May 26, 2005

<u>VIA ELECTRONIC MAIL AND HAND DELIVERY</u>

Honorable Kristi Izzo, Secretary
Board of Public Utilities
Two Gateway Center
Newark, NJ 07102

Re: In the Matter of the Petition of Atlantic City Electric Company for Approval of a Power Purchase Agreement with Valero Refining Company and for Associated Rate Treatment
BPU Docket No. EE03110943

Dear Secretary Izzo:

Enclosed please find the original and eleven copies of the comments of the Division of the Ratepayer Advocate (Ratepayer Advocate) on the above-referenced matter. Kindly stamp the extra copy as "filed" and return it in the enclosed, self-addressed stamped envelope. Thank you for your assistance.

Atlantic City Electric Company (Atlantic or Company) has filed a petition requesting that the Board of Public Utilities (Board or BPU) approve a proposed power purchase agreement (PPA) it entered into with the customer, Valero Refining Company (Valero). The proposed PPA would run for ten years with automatic extensions from year to year until terminated upon 90 days written notice and replaces a previous power purchase agreement that has expired. Under the proposed PPA, Atlantic would purchase the net electrical output from Valero's cogeneration facility as a "qualified facility" as that term is defined in the federal Public Utility Regulatory Policies Act of 1978, 16 U.S.C.A. 2601, *et seq.* (PURPA). The price per kilowatt-hour (kWh) that Atlantic would pay Valero is established at the PJM locational marginal price (LMP) as computed by PJM at the generation bus-bar. Valero would also pay to Atlantic a monthly administrative fee of $5,000.00 which is adjusted each year based on the Consumer Price Index.

The Valero cogeneration facility has a rated output of approximately 43.5 megawatts (MW). Atlantic states that Valero has peak electric needs of approximately 50 MW and that during most hours, the Valero electricity needs will exceed the output of the cogeneration facility because the facility will generally run only when the refinery is also operating. The original petition stated that Valero would be a BGS-CIEP customer and also a standby service customer. However, Valero has stated that since the petition was filed, it has obtained electric supply service from a third party supplier since June 1, 2004. *Response to RAR-8(a).* [1]

The original petition requested approval of the proposed PPA and also requested approval of Atlantic's proposed ratemaking treatment to pass the costs and revenues under the proposed PPA through the rates for basic generation service (BGS). The petition alleged that the payments to Valero would operate such that there should be no cost or revenue impact on Atlantic and its customers. However, discovery responses in this matter indicate that that allegation is not always the case. There appear to be situations (discussed more fully below) under which Atlantic's other ratepayers are at risk

[1] Valero receives its distribution service under Atlantic's tariff Transmission General Service (TGS). *Response to RAR-8(b).*

for higher rates due to the proposed PPA. To the extent that the net of the costs and revenues under the PPA results in an underrecovery, that underrecovery will increase ACE'deffered balance and will result in Atlantic's other ratepayers paying rates that are higher than necessary. The Ratepayer Advocate urges the Board to prevent such a negative impact on Atlantic's other ratepayers. Furthermore, Atlantic has declined to provide cost justification underlying the monthly $5,000.00 administrative fee, so that it is impossible to determine if the $5,000.00 sufficiently covers all administrative costs imposed upon Atlantic by the proposed PPA. *Response to S-6 and RAR*-5. It should also be noted that the new fee is less than the administrative fee under the original, now expired, PPA,[2] but Atlantic has not shown that its costs to administer the PPA are less than before. *Id*. It may very well be that Atlantic's other ratepayers are subsidizing the administrative costs of the proposed PPA. The Ratepayer Advocate believes that the Board should not permit any such subsidization.

It appears that Valero believes the justification for approval of the PPA lies in the Public Utility Regulatory Policies Act of 1978 (PURPA) as that statute is embodied in the utility's Small Power Purchase (SPP) tariff. *Responses to RAR-18 and RAR-19*. While the Ratepayer Advocate has received Valero's response to our discovery requests concerning the justification to approve the PPA, Atlantic has yet to respond. Therefore, it is not entirely clear upon what basis Atlantic believes the BPU should approve the PPA. However, in its original petition, Atlantic alleges that the PPA is "in the public interest"

[2] Atlantic's response to S-9, Attachment 1, shows that the administrative fee for the month of October 2003 was $6,304.80. This is an admittedly small difference, but the response to S-6 notes that the administrative fees under both the original PPA and the proposed PPA were "negotiated" by the contracting parties, and, thus, have no cost of service justification, and that there is "no cost of service study or other documentation that attempts to allocate or assign the specific cost of services" that Atlantic provides under the proposed PPA.

and that the BPU "should take into consideration that, the Valero cogeneration facility is a qualified facility under PURPA and, as such, has certain federally-derived rights to have Atlantic purchase its power." *Petition, para. 11*. The Petition does not contain any other justification to approve the PPA. It seems, then, that the Board should not approve the PPA until Atlantic states with more detail the legal justification and policy justification for approving the PPA.

Valero has stated that the BPU policy mentioned in Atlantic's SPP tariff justifies approving the proposed PPA. The SPP tariff provides that a qualifying facility (QF) with capacity greater than 1000 kW is required to enter into a separate contract with Atlantic. (See copy of SPP tariff attached.) The SPP tariff states that a QF is "entitled to a contract at full avoided energy costs and, if eligible, capacity costs. Customer specific contracts are subject to approval by the New Jersey Board of Public Utilities." Valero alleges that the proposed PPA "provides for payments for energy at the PJM LMP, which is identical to the energy price provided in the tariff for QFs less than 1,000 kwh." *Response to RAR-19.* However, Atlantic admits that there are times when the price paid to Valero is different than the price that Atlantic would otherwise pay for energy.

Atlantic made the following statement in its "Preliminary Responses to Data Requests", concerning BPU Staff data request S-7:

> …Specifically, ACE purchases excess energy from Valero at a market based price and sells the same energy into the PJM market at a market based price. Because of the way in which PJM operates its markets, the market price for the purchases may be slightly different from the market price for sales. However, the difference is likely to be minimal and the impact of this purchase and sales on revenues is also likely to be minimal. The exact impact, however, will not be known until after some experience with purchases of the excess energy under the PPA.

Any difference between the prices paid and the prices received for excess energy generated by Valero, whether positive or negative, would be debited or credited to Atlantic's deferred balance. Thus, the possibility remains that Atlantic's other ratepayers will be "harmed" in at least this one aspect of the proposed PPA.

Subsequent to this response, Atlantic provided further information. In Atlantic's response to S-43, the Company stated:

> Under the PPA, net energy is purchased when available and at the PJM LMP for the Valero bus. The energy prices charged to BGS-CIEP customers are the hourly PJM average Atlantic Electric (AECO) zonal LMP. The average AECO zonal LMP in each hour is a load weighted LMP aggregate of all of the load buses in the zone. In many hours the LMP at all buses in a particular zone are equal, but the price at any specific bus in any particular hour can be either higher or lower than the megawatt weighted average zonal LMP for that same hour, and it is difficult to predict when and if the Valero bus price will be higher or lower than the zonal average price. However both are reflective of the real-time spot market price for energy in any given hour and, as such, for purposes of comparing the BGS-CIEP energy price to the PPA price these are assumed to be basically equivalent.

Therefore, Atlantic admits that there are times when Atlantic will pay Valero a price that is higher than it would otherwise pay. Under these circumstances, it cannot reasonably be said that the proposed PPA only charges Atlantic customers the full avoided energy costs. Under these circumstances, Atlantic's other ratepayers will pay higher than the full avoided energy costs. Admittedly, the price differentials have recently not been very large.[3] However, the contracting parties have not pointed to any exception to the requirement that Atlantic's customers may only be charged the avoided energy costs and nothing more. That situation is not permitted under PURPA or under

[3] Atlantic states that the price differentials over the past year have been approximately a net underrecovery of about $5,000.00 in most months for electric supply related to Valero. *Response to RAR-12*.

the SPP tariff. In this way, it can be seen that the proposed PPA does not satisfy all the terms required under PURPA or the SPP tariff. For this reason, the Board should not approve the proposed PPA under its current terms.

Another issue that has arisen is the manner in which PJM assesses its charges for the Valero load. The proposed PPA relies on the assumption that, for the PJM costs, Atlantic will charge, and Valero will pay for, electrical supply based on the net amount, rather than the gross amount, delivered to Valero. The petition does not provide clear assurance that PJM will treat Valero on the net basis for the full duration of the PPA and any future extensions. Under the proposed PPA, if PJM is allowed to bill on a gross basis, Atlantic and its ratepayers will be exposed to additional, significant PJM transmission and/or ancillary services charges. That is, the proposed PPA requires the difference between the amounts that PJM bills to Atlantic and that recovered under the PPA from Valero be accumulated in Atlantic's deferred balance for later recovery from Atlantic's ratepayers.

The difference between PJM charges based on net versus gross usage is significant. Atlantic's responses to data requests have shown that this difference is on the order of $2 million to $3 million in most months. *Responses to S-10, S-39, RAR-7.* [4] Since June 1, 2004 however, PJM has billed its charges based only on the net usage by Valero. The Federal Energy Regulatory Commission (FERC) has at least preliminarily permitted PJM's billing to be done on this net basis. However, there is no assurance that

[4] The Ratepayer Advocate recognizes that these responses note that they do not reflect the alleged right of Valero to receive revenues for its generation capacity and energy into the PJM market on a gross basis. However, the hypothetical capacity revenues would not be significant enough to provide very much of an offset to the additional costs to other ratepayers. Therefore, this point does not significantly reduce the large exposure that other customers have to higher rates if the PJM charges should revert to a gross usage basis.

this situation will not be reversed at some point in the future and that Atlantic and its ratepayers will once again incur these large monthly charges. Since the proposed PPA does not prevent this significant harm to Atlantic's other ratepayers, the Ratepayer Advocate believes that the Board should not approve the proposed PPA in its current form.

The Ratepayer Advocate believes that the Board does not yet have sufficient information to approve the PPA in its current form. However, if the Board decides to consider approving the PPA, the Ratepayer Advocate believes that any approval should be conditioned on Atlantic's ratepayers being protected from paying excessive rates under the PPA. The conditions that the Ratepayer Advocate urges the Board to impose upon the PPA include that (1) Atlantic's ratepayers should never be charged any rates higher than the PJM energy rates Atlantic actually pays to PJM and that (2) the payments for PJM charges for which Atlantic's other customers are responsible under the PPA be limited to the net usage by Valero as opposed to the gross usage and that (3) Atlantic's other customers should not subsidize the administrative costs of the proposed PPA. The second condition concerning the net versus gross usage by Valero should continue to be required of the parties even if in the future the FERC and/or PJM changes the billing procedure for Valero back to gross usage or to some other less advantageous procedure.

Respectfully submitted,

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RATEPAYER ADVOCATE

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