

February 22, 2005

Magalie R. Salas
Secretary
Federal Energy Regulatory Commission
888 First Street, N.E.
Washington, D.C. 20426

RE: PJM Interconnection, L.L.C.
Docket No. ER05-513-000

Baltimore Gas and Electric Company and
PEPCO Holdings, Inc. Operating Affiliates
Potomac Electric Power Company;
Delmarva Power & Light Company,
And Atlantic City Electric Company
Docket No. ER05-515-000

(Not Consolidated)

Dear Secretary Salas:

Enclosed for electronic filing is the Joint Consumer Advocate's Protest and Request for Evidentiary Hearing, in the above-referenced proceeding.

Sincerely,

/s/ filed electronically

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Enclosure

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL REGULATORY COMMISSION

PJM Interconnection, L.L.C.	:	Docket No. ER05-513-000
Baltimore Gas and Electric Company and PEPCO Holdings, Inc. Operating Affiliates	:	Docket No. ER05-515-000
Potomac Electric Power Company;	:	
Delmarva Power & Light Company,	:	
And Atlantic City Electric Company	:	

(Not Consolidated)

JOINT CONSUMER ADVOCATES' PROTEST
AND REQUEST FOR EVIDENTIARY HEARING

Pursuant to Rule 211 of the Commission's Rules of Practice and Procedure, 18 C.F.R. § 385.211, the Pennsylvania Office of Consumer Advocate ("Pa. OCA"), the Maryland Office of People's Counsel ("MPC"), and the Office of the People's Counsel for the District of Columbia ("DC OPC") (herein designated as "Joint Consumer Advocates"), file this Protest to PJM Interconnection, L.L.C.'s ("PJM") filing in Docket No. ER05-513-000 and to Baltimore Gas & Electric Company's and the PHI Holding Companies' filing in Docket No. ER05-515-000. In support of this Protest, Joint Consumer Advocates submit as follows:

1. Joint Consumer Advocates have jointly intervened by separate documents in both PJM's filing in Docket No. ER05-513-000 and in Baltimore Gas & Electric Company's and the PHI Holding Companies' filing in Docket No. ER05-515-000. Joint Consumer Advocates represent the interests of retail consumers in the District of Columbia, Maryland and Pennsylvania who receive their energy from load serving entities within PJM and who transport

that power to retail consumers over the transmission systems owned by the PJM TOs and managed by PJM.

2. Joint Consumer Advocates file a single Protest to both filings because of the inter-related nature of these filings. The formula rate issue in Docket No. ER05-515 is one of the options proposed as a method of harmonizing rates for new and existing facilities in Docket No. ER05-513. Consumers in Pennsylvania, as well as those in Maryland and the District of Columbia, may be affected by the harmonization filing in Docket No. ER05-513. While neither BG&E nor the PHI Companies provide transmission service directly to retail consumers in Pennsylvania, retail consumers in Pennsylvania may nonetheless be affected by the formula rate filing in Docket No. ER05-515. The formula rate filing will establish the elements and components of a formula rate approach that could be utilized by other TOs within PJM in the future. Any of the PJM TOs, including those electric utilities serving Pennsylvania retail consumers, may elect this approach at any time under PJM's filing in Docket No. ER05-513-000. Since PJM's filing in Docket No. ER05-513-000 sets forth a common methodology for all TOs in PJM, it is reasonable to conclude that any action taken by the Commission in this docket to establish the formula for formula rates for a few of the PJM TOs could apply to other PJM TOs that may seek authorization for formula rates in the future. Absent participation in this proceeding, the Pa. OCA may not have an opportunity in the future to be meaningfully heard with respect to the elements and components of the formula rate structure, including the important consumer protection additions to the formula rate the Pa. OCA believes are necessary to ensure adequate consumer protection under such a regulatory regime.

3. On January 31, 2005, several transmission owners in the PJM Interconnection, L.L.C., a Regional Transmission Organization managing the electric transmission systems of

electric utilities throughout the Mid-Atlantic and Mid-Western regions of the nation, submitted proposed revisions to Schedule 12 of the PJM Open Access Transmission Tariff (“OATT”), to establish procedures by which the PJM Transmission Owners (“TOs”) may, if they so choose, recover the costs incurred in new transmission facilities and harmonize the rate treatment of new and existing facilities. PJM and these TOs made this filing pursuant to the settlement agreement filed on May 26, 2004 in Docket No. ER04-156-000, *et al.* These TOs include the electric utilities serving Pennsylvania, Maryland and the District of Columbia.

4. PJM submitted the filing in Docket No. ER05-513 pursuant to a commitment undertaken by the PJM TOs as part of the May 26, 2004 Settlement in Docket No. ER04-156-000 *et al.* That Settlement requires them to propose a method of harmonizing the rate treatment of new and existing facilities if the PJM TOs seek rate recovery of their investment in new facilities. *Allegheny Power System Operating Companies, et al.*, 108 FERC ¶ 61,167 (2004). Schedule 12 of the PJM OATT allows PJM TOs to implement a surcharge to recover the costs of investment in new transmission facilities constructed under Schedule 12 in conjunction with PJM’s Regional Transmission Expansion Planning (“RTEP”) process. They proposed three options for accomplishing this harmonization: a) they could chose to recover the costs of new facilities through existing transmission rates, i.e. forego filing for a surcharge recovery mechanism; b) they could choose to implement a surcharge and credit all surcharge revenues except for revenues associated with rate of return on equity incentive adders against existing transmission rates; or c) they could choose to implement formula rates that would change every year to reflect updated information in each utility’s FERC Form 1 annual report.

5. On January 31, 2005, Baltimore Gas & Electric Company (“BG&E”); and the PHI Operating Companies, *i.e.* Potomac Electric Power Company, Delmarva Power & Light

Company, and Atlantic City Electric Company (“the PHI Companies”) submitted applications to implement a transmission cost of service formula rate under the revised Schedule 12 of the PJM tariff as proposed in Docket No. ER05-513. These TOs made this filing pursuant to the same settlement agreement filed on May 26, 2004 in Docket No. ER04-156-000, *et al.* Thus, BG&E and the PHI Companies have elected in this filing to restate their rates through the formula rate option.

PROTEST

6. Joint Consumer Advocates protest both PJM’s filing at Docket No. ER05-513-000 and BG&E’s and the PHI Companies’ filing at Docket No. ER05-515-000. Due to the related nature of these filings, Joint Consumer Advocates have combined their Protest into a single document to be filed in both dockets.

Harmonization Issues in Docket No. ER05-513 Associated With Option 2

7. The filing in Docket No. ER05-513 proposes three options for harmonizing rate recovery for existing transmission facilities with rate recovery for new transmission facilities. Joint Consumer Advocates protest here the second option that provides for harmonization by crediting surcharge revenues minus any authorized ROE incentive adders against existing transmission rates. While no TO has elected to proceed under Option 2 at this time, Commission action on this filing will establish the mechanism for harmonizing rates for existing and new facilities when any TO seeks surcharge rate recovery for new facilities in the future. Consequently, protest of that mechanism is ripe for consideration in this docket.

8. PJM’s and the TOs’ filing in Docket No. ER05-513-000 does not satisfy the requirements for harmonization set forth in the Commission’s order in Docket No. ER04-156-000 or the provisions in the Settlement filed May 26, 2004 in that docket. The Commission’s

January 16, 2004 Order in Docket No. ER04-156-000, *et al.*, approved the concept of surcharge recovery for the costs associated with new investment constructed pursuant to PJM's RTEP process, but required the PJM Transmission Owners to "harmonize" surcharge rates with existing transmission rates. *Allegheny Power System Operating Companies, et al.*, 106 FERC ¶ 61,016 (2004). The Commission imposed this harmonization requirement as a remedy for the concerns raised by intervenors in that docket. Those intervenors generally alleged that the Commission could not authorize recovery of new investment costs through surcharges without first ensuring that existing transmission rates are just and reasonable. *Id.* at ¶ 3. The Settlement resolving the procedural issues in that docket obligated the PJM Transmission Owners to "harmonize the rate treatment of new and existing facilities." *Allegheny Power System Operating Companies, et al.*, 108 FERC ¶ 61,167 (2004) ("Order Accepting Settlement Agreement").

In their filing in Docket No. ER05-513, the PJM and the TOs proposed to comply with this obligation under Option 2 by crediting all surcharge revenues except for those revenues associated with any return on equity incentive adders, against the existing transmission rates of the PJM Transmission Owner(s) undertaking the construction of the new facilities. Filing at p. 3. Joint Consumer Advocates protest the proposed harmonization mechanisms under Option 2 on grounds that the mechanism does not in fact harmonize the surcharge and existing rates.

First, the PJM Transmission Owners' proposal does not achieve full harmonization under Option 2. There is no means for ensuring that the resulting transmission rate netted after the surcharge revenue credit offset produces an end result rate that is just and reasonable for consumers. The PJM TOs plan to credit all surcharge revenues except those associated with any ROE incentive adders that may be authorized by the Commission. Under this proposal,

consumers will pay more in surcharges than is credited against existing transmission rates.

Absent any effort by the Commission to determine the exact level of depreciation over time for the existing facilities owned by the Transmission Owner, as well as the increase in volumes transacted on that system over this same period, combined with the fact that the TOs will retain a portion of the surcharge revenues, the Commission and customers cannot ensure that existing rates are just and reasonable for this Transmission Owner. Where consumers do not receive a full offset of the revenues they will pay under the surcharge, full harmonization is not achieved.

There is no reasonable basis to believe that the revenues produced by any surcharge designed to recover new investment costs will exactly match the decrease in costs associated with existing facilities that stem from depreciation or increased volumes transacted across that system. This is especially true where not all surcharge revenues will be used to offset existing rates. If the PJM TOs are permitted to retain any portion of the surcharge revenues, absent a Section 206 investigation under Option 2 to refresh each Transmission Owner's existing rates, it is likely that utilities will over-recover their costs.

Second, the harmonization remedy proposed by the PJM Transmission Owners under Option 2 is too simplistic an approach to the problem. The proposed remedy fails to capture the nuances of the PJM RTEP process that allows PJM to allocate the costs of new investments to customers of Transmission Owners located in zones other than the Transmission Owner(s) constructing the new facilities. Schedule 12 of the RTEP allows PJM to allocate the costs of the new facilities constructed in response to a PJM order to any zone determined to benefit from the new facilities. Beneficiary zones may well be zones other than those associated with the Transmission Owner(s) constructing the facilities. In cases where the costs of the new facilities are allocated to a zone other than the zone owned by the Transmission Owner undertaking the

construction, crediting the surcharge revenues to the constructing Transmission Owner does nothing to ensure that the existing rates of those customers paying the surcharge have been harmonized.

The PJM Transmission Owners might argue that the question of whether the total cost paid by customers in this situation is reasonable will be a matter for state commission resolution. This argument contains no merit. State commissions only regulate the retail rates of Transmission Owners. Under the Filed Rate Doctrine, the state commissions may not be able to disallow surcharge rates approved and imposed by this Commission. Consequently, the proposed harmonization mechanism under Option 2 does not in fact harmonize rates or redress the over-earnings concerns of consumers in a situation where costs of new facilities are regionalized and allocated to a zone other than the zone of the Transmission Owner constructing the facilities.

The goal, and the Commission's central responsibility, is to protect consumers from paying unjust and unreasonable rates. This obligation becomes more complicated where regionalization of new investment costs is involved, and where the TOs wish to retain a portion of the surcharge revenues through any ROE incentive adders. The Commission should reject the proposed surcharge credit mechanism as an unacceptable method of harmonizing existing and surcharge rates under Option 2.

Scope of Facilities Covered By Schedule 12 in Docket No. ER05-513

9. Joint Consumer Advocates further protest the filing in Docket No. ER05-513 on grounds that the TOs attempt to sweep too broad a category of new investment in transmission facilities into the Schedule 12 process. PJM and the TOs do not differentiate between new facilities constructed in accordance with the Schedule 12 RTEP process and those constructed

solely in accordance with the desires of the TOs. The Schedule 12 process only covers those new transmission projects approved by PJM as part of the RTEP process. TOs sometimes do construct additional projects that have not been subject to the regional planning process and approval by PJM. That latter class of facilities should not be part of this surcharge recovery mechanism as they are not provided for in the Schedule 12 process approved by the Commission.

Return on Equity and Customer Protection Issues in Docket No. ER05-515

10. Joint Consumer Advocates also protest the BG&E and PHI Companies' filing at Docket No. ER05-515 on grounds that the rate formula proposed may be unjust and unreasonable and does not provide sufficient protection for consumers. Sections 205 and 206 of the Federal Power Act require that rates for monopoly transmission services be filed and approved by the Commission as just and reasonable. The Commission has in the past used formula rates to comply with these requirements. The end result, whether a stated rate, or a formula rate, must ensure that consumers pay only just and reasonable rates. The formula proposed by BG&E and the PHI Companies does not comply with this requirement.

First, the formula may be unjust and unreasonable because it allows recovery of costs that may be inappropriate. The Commission should thoroughly investigate the formula proposed to ensure that each category of cost included is appropriate for recovery from consumers.

Second, the formula is devoid of any protections that will ensure that only prudent costs are passed through the formula. Under stated rates, consumers retain rights to protest a utility filing and challenge the prudence, propriety and application of the rates stated therein. The formula proposed by BG&E and the PHI Companies is not premised on limiting the costs that flow through the formula to only prudently incurred costs. Additionally, the Companies propose to post notice of the new formula rates on their OASIS websites, but do not propose to file the

annual changes in the formula rates with the Commission. The Companies do not propose to provide consumers access to any method to verify the data input into the formula each year, or to provide a forum in which consumers can challenge such inputs as not in conformance with the formula. Joint Consumer Advocates submit that the Commission at a minimum require BG&E and the PHI Companies to modify the formula to adopt the essential consumer protection protocols set forth in the Joint Protest filed this same day in this same docket by the Customers and Officials for Sensible Transmission (“COST”) ad-hoc coalition.

Third, Joint Consumer Advocates protest the Return on Equity (“ROE”) included in the formula rates. The ROE authorized any utility is often a highly controversial issue in rate cases and is almost always an issue set for hearing due to the disputed facts involved in developing this subjective cost element of utility rates. The ROE sought by BG&E and the PHI Companies has not been shown to be just and reasonable. These Companies seek an ROE of 14.5%, well above the range of reasonable returns recently authorized by the Commission for utilities of similar risks. The proxy group used by the Companies to calculate their proposed ROE is also subject to dispute, as it contains companies that Joint Consumer Advocates would dispute are similar in risk to BG&E and the PHI Companies. The calculation of dividend yields and growth rates are another area of subjective judgment in the selection of data inputs into the DCF model used to calculate returns for electric utilities. Joint Consumer Advocates submit that the data inputs used by BG&E and the PHI Companies produce unreasonable and excessive results for the ROE calculation.

Finally, Joint Consumer Advocates protest the ROE incentive adders. BG&E and the PHI Companies seek two incentive adders, a 50 basis point adder for joining an RTO and a 100 basis point adder for constructing new transmission. Neither adder is warranted for these

Companies under this proposal. Both Companies have been members of PJM for decades. While that participation predates the development of RTOs, PJM has since the late 1960s coordinated operation and management of the transmission systems of these and other electric utilities throughout the PJM region, including the economic dispatch of the generation owned by PJM members. The conversion of PJM from a tight power pool to an Independent System Operator (“ISO”) in 1996, and from an ISO to an RTO in 2000, was undertaken by these TOs because it was in their best interest and to their benefit to coordinate wholesale competitive market activities. Additionally, both events occurred long before the Commission issued its Proposed Policy Statement on transmission incentives that proposed a 50 basis point ROE adder to encourage utilities in non-RTO regions to join an RTO. Incentives can be awarded only when some consumer benefit will be attained thereby. *City of Detroit v. Federal Power Commission*, 230 F2d. 810, 817 (D.C. Cir. 1955). The proposal for the 50 basis point ROE adder fails this test.

Nor is the 100 basis point ROE adder reasonable. The formula rate mechanism in and of itself provides an incentive to the utilities by ensuring annual recovery of all costs associated with existing and new facilities. In fact, since the formula will include the costs associated with new investment still under construction and anticipated to be completed within the year that the formula rates are in effect, the mechanism provides incentive to undertake the construction. No additional incentive is warranted. Certainly the 100 basis point ROE adder should not be provided for construction undertaken for reliability reasons or in response to a direct order from PJM under the RTEP process to upgrade the system. Since such construction is a part of the TO’s obligation voluntarily undertaken in agreeing to be a PJM member, providing additional

incentive will not produce additional benefits for consumers. As discussed above, *City of Detroit* requires that any incentive awarded must provide targeted consumer benefits.

The ROE incentive adders should further be rejected as an unwarranted interference with, and distortion of, the economic transmission planning process in Schedule 12 of the PJM tariff. Schedule 12 allows PJM to order the construction of new transmission where the benefits of the upgrades in foregone economic congestion costs exceed the cost of the upgrades. Additionally, the RTEP process allows a variety of solutions to congestion and reliability problems to compete, including generation, transmission and demand side solutions. Providing the ROE incentive adders for the transmission solution distorts the evaluation of the alternative, competitive solutions by imposing additional costs on the transmission solution. Thus, while the transmission solution may in fact be the less expensive alternative without the ROE incentive adders, uneconomic generation may be constructed instead because the generation solution may appear less expensive due solely to the ROE incentive adders.

Allowing ROE incentive adders may also distort the cost benefit analysis in the economic transmission process. If the ROE incentive adders are not factored into the cost benefit analysis undertaken by PJM, consumers may be faced with a transmission solution that is not the least expensive alternative if the ROE incentive adders inflate the end result project cost above the cost of a generation solution. If the ROE incentive adder is included in the cost benefit analysis, then the problem discussed above occurs, where transmission that may be the least cost solution without the adders, becomes less attractive in comparison to a generation project. Under either scenario, the cost comparison is distorted and consumers are not assured that the least cost solution is selected. The Commission should reject these ROE incentive adders.

11. Joint Consumer Advocates reserve the right to raise additional issues during the course of these proceedings.

WHEREFORE, Joint Consumer Advocates respectfully request that the Commission a) reject Option 2 in PJM's and TOs' filing at Docket No. ER05-513-000 as inconsistent with the Commission's orders and the Settlement in Docket No. ER04-156-00; b) reject BG&E's and the PHI Companies' filing at Docket No. ER05-515-000, or modify that filing to include the consumer protection provisions discussed herein, to lower the return on equity authorized and to reject the Return on Equity incentive adders; or c) in the alternative set both filings for full evidentiary hearing.

Respectfully submitted,
/s/ filed electronically

/s/ filed electronically

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CERTIFICATE OF SERVICE

PJM Interconnection, L.L.C. : Docket No. ER05-513-000

Baltimore Gas and Electric Company and : Docket No. ER05-515-000
PEPCO Holdings, Inc. Operating Affiliates :
Potomac Electric Power Company; :
Delmarva Power & Light Company, :
And Atlantic City Electric Company :

(Not Consolidated)

I hereby certify that I have this date served the foregoing document upon each person designated on the official service list compiled by the Secretary in the above-referenced proceeding, in accordance with Rule 2010 of the Commission's Rules of Practice and Procedure.

Dated at Harrisburg, PA this 22nd day of February, 2005.

Respectfully submitted,

/s/ filed electronically

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