmission § 4.2)



SOLR definitions

- **FERC**

- “Supplier of Last Resort shall mean a supplier that takes over the responsibility of electricity supply for eligible customer, under the conditions prescribed within this rule, in the case when supplier with which eligible customer has signed the contract terminates its operation”

- **RSERC**

- "Supplier of Last Resort shall mean the supplier that is appointed to assume responsibility for electricity supply of the eligible customer, under the terms and conditions prescribed by this Rule Book, when the supplier of eligible customers that the eligible customer has the contract on supply concluded with, stops supplying the electricity”



Observations about these definitions

- Both definitions assume a customer *had a supplier already in place*, and lost it
- Neither definition covers customers who can not find a supplier
- Definition of DS not included
- Each reserves opportunity to further define in post-transitional period



Customer choice of supplier

- **FERC** (§ 8)
 - An eligible customer has the right of free purchase of electricity on its own choice.
- **RSERC** (§ 14)
 - The eligible customer may freely choose the supplier of eligible customers and contract with him the quantity and price of electricity per capacity, quantity of electricity and time of consumption, ...



Customer choice of supplier

- This language is not mandatory – customer not forced to choose
- Thus, rules need to address customers who do not choose and provide for DS
- Consider whether medium and large customers should be provided with SOLR protection post-transition
 - Effect on market development of allowing SOLR for large customers



Options

- Croatia law re DS:

“An eligible customer from the household category or a small customer who does not wish to exercise his right to become an eligible customer, or is not able to find a supplier, shall contract electricity supply with the company performing the public service obligation, pursuant to the tariff system for electricity supply which does not include eligible customers.”



Switching restrictions

- Rules impose annual deadlines by which Eligible Customers must choose supplier
 - **FERC** (§ 10) – Rule cover all periods, including transition period
 - **RSERC** (§ 11) – Rule cover transition period only; does not address post-transition
- In each rule, failure to select supplier by deadline means customer continues at regulated tariff prices for the next year; this may impede market development and opening
- Restrictions tied to power balance deadlines; power balance is really just a forecast
 - Can recalculate forecast (power balance) more frequently, e.g., once a month
 - Decouple power balance calculations from market opening considerations



ERGEG Guidelines on switching suppliers

- Create conditions for customers to make informed choices
- Customers should not be charged a fee for switching between competitive suppliers
- Customers should have confidence in market, market participants and switching process
- Comparable price information is essential
- Billing must be accurate
- Customers should only need to contact one party
- Switching process should be quick
- ERGEG Guidelines do not address switching to DS



Switching between competitive suppliers in BiH

- **FERC (§13)**

- *Cannot restrict eligible customers from changing to another supplier and cannot impose special fee for changing*

- **RSERC (§15)**

- *“The contract on access to the network, contract on connection or any other contract with the Balance Responsible Party cannot contain any provisions which anyhow limits the eligible customer to choose the supplier or imposes him a special fee in case of the supplier switching.” T&D operators also cannot obtain fees for switching customers.*
 - May need to clarify supply contract also cannot impose fee



Switching between competitive suppliers in BiH

- ERGEG silent on fee or penalty for this kind of switching
- Some countries impose a fee between competitive suppliers and DS to avoid “gaming” and increasing costs to DS customers
- Switching could also be a breach of supply contract
- FERC and RSERC rules silent on fees for switching to DS
- Role of regulator to develop and enforce switching conditions is essential – fee or no fee



Selection of SOLR

- Current rules designate the incumbent supplier in the relevant geographic area as the SOLR
 - **FERC** (§ 15) – “supplier to tariff customers”
 - **RSERC** (§§ 20 & 21) – “supplier with public service obligation”
- No default supplier defined (but reservation to define in future)
- Possibility of tender process



Considerations for regulator on ex ante v. ex post SOLR tariffs

- Most tariffs are set in advance to give certainty and price signals to customers
- SOLR tariffs can be established ex ante, in whole or in part
- Even if SOLR tariff is ex ante, regulator may also need to review tariff component for supply ex post
- By definition, SOLR is less predictable than other categories of regulated service
 - Retrospective review reduces risk
- But
 - Time intensive
 - Accounting intensive
 - Customers may have to pay retroactively



Defining when there is a competitive supplier risk of default in the market not as easy as it sounds

- Different factors surround possible default or market exit events – bankruptcy, force majeure, planned termination, license issue
- Eligible Customer rules do not address these specific contingencies



Bankruptcy – Must determine criteria of when supplier is bankrupt for purpose of triggering SOLR

- Local law may define bankruptcy
- Supplier has defaulted or is it about to default on its payments
- Supplier has filed for bankruptcy protection
- Too early announcement of bankruptcy by operator or some party other than supplier, court or regulator, may cause mass switching and create chaos in the sector
- Customer choice still requires basic need to protect customers
- Check other current legislation carefully before developing new regulation on SOLR



Force Majeure – Unexpected interruption of supply beyond control of competitive supplier

- Can be very short duration – minutes or hours
 - Competitive supplier may have its own back-up supply)
 - Ancillary services can cover
- This type of limited outage may not require SOLR
- Longer duration – days, weeks or months – will require SOLR
- Determining difference between non-SOLR minor interruption and major force majeure event is difficult
- Must be done by regulator
- Must be done so customers, ISO, ancillary services and SOLR providers know when and how to act



Planned exit and license issues

- Competitive suppliers may choose to leave market upon conclusion of contracts
 - Supplier normally facilitates transfer to new supplier
 - But if no new supplier, SOLR steps in
- License revocation or suspension by regulator
 - Can trigger need for SOLR



SOLR must keep separate accounts from its normal supply business

- Critical for tariff evaluation
- Regulator should set guidelines for account separation, and review accounting structure/plan



Regulator may impose regulatory reporting requirements on SOLR

- See, *e.g.*, Romania, where regulator requires status report that is made public on customer participation in SOLR services, including:
 - Number of customers that switched
 - Average length of time with SOLR service before customers return to market
 - Number of customers disconnected by DSO for nonpayment of SOLR



Scenarios to consider

- Regulators likely will confront interruptions in supply that can cause need for SOLR
- We have developed some common examples of these events
- Purpose is to discuss collectively how the regulatory system would function
- There are few absolute right and wrong answers
- The goal is to help regulators prepare for the transition and post-transition periods



Bankruptcy

- Supplier to most industrial customers, about half of the commercial customers, and over half of the residential customers, has gone bankrupt. Supplier and bankruptcy proceedings are in another country.
- Supplier can no longer buy electricity, buy fuel, pay its transmission charges, or deliver power to the delivery points as promised per the contracts.
- It will take several days, if not weeks or months, to devise even a preliminary bankruptcy reorganization plan and reinstitute power deliveries, if at all.



What happens?

- How do people get power?
 - Who supplies electricity?
 - Who reads the meters?
 - Who pays whom?
 - What rates do they pay?





Force Majeure

- Due to severe storm activity, one of the two main transmission lines on which major supplier relies is inoperable and will remain so for at least 6-12 months.
- Supplier cannot contract for alternate transmission capacity and thus can supply only 30% to 40% of its contracted load, which is equally divided between industrial and household customers.



What happens?

- Which customers remain supplied (unsupplied customers pay SOLR price)?
- Need to allocate supply to critical customers who lost supply?
- Will SOLR agreement cover partial default by a competitive supplier?
- Are billing and accounting systems able to deal with partial defaults with accuracy?



Household customers don't choose

- January 1, 2015 arrives. By January 2, less than 20% of the residential customers have actually migrated to competitive supplier. Under applicable regulations, all household customers are supposed to have separately contracted for their electricity supply.



What happens?



Large customer switch

- A large industrial customer has long term contract for supply of power to its manufacturing facility. Over the last few years, the price of electricity from other suppliers has consistently gone down, and the contract rate currently is well above market rate.
- This customer, who employs 1500 people, has told the government and the regulator that if it cannot switch to the DS and terminate its current supply contract, it will either go bankrupt or have to shut down its facilities in BiH and move the jobs out of the country. It is willing to risk lawsuits with its current supplier to find a lower cost alternative.

What happens?



Other tasks regulators need to accomplish for market opening

- In addition to SOLR and DS, regulators must review and amend:
 - Tariffs methodologies
 - Licensing rules
 - Pro Forma Contracts for market participants, including
 - Ancillary services
 - Balancing process
 - Financial settlement
- Key role is for regulators to lead process with market participants to build consensus on these diverse issues



Specifically, the regulators should:

- Revise tariffs and licenses to conform with new market processes
- Supervise revision and adaptation of market rules
- Provide needed transparency
 - Forum for complaints
 - Market monitor
 - Information gathering
- Actively monitor and enforce new licenses, tariffs, rules and procedures



Examples:

- Regulators could lead development of processes for pro forma contracts through Market Working Group structure
- This approach helps facilitate harmonization
- Outcome of process could be development of either:
 - Detailed, pro forma contracts for all services
 - or**
 - Detailed rules describing essential terms, with annexed broad outline contract



- In either case, Regulators should prepare appropriate pricing structures (negotiated, bid-based, cost pass-through) for balancing, ancillary services and financial settlement
- Could hold technical conferences with interested stakeholders to receive input on key terms, or require suppliers to submit draft contracts for approval



USAID
FROM THE AMERICAN PEOPLE

Regulatory and Energy Assistance

Hvala!

John Gulliver

Deborah Shaw

Pierce Atwood LLP

One Monument Square

Portland ME USA

Tel: +1-207-791-1296

jgulliver@pierceatwood.com

dshaw@pierceatwood.com