POWER POINTS

BGS Energy Auction

March 2004

Third BGS Energy Auction

"New Jersey is the only state in the country to secure its entire electric needs with an auction. We have once again been able to take advantage of a very robust and active energy market at the wholesale level and get the best possible electric prices for our homes and businesses." – **Jeanne M. Fox**,
New Jersey Board of Public Utilities President

There has been much discussion on how electric deregulation has stalled or is not working in the United States. Some have claimed that the test of competition is how many customers switch providers. New Jersey's experience with deregulation may show that the real benefit from deregulation -- lower prices -- is not a function of how many people switch in the retail market, but how many suppliers are active and selling in the wholesale market.

Over the last three years, New Jersey has achieved significant success in creating a robust wholesale market for electricity. The number and diversity of suppliers have grown over the years and real price savings have been realized by consumers. In February 2004, the state completed its third auction to secure Basic Generation Service (BGS) using an innovative internet-based auction process to meet the electricity demands of the state's retail customers.

The auction not only reduced prices for consumers (at a time of soaring gas costs), but also protected consumers from fuel price volatility by locking in prices for 12-month and 36-month terms. The BGS auction process is a model transferable across the United States for properly designed and functioning competitive markets. New Jersey is leading the nation in creating open, transparent and efficient markets for electricity and ensuring that companies rather than consumers bear the risk of generation investment.

The 2004 auction will allow residential consumers in New Jersey to save approximately $24 million annually as compared with the rate resulting from last year's auction. Residential customers of Public Service Electric & Gas, Rockland Electric and Jersey Central Power & Light will see decreases on an annual basis ranging from 0.5% to 1.5% while residential customers of Conectiv will see a slight increase of 0.7%.

How did BGS develop?

Since August 1999, customers in New Jersey have been able to choose their electric supplier. Customers who do not choose a new supplier, or who leave a third party supplier, are provided default electricity supply service by their local electric utility through BGS. The New Jersey Board of Public Utilities (NJBPU) again determined that BGS electricity supply would be purchased by New Jersey's four Electric Distribution Companies (EDCs) - PSE&G, JCP&L, Conectiv and Rockland Electric Company in a competitive internet-based auction process. The first auction was held in February 2002 and a second in February 2003. New Jersey is the only state in the nation to use an auction of this type to competitively secure its default electric supply.

How does the BGS auction process work?

The process in 2004 consisted of two concurrent auctions: one for larger customers (about 1850 statewide) and one for smaller commercial and residential customers. This was similiar to the process used in 2003. The group of larger customers has an energy rate based on hourly PJM spot market prices while the smaller customer group had prices that are fixed seasonally. The NJBPU decided to split these two customer groups because the NJBPU felt that large customers are better able to adjust usage to hourly market price fluctuations.

This year's large customer group was slightly bigger than it was last year because the NJBPU decided that all industrial and commercial customers with peak electric usage requirements of greater than 1500 kilowatts (kW) should now be considered part of the large customer group.

The auction for energy to serve the smaller customer group (smaller industrial and commercial customers and residential customers) was split into two different durations. Rather than bidding on the entire load for one

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year, one third was offered for a 12-month term and one-third was offered for a 36-month term. One-third of the load for the smaller customer group (approximately 5400 MW) had already been procured in last year's auction with a 34-month term. Therefore, as of June 1, 2004, one-third of the supply for the smaller customer group will have a remaining term of 12 months, one-third will have a remaining term of 24 months and one-third of the supply will have a remaining term of 36 months. Using staggered terms provides economic benefits by spreading the risk of weather fluctuations, market conditions, economic activity, and fuel price uncertainty. Future auctions are expected to be for 36-month terms.

Both auctions were conducted using a descending clock format, and both were implemented through a secure internet platform. Prospective BGS suppliers submit supply bids stating how much load they wish to serve at a given price. As long as the supply bid is greater than the supply needed, prices decrease each round. Prices continue to decrease until the supply bid equals just the amount needed.

The BPU reviewed the auction results within two business days of the auction closing to minimize bidder uncertainty. As offers made at the auction were binding, there were no post-auction negotiations. All companies are bound by the auction results. The following charts provide a brief description of the results:

Commercial Industrial Energy Prices (CIEP)

The BGS-CIEP auction began on February 2, 2004 and ended on February 6 after 52 rounds of bidding with the following closing prices for each company:

CIEP – 12 Month Tranches

Company	Total Tranches*	Closing Wholesale Price per MW-day
Conectiv	**14**	**$49.90**
JCP&L	**28**	**$54.98**
PSE&G	**65**	**$52.01**
Rockland Electric	**1**	**$57.96**

*A tranche in the BGS-CIEP Auction is equivalent to approximately 25 MW. The winning bidders in the auction were: Consolidated Edison; Constellation Power Source, Inc.; Dominion Retail Inc.; PPL Energy Plus, LLC; PSEG Energy Resources & Trade, LLC and Select Energy Inc.

Fixed Pricing (FP)

The BGS-FP Auction began February 2, 2004 and ended February 10 after 71 rounds of bidding with the following closing prices for each company:

FP – 12 Month Tranches

Company	Total Tranches*	Cents per kilowatt-hour
Conectiv	**8**	**5.473**
JCP&L	**12**	**5.325**
PSE&G	**28**	**5.479**
Rockland Electric	**2**	**5.566**

FP – 36 Month Tranches

Company	Total Tranches*	Cents per kilowatt-hour
Conectiv	**7**	**5.513**
JCP&L	**15**	**5.478**
PSE&G	**28**	**5.515**
Rockland Electric	**1**	**5.597**

*A tranche in the BGS-FP Auction is equivalent to approximately 100 MW. The FP winning bidders were: BP Energy Company; Conectiv Energy Supply, Inc.; Consolidated Edison Energy, Inc; Constellation Power Source, Inc.; DTE Energy Trading, Inc; FPL Energy; J. Aron & Company; Morgan Stanley Capital Group Inc.; NRG New Jersey Energy Sales LLC; PSEG Energy Resources & Trade, LLC; Reliant Energy Services, Inc.; Select Energy, Inc.

The auctions were proposed by PSE&G and the other NJ EDCs, administered by NERA a consulting firm hired by the NJ EDCs, and monitored by the NJBPU Staff and their consultant, Charles River Associates.

More information on the auction is available on the NJ BGS Auction website at ***www.bgs-auction.com.*** More information on PSEG is available on our website ***www.pseg.com.***

Conclusion

The BGS auction process enables consumers to achieve access to competitive supply markets. It provides a mechanism that allows the benefits of wholesale competition to flow to the retail customer. The process not only has delivered better pricing, but also has reduced price volatility. It demonstrates that competition can work well when allowed to work under fair rules.