

Before the

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PENNSYLVANIA PUBLIC UTILITY COMMISSION

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PECO Energy Company's Application  
for Approval of its Restructuring Plan  
and Joint Petition for Partial Settlement

PA PUBLIC UTILITY COMMISSION  
PROTHONOTARY'S OFFICE  
R-00973953

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Petition of Enron Energy Services Power, Inc.,  
for Approval of an Electric Competition and  
Choice Plan and or Authority Pursuant to  
Section 2807(e)(c) of the Public Utility Code  
to Serve as the Provider of Last Resort in the  
Service Territory of PECO Energy Company

P-00971265

ORIGINAL

**MAIN BRIEF OF CONECTIV ENERGY**

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## I. INTRODUCTION

Before the Commission is the full record in this proceeding, including to the base case submitted by PECO Energy Company (the "PECO Plan") and all other active parties, the Joint Petition for Partial Settlement ("Partial Settlement"), the testimony of those parties who were not signatories to the Partial Settlement, the plan of the Environmentalists (the "environmentalists Plan"), and the Enron Choice Plan ("Enron Plan"). Through the Commission's decision in this proceeding, a signal will be sent to not only alternative generation suppliers who have become licensed in this Commonwealth, but also the nation as a whole.

The goal to be reached in this proceeding by the Commission is simply stated: the promotion of electric generation competition in this Commonwealth, for the purpose of securing lower priced electrical service now and in the future for the citizens of this Commonwealth. As is evident by the sheer size of the record in this proceeding, the method of reaching that goal is extremely complex.

This is the setting for the Commission's decision. Whether to accept a Partial Settlement that prevents competition for the foreseeable future or, to order that PECO receive the \$5.461 billion it agreed to, provide the temporary rate reduction of the

Partial Settlement, and create an environment in which competition can occur. The Commission should embrace the purposes of the Act and choose the latter course.

## II. THE LEGISLATIVE MANDATE

The stated goal of the Electricity Generation Customer Choice and Competition Act (hereinafter "the Act") is to permit retail customers the opportunity to obtain direct access to a competitive generation market<sup>1</sup> in order to contain the costs of generating electricity through competition<sup>2</sup>

The Commission has been charged by the Legislature with the task of guiding the electric industry of this Commonwealth from a regulated monopolistic environment to an open competitive market.<sup>3</sup> In carrying out this transition, the Legislature required the filing of restructuring plans by all utilities "to implement direct access to a competitive market for the generation of electricity." 66 Pa C.S. § 2806(d). As a result of

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<sup>1</sup> 66 Pa.C.S. §2802(3)

<sup>2</sup> 66 Pa.C.S. §2802(5)

<sup>3</sup> The Legislature recognizes that the Act merely establishes certain ground rules for the transition from regulation to total competitions. See, e.g., 66 Pa. C.S. § 2802 (15)

this Legislative mandate and the Commission's Orders, PECO Energy filed its Restructuring Plan (the "PECO Plan"). During the course of this proceeding, certain parties entered into unilateral discussions which resulted in the Joint Petition for Settlement (the "Partial Settlement"), Enron Energy Services Power, Inc. filed an alternative to the PECO Plan and the Partial Settlement (the "Enron Plan"), and the Environmentalists filed their own plan, building upon those already submitted (the "Environmentalists Plan"). Several electric generation suppliers, including Conectiv Energy presented testimony regarding certain modifications to the Partial Settlement under the umbrella of an informal coalition -- the Pennsylvania Electric Competition Coalition ("the Coalition).

The Commission is not required to take or leave any of the proposals in toto, but has the requisite authority to modify any of the proposals submitted not only under the pre-existing Public Utility Code but specifically under the Act. In countless proceedings, the Commission has modified settlements, most recently the Pilot Proceedings at P-00971168 et al., put forward by the Pennsylvania Electric Association in the pilot cases.

The Act also contemplates that the Commission shall have broad discretion in the acceptance, rejection, or modification of

any of the above plans placed before it. Consistent with Section 2806(f) of the Act, 66 Pa.C.S. §2806(f), the Commission may accept, modify, or reject any plan submitted to it. All preconditions of the Act necessary for the modification of the plan have been met. All proposals have been the subject of "open evidentiary hearings with proper notice and opportunity for all parties to cross-examine witnesses". Subsequent to these requisite hearings, the Act provides for the Commission to: "...issue an order accepting, modifying or rejecting such a plan at the earliest date possible, but no later than nine (9) months from the filing of the restructuring plan." Clearly, the Act provides the Commission with full authority to modify the original PECO plan and all others.

### III. CONECTIV ENERGY'S POSITION

It has consistently been Conectiv Energy's position that the electric distribution utilities, PJM, the Commission, suppliers, marketers, and other interested parties should work together to provide, as soon as possible, customers with meaningful choice.

In order for meaningful choice to be available to the citizens of Pennsylvania, the Partial Settlement should not be adopted unless it is modified. The Partial Settlement contains

major flaws and/or inconsistencies with the Act which will permit recovery of more than that agreed to in the Partial Settlement. Conectiv Energy submits that PECO should be permitted to fully recover both the agreed upon nominal stranded costs as well as a return on that investment. Conectiv Energy also believes that subsumed within the \$5.461 billion amount is a return on that investment.

**IV. PECO WILL OVERRECOVER THE STRANDED COSTS PERMITTED BY THE PARTIAL SETTLEMENT**

As more fully explained below, Conectiv Energy submits, and the Record supports a conclusion that the Partial Settlement will result in the overrecovery of revenues by PECO through a combination of the failure to incorporate load growth, an improper net present value calculation, an improper valuation of securitization, a mismatch of GS and HT revenues, and an improper allocation of transmission and distribution costs.

**A. OVERVIEW**

Within the context of this proceeding, PECO first claimed stranded costs of \$6.8 billion and a revised estimate of \$7.461 billion. As part of the Partial Settlement at issue herein, PECO

has agreed to recover \$5.461 billion of its claim and to write off \$2 billion.

Conectiv Energy does not dispute the amount to be recovered as stipulated in the Partial Settlement. Nor does Conectiv Energy dispute the legal authority of a utility to recover its known and measurable net electric generation related costs, which would traditionally be recovered from ratepayers under a regulated environment.<sup>4</sup> The issue is whether PECO will receive the \$5.461 billion it agreed to or more.

**1. PECO'S PROJECTED LOAD IS UNDERSTATED**

For purposes of calculating its CTC/ITC recovery, PECO utilizes a flat sales level of 33,569,358 mwh in each year the Partial Settlement is in effect. Partial Settlement, Appendix C. These projected sales are understated when measured against other forecasts contained in the record.

The flat sales figures are inconsistent with the projected sales figures PECO has reported to various governmental agencies. Conectiv Energy Cross Examination Exhibit 2 consists of the 1997

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<sup>4</sup> Conectiv Energy believes that a utility should be permitted a return *of*, and a return *on*, its investment including stranded costs. Conectiv Energy does not share PECC Witness Mitnick's "opinion" on this subject. Tr. 836-838.

Annual Resource Planning Report filed by PECO with this Commission on May 1, 1997. As part of that report, all jurisdictional utilities are required to project future sales under three scenarios: (1) high, (2) base, and (3) low. Despite PECO's projection of flat sales through 2008 of approximately 33,569,358 mwh in this proceeding, Its Historic and Forecast Energy Demand (base case) indicates the cumulative sales growth through the settlement years of approximately 10%. PECO also projects a 0.8% annual demand growth in its most recent FERC Form 714.

These varying sales figures are graphically indicated below.

SALES FIGURES

	<u>PECO-No Growth</u>	<u>FERC FORM 714</u>	<u>PUC IRP</u>
1999	33,569,358	34,381,485	34,522,000
2000	33,569,358	34,656,537	34,886,000
2001	33,569,358	34,933,789	35,379,000
2002	33,569,358	35,213,260	35,750,000
2003	33,569,358	35,494,966	36,125,000
2004	33,569,358	35,778,925	36,499,000
2005	33,569,358	36,065,157	36,882,000
2006	33,569,358	36,353,678	37,266,000
2007	33,569,358	36,644,507	37,656,000
2008	33,569,358	36,937,664	38,049,000

Source PECC Exh. 1A.

PECO experts add additional credence to Conectiv Energy's position by basing all of their market price projections upon the MAAC (PJM) Net Energy and Peak Demand forecasts in PECO Exhibit JBF-6 and PECO Statement No. 4 at pages 10-11. As is evident from this exhibit PJM load is expected to increase from 242,963 Gwh in 1996 to 276,054 Gwh in 2005 -- more than 14% over 9 years.

Finally, in its original filing with the Commission (PECO Statement No. 15) PECO witness Cucchi states:

PECO has used a load growth scenario that reflects the Company's most likely assumptions regarding economic variables such as household and employment growth. This scenario has been the base load growth scenario. This base load growth scenario for the years 1997 through 2006 is shown in Exhibit GAC-3 to my testimony. The base load growth forecast incorporated both end-use and econometric forecasts.

PECO Statement 15 at pages 36-37. The data contained in Mr. Cucchi's Exhibit GAC-3 is taken from PECO Energy Company's 1996 Annual Resource Planning Report.

The testimony of Dr. Richard H. Silkman, a witness presented on behalf of CEPA, TAG, ACORN, State Senator Vincent J. Fumo and John W. Long, Jr., provides an explanation for an increase in consumption in a competitive market. In discussing rate reductions, Dr. Silkman explains the results of reduced rates which can be achieved through competition:

Residential customers will use more electricity as a result of being less concerned about the price they must pay per unit of consumption. They may turn up thermostats, leave lights on for longer periods, install additional lighting, purchase additional electrical appliances or switch from non-electric to electric technologies for such things as space or water heating.

CEPA Statement. 1 at pages 7-8 (Tr. 579). Similarly, Enron Witness Bruce R. Oliver testified that increased supplier activity will increase electric sales. (Tr. 1611-1612).

PECC Witness Mitnick, utilized three scenarios in developing his customer credit -- PECO's no growth claim, a 0.8% growth scenario (based upon information submitted by PECO to the Federal Energy Regulatory Commission; and a growth scenario based upon PECO's report to this Commission.

**2. PECO'S NET PRESENT VALUE CALCULATION REPRESENTS AN OVER COLLECTION**

The next step is to determine the net present value of the CTC revenue stream. PECO has understated its recoverable revenue stream.

Two issues have been the focus of attention: (1) the appropriate discount rate and (2) the date to which the net present value is calculated.<sup>5</sup> Although other parties responding to the initial filing of PECO proffered different discount rates, Mr. Mitnick, in an effort to remove controversy in the proceeding utilized PECO's proposed 8.71% discount rate in his calculations.

The second piece of the net present value calculation is the date to which the revenue stream is discounted.

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<sup>5</sup> Neither Conectiv Energy nor PECC have challenged the amount of stranded costs contained in the settlement agreement.

PECC witness Mitnick consistently utilized the January 1, 1999 date to preserve the fundamental premise of stranded cost recovery. As is provided by the Act the basic premise of the ITC/CTC charge is to recover those costs:

which traditionally would be recoverable under a regulated environment but which may not be recoverable in a competitive electric generation market.

66 Pa. C.S. § 2803. Competition begins January 1, 1999. Until that time, PECO will be recovering regulated rates without the presence of material competition. Stranded costs cannot arise until competition starts.

Utilizing PECO's discounted rate and a valuation date of January 1, 1999, Mr. Mitnick calculated a net present value recovery of the CTC stream at \$6,317,129,387, rather than the \$5,461,000,000 contained in the Partial Settlement.

### **3. PECO WILL RECEIVE A BENEFIT FROM SECURITIZATION**

PECC Exhibit 1A, Table SAM-SR1C, Mr. Mitnick graphically illustrates the value of securitization of \$4 billion as set forth in the Partial Settlement utilizing a value of .75% for every million dollars as reflected on PECO's Form 10-K. Mr. Mitnick graphically illustrates the results in column 9 of PECC Exhibit 1A Table SAM-SR1, page 2.

4. PECO'S MISMATCH OF SALES FOR RATES GS AND HT RESULTS IN AN OVER COLLECTION OF APPROXIMATELY \$215,000,000

PECO has utilized differing sales figures for various classes of customers in developing its Table A to the Partial Settlement and in its Proof of Revenues.

In PECC Statement No. 3, PECC Witness Reising analyzes these sales figures stating:

My review of the rate design indicates that there is a significant mismatch between the energy sales units used for cost allocation <sup>6</sup> and the billing energy amounts used for rate design purposes. <sup>7</sup> While there are small differences for several classes, ... there is a major discrepancy for rates HT and GS.

\* \* \*

If my review of this cost allocation and rate design data is correct, it means that PECO's total costs have been allocated on one basis and PECO's rates designed on a different basis, with the result that the proposed rates for the HT and GS classes are substantially overstated.

PECC Statement No. 3, p. 16-17; In response to Mr. Reising's criticisms, PECO witness Clemmer testified that the total sales for each rate classification in the proof-of-revenue "... are not

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<sup>6</sup> PECO Exhibit RAC-10.

<sup>7</sup> Appendix C to the Partial Settlement.

essential to the development of rates." PECO Statement No. 12-RJ. Mr. Clemmer offers his Exhibit RAC-12 for the proposition that he is able to produce the same revenues for Rate class GS contained in Appendix C to the joint settlement using kwh sales substantially lower than those proffered by Mr. Hill in his Appendix C. Mr. Clemmer states:

There would be no additional revenues generated by this difference (the difference between Rate GS sales of 685,357 vs. 659,600) in kilowatt hour totals on a proforma basis verses that was derived in the sample.

Tr. 1097.

Such a disconnect between sales and revenues is logically impossible. Correction to reflect the appropriate revenue recovery yields an additional \$215,000,000 in over collections.

**5. TRANSMISSION AND DISTRIBUTION COSTS ARE IMPROPERLY ALLOCATED**

Mr. Paul D. Reising presented testimony on behalf of PECC relative to the proposed transmission and distribution charges contained within the proposed settlement. PECC Statement No. 3.

In response to the Commission's restructuring filing requirements (M-00960890F0003), PECO submitted a cost of service allocation study and a functionalized cost study by class-of-

service. As stated by PECO witness Clemmer, the study was prepared using year ending December 31, 1996 data. PECO Statement 12, p. 4. Although presented as a traditional cost of service study, Mr. Clemmer attempted to unbundle and assign costs to the production, transmission and distribution functions. (Id., p.6).

The flaw in Mr. Clemmer's analysis is his insistence that even if all of the functions associated with the sale of generation, i.e., sales force, administrative costs associated with the sales, etc., are removed, the PECO transmission and distribution company, would still incur those costs which should be directly allocated to the T&D function. (Tr. 1050-1055).

Similarly, executive costs were totally assigned to the T&D function even though it was acknowledged that the executives would spend time on all functions of the business, generation, as well as transmission and distribution. (Tr. 1056-1063).<sup>8</sup>

In short, Mr. Clemmer merely looked to whether a particular cost might continue. If that cost might continue after the

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<sup>8</sup> OCA witness Lee Smith points out other errors. For example, PECO did not take into account whether the size of the operation would be reduced (OCA Statement. No. 45, p. 3); allocated to the production function 30% of total office supplies and 59% of the credits for those same office supplies (id. P. 4).

advent of competition in 1999, that cost was assigned to the T&D function (Tr. 1055).<sup>9</sup>

As another example, the costs being incurred by Horizon, a PECO Energy EGS have not been assigned as Horizon did not exist during the 1996 calendar year which formed the basis of the cost of service study (Tr. 1073, 1102).

In his supplemental testimony (PECC St. 3), PECC Witness Reising reviewed the attempt by PECO to correct its errors through rebuttal testimony and concluded:

...that Mr. Clemmer's analysis does not support his effort to functionalize labor-related A&G expenses in a manner different than that historically approved by the Commission using functional labor expenses. As a result, it is my opinion that the Company's T&D charges shown in the proposed settlement should be rejected and T&D charges should be recomputed in accordance with the functional cost of service proposed by Enron, which was summarized in Exhibit 3, PDR-2.

PECC Statement No. 3, p. 10. As a result of Mr. Reising's recommendations, the average T&D charge is \$0.0258 per kwh--more than half a cent less than PECO's proposed \$0.0047 of \$0.0311 (\$0.0047 for transmission and \$0.0264 for distribution).

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<sup>9</sup> PECC Witness Reising points out other deficiencies in the allocation of administrative and general expenses (other than property insurance and employee pensions and benefits which were allocated to all functions); general and common plant; and intangible plant.

**B. A RETURN ON PECO'S INVESTMENT IS SUBSUMED WITHIN ITS CALCULATIONS AND NEED NOT BE VIEWED AS AN ADDITIONAL AMOUNT TO BE RECOVERED**

That PECO has always included a return on component in its stranded claim is evident. The original filing, Schedule 10 of Mr. Cohn's direct testimony, includes a return on component in calculating the "Annual CTC Revenue Requirements." The return on component, using 13.71%, is shown as \$1,917,470,000 in nominal dollars in Schedule 10, page 2, column 7. These return on dollars are then included in the total revenue requirement which nominally is \$8,818,587,000, with a present value of \$6,927,584,000. PECO Statement No. 3, Schedule 10, p. 2, columns 5 and 6. The levelized net present value annual revenue requirement, grossed up for Gross Receipts Tax ("GRT"), is shown as \$1,392,791,000, which is what PECO witness Clemmer then uses to calculate rates.<sup>10</sup>

Mr. Cohn's annual CTC revenue requirement amounts (including return on investment) from Schedule 10, p. 1, column 5, reappear in PECO Witness Hill's Rebuttal Testimony, Exhibit TPH-18. Using "the new PECO discount rate of 8.71%," the nominal amounts for

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<sup>10</sup> PECO Statement No. 12, Exhibit RAC-2, page 1.

the years 1999-2005 are equated on a present value basis to \$6.8 billion. The purpose of this Exhibit TPH-18 is to state the PECO stranded claim and then quantify the disallowances to the claim proposed by other parties. Exhibit TPH-17 summarizes other parties' positions, such as "no return allowed on stranded plant," and the effect of those positions is what Exhibit TPH-18 purports to show.

These exhibits are clear that PECO has been claiming the right to recover net present value of \$6.8 billion on January 1, 1999 -- an amount which has included the return on component that Mr. Cohn had always reflected in his claim, and that Mr. Hill repeated in his rebuttal exhibits. The Partial Settlement specifically states that the \$5.461 billion is the Company's \$7.461 billion total stranded cost less the \$2 billion write-off. Partial Settlement Paragraph 17. Thus, it is clearly established that return on investment was in the total stranded claim, which net of the write-off, established PECO's recovery in the Partial Settlement.

The CTC/ITC revenue stream should reflect this stipulated amount. Conective Energy, like other parties, believes that whatever the allowed stranded claim is, its recovery should include compensation for the time value of money through the

appropriate discount rate. There is no apparent basis for adding anything further to the stream of properly discounted CTC/ITC revenues.

1. **NET PRESENT VALUE MUST BE STATED ON A SEPTEMBER 1, 1999 BASIS**

PECO claims the valuation date for net present value should be changed from January 1, 1999 to September 1, 1998, on the grounds that its proposed temporary rate reduction starts then.

This formulation is in error for at least two reasons. First, it is clear that PECO implicitly recovers stranded costs during the 4-month period. Because rates do not change from September 1, 1998 to January 1, 1999, it seems inherent that the implicit recovery is similar to the stranded recovery in 1999, and PECO seems to concede this (Tr. 976).

Second, and perhaps more importantly, competition under the Act does not begin until January 1, 1999, not September 1, 1998. Conectiv Energy submits that until competition begins, none of PECO's costs could be considered as stranded.

## 2. THE TRANSMISSION AND DISTRIBUTION RATE CAP EXTENSION

PECO attaches a large value to the extension of the T&D rate cap for 2 and ½ years.<sup>11</sup> As with other alleged settlement concessions, this provision was portrayed as a value to customers on top of the supposed stranded cost write-off and PECO's total stranded cost recovery of \$5.461 billion. PECO claims that this concession (and others) as additional stranded costs should be added to the \$5.461 billion agreed upon.

Even if this shift is appropriate, and even if a T&D concession is properly defined as a stranded cost under the statute,<sup>12</sup> PECO has inflated the value of this concession. PECO's valuation assumes its T&D unit cost is 3.11¢/kwh, that O&M expense will escalate at 3% annually, and that sales will not increase to reduce the unit cost.

As discussed earlier, the T&D unit cost is not more than 2.37¢/kwh. Enron Statement No. 7-R. Even when PECC Witness Reising had previously calculated a higher T&D unit amount

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<sup>11</sup> The Customer Notice incorrectly states that the rate cap is extended for 3 years. NEV Cross Examination Exhibit

<sup>12</sup> As set forth below, Conectiv Energy submits that none of the concessions discussed in this section are stranded costs under the definition section of the Act.

(2.63¢/kwh), he pointed out that it would take a highly improbable rate of increase in T&D expense, net of sales growth, to drive the unit cost above 3.11¢/kwh by the year 2003. PECC Statement No. 3 at pages 17-18.

With respect to PECO's projection of significant O&M cost increases, it is worth pointing out that PECO itself presented the following historical data on Non-Fuel O&M unit costs in Exhibit TPH-11;

1990	3.23¢/kwh
1991	2.95¢/kwh
1992	3.16¢/kwh
1993	2.88¢/kwh
1994	2.85¢/kwh
1995	2.58¢/kwh
1996	2.35¢/kwh

### 3. THE FOUR MONTH RATE REDUCTION

PECO has assigned a value to the first 4 months of the temporary rate reduction, and added the amount to its "Components Included in CTC Revenue Recovery". PECO Exhibit TPH-35. As with other settlement concessions, it is unclear why this concession, presumably made to achieve settlement, has suddenly become a stranded cost. And, indeed, if the first 4 months of the temporary rate reduction represents a stranded cost, why not all months of the temporary rate reduction?

C. THE JOINT PETITION FOR PARTIAL SETTLEMENT CONTRADICTS THE EXPRESS PROVISIONS OF THE ELECTRIC GENERATION CUSTOMER CHOICE AND COMPETITION ACT

In reviewing the voluminous testimony presented in this proceeding, one must not become mired in the details and overlook the fundamental purpose and provisions of the Act. Conectiv Energy submits that the Partial Settlement violates the Act in two distinct areas: (1) the lack of a reconciliation of the CTC revenues, and (2) the collection of the negotiated concessions through the CTC.

Conectiv Energy does not dispute the concessions obtained by the industrial customers and various consumer groups won in the Partial Settlement negotiations. Conectiv Energy does dispute the method whereby the revenues associated with these "concessions" are to be collected -- through the inclusion of the amounts associated with these programs as transition costs, recoverable either through securitization or the ITC. PECO Witnesses conceded that these are not stranded costs.

Section 2803 of the Act, 66 Pa.C.S. §2803 defines transition costs as:

An electric utility's known and measurable net generation-related costs, determined on a net present value basis over the life of the asset or liability as part of its restructuring plan, which traditionally would be recoverable under a

regulated environment but which may not be recoverable in a competitive electric generation market and which the commission determines will remain following migration by the electric utility.

The Act continues, describing in great detail the nature of the costs to be recovered as transition costs, none of which even remotely resemble the concessions "given" by PECO to the other parties to the Partial Settlement. Conectiv Energy believes that the CTC mechanism is not the proper vehicle to recover these costs.

#### **V. THE PARTIAL SETTLEMENT WILL THWART COMPETITION**

If anything is to be learned from the Pilot Programs mandated under the Act, it is that robust competition and customer savings can be achieved through the right price structures. From the overwhelming number of customers who desired to participate in the programs, it is clear that the citizens of Pennsylvania are looking for competitive alternatives. Conectiv Energy submits and the record supports the need for a sufficient customer credit to permit the competitive market initiated by the pilot programs to continue to develop and flourish. Conective Energy submits that the customer credit proposed in the Partial

Settlement will not preserve the competition that has already started and deny customers of competitive benefits.

**A. THE CUSTOMER CREDIT**

The importance of establishing a reasonable credit cannot be underestimated as this is the price which all new entrants must beat in order to compete. As pointed out by PECC Witness Hull if the generation credit is set to low, an Electric Generation Supplier must loose money and the competition envisioned the Act may cease upon the expiration of the pilot programs. See, e.g., PECC Statement 2 at page 4.<sup>13</sup>

While all parties agree that the right customer credits are is nigh impossible to predict over the long transition period, two theories have been advanced: (1) the charges should be based upon projected wholesale energy and capacity sales, or (2) through a proper allocation of costs among Transmission and Distribution charges and the CTC, with the residual becoming the generation credit.

The Act itself does not provide a convenient formula for determining the customer credit, however some limited guidance is

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<sup>13</sup> This sentiment is shared by CEPA Witness Silkman who testified that as a consultant, he would not recommend to a client that a product be sold below cost. (Tr. 1982-1983).

provided. Pursuant to the Act, § 2804(4) two related price caps are established: (1) an overall rate cap set at the level of rates as of January 1, 1997 and (2) a generation cap. In addition, the entire basis of the Act is to promote competition in the Commonwealth. In order to do so the customer credit must permit EGS's sufficient opportunity to recover not only the wholesale price of energy and capacity but also a recovery of its sales expenses, overhead, returns, etc.

Perhaps no single element in this proceeding is more important to Electric Generation Suppliers than a properly established customer credit. This figure will serve as a benchmark against which EGS's must compete, will establish the level of competition that will take place in the Commonwealth, and will provide the consumers of Pennsylvania the opportunity to realize the ultimate goal of competition -- lower prices. As one would expect, this area represented the most contentious portion of the proceeding.

PECC witness Mitnick stated with regard to the 2.8¢ per kwh charge in the Partial Settlement:

PECO calculated the generation cap as a residual after shifting costs of selling and marketing electricity to the distribution charge. PECO plans to recover funds through transmission and

distribution, and has made the generation cap as low as possible to block competition.

\* \* \*

A Consumer Credit should be calculated exactly the opposite from the way PECO calculated the generation cap. First, assign the true cost to the transmission and distribution system, excluding all costs not directly related to these functions. Second, set the CTC and ITC charges so that PECO will receive only the Commission-determined level of stranded costs recovery... . Third, an amount should be allocated for a Consumer Credit which is large enough to permit customers to shop for energy.

PECC Statement No. 1, p.20. In light of this statement, Mr.

Mitnick recommended the following customer credits:

January 1, 1999	3.80¢/kwh
January 1, 2000	4.02¢/kwh
January 1, 2001	4.41¢/kwh
January 1, 2002	4.61¢/kwh
January 1, 2003	4.71¢/kwh
January 1, 2004	4.93¢/kwh
January 1, 2005	5.10¢/kwh
January 1, 2006	5.29¢/kwh
January 1, 2007	5.48¢/kwh
January 1, 2008	5.68¢/kwh

As is evident, the rate of 2.8¢ per kwh, the Partial Settlement's proposed customer credit is totally insufficient to foster any competition in Pennsylvania. As stated by PECC witness Hull, customers are not likely to switch suppliers unless

and until suppliers can offer extra incentives either in price or other goods or services. Witness Hull opines that in order to provide a 10% savings to customers, the supplier would be forced to reduce its generation price below cost by 32%. PECC Statement No. 2, pp. 8-9. She further portrays graphically that under the Partial Settlement such incentives are not possible as suppliers will loose money even if the match PECO's customer credit. Given her market price projections, Ms. Hull testified that an EGS can expect to loose 1.035¢ per kwh in 1999; 1.139¢ per kwh in 2000; 0.828¢ per kwh in 2001; 0.621¢ per kwh in 2002; and 0.518¢ per kwh in 2003.<sup>14</sup> PECC statement No. 2, p. 13, Table One. On a cumulative basis, each EGS will have experienced a total loss of 4.140¢ per kwh over the five year period.

PECO defends its customer credits based upon projections of the cost of energy and capacity in the wholesale market. Conectiv Energy submits that these wholesale numbers cannot be utilized as a surrogate for the customer credit unless and until

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<sup>14</sup> In her analysis, Ms. Hull used the very conservative wholesale price projections for capacity and energy of 3.40¢ in 1999; 3.50¢ in 2000; 3.60¢ in 2001; 3.70¢ in 2002; and 3.80¢ in 2003. To this figure must be added .20¢ per kwh for line losses, GRT, and load factor. These prices do not include any administrative costs, return etc., for the supplier which Ms. Hull has estimated at a conservative .20¢ per kwh. PECC Statement No. 2, p. 13-14.

these figures are corrected for line losses, load factor, reserve margins, gross receipts tax, and costs of doing business of the EGS. To accept the wholesale numbers that have been presented in this proceeding as a basis for the customer credit would doom competition to failure.

Despite PECO presenting three witnesses who testified to market pricing, PECO relied primarily upon the testimony of Dr. William H. Heironymus (PECO Statement No. 6, 6-R). Dr. Heironymus, in his rebuttal testimony developed an all hours energy price of \$20.50 and an all hours capacity price of \$16.00 at the wholesale level. Even assuming that these extremely low and unsupported figures are correct for 1999, when Dr. Heironymus' prices are adjusted for line loss, load factor (both at the PECO system average), reserve margin and gross receipts tax, the resultant retail price, without any supplier costs, is 2.9¢ per kwh, or in excess of the customer credit contained in the Partial Settlement.

That the \$16.00/kw-year is unreasonably low is clear from the record. For example OCA witness Douglas Smith projected a 1999 a capacity price of \$19.72/kw year. OCA Statement No. 2S.<sup>15</sup>

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<sup>15</sup> Based upon the information contained in OCA Exhibit LS-13,  
(continued...)

Recent prices secured through PECO's own Power Team<sup>16</sup> suggest that even this number is well below the actual current price.<sup>17</sup> As testified to by PECC Witness Douglass, on October 7, Mr. Douglass was able to purchase 75 megawatts of capacity for the month of November only from PECO at a price of approximately \$25.50/kw year (Tr. 637-638). Significantly, Mr. Douglass offered to purchase capacity for a longer period of time at a higher price from PECO. That offer was refused. (Tr. 638).

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(...continued)

the energy and capacity prices forecast by OCA Witness Douglass Smith would result in a customer credit of 2.9¢ per kwh. However, it appears that witness Smith utilized an average line loss adjustment of 4.573% which is inconsistent with the system average line loss of 7% utilized by most other parties to the proceeding. (See, e.g., PECO Statement No. 6RJ at page 5). Additionally it appears that while there was an adjustment for load factor implicit in witness Smith's load weighted market price, the calculation does not adequately reflect this factor. By correcting for line loss and load factor in the traditional manner, the 1999 price (including gross receipts tax) becomes 3.15¢ per kwh. Additionally, the price does not reflect any of the selling, administrative and other costs incurred by an EGS. Conectiv Energy does not endorse this figure, merely presenting this as an example that even the OCA's own witness provided testimony at odds with the Partial Settlement.

<sup>16</sup> PECO's Power Team is responsible for the purchase and sale of wholesale energy and capacity on the PJM market.

<sup>17</sup> All witnesses project a rise in the price of capacity over subsequent years. For example OCA Witness Smith projects the price of capacity to rise to \$30.07 in the year 2000, \$34.40 in 2001, and to \$62.19 in the year 2015. OCA Exhibit DSC-8.

Similar purchases by Mr. Douglass were also for one month durations. (Tr. 632, 634). Clearly, PECO's own internal Power Team would not sell any long term capacity for Dr. Heironymus' \$16.00/kw year or Mr. Smith's \$19.72/kw-year.

PECO attempts to deflect this criticism by claiming that it would sell both energy and capacity through a "Standard Offer" for 3.0¢ per kwh for residential and commercial load. However, several conditions are attached. For example, the offer is good only for the term of the pilot programs and would not be available after the conclusion of those same pilots. Similarly, the amount of energy and capacity available to a particular EGS would be limited to the amount of energy and capacity lost by PECO through customer selecting an EGS other than PECO. Clearly, this is an attempt by PECO to remove the potential argument that no energy and capacity is available for the pilot programs. Significantly, PECO's offer to sell power for 3.0¢ per kwh, is a further indication that the 2.8¢ per kwh contained in the Partial Settlement is unreasonable.

Implicit in CEPA Witness Silkman's cross-examination regarding the comparison of the Partial Settlement and the Enron Choice plan was the recognition that the Partial Settlement could thwart competition in the early years. (Tr. 1983-1985).

Conectiv Energy submits that this Commission should not permit the Partial Settlement to take away the benefits of competition that is currently being enjoyed by the citizens of this Commonwealth.

**B. PECO'S ABILITY TO DISCOUNT BUNDLED SERVICE PRESENTS AN ANTI-COMPETITIVE BARRIER**

Pursuant to Paragraph 33 of the Partial Settlement, PECO, as the distribution company, will be able to offer a "standard market rate" for those customers who either elect not to choose an alternative supplier or who are unable to choose because of the phase-in mandated by the Act. Specifically, the Partial Settlement provides:

PECO's distribution company will satisfy this obligation by purchasing required amounts of energy and capacity at wholesale from other generation suppliers, including its affiliated generation entity, and reselling that energy and capacity at standard market rates determined by PECO...

Mr. Hill has given this provision a broad interpretation. Instead of offering this standard market rate to only those customers who elect not to choose or who cannot choose, Mr. Hill states:

PECO's understanding of the settlement is that we will create a standard market rate available for

all customers that would be offered by the distribution company and not just default customers anyone could take.

Tr. 519. It is through this mechanism that PECO could meet or better any price offer that may be made to a customers by an EGS with the only proviso that the price be set below the customer credit.

This mechanism would have a tremendous chilling effect upon competition. For example, no matter what an EGS could offer a potential customer, either via price discounts or other services, PECO will be able to meet or beat that price as it will establish what it believes is the standard market. One must question why anyone would choose to migrate to an EGS when in fact they could gather offers, present those offers to PECO, and be assured that PECO will meet that offer with its unique advantage.

## VII. CONCLUSION

In view of the foregoing, Conectiv Energy submits that the record in this proceeding is clear:

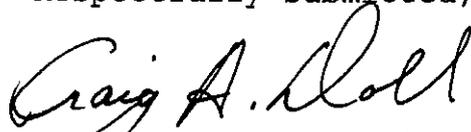
1. The Joint Petition for Partial Settlement would result in an over recovery from its ratepayers of 2 billion dollars even assuming the potential for a 10% rate cut for customers.

2. The Joint Petition for Partial Settlement understates the customer credit to which the citizens of Southeastern Pennsylvania are entitled and through which they can truly enjoy the benefits of competition -- lower prices. To insure true competition Conectiv Energy urges the Commission to increase the level of the customer credit.

3. The likely result of adoption of the Joint Petition for Partial Settlement, without amendment, arguably is the elimination of competition contemplated by the Act and initiated through the pilot programs.

Conectiv Energy requests that this Honorable Commission reject the Joint Petition for Partial Settlement as stated, and modify the Joint Petition as set forth herein.

Respectfully submitted,



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