

PUBLIC SERVICE COMMISSION OF THE DISTRICT OF COLUMBIA  
1333 H STREET, N.W., SUITE 200, WEST TOWER  
WASHINGTON, D.C. 20005

ORDER

October 24, 2005

FORMAL CASE NO. 945, IN THE MATTER OF THE INVESTIGATION INTO  
ELECTRIC SERVICE MARKET COMPETITION AND REGULATORY  
PRACTICES, ORDER NO. 13794

**I. INTRODUCTION**

1. By this Order, the Public Service Commission of the District of Columbia ("Commission") approves the Generation Procurement Credit Rider ("GPC") filed by the Potomac Electric Power Company ("PEPCO" or "Company") on July 12, 2005.<sup>1</sup> This particular phase of the proceeding examines PEPCO's compliance with divestiture sharing distribution obligations that are set forth in the Phase I and Phase II settlement agreements approved by the Commission.<sup>2</sup> This Order addresses issues relating to the Commission's efforts to restructure the District of Columbia's retail electricity market pursuant to the District of Columbia Retail Electric Competition and Consumer Protection Act of 1999.<sup>3</sup>

**II. BACKGROUND**

2. By Order No. 13650, the Commission directed all interested parties to file comments on PEPCO's proposed 2005 GPC Rider within ten (10) days from the date of the Order.<sup>4</sup> Reply comments were due within fifteen (15) days. By Order No. 13743, the Commission granted OPC's motion to extend the comment period.<sup>5</sup> Subsequently, an

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<sup>1</sup> *Formal Case No. 945, In The Matter Of The Investigation Into Electric Service Market Competition and Regulatory Practices, ("F.C. 945")*; Letter to Freda A. James, Acting Commission Secretary, from Paul H. Harrington, PEPCO Associate General Counsel, ("GPC Letter") filed July 12, 2005.

<sup>2</sup> *See F.C. 945, Non-Unanimous Agreement of Stipulation and Full Settlement Regarding Divestiture Issues ("Phase I Settlement")*, dated November 8, 1999, as approved through Order No. 11576 at Appendix A, rel. December 30, 1999; *F.C. 945, Order No. 11613*, rel. February 17, 2000 (Order establishing Phase II of Formal Case No. 945 to address the issue of PEPCO's post-divestiture unbundled rate structure); and *F.C. 945, Non-Unanimous Agreement of Stipulation and Full Settlement Regarding Unbundled Rate Issues ("Phase II Settlement")*, approved through Order No. 11845, rel. December 5, 2000.

<sup>3</sup> D.C. Code, 2001 Ed. §§ 34-1501 – 1520.

<sup>4</sup> *F.C. 945, Order No. 13650*, rel. August 2, 2005.

<sup>5</sup> *F.C. 945, Order No. 13743*, rel. August 19, 2005.

extension was granted to PEPCO with respect to the submission of its reply comments.<sup>6</sup> OPC submitted comments on August 18, 2005,<sup>7</sup> and PEPCO submitted its reply comments on August 26, 2005.<sup>8</sup> No other party submitted comments on PEPCO's 2005 GPC filing.

3. In Order No. 11576, the Commission approved the Phase I Settlement, which authorized PEPCO to sell the bulk of its electric generating assets.<sup>9</sup> The Commission's decision to approve the Phase I Settlement was based on its evaluation of the benefits to District ratepayers, as well as its determination that these benefits outweighed any potential detriment resulting from the divestiture. As part of the Phase I Settlement, the Commission found that the GPC provision was in the public interest because it benefited both ratepayers and shareholders.

4. Article IV of the Phase I Settlement establishes the general parameters for calculation of the GPC credit.<sup>10</sup> As specified in Article IV of the Phase I Settlement, during the rate cap period, any gains realized by PEPCO from the provision of Standard Offer Service ("SOS") generation are subject to sharing with DC ratepayers. The Phase I Settlement allows for a GPC mechanism whereby PEPCO will share profits gained from its divestiture of generation services and procurement of energy in the open market with all ratepayers and shareholders.<sup>11</sup> Specifically, if PEPCO receives profits of \$20 million or less, ratepayers would receive 80 percent of such profits, and shareholders would receive 20 percent. If PEPCO's profits exceed \$20 million, the Phase I Settlement provides that ratepayers would receive 60 percent of such profits, and shareholders would receive 40 percent.<sup>12</sup> Finally, the sharing of any net profits with ratepayers is to be done via a per kilowatt-hour ("kWh") credit.<sup>13</sup>

5. The Phase I Settlement further specified that PEPCO would retain the portion of the net profit, if any, that would otherwise flow to ratepayers up to the amount

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<sup>6</sup> F.C. 945, Order No. 13749, rel. August 26, 2005.

<sup>7</sup> F.C. 945, Comments of the Office of the People's Counsel on the Proposed Generation Procurement Credit Rider Filed By Potomac Electric Power Company on July 12, 2005 Pursuant to Order No. 13650, filed August 18, 2005 ("OPC Comments").

<sup>8</sup> F.C. 945, Reply Comments of Potomac Electric Power Company, filed August 26, 2005 ("PEPCO Reply Comments").

<sup>9</sup> F.C. 945, Order No. 11576, rel. December 30, 1999.

<sup>10</sup> *Id.* at § 4.01. Paragraphs 2, 5, and 7 of the Phase II Settlement include further refinements with respect to the GPC calculation, which are addressed later in this Order.

<sup>11</sup> *Id.* at § 4.01.

<sup>12</sup> *Id.*

<sup>13</sup> In effect, any net profit is allocated to the residential and commercial classes on a kWh basis.

of the guaranteed rate reductions included in Sections 3.03 and 3.05 of the settlement.<sup>14</sup> Residential customers received a base rate reduction of 2.77 mills per kWh on February 8, 2001 and February 8, 2005.<sup>15</sup> Commercial customers received a base rate reduction of 1.09 mills per kWh at that same time. Accordingly, the proposed GPC bill credit reflects the shared savings amounts in excess of the above levels.<sup>16</sup>

6. As previously noted, the Phase II Settlement also addresses the GPC calculation. In Paragraph 2, the GPC calculation is amended to include the net benefits, if any, associated with PEPCO's Energy Use Management ("EUM") (i.e., curtailable load) programs. While PEPCO suspended such programs as of December 31, 2004, PEPCO has included net EUM program results through the end of 2004 in its 2005 GPC filing.<sup>17</sup>

7. Paragraph 5 of the Phase II Settlement clarifies that any GPC credit will be distributed to customers over a twelve-month period (on a cents per kWh basis). In addition, Paragraph 5 specifies that if the difference in actual versus intended GPC credits, to either class of customers, is greater than \$100,000 during a given twelve-month period, PEPCO will adjust the GPC credit, as necessary, to reflect the amount of the difference, with interest.<sup>18</sup>

8. In Order Nos. 12635 and 13378, the Commission concluded that the second GPC Application period began on June 1, 2003 and ended on May 31, 2004. The Commission also ruled that the third GPC Application period would begin on October 1, 2005. As of the date of PEPCO's 2005 GPC filing (i.e., July 12, 2005), the third GPC Application Period had not yet ended. Accordingly, PEPCO's 2005 GPC filing quantifies only the actual versus intended results of the second GPC Application Period, which are discussed below.

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<sup>14</sup> See Article 3.03 and 3.05 of the Phase I Settlement.

<sup>15</sup> PEPCO implemented the guaranteed rate reductions via its January 29, 2001, Compliance Filing. The guaranteed rate reductions ended with the implementation of the District's new SOS service. In Order No. 13378 issued on September 13, 2004, the Commission ruled in part that PEPCO was correct to apply accelerated depreciation to EUM equipment, assuming that the useful life of the equipment would end on December 31, 2004. PEPCO's 2005 filing reflects such accelerated depreciation.

<sup>16</sup> As discussed below, residential customers will not receive any 2004 GPC bill credit since their guaranteed rate reduction exceeds the ratepayer's share of the generation procurement margins.

<sup>17</sup> OPC submitted comments regarding PEPCO's net EUM benefit calculation, which are discussed later in this Order.

<sup>18</sup> The GPC adjustment may be either positive (for an under-credit) or negative (for an over-credit).

### III. PEPCO's Proposed 2005 GPC

9. In its July 12, 2005 GPC Filing, PEPCO indicates that the total generation procurement margin for the period February 8, 2004 through February 7, 2005 is \$6.21 million.<sup>19</sup> According to PEPCO, the customers' share of that amount equals \$4.966 million, or \$0.00044 per kWh.<sup>20</sup> Further, according to PEPCO, after reducing the customers' share of the generation procurement margin for the guaranteed rate reductions already provided to customers beginning February 8, 2001, PEPCO calculates that the GPC would provide non-residential customers in the District of Columbia with a net GPC credit of \$0.00044 per kWh. For residential customers, because the average customer's share of \$0.00044 per kWh is less than the guaranteed rate reduction of \$0.00277 per kWh, the residential GPC amount is zero.<sup>21</sup> For non-residential customers, because the average customer's share of \$0.00044 per kWh is less than the guaranteed rate reduction of \$0.00277 per kWh, the non-residential GPC amount is zero.<sup>22</sup>

10. Table 1 below presents the total 2005 GPC margins to be shared between PEPCO and DC ratepayers and compares the result to 2004.

Table 1

	<i>12 Months Ended 2/7/05</i>	<i>12 Months Ended 2/7/04</i>
SOS Generation Revenue	\$326,678,611	\$254,330,059
Net EUM Revenue	208,871	(1,242,656)
SOS Procurement Expense	<u>(320,679,228)</u>	<u>(214,483,531)</u>
Total GPC Margin	\$6,208,254	\$38,603,871

11. As shown in Table 1, the Total GPC Margin declined from \$38.60 million for the twelve month period ending February 7, 2004 to \$6.21 million in 2005. The primary cause of this decline was an increase in SOS Procurement Expense of \$106.2 million, which will be discussed in detail below.

12. Table 2 shows the application of the sharing agreement contained in the Phase I Settlement to the 2005 results. After dividing the Total GPC Margin of \$6.21

<sup>19</sup> GPC Letter at 2.

<sup>20</sup> *Id.*

<sup>21</sup> *Id.*

<sup>22</sup> *Id.*

million into tiers, the ratepayers' share (before guaranteed rate reduction offsets) is \$4.97 million.

Table 2

<i>Total GPC Margin</i>	<i>\$6,208,254</i>
<i>Customer Share of the Margins</i>	
80% of First \$20.0 million	\$4,966,603
60% of any Remaining	-
<b>Total Customer Share</b>	<b>\$4,966,603</b>

13. Since the ratepayers' share of PEPCO's GPC profit is to be distributed on a kWh basis, PEPCO appropriately divides the above \$4.97 million by total estimated distribution sales to arrive at an average (gross) GPC credit of 0.44 mills per kWh.<sup>23</sup> However, the Phase I Settlement provides for a reduction in the average GPC credit up to the amount of the guaranteed rate reduction received by each customer class. Since the Phase I Settlement's guaranteed rate reduction varies by class, the net GPC credit will also differ by class. This step in the calculation is summarized in Table 3 below.

Table 3

	<i>Residential</i>	<i>Commercial</i>
Gross GPC Credit	\$0.00044	\$0.00044
Guaranteed Rate Reductions	<u>0.00277</u>	<u>0.00109</u>
<b>Net GPC Credit</b>	<b>\$ -</b>	<b>\$ -</b>

14. Table 3 reveals that the guaranteed credit of both the residential and commercial classes exceeds its gross GPC Credit. Accordingly, neither residential nor commercial customers are entitled to receive a 2005 GPC bill credit, based on the GPC margins earned by PEPCO over this period.<sup>24</sup>

15. Attachment C to PEPCO's 2005 GPC filing reports the actual versus intended payout results, by customer class, from the second GPC Application Period which ended May 31, 2004. As shown in Attachment C, residential customers received

<sup>23</sup> PEPCO uses an estimated level of distribution sales of 11,269,676,283 kWh for the twelve-month period beginning June 1, 2005.

<sup>24</sup> This result for commercial customers does not include the return of a small shortfall in actual GPC payments from the second GPC Application period.

actual GPC credits of \$910,709, which is \$9,992 less than intended. Since this difference is less than \$100,000, no reconciling adjustment is required for residential customers.<sup>25</sup> With respect to commercial customers, Attachment C shows that actual GPC credits totaled \$18.88 million, or \$150,642 less than intended. Since this difference is greater than \$100,000, a reconciling adjustment is required for commercial customers. By dividing the \$150,642 by the expected level of commercial kWhs, PEPCO arrives at a 2005 GPC bill credit for commercial customers of \$0.00002 per kWh.<sup>26</sup>

#### IV. Comments and Reply Comments

##### A. OPC Comments

16. OPC's comments are limited to two topics. Specifically, OPC argues that PEPCO has improperly: 1) employed accelerated amortization of its EUM Equipment to inflate its EUM program expenses; and 2) used the higher energy rates negotiated in Amendment No. 2 to the Transition Power Agreement ("TPA") with Mirant to calculate SOS Procurement Expense. OPC claims that the above changes in the GPC "formula" combine to reduce significantly the size of the Generation Procurement Margin, which is shared with ratepayers. As discussed below, OPC recommends that the Commission: a) reject PEPCO's use of accelerated depreciation; b) require PEPCO to employ the *original* TPA energy rates to calculate SOS Procurement Expense; and c) reject PEPCO's claim against the Mirant estate (in the amount of the TPA rate increase) as the basis to defer ratepayers' "rightful benefit" under the GPC agreement.

##### a. Energy Use Management Programs

17. With respect to the accelerated amortization issue, OPC notes that the Commission ruled in PEPCO's favor in Order No. 13378. However, OPC states that the Commission "based its decision regarding the calculation of EUM equipment costs on findings that the proper amortization treatment was purely an accounting issue and that the useful life of the EUM equipment would end on December 31, 2004."<sup>27</sup> OPC argues that the Commission was "wrong on both points and would be wrong to do so with regard to the fourth application period."<sup>28</sup>

18. In its current comments, OPC discusses PEPCO's previous explanation for using accelerated depreciation. Specifically, in its 2004 GPC Reply Comments, PEPCO stated that the useful life of the EUM equipment would end on December 31, 2004 since market earnings were projected to be insufficient to cover EUM program operating

<sup>25</sup> See Paragraph 5 of the Phase II Settlement.

<sup>26</sup> Per Attachment C, PEPCO divides \$150,642 by 9,069,636,693 kWh, which equates to a GPC credit of \$0.00002 per kWh.

<sup>27</sup> See OPC Comments at 4.

<sup>28</sup> *Id.*