



**A SPECIAL PERFORMANCE AUDIT
OF THE
PENNSYLVANIA PUBLIC UTILITY
COMMISSION**

ELECTRIC UTILITY DEREGULATION

JULY 2010

Bureau of Departmental Audits

July 22, 2010

The Honorable Edward G. Rendell
Governor
Commonwealth of Pennsylvania
225 Main Capitol Building
Harrisburg, PA 17120

Dear Governor Rendell:

This report contains the results of the Department of the Auditor General's special performance audit of the Pennsylvania Public Utility Commission (PUC) and the state's deregulation of the electric industry. This audit was conducted pursuant to Sections 402 and 403 of The Fiscal Code and in accordance with generally accepted government auditing standards (GAGAS). The aforementioned standards require that we plan and perform the audit in order to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Our audit found that the PUC could have done a better job to adequately educate consumers regarding electricity rate increases resulting from rate cap expiration. Specifically, between January 1, 2000, when the first electric company's rate cap expired (increasing electricity rates by 27 percent), and April 2007, after six electric companies' rate caps had expired, the PUC made minimal efforts to educate consumers regarding impending rate increases and how to mitigate increased electricity costs. In addition, during this period, the PUC did not require electric companies to provide such education. The PUC indicated that it was not concerned about consumer education during that period because these service areas encompassed only 15 percent of Pennsylvania ratepayers and the remaining rate caps would not expire until December 31, 2009 or 2010. As a result, consumers in this service area eventually suffered drastic rate increases, prompting the PUC to react to develop policies to mitigate the impact of such rate increases on consumers. We are deeply concerned by the PUC's reactive approach to this continuing imperative situation.

The PUC did draft a new policy in May of 2007 to implement a statewide education plan to be conducted by both the state and electric companies. However, it was only partially implemented due to the PUC being unsuccessful in obtaining the \$5 million in resources it originally believed it needed to conduct a sufficient statewide campaign. Consequently, the PUC had to rely on the electric companies' consumer education programs, which the PUC then stated was sufficient. Again, we disagree with the delayed response of the PUC and its overreliance on electric companies to deliver such a critical message to consumers, a message that was potentially less than adequate. In fact, a self-evaluation by PPL (whose rate caps expired on December 31, 2009) for the quarter ended September 30, 2009 showed that 57 percent of its consumers were unaware of when rate caps would expire and significant rate increases would ensue. Moreover, the PUC stated that only 20 percent of PPL customers eventually switched services when their rate cap expired. The aforementioned figures further buttress the viewpoint that the earlier the consumer is educated, the better off the consumer will be in realizing savings on electric costs, considering the PUC states that once a consumer makes a decision to change to an alternate supplier, it takes up to 8 weeks to change suppliers and obtain lower rates.

Finally, we found that after the initial expiration of rate caps, when the range of consumers' electric rates for various companies increased between 27 and 73 percent, the PUC directed the electric companies that remained under rate caps to file phase-in or pre-payment plans for consumers if the companies expected that electric generation rates would increase by more than 25 percent when rate caps expired. The PUC does not currently oversee or monitor these pre-payment programs.

We offer six recommendations that will strengthen PUC policies and controls, which will allow consumers to plan and take necessary measures to address the financial impact of forthcoming electricity rate increases. We are pleased that the PUC has expressed agreement with our recommendations pertaining to the need for it to improve its monitoring of the electric companies' programs to mitigate significant rate increases offered to consumers.

We will follow up at the appropriate time to determine whether and to what extent the PUC implemented our recommendations.

Sincerely,

JACK WAGNER
Auditor General

TABLE OF CONTENTS

	<u>Page</u>
<i>Results in Brief</i>	1
<i>Background</i>	3
<i>Audit Objectives, Scope, and Methodology</i>	7
<i>Finding No. 1 – The PUC Could Have Done a Better Job to Adequately Educate Consumers Regarding Electric Rate Increases Due to Rate Cap Expiration</i>	8
Agency Response.....	13
Auditors’ Conclusion	16
<i>Finding No. 2 – PUC Should Improve Its Monitoring of the Electric Companies’ Programs to Mitigate Significant Rate Increases Offered to Consumers</i>	20
Agency Response.....	21
Auditors’ Conclusion	22
<i>Distribution List</i>	23



*Public Utility Commission
Electric Utility Deregulation*

*Pennsylvania Department of the Auditor General
Jack Wagner, Auditor General
July 2010*

***Results in
Brief***

The Department of the Auditor General conducted a special performance audit of the Pennsylvania Public Utility Commission (PUC) and the state's deregulation of the electric industry for the period of July 1, 2002 through November 30, 2009. Our audit has resulted in two findings and six recommendations. We found the following:

- **Finding No. 1** We discuss how the PUC, upon the enactment of the Electricity Generation Customer Choice and Competition Act (Act), could have done a better job to adequately educate consumers regarding electricity rate increases. Specifically, between January 1, 2000, when the first electric company's rate cap expired (increasing electricity rates by 27 percent), and April 2007, after six electric companies' rate caps had expired, the PUC made minimal efforts to educate consumers regarding impending rate increases and how to mitigate increased electricity costs. Moreover, during this period, it also did not require electric companies to provide such education.

Additionally, PUC final policies issued in May 2007 required the PUC to implement a statewide education campaign and required electric companies to develop a consumer education plan for their service areas. The statewide campaign was to complement the electric companies' education efforts. We have concluded that the PUC has provided the consumer education that it could with the resource that it had available; however, without an adequate statewide campaign, PUC's efforts were not enough to adequately provide electric rate cap expiration and mitigation education to consumers. Furthermore, it did not adequately oversee the electric companies' consumer education plans.

For consumers whose rate caps will expire on December 31, 2010, we recommend that the PUC seek approval for funding of a regional education campaign. Furthermore, we recommend that it develop and implement a regional PUC consumer education campaign, including performing outreach at public venues such as senior centers, bingo halls, churches, legislator-sponsored events, PCN-moderated programs with PUC management, etc., and perform an ongoing evaluation of the campaign's effectiveness. Finally, subsequent to the completion of electric deregulation, we recommend that the PUC assess/monitor the financial impact of electric deregulation on Pennsylvania consumers to determine what additional assistance/education can be provided in order to minimize consumers' future electricity costs.

***Public Utility Commission
Electric Utility Deregulation***

*Pennsylvania Department of the Auditor General
Jack Wagner, Auditor General
July 2010*

Results in Brief

- **Finding No 2** We explain how our audit disclosed that the PUC should improve its monitoring of pre-payment programs, offered by electric companies for consumers, intended to mitigate the impact of significant rate increases. Specifically, after the initial expiration of rate caps, when the range of consumers' electric rates for various companies increased between 27 and 73 percent, the PUC directed the electric companies that remained under rate caps to file phase-in or pre-payment plans for consumers, if the companies expected that electric generation rates would increase by more than 25 percent when rate caps expired. The PUC does not currently oversee or monitor these programs.

The PUC has expressed agreement with our recommendations pertaining to monitoring, including that it require electric companies that are offering pre-payment programs to provide during PUC financial audits the information necessary to review the amount of advance payments collected and interest earned, as well as the amounts credited to consumers' electric bills once rate caps have expired. In addition, we recommend that it direct staff to include as part of existing financial audits a review of pre-payment programs used by electric companies to ensure that consumers' monies are being properly managed, interest is accurately calculated and credited, and consumers are receiving the benefits according to the approved plans.

*Public Utility Commission
Electric Utility Deregulation*

*Pennsylvania Department of the Auditor General
Jack Wagner, Auditor General
July 2010*

Background **The Public Utility Commission**

Utility service is a critical element to the health and safety of Pennsylvania's residential and business customers. The Public Utility Commission (PUC) was created by Act 43 of 1937 to ensure that electric, natural gas, water, and local telephone service is available upon request at a reasonable rate and provided safely with a reliable level of service. PUC is comprised of five full-time commissioners with staggered five-year terms who are nominated by the Governor and confirmed by the Pennsylvania Senate. The commissioners set policy on matters affecting utility base rates and service, as well as on personnel, budget, fiscal, and administrative matters. Additionally, the commissioners take official action on cases during regularly scheduled public meetings.

PUC regulates about 8,000 companies providing electricity; natural gas; steam heat; water; waste water collection and disposal; telephone; transportation of passengers and property by train, bus, truck, taxicab, and limousine; transmission of gas and oil by pipeline; and public highway-railroad crossings. PUC derives its funding from assessments of these companies. These assessments are deposited into a restricted account within the General Fund for use solely by PUC.

According to PUC, during the past twenty years, its focus has expanded from the traditional role of approving cost-based rates and regulating the service of all public utilities to a broader mandate of also enabling and facilitating competitive markets for the electric, natural gas, and telecommunications industries.

Public Utility Commission
Electric Utility Deregulation

Pennsylvania Department of the Auditor General
Jack Wagner, Auditor General
July 2010

Background

Electric Deregulation

The Electricity Generation Customer Choice and Competition Act (Act), effective January 1, 1997, was enacted to move Pennsylvania to retail electric competition.¹ Under this Act, all electric distribution companies, 11 in total, were required to divide their electric service into distribution, transmission, and generation services. Distribution and transmission would continue to be regulated; however, generation (electric rates) would be unregulated. Electric companies were required to provide open and non-discriminatory access to the electric rate markets. In order to ease transition to the competitive markets, the Act provided that electric rates would be capped for various periods of time at levels that existed as of January 1, 1997. When the electric rate caps expire, generation will be provided at prevailing market prices.

Electric Generation Rates

Based on information provided by PUC, the following table summarizes the electric rate cap status for Pennsylvania's 11 electric distribution companies:

Company Name	Percent of PA Ratepayers	Electric Rate Cap Status	Percent of Rate Increases After Rate Cap Expiration
Wellsboro Electric.	0.1%	Expired-January 1, 2000	27%
Duquesne Light	10.6%	Expired-December 31, 2001	-14%*
Citizens Electric	0.1%	Expired-February 1, 2002	37%
Pike County Light & Power	0.1%	Expired-December 31, 2005	73%
UGI Utilities	1.1%	Expired-December 31, 2006	33%
Pennsylvania Power	2.8%	Expired-December 31, 2006	35%
PPL Electric Utilities.	24.6%	Expired-December 31, 2009	30%
Metropolitan-Edison	9.5%	Will expire December 31, 2010	unknown
Pennsylvania Electric	10.6%	Will expire December 31, 2010	unknown
PECO Energy.	27.8%	Will expire December 31, 2010	unknown
Allegheny Power	12.7%	Will expire December 31, 2010	unknown

*-Rate decrease is due to the electric rates being high at the time rate caps were set.

¹ Act 138 of 1996, as amended; 66 Pa. C.S. § 2801 *et seq.*

***Public Utility Commission
Electric Utility Deregulation***

*Pennsylvania Department of the Auditor General
Jack Wagner, Auditor General
July 2010*

Background

Since electric rate caps are not due to expire until December 31, 2010 for Metropolitan-Edison, Pennsylvania Electric, PECO Energy, and Allegheny Power, the anticipated rate increases at expiration are currently unknown; however, based on current market prices, significant rate increases are expected for these companies, with the possible exception of PECO Energy.

Consumer Choice

As rate caps expire and anytime afterwards, Pennsylvania consumers can choose the company that generates the electricity they use. Selecting a company may be based on the rate charged, special services provided, or environmental priorities.

Rate Mitigation

PUC cannot regulate electric rates once rate caps expire; however, the significant rate increases shown in the above table emphasize the importance of other mitigation measures. As a result of PUC's May 17, 2007 Final Order, Docket Number M-00061957, the PUC was responsible for undertaking various mitigation measures, including consumer education and rate mitigation.

Regarding consumer education, PUC's Office of Communications was instructed to implement a statewide consumer education program. Additionally, all electric companies were required to develop consumer education plans for their respective service territories.

Also, with respect to rate mitigation, PUC has approved rate-mitigation plans such as phase-in or pre-payment plans after directing all utilities to file such programs if electric generation prices increase by more than 25 percent when rate caps expire. Pre-payment plans were approved for PPL Electric Utilities, Metropolitan-Edison, and Pennsylvania Electric.

***Public Utility Commission
Electric Utility Deregulation***

*Pennsylvania Department of the Auditor General
Jack Wagner, Auditor General
July 2010*

Background

Additionally, based on Act 129 of 2008, signed into law October 15, 2008, the PUC has approved consumer energy efficiency and demand response programs submitted by Pennsylvania's seven major electric utilities. These programs are to encourage energy efficiency, such as installation of high efficiency lighting and appliances, repair or replacement of heating or cooling systems, and weatherization of homes and businesses. Furthermore, PUC is reviewing the seven major electric companies' smart meter technology procurement and installation plans required to be submitted to the PUC. Smart meter technology reduces usage or shifting load from periods when demand and prices for electricity are high to periods when demand and prices are low, and can assist with reducing overall energy costs.

***Objectives,
Scope, and
Methodology***

Objectives

The objectives of this special performance audit were to determine:

- How the Public Utility Commission (PUC) plans to prepare consumers for the substantial rate increases in electric utility costs upon deregulation (See Finding One and Finding Two); and
- The adequacy of the steps PUC is taking to help mitigate potential future significant increases in electricity prices (See Finding Two).

Scope

Our audit covered PUC's duties and responsibilities with regard to electric utility deregulation for the period July 1, 2002 through November 30, 2009.

Methodology

The methodology in support of the audit objectives included:

- reviewing appropriate laws, PUC policies and procedures, related information from PUC's website, and newspaper articles;
- interviewing and corresponding with PUC's management and staff from the offices of the Director of Operations; Communications; Conservation, Economics, and Energy Planning; Consumer Services; Fixed Utility Services; and Law Bureau, to assess controls and gain an understanding of policies and procedures related to electric utility deregulation;
- reviewing documentation supporting PUC's price mitigation measures to determine the adequacy of steps PUC is taking;
- reviewing documentation of PUC's consumer education to determine how PUC is preparing consumers for the substantial electric rate increases upon deregulation and evaluate for adequacy; and
- reviewing documentation supporting PUC's monitoring of electric distribution companies' consumer education and evaluating the adequacy of PUC's oversight to ensure that consumers are being prepared for the substantial electric rate increases upon deregulation.

***Finding
One***

The PUC Could Have Done a Better Job to Adequately Educate Consumers Regarding Electric Rate Increases Due to Rate Cap Expiration

On December 3, 1996, the Governor of Pennsylvania signed into law the Electricity Generation Customer Choice and Competition Act (Act) for the purpose of deregulating electric generation rates.² In order to ease transition to the competitive markets, the Act provided that the electric rates would be capped for 11 Pennsylvania electric distribution companies (electric companies) throughout Pennsylvania for various periods of time at levels that existed as of January 1, 1997. When the electric rate caps expired, electricity would be provided at prevailing market prices. In 1996, it was expected that consumers would not face significant electric rate increases because existing competition would offset the potential for these increases. As a result, PUC did not educate consumers at that time about the effects of rate cap expiration and what could be done to mitigate its effects. However, while rate caps have been in effect, wholesale prices for electricity have risen significantly, resulting in increases to retail prices as rate caps expire.

Between January 1, 2000, when the first electric company's rate cap expired (increasing electricity rates by 27 percent), and April 2007, after six electric companies' rate caps had expired, the PUC 1) made minimal efforts to educate consumers regarding impending rate increases and how to mitigate increased electricity costs, and 2) did not require electric companies to provide such education. PUC was not concerned about consumer education during that period because these service areas encompassed only 15 percent of Pennsylvania ratepayers and the remaining rate caps, representing 85 percent from five electric companies, would not expire until December 31, 2009 or 2010. We disagree with PUC's reasoning that consumer education was not necessary during this time period because only 15 percent of ratepayers were affected by these rate cap expirations. Additionally, PUC did not expect increases in Duquesne and Penn Power service territories to be significant when their rate caps expired on December 31, 2001, and December 31, 2006, respectively. However, while Duquesne's rates did not increase, Penn Power's rates increased significantly by 35 percent, according to information provided by the PUC. Furthermore, during this time, PUC allocated its resources to other pressing topics, including low-income programs, the Pennsylvania One Call program,

² Act 138 of 1996, as amended; 66 Pa.C.S. § 2801 *et seq.*

Finding No. 1

changes in utility terminations, Be Utility Wise and heat wave conservation, and Telecommunications Relay Service. Any outreach related to electricity focused on shopping and choice.

According to information provided by PUC, in 2006, after the December 31, 2005 rate cap expiration of the Pike County Light and Power service territory, the electricity rates for that area jumped 73 percent. Based on an outpouring of concern by these consumers, in May 2006, the PUC began proceedings to develop policies to address potential electric rate increases. The final policies were issued on May 17, 2007. They required the PUC's Office of Communications to implement a statewide education campaign and required all electric companies to develop a consumer education plan for their service areas. The statewide campaign was to complement the electric companies' education efforts.

According to the May 17, 2007 policies, the statewide education campaign was to be funded by \$5 million in assessments to the electric companies. However, these assessments needed to be approved as part of the 2008-09 state budget. They were not. As a result, PUC did not have the resources to conduct a sufficient statewide education campaign.

In lieu of obtaining funding, PUC management stated that it conducted some small-scale consumer education by utilizing three PUC educators and/or officials to attend or host various events throughout Pennsylvania. We reviewed PUC's documentation regarding these events and found that, between July 2008 through October 2009, management either hosted or attended 263 events in 29 of Pennsylvania's 67 counties. PUC's educational

Finding No. 1

efforts for the majority of these events involved PUC management staffing information tables with brochures/literature explaining electric rate cap expiration. Moreover, of the 263 events, 82 (31 percent) included PUC management offering an actual presentation on electric deregulation, rate cap expiration, and rate mitigation, which it conducted in 14 counties. PUC provided the consumer education it could with the resources it had; however, without sufficient funding for a statewide education campaign, PUC's consumer education efforts were not enough to adequately provide electric rate cap expiration and mitigation education/information to consumers.

Furthermore, with regard to assessing the effectiveness of the educational efforts actually made by the PUC, management asserted that, while it intended to conduct benchmarking and evaluation surveys as part of its statewide education campaign, the lack of a funding mechanism prohibited these efforts. Therefore, the PUC has not evaluated whether the above efforts were effective in educating the consumers who attended these events.

In addition to the PUC policy to develop a statewide education campaign, the May 2007 policies/regulations required all electric companies to adopt a consumer education plan for their territories, which would educate consumers in accordance with various energy education standards, including explaining how electric rates are charged to customers, the date that caps for the customers' service territories will expire, the possible rate increases, options for selecting electric generation suppliers, and efficiency and conservation choices. According to management, because the PUC did not receive funding for a statewide consumer education campaign, it has heavily relied on consumer education offered by the electric companies.

Finding No. 1

PUC's oversight of the electric companies' consumer education plans involves reviewing the electric companies' educational materials, such as an advertisement, in order to ensure that the materials cover the education standards. The PUC does not perform independent evaluations or measure performance of the effect that the educational materials have on increasing consumers' knowledge. Additionally, the PUC instructed electric companies to perform their own self-evaluations of consumer knowledge; however, the PUC performs only a cursory review of these results. According to the PUC, the lack of funding has precluded PUC from evaluating the effectiveness of these plans, indicating that the real gauge of consumer education effectiveness is the public's reaction when the generation rate caps expire. Although public reaction after rate cap expiration would indicate whether the electric companies' consumer education plans as well as any efforts performed by the PUC were effective, this ultimate assessment does not afford the opportunity for the PUC or the electric companies to increase/change educational approaches prior to the actual rate cap expiration. In other words, if PUC performed an effective assessment prior to a rate cap expiration date and concluded that most consumers are not aware that electric rates will be rising, the PUC and/or electric companies could increase/change their educational efforts prior to the rate cap expiration date, in order to increase consumer awareness and thereby minimize the panic or public outcry that would occur.

In addition to consumer education programs, the PUC has performed outreach to media outlets to attempt to get information to consumers regarding rate cap expiration, electric rate increases, and ways to mitigate the rate increases. According to the PUC, over 130 newspaper stories appeared in state and national publications and at least one television outlet in most of the major Pennsylvania media markets covered these issues. Speciality television programs such as the "PCN Call-In" also included monthly programming for the PUC. However, information actually getting to the consumers is contingent on the various media outlets deciding whether to report the information and how to report the information. This is outside the control of the PUC. While this media outreach is beneficial to educating the consumer, it does not replace the need for an adequate consumer education program provided directly by the PUC.

Finding No. 1

Without an adequate consumer education program, Pennsylvania consumers will not be adequately informed of when generation rate caps are expiring in their service territories and that their electric rates will be significantly increasing. Additionally, they will not be aware of ways they can mitigate these rate increases and potentially lower their monthly electric bills, which will be significantly increasing. For instance, a self-evaluation performed by PPL for the quarter ended September 30, 2009 showed that 57 percent of its consumers were unaware of when rate caps would expire and significant rate increases would ensue. With PPL consumers totaling over one million, these results show that over a half million consumers may not be aware of rate cap expiration on December 31, 2009 and resulting significant rate increases. These significant rate increases may create financial hardships for many consumers, which they will not be adequately prepared to handle.

In November and December 2009, the PUC has attempted to present information to consumers about electric deregulation, electric rate cap expiration, and subsequent rate increases in the PPL service territory due to the rate cap expiration on December 31, 2009. PUC's efforts included PUC sponsored presentations; a push by PUC to make the media aware of the situation so that the media would promote awareness to the consumers; public television programs including PPL and PUC representatives; and PPL forwarding joint PUC/PPL letters to consumers. We believe that PUC's recent outreach efforts will help consumers better understand the effect of rate cap expirations. However, adequate time is necessary for consumers to receive, become aware, and process this information in order to make informed decisions regarding choices necessary to mitigate the significant rate increases. For instance, once a consumer makes a decision to switch to an alternate supplier offering lower generation rates, PUC's website states that it may take up to 8 weeks for the switch to occur and lower rates to take effect. For consumers whose rate increases will create financial hardship, not having sufficient notice to adequately plan on how to pay for these increases, may lead to a loss of their electricity and the need for financial assistance.

Finding No. 1

Recommendations: For consumers whose rate caps will expire on December 31, 2010, we recommend that PUC:

1. Seek approval for funding of a regional PUC education campaign;
2. Develop and implement a regional PUC consumer education campaign, including performing outreach at public venues including senior centers, bingo halls, churches, members of General Assembly events, PCN moderated shows with PUC management, etc. and perform an ongoing evaluation of the effectiveness of such a campaign; and
3. Evaluate the effectiveness of the electric companies' consumer education efforts.

Additionally, subsequent to the completion of electric rate cap expiration, we recommend that PUC:

4. Assess/monitor the financial impact of electric deregulation on Pennsylvania consumers to determine what additional assistance/education can be provided to consumers in order to minimize consumers' future electricity costs.

Agency Response: The Public Utility Commission agrees that more funding for education, particularly for a statewide campaign, would have been beneficial and would have complemented the significant education provided by the Commission, the Office of Consumer Advocate, electric distribution companies and electric suppliers. However, this finding overstates the incremental value of the statewide campaign proposed by the Commission in 2007 and understates the value of the actual education provided by the groups identified above. The finding also focuses on the need for education about the problem – rising electricity costs – while the Commission and its partners have focused instead on educating consumers about what they can do to help keep their bills low, such as shopping for a competitive supplier with a cheaper rate than the utility; conserving energy; and getting help paying bills. In the Commission's judgment, the overall efforts to educate consumers regarding future rate increases have been successful based on the following:

Finding No. 1

- Other than the issuance of this audit, little public or public official outcry exists that more education was needed. And, in fact, support from elected officials did not exist to fund the statewide campaign, and there may have been a public outcry if consumers were charged for an advertising campaign on top of rate increases and the existing education campaigns by electric distribution utilities.
- As of February 1, 419,846 customers statewide have switched to a competitive supplier with the highest rate of switching being 288,207 (20 percent) in the PPL service territory. Consumers are making this switch because they know they can, thanks to the education. In the PPL service territory alone, eight out of 20 licensed electric suppliers are making offers to residential customers. We understand these stats make Pennsylvania once again a leader for its implementation of electric competition.
- The Commission continues to make adjustments to its education efforts following feedback from consumers at the Farm Show, legislative events and Commissioner presentations. Some of those enhancements are explained below.
- The Commission has been educating Pennsylvanians about how to shop and about their rights as consumers, and available programs to help, since the competition law was passed in 1996, including and continuing during the rate cap expirations of Duquesne Light, Pike County Light and Power, and Penn Power. Care has been taken not to promise choices and competitive offers until we know they will exist. Warning customers about increases that may or may not occur and choices that may or may not materialize years in advance could have created false public expectations. The Commission made a conscious decision not to simply announce the problem of potentially higher rates without concrete information about what those rates will be and how consumers can find alternatives and assistance.

Finding No. 1

- The Commission did allocate substantial resources to this education: three full-time and one part-time educator, as well as media relations personnel. The Commission directed the electric utilities to spend millions of dollars in ratepayer-recovered funds to educate their customers about rate caps, shopping, conservation and low-income programs. For example, the Commission directed PPL to spend approximately \$5 million for 2009 alone on education efforts to prepare PPL consumers for the expiration of rate caps. The PECO consumer education plan, reviewed and approved by the Commission includes a total multi-year budget of \$6.5 million.
- The Commission continues to roll out new educational tools and fact sheets, including the following, which were distributed to consumers to coincide with the expiration of PPL's rate caps: "The Expiration of Rate Caps: Where to Shop"; "Electric Bill Breakdown"; and "Using Alternative Energy at Home in Pennsylvania."

Related to the recommendations included, the Commission notes the following (responses are numbered to match the recommendation):

1. The Commission already oversees regional campaigns: the electric distribution company consumer-education plans which continue for several years. These utility companies have been spending millions to educate ratepayers about rate caps and actions to cope. Also, the Act 129 marketing will occur in most electric service territories.
2. The Commission already carries out all of these types of outreach and will continue. We are particularly proud of our partnership with members of the General Assembly at their events for constituents.
3. The Commission continues to evaluate the effectiveness of the electric utilities' consumer-education efforts. In fact, staff recently concluded that electric distribution utilities need to enhance their outreach to seniors, minority and low-income populations. The Commission will be directing utilities to enhance their plans in this regard for 2010.

Finding No. 1

4. As alluded to at No. 3 above, the Commission and utility consumer-education efforts are constantly shifted to adapt. Consumer-education meetings are held with utilities regularly. The consumer-education plans filed by the utilities in December 2007 all have been adjusted and revised to take advantage of new opportunities and address new challenges. As another example, the Commission is currently developing a separate, user-friendly website to allow electric customers to input their zip code and see the electric suppliers and competitive offers available to them. This tool should be operational by the end of first-quarter 2010, before 60-some percent of Pennsylvanians come out from under rate caps.

Auditors' Conclusion: The PUC has responded that it is already performing our Recommendations 1 through 4; however, we do not agree. We have concluded that the PUC has provided the consumer education that it could with the resources that it had available; however, without an adequate statewide campaign, PUC's efforts were not enough to adequately provide electric rate cap expiration and mitigation education to consumers. We disagree with PUC's response that adequate consumer education has been provided. In fact, when asked by the auditors whether the PUC's consumer education efforts were adequate to educate the vast majority of Pennsylvania's electric consumers, PUC management admitted that these efforts were inadequate. The PUC emphasizes this deficiency further in its official response to our findings, stating, "In fact, [PUC] staff recently concluded that electric distribution utilities need to enhance their outreach to seniors, minority and low-income populations." These groups comprise a significant segment of Pennsylvania's overall population. Moreover, they are some of the more economically vulnerable segments of our population. Therefore, by failing to ensure that the aforementioned groups receive early and adequate consumer education, the PUC has confirmed our finding that it is reactive in its mitigation efforts. As noted in our finding, the PUC only hosted or attended 263 educational events in 29 of Pennsylvania's 67 counties, with actual presentations only being conducted in 14 of those counties between July 2008 and October 2009. Additionally, the PUC did not assess the effectiveness of its educational efforts, such as benchmarking and evaluation surveys, due to the lack of a funding mechanism.

Finding No. 1

Instead, the PUC has relied heavily on consumer education and self-evaluations performed by the electric companies. Unfortunately, the media has quoted PPL representatives as stating that it is indifferent as to whether a consumer stays with PPL or switches to an alternate supplier offering lower rates. This indifference and perspective are not in the best interest of the consumer and they indicate that the electric companies derive no substantial benefit from educating consumers. Additionally, based on interviews with management, we found that PUC's oversight of the electric companies' consumer education plans to be inadequate. As stated in our finding, PUC's oversight of the electric companies' consumer education plans involves reviewing the electric companies' educational materials, such as an advertisement, in order to ensure that the materials cover the education standards. The PUC does not perform independent evaluations or measure performance of the effect that the educational materials have on increasing consumers' knowledge. The PUC instructed electric companies to perform their own self-evaluations of consumer knowledge; however, the PUC performs only a cursory review of the results.

Furthermore, as our finding states, between January 2000 and April 2007, PUC made minimal efforts to educate consumers regarding impending rate increases and how to mitigate increased electricity costs and did not require electric companies to provide such education. We disagree with PUC's reasoning that consumer education was not necessary during this time period because only 15 percent of ratepayers were affected by these rate cap expirations. It was not until after the December 31, 2005 rate cap expiration of the Pike County Light and Power service territory in which rates soared 73 percent and there was an outpouring of concern by these consumers that PUC began proceedings to develop policies to address potential electric rate increases. We are deeply concerned by PUC's reactive approach to this continuing imperative situation. These substantial electric rate increases potentially created great financial hardship for thousands of consumers. Failing to provide education to prepare consumers for potentially significant rate increases, guidance for what to do when rate caps expire, and information about ways electricity price increases can be mitigated since the inception of this deregulation process is not acceptable. To assume that rate increases may or may not occur, as the PUC states in its official response, demonstrates simplicity of preparation on the part of the PUC. Instead, PUC should prepare adequately for the worst-case scenario.

Finding No. 1

While, as of February 1, 2010, the PUC states that eight electric suppliers are making offers to residential customers in the PPL service territory and 20 percent of consumers in the PPL service territory have switched to one of these competitive suppliers, consumer education remains vitally important. Adequate consumer education may increase the percent of Pennsylvania consumers who switch to a lower cost electric supplier. This, in turn, is important to keep competitive suppliers in Pennsylvania and to keep electric costs lower for consumers. It should also be noted that, between November 2009 and February 2010, various media outlets have taken a substantial interest in the rising electric costs in the PPL service territory and covered the issue accordingly. This media coverage may have largely impacted the consumers who choose to switch to a lower priced competitive electric supplier. We caution the PUC that media decisions pertaining to what issues are addressed and how they are covered are out of the control of the PUC and should not replace an adequate consumer education campaign.

Additionally, as stated in the finding, consumers must have sufficient notice of potential increases in electric rates and ways to mitigate the costs in order to adequately plan on how to pay for these increases or reduce their costs. Therefore, we continue to make our recommendations as elaborated on below.

Regarding Recommendation 1, the PUC states that it already oversees regional campaigns performed by the electric companies. However, we also recommend that the PUC seek approval for funding in order to perform an adequate consumer education campaign for consumers whose rate caps will expire on December 31, 2010 to supplement the education performed by the electric companies.

Regarding Recommendation 2, we not only recommend implementing the regional campaign referred to in Recommendation 1, but we also recommend that the PUC perform an ongoing evaluation of effectiveness of such a campaign.

Regarding Recommendation 3, the PUC is relying on self-evaluations performed by the electric companies. We also recommend that the PUC perform its own evaluation of effectiveness of the electric companies' consumer education efforts in conjunction with Recommendation 2 above.

Finding No. 1

Regarding Recommendation 4, we acknowledge that the PUC consumer education efforts are ongoing and are shifted to adapt, including, as stated in the PUC's response, developing a separate website to allow electric consumers to input their zip code and see the electric suppliers and competitive offers available to them. We also continue to recommend that the PUC assess and monitor the financial impact of electric deregulation on consumers once rate caps expire to determine what additional assistance and/or education can be provided to consumers in order to minimize consumers' future electricity costs.

We are confident that, if our recommendations are implemented, this report will assist in preparing consumers for the substantial rate increases in electric utility costs upon rate cap expiration and educating the consumers on ways to mitigate these significant increases in electricity prices. Additionally, the report will further strengthen the management controls within the PUC.

***Finding
Two***

PUC Should Improve Its Monitoring of the Electric Companies' Programs to Mitigate Significant Rate Increases Offered to Consumers

According to PUC management, after recognizing the effects of the rate cap expirations which occurred between 2000 and 2006, whereby the range of consumers' electric rates for five companies increased between 27 and 73 percent, and the rates of one company which had initially high rate caps decreased by 14 percent, PUC directed the electric companies remaining under rate caps to file phase-in or pre-payment plans if they expected that electric generation rates would increase by more than 25 percent when the rate caps expire. Of the five companies, three companies, PPL Electric Utilities Corporation, Metropolitan-Edison Co., and Pennsylvania Electric Co., were required to file pre-payment plans with the PUC, which the PUC approved on August 7, 2008, February 26, 2009, and February 26, 2009, respectively. Pre-payment programs allow consumers, on a voluntary basis, to make advance payments on their electric bills prior to rate cap expiration. These extra payment amounts accumulate in participating consumers' accounts and earn interest. Once the rate caps expire and the electric rates increase, electric companies then credit the advance payment amounts and the interest to the respective consumers' monthly electric bills over a two-year period, which will help consumers budget and mitigate the increased monthly electric bills.

PUC management indicated that it is the electric companies' responsibility to implement and administer the pre-payment program. PUC does not oversee or monitor these programs to ensure that the electric companies are properly managing the consumers' advance payments, including accurately calculating and crediting the amount of interest due to the consumer. PUC only requires the electric companies to report the number of consumers enrolled in the programs. No reporting is required for pre-payment monies collected, interest earned, and credits to future monthly bills. Additionally, while PUC does perform reviews of financial records during periodic financial audits of the electric companies, PUC management stated that no reviews or audits have been performed related to the pre-payment programs. PUC management believes that it is unnecessary for it to monitor these pre-payment programs, stating that if consumers have problems with their electric bills or implementation of the pre-payment program, consumers will complain to PUC. Once a consumer complains, PUC will then investigate the complaint and resolve it accordingly. We disagree with this reactionary approach

Finding No. 2

because a consumer may not realize a problem exists. For example, if the electric company is supposed to calculate interest at six percent, but only credits the consumer with interest calculated at four percent, a consumer may not catch this discrepancy. As a result, consumer complaints should not be the sole control relied upon by PUC. Monitoring of the pre-payment program should be proactive to ensure the program is being properly administered. Without monitoring these pre-payment programs, PUC cannot be assured that consumers will receive proper credits for monies pre-paid and interest earned to reduce their future electric bills and mitigate the rate increases after rate caps expire.

Recommendations: We recommend that PUC:

5. Require electric companies that are offering pre-payment programs to provide during PUC financial audits the information necessary to review the amount collected and interest earned, as well as the amounts credited to consumers' electric bills once rate caps have expired; and
6. Direct staff to include as part of existing financial audits a review of pre-payment programs used by electric companies to ensure that consumers' monies are being properly managed, interest is accurately calculated and credited, and consumers are receiving the benefits according to the approved plans.

Agency Response: The Commission agrees with these recommendations and plans to implement them. The only reason that no auditing has yet occurred is the timing of the implementation of the rate mitigation programs. Specifically, we are only now in January 2010, with the expiration of rate caps in the PPL service area, reaching the point when some customers participating in these programs will start reaping the benefits. Credits on customer bills from other pre-payment programs will not begin until 2011.

A standard component of financial audits performed by Commission staff is a review of the companies' billing systems and procedures. The Commission is pleased to include as part of those audits a review of any pre-payment programs offered by electric companies. To ensure that such a review occurs, the Commission will direct audits staff to obtain the necessary data from the electric companies and determine whether consumers are receiving the intended benefits under these approved plans.

Finding No. 2

Auditors' Conclusion: We commend the PUC for its concurrence with Finding 2 and its plans to implement our Recommendations 5 and 6.

***Public Utility Commission
Electric Utility Deregulation***

*Pennsylvania Department of the Auditor General
Jack Wagner, Auditor General
July 2010*

Distribution List

The Honorable Edward G. Rendell
Governor
Commonwealth of Pennsylvania
Harrisburg, PA 17120

The Honorable James H. Cawley (3)
Chairman
Pennsylvania Public Utility Commission
3rd Floor, Commonwealth Keystone Building
Harrisburg, PA 17120

The Honorable Robert M. McCord (2)
State Treasurer
129 Finance Building
Harrisburg, PA 17120

Mr. Phillip R. Durgin, Executive Director
Legislative Budget and Finance Committee
400 Finance Building
Harrisburg, PA 17120

The Honorable Donald L. Patterson
Inspector General
Executive House
101 South Second Street, 3rd Floor
Harrisburg, PA 17101

Ms. Sharon Anderson (4)
State Library of Pennsylvania
Serials Records Section
218 Forum Building
Harrisburg, PA 17120

Mr. John J. Kaschak, Director
Bureau of Audits
Office of the Budget
8th Floor, Forum Place
Harrisburg, PA 17101

***Public Utility Commission
Electric Utility Deregulation***

*Pennsylvania Department of the Auditor General
Jack Wagner, Auditor General
July 2010*

This report is a matter of public record. Copies of this report may be obtained from the Pennsylvania Department of the Auditor General, Office of Communications, 318 Finance Building, Harrisburg, PA 17120. If you have any questions regarding this report or any other matter, you may contact the Department of the Auditor General by accessing our website at www.auditorgen.state.pa.us.