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May 23, 2023

Andrew Johnston, Executive Secretary
Maryland Public Service Commission
6 St. Paul Street, 16th Floor
Baltimore, Maryland 21202

Re: Case No. 8797 – OPC Request for Evidentiary Hearing on Potomac Edison Petition for Consent and Approval to Terminate PURPA Contract with AES WR Limited Partnership

Dear Mr. Johnston:

The Office of People's Counsel understands that the Commission intends to hold a legislative-style hearing on May 31, 2023 concerning the Petition for Consent and Approval to Terminate PURPA Contract with AES WR Limited Partnership filed by Potomac Edison in this matter on April 17, 2023. For the reasons set forth below, OPC respectfully requests that the Commission cancel this hearing and instead schedule an evidentiary hearing on the matter no earlier than June 12, 2023.

Background of Potomac Edison-AES Warrior Run, LP PURPA Contract

The contract that PE's petition concerns is an Electric Energy Purchase Agreement ("EEPA") entered into by PE and AES WR Limited Partnership ("WR") under the Public Utility Regulatory Policies Act of 1978 ("PURPA").[1]

PURPA was enacted amidst the energy turmoil of the 1970s to encourage smaller-scale, non-utility owned electric power generation, as well as cogeneration facilities. At the time, most electric power generation in the United States, including in Maryland, was owned by electric utilities. PURPA required—and continues to require—utilities to buy electric power from "Qualifying Facilities" ("QFs") at "the incremental cost to the electric utility of alternative electric energy,"[2] which is "the cost to the electric utility of the electric energy which, but for the purchase from such cogenerator or small power

[1] 16 U.S.C. § 2601 et seq.
[2] 16 U.S.C. § 824a-3(b).

producer, such utility would generate or purchase from another source."[3] The cost that utilities are required to pay QFs is often described by the shorthand, "avoided cost."

Under the Federal Energy Regulatory Commission regulations in place at the time the EEPA between PE and WR was executed in 1988, a QF could elect to have a utility's avoided cost rate calculated in either of two ways: (1) through a determination made at the time the QF delivered power to the utility (resulting in a variable rate that fluctuated with the utility's actual avoided costs), or (2) through a contract or other legally enforceable obligation ("LEO") that fixed the avoided cost rate for a period of time going forward.[4]

According to the EEPA, "although the Project is to be a 'qualifying facility' within the meaning of PURPA… Buyer and Seller have negotiated and reached agreement upon the terms and conditions hereof (including those as to price) by arm's-length negotiations without regard for the specific provisions and requirements of PURPA…" In practical terms, the EEPA determines the price for PE's electric power purchases from WR through complex formulas based in part on the price of power generated by "proxy units" formerly owned by Allegheny Power System, Inc., (PE's former holding company), which merged with FirstEnergy in 2011. At least since Allegheny Power joined PJM Interconnection, L.L.C., these formulas have had little to do with PE's actual avoided costs.[5]

When restructuring occurred after Maryland's enactment of the Electric Customer Choice and Competition Act of 1999, the Commission approved a settlement agreement concerning the recovery of PE's WR costs whereby, starting on July 1, 2000, the surcharge that PE was already using to collect WR-related costs would be set equal to the amount that PE was required to pay WR under the EEPA, less payments PE received from selling WR's energy, capacity, and ancillary services output on the wholesale market.[6]

Under this arrangement, PE has paid much more for WR's power over the last 22 years than PE would have paid buying an equivalent amount of power on the PJM wholesale electricity markets. As PE has acknowledged in its petition:

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[3] 16 U.S.C. § 824a-3(b)(1)-(2).
[4] *See* FERC Order No. 872-A in Docket Nos. RM19-15-001 and AD16-16-001, Qualifying Facilities Rates and Requirements – Implementation Issues under the Public Utility Regulatory Act of 1978 (November 19, 2020) at par. 47-48.
[5] To the extent that the EEPA bases PE's avoided costs on something other than the cost of delivered energy, it is similar to a long-term contract that fixes a utility's avoided costs. In its 2020 PURPA rulemaking, FERC revised its PURPA regulations to authorize states to prohibit these types of contracts. FERC reasoned that "it is inevitable that, over the life of a QF contract or other LEO, a fixed avoided cost energy rate, such as that used in past years, will deviate from actual avoided costs." FERC Order No. 872-A, *id.,* at par. 76.
[6] Order No. 75851.

> …while the WR Project EEPA has provided energy, capacity and some ancillary services to PE for resale on behalf of its customers, the cost of the agreement to PE's customers has been excessive as compared to other available sources. Through calendar year 2022, the WR Project EEPA has cost PE customers nearly $1.3 billion (the difference between payments to the WR Project versus revenues received from the market sales for the facility output).[7]

In short, the terms of the EEPA that PE and WR negotiated in 1988 have led to PE's overpaying for WR's output—to the benefit of WR and the detriment of PE's customers.

PE's Petition to Terminate PURPA Contract

On March 23, 2023, PE and WR entered into an agreement to terminate the EEPA ("termination agreement"). Under the agreement, PE would pay WR $357 million to be relieved of its contractual obligations to buy power from WR. The $357 million would be paid in 78 monthly installments of $4.5777 million from July, 2023 to December, 2030.

According to PE's petition, WR was willing to negotiate the termination of the EEPA – which, again, has been a very lucrative contract for WR – because in 2022, AES, the parent company of WR, stated its intent to exit the coal generation business by 2025. PE argues that the Commission should approve the termination agreement because PE's forecast of PJM market conditions has PE's customers paying $79 million less under the termination agreement between July, 2023 and the end of 2030 than they would pay if the EEPA remained in place. PE supports it contention that the termination agreement will save its customers money with a financial analysis based on a financial model it created. PE has also provided a report by Levitan & Associates, Inc. ("LAI") that "confirms[s] that the conclusion of the Potomac Edison financial modeling and analysis that the expected present value of the Net Buyout Benefit is positive, significant and provides benefits to Potomac Edison's ratepayers."[8]

PE also contends that fixing PE's contractual obligation to WR at $4.5777 million per month will benefit PE's customers by stabilizing the amount of the WR surcharge they pay on their monthly bills. Currently, the surcharge is adjusted annually because the revenue that PE receives from bidding WR's power into the PJM markets (and therefore the difference between those revenues and the larger amounts that PE pays to WR under the EEPA) goes up and down, based on market conditions.

[7] Petition, at 5.
[8] LAI, Warrior Run EEPA Termination Financial Analysis Review (April 3, 2023) at 8.

Importantly, the termination agreement contains a self-destruct provision: it states that the agreement will itself "terminate and have no effect" at 11:59:59 PM on June 30, 2023 in the absence of, among other things, "an order by the MD PSC acceptable to Potomac Edison approving the termination of the Project Documents pursuant to this Termination Agreement and providing full cost recovery to Potomac Edison for the costs, including its costs of capital, related to the termination for which Potomac Edison has theretofore sought or will seek recovery."[9]

In mid-March, Potomac Edison gave notice to OPC that it was in negotiations with WR concerning a buyout of the EEPA, and on April 10 and 13 PE provided Staff and OPC with drafts of two direct testimonies and supporting exhibits, along with the supporting LAI report on April 10 and April 13.

On April 17, 2023, PE filed the petition, along with three direct testimonies and supporting exhibits and the supporting LAI report.

On April 19, 2023, OPC entered its appearance in this matter. On April 28, OPC served its first set of data requests on PE. On May 11, OPC secured the services of a consultant to assist in the review of the petition, and thereafter served two additional sets of DRs on PE, on May 15 and May 19. In light of the fact that OPC's DRs included several questions about the WR Project that PE was unable to answer, OPC also served a set of DRs on WR. (WR has informed OPC that it will not answer those DRs because it is not a party to this matter).

On May 1, 2023, Montgomery County entered its appearance. On May 2, 2023, outside counsel for PE filed a motion for admission Pro Hac Vice.

On May 19, OPC learned from a review of the draft agenda for the Commission's May 31, 2023 administrative meeting that the Commission had included PE's petition on that agenda. On May 22, in response to an inquiry by OPC, the Executive Secretary of the Commission advised OPC and the other parties to this proceeding that the Commission would hold a legislative-style hearing on May 31.

Need for and Timing of an Evidentiary Hearing

[9] PE's petition does not explain why PE and WR chose a self-termination date so soon after the date the termination agreement was executed. The Direct Testimony of Robert B. Reeping states that "[e]ven assuming both parties are amenable [to renegotiating the contract after June 30], it would require the parties to … to determine a new price due to the delay in the transaction closing, which would almost certainly impact the value proposition for the Company's customers. It would also keep PE's customers at risk to the market and operations which could lead to a more significant loss than under the proposed recommendation herein." Reeping, at 8-9.

OPC requests that the Commission cancel the legislative-style hearing scheduled for May 31 and instead schedule an evidentiary hearing on June 12 or later, because discovery in this matter is ongoing and OPC believes, based on the discovery conducted so far, that there will be disputed issues of fact in this matter. OPC's expert witness will not be available to testify in person before the Commission until starting on Monday, June 12.

Since receiving actual notice from PE about the petition, OPC has worked diligently to review and analyze the petition and conduct discovery within the artificial time constraint created by the termination agreement's self-termination provision. OPC expects to receive answers to its second and third set of DRs to PE on Thursday, May 25 and Tuesday, May 30, respectively. With the benefit of those answers, OPC believes that it will be in a position to complete its analysis of the termination agreement and PE's supporting financial modeling, and so to take a position supporting or opposing PE's petition. Based on its review of PE's financial analysis to date, OPC anticipates that that there will be disputed issues of fact in this matter and that it will seek to introduce expert testimony on those issues.

Significantly, PE's contention that the termination agreement will save PE's customers money is premised on the WR Project's continuing to operate profitably through 2030 essentially in the same way it has operated for the last two decades. This premise rests on assumptions that require evaluation, given the age of the plant, the poor economics of coal generation in the PJM market, and recent changes to PJM's capacity market—not to mention the stated intent of AES to exit coal generation by 2025.

The $357 million that PE proposes to pay WR under the termination agreement is a very large sum of money. According to PE, the payment is justified by the results of complicated financial modeling and power market forecasting. Indeed, that modeling and forecasting provide the main basis for PE's conclusion that the termination agreement will have a net benefit for PE's customers. In these circumstances, it would be insufficient for the Commission to consider and rule on PE's petition through a legislative-style hearing. Due process requires an adequate opportunity for OPC—on behalf of residential customers who will be footing most of the $357 million price tag—to evaluate and potentially challenge PE's analyses. Moreover, OPC believes that the Commission needs such a presentation of evidence to determine whether PE's petition will result in just and reasonable rates for PE's customers. Accordingly, the Commission should hold a full evidentiary hearing where OPC can present the testimony of its expert witness and cross-examine PE's witnesses.

OPC further requests that the Commission invite WR to attend the evidentiary hearing and answer questions. PE's contention that the termination agreement will save PE's customers money is premised on the WR Project's continuing to operate through 2030 if the EEPA remains in place. Given the age of the plant, the poor economics of

coal generation in the PJM markets, and recent changes to PJM's capacity market, it is possible that the WR Project may become uneconomical between now and 2030 even with the EEPA payments. In that case, the Commission's approval of the termination agreement would amount to a massive ratepayer-funded windfall for WR. Therefore, the Commission should ask WR to appear before it to show why this premise is justified.

Thank you very much.

Sincerely,

/electronic signature/
Mark Szybist
Assistant People's Counsel

Encl.
cc: all parties of record
cc: Brian Quinn, Esq, attorney for AES Warrior Run Limited Partnership