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PUBLIC SERVICE COMMISSION OF THE DISTRICT OF COLUMBIA
1325 G STREET, N.W., SUITE 800
WASHINGTON, D.C. 20005

OPINION AND ORDER

August 27, 2015

FORMAL CASE NO. 1119, IN THE MATTER OF THE JOINT APPLICATION OF EXELON CORPORATION, PEPCO HOLDINGS, INC., POTOMAC ELECTRIC POWER COMPANY, EXELON ENERGY DELIVERY COMPANY, LLC AND NEW SPECIAL PURPOSE ENTITY, LLC FOR AUTHORIZATION AND APPROVAL OF PROPOSED MERGER TRANSACTION, Order No. 17947

Before the Commission:

Betty Ann Kane, Chairman
Joanne Doddy Fort, Commissioner
Willie L. Phillips, Commissioner

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THEREFORE IT IS ORDERED THAT: 171

OPINION OF COMMISSIONER WILLIE L. PHILLIPS, CONCURRING,
IN PART, AND DISSENTING, IN PART, FORMAL CASE NO. 1119,
ORDER NO. 17947 1

I. INTRODUCTION

1. By this Order, the Public Service Commission of the District of Columbia ("Commission") determines that the Joint Application as filed for approval by the Commission, pursuant to D.C. Code §§ 34-504 and 34-1001, for a change of control of the Potomac Electric Power Company ("Pepco") to be effected by the Proposed Merger of Pepco Holdings, Inc. ("PHI") with Purple Acquisition Corp. ("Merger Sub"), a wholly-owned subsidiary of Exelon Corporation ("Exelon") ("Joint Application") filed by Exelon, PHI, Pepco, Exelon Energy Delivery Company, LLC ("EEDC"), and New Special Purpose Entity, LLC ("SPE") (collectively, the "Joint Applicants") is not in the public interest and, therefore, is **denied**.

2. On April 30, 2014, Exelon Corporation announced Exelon's purchase of PHI. On June 18, 2014, the Joint Applicants filed a Joint Application for approval by the Commission, pursuant to D.C. Code §§ 34-504 and 34-1001, for a change of control of Pepco (the "Proposed Merger"). Upon completion of the Proposed Merger, Exelon would become the sole owner of PHI and PHI's subsidiaries, including Pepco, and Pepco would be controlled in the future by Exelon under a management structure that is described in detail in this Order.

3. In this proceeding, the Commission must decide who will control the District's only local electric distribution company at a time when our city's leadership, at the urging of many residents, has mandated that the District must pursue a cleaner and greener future that includes more renewable energy resources and more distributed generation and at a time when the electric industry is undergoing significant transformation. The proposed change in ownership and control of Pepco must also be decided in the context of the public policy contained in District law that requires the electric company to be focused on distribution only, and to operate in a safe and reliable manner on a nondiscriminatory basis for all customers and suppliers.

4. This proceeding has generated more interest and more active participation by parties and interested persons than any other proceeding in the Commission's more than a century of operations. We fully respect, and have carefully considered, the submissions of the many parties and commenters, including the Government of the District of Columbia, the Office of the People's Counsel, the General Services Administration, DC Water, the solar and wind advocates, the consumer advocates, the Advisory Neighborhood Commissions ("ANCs"), members of the Council of the District of Columbia ("District Council"), and the interested persons who participated in our community hearings. Most of these parties and interested persons opposed the transaction and asked the Commission to deny the application. Failing that, the parties asked the Commission to impose conditions that would mitigate their concerns.

5. As we have been reminded throughout this process, this decision is one of the most significant decisions that the Commission will ever make. Unlike a rate case, this decision will affect a permanent change in the ownership and control of the District's local electric distribution company. A rate case decision lasts only until the next rate case. This decision is forever.

6. It is a decision that the Commission must make based on the record before it, not based on aspirational goals that cannot be demonstrated. The Joint Applicants had full

knowledge of the concerns and proposed solutions of the parties, as well as the questions raised by the Commission at the evidentiary hearings, in bench requests for further information and in data requests. The Joint Applicants were free to meet together with the parties to see if their objections could be resolved and a settlement could be reached. By law, the Commission staff is not a party to the case, only advisory to the Commission, and could not participate in such settlement discussions. Nevertheless, there was no settlement brought to the Commission that would have evidenced general agreement on those mitigating factors which would have satisfied the concerns of the parties. At the close of the record, in positions taken in the final briefs, the position of opponents to the Proposed Merger did not change, even as the Joint Applicants added additional commitments as a result of settlements reached in other jurisdictions to address concerns that were raised. Therefore, we consider the Joint Application as it stands on this record, not as it might have been proposed.

7. Cognizant of the statutory obligations placed on the Commission, we considered the effect of the Proposed Merger on the following seven factors to determine if the Proposed Merger is in the public interest:

> [T]he effects of the transaction on: (1) ratepayers, shareholders, the financial health of the utilities standing alone and as merged, and the economy of the District; (2) utility management and administrative operations; (3) public safety and the safety and reliability of services; (4) risks associated with all of the Joint Applicants' affiliated non-jurisdictional business operations, including nuclear operations; (5) the Commission's ability to regulate the new utility effectively; (6) competition in the local retail, and wholesale markets that impacts the District and District ratepayers; and (7) conservation of natural resources and preservation of environmental quality.[1]

We also informed parties that because the circumstances of each merger are unique, every public interest factor may not be relevant or weighed equally from one merger to another.

8. In the Standard of Review Section of this Order, we explain how we will use the findings from our review of the effects of the Proposed Merger on the seven public interest factors to assess the transaction as a whole and make the public interest determination that is required by D.C. Code §§ 34-504 and 34-1001. We must find that the Proposed Merger benefits the public rather than merely leaves it unharmed, balancing the interests of shareholders and investors with the interests of ratepayers and the District community at large.

9. Throughout the proceeding, the Joint Applicants have argued that they have clearly shown that the Proposed Merger is in the public interest under the various public interest

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[1] *Formal Case No. 1119, In the Matter of the Joint Application of Exelon Corporation, Pepco Holdings, Inc., Potomac Electric Power Company, Exelon Energy Delivery Company, LLC and New Special Purpose Entity, LLC for Authorization and Approval of Proposed Merger Transaction* ("*Formal Case No. 1119*"), Order No. 17597, ¶ 124, rel. August 22, 2014.

factors and the precedents set by this Commission. They have put forth arguments to counter each of the criticisms and concerns raised by the parties as well as by the thousands of interested persons who have voiced their opposition to placing the control of Pepco into the hands of the management of a diversified utility holding company that receives 63% of its revenues from generation assets. As the proponent of the proposed transaction and the approval order that is being sought, the Joint Applicants bear the burden of persuasion.[2]

10. The bulk of this order contains our review, analysis, and findings with respect to the effect of the Proposed Merger on each of the seven public interest factors. For the reasons that we set out in this order, we find that the impact of the Proposed Merger is a mixed one. There are a few elements of the Proposed Merger that produce a clear direct and tangible benefit --most notably the $1.6 billion premium that would be paid to current PHI shareholders to buy out the interest of the current PHI shareholders at no cost to District ratepayers and the offer of a $33.75 million Customer Investment Fund ("CIF") (*i.e.*, the equivalent of $128 per ratepayer according to the Joint Applicants' customer meter count for the District -- a count that we call into question in this Order) which could be used by the Commission to fund a beneficial purpose of the Commission's choosing.[3] While the Joint Applicants have persuaded the Commission that not everything that has been argued by the opponents of the Proposed Merger is true, the record in this proceeding persuades us that there are a number of effects of the Proposed Merger that are neither beneficial nor harmful, that is, they are neutral. There are also some effects of the Proposed Merger that are harmful or that have a reasonable potential for harm. For example, we found no benefit in the offer of increased reliability at a capped cost because it offers no increased reliability under our Electric Quality of Service Standards; rather, it relies on the increased reliability of the DC PLUG initiative that began before the Merger Application was submitted and it has terms and conditions that have already voided the cap that was offered. Similarly, we found no benefit to District ratepayers in a new management structure that did not include the Pepco Region President in the Executive Committee for Exelon Utilities, thereby diminishing the influence of Pepco within the new structure and that would result in a more complex regulatory structure that would negatively impact the Commission's ability to regulate Pepco. Pepco will become a second tier company in a much larger corporation whose primary interest is not in distribution, but in generation. At a time of change in the energy field, Pepco's ability to adapt will be constrained by an increased management bureaucracy. We are also

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2 *See People's Counsel of the District of Columbia v. Public Service Commission of the District of Columbia*, 474 A.2d 835, 837 (D.C. 1984) (the proponent of an order bears the burden of persuasion); *Washington Public Interest Organization v. Public Service Commission of the District of Columbia*, 393 A.2d 71, 77 (D.C. 1978) (the D.C. Court of Appeals has interpreted the phrase "burden of proof" to mean burden of persuasion); D.C. Code § 2-509 (b) (2001) ("In contested cases, except as may otherwise be provided by law, other than this subchapter, the proponent of a rule or order shall have the burden of proof.").

3 *See Formal Case No. 1119*, Order No. 17530, ¶ 26, rel. June 27, 2014, citing *Formal Case No. 1002, In the Matter of the Joint Application of Pepco and the New RC, Inc. for Authorization and Approval of Merger Transaction* ("*Formal Case No. 1002*"), Order No. 12395, ¶ 17, rel. May 1, 2002; and *Formal Case No. 951, In the Matter of the Joint Application of BG&E, Pepco and Constellation Energy for Authorization and Approval of Merger* ("*Formal Case No. 951*"), Order No. 11075, pp. 17-18, rel. October 20, 1997; *Formal Case No. 1119*, Order No. 17597, ¶ 88, rel. August 22, 2014.

concerned about the inherent conflict of interest that might inhibit our local distribution company from moving forward to embrace a cleaner and greener environment.

11. Consequently, when this Proposed Merger is considered as a whole, for all of the reasons set forth in our Order, we conclude that the Joint Applicants have not met their burden of persuading this Commission that the Proposed Merger is in the public interest under D.C. Code §§ 34-504 and 34-1001. Therefore, the Joint Application is denied.

II. BACKGROUND

12. This Order's Background section consists of a description of the Joint Applicants, a description of the Proposed Merger, a summary of the procedural history of *Formal Case No. 1119*, and, finally, a summary of the four community hearings in this case and public comments filed on the record of this case by non-parties.

A. Description of the Joint Applicants

13. PHI is the public utility holding company that was created in 2002 as a result of the merger of Pepco and Conectiv.[4] PHI directly and indirectly owns three electricity and natural gas distribution utilities. PHI directly owns Pepco, a District of Columbia and Virginia corporation with its headquarters in the District of Columbia, which has 264,000 electric customers in the District and 537,000 customers in Montgomery and Prince George's Counties in Maryland.[5] PHI indirectly, through its Conectiv subsidiary, owns Delmarva Power & Light Company ("Delmarva Power") and Atlantic City Electric Company ("ACE"), which together serve approximately 1 million electric customers and 126,000 natural gas customers.[6] In addition, PHI, through Pepco Energy Services, Inc. and its subsidiaries (collectively, "PES"), provides energy efficiency and other energy-related services.

14. Exelon is a utilities services holding company, which, through its subsidiaries, both generates electricity and delivers electricity and natural gas to customers.[7] Exelon was formed in 2000 by the merger of PECO Energy Company ("PECO") and Unicom Corporation, the parent of Commonwealth Edison Company ("ComEd"). In 2012, Exelon merged with Constellation Energy Group, Inc. ("Constellation"), which added Baltimore Gas and Electric ("BGE") to the Exelon family of companies. Exelon operates through its principal subsidiaries, Exelon Generation Company, LLC ("Exelon Generation") and a family of three public utility companies.

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4 *Formal Case No. 1119*, Joint Application of Exelon Corporation, Pepco Holdings, Inc., Potomac Electric Power Company, Exelon Energy Delivery Company, LLC and New Special Purpose Entity, LLC for Authorization and Approval of Proposed Merger Transaction, p. 3, filed June 18, 2014 ("Joint Application").

5 *Formal Case No. 1119*, Joint Application at 5 and Exhibit 4.

6 *Formal Case No. 1119*, Joint Application at 5 and Exhibit 4.

7 *Formal Case No. 1119*, Joint Application at 3.

15. Exelon Generation, a wholly owned subsidiary of Exelon Ventures Company, LLC conducts Exelon's generation business includes its generation fleet, wholesale energy marketing operations and a competitive retail sales business. Through various subsidiaries, Exelon Generation is also a retail competitive energy provider. Exelon Nuclear, a division of Exelon Generation, operates the largest fleet of nuclear plants in the nation. The fleet consists of 23 reactors at 14 locations in Illinois, Maryland, Nebraska, New Jersey, New York, and Pennsylvania.[8]

16. EEDC is the Exelon subsidiary that directly and indirectly owns three regulated electricity and natural gas distribution companies. EEDC directly owns 100 percent of the common stock of ComEd and PECO, and indirectly, through RF Holdco, LLC, owns 100 percent of the common stock of BGE.[9] RF Holdco LLC, which owns BGE, is a bankruptcy remote special purpose entity created specifically to "ring-fence" BGE. SPE is "a bankruptcy-remote special purpose entity being created to ring-fence PHI and PHI's energy distribution utilities," which is similar in structure to RF Holdco, LLC.[10] Together these Exelon-owned energy delivery companies – ComEd, PECO, and BGE – provide distribution service to $6.6 million electric customers in Illinois, Pennsylvania, and Maryland.[11]

17. Merger Sub is a Delaware corporation and a wholly owned subsidiary of Exelon that was formed for the sole purpose of effecting the Merger. Upon completion of the Merger, Merger Sub will be merged into PHI and cease to exist as a separate legal entity.[12]

B. The Proposed Merger Transaction

18. On April 30, 2014, Exelon announced Exelon's purchase of PHI. On June 18, 2014, the Joint Applicants filed the Joint Application for approval by the Commission, pursuant to D.C. Code §§ 34-504 and 34-1001, for a change of control of Pepco to be effected by the Proposed Merger of PHI with Merger Sub, a wholly owned subsidiary of Exelon.[13]

19. Exelon, PHI, and Merger Sub are parties to an Agreement and Plan of Merger ("the Proposed Merger Agreement") under the terms of which PHI will merge with Merger Sub and, as the surviving corporation, PHI will become an indirect, wholly owned subsidiary of Exelon, and PHI's stock will no longer be publicly traded.[14] Specifically, PHI will become the subsidiary of SPE, and SPE will be a subsidiary of EEDC, which owns Exelon's regulated public

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8 *Formal Case No. 1119*, Joint Application at 4.

9 *Formal Case No. 1119*, Joint Application at 3.

10 *Formal Case No. 1119*, Joint Application at 3.

11 *Formal Case No. 1119*, Joint Application at 4.

12 *Formal Case No. 1119*, Joint Application at 6.

13 *Formal Case No. 1119*, Joint Application at 1.

14 Joint Applicants (A) at 20:15-19 (Crane).

utility companies.[15] Upon completion of the Proposed Merger, PHI's subsidiaries will operate as part of Exelon's holding company system.[16]

20. The Proposed Merger is structured as an all-cash transaction for approximately $6.8 billion.[17] Upon consummation of the Proposed Merger, each PHI shareholder will receive $27.25 in cash for each outstanding share of PHI common stock not held by PHI, Exelon, Merger Sub, a PHI or Exelon affiliate, or a dissenting PHI stockholder properly asserting appraisal rights.[18] The common stock of Exelon will be unaffected by the Proposed Merger.[19] There will be no change in the outstanding debt of Pepco or PHI as a result of the Proposed Merger. The Joint Applicants have committed not to refinance PHI's currently outstanding long-term debt or have PHI issue new long-term debt.[20] PHI will continue to be able to issue preferred stock.

21. The Proposed Merger Agreement provides for a $180 million reverse break-up fee. Exelon will purchase up to $180 million of non-voting preferred stock in PHI. Under certain conditions, PHI will retain these proceeds if the Proposed Merger does not close. Through the date of the close of the evidentiary hearing, April 22, 2015, PHI had issued $144 million of non-voting preferred stock to Exelon. An additional $18 million of stock was issued on April 27, 2015, and an additional $18 million was issued on July 26, 2015.[21] The $144 million has been used as equity in the three utilities, for payment of commercial paper, or applied to fund PHI dividends.[22]

22. Following completion of the Proposed Merger, PHI will have a seven-member board of directors, including at least three independent directors as defined by New York Stock Exchange Rules. Of the four remaining directors, at least one shall be selected from among the officers or employees of PHI or a PHI subsidiary. The board will include three outside directors from the service territories of PHI's three utility subsidiaries.[23] The PHI board of directors will select Pepco's board of directors, and the Pepco board of directors, in turn, will choose Pepco's officers.[24] Mr. David Velazquez, currently PHI's Executive Vice President – Power Delivery,

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15 *Formal Case No. 1119*, Joint Application at Exhibit 4; *see also* Joint Applicants (C) at 5:8-16 (O'Brien).

16 Joint Applicants' Br. at 10.

17 Joint Applicants (F) at 4:10 (Khouzami).

18 Joint Applicants (F) at 4:10-14 (Khouzami).

19 Joint Applicants (F) at 4:14-16 (Khouzami).

20 Joint Applicants (F) at 4:16-19 (Khouzami); Joint Applicants (4A)-2 at 7, Commitment 47.

21 Joint Applicants' Br. at 11.

22 Tr. at 3401:10-17 (Commission Cross of McGowan).

23 Joint Applicants (4A)-2 at 6, Commitment 38; Joint Applicants (C) at 7:2-4 (O'Brien).

24 Joint Applicants (3C) at 14:8-11 (O'Brien).

will serve as CEO and President of PHI upon current PHI CEO Joseph M. Rigby's retirement after closing of the Proposed Merger.[25] Mr. Christopher M. Crane will continue to serve as CEO and President of Exelon following the Proposed Merger.[26]

23. On or about the effective date of the Proposed Merger, PHI will be converted from a corporation to a limited liability company or "LLC," and PHI will no longer be a publicly traded company.[27] As a consequence, a number of corporate functions associated with its public status (*e.g.*, investor relations) will no longer be performed at the PHI level.[28] However, PHI and Pepco will continue to maintain headquarters in the District of Columbia at Edison Place, and the existing operational management structure of PHI will remain substantially the same.[29] PHI's senior management will generally continue to be PHI Service Company ("PHISCo") employees and will continue to establish priorities and respond to local conditions as they do today.[30] Pepco's local management will continue to have the authority and responsibility to develop Pepco's capital and Operations & Maintenance ("O&M") expense budgets, subject to the financial threshold levels specified in the Delegation of Authority ("DOA").[31] While Exelon's CEO and Executive Committee will review Pepco's budgets, the DOA reveals that the PHI Board of Directors (rather than the Pepco Board of Directors) will approve Pepco's budgets.[32]

24. The Joint Applicants submit that, upon consummation of the Proposed Merger, "Pepco will continue to operate within the District of Columbia as an electric public utility subject to the continuing jurisdiction of the Commission pursuant to the District of Columbia Public Utilities Act, as amended, D.C. Official Code §§ 34-101 et seq., and without any reduction in the Commission's existing oversight or authority over Pepco."[33] Thus, according to the Joint Applicants, the Proposed Merger will not adversely impact any of the day-to-day operations of Pepco, or the Commission's oversight of Pepco and will enhance the capabilities of Pepco to fulfill its obligation to provide safe, adequate and reliable service to its retail customers in the District of Columbia.[34]

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25 Joint Applicants (3C) at 9:17-18, 14:12-15 (O'Brien).

26 *Formal Case No. 1119*, Joint Application at 18.

27 Joint Applicants (C) at 6:22-23 (O'Brien).

28 Joint Applicants (A) at 20: 15-19 (Crane); Joint Applicants (C) at 7:8-12 (O'Brien).

29 Joint Applicants (4A)-2 at 3, Commitment 10; Joint Applicants (C) at 12:22-23 (O'Brien).

30 Joint Applicants (B) at 6:2-7:5 (Rigby); Joint Applicants (3C) at 9:19-10:5 (O'Brien).

31 Joint Applicants (4A)-2 at 4, Commitment 24; Joint Applicants (C) at 7.1:1-8:7 (O'Brien).

32 Joint Applicants (4A)-2 at 4, Commitment 24; Joint Applicants (C) at 7.1:1-8:7 (O'Brien).

33 Joint Applicants (4A)-2 at 14, Commitment 73; *see also* Section VI.E, *infra*, addressing Factor 5.

34 Joint Applicants' Br. at 12.

C. Procedural History

25. On June 27, 2014, in Order No. 17530, the Commission directed that: (1) any interested person desiring to formally intervene in this proceeding file a Petition to Intervene with the Commission no later than July 11, 2014;[35] (2) the Joint Applicants, the Office of the People's Counsel ("OPC" or "Office"), and any intervenors who chose to do so, were permitted to file a brief with the Commission on the issue of whether this case should be classified as a "rate case" or "other investigation" for purposes of D.C. Code § 34-912 on or before July 11, 2014 with reply briefs to be due on or before July 18, 2014;[36] (3) any party was permitted to file comments upon the six factors discussed in the Order and/or propose additional factors to be considered by the Commission in determining whether the Proposed Merger is in the "public interest" on or before July 18, 2014;[37] and (4) OPC and any intervenors were permitted to file comments on the Joint Applicants' proposed procedural schedule by July 18, 2014.[38]

26. On August 22, 2014, in Order No, 17597, the Commission: (1) granted and denied the Petitions to Intervene and Motions for Special Appearance as identified therein; (2) determined that this case should be classified as an "other investigation" as opposed to a "rate case" for purposes of D.C. Code § 34-912; (3) amended the public interest factors used to evaluate whether this Proposed Merger is in the public interest for the purpose of D.C. Code § 34-504 by amending four existing factors and adding a new seventh public interest factor; and (4) set forth the procedural schedule for this proceeding.[39] A five-day evidentiary hearing was scheduled to commence on January 5, 2015.

27. OPC is a statutory party of right and the following entities were granted party status: the Apartment and Office Building Association of Metropolitan Washington ("AOBA"); the District of Columbia Government ("District Government"); DC Solar United Neighborhood ("DC SUN"); District of Columbia Water and Sewer Authority ("DC Water"); U.S. General Services Administration ("GSA"); GRID2.0 Working Group ("GRID2.0"); Maryland DC Virginia Solar Energy Industries Association ("MDV-SEIA"); Mid-Atlantic Renewable Energy Coalition ("MAREC"); Monitoring Analytics, Inc., as the Market Monitor for PJM ("PJM Market Monitor"); the National Consumer Law Center, National Housing Trust and the National Housing Trust-Enterprise Preservation Corporation ("NCLC/NHT"); and NRG Energy, Inc. ("NRG").

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35 *Formal Case No. 1119*, Order No. 17530, ¶¶ 30, 36, rel. June 27, 2014.

36 *Formal Case No. 1119*, Order No. 17530, ¶¶ 29, 33, rel. June 27, 2014.

37 *Formal Case No. 1119*, Order No. 17530, ¶¶ 27, 34-35, rel. June 27, 2014.

38 *Formal Case No. 1119*, Order No. 17530, ¶¶ 28, 34, rel. June 27, 2014.

39 *Formal Case No. 1119*, Order No. 17597, ¶¶ 28, 34, rel. August 22, 2014.

28. On September 8, 2014, the District Government filed a Motion for Revision of Procedural Schedule.[40] On September 11, 2014, OPC filed its Application for Reconsideration of Order No. 17597.[41]

29. On September 19, 2014, the Joint Applicants filed Supplemental Direct Testimony in accordance with Order No. 17597.

30. On October 9, 2014, in response to the District Government's Motion and OPC's Application, the Commission issued Order No. 17654, which extended various procedural deadlines and moved the evidentiary hearing from January 5-9, 2015 to February 9-13, 2015.[42]

31. On November 3, 2014, OPC, AOBA, District Government, DC SUN, DC Water, GRID2.0, MAREC, Market Monitor, and NCLC/NHT filed their Direct Testimony. On December 17, 2014, the Joint Applicants filed Rebuttal Testimony.[43]

32. The Commission convened four (4) community hearings seeking input from the public on the Joint Application. The hearings were held between December 17, 2014, and January 20, 2015, at various times and locations throughout the District of Columbia.[44] The Commission also encouraged interested community members to submit written comments on the record until May 27, 2015, when the record in this matter closed. During the course of the four (4) community hearings, a total of 178 interested persons, including residential and commercial customers, vendors serving Exelon companies, non-profit organizations, various trade associations, and representatives of ANCs submitted oral testimony. A further, 3,207 interested persons, consisting of District residential; and commercial customers, some residents of Maryland and Virginia, vendors of existing Exelon companies, ANCs and members of the District Council submitted written testimony and comments during the course of this proceeding.

33. The bulk of the community comments expressed a general opinion on whether the Proposed Merger should be approved. Some of the comments discussed the effect of the transaction on one or more of the seven (7) factors being considered by the Commission in determining whether to approve the Proposed Merger, with the specific oral and written comments focused on four main issues: (1) the impact of the Proposed Merger on low-income ratepayers; (2) the impact of the Proposed Merger on renewable development within the District;

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40 *Formal Case No. 1119*, Motion of the District of Columbia for Revision of Procedural Schedule Announced in Order No. 17595, filed September 8, 2014 ("District Government's Motion").

41 *Formal Case No. 1119*, Office of the People's Counsel's Application for Reconsideration of Order No. 17597, filed September 11, 2014.

42 *Formal Case No. 1119*, Order No. 17654, ¶ 55, rel. October 9, 2014.

43 In this case, the Direct Testimony of the Joint Applicants, OPC, or any intervenor is cited, for example, as "District Government (-) (name of witness)"; while Rebuttal Testimony is cited as "Joint Applicants (3-) (name of witness)".

44 *Formal Case No. 1119*, Notice of Community Hearings, issued November 21, 2014; *see also*, Vol. 68 No. 48 *D.C. Reg*.

(3) the risks associated with Exelon's ownership of nuclear plants and the potential impact of this ownership on District residents; and (4) the impact of the Proposed Merger on reliability and quality of service in the District.

34. On January 13, 2015, AOBA filed a Motion to Revise the Procedural Schedule and requested five additional hearing days.[45] On January 29, 2015, the Commission granted AOBA's Motion in part by adding two additional hearing days on February 25th and 26th while reserving February 27th in the event an additional hearing day was needed.[46]

35. On February 4, 2015, the Joint Applicants filed a Motion to Submit Supplemental Rebuttal Testimony with the Supplemental Rebuttal Testimony attached.[47] On February 5, 2015, OPC filed an unopposed motion to postpone the evidentiary hearings that were scheduled to start on February 9, 2015 by a minimum of two days and to postpone procedural deadlines for the filing of cross-examination exhibits.[48] Also on February 5, 2015, AOBA filed its Opposition and Request for Alternative Relief in Response to the Joint Applicants' Motion.[49] Among other relief, AOBA requested that the hearings commence March 9, 2015 or at a time thereafter.

36. At a hearing on February 9, 2015, the Commission ruled that the Joint Applicants' Motion to File Supplemental Rebuttal Testimony was denied, but it *sua sponte* granted the Joint Applicants the right to file limited Supplemental Direct Testimony. The Commission thereafter issued Order No. 17802, which adopted a revised procedural schedule which was negotiated by the parties at the hearing.[50] The Commission also memorialized the bench rulings made during the hearing that, among other things: (1) denied Joint Applicants' Motion; (2) granted the Joint Applicants leave to file amended Supplemental Direct Testimony in accordance with paragraph 28 of the Order;[51] (3) granted AOBA's and OPC's Motions filed on February 5th; (4) moved the

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45 *Formal Case No. 1119*, Apartment and Office Building Association of Metropolitan Washington's Motion to Revise the Procedural Schedule, filed January 13, 2015.

46 *Formal Case No. 1119*, Order No. 17790, ¶ 18, rel. January 29, 2015.

47 *Formal Case No. 1119*, Joint Applicants' Motion to File Supplemental Rebuttal Testimony and Supplemental Rebuttal Testimony and Exhibits, filed February 4, 2015.

48 *Formal Case No. 1119*, Unopposed Motion of the Office of the People's Counsel to Delay the Start of Evidentiary Hearings and to Postpone Procedural Deadlines set forth in Commission Order No. 17790, filed February 5, 2015.

49 *Formal Case No. 1119*, Opposition of the Apartment and Office Building Association of Metropolitan Washington and Request for Alternative Relief to the Joint Applicants' Motion to File Supplemental Rebuttal Testimony, filed, February 5, 2015.

50 *See Formal Case No. 1119*, Order No. 17802, ¶ 30, rel. February 11, 2015.

51 Paragraph 28 of Order No. 17802 directed the Joint Applicants to "file any new commitments as Supplemental Direct Testimony and to file revisions and corrections as well as conforming Amended Direct, Amended Supplemental Direct and Amended Rebuttal Testimony reflecting changes." *See Formal Case No. 1119*, Order No. 17802, ¶ 28, rel. February 11, 2015.

evidentiary hearings to March 30 through April 8, 2015; and (5) directed all parties to file conforming testimony by March 25, 2015.[52]

37. On February 18, 2015, the Joint Applicants filed their Supplemental Direct Testimony.[53] OPC and the Intervenors filed their Amended and/or Answering Testimony on March 18, 2015. Eleven days of evidentiary hearings were held on March 30 – April 8, 2015 and April 20, 2015 – 22, 2015.[54] Initial Briefs were filed on May 13, 2015. On May 15, 2015, MAREC filed its Request for Leave to File Post-Hearing Brief Two Days Out of Time and its Initial Post Hearing Brief.[55] On May 15, 2015, the Commission granted motions filed by DC SUN, Joint Applicants, District Government, OPC, and GRID2.0 to correct the transcript.[56] On May 27, 2015 a Community Brief was filed.[57] On May 27, 2015, Reply Briefs were filed, at which time the record closed.[58]

III. STANDARD OF REVIEW

38. The Commission reviews merger applications pursuant to D.C. Code §§ 34-504 and 34-1001. Our review under these provisions is guided by our prior orders, where the Commission addressed other applications made pursuant to D.C. Code §§ 34-504 and 34-1001.

A. Jurisdiction

39. The Commission has jurisdiction over the Proposed Merger under D.C. Code §§ 34-504 and 34-1001.[59] D.C. Code § 34-504 provides in pertinent part that:

> No public utility . . . shall purchase the property of any other public utility for the purpose of effecting a consolidation until the Commission shall have determined and set forth in writing that said consolidation will be in the public interest, nor until the

[52] *Formal Case No. 1119*, Order No. 17802, ¶¶ 38-41, rel. February 11, 2015.

[53] *Formal Case No. 1119*, February 17, 2015 Supplemental Direct Testimony and Exhibits of Joint Applicant Witnesses Crane, Alden, Gausman, Khouzami, Tierney, and Lapson, filed February 18, 2015. Cited as "Joint Applicants (4-) (name of witness)."

[54] Transcripts of the Commission's Evidentiary Hearings are cited as "Tr."

[55] *Formal Case No. 1119*, Request for Leave to File Post-Hearing Brief Two Days Out of Time and Initial Post-Hearing Brief, filed May 15, 2015. The Commission grants the Motion and accepts the Brief.

[56] *Formal Case No. 1119*, Order No. 17882, rel. May 15, 2015.

[57] *Formal Case No. 1119*, (Written) Testimony of the Community Brief of District of Columbia Consumers Regarding the Proposed Merger of Exelon Corporation Pepco Holdings, Inc., filed May 27, 2015.

[58] Post-hearing initial briefs are cited, for example, as "AOBA Br."; and a post-hearing reply brief is cited as "District Government R.Br."

[59] *See also*, *Formal Case No. 1002*, Order No. 12189, ¶¶ 3-7, rel. September 19, 2001.

> Commission shall have approved in writing the terms upon which said consolidation shall be made.[60]

D.C. Code § 34-1001 provides in pertinent part that:

> No franchise nor any right to or under any franchise to own or operate any public utility as defined in this subtitle . . . shall be assigned, transferred, or leased, nor shall any contract or agreement with reference to or affecting any such franchise or right be valid or of any force or effect whatsoever unless the assignment, transfer, lease, contract, or agreement shall have been approved by the Commission in writing . . .[61]

In reviewing the Proposed Merger that includes a change of control over Pepco, the company that holds the electric distribution franchise for the District of Columbia, the Commission must determine if the transaction is in the public interest and issue our decision in writing.[62] If the Commission finds that the Proposed Merger is in the public interest, we must also "approve in writing the terms upon which said consolidation shall be made."[63]

B. Prior Commission Merger Decisions

40. This Commission has determined that "each merger is a unique combination of companies at a distinct time in the development of the electricity market,"[64] and each merger is assessed on its own facts as they relate to the companies involved and the development of the electricity market in the District. Indeed, this is the third time in the past two decades that Pepco has sought Commission approval of a merger and change of control transaction. As discussed below, each proposed transaction has involved different corporate structures and different relationships to the changing electricity market in the District.

1. Formal Case No. 951

41. In *Formal Case No. 951*, Pepco and BGE, two vertically integrated utility companies, sought Commission approval to merge the two companies and transfer Pepco's electric utility franchise to a new utility company to be known as Constellation Energy Corporation to be headquartered in Annapolis, Maryland.[65] This merger occurred before the

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60 D.C. Code § 34-504 (2001) (Emphasis added).

61 D.C. Code § 34-1001 (2001).

62 *See* D.C. Code § 34-1001 (2001) as applied in *Formal Case No. 1002*, Order No. 12395, ¶ 16, rel. May 1, 2002; *Formal Case No. 951*, Order No. 11075, p. 14, rel. October 20, 1997.

63 D.C. Code § 34-504 (2001).

64 *Formal Case No. 1119*, Order No. 17530, ¶ 27, rel. June 27, 2014.

65 *Formal Case No. 951*, Order No. 11075, p. 1, rel. October 20, 1997.

electricity market in the District was restructured and both companies had significant electricity generation capacity imbedded in their respective rate bases.

42. *Formal Case No. 951* was the first merger case that presented to the Commission "the question of 'public interest' as applied to a consolidation of utility companies or as applied to the purchase by one utility company of the property of another."[66] Pepco and BGE sought Commission approval to merge the two companies into a new entity to be known as Constellation Energy Corporation to be headquartered in Annapolis, Maryland.[67] The Commission recognized that "the answer as to how 'public interest' is to be measured varies widely" with some state statutes enumerating specific criteria while "others, like the District, rely on the regulatory authority to determine the appropriate yardstick."[68] To chart a course forward, "the Commission requested parties to provide their comments, and itself conducted research to determine the factors that should properly be considered in this case."[69]

43. After reviewing comments from the parties, the Commission formulated its evaluation criteria. First, the Commission explicitly rejected a "no adverse impact" test submitted by the applicants and WGL "as too simplistic" and instead stated, "to be in the public interest, this merger must benefit the public rather than merely leave it unharmed."[70] Second, the Commission noted it has traditionally "balanced the interests of a utility's shareholders and investors with the interests of ratepayers and the community."[71] Third, the Commission considered "the financial stability of the merging companies and what effect approval or disapproval of the merger would have on future investment."[72] Concluding, "the merger, as proposed, benefits the pecuniary interest of both shareholders and the merging companies," the Commission went on to state, "that those benefits must not come at the expense of ratepayers."[73] The Commission stated "[t]o be approved, this merger must produce a direct and traceable financial benefit to ratepayers."[74] The Commission also, referring back to its summation of a GSA argument that ratepayers should see a "profound benefit," stated:

> We do not agree that those benefits must be 'profound.' Instead, the Commission concludes that any savings that result must be shared with ratepayers, and be shared in such a proportion that

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66 *Formal Case No. 951*, Order No. 11075, p. 16, rel. October 20, 1997.

67 *Formal Case No. 951*, Order No. 11075, p. 1, rel. October 20, 1997.

68 *Formal Case No. 951*, Order No. 11075, p. 16, rel. October 20, 1997.

69 *Formal Case No. 951*, Order No. 11075, p. 16, rel. October 20, 1997.

70 *Formal Case No. 951*, Order No. 11075, p. 17, rel. October 20, 1997. (Citation omitted).

71 *Formal Case No. 951*, Order No. 11075, p. 17, rel. October 20, 1997.

72 *Formal Case No. 951*, Order No. 11075, p. 17, rel. October 20, 1997.

73 *Formal Case No. 951*, Order No. 11075, p. 18, rel. October 20, 1997.

74 *Formal Case No. 951*, Order No. 11075, p. 18, rel. October 20, 1997.

> ratepayers are compensated for the risks inherent in the companies' decision to merge.[75]

44. The Commission rejected the parties' suggested extensive merger evaluation criteria indicating its belief that "sound public policy militates against adoption of a laundry list of standards, notwithstanding the complexity of this case. We believe, and our research has shown, that the criteria to judge the 'public interest' can be distilled into several broad categories."[76] After considering the parties' comments, and approaches taken in other states and by the Federal Energy Regulatory Commission ("FERC"), the Commission concluded that a merger "<u>taken as a whole</u> must be consistent with the public interest."[77] The Commission indicated that its decision weighs the benefits and burdens of the transaction, and analyzes the propriety of the merger with respect to six broad categories:

> (1) ratepayers, shareholders, the financial health of the utilities standing alone and as merged, and the local economy; (2) utility management and administrative operations; (3) the safety and reliability of services; (4) risks associated with nuclear operations; (5) the Commission's ability to regulate the new utility effectively; and (6) competition in the local utility market.[78]

45. Finally, the Commission stated, "[a]s required by the Commission's enabling statute, this Order sets forth our declaration that the Proposed Merger of PEPCO and BGE is in the public interest and determines the terms upon which said consolidation shall be made."[79]

46. The applicants for the Pepco and BGE merger offered to do the following to make the proposed merger beneficial to ratepayers and in the public interest: share the $1.313 billion in estimated net merger savings in the first ten years following the merger equally between customers and the shareholders of Constellation through a two and one-half year base rate freeze (with two conditions), a commitment to contribute $5.1 million of the ratepayers' share of merger savings annually to low-income and economic development programs during the rate freeze period, and a Synergy Sharing Mechanism.[80] To reach its conclusion that the proposed merger was in the public interest, the Commission accepted the terms set out in the application but added the following terms as a condition of its approval of the proposed merger:

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75 *Formal Case No. 951,* Order No. 11075, p. 18, rel. October 20, 1997.

76 *Formal Case No. 951*, Order No. 11075, p. 18, rel. October 20, 1997.

77 *Formal Case No. 951,* Order No. 11075, p. 20, rel. October 20, 1997, citing "Policy Statement Establishing Factors the Commission May Consider in Evaluating Whether a Proposed Merger is Consistent with the Public Interest, "FERC Docket No. RM96-6-000, Order No. 592 (Dec. 18, 1996) at 12-13 (emphasis added).

78 *Formal Case No. 951*, Order No. 11075, p. 20, rel. October 20, 1997.

79 *Formal Case No. 951,* Order No. 11075, p. 20, rel. October 20, 1997, citing the predecessor to D.C. Code § 34-504 (2001).

80 *Formal Case No. 951,* Order No. 11075, p. 24, rel. October 20, 1997.

(1) $345 million of net merger savings are available to D.C. over the first 10 years of the merger;
(2) the merger savings are shared on the basis of 75% to ratepayers and 25% to shareholders;
(3) the proposed Synergy Sharing Mechanism will not be implemented;
(4) $5 million of the ratepayer portion of the savings is devoted to the establishment of an economic development fund;
(5) base rates are capped for four years;
(6) the remaining $94.5 million for the four-year base rate cap period will be distributed to ratepayers as a surcredit to monthly bills beginning the first day of the month after the effective date of the merger;
(7) the surcredit is calculated on a per kWh basis;[81]
(8) D.C. ratepayers' regulated rates will not include current or future costs of any kind attributable to BGE's Calvert Cliffs nuclear facility; Constellation's application to set rates following the expiration of the base rate cap must calculate rates for District consumers on the basis of service from Pepco's plants and not BGE's plants;[82]
(9) require Constellation's D.C. administrative base include corporate personnel knowledgeable of the needs and interests of the District of Columbia and accountable to the Commission for all services Constellation provides in the District;
(10) Constellation is required to produce any books, accounts, record and papers the Commission may order, at its District offices and for immediate inspection by the Commission;[83]
(11) require Constellation to devote additional management and supervisory personnel to the operation of its District of Columbia facilities and services;
(12) require Constellation's D.C. management team include sufficient personnel to respond to emergency situations (*i.e.*, power outages and service interruptions due to severe weather) in the District of Columbia;[84] and
(13) Constellation to submit a written agreement to be bound by the terms of the 1991 Memorandum of Understanding regarding the use of minority business enterprises and Constellation's specific procurement goals for District of Columbia businesses.[85]

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81 *Formal Case No. 951*, Order No. 11075, p. 66, rel. October 20, 1997.

82 *Formal Case No. 951*, Order No. 11075, p. 71, rel. October 20, 1997.

83 *Formal Case No. 951*, Order No. 11075, p. 81-82, rel. October 20, 1997.

84 *Formal Case No. 951*, Order No. 11075, p. 82, rel. October 20, 1997.

85 *Formal Case No. 951*, Order No. 11075, p. 96, rel. October 20, 1997.

47. On January 2, 1998, following the issuance of Order No. 11075, Pepco, BGE, and Constellation notified the Commission that they were withdrawing the application.[86]

2. Formal Case No. 1002

48. In *Formal Case No. 1002*, the applicants for the Pepco and New RC merger proposed to merge two wholly-owned, newly formed subsidiaries of New RC with and into Pepco and Conectiv such that Pepco and Conectiv would become wholly-owned subsidiaries of New RC.[87] This resulted in New RC, which later became PHI, owning the three electric distribution companies, ACE, Delmarva Power, and Pepco.

49. In summarizing the applicable standard in *Formal Case No. 1002*, Order No. 12395, the Commission stated: "the controlling legal standard in this case is the same as that applied by the Commission in [*Formal Case No. 951*,] Order No. 11075."[88] The Commission said "[t]he Applicants must demonstrate, therefore, that the findings on the issues designated in this proceeding show that the proposed merger is in the public interest."[89] The Commission recognized that in examining shareholder and ratepayer benefits:

> that merging companies would not venture into a transaction if there were no benefits to be accrued by the merging companies' shareholders. Thus, in determining whether the proposed Merger in this case is in the public interest, the Commission will assess whether the [Proposed] Merger will produce direct and traceable financial benefits to District ratepayers.[90]

The Commission, citing back to *Formal Case No. 951*, reiterated, "such benefits need not be profound."[91] The Commission went on to state that, "[i]n performing the 'public interest' analysis, the Commission considers the proposed Merger's effects with respect to the 15 designated issues set forth [earlier in *Formal Case No. 1002*]" and its "consideration and analysis of [the issues in *Formal Case No. 1002*] are based on the entire record in this proceeding, and the conclusions and decisions we reach herein are limited to those which are based upon substantial evidence from the record."[92]

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[86] *Formal Case No. 951*, Notice of Withdrawal of Application for Merger Approval and Application for Reconsideration and Motion to Terminate Proceedings, filed January 2, 1998.

[87] *Formal Case No. 1002*, Order No. 12395, ¶ 1, rel. May 1, 2002.

[88] *Formal Case No. 1002*, Order No. 12395, ¶ 24, rel. May 1, 2002.

[89] *Formal Case No. 1002*, Order No. 12395, ¶ 24, rel. May 1, 2002.

[90] *Formal Case No. 1002*, Order No. 12395, ¶ 24, rel. May 1, 2002.

[91] *Formal Case No. 1002*, Order No. 12395, ¶ 24, rel. May 1, 2002, citing *Formal Case No. 951*, Order No. 11075, p. 18, rel. October 20, 1997.

[92] *Formal Case No. 1002*, Order No. 12395, ¶ 25, rel. May 1, 2002, citing *Pepco v. D.C. Public Service Commission*, 402 A.2.d 14, 18 (D.C. 1979); *Consolidated Edison v. NLRB*, 305 U.S. 197, 229 (1938).

50. The applicants for the Pepco, Conectiv and New RC merger offered to do the following to make the proposed merger beneficial to ratepayers and in the public interest among other things: (1) maintain Pepco's headquarters in the District and locate PHI's headquarters in District;[93] (2) committed to continue its support of social and charitable activities in the District;[94] (3) any decrease in the number of employees will be accomplished through attrition;[95] and (4) submission of proposed service quality guarantees to members of the Productivity Improvement Working Group and inclusion of any recommended guarantees in Pepco's Productivity Improvement Plan.[96]

51. Following the evidentiary hearing in the case, Pepco, Pepco Holdings, Inc., OPC, AES, NewEnergy, AOBA, GSA, International Brotherhood of Electrical Workers ("IBEW"), and the Washington Metropolitan Area Transit Authority ("WMATA") submitted a Unanimous Agreement of Stipulation and Full Settlement ("Settlement Agreement"). The District Government and WGL, the two additional parties to the proceeding, did not oppose the Settlement Agreement and were not signatories to the Agreement.[97] The Settlement Agreement added the following terms to the proposed merger:

(1) distribution rates for residential customers were frozen for two and half years and for low-income Residential Aid Discount customers were frozen for four and half years;
(2) Pepco would not seek cost recovery of (a) merger-related costs (the District's share was estimated to be $46 million), (b) the acquisition premium, (c) cost of "golden parachutes," and (d) transitions costs;
(3) commitment to the development of any appropriate service quality guarantee and reliability program;
(4) commitment to achieve at least a 35 percent common equity ratio at the holding company level within five years of the close of the merger;
(5) Pepco should contribute $2 million to a smart meter pilot program;
(6) in all rate cases Pepco will bear the burden of affirmatively proving the reasonableness of all affiliate expenses charged to Pepco;
(7) in any rate case or proceeding, OPC and Commission Staff will have full access to all financial statements of regulated and unregulated subsidiaries;
(8) Pepco will pay for two and half years the Reliable Energy Trust Fund surcharges;
(9) filing of a Cost Allocation Manual explaining how costs are allocated to Pepco along with annual reports; and

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93 *Formal Case No. 1002*, Order No. 12395, ¶ 32, rel. May 1, 2002.

94 *Formal Case No. 1002*, Order No. 12395, ¶ 32, rel. May 1, 2002.

95 *Formal Case No. 1002*, Order No. 12395, ¶ 32, rel. May 1, 2002.

96 *Formal Case No. 1002*, Order No. 12395, ¶ 33, rel. May 1, 2002.

97 *Formal Case No. 1002*, Unanimous Agreement of Stipulation and Full Settlement, filed February 27, 2002 ("Settlement Agreement"); *Formal Case No. 1002*, Order No. 12395, ¶ 4, rel. May 1, 2002.

(10) a commitment to seek Commission approval regarding charges to suppliers.[98]

To reach its conclusion that the proposed merger as conditioned by the Settlement Agreement was in the public interest, the Commission accepted the terms set out in the application but added the following terms as a condition of its approval of the proposed merger: (1) commitment to track direct merger transaction costs and file reports with the Commission, with no corresponding need to track the Merger-related savings of $45.8 million;[99] and (2) rejected the Settlement Agreement commitment to achieve at least a 35 percent common equity ratio at the holding company level within five years of the close of the merger.[100]

52. The Commission considered and approved without additional conditions an unopposed settlement agreement regarding the proposed merger of Pepco and Conectiv, a holding company that owned two distribution companies, ACE and Delmarva Power, such that Pepco and Conectiv would become wholly-owned subsidiaries of New RC (the company that would eventually become PHI) and PHI would become the parent company of all three distribution utilities.[101] The merger approved in *Formal Case No. 1002* came on the heels of passage of the Retail Electric Competition and Consumer Protection Act of 1999 that deregulated the sale of electricity in the District by allowing competition for electricity generation and specifically provided for the sale Pepco's generation assets or the transfer of such assets to an affiliate.[102]

3. Formal Case No. 1119

53. On June 27, 2014, the Commission declined to designate specific issues in this case as it did in *Formal Case No. 1002*, because the Commission "believes the issue in this proceeding is whether the proposed merger is in the public interest" as required by D.C. Code §§ 34-504 and 34-1001.[103] Further the Commission stated, "[i]n *Formal Case No. 1002*, Order No. 12395, the Commission set forth the standard in determining the appropriate disposition of the proposed merger."[104] In Order No. 17530, the Commission noted our prior statement from *Formal Case No. 951*, which was cited in *Formal Case No. 1002*, that "for the proposed merger to be in the public interest, the proposed merger "must benefit the public rather than merely leave it unharmed."[105]

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98 *Formal Case No. 1002*, Order No. 12395, ¶ 37, rel. May 1, 2002.

99 *Formal Case No. 1002*, Order No. 12395, ¶ 67, rel. May 1, 2002.

100 *Formal Case No. 1002*, Order No. 12395, ¶ 128, rel. May 1, 2002.

101 *Formal Case No. 1002*, Order No. 12395, ¶ 1, rel. May 1, 2002.

102 *See Formal Case No. 1002*, Order No.12395, ¶ 2, rel. May 1, 2002.

103 *Formal Case No. 1119*, Order No. 17530, ¶ 27, rel. June 27, 2014.

104 *Formal Case No. 1119*, Order No. 17530, ¶ 23, rel. June 27, 2014.

105 *Formal Case No. 1119*, Order No. 17530, ¶ 24, rel. June 27, 2014, citing *Formal Case No. 1002*, Order No. 12395, ¶ 17, rel. May 1, 2002; and *Formal Case No. 951*, Order No. 11075, p. 17, rel. October 20, 1997.

54. As we explained in Order No. 17530, determining whether a proposed merger is in the public interest has traditionally been done by considering: "(1) whether the transaction balances the interests of shareholders and investors with ratepayers and the community; (2) whether the benefits to the shareholders do or do not come at the expense of the ratepayers; and (3) whether the proposed merger produces a direct and tangible benefit to ratepayers."[106]

55. Since the Commission has determined that "each merger is a unique combination of companies at a distinct time in the development of the electricity market," we requested comments from the parties as to the appropriate public interest factors on which to assess the Proposed Merger.[107] In Order No. 17597, following extensive comments by the parties that focused on new statutory language for Commission decision-making and circumstances relevant to the application at issue, the Commission amended four of the six existing public interest factors from *Formal Case Nos. 951* and *1002* and added a new seventh public interest factor to incorporate all four of the supervisory and regulatory factors set out in D.C. Code § 34-808.02.[108] Thus, in this case the Commission will consider the effects of the transaction on:

> (1) ratepayers, shareholders, the financial health of the utilities standing alone and as merged, and the economy of the District; (2) utility management and administrative operations; (3) public safety and the safety and reliability of services; (4) risks associated with all of the Joint Applicants' affiliated non-jurisdictional business operations, including nuclear operations; (5) the Commission's ability to regulate the new utility effectively; (6) competition in the local retail, and wholesale markets that impacts the District and District ratepayers; and (7) conservation of natural resources and preservation of environmental quality.[109]

Further, the Commission stated, "[w]e believe that testimony that focuses on the effect of the proposed merger on . . . [the public interest factors] will provide a record sufficient for the Commission to determine if the proposed merger is in the 'public interest.'"[110]

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[106] *Formal Case No. 1119*, Order No. 17530, ¶¶ 24 and 26, rel. June 27, 2014, citing *Formal Case No. 1002*, Order No. 12395, ¶ 17, rel. May 1, 2002; and *Formal Case No. 951,* Order No. 11075, pp. 17-18, rel. October 20, 1997.

[107] *Formal Case No. 1119*, Order No. 17530, ¶ 27, rel. June 27, 2014.

[108] D.C. Code § 34-808.02 reads: In supervising and regulating utility or energy companies, the Commission shall consider the public safety, the economy of the District, the conservation of natural resources, and the preservation of environmental quality.

[109] *Formal Case No. 1119*, Order No. 17597, ¶ 124, rel. August 22, 2014.

[110] *Formal Case No. 1119*, Order No. 17530, ¶ 27, rel. June 27, 2014.

C. Assessing the Public Interest

56. To determine if the Proposed Merger is in the public interest pursuant to D.C. Code §§ 34-504 and 34-1001,[111] the Commission will first look at the effect of the Proposed Merger transaction on each of the seven public interest factors, identifying the benefits and the burdens of the transaction, if any. We note, however, that because the circumstances of each merger are unique, every public interest factor may not be relevant or equally weighted from one merger to another.[112] In our review, the Joint Applicants, as the proponent of the order, bear the burden of persuasion.[113] This means the Joint Applicants have the burden of convincing the Commission that the Proposed Merger is in the public interest under D.C. Code §§ 34-504 and 34-1001.

57. Next, we will use our findings from our review of the effects of the Proposed Merger on the public interest factors to assess the transaction as a whole. In making our ultimate public interest determination under D.C. Code §§ 34-504 and 34-1001 and determining whether the Proposed Merger "benefit[s] the public rather than merely leaves it unharmed," we will take into account "(1) whether the transaction balances the interests of shareholders and investors with ratepayers and the community; (2) whether the benefits to the shareholders do or do not come at the expense of the ratepayers; and (3) whether the proposed merger produces a direct and tangible benefit to ratepayers."[114] We note that the language of the third determination – "a direct and tangible benefit" – has been revised from "direct and traceable financial benefits," which was the language that was used in the *Formal Case Nos. 951 and 1002* decisions.[115] This change was made to recognize that benefits can be broader than mere financial benefits and enables the Commission to assess a merger application to take account of all of its effects on the District and ratepayers.

58. Finally, if the Commission determines that the Proposed Merger is in the public interest, we will set out and "approve in writing the terms upon which said consolidation shall be made.[116]

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[111] D.C. Code §§ 34-504, 34-1001 (2001).

[112] *See Formal Case No. 1119*, Order No. 17530, ¶ 27, rel. June 27, 2014.

[113] *See People's Counsel of the District of Columbia v. Public Service Commission of the District of Columbia*, 474 A.2d 835, 837 (D.C. 1984) (the proponent of an order bears the burden of persuasion); *Washington Public Interest Organization v. Public Service Commission of the District of Columbia*, 393 A.2d 71, 77 (D.C. 1978) (the D.C. Court of Appeals has interpreted the phrase "burden of proof" to mean burden of persuasion); D.C. Code § 2-509 (b) (2001) ("In contested cases, except as may otherwise be provided by law, other than this subchapter, the proponent of a rule or order shall have the burden of proof.").

[114] *See Formal Case No. 1119*, Order No. 17530, ¶ 26, rel. June 27, 2014, citing *Formal Case No. 1002*, Order No. 12395, ¶ 17, rel. May 1, 2002; and *Formal Case No. 951*, Order No. 11075, pp. 17-18, rel. October 20, 1997; *Formal Case No. 1119*, Order No. 17597, ¶ 88, rel. August 22, 2014.

[115] Compare *Formal Case No. 1119*, Order No. 17530, ¶ 27, rel. June 27, 2014 with *Formal Case No. 1002*, Order No. 12395, ¶ 24, rel. May 1, 2002 and *Formal Case No. 951*, Order No. 11075, p. 18, rel. October 20, 1997.

[116] D.C. Code § 34-504 (2001).

IV. SECTIONS 34-504 AND 34-1001: PUBLIC INTEREST DETERMINATION

A. Introduction

59. The Joint Applicants have provided numerous updates and clarifications to their Joint Application. Since filing the Joint Application on June 18, 2014, the Joint Applicants have submitted an additional three rounds of testimony, on September 19, 2014, December 17, 2014, and February 18, 2015. Additionally, twelve witnesses presented live testimony for the Joint Applicants responding to OPC, Intervenor, and Commissioner questions regarding the Joint Application and adopting or accepting as evidence for the record numerous data request responses and cross examination exhibits. These documents form the evidentiary record upon which the Commission makes its decision. We note, as did several of the parties, that the Joint Applicants did not in some cases amend the Joint Application and its supporting documents to reflect changes that the Joint Applicants made in later filings. Where there is a discrepancy between the Joint Application and later record evidence, we will note that discrepancy and make a determination from the evidence before us as to what document is controlling.

B. Order No. 17597 Public Interest Factors

60. The Commission will now review the effects of the Proposed Merger on each of the seven public interest factors.

1. FACTOR 1: The effects of the transaction on ratepayers, shareholders, the financial health of the utilities standing alone and as merged, and the economy of the District[117]

a. The effects of the transaction on ratepayers

<u>Summary of Joint Applicants' Position Pertaining to Factor No. 1: Ratepayers</u>

61. According to the Joint Applicants, the Proposed Merger will have several beneficial effects on District ratepayers: a direct and immediate benefit from the establishment of a CIF for use in the District of Columbia that shares with ratepayers the synergy savings from the merger, additional synergy savings that will result in lower rates than would occur in the absence of the Proposed Merger, a commitment to maintain low-income assistance programs and to maintain and promote energy efficiency and demand response; strong ring-fencing provisions, and enhanced reliability from additional investments and shared best practices.

62. The primary direct benefit offered by the Joint Applicants is the CIF for use in the District of Columbia, which began at a $14 million level and was subsequently increased to $33.75 million. Joint Applicants contend that the CIF will equate to an immediate, direct and

[117] Although we have divided Public Interest Factor No. 1 into four separate sub-factors for purposes of our analysis and discussion, we caution that some matters argued by the parties and the public, and/or discussed by the Commission, may be relevant to, and discussed within, one or more of the sub-factors. Similarly, matters argued by the parties and the public, and/or discussed by the Commission related to a specific public interest factor may be relevant to, and discussed within one or more public interest factor if relevant.

traceable financial benefit of approximately $128 per metered customer.[118] The Joint Applicants cite direct customer rebates, energy efficiency programs, and low-income assistance as examples of how the CIF can be used; but have left it to the Commission's discretion to utilize the CIF in a manner that the Commission concludes will achieve the greatest good.[119]

63. The Joint Applicants' original synergy study estimated that the net cost savings for PHI utility operating companies resulting from the Proposed Merger would approximate $92 million over the first five years, which the Joint Applicants increased to $100 million for the purpose of allocating the CIF.[120] The Joint Applicants sought to develop an appropriate and simple metric that would be a good proxy for the manner by which the net synergies would flow through to the three companies and four jurisdictions on a cost-of-service ratemaking basis so that the net synergy savings could be allocated upfront.[121] The Joint Applicants determined that the metered customer count was a good proxy to use to allocate the $100 million among the various jurisdictions, arguing that it is closely aligned to how the net synergies will actually benefit those jurisdictions.[122] In the synergy study, the methodology used to project cost savings to each utility was based on the Modified Massachusetts Formula.[123] Since Pepco serves two jurisdictions, the study further allocated the cost savings attributable to Pepco to both Maryland and the District of Columbia based on the number of metered customers, arguing that this was a close estimate of how these types of administrative and general costs would generally be allocated between Maryland and the District of Columbia under the Pepco cost of service study used in distribution rate cases.[124]

64. Since the goal of the Joint Applicants was to be equitable to all jurisdictions, they contend that the CIF should be allocated using the same method as will be used to allocate the synergy savings under the service companies' cost allocation manuals. The Joint Applicants argue further that it would be inequitable to allocate benefits in one jurisdiction differently from how they are allocated in another.[125] Consequently, the Joint Applicants rejected arguments made by some parties to this proceeding for the use of other allocation metrics, such as rate base per customer or kilowatt hour sales, in the District of Columbia, concluding that the use of those metrics is inconsistent with how cost savings will flow to customers in future rate proceedings

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118 Joint Applicants' Br. at 33, citing Joint Applicants (4A)-2 at 1, Commitment 6; Joint Applicants (4F) at 4:11-15 (Khouzami).

119 Joint Applicants' Br. at 33, citing Joint Applicants (4A)-2 at 1 and 4, Commitments 6, 21, and 23.

120 Tr. at 2945:19-2946:2:10-11 (McGowan Cross); Tr. at 3361:21-3362:5 (Commission Cross of McGowan); Joint Applicants (3F)-1.

121 Tr. at 2946:3-8 (McGowan Cross).

122 Tr. at 2946:9-20 (McGowan Cross).

123 Joint Applicants (3F)-1 at 9 of 12.

124 Joint Applicants Br. at 34-35.

125 Joint Applicants Br. at 35, citing Tr. at 2968:4-10 (McGowan Cross).

pursuant to applicable allocation formulas in the cost allocation manuals and, therefore, would be inappropriate.[126]

65. The Joint Applicants initially proposed a $14 million CIF for the District of Columbia based on its customer meter count of 264,384, which was 14% of the total customer count from all the PHI utility operating companies. In their Supplemental Direct Testimony, the Joint Applicants increased the CIF to $33.75 million explaining this amount represented the same 14% but closer to 10-year synergy savings rather than 5-year savings. The Joint Applicants further contend that the CIF will provide District of Columbia customers upfront with about 94% on a net present value basis of the expected ten-year net synergy savings resulting from the Proposed Merger and they have committed to flow through 100% of the actual synergy savings allocable to Pepco-DC in future rate proceedings.[127] The Joint Applicants submit that the CIF has been designed to ensure that customers receive the full benefit of actual synergy savings, regardless of the timing or frequency of rate filings.[128]

66. According to the Joint Applicants, District of Columbia customers will realize additional direct and traceable financial benefits as Proposed Merger synergies are fully recognized in future rate proceedings in the form of rates that are lower than they would have been absent the Proposed Merger.[129] The Joint Applicants represent that the total Proposed Merger synergies, including both regulated and non-regulated affiliates, is $225 million over the first 5 years. About two-thirds of those synergies will go to the customers of regulated entities, PHI, BGE, PECO, and ComEd, through lower rates.[130] The Joint Applicants contend that the Merger will produce substantial synergies through the realization of economies of scale[131] and the elimination of duplicative functions primarily in enterprise-wide corporate operations. These savings translate to direct and traceable financial benefits to Pepco's customers, which will continue to accrue to customers for years to come.[132] On a 10-year basis, the Joint Applicants assert that the synergy savings will amount to about $ 51 million to the District.[133] Thus, the Joint Applicants contend that their proposal to provide a $33.75 million CIF and flow through in rates 100% of the actual synergy savings allocable to Pepco-DC means that customers will enjoy

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[126] Joint Applicants Br. at 35, citing Tr. at 2961:9-18; 2861:18-21 (McGowan Cross).

[127] Joint Applicants' Br. at 33-34, citing Joint Applicants (4A)-2 at 1, Commitment 6.

[128] Joint Applicants' Br. at 33, citing Joint Applicants (3A) at 7:2-5 (Crane).

[129] Joint Applicants Br. at 36, citing Joint Applicants (A) at 13:14-19 (Crane); Joint Applicants (3L) at 14:3-5 (McGowan).

[130] Tr. at 2030.

[131] Joint Applicants Br. at 36, citing Joint Applicants (A) at 6:1-3 (Crane).

[132] Joint Applicants Br. at 36, citing Joint Applicants (3F) at 13:15-18 (Khouzami).

[133] Joint Applicants (4F)-1 (Supp. Direct Khouzami), Joint Applicants (4L) at 12-13 (McGowan).

double recovery of some of the synergy savings.[134] To permit verification of the synergy savings, the Joint Applicants propose to provide a side-by-side comparison of pre- and post-Merger shared services costs allocated to Pepco. The Joint Applicants propose to make a filing comparing Pepco's allocated shared service costs for 2013 (the first full year before Merger activities began) versus Pepco's allocated shared service costs in 2016 (the first full year after the Merger has closed). This comparison, the Joint Applicants allege, will demonstrate that customers are getting the benefits of the Proposed Merger through rates.[135] Furthermore, the Joint Applicants agree to track all Proposed Merger-related savings and costs until Pepco's next rate case proceeding and account for such savings in that proceeding.[136] Finally, the Joint Applicants have committed to the same tax indemnity provision ordered by the Maryland Public Service Commission ("MD PSC") in the Exelon-Constellation merger. The Joint Applicants have revised the indemnity provision to include local income taxes to ensure that the taxes included in rates are no greater than they would have been on a Pepco standalone basis.[137]

67. The Joint Applicants state that Pepco customers will see an additional $121.6 million in tangible, quantifiable benefits as a result of its Enhanced Reliability Commitments. They point out that Pepco will continue implementation of its District of Columbia undergrounding project ("DC PLUG") as currently planned and, moreover, improve upon its reliability targets, with financial penalties in the event that Pepco does not achieve increased performance levels for system reliability.[138]

Summary of OPC and Intervenors' Position Pertaining to Factor No. 1: Ratepayers

68. OPC maintains that the Joint Applicants themselves contend that only two elements of the proposed transaction provide direct, tangible, quantifiable benefits to Pepco customers: (1) the CIF; and (2) "enhanced" reliability commitments. OPC argues both of these are woefully inadequate.[139] The Office avers that through a number of settlements and related

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[134] Joint Applicants Br. at 36, citing Joint Applicants (3L) at 15:5-8 (McGowan). According to the Joint Applicants, the long term running rate for net synergy savings is $7 million a year in perpetuity starting from Year 5. Tr. at 190.

[135] Joint Applicants Br. at 36.

[136] Joint Applicants Br. at 36, citing Joint Applicants (4A)-2 at 1, Commitment 5; Joint Applicants (3F) at 9:9-13 (Khouzami).

[137] Joint Applicants Br. at 37, citing Joint Applicants (4F) at 6:20-7:7 (Khouzami). Joint Applicants also maintain that the tax indemnity would also alleviate any concerns about limitations of NOLs that could be used going forward. If those IRC section 382 limitations were triggered, Exelon would ensure that Pepco and its customers are made whole. Tr. at 2143:5-14 (Commission Cross of Khouzami). Joint Applicants (4A)-2 at 17.

[138] Tr. at 2253:6-12 (Tierney Cross); Joint Applicants' (G) at 6, Table SFT-1 (Tierney).

[139] OPC's Br. at 36, citing Joint Applicants (G) at 8:16-19 (Tierney); *See also*, Joint Applicants (G) at 6:2-4 (where Dr. Tierney characterizes "the District-specific Customer Investment Fund and the Enhanced Reliability Commitments" as the "two sets of tangible, quantifiable benefits to Pepco customers"); Tr. at 2425:11-20 (where Dr. Tierney confirms that she did not attempt to quantify the potential benefit of any commitments other than the CIF and the reliability commitment); *see also*, Joint Applicants (3G) at 15:2-3 (where Dr. Tierney testifies that she "only

proposals in other jurisdictions, the Joint Applicants increased the CIF from its original proposal of $100 million to $238 million.[140] Of that amount, the District's portion of the increased CIF is $33.75 million.[141]

69. OPC challenges the sufficiency of the CIF for several reasons. First, the $33.75 million figure is only $3.6 million more than the "golden parachute" compensation for five senior executives of PHI who will resign from their positions as a result of the Proposed Merger.[142] Second, any benefit from the CIF is "highly dependent" on how the Commission decides to allocate that fund.[143] By not proposing any specific deployment of the CIF, the Joint Applicants deprived the parties of the ability to know, *ex ante*, what the impact of the CIF is likely to be. According to OPC, it is simply impossible to know whether any benefits resulting from the CIF will offset the qualitative and quantitative harms associated with the transaction.[144] Third, assuming that the CIF, either in total or in part, is provided to customers as a rate credit, any such benefit would quickly be eroded, and any benefit provided by the CIF is likely to be more than offset by anticipated rate increases.[145] Fourth, many of the alleged benefits are not anticipated to materialize until several years into the future; thus, a rate credit to current customers would not offset the harm that future customers may face if the projected benefits do not actually materialize.[146] Fifth, the original $14 million allocation to the District, and the revised $33.75 million allocation, constitutes only about 14% of the total CIF based on Exelon's decision to distribute that fund among the four jurisdictions implicated by the transaction on a metered-customer basis. OPC adds that using metered customers as the basis for allocating the CIF understates the allocation to the District to the direct benefit of the other jurisdictions involved in this proceeding.[147] OPC concludes that the CIF: (1) is not the product of a fair allocation methodology among the various jurisdictions; and (2) fails to compensate ratepayers for the risks of the transaction. It argues that, if the Commission is inclined to approve the transaction, one condition of any such approval must be a substantial increase to the District's CIF; otherwise there would be no substantial evidence upon which to base a decision that the public interest standard was satisfied.[148]

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quantified the two Regulatory Commitments – the [CIF] and the Reliability Improvements…."). OPC's arguments pertaining to the reliability commitment will be addressed in Public Interest Factor No. 3, *infra*.

[140] OPC's Br. at 36-37, citing Tr. at 1833:1-8 (Khouzami).

[141] OPC's Br. at 37.

[142] OPC's Br. at 37, citing Tr. at 639:6-10 (Rigby).

[143] OPC's Br. at 37, citing Tr. at 2462:14 to 2463:1 (Tierney).

[144] OPC's Br. at 37.

[145] OPC's Br. at 37-38.

[146] OPC's Br. at 38.

[147] OPC's Br. at 38.

[148] OPC's Br. at 39.

70. As set forth in Paragraph 68 above, OPC previously noted that the Joint Applicants' characterize only two components of their proposal as direct, tangible, quantifiable benefits to Pepco customers, *i.e.*, the CIF and the "enhanced" reliability commitments. However, the Joint Applicants generally allege that the transaction will provide ratepayers the benefit of millions of dollars of synergy savings.[149] OPC challenges the validity of this claim as well, arguing first, the Joint Applicants' analysis shows that the costs to achieve synergies are front-loaded, whereas synergy savings that would flow to ratepayers are back-loaded. Because long-term estimates are more difficult to make than short-term estimates, and because it is more difficult to trace transaction-related synergies as the companies become further entwined, OPC contends that the Joint Applicants are unable to demonstrate any benefit to ratepayers, let alone a direct and traceable one.[150] Second, OPC submits, the Joint Applicants have overstated the costs to achieve, thereby diminishing any synergy savings that ratepayers may realize. Notably, according to OPC, the Joint Applicants inappropriately characterize certain regulatory support costs as costs to achieve instead of transaction costs, thus unnecessarily burdening ratepayers.[151] Finally, the Office asserts that the Joint Applicants' proposal to recover the non-accelerated portion of Supplemental Executive Retirement Plan ("SERP") costs is contrary to Commission precedent.[152]

71. More specifically, OPC contends that under the Joint Applicants' proposal, Pepco's next base rate case will result in ratepayers paying rates that are higher than they otherwise would due to the fact that costs to achieve would be recovered through rates. The Joint Applicants project that costs to achieve will outweigh synergies by $2 million in the pre-closing period. In year one, the costs to achieve are projected to be $7 million, in comparison to projected synergies of $3 million. OPC understands that Pepco will seek to recover through rates the $2 million in costs to achieve incurred in the pre-closing period. Thus, OPC states, if the Joint Applicants' estimates of costs to achieve and synergy savings are accurate, Pepco's cost of service in the first rate case following the acquisition is likely to be $6 million higher than it would be in the absence of the transaction. OPC contends that it is only in year two that the projected synergy savings will allegedly turn positive and that projected net benefit only amounts to $2 million.[153]

72. OPC notes that although the Joint Applicants would not be in violation of any of the 91 commitments in Exhibit Joint Applicants (4A)-2 if the synergy estimates never materialize, the Joint Applicants would have recovered their costs to achieve by virtue of the fact

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149 OPC's Br. at 48.

150 OPC's Br. at 48.

151 OPC's Br. at 49.

152 OPC's Br. at 49, citing *e.g.*, *Formal Case No. 1103, In the Matter of the Application of the Potomac Electric Power Company for Authority to Increase Existing Retail Rates and Charges for Electric Distribution Service* ("*Formal Case No.1103*"), Order No. 17424, ¶ 566(r), rel. March 26, 2014 (noting the removal of SERP costs).

153 OPC's Br. at 49-50.

that the costs to achieve are front-loaded (*i.e.*, are incurred within the first year of the merger according to page 8 of Joint Applicants witness Khouzami's Rebuttal Testimony). Thus, instead of producing a benefit to ratepayers, OPC maintains that the Joint Applicants' proposal essentially ensures that the Joint Applicants and their shareholders will be made whole while simultaneously putting the risk on ratepayers that: (1) synergies will actually be achieved; and (2) achieved synergy savings will more than offset the costs to achieve. The Office asserts that this asymmetrical sharing of benefits and risks is unfair and contravenes Commission precedent; there is no basis for placing this undue risk on ratepayers. For this reason, OPC asks the Commission to find that the Joint Applicants have failed to demonstrate that the transaction will produce a net benefit to ratepayers, and that such a finding supports the broader conclusion that the proposed transaction is not in the public interest.[154]

73. OPC also asserts that the Joint Applicants' categorization of regulatory support costs as costs to achieve, and therefore recoverable from ratepayers, benefits shareholders at the expense of ratepayers.[155] OPC states that regulatory support costs include costs associated with the hearings in the four jurisdictions as well as before FERC.[156] Referring to an observation made by Commissioner Brenner of the MD PSC, without regulatory approval of these jurisdictions, there can be no consummation of the transaction.[157] According to OPC, Mr. Khouzami's definition that transaction costs include those costs "up and to the point of effectuating the merger agreement" should necessarily include regulatory support costs (*i.e.*, the costs associated with hearings in the four jurisdictions and before FERC). OPC asserts that the Joint Applicants' own definitions of transaction costs and costs to achieve necessitate defining regulatory support costs as transaction costs.[158] If the transaction were approved, Pepco would recover costs to achieve from ratepayers because it proposes to flow net synergy savings through to ratepayers through rates. However, OPC notes, Pepco does not propose to recover transaction costs from ratepayers.[159] OPC concludes that the consequence of characterizing regulatory support costs as costs to achieve is that ratepayers are burdened with $15 million in excessive costs, a portion of which would be allocated to the District, which OPC notes Mr. Khouzami believed the District's allocation would be below $2 million.[160] Thus, the Joint Applicants'

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154 OPC's Br. at 50-51.

155 OPC's Br. at 55-56.

156 OPC's Br. at 55, citing Tr. at 1800:4-8 (Khouzami).

157 OPC's Br. at 55, citing Tr. at 1801:22 to 1802:3 (discussing Mr. Khouzami's testimony in Maryland PSC Case No. 9361)

158 OPC's Br. at 55.

159 OPC's Br. at 55-56, citing Joint Applicants (4A)-2 at 1, Commitment 1(a); Joint Applicants (F) at 25:11-15 (Khouzami).

160 OPC's Br. at 56, citing Joint Applicants (3F)-1 at 8; Tr. at 1803:12-16 (Khouzami).

proposal to characterize regulatory support costs as costs to achieve essentially eliminates shareholders' responsibility for these costs and burdens ratepayers with excessive costs.[161]

74. **AOBA.** AOBA contends that the labeling of the pool of dollars as a "Customer Investment Fund" is simply an arbitrary characterization of those funds that has no relationship to cost-based ratemaking concepts or an actual investment activity on the part of Exelon. AOBA asserts that Exelon leverages the naming of that fund to suggest that the pool of direct merger benefits it commits to create would be equitably allocated among the PHI utilities and the jurisdictions in which they provide service on a uniform dollars per customer basis. Yet, AOBA submits, the record of this proceeding clearly demonstrates that the Joint Applicants' uniform dollars per customer allocation of the proposed CIF dollars is not equitable.[162] AOBA states further that, although the Joint Applicants argue that the total amount of CIF dollars offered to the PHI utilities is linked to estimated costs savings that would flow from Merger-related synergies, the record establishes that such cost savings are not generated on the basis of numbers of customers served and would not flow to the individual PHI utilities or the jurisdictions in which they provide service on a uniform dollars per customer basis. Rather, AOBA claims, any Proposed Merger-related synergy cost savings would flow to the PHI utilities through either established PHI cost sharing allocation procedures or the jurisdictional cost allocation methods that this Commission has accepted in past Pepco rate proceedings.[163]

75. AOBA contends that the Joint Applicants have attempted to support this level of direct Proposed Merger benefits ($128 per customer) by arguing that the new amount of direct merger benefits approximates the Joint Applicants' estimated ten-year net synergy savings and approximates that ratio of direct merger benefits to estimated net synergy savings to which Exelon ultimately agreed in 2012 in the Exelon-Constellation merger proceeding before the MD PSC (Case No. 9271).[164] AOBA goes on to assert that the Joint Applicants provide no compelling argument for why this Commission should now view approximately ten years of net synergy savings, as opposed to some other measure of net synergy savings (*e.g.*, 7 years, 12 years, 15 years, or 20 years), as the appropriate determinant of the level of overall direct Merger benefits to be provided for the PHI utilities.[165] AOBA submits that the Joint Applicants' estimates of net synergy savings have never defined either the value of the Proposed Merger to Exelon or a defensible limit on the amount of direct Proposed Merger benefits to be provided to customers of the PHI utilities. AOBA maintains that the synergies represent a very small element of the accretion in this transaction; rather, the real value of this transaction for Exelon is

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161 OPC's Br. at 56.

162 AOBA's Br. at 72.

163 AOBA's Br. at 73.

164 AOBA's Br. at 75-76. AOBA claims to have reviewed the Maryland Commission's decision on that issue in that proceeding (Order No. 84698) and it found no evidence of any discussion of such a ratio. AOBA's Br. at 776 n. 92.

165 AOBA's Br. at 76.

found in the incremental leverage it provides at the holding company level.[166] Thus, AOBA states "that [the Joint Applicants' assertion that] the direct Proposed Merger benefits provided to customers of the PHI utilities are defined by, or limited to, Exelon's estimates of net synergy savings greatly misrepresents the nature of the proposed transaction and its value to Exelon."[167]

76. AOBA also finds fault with the method in which the Joint Applicants allocated the direct merger benefits among the PHI utilities and the jurisdictions in which they provide service.[168] AOBA states that the customer count based allocations used by the Joint Applicants is apparently a derivative of the method used to distribute a similar customer investment fund among BGE customers in the Exelon-Constellation merger proceeding in Maryland. Since that method was accepted for BGE, it appears to AOBA that the Joint Applicants assumed early in the Proposed Merger discussions that a similar allocation approach would be viewed as reasonable by each of the jurisdictions affected by this Proposed Merger. However, AOBA asserts, BGE is a single utility with all of its operations within one jurisdiction, and, as a result, there was no need in the BGE proceeding (Case No. 9271) for the merging entities (Exelon and Constellation) to address either inter-utility or inter-jurisdictional allocations.[169] AOBA points to its Exhibit 78 to show that the synergies that would flow to each PHI jurisdiction are *not* uniform on a dollars per customers basis. Rather, synergy savings for Pepco are noticeably higher on a dollars per customer basis than similar measures computed for ACE and Delmarva Power. Moreover, AOBA contends, the methods the Joint Applicants have used to allocate CIF dollars among jurisdictions do not correspond to the methods used to allocate similar costs by jurisdiction in Pepco's last base rate proceeding (*Formal Case No. 1103*).[170]

77. AOBA witness Oliver documented the differing characteristics between the District of Columbia service territory and PHI's service territories in the other jurisdictions (*e.g.*, the District contains an unusually small percentage of industrial load and a greater portion of commercial office and apartment load as compared to the other PHI service territories), and concluded that these characteristics result in a much higher average distribution rate base investment per customer for Pepco's District of Columbia service than is found for any of the other jurisdictions in which the PHI utilities provide service.[171] AOBA concludes:

> [T]he Commission must reject the Joint Applicants approach to this matter as it produces results that are substantially adverse to interests of the District of Columbia. As AOBA witness Oliver demonstrates in Exhibit AOBA (2A)-2 and explains in his Supplemental Direct Testimony, his advocated rate base allocation

166 AOBA's Br. at 76, citing Tr. at 33:20-34:7.

167 AOBA's Br. at 76.

168 AOBA's Br. at 77.

169 AOBA's Br. at 77-78.

170 AOBA's Br. at 79.

171 AOBA's Br. at 79.

> of CIF dollars distributes the same total dollar amount to the PHI utilities and the jurisdictions they serve that the Joint Applicants' customer-based allocation achieves. However, witness Oliver's alternative better reflects the drivers of this Merger and the greater investment per customer that is found for Pepco's District of Columbia service. The approach AOBA witness Oliver presents also avoids issues regarding the appropriateness of the measures of numbers of customers that the Joint Applicants have employed.[172]

78. AOBA criticizes the Joint Applicants for offering no specific proposals for use of the CIF dollars that they offer for the District of Columbia; rather, the Joint Applicants have maintained that all determinations regarding use of those funds will be left to the Commission. AOBA argues that, if the Commission should choose to adopt an application of direct Merger benefits in this proceeding (as CIF dollars, energy efficiency funding, or in some other form) that has not been analyzed by witness Tierney, no record exists to support any assessment of the economic or employment impacts of such alternatives. Given the lack of record in support of an appropriate allocation of CIF dollars, a Commission decision to approve the Proposed Merger will require additional proceedings to assess options for use of CIF dollars and the benefits associated with such options.[173] Under a scenario in which this Commission approves the Proposed Merger, AOBA submits that this Commission should defer determinations regarding the use(s) of any CIF dollars for consideration in Pepco's next base rate proceeding. This procedural alternative would allow for the Commission to make its determinations regarding possible applications of CIF dollars in the context of updated class cost of service results and a better developed record regarding the merits of alternative uses of those funds. Moreover, the Commission would be in a better position to consider the value to ratepayers of using proposed CIF dollars to partially offset Pepco's next rate increase request.[174]

79. **District Government.** The District Government alleges that the Proposed Merger does not offer any genuine value to District of Columbia retail electric consumers for three reasons: (1) Exelon's refusal to share with customers the lowered cost of capital resulting from its financing of the Merger means that, in every practical sense, District of Columbia retail electric consumers (and retail electric consumers served by other PHI operating companies) would end up paying the $1.6 billion acquisition premium Exelon has offered for PHI's stock;[175] (2) Exelon's proposed $33.75 million "Customer Investment Fund" suffers from two major shortcomings: (a) it has not been persuasively shown to provide any net gain to the District or District of Columbia retail electricity consumers, and (b) it under-allocates any benefit that it might otherwise be argued to provide because the allocation methodology used by Exelon discriminates against District of Columbia retail electricity consumers;[176] and (3) the Joint

[172] AOBA's Br. at 81-82.

[173] AOBA's Br. at 84.

[174] AOBA's Br. at 85.

[175] District Government Br. at 17.

[176] District Government Br. at 18.

Applicants' claims of secondary (or "multiplier effect") economic benefits accruing to the District or District of Columbia retail electricity consumers from either the CIF or the Joint Applicants' "Reliability Commitment" are "wildly overstated and analytically unsound" and unworthy of acceptance by the Commission.[177]

80. Concerning Exelon's failure to share the Proposed Merger finance benefits, District Government witness Wilson explains:

> The difference between Exelon's estimated acquisition debt cost and the bottom end of this estimated equity return range . . . would result in a ratepayer-funded finance cost gain for Exelon of $94.9 million annually for each $1.0 billion of equity-funded D.C. rate base that becomes effectively debt-funded as a result of Exelon's proposed transaction financing. This would permit Exelon to recover the $1.6 billion premium paid to PHI stockholders, plus transaction financing fees, from Pepco's ratepayers and from the ratepayers of PHI's other operating utilities in less than five years. The estimated financing cost savings (which Exelon intends to charge to – rather than share with – Pepco's ratepayers) will then be used to fund Exelon's acquisition premium and add to Exelon's profits.[178]

81. With regard to the CIF shortcomings, the District Government claims its witnesses (Smith and Comings) presented analyses showing that there is no evidence to support the notion that Joint Applicants' proposed CIF is sufficiently large to offset future reductions in District of Columbia jobs that the Joint Applicants are likely to require in order to achieve their claimed Merger "synergies."[179] The District Government states that, over the course of this proceeding, the Joint Applicants have reduced the levels of reductions-in-force on which they anticipate relying to achieve their Proposed Merger "synergies" from approximately 397 full-time equivalent positions to approximately 257 full-time equivalent positions.[180] However, the District Government asserts that the Joint Applicants have yet to disclose the location(s) from which those positions will be eliminated or to otherwise provide any assessment of the impact of merger-related reductions-in-force on employment in the District of Columbia. As a result, the reduced levels of reductions-in-force do not affect the original analysis of the District's witnesses

[177] District Government Br. at 19, citing District Government (C) at 8:21–10:7 (Comings).

[178] District Government Br. at 19, quoting District Government (F) at 11:5-12:5 (Wilson).

[179] District Government Br. at 22, citing District Government (A) at 70:3-93:17 (Smith); District Government (C) at 5:1-15:12 (Comings).

[180] District Government Br. at 22-23, citing the comparison between Confidential District Government (C)-2 (original synergy reduction-in-force forecast) and Confidential Joint Applicants (3F)-2) (current synergy plan involves the elimination of 257 positions (200 currently filled and 57 currently unfilled)) (Tr. at 2055:7-2056:9) (Khouzami).

that the Joint Applicants have failed to show that the Proposed Merger produces any net benefit in the District.[181]

82. The District Government also argues that the proposed CIF is also problematic because, even if it did create some possible net benefit to the District, the Joint Applicants' methodology for allocating merger synergies (and hence the distribution of the CIF by retail regulatory jurisdiction) discriminates against the District. The Joint Applicants allocated the CIF to PHI in total based on their "modified Massachusetts formula," and then to each PHI utility operating company based on the ratio of that company's meter accounts to the total number of meter accounts in all PHI utility operating companies.[182] This allocation methodology moves approximately 14 percent of the Joint Applicants' PHI-wide, synergy-based CIF to the District of Columbia. In contrast, Pepco's District of Columbia operations represent 23 percent of all PHI electric utility operating company sales, 25 percent of total rate base for all PHI utility operating companies, and 24 percent of net income for all PHI electric utility operating companies, in a system where almost all rates are volumetric.[183] Referring to AOBA witness Oliver's testimony, the District Government submits that the Joint Applicants' allocation of claimed merger synergies to the District of Columbia on the basis of meter accounts substantially, unreasonably, and discriminatorily reduces the size of the District of Columbia's share of the fund as compared to any reasonable, rational allocation methodology consistent with accepted principles of cost causation and cost incurrence.[184] Thus, the District Government concludes that the Joint Applicants are not proposing to treat District of Columbia retail electricity consumers fairly in connection with the pending Proposed Merger proposal.[185]

83. **NCLC/NHT.** NCLC/NHT argue that the Joint Applicants' Low-Income Commitment to maintain its low-income customer assistance programs pursuant to current requirements and commitments does not provide any incremental benefit to low-income customers of Pepco.[186] Instead, NCLC/NHT maintain, the Joint Applicants admit this is merely a commitment to provide certainty that the existing low-income programs will continue post-

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181 District Government Br. at 23.

182 District Government Br. at 24-25, citing Tr. at 1985:6-1996:6 (Khouzami); District Government Confidential Cross Examination Exhibit No. 84 (Joint Applicants' Response to Data Request AOBA 1-23 Attachment A (Errata Version 1)) at 70-78; Joint Applicants (F)-2 and (3F)-1 at 8; but compare Tr. at 3376:12-3378:17 (McGowan) describing a slightly different method of allocation. McGowan said the $100 million in synergies were split at the PHI level among the 3 operating utilities (Pepco, DPL, and ACE) based on where the synergies were derived from according to the synergy study, and then the synergy savings were allocated among jurisdictions (*i.e.*, Pepco Maryland & Pepco-DC) based on meter count.

183 District Government Br. at 25, citing Tr. at 3383:15-3385:9 (McGowan).

184 District Government Br. at 25, citing AOBA (2A) at 22:15-33:13 (Oliver), AOBA (2A)-1, AOBA (2A)-2.

185 District Government Br. at 25-26.

186 NCLC/NHT's Br. at 5, citing Joint Applicants (4A)-2 at 4, Commitment 21. NCLC/NHT state that this commitment to maintain a program is only a separate and distinct benefit if one assumes Pepco will, in the near future, reduce its commitment to low-income programs. However, NCLC/NHT submit that Pepco has no intent to degrade its low-income customer commitments. NCLC/NHT's Br. at 5, n. 14, citing Tr. at 3338:8-12 (McGowan).

merger.[187] Similarly, the Joint Applicants have failed to establish a direct benefit regarding their commitment to maintain and promote existing energy-efficiency programs.[188] The Joint Applicants rely upon the current CIF commitment, the equivalent of $128 per residential ratepayer,[189] to provide: (a) direct and traceable benefits to potentially all ratepayers, (b) specific benefits for low-income ratepayers, and (c) energy efficiency investments to satisfy Factor No. 7, but they have declined to offer any specific proposals as to how the CIF can accomplish these diverse ends.[190] Additionally, NCLC/NHT assert that the Joint Applicants have also failed to provide concrete assurances that low-income households will receive an equitable share of any direct and tangible benefits.[191]

84. NCLC/NHT point out that there is a significant need for energy efficiency investment in the District's multifamily affordable housing stock in order to address the energy and housing affordability crisis facing low-income District renters.[192] NCLC/NHT note that the District of Columbia has a disproportionately large percentage of renters as opposed to homeowners and has an unusually high percentage of housing units in multifamily buildings, particularly large multifamily buildings.[193] NCLC/NHT contend that investments in energy efficiency in multifamily housing provide a broad range of benefits, including: (1) direct benefits to owners and residents that include lower utility bills, lower maintenance costs, and increased health, comfort and safety (*e.g.*, drafts are reduced and heating systems become more reliable); (2) energy efficiency investments can benefit all ratepayers by reducing demand and the need for investment in new generation and transmission capacity, and by avoiding the need to purchase additional energy at the most expensive hours; (3) efficiency investments in affordable multifamily housing help to preserve the stock of such units by lowering energy bills, which are often the largest operating cost; and (4) energy efficiency retrofits provide business and job opportunities to local contractors and members of the building trades.[194]

85. NCLC/NHT also assert that the settlements reached by the Joint Applicants in other jurisdictions include much more fully defined and valuable benefits for ratepayers and the public than what the Joint Applicants have formally committed to providing in the District. The benefits offered elsewhere, particularly in Maryland, include energy efficiency programs that are targeted to low-income households.[195] NCLC/NHT assert that to the extent that the Joint

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187 NCLC/NHT's Br. at 5, citing Tr. at 616:4-7; Tr. at 619-620 (Rigby).

188 NCLC/NHT's Br. at 5, citing Tr. at 818:6-19; Tr. at 818-819 (McGowan).

189 NCLC/NHT's Br. at 5-6, citing Joint Applicants (A) at 12-13 (Crane); Joint Applicants (G) at 5:8-9 (Tierney).

190 NCLC/NHT's Br. at 6, citing Joint Applicants (A) at 13:3-8 (Crane).

191 NCLC/NHT's Br. at 6.

192 NCLC/NHT's Br. at 7, citing NCLC/NHT (A) at12:12-13:5 (Bodaken).

193 NCLC/NHT's Br. at 7.

194 NCLC/NHT's Br. at 7-8.

195 NCLC/NHT's Br. at 8.

Applicants have entered settlements in the other jurisdictions that provide better-defined and valuable benefits for ratepayers and the environment, the Commission should feel compelled to impose similar conditions here, if the Merger is approved at all.[196] NCLC/NHT summarize relevant portions of the settlement reached in Maryland as providing substantial, tangible benefits for low-income households that should be made conditions of the merger here, should the Commission decide to approve the merger.[197] These include, in Montgomery County, "a minimum of 10% of [energy efficiency] incentives and financing [will be targeted to] benefit multi-family communities" and a portion of the funds will be devoted to expanding weatherization programs that serve low-income households.[198] NCLC/NHT adds that in Prince George's County, the "Transforming Neighborhoods Initiative," which will receive 50% of the funding allocated to the county, will target six neighborhoods "that face significant economic, health, public safety and educational challenges" and provide funding for energy efficiency, rooftop solar and other energy measures.[199] Additionally, the Maryland Multi-Party Settlement provides that the Maryland PHI companies will "engage in discussions with NCLC to consider in good faith the development of a mutually agreeable Arrearage Management Program ("AMP") for low-income customers in arrears."[200] Massachusetts utilities were mandated by law in 2005 to offer AMPs to residential customers in arrears,[201] and, based on the success of the Massachusetts AMP model, Maine followed suit in 2013.[202] AMPs not only help low-income customers in arrears to avoid termination of utility service, evidence to date suggests that they can also reduce company collection costs and improve the payment behavior of payment-troubled customers.[203] They thus hold out the promise of substantial benefits for low-income customers and ratepayers alike. NCLC/NHT urges the Commission not to approve the merger unless conditions are attached that target tangible and substantial benefits to low-income households comparable to the ones noted above. In particular, NCLC/NHT argues that if the merger is approved, conditions should be imposed that would require substantial energy efficiency investments in low-income housing, with a specific set aside for affordable multifamily housing; adoption of a Green

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196 NCLC/NHT's Br. at 8-9.

197 NCLC/NHT's Br. at 9.

198 NCLC/NHT's Br. at 10-11, citing OPC Cross Examination Exhibit No. 7, pp. 25-26 of 70 (Multi-Party Settlement ¶ 6).

199 NCLC/NHT's Br. at 11, citing OPC Cross Examination Exhibit No. 7, pp. 24-25 of 70 (Multi-Party Settlement ¶ 5).

200 NCLC/NHT's Br. at 11, citing OPC Cross Examination Exhibit No. 7, pp. 32-33 of 70 (Multi-Party Settlement ¶ 25).

201 NCLC/NHT's Br. at 11, citing 2005 Mass. Acts, Ch. 140, § 17.

202 NCLC/NHT's Br. at 11, citing Me. Rev. Stat. Ann. tit. 35-A, § 32 14, ¶ 2-A.

203 NCLC/NHT's Br. at 11-12, referencing NCLC's report, "Helping Low-income Utility Customers Manage Overdue Bills through Arrearage Management Programs" (Sept. 2013), available at http://tinyurl.com/ocdg4av.

Sustainability Fund along the lines included in the Maryland Settlement; and a process for evaluating the merits of implementing an Arrearage Management Program in the District.[204]

86. **DC Water.** DC Water recites the recent history and development of the CIF beginning with the Joint Applicants' initial application in which they proposed to establish a $100 million CIF which would be allocated among all PHI jurisdictions based on respective customer counts with the regulatory commission in each jurisdiction free to use its portion of the CIF in whatever fashion it sees fit. Under the Joint Applicants' proposal, the District's share of the CIF was $14 million. DC Water contends that this figure was purportedly developed by allocating the $100 million among the PHI jurisdictions based on customer count, which equated to a benefit of approximately $52.95 per District customer.[205] According to DC Water, the Joint Applicants characterize the CIF as a mechanism "to provide an immediate tangible benefit to PHI customers from the Proposed Merger-related savings the PHI utilities are expected to achieve during the first five years following completion of the merger."[206] DC Water states that the Joint Applicants eventually adjusted their proposals here to incorporate certain provisions from the New Jersey Settlement "as a way of offering District of Columbia customers comparable value as that provided to New Jersey customers."[207] One such adjustment was to increase the District's share of the CIF from $14 million to $33.75 million.[208] DC Water states further that, although the Joint Applicants made an attempt to link this new CIF figure with projected synergy savings (now representing 10 years of savings), Joint Applicants witness Crane made it clear on cross examination that the real rationale for the change in the CIF was simply to get New Jersey on board with a settlement, without regard to synergy savings.[209]

87. In DC Water's view, the Joint Applicants' initial effort to link synergy savings to their proposed CIF was nothing more than an artifice to limit the costs of obtaining regulatory approval. Early on in this transaction, Exelon management made clear that synergy savings played a very small role in driving this merger deal.[210] According to DC Water, "abundant record evidence was introduced to support the conclusion that a primary driver in this transaction for Exelon was a desire to increase revenue stability through the acquisition of additional regulated, rate base assets which will, inter alia, protect Exelon's dividend."[211] Thus, DC Water submits, "synergy savings is not driving this deal and therefore is not an appropriate metric for

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[204] NCLC/NHT's Br. at 12.

[205] DC Water's Br. at 8, citing Joint Applicants (G) at 6, Table SFT-1 and at 7 n. 2 (Tierney); Joint Applicants (3F) at 12:14 (Khouzami).

[206] DC Water's Br. at 8, citing Joint Applicants (F) at 20:14-17 (Khouzami); c.f. Joint Applicants (2F) at 11:17-20 (Khouzami).

[207] DC Water's Br. at 9-10, citing Joint Applicants (4A) at 7:18-24 (Crane).

[208] DC Water's Br. at 10, citing Joint Applicants (4A)-2 at 1, Commitment 6.

[209] DC Water's Br. at 10, citing Joint Applicants (3F)-1.

[210] DC Water's Br. at 10, citing District Government Cross Examination Exhibit No. 3 at 16.

[211] DC Water's Br. at 11, quoting District Government Cross Examination Exhibit No. 3 at 5.

determining how best to measure the benefit that ratepayers must receive to satisfy the Commission's merger standards. The transaction is being undertaken to provide very real and substantial benefits to Exelon and PHI shareholders. Thus, the Commission's focus must be [on] how those benefits compare to the benefits that Pepco's ratepayers will realize as a result of the merger."[212]

88. DC Water argues that the Joint Applicants' proposed $33.75 million District ratepayer benefit pales in comparison to the risks associated with Exelon's proposed acquisition of Pepco.[213] Stating that there can be no argument that the Proposed Merger significantly increases the risks faced by Pepco's ratepayers, DC Water asserts that the Proposed Merger will dramatically change the corporate environment in which Pepco operates. Today, DC Water contends, Pepco itself is solely an electric distribution company and is part of a corporate family that is dominated by low-risk electric distribution companies, with only very limited exposure to electric commodity and supply markets. According to DC Water, "[i]f the Proposed Merger goes forward, Pepco will be subsumed into a corporate family that, at present, receives over 60% of its revenues from generation related activities, much of it [being] nuclear."[214] DC Water points out that the Joint Applicants themselves readily acknowledged the challenges faced by Exelon's generation operations.[215] DC Water concludes that "[w]hen viewed in the context of the transactions' benefits for the Joint Applicants and the risks associated with the acquisition for ratepayers, it is clear that the proposed $128 per customer benefit for District ratepayers is woefully inadequate."[216]

89. **GRID2.0.** GRID2.0 states that, as a tangible benefit to ratepayers, the Joint Applicants present a CIF derived from operational savings variously estimated from $95 million over the first 5 years to roughly twice that following a settlement with the New Jersey PSC. GRID2.0 argues that, if this money is attributable to real operational savings, but the Commission allocates them to some purpose other than rate reduction while not reducing rates, the Commission would, in effect, be authorizing post-merger rates that exceed post-merger costs – a result inconsistent with just and reasonable ratemaking in a cost-based ratemaking context.[217] GRID2.0 further argues that by accepting this separate inducement, the Commission would be implicitly articulating a policy of evaluating mergers on bases other than their integral benefits and creating the appearance of putting a government privilege up for sale.[218] GRID2.0 also

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212 DC Water's Br. at 11.

213 DC Water's Br. at 16.

214 DC Water's Br. at 16, citing DC Water (A) at 24-25 (Gorman); District Government (F) at 35-39 (Chambers).

215 DC Water's Br. at 16, citing Tr. at 166-67, 180-83; 307-313; *Formal Case No. 1119*, Joint Application at Exhibit No. 1 (Exelon 2013 SEC 10K).

216 DC Water's Br. at 17.

217 GRID2.0's Br. at 5.

218 GRID2.0's Br. at 5.

contends that any allocation of merger-related cost reductions, other than pro rata to load, consumption, or some other criterion supported by the Commission's statutory authority and factual findings, would constitute discrimination.[219] Consequently, GRID2.0 asserts, the one supposed tangible result from the Proposed Merger is misrepresented and should instead be calculated as a rate reduction to consumers.[220]

90. With regard to other purported benefits, GRID2.0 maintains that:

> [B]eyond the CIF, [the other purported benefits] have one or both of the following weaknesses: either they are accompanied by no commitment (and no consequences for non-achievement); or, they are not properly attributable to the merger because they are achievable by Pepco without the merger. One or both of these weaknesses apply to the categories of "best practices," synergy estimates, distribution improvements, employment savings, load growth and load management actions, conceptual categories like "bargaining power" and "economies of scale," and the notion that Pepco will benefit from Exelon's financial support. "Best practices" remain undefined and unquantified; we don't know what they are or what they are worth.[221]

91. GRID2.0 stresses that the Joint Applicants have not made a case to substantiate their assertions that the Proposed Merger will provide improvements or benefits to District ratepayers, and the Commission should disregard them for two reasons:

> First, they are too vague and unsupported to be counted against the risks that Pepco's ratepayers will experience from this transaction. Recognizing that a benefit need not be proven to a certainty, none-the-less there [are] dozens of mergers since the mid-1980s from which the Applicants could have drawn data. Exelon has provided no evidence of improvements attributable to any merger. Second, to count as benefits from a merger benefits that are achievable without a merger is to reward shareholders of low-performing companies with acquisition premiums, because acquirers can demonstrate "benefits" from the merger.[222]

92. GRID2.0 also points out that, because Pepco does not own generation, it has no reason to support higher cost for electricity supply and should pursue policies that result in improved quality and lower costs for ratepayers. Exelon in contrast, has a fiduciary

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219 GRID2.0's Br. at 6, citing GRID2.0 (A) 121: 5-25 (Hempling).

220 GRID2.0's Br. at 6.

221 GRID2.0's Br. at 6.

222 GRID2.0's Br. at 12.

responsibility to maximize profits from its merchant generation fleet.[223] According to GRID2.0, "should Exelon acquire Pepco it would result in a fundamental and reconcilable conflict of interest between the corporate owner and the subsidiary which will pit the interest of Exelon stockholders in maximizing profit against the interest of DC ratepayers in minimizing cost."[224] GRID2.0 continues that, as a buyer of electric power, Pepco's interest is in procuring low-cost sources; as owners and traders of generation, Exelon's affiliates want high-priced sales. As a result, GRID2.0 avers that this difference in business goals can cause conflict in five policy areas: transmission access to lower cost generation supplies, wind and solar displacing nuclear and fossil, distributed energy resources, retail competition, and Standard Offer Service. GRID2.0 discusses each of these in some detail[225] to illustrate the conflicts arising from Exelon's control of Pepco, and states that, "[w]hen the PSC needs to design a request for proposals for generation, or press for changes in PJM's organized markets and transmission planning to get lower generation or transmission prices, or establish demand response and energy efficiency programs, or help consumers switch among suppliers, it no longer can rely on Pepco for objective advice: not because Pepco will be dishonest, but because it will be conflicted."[226] GRID2.0 concludes:

> Thus, with an apparent opportunity cost to ratepayers, all evidence pointing to the proposed merger being solely motivated by stockholders' financial interests, no substantive merit arising directly as a result of the merger, and significant conflicts of interest between Exelon's business objectives and those of Pepco ratepayers, GRID2.0 asserts there is no support for a finding that the merger is in the public interest and causes no harm; and respectfully requests that the PSC reject the application of the Joint Applicants.[227]

Summary of Community Comments Pertaining to Factor No. 1: Ratepayers

93. Some community commenters, as referenced in paragraph 32 *supra*, expressed concern that rates will increase under the Proposed Merger and that the level of increase would be greater than the amount of the rate relief available under the CIF that the District is being offered. Some commenters have a concern that District ratepayers will be asked to shoulder some of the costs and the risks related to Exelon's aging fleet of nuclear plants. Additionally, several organizations that provide affordable housing to families and seniors expressed concern that there were no specific commitments to provide additional assistance for low-income consumers, the majority of whom are renters who are more heavily impacted financially by

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223 GRID2.0's Br. at 13, citing Tr. at 437:1-14 (Crane).

224 GRID2.0's Br. at 13.

225 GRID2.0's Br. at 14.

226 GRID2.0's Br. at 22, citing GRID2.0 (A) 60:10-25; 61: 1-26; 62: 1-23; 63: 1-24; 64:1-3 (Hempling).

227 GRID2.0's Br. at 22.

housing and utility costs. Some of these commenters urged the Commission to use some or all of the CIF to provide rate relief assistance for low-income consumers, to reduce or eliminate arrearages for past due electric bills and to support energy efficiency programs for low-income housing to provide long term relief for renters through lower utility bills or lower rents.

Discussion Pertaining to Factor No. 1: Ratepayers

94. The record contains evidence that the transaction will affect ratepayers in four distinct ways. First, the transaction would result in the establishment of a CIF of $33.75 million for use in the District of Columbia – an amount that the Joint Applicants claim is a direct and traceable financial benefit of approximately $128 per metered customer based on a customer meter count of 264,384.[228] Parties questioned the size of the CIF allocated to the District by first questioning the fairness of using customer meter counts as the allocation factor, then questioning the derivation of the revised CIF of $33.75 million, and finally questioning the accuracy of the customer meter count used for the calculation of the District's share of the CIF. As to the fairness of the overall allocation of CIF to the District of Columbia, the record establishes that the Joint Applicants allocated an amount of the anticipated synergy savings to PHI in total based on the "Modified Massachusetts Formula," and then allocated a portion of that savings to each PHI utility operating company based on the ratio of that company's meter accounts to the total number of meter accounts in all PHI utility operating companies.[229] That resulted in the initial allocation of $14 million of the $100 million in PHI's five-year synergy savings being allocated to the District. Additionally, the record shows that the District of Columbia's portion of the CIF as it was revised in the Joint Applicants' Supplemental Direct Testimony is not based totally on the synergy savings for the customer meter counts as the Joint Applicants initially represented. Rather, the CIF was adjusted following the Joint Applicants' settlement with the New Jersey Board of Public Utilities to offer the District a CIF based on the same $128 per customer that was being used in New Jersey without regard to synergy savings, a fact that Joint Applicants witness Mr. Crane acknowledged during the hearings.[230] The Joint Applicants later represented that the revised CIF of $33.75 million represents a Net Present Value ("NPV") of 94% of the 10-year synergy savings, a fact that was disputed on the record. Thus, there is a real question as to what the $33.75 million CIF really represents and whether it actually represents synergy savings for a specific time period as the Joint Applicants later alleged.

95. Several parties have argued that using metered customers as the basis for allocating the CIF understates the allocation to the District to the direct benefit of the other jurisdictions involved in the merger proceedings. Under this allocation methodology, the District is allocated only approximately 14 percent of the Joint Applicants' PHI-wide, synergy-based CIF. If any of several other allocation factors were used, the District's CIF would have been

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228 Joint Applicants' Br. at 33, citing Joint Applicants (4A)-2 at 1, Commitment 6; Joint Applicants (4F) at 4:11-15 (Khouzami).

229 Tr. at 1985:6-1996:6 (Khouzami); District Government Confidential Cross Examination Exhibit No. 84 (Joint Applicants' Response to Data Request AOBA 1-23 Attachment A (Errata Version 1)) at 70-78; Joint Applicants' (F)-2 and (3F)-1 at 8.

230 Tr. at 57:16-58:4; 58:13-19.

higher because Pepco's District of Columbia operations represent 23 percent of all PHI electric utility operating company sales, 25 percent of total rate base for all PHI electric utility operating companies, and 24 percent of net income for all PHI electric utility operating companies in a system where almost all rates are volumetric.[231] Given that the Joint Applicants have admitted that the PHI utilities will enhance Exelon's earnings picture for the future and that this is a major reason for the acquisition, the Commission concludes that contribution to the earnings, which is measured by rate base, net income, or sales, would be a more reasonable basis for the jurisdictional allocations.[232]

96. The Commission concludes that the Joint Applicants' allocation of the CIF for the District of Columbia based on the meter accounts unreasonably and discriminatorily reduces the size of the District of Columbia's CIF and uses an allocation factor that is not consistent with accepted principles of cost causation and cost incurrence and is not reflective of the major reason for the acquisition of PHI.[233]

97. Even assuming that customer meter counts is a fair way of allocating the CIF, questions were raised during the hearing with respect to the accuracy of the customer meter count itself. First, the customer meter count used by the Joint Applicants is lower than the customer meter count used by Pepco when reporting to the Commission on smart meters. Those reports show a customer meter count of 277,222 installed as of December 2013. In addition, there are 4,318 non-AMI meters remaining to be switched out, for a total of 281,540 meters.[234] Furthermore, as noted by the District Government and DC Water, it is unclear how customers with multiple meters are being treated under this allocation method. When questioned, the Joint Applicants said they were treated as regular residential customers. Based on the record evidence at the hearing, we find the customer count number of 264,384 that was used by the Joint Applicants to be lower than the District's actual meter count of 281,540, thereby lowering the initial percentage used to calculate the CIF for the District.[235] Additionally, when calculated based on the actual number of meters, the direct and traceable financial benefit per customer drops from $128 to approximately $120 per customer.

98. Second, the Proposed Merger offered nothing new for low-income ratepayers. The Joint Applicants have not included any specific provisions for assistance to low-income customers in its application or its commitments; they merely offer to continue low-income customer assistance programs pursuant to current requirements.[236] Under questioning by Chairman Kane, Joint Applicants witness Crane conceded the "only customer assistance fund program in the District, aside from federal funds like the [Low-income Home Energy Assistance

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231 Tr. at 3383:15-3385:9 (McGowan).

232 Tr. at 205.

233 AOBA (2A) at 22:15-33:13 (Oliver), AOBA (2A)-1, AOBA (2A)-2.

234 *See* Tr. at 3387:3-7 (Commission Cross of McGowan), Commission Cross Examination Exhibit No. 2.

235 *See* Joint Applicants' (4F) at 5 (Khouzami), Tr. at 3387:3-7 (Commission Cross of McGowan).

236 Joint Applicants' (4A)-2 at 4, Commitment 21.

Program ("LIHEAP")], is the Residential Aid Discount Program [("RAD")], and that it's paid for by a $5.5 million surcharge on other customers."[237] Further, Mr. Crane agreed that the Joint Applicants were only agreeing to comply with whatever low-income programs the Commission directs. The Joint Applicants maintain that the Commission can use a portion of the CIF to further support low-income programs or provide specific rate relief to low-income customers if it so choses.

99. As noted by several parties, the Joint Applicants have offered additional assistance for low-income customers in Maryland and Delaware as part of its settlement proposals. Specifically, they have offered to zero out certain past due accounts receivables and establish a special fund to further enhance low-income assistance programs. No such offers are before this Commission in this proceeding. Consequently, we find no new or incremental benefit for the low-income customers of Pepco in the District in the Joint Applicants' commitments. All the Joint Applicants have offered here is to continue to provide post-merger the existing Commission-mandated low-income discount aid program and to provide a CIF that could be used to support low-income residents if the Commission chooses to do so.[238] If the Commission decides to use the CIF for some other purpose, there would be no new benefit for low-income customers under the Joint Applicant's proposal.[239]

100. A third effect of the transaction claimed by the Joint Applicants is the impact of the synergy savings. They claim that their proposal would pass through to District customers synergy savings that result from the transaction and as a result, ratepayers would pay lower rates than they would absent the Proposed Merger. Specifically, the Joint Applicants claim that a portion of these synergy savings are being made immediately available through the CIF (purportedly based on 94% of the 10-year synergy savings) while additional synergy savings will be passed on through rate reductions in future rate proceedings. However, as noted in AOBA's briefs, the Joint Applicants' purported commitment to pass 100% of allocable achieved synergy savings to Pepco-DC is not found anywhere in the Joint Applicants' District of Columbia Merger Commitments as presented in Appendix B to the Joint Applicants' Initial Brief or in Joint Applicants' Exhibit (4A)-2. This purported commitment, which is set out in the Joint Applicants' Initial Brief, is premised on a representation made in Joint Applicants witness Khouzami's Direct Testimony. During questioning at the hearing, however, Joint Applicants witnesses Crane and Rigby, the CEOs of Exelon and PHI respectively, confirmed that Joint Applicants Exhibit (4A)-2 contained the entirety of the Joint Applicants' commitments in this proceeding. We find that the record before us contains no commitment by the Joint Applicants to pass on 100% of allocable achieved synergy savings to Pepco-DC, nor does it contain any documentation of the specific allocation factors that will be used to determine the District of Columbia's share of any future synergy savings that might be achieved.

[237] Tr. at 516:15-518:5.

[238] Tr. at 616:4-7; Tr.619-620 (Rigby).

[239] Joint Applicants' Exhibit (A) at 13:3-8 (Crane).

101. Further, while the Joint Applicants commit that they will not seek recovery in rates of transaction costs incurred in connection with the Proposed Merger,[240] they have not made the same commitment for transition costs or costs to achieve, unlike the Settlement Agreement in *Formal Case No. 1002*, wherein the transition costs were paid by the proponents of the proposed mergers and rates were capped for several years, thereby ensuring that ratepayers paid lower rates following the merger transaction.[241] This includes, among other things, regulatory support costs classified by the Joint Applicants as transition costs, but argued by OPC to be transaction costs.[242] The Joint Applicants' proposal to characterize regulatory support costs as cost to achieve essentially eliminates shareholders' responsibility to pay for the $15 million in costs incurred to approve the Proposed Merger and places the cost of this Merger Application directly on ratepayers despite the fact that ratepayers did not ask for, and in many cases do not approve of, the proposed transaction.[243] The estimated cost to District ratepayers of these regulatory costs is about $2 million.[244] Additionally, the Joint Applicants do not commit to placing any limit on these transition costs, including the cost to achieve for this transaction. Indeed, in response to OPC cross examination regarding whether Pepco will seek to recover cost to achieve if the cost to achieve exceeds synergies, Joint Applicants witness Khouzami indicated that he thinks Pepco would.[245] In addition, when AOBA asked Joint Applicant witness Khouzami what happens when synergy savings are not achieved until year 5 and Pepco only commits to tracking savings until the next distribution rate case, (which could be in less than a year), he stated, "[b]ased on what we provide them, they will not have the fifth year synergies as actual data."[246] Mr. Khouzami further conceded that the Commission cannot verify whether the CIF offered was sufficient to match the 10-year synergy savings estimate, 94% of which purportedly comprises the $33.75 million CIF.[247] We find that there are no commitments to provide the District's share of the 10-year synergy savings other than the portion of those savings that are contained in the proposed $33.75 million CIF. In addition, the Proposed Merger places on ratepayers as transition costs the costs to achieve the Proposed Merger, including the regulatory cost of the Merger approval proceeding that would result in District ratepayers paying about $2 million of these transition costs.[248]

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240 Joint Applicants (4A)-2 at 4, Commitment 1b.

241 *Formal Case No. 1002*, Settlement Agreement at ¶ 5(d).

242 OPC's Br. at 49. We note that in Joint Applicants (4A)-2, regulatory support costs were not classified as transaction costs. The total transaction cost amounts to $338 million. Tr. at 2070.

243 Joint Applicants (3F)-1.

244 Tr. 1803:12-17.

245 Tr. 1791:5-1798:5; OPC Cross Examination Exhibit No. 85.

246 Tr. 1876:4-10; 1890:13-1891:2 (Khouzami). Tr. at 2902:11-2903:5 (McGowan) ("I think it's reasonable that we would [file a distribution rate case] within the first 12 months" after the Proposed Merger closes.)

247 Tr. 1895:11-20.

248 Joint Applicants (4A)-2 at 1, Commitments 4 and 5; AOBA Cross Examination Exhibit No. 89, the Joint Applicants' response to AOBA Data Request 4-7; AOBA Cross Examination Exhibit No. 81, the Joint Applicants'

102. Joint Applicants witness McGowan added, "Based on current capital forecasts, I estimate Pepco customers will receive a benefit of approximately $39 million based on our decision to delay the current rate-case cycle. Therefore, in addition to the many other benefits customers and the District of Columbia will receive upon the closing of the Merger, at a minimum, customers will receive approximately $73 million in benefits as a result of the merger (*i.e.*, the $33.75 million CIF and approximately $39 million in reduced rates due to Pepco's decision to delay the current rate-case cycle)."[249] Mr. McGowan conceded under questioning from the District Government that he does not actually know what the Commission would do in the event that Pepco were to make rate filings based on a full record, and he acknowledged that the Commission could deny any rate increases.[250] Mr. McGowan further conceded the Commission can grant an increase significantly smaller than requested.[251] The record evidence reveals that Pepco decided against filing a rate case because, as Mr. McGowan responded under questioning from the District Government, "[T]he merger presented a very unique opportunity to combine with Exelon to provide very significant value to our customers and our company, and we felt it was important to have the Commission, our company and all intervenors focus on the merger application and not be distracted or have another filing pending in front of the Commission."[252] Mr. McGowan further stated, in response to questioning by the District Government, that whatever rate increases, if any, that might have occurred had Pepco filed a rate case, will now not happen regardless of whether or not the merger is approved.[253] We find that the Joint Applicants' assertion that Pepco's District of Columbia customers will receive an approximate benefit of $39 million based on Pepco's decision to delay the filing of a distribution rate case is unsupported by the record evidence.

103. The Joint Applicants assert that the Proposed Merger will result in ratepayers paying lower rates than they would pay absent the Proposed Merger and benefiting from additional synergy savings. The record does not support this assertion. The Joint Applicants project that Pepco-DC's share of the cost to achieve, which totals $11 million, will outweigh synergies by $2 million in the pre-closing period.[254] In year one, the costs to achieve are $7 million, in comparison to projected synergies of $3 million. The Joint Applicants testified that they expect to file a new rate proceeding within the next year. Consequently, Pepco's next base rate case could result in District of Columbia ratepayers paying rates that are higher than they otherwise would have been due to the fact that costs to achieve will be recovered through rates.

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response to AOBA Data Request 3-9; and AOBA Cross Examination Exhibit No. 63, the Joint Applicants' response to AOBA Data Request 3-10.

[249] Joint Applicants (3L) at 13:13-20; *see also*, District Government Confidential Cross Examination Exhibit No. 120 (Joint Applicants' Response to OPC Data Request 18-112).

[250] Tr. at 3266:9-17.

[251] Tr. at 3266:18-21.

[252] Tr. at 3267:22-3268:7.

[253] Tr. at 3270:4-10.

[254] Joint Applicants (3F) at 8 (Figure CVK-2) (Khouzami); Joint Applicants (4F)-1.

If the synergy estimates are slow to materialize or do not materialize at all, the Joint Applicants could recover their cost to achieve, which are incurred pre-merger, within the first year of the Proposed Merger – before ratepayers receive any additional savings from synergies.[255] Based on the record before us, we conclude that the Joint Applicants' proposal essentially ensures that the Joint Applicants and their shareholders will recover their transition costs from the Proposed Merger, including the regulatory cost to approve the merger, while simultaneously shifting to ratepayers the risk that the promised synergies will actually be achieved and the achieved synergies will more than offset the cost to achieve.

104. A fourth effect of the transaction for ratepayers, according to the Joint Applicants, is its impact on enhanced reliability. The Joint Applicants estimate that there will be $121.6 million in tangible, quantifiable benefits as a result of their "Enhanced Reliability Commitments." Numerous parties have argued that these estimates are flawed and inflated because they are based on data from 2011-2013 and ignore reliability improvements that occurred in 2014 and the impact of the DC PLUG project that predates the Proposed Merger. For reasons that we set out in greater detail in our discussion of Factor No. 3, we acknowledge that the transaction may have some impact on Pepco's distribution system reliability, as the Joint Applicants assert, but we agree with the parties that the Joint Applicants' estimates of the tangible, quantifiable benefits of the reliability improvements that are the result of the Proposed Merger itself are substantially inflated.

105. Finally, although not a direct effect of the transaction for ratepayers, we note and find that the hearing testimony confirms that "ratepayer benefit" was not considered as an element of the competitive bidding process for the purchaser of PHI.

106. From these facts, the Commission has concluded further that the Proposed Merger will have a mixed impact on ratepayers. The Proposed Merger would provide a $33.75 million CIF, the specific nature of which has yet to be determined because the Joint Applicants left to the Commission the decision on the specific use of the CIF. Although others have suggested, and the Commission has found, that the way that the CIF was calculated and the size of the CIF being offered disadvantages District ratepayers, it is still, nevertheless, a direct and tangible benefit of the Proposed Merger and one to be considered. Additionally, under Public Interest Factor No. 1, the Commission concluded that the Proposed Merger would have a positive impact on Pepco's Net Operating Loss Carry-forward ("NOLC") position because Exelon could use Pepco's losses at a faster rate than PHI. That benefit would potentially reduce the size of Pepco's rate base which translates to a lower revenue requirement and, by extension, to potentially lower rates for District ratepayers. We do not accept as a benefit of the Proposed Merger for District ratepayers the $39 million savings asserted by the Joint Applicants from the delayed filing of a Pepco rate proceeding. First, the amount is purely speculative and is not supported on this record. Second, even if the decision to delay the filing was merger-related, it is a savings that occurred before the Proposed Merger, not one that would be an effect if the Proposed Merger is consummated.

[255] Joint Applicants (3F) at 8 (Khouzami).

107. We have concluded further that the Proposed Merger has some impacts on District ratepayers that are mixed. The Joint Applicants assert that there will be synergy savings that will benefit District ratepayers in the future such that their rates will be lower with the Proposed Merger than without it. The Joint Applicants are confident enough in their synergy savings predictions that they have used them to establish the amount of CIF funding for the District and for the other jurisdictions, and they offer to share any additional synergy savings that come in the future with District ratepayers; however, the record evidence to support their claim is inconclusive. The testimony shows that synergy savings were not the driving force behind the Proposed Merger and that the bulk of the anticipated synergy savings will come from further revisions to the shared services arrangements. Moreover, the Commission's experience with shared service arrangements for Pepco through the PHISCo has already raised concerns about the proper recording and tracking of costs and the allocation of costs to District ratepayers. On the record of this proceeding, the Commission is not persuaded that adding a second shared services company that will service a larger number of companies, both regulated and unregulated, is a clear financial benefit to District ratepayers because it exposes District ratepayers to higher potential costs if the costs are not appropriately tracked and allocated. In addition, it presents an increased regulatory burden for the Commission as we aim to ensure costs are tracked, recorded and allocated accurately from multiple service companies.

108. We have a further concern based on the record of this proceeding about whether the level of achieved synergies will be sufficient to offset the cost to achieve of the Proposed Merger. What is clear is that the Joint Applicants in this proceeding have not committed to absorb the transition costs or the cost to achieve and have proposed that these costs be borne by ratepayers, unlike the Settlement Agreement in *Formal Case No. 1002*, wherein the transition costs were paid by the proponents of the proposed merger and rates were capped for several years, thereby ensuring that ratepayers paid lower rates following the merger transaction.[256] One specific transition cost that will be assessed to DC ratepayers is their share of the $15 million regulatory costs to pay for the merger proceedings – a cost estimated to be $2 million. Consequently, in Pepco's next base rate case, that we were told would be filed as early as this year, District ratepayers could end up paying higher rates than they otherwise would have to pay due to the recovery of some of the Proposed Merger's cost to achieve.

109. We find, however, that the Joint Applicants have made commitments that protect District ratepayers from incurring several merger-related costs, such as the cost of the $1.6 billion stock premium that is being paid to shareholders and the cost related to any push down accounting that may occur as a result of the merger. However, the Joint Applicants have also made commitments under the Proposed Merger that would add additional costs that would need to be paid by District ratepayers. In addition to the transition costs (including the regulatory costs) and the cost to achieve discussed above, District ratepayers would be responsible for paying the costs related to the hiring and training of the 102 union workers that the Joint Applicants have committed to hire for Pepco-DC if the Proposed Merger is consummated. The only additional funding that would be available to cover that commitment would be the funding from the CIF.

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256 *Formal Case No. 1002*, Settlement Agreement at ¶ 5(d).

b. The effects of the transaction on shareholders

Summary of Joint Applicants' Position on Factor No. 1: Shareholders

110. Under the Proposed Merger transaction, Exelon is proposing to acquire all of the outstanding stock of PHI for $6.8 billion to be financed through debt to be issued and serviced by Exelon at the holding company level, issuing Exelon common stock and mandatory convertible securities, and from the sale of non-core assets at Exelon Generation.[257] After the purchase, PHI will become a limited liability company and an indirect, wholly owned subsidiary of Exelon with its shares held by a bankruptcy-remote Special Purpose Entity; PHI's stock will no longer be publicly traded. After the purchase and the acquisition of 1,978,000 customers from PHI with a rate base of $7 billion, Exelon would be providing distribution services to a total of 9,778,000 customers and have a rate base of $25.7 billion from its regulated companies.[258] The acquisition will diversify Exelon's business holdings and increase Exelon's corporate earnings from its regulated operations from the 50% range in 2013 to 58-61% projected for 2015 and 2016.[259]

111. The Joint Applicants testified that current PHI shareholders, as a group, will receive a payout of their shares equal to a $1.6 billion acquisition premium in the aggregate or $27.25 per share – a price that is 19.6% over the closing of PHI's common stock prior to the announcement of the Proposed Merger – and then cease to be stockholders.[260] They explain that a premium is a market-determined increment paid by an acquirer to replace all of the existing shareholders of the merged entity in a change-of-control transaction.[261] The Joint Applicants contend that there is nothing unique about Exelon's paying a premium to PHI shareholders to consummate the Merger, and asserts that such premiums are routinely paid by acquirers, as even OPC witness Dismukes conceded when questioned on this point on cross-examination.[262] The Joint Applicants conclude that the record evidence demonstrates that the premium Exelon would provide to PHI's shareholders is reasonable and consistent with broadly accepted industry practices that are necessary to properly compensate existing shareholders of a merging entity in a change-of-control transaction.[263]

112. Noting that the Commission has recognized that a "merger . . . benefits the pecuniary interests of both shareholders and the merging companies," but has held that "those

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[257] Joint Applicants (F) at 5:6-11 (Khouzami).

[258] DC Water (A)-1 at 4.

[259] Tr. at 133:11-134:7 (Crane), *see also*, Joint Applicants (A) at 9:18-20 (Crane).

[260] Joint Applicants' Br. at 40, citing Joint Applicants (3B) at 5:7-9 (Rigby).

[261] Joint Applicants' Br. at 39.

[262] Joint Applicants' Br. at 39-40, citing Tr. at 2706:12-2707:7 (Dismukes).

[263] Joint Applicants' Br. at 40.

benefits must not come at the expense of ratepayers,"[264] the Joint Applicants have committed not to seek to recover from customers of PHI's utility subsidiaries the premium Exelon is paying for PHI's shares.[265] The Joint Applicants contend that contrary to the "double leverage" argument asserted by District Government witness Wilson, they are not seeking to indirectly recover the premium it would pay to PHI stockholders through its financing of the acquisition of PHI's stock,[266] and they note that District Government witness Dr. Wilson's "double leverage" argument has been widely discredited by a large body of peer-reviewed academic literature on corporate finance and has never been adopted or endorsed by this Commission.[267] Additionally, the Joint Applicants have committed that they will not seek to recover any transaction costs from utility customers; will not record any impacts of purchase accounting at the PHI utility company-level; will maintain historical cost accounting at each of the PHI utility companies; and will not record any goodwill or fair value adjustments from the Merger at the PHI utility companies.[268]

Summary of OPC and Intervenors' Position
Pertaining to Factor No. 1: Shareholders

113. OPC notes that Mr. Rigby testified that PHI was not for sale when first approached by Exelon; however, it later accepted offers from Exelon and other bidders because PHI's board was not satisfied with the value that PHI was delivering to its shareholders.[269] OPC claims that the prospects of increasing shareholder value through an acquisition premium quickly changed the board's view about whether PHI was for sale. The Office states that Exelon made a "directional" bid to acquire PHI for $22 per share in February 2014,[270] and over the next several weeks a bidding war ensued which resulted in Exelon agreeing to purchase PHI for $27.25 per share.[271] OPC concludes that the purchase price would provide PHI's shareholders the benefit of a $1.6 billion acquisition premium, and "for its part, Exelon was willing to pay the massive

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264 Joint Applicants' Br. at 41, quoting from *Formal Case No. 951*, Order No. 11075, p. 18, rel. October 20, 1997.

265 Joint Applicants' Br. at 41, citing Joint Applicants' (3B) at 5:13-6:2 (Rigby); *see* Joint Applicants' (4A)-2 at 1, Commitment 1.

266 According to Joint Applicants witness Lapson, the concept of Double Leverage applies in any corporate sector and is not specific to utilities; it may be applied in any situation in which a parent company owns a subsidiary and provides capital to the subsidiary. Ms. Lapson explains that, the adherents of the concept of double leverage claim that the cost of capital supplied by the parent to the subsidiary is equal to the parent's cost of raising capital. If the subsidiary has its own debt, and the parent uses a mix of equity and debt to fund equity into the subsidiary, the proponents of the double leverage theory say that the debt leverage of the parent is combined with debt leverage of the subsidiary to form a double layer of debt financing (*See* Joint Applicants (3K) at 27:7-16 (Lapson)).

267 Joint Applicants' Br. at 41-42, citing Joint Applicants (3K) at 25:8-32:2 (Lapson).

268 Joint Applicants' Br. at 41, citing Joint Applicants (4A)-2 at 1, Commitments 1-3.

269 OPC's Br. at 34, citing Tr. at 868:2-3 (Rigby).

270 OPC's Br. at 34-35, citing Tr. at 351:20 to 352:1 (Crane).

271 OPC's Br. at 35, citing District Government Cross Examination Exhibit No. 1 at 1-7 (pages 25 to 31 of PHI's August 12, 2014 Definitive Proxy Statement).

acquisition premium because of the benefit the transaction provided to Exelon's shareholders."[272] OPC submits, "by acquiring PHI, Exelon would increase the proportion of earnings from regulated operations to between 58% and 61%."[273]

114. **District Government.** The District Government asserts that Exelon will in fact recover the $1.6 billion premium it proposes to pay for PHI's stock through rates, including District of Columbia retail rates, because it proposes to retain the entire benefit of the low-cost debt component of the financing of its acquisition of PHI for its shareholders, while leaving in place and increasing retail rates at the PHI utility operating companies. The District Government concludes that Exelon is paying $6.8 billion to buy a holding company that has balance sheet equity of about $4.3 billion. The District Government contends that no business pays a $1.6 billion premium over market price of stock in a $6.8 billion stock purchase transaction for the privilege of generating 2.1 percent of the $1.6 billion in premium in savings over 10 years and then giving the claimed savings away.[274] The District Government claims that Exelon's financing plan for the Proposed Merger, the basis for its $27.25 per share offer to PHI, assumes that rate-funded cash from the elimination of the PHI dividend will be used to offset Exelon's acquisition-related debt.[275] Thus, according to the District Government, absent mitigation recommended by its witness, Dr. Wilson,[276] the principal benefit of this Proposed Merger to the shareholders of Exelon and those of PHI will be achieved entirely at ratepayer expense.[277]

115. **DC Water.** As referenced in Paragraph 113 above related to OPC's arguments, DC Water also claims that a primary driver in this transaction for Exelon is a desire to increase revenue stability through the acquisition of additional regulated, rate base assets which will, inter alia, protect Exelon's dividend.[278] Additionally, DC Water avers that the transaction is being undertaken to provide very real and substantial benefits to Exelon and PHI shareholders. Thus, DC Water contends that the Commission's focus must be on how those benefits compare to the benefits that Pepco's ratepayers will realize as a result of the Proposed Merger.[279] In this regard,

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272 OPC's Br. at 35.

273 Joint Applicants (A) at 9:18-20 (Crane).

274 Tr. at 32 and 33.

275 District Government's Br. at 2, citing District Government Cross Examination Exhibit No. 92 at 17.

276 Dr. Wilson recommends that the Commission undertake one of two possible methods for mitigating this adverse impact of the Proposed Merger, if the Commission allows the Merger to proceed. First, the Commission should direct the Joint Applicants to provide a rate credit of at least $50 million per year to District customers, in order to offset the economic effect of Exelon's failure to share the benefit of cost of capital reductions attributable to its Merger financing. Alternatively, the Commission should direct that a comparable annual amount be treated by the merged company as a customer contribution to capital made over each of the first five years following the consummation of the Proposed Merger, and treated as a reduction to Pepco rate base for approximately the next twenty years. District Government (F) at 18:8-11, 19:3-20:16 (Wilson); District Government (F)-1.

277 District Government's Br. at 2.

278 DC Water's Br. at 11, quoting from District Government Cross Examination Exhibit No. 3 at 5.

279 DC Water's Br. at 11.

DC Water asserts that record evidence demonstrates that Exelon, PHI shareholders, PHI senior management and the Joint Applicants' advisors will reap handsome rewards if this transaction goes forward.[280] DC Water states that, for Exelon, it is no secret that a key Merger driver is the goal of obtaining significantly more revenue stability through increased regulated rate base operations, and from Exelon's perspective, diversification of its revenue base with additional rate base assets will provide nearly certain coverage of its dividend.[281] DC Water states that the Joint Applicants projected at the time the acquisition was announced that it would be net accretive to Exelon by $0.15 per share in 2015 increasing to $0.20 per share in 2017.[282] DC Water calculates at 860 million shares outstanding, this translates to an expectation that Exelon would realize increased annual earnings per share from the PHI acquisition of $129 million in 2015, increasing to $172 million by 2017.[283] Moreover, according to the DC Water, a significant element of the acquisition – Pepco's District operations – comes with the bill stabilization adjustment mechanism as well as the added benefit of the DC PLUG mechanism, which will allow further large rate base increases with guaranteed rate recovery. DC Water points out Joint Applicants witness Crane's description of the DC PLUG initiative as "unique" and agreed that it should be viewed by shareholders as a significant positive of the deal.[284]

116. DC Water maintains that PHI's shareholders walk away with a payday of $1.6 billion over the price of their shares immediately prior to announcement of the merger.[285] It is also noteworthy, according to DC Water, that PHI shareholders are receiving a significantly greater premium – about $387 million – than realized by Constellation shareholders, and a handful of PHI and Pepco executives stand to garner merger related compensation bonuses of $17.5 million – well in excess of the $14 million CIF that the Joint Applicants originally proposed to share with the District's ratepayers.[286] DC Water adds that the Joint Applicants' financial and legal advisors will also see a lucrative payday in this transaction.[287]

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280 DC Water's Br. at 14.

281 DC Water's Br. at 14, citing District Government Cross Examination Exhibit No. 2 at 4 (Exelon explains in its April 30, 2014 announcement of the Merger that the transaction "increases Exelon's **utility derived** earnings and cash flows, providing a solid base for the dividend and **maintaining the upside** from a recovery in power markets." (emphasis in original)).

282 DC Water's Br. at 14, citing DC Water (A)-1 at 1; District Government Cross Examination Exhibit No. 3 at 5.

283 DC Water's Br. at 14-15, citing Tr. at 2576-77 (Lapson).

284 DC Water's Br. at 15, citing Tr. at 467-68; DC Water (A)-1 at 3.

285 DC Water's Br. at 15, citing DC Water (A) at 16-17 (Gorman); Tr. at 126-27.

286 DC Water's Br. at 16, citing DC Water (A) at 16:17-18 (Gorman). District Government Cross Examination Exhibit No. 1 at 49. DC Water adds that the representations of executive merger-related compensation set forth in District Government Cross Examination Exhibit No. 1, which is PHI's definitive proxy statement dated August 12, 2014, may be understated. On cross examination, PHI's Mr. Rigby clarified that, in fact, if the Merger closes, he alone can anticipate total merger-related compensation in the range of $20 million. Tr. at 696.

287 DC Water's Br. at 16, citing Joint Applicants (F)-2 at 11; (3F)-2 at 8; AOBA (A) at 45.

Discussion Pertaining to Factor No. 1: Shareholders

117. While recognizing that a "merger . . . benefits the pecuniary interests of both shareholders and the merging companies," this Commission has held that "those benefits must not come at the expense of ratepayers."[288] The Joint Applicants have argued that the stock premium Exelon is paying to PHI shareholders will not come at the expense of ratepayers because its application includes a commitment to not seek recovery of any portion of the $1.6 billion stock premium for the PHI shares from customers of PHI's utility subsidiaries.[289] Additionally, the Joint Applicants have committed that they will not seek to recover any transaction costs from utility customers; will not record any impacts of purchase accounting at the PHI utility company-level; will maintain historical cost accounting at each of the PHI utility companies; and will not record any goodwill or fair value adjustments from the Proposed Merger at the PHI utility companies.[290] The District Government argues that Exelon will in fact recover some portion of the $1.6 billion premium it proposes to pay for PHI's stock through rates, including through District of Columbia retail rates, because it proposes to retain the entire benefit of the low-cost debt component of the financing of its acquisition of PHI for its shareholders.

118. The record evidence shows that the fair market value for PHI was determined based on the totality of the circumstances by the PHI Board of Directors through a competitive bidding process.[291] So while the size of the acquisition premium, $1.6 billion, draws headlines, it is not, standing alone, grounds for the Commission to accept or reject the Proposed Merger. The Joint Applicants' Commitments 1 and 2 shield ratepayers from bearing the costs of the acquisition premium.[292] In addition, the Joint Applicants have committed that they will not record any impacts of purchase accounting at the PHI utility company-level; will maintain historical cost accounting at each of the PHI utility companies; and, will not record any goodwill or fair value adjustments from the Proposed Merger at the PHI utility companies.[293] The Commission has considered and rejected the District Government's argument that "rate-funded cash from the elimination of the PHI dividend" will be used to pay for the premium and, therefore, should be considered in our assessment of the effect of this transaction on ratepayers. Currently, Pepco's rates incorporate a return on equity, which is money ratepayers pay to shareholders as compensation for shareholder-provided capital from PHI. PHI pays dividends to shareholders from this return on equity. Under any change of control situation, ratepayers would still pay rates that include a Commission-set return on equity to compensate shareholders for their capital contribution. Whether those funds would then be used to finance a portion of the

288 *Formal Case No. 951*, Order No. 11075, p. 18, rel. October 20, 1997.

289 Joint Applicants (3B) at 5:13-6:2 (Rigby); *see* Joint Applicants (4A)-2 at 1, Commitment 1.

290 Joint Applicants (4A)-2 at 1, Commitments 1-3.

291 *See* District Government Cross Examination Exhibit No. 1 at 25-32; Joint Applicants (3B) 3:6-12 (Rigby).

292 *See* Joint Applicants (4A)-2 at 1, Commitments 1-2.

293 Joint Applicants (4A)-2 at 1, Commitments 1-3.

premium rather than to pay a dividend to shareholders is beyond the purview of this Commission.

119. Joint Applicants witness Crane confirms that PHI shareholders will get upfront, direct cash benefit from the Proposed Merger.[294] As DC Water calculated based on Joint Applicants witness Lapson's testimony, there is an expectation that Exelon, as the new sole shareholder of PHI, would realize increased annual per share earnings from the PHI acquisition of $129 million in 2015, increasing to $172 million by 2017.[295] This purchase price provides PHI's shareholders with a 19.6% increase in its individual share price and a total shareholder benefit of a $1.6 billion acquisition premium. The transaction will also provide Exelon, as the new sole shareholder, with an increase in the proportion of its earnings that would come from regulated operations; with the percentage rising from the 50% range in 2013 to 58%-61% projected for 2015 and 2016.[296] Thus, the Commission finds, based on the record evidence that the Proposed Merger will provide very real and substantial benefits to both the existing PHI shareholders whose stock is being acquired and to Exelon as the new shareholder of PHI.

c. The effects of the transaction on the financial health of the utilities standing alone and as merged[297]

Summary of Joint Applicants' Position Pertaining to Factor No. 1: the Financial Health of the Utilities Standing Alone and as Merged

120. The Joint Applicants assert that the proposed transaction would have the effect of financially strengthening Pepco and Exelon as merged. The Joint Applicants submit that Post-Merger, Pepco will be part of a larger enterprise and, in that way, gain access to a number of additional resources, including the financial strength of Exelon.[298] In addition, the Joint Applicants confirmed that Pepco is in no danger of losing access to adequate equity funding as a result of the Proposed Merger.[299] While there is no legal requirement that Exelon fund PHI and Pepco, the Joint Applicants say this is not relevant; PHI does not have a formal legal requirement to fund Pepco, but it funds Pepco because it has an expectation that the Commission will allow a just and reasonable return on that invested capital.[300] The Joint Applicants contend that Exelon will have the same motivation and that it would be illogical for Exelon to purchase PHI if it did not intend to continue to make equity investments in PHI that will allow Pepco to grow, while

294 Tr. at 127:7-15.

295 DC Water's Br. at 14-15, citing Tr. at 2576-77 (Lapson).

296 Tr. at 133:11-134:7 (Crane), see also, Joint Applicants (A) at 9:18-20 (Crane).

297 The arguments from OPC and District Government concerning the Financial Health of the Utilities Standing Alone and as Merged were taken from the parties' discussion under Public Interest Factor No. 4.

298 Joint Applicants' Br. at 48, citing Joint Applicants (A) at 5:22-6:1 (Crane).

299 Joint Applicants' Br. at 49, citing Tr. at 2483:5-8 (Lapson Rejoinder).

300 Joint Applicants' Br. at 50, citing Tr. at 2483:9-2484:5 (Lapson Rejoinder).

providing a just and reasonable return to Exelon, thus fulfilling the expectations of Exelon's investors.[301] Furthermore, the Joint Applicants argue that Pepco's financial health as merged will be strengthened by Exelon's commitment not to rollover or refinance PHI's long-term debt,[302] its commitments on minimum equity levels for dividends,[303] its commitments on not pushing down goodwill in its accounting for the transaction,[304] its commitment to a tax indemnification provision,[305] and Exelon's ability to use PHI's NOLCs faster than Pepco could use them standing alone, thereby reducing its rate base. The Joint Applicants contend that all these measures ensure that Pepco will not be harmed by the Merger and will likely be financially stronger.[306]

121. The Joint Applicants assert that Exelon's financial strength is recognized by the financial community, and that the financial community accepts that any residual risk resulting from Exelon's unregulated business will be completely mitigated through the "gold standard" of ring-fencing measures that the Joint Applicants have included as part of its application.[307] The Joint Applicants further assert that the credit rating agencies have also recognized that the Proposed Merger will financially strengthen Pepco,[308] while the failure to close the Proposed Merger could have a negative impact on Pepco.[309]

122. The Joint Applicants further maintain that even if Exelon were unwilling or unable to fund PHI and Pepco, PHI and Pepco would still have access to adequate equity capital because Pepco's primary source of equity would be its retained earnings.[310] Joint Applicants claim that, in the event those retained earnings were insufficient due to Pepco's large capital budget, PHI and Pepco could still issue preferred stock.[311] According to the Joint Applicants,

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301 Joint Applicants' Br. at 50, citing Tr. at 2484:6-15 (Lapson Rejoinder).

302 Joint Applicants' Br. at 47, citing Joint Applicants (4A)-2 at 7, Commitment 47.

303 Joint Applicants' Br. at 48, citing Joint Applicants (4A)-2 at 10, Commitment 61.

304 Joint Applicants' Br. at 48, citing Joint Applicants (4A)-2 at 1, Commitment 1.

305 Joint Applicants' Br. at 48, citing Joint Applicants (4A)-2 at 17, Commitment 91.

306 Joint Applicants' Br. at 48, citing Joint Applicants (4K) at 4:5-5:7 (Lapson); Tr. at 2843:20-2844:7 (McGowan Rejoinder).

307 Joint Applicants Br. at 48.

308 Joint Applicants' Br. at 48, citing Joint Applicants Confidential Cross Examination Exhibit No. 17 at 1 of 7; Joint Applicants Confidential Cross Examination Exhibit No. 18 at 5 of 9.

309 Joint Applicants' Br. at 49, citing Joint Applicants (3B) at 9:4-13 (Rigby).

310 Joint Applicants' Br. at 50, citing Tr. at 2484:20-2485:1 (Lapson Rejoinder).

311 Joint Applicants' Br. at 50, citing Tr. at 2485:1-9 (Lapson Rejoinder).

after the Proposed Merger closes, PHI and Pepco will have no preferred stock outstanding, and the issuance of preferred stock would provide a source of funds for capital expenditures.[312]

123. The Joint Applicants aver that several of the OPC and intervenor proposals, if adopted, would pose a risk of financially adverse consequences to Pepco and its customers.[313] Most notably, the Joint Applicants cited OPC's recommendation for an additional rate moratorium of at least three years, which would, according to the Joint Applicants, weaken Pepco financially if implemented.[314] The Joint Applicants contend that OPC's proposed rate moratorium would be in addition to the moratorium that District of Columbia customers have already realized because Pepco did not file a rate case during the pendency of the Proposed Merger proceeding. They allege that Pepco continues to invest millions of dollars annually in infrastructure and reliability improvements for its customers. If Pepco was subject to an additional three-year moratorium, and continued to invest in infrastructure and reliability improvements based on its current capital forecast, Pepco's return on equity would fall to approximately 3.2% by the end of December 2018.[315] The Joint Applicants contend that such a result would be unreasonable and, therefore, they argue that Pepco should be allowed to request timely recovery of the investments it is making in its infrastructure by filing a rate case immediately following approval of the proposed transaction. The Joint Applicants assert that an additional rate moratorium of any duration would put pressure on investments and spending at Pepco, and would make any incremental increases in investment levels very challenging.[316]

124. The District Government proposed the imposition of a number of requirements before the Proposed Merger is approved that the Joint Applicants have conservatively estimated to cost between $900 million and $1.1 billion, excluding the accounting for District Government witness Dr. Wilson's double leverage penalty.[317] According to the Joint Applicants, the cost impact of the District Government's total recommendation is approximately 21-25 times the annual earnings of the Pepco-DC distribution operations and approximately 75-89 times the total net synergies of $14 million the transaction will generate for Pepco's District of Columbia customers during the first five years after the Proposed Merger closes. The Joint Applicants note further that, due to the existence of the "most favored nation" clauses in the Joint Applicants' settlements in New Jersey, Delaware, and Maryland, if the District Government's recommendations were implemented, then PHI-wide the total cost of the proposed transaction for the Joint Applicants would be between approximately $7.35 billion and $8.75 billion.[318]

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312 Joint Applicants' Br. at 50, citing Tr. at 2485:10-13 (Lapson Rejoinder).

313 Joint Applicants' Br. at 51, citing Joint Applicants (3K) at 23:17-18 (Lapson).

314 Joint Applicants' Br. at 51, citing OPC (A) at 30:3-7; 135:13-17 (Dismukes).

315 Joint Applicants' Br. at 51, citing Joint Applicants (3L) at 17:9-11 (McGowan).

316 Joint Applicants' Br. at 51.

317 Joint Applicants' Br. at 52, citing Joint Applicants (3L) at 3:20-22 (McGowan).

318 While these matters were presented in the testimony of District Government witnesses, the District Government did not include in any argument in its briefs regarding this matter.

Summary of OPC and Intervenors' Position Pertaining to Factor No. 1: the Financial Health of the Utilities Standing Alone and as Merged

125. OPC submits that PHI and Pepco do not benefit from Exelon's "strong balance sheet" as the Joint Applicants contend.[319] OPC argues that its witness Woolridge demonstrated that neither Joint Applicants witness Crane nor Joint Applicants witness Lapson cite any "traceable" benefits to Pepco or its customers from the financial strength of Exelon.[320] In fact, OPC contends that OPC witness Woolridge notes a number of factors that indicate Exelon is riskier than Pepco, including: (1) higher risk associated with its commercial generation business (57% of which comes from nuclear); (2) lower S&P credit ratings; (3) a significantly higher percent of unregulated revenues; (4) a dividend cut in 2013; (5) very poor long-term stock performance; and (6) the need to maintain a higher common equity ratio due to its risk.[321]

126. OPC asserts that, from the perspective of the markets, if any benefits are conferred by the proposed transaction, the benefits go to Exelon and not Pepco.[322] OPC also asserts that, as analysts' reviews indicate, the acquisition of PHI's relatively stable distribution business would be beneficial to Exelon and fit the current market theme of energy companies buying more regulated assets.[323] According to OPC, the tangible benefits that Exelon would derive from Pepco's stability are evidenced in S&P's decision to use Pepco's "medial volatility tables to assess the pro forma company's financial measures because of the meaningful increase in regulated cash flows."[324] In addition, OPC claims that S&P noted that, post-transaction, Exelon's regulated base would be nearly 50% of cash flows and would provide 80-90% of the parent company's external dividend. In sum, OPC concludes that Mr. Crane's claims that the financial strength of Exelon is a benefit to PHI and Pepco should be disregarded, as they are not supported by any evidence.[325]

127. OPC further submits that the Joint Applicants failed to demonstrate that the proposed transaction would not negatively impact ratepayers with respect to the use of PHI's NOLCs.[326] Based on the testimony provided by OPC witness Ms. Ramas, OPC asserts that the acquisition of PHI by Exelon will trigger the Internal Revenue Code ("IRC") Section 382

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[319] OPC's Br. at 108.

[320] OPC's Br. at 108.

[321] OPC's Br. at 108-109 citing OPC (D) at 13:5-22, 14: 1-17 (Woolridge).

[322] OPC's Br. at 109.

[323] OPC's Br. at 109, citing OPC (D) at 15:7 to 19:1 (Woolridge).

[324] OPC's Br. at 109, citing OPC (D)-6 (Standard & Poor's Ratings Services, Exelon Corp. and Pepco Holdings Ratings are Affirmed on Acquisition Announcement, April 30, 2014, p.5. Document provided as Joint Applicants Confidential Response to OPC Data Request 11-5, Attachment A, pp. 295-305).

[325] OPC's Br. at 109.

[326] OPC's Br. at 110.

limitation to tax carry forwards.[327] OPC also asserts that IRC Section 382 places limitations on the amount of NOLs that can be used annually;[328] however, OPC states the total amount of annual IRC Section 382 limitation on the use of Pepco's and PHI's NOLCs has not been finalized at this time. Based on the Joint Applicants' Response to Confidential Bench Data Request No. 5, OPC argues that it is clear that, as of April 17, 2015, the Joint Applicants have not, and cannot, provide a final IRC 382 limitation analysis.[329]

128. OPC witness Ramas explains the significance of this issue as well as a potential consequence of a NOLC position:

> [I]n Pepco's last rate case, "the fact that PHI and Pepco were in a NOLC position caused the ADIT offset to rate base to be lower than it would otherwise be absent the NOLC position. If the IRC Section 382 annual limitations on the use of the NOLCs causes the NOL deferred tax asset to reverse more slowly on Pepco's books than what would transpire absent the annual limitations on the use of the NOLs, a higher rate base could result. This is due, in part, to a potentially longer period for utilizing the NOLCs due to the annual limitations."[330]

According to OPC, at the hearing Commissioner Fort asked Joint Applicants witness Khouzami whether he was familiar with the Commission's order in Pepco's last rate case, *Formal Case No. 1103*, where there was an issue with respect to how the NOLC was being treated for rate base purposes.[331] OPC claims that Mr. Khouzami's response was far from reassuring.[332] According to OPC, although he did not know "the specifics of what was discussed" in the last rate case, Mr. Khouzami stated that he "think[s]:" (1) Item 1 of Exhibit (4A)-2 "should alleviate some concerns about limitations of net operating loss that could be used going forward due to the 382 limitation;"[333] and (2) "we'll be in the same position pre-merger versus post-merger."[334] This type of speculation, in OPC's opinion, does not come close to satisfying the Joint Applicants' burden of demonstrating that the transaction is in the public interest.[335]

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327 OPC's Br. at 111, citing OPC (C) at 28:11-12 (Ramas).

328 OPC's Br. at 111, citing OPC (C) at 28:12-13 (Ramas).

329 OPC's Br. at 111.

330 OPC's Br. at 111, citing OPC (C) at 29: 10-17 (Ramas).

331 OPC's Br. at 111.

332 OPC's Br. at 111.

333 OPC's Br. at 111-112, citing Tr. at 2143:7-10.

334 OPC's Br. at 112, citing Tr. at 2143:4-5, 2145:2-3.

335 OPC's Br. at 112.

129. OPC states that a compounding concern is whether the NOLC issue will be exacerbated by the transaction.[336] OPC notes that Commissioner Fort explored this issue at the hearing, asking, "[w]ith the new structure and with Exelon coming in, are we going to have some of the same issues that we faced in a prior case, but on a larger level because of how Exelon . . . treats their net operating loss and how they interact with their utilities in that regard?"[337] OPC contends that Mr. Khouzami dodged this straightforward question, contending that the Joint Applicants are "mindful of previous Commission Orders."[338] OPC notes, as Commissioner Fort observed, that response does not "tell me whether or not there is actually an issue."[339]

130. In an apparent attempt to respond to Commissioner Fort's questions, OPC states that the Joint Applicants provided a Confidential Response to Bench Data Response No. 5.[340] As explained at the hearing, OPC argues that this data response indicates, "Exelon anticipates being able to consume PHI's NOLC, net operating loss carry forward by 2017."[341] In addition, OPC submits, "PHI and Pepco anticipate they will not be able to use the NOLC carry-forward fully to 2019." [342] OPC asserts that, while the representations in this data response are a step forward, as OPC witness Ramas noted, they do not "alleviate my recommendation that that information, once it's known, be reported to the Commission so it has it to evaluate in future proceedings."[343] In addition, while the Joint Applicants suggest that Commitment 91 on Exhibit (4A)-2 might address concerns about the NOLC, OPC contends that there is no specific language in Commitment 91 regarding this point.[344]

131. OPC submits that an additional reporting requirement serves the important purpose of protecting Pepco's District ratepayers from excessive costs.[345] Put simply by Commissioner Fort at the hearing, "the concern, of course, that the Commission has is if it's not timely used, the rate base would be higher than it needs to be, and if it's a higher rate base, it is a higher cost to D.C. ratepayers."[346] OPC states that, if the Commission approves the transaction, this concern should be addressed through a mandatory, enforceable commitment requiring the Joint Applicants to file a report with the Commission describing, in detail, the amount of any

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336 OPC's Br. at 112.

337 OPC's Br. at 112, citing Tr. at 2144:13-17.

338 OPC's Br. at 112, citing Tr. at 2145: 7-8.

339 OPC's Br. at 112, citing Tr. at 2146:5-6.

340 OPC's Br. at 112.

341 OPC's Br. at 112, citing Tr. at 2755:11-13.

342 OPC's Br. at 112, citing Tr. at 2755:20-22.

343 OPC's Br. at 112-113, citing Tr. at 2756:5-8.

344 OPC's Br. at 113.

345 OPC's Br. at 113.

346 OPC's Br. at 113, citing Tr. at 2149:18-22.

IRC Section 382 limitations on the use of PHI's NOLC post-transaction as well as whether this position will be further impacted by how Exelon treats its NOLs.[347] OPC submits that requiring a filing of a detailed description of the impact of any IRC Section 382 limitations will help ensure that the transaction is in the public interest.[348]

Discussion Pertaining to Factor No. 1: the Financial Health of the Utilities Standing Alone and as Merged

132. The effects of the Proposed Merger on the financial health of the Joint Applicants, Exelon, PHI and Pepco, standing alone and as merged are the focus of our inquiry here.

133. **Effect on the Financial Health of Exelon.** The record evidence has established that there are significant benefits that accrue to the financial health of Exelon from the Proposed Merger. Specifically, the evidence submitted indicates that the acquisition of PHI's relatively stable distribution business would be a boon to Exelon and fit the current market theme of energy companies buying more regulated assets.[349] S&P noted that, post-transaction, Exelon's regulated base would be nearly 50% of cash flows and would provide 80%-90% of the parent company's external dividend.[350] The very real benefits of the transaction to Exelon are further evidenced by S&P's decision to "employ the medial volatility table" in their credit assessment because of the meaningful increase in regulated cash flows.[351]

134. Joint Applicants witness Lapson testified that there is no real difference between the long-term credit ratings of PHI and its utility subsidiaries and the long-term credit ratings of Exelon and its utility subsidiaries. However, during cross-examination, Ms. Lapson acknowledged that although Exelon and PHI may have similar credit ratings at a point in time, it is not necessarily a sound basis for a conclusion that their credit ratings will remain similar over time.[352] After reviewing the credit ratings, bonds and CDs spreads as presented by the Joint Applicants and parties in this proceeding, the Commission concludes that the record does not clearly demonstrate that the Proposed Merger will add to Pepco's financial strength, nor does it show an immediate harm either. The Commission notes our concerns that the pressure to meet

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[347] OPC's Br. at 113.

[348] OPC's Br. at 113.

[349] OPC (D) at 15:7 to 19:1 (Woolridge).

[350] *See* OPC (D)-6 (Standard & Poor's Ratings Services, Exelon Corp. and Pepco Holdings Ratings are Affirmed on Acquisition Announcement, April 30, 2014, p.5. Document provided as Joint Applicants Confidential Response to OPC Data Request 11-5, Attachment A, pp. 295-305)

[351] *See* OPC (D)-6 (Standard & Poor's Ratings Services, Exelon Corp. and Pepco Holdings Ratings are Affirmed on Acquisition Announcement, April 30, 2014, p.5. Document provided as Joint Applicants Confidential Response to OPC Data Request 11-5, Attachment A, pp. 295-305) (S&P currently uses a standard volatility table for assessing Exelon because of Exelon's non-regulated business. This table has a more rigorous "financial ratio" to account for the added risks.)

[352] Tr. at 2523:8-17 (Lapson Cross).

the earnings accretion expectations and the synergies necessary to justify the purchase could lead to pressures for cost cutting and investment curtailments that may be detrimental to customers.[353]

135. **Effect on the Financial Health of PHI.** With respect to PHI, the Commission begins by noting that Joint Applicant witness Joseph Rigby, PHI's CEO, testified that prior to receiving the acquisition offer from Exelon "the board had confidence in a stand-alone plan. [However, [t]he board was not satisfied that we were not delivering competitive shareholder value."[354] Exelon's offer to acquire all of PHI's stock for $6.8 billion, including a $1.6 billion stock premium for shareholders, clearly delivered significant shareholder value to the PHI Board. Mr. Rigby stated that although PHI is not cash positive, given the current heavy construction schedule, Pepco has a strong financial profile as a stand-alone company and PHI is able to issue long-term debt.[355] Further, Mr. Rigby stated "[i]f the merger does not proceed, PHI had a dialogue with its Board of Directors that it needs to be prepared for multiple outcomes . . . we are continuing to think through and not to be caught flat-footed should the outcome not play out the way we want it to."[356] In addition, the Commission notes that the November 18, 2014 credit ratings contained in Joint Applicants witness Lapson's supplemental direct testimony shows that PHI's "middle of three ratings" of "BBB" is the same as Exelon's. The Commission also notes that the most recent confidential Moody's credit opinion of Pepco (issued on January 29, 2015) indicates that it has a stable financial profile and adequate sources of liquidity.[357] In addition, the April 10, 2015 Fitch Ratings indicate that the pending merger has no direct effect on Pepco's credit quality.[358] Furthermore, the record establishes that Exelon committed to pay PHI $180 million as a reverse break-up fee. By the close of the record, $144 million had been paid to PHI in exchange for 14,400 shares (each share valued at $10,000) of preferred stock and additional payments of $18 million were due on April 27 and July 26, 2015 ($36 million in total). Given the testimony of witness Rigby, his characterization of the Board having confidence in PHI's stand-alone plan, and the credit opinion of Moody's and Fitch with regards to Pepco, the Commission concludes that PHI is financially healthy as a stand-alone company and would continue to be so if the Proposed Merger is not consummated. If the Proposed Merger were consummated, PHI would cease to exist as a stand-alone company. PHI's post-merger financial health would largely be tied to the financial health of its parent's company, Exelon, and the decisions that it makes as it operates the PHI subsidiary utilities.

136. **Effect on the Financial Health of Pepco.** With respect to Pepco, the record shows that Exelon's CEO, Mr. Crane, touted the financial strength of Exelon and noted that it would be a benefit to Pepco. However, Mr. Crane testified that over the "first five years of

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353 OPC (D) at 8:10-13 (Woolridge).

354 Tr. at 867:20-868:12.

355 Tr. at 869:10-17.

356 Tr. at 780:18-781:5.

357 *See* Joint Applicants Confidential Cross Examination Exhibit No. 30.

358 *See* Joint Applicants Confidential Cross Examination Exhibit No. 31.

[Exelon] joining with PEPCO, there's negative cash flows at PEPCO. So we would be flowing cash equity into PEPCO to support the current commitments."[359] Mr. Crane deferred questions about the details of the total negative cash flow to Joint Applicants witness Mr. Khouzami.[360] However, when AOBA questioned Mr. Khouzami about Pepco's negative cash flows in the years following the merger, Mr. Khouzami stated, "I have not done the analysis."[361] Therefore, we are left with a record that has inconsistent testimony on the immediate financial impact on Pepco with respect to its cash flow after the Proposed Merger closes.

137. OPC witness Woolridge testified that there are a number of factors that indicate Exelon is actually riskier than Pepco, including: (1) higher risk associated with its commercial generation business, 57% of which comes from nuclear; (2) lower S&P credit ratings; (3) significantly higher percent of unregulated revenues; (4) a dividend cut in 2013; (5) very poor long-term stock performance; and (6) a need to maintain a higher common equity ratio due to its risk.[362] While Exelon's financial health may be at higher risks for the reasons cited by OPC's witnesses, these are risks that would have been known and factored into Exelon's credit ratings by the three credit rating agencies whose ratings of Exelon, PHI and Pepco have been entered into our record.

138. The Proposed Merger also changes how Pepco will access capital by removing some of the equity issuance decisions that are currently made at the Pepco or PHI level and taking it up several layers of management to the Exelon Board as set out in the Delegation of Authority document. The Proposed Merger would also result in Pepco competing with a larger pool of companies (*i.e.*, seven as opposed to four regulated utilities and Exelon's unregulated generation affiliates) for additional investment dollars.

139. Another area where the Proposed Merger has a potential impact on the financial health of Pepco is in regard to its use of its NOLC. As explained by OPC witness Ramas, the acquisition of PHI by Exelon triggers the Internal Revenue Code Section 382 limitation to tax carry forwards.[363] According to OPC, IRC Section 382 places limitations on the amount of NOLs that can be used annually. However, the total amount of annual IRC Section 382 limitation on the use of the PHI's NOLC has not been finalized at this time. In response to OPC's question regarding the Joint Applicants' best estimate of the annual IRC Section 382 limitation on the use of PHI's NOLC, the Joint Applicants stated they "have made no such computation or estimate."[364] In addition, based on the Joint Applicants' Response to Confidential Bench Data Request No. 5, the Commission notes that, as of April 17, 2015, the Joint Applicants have not, and cannot, provide a final IRC 382 limitation analysis.

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359 Tr. at 512:13-17 (Crane).

360 Tr. at 513:15-20 (Crane).

361 Tr. at 1941:15-19 (Khouzami).

362 OPC (D) at 13:5-22, 14: 1-17 (Woolridge).

363 OPC (C) at 28:11-12 (Ramas).

364 OPC (C)-16.

140. At the hearing, Commissioner Fort asked Joint Applicants witness Khouzami whether he was familiar with the Commission's order in Pepco's last rate case, *Formal Case No. 1103*, where there was an issue with respect to how Pepco's NOLC was being treated for rate base purposes. Although Mr. Khouzami did not know "the specifics of what was discussed" in the last rate case, he stated that he "think[s]:" (1) Commitment 91 of Exhibit (4A)-2 "should alleviate some concerns about limitations of NOLs that could be used going forward due to the 382 limitation"[365] and (2) "we'll be in the same position pre-merger versus post-merger."[366]

141. Subsequently, the Joint Applicants provided a Confidential Response to Bench Data Request No. 5.[367] As explained at the hearing, OPC confirms that this data request response indicates that Exelon anticipates being able to consume PHI's NOLC, net operating loss carry forward by 2017.[368] In addition, PHI and Pepco anticipate they will not be able to use the NOLC carry-forward fully until 2019.[369] This forecast would allow the Pepco NOLCs to be used two years before PHI would be able to fully consume them in the absence of the Merger.[370] Based on this evidence, the Commission concludes that Pepco's ability to use its NOLCs will be enhanced by the Proposed Merger to the benefit of District ratepayers; however the amount of the purported benefit has not been quantified on the record.

142. The Commission concludes, that based on the record, the initial impact of the Proposed Merger on Pepco's cash flow is inconclusive while the impact on its NOLC position is positive. The record evidence further indicates that there would be no significant improvement in Pepco's credit ratings due to the Proposed Merger. Pepco will face competition for shareholder capital from a larger number of regulated affiliates as well as a number of unregulated affiliates who may need resources to stem losses. Finally, both Pepco and PHI, as subsidiaries of Exelon, will be exposed to additional financial risks from the Proposed Merger due to Exelon's unregulated businesses. The Joint Applicants have proposed a number of ring-fencing commitments in Attachment 4(A)-2 to provide a level of protection for PHI, Pepco and Pepco's ratepayers. The presence of these strong ring-fencing provisions mitigates the additional financial risks that are present from the unregulated Exelon businesses so they are less harmful to District ratepayers if the Proposed Merger is consummated.

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[365] Tr. at 2143:7-10 (Commission Cross of Khouzami).

[366] Tr. at 2143:1-14 (Commission Cross of Khouzami).

[367] Joint Applicants Confidential Cross Examination Exhibit No. 26.

[368] Tr. at 2755:11-13.

[369] Tr. at 2755:20-22.

[370] Tr. at 2755:11-22.

d. The effects of the transaction on the economy of the District

Summary of Joint Applicants' Position Pertaining to Factor No. 1: the Economy of the District

143. The Joint Applicants submit that the $33.75 million CIF and the strengthened reliability commitments of the Joint Applicants will also create significant benefits for the District of Columbia's economy. In addition, the Joint Applicants contend that the District economy will also be benefited by new jobs that will come to the District as a result of the merger. Finally, they contend the District economy will be enhanced by the Joint Applicants' commitments to do business with minority owned businesses and to provide some level of charitable contributions to nonprofits in and around the District.

144. Using the IMPLAN social accounting economic model – the same model used by the Mayor's Power Line Undergrounding Task Force and District of Columbia and regional entities[371] – Dr. Tierney calculated that the changes in economic activity associated with the CIF and enhanced reliability will lead to $168.4 million to $260.5 million in overall economic value to the District of Columbia and 1,506 to 2,407 new job-years.[372] The substantial range in the projected economic benefits arising from these Proposed Merger commitments is attributable to three possible scenarios Dr. Tierney used to illustrate the effects of how the Commission might determine to spend the CIF, *i.e.*, a bill credit to each customer, a bill credit to low-income customers, or spending in the form of energy efficiency measures based on the current programs of the District of Columbia's Sustainable Energy Utility ("SEU").[373] Dr. Tierney's scenario showed that spending the CIF on energy efficiency (for example, the purchase and installation of more energy efficient appliances or equipment) results in a substantially larger economic impact and more job-years.

145. The Joint Applicants have made further commitments to ensure that the Merger will result in substantial positive economic benefits. These include a good-faith effort by Pepco to hire 102 unionized employees and the transfer of certain non-regulated operations to the District of Columbia, which are expected to result in the Proposed Merger being job positive. These jobs will be in addition to the 1,506 to 2,407 job-years in the District of Columbia projected by Dr. Tierney to flow from the broader economic benefits of the CIF and customer savings associated with the Joint Applicants' reliability commitments.[374] The Joint Applicants also expected the merger to produce incremental tax revenues to the District of Columbia of

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[371] *See* Joint Applicants (G)-2 (listing use of IMPLAN by Mayor's Office and other District and regional entities).

[372] Joint Applicants' Br. at 54. One full time job-year is equivalent to one full-time job lasting one year or two half-time jobs lasting one year. As Dr. Tierney explained, her use of jobs and job-years was consistent with normal conventions in reporting employment information. *See* Joint Applicants (3G) at 16:10-17:4 n.22 (Tierney).

[373] Joint Applicants' Br. at 54.

[374] Joint Applicants' Br. at 56.

approximately \$6.2 million to \$10.8 million.[375] Also after the Proposed Merger closes, the Joint Applicants estimate that the total District of Columbia tax paid by the Joint Applicants will increase.[376] The Joint Applicants also offered commitments to maintain PHI's supplier diversity programs[377] and PHI's charitable giving. With respect to the latter, the Joint Applicants have committed to continue providing charitable contributions and support to local nonprofits for at least ten years following consummation of the Proposed Merger at an annual average of at least \$1.6 million.[378] Joint Applicants witness Mr. Crane also testified that "Exelon is making commitments to maintain and promote the PHI utilities' low-income customer assistance, energy-efficiency and demand response programs, and those commitments are separate and apart from the commitment to create and fund the Customer Investment Fund."[379]

146. The Joint Applicants anticipate that the Proposed Merger will be job positive for the District of Columbia for several reasons. First, Exelon has committed that, for a period of two years following consummation of the Proposed Merger, there will be no net reductions in the employment levels of Pepco due to involuntary attrition as a result of the Proposed Merger integration process.[380] Second, the Joint Applicants will make good-faith efforts to hire an additional 102 union employees in the District of Columbia within the first two years after the Proposed Merger closes.[381] These employees are expected to fill District of Columbia utility field operations positions.[382] Third, Exelon will move PHI's competitive business unit, PES, from Arlington, Virginia into the PHI/Pepco Edison Place building located in the District of Columbia within one year following completion of the Merger. According to the Joint Applicants, there will be some job reductions at PHI's non-utility companies – primarily at PHISCo – and it is these job reductions that will be passed through to Pepco's customers in future rate cases as synergy savings.[383]

Summary of OPC and Intervenors' Position Pertaining to Factor No. 1: the Economy of the District

147. OPC challenges the Joint Applicants' contention that the proposed transaction will produce 1,506 to 2,407 new jobs, \$168.4 to \$260.5 million in economic benefits, and \$6.2

375 Joint Applicants' Br. at 56, citing Joint Applicants (4G) at 4, Table SFT-(4G)-1 (Tierney); Tr. 2133:1-4 (Commission Cross of Khouzami).

376 Joint Applicants' Br. at 56, citing Tr. at 2133:1-14 (Commission Cross of Khouzami).

377 Joint Applicants' Br. at 56, citing Joint Applicants (4A)-2 at 4of 17, Commitment 20.

378 Joint Applicants' Br. at 60, citing Joint Applicants (4A)-2 at 4 of 17, Commitment 22.

379 Joint Applicants' Br. at 60, quoting Joint Applicants (A) at 13:8-11 (Crane).

380 Joint Applicants' Br. at 57, citing Joint Applicants (C) at 16:18-21 (O'Brien).

381 Joint Applicants' Br. at 57, citing Joint Applicants (3F) at 4:17-19 (Khouzami).

382 Joint Applicants' Br. at 57, citing Tr. at 2866:14-18 (McGowan Cross).

383 Joint Applicants' Br. at 58.

million to $10.8 million in incremental tax revenues. OPC claims that the purported benefits to the District economy as submitted by Joint Applicants witness Tierney are either grossly overstated or are presented in a misleading manner.[384] The Office asserts that Dr. Tierney's analysis is flawed because it ignores Pepco's improved reliability performance in 2014. OPC states:

> [B]y strategically ignoring Pepco's significantly improved reliability performance in 2014, Exelon compares its reliability commitment to a baseline that: (1) gives undue weight to the period before Pepco began taking measures to improve its reliability performance; and (2) assumes that Pepco's reliability performance will not improve beyond the 2011 to 2013 average[,] even through substantial evidence suggests Pepco's reliability will improve. The effect of Dr. Tierney's analysis is to overstate the positive impact of Exelon's reliability proposal. It is beyond dispute that an impact analysis that ignores Pepco's 2014 reliability performance results in overstated projections of new jobs, economic benefits, and incremental tax revenues.[385]

148. OPC also criticizes Dr. Tierney's projection of 1,506 to 2,407 new jobs as being presented in "job years." OPC does not dispute that a job-years analysis is an acceptable approach for performing an economic analysis; however, it contends that a "job years" analysis does not tell the complete picture in this regulatory proceeding. Assuming that the transaction results in new jobs at the low end of Dr. Tierney's projected range, Dr. Tierney explained that the proposed transaction could actually result in 50 new jobs, not 1,500 new jobs.[386] However, the Joint Applicants did not explain that important nuance in making representations to the public. Rather, according to OPC, "they simply and resolutely represented to the public that 'the merger commitments *will produce approximately 1,500 to 2,400 new jobs*.'" OPC submits that this "misrepresentation" distorts the true impact of the transaction and overstates the induced and indirect impacts.[387]

149. According to OPC, several components comprise Joint Applicants' commitments regarding employment: (1) Dr. Tierney's assessment of jobs that will purportedly be created as an indirect or induced impact of the proposed transaction (discussed in the preceding paragraph); (2) a commitment to use good-faith efforts to hire 102 new union employees;[388] (3) a commitment to move at least 50 employees of Pepco Energy Services from Arlington, Virginia

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384 OPC's Br. at 40.

385 OPC's Br. at 41.

386 OPC's Br. at 41. OPC clarifies that under a "jobs years" analysis, 50 jobs that lasted for 30 years would be presented as 1,500 jobs. OPC's Br. at 41, citing Tr. at 2465:4-8 (Tierney).

387 OPC's Br. at 42.

388 OPC's Br. at 42, citing Joint Applicants (4A)-2 at 4, Commitment 17.

to PHI's office at Edison Place in the District;[389] (4) a commitment that there will be no net involuntary attrition for a period of two years following approval of the transaction;[390] and (5) a commitment to provide Pepco employees with compensation and benefits that, in the aggregate, are at least as favorable as compensation and benefits that employees received immediately before the Application was filed.[391] In addition to Dr. Tierney's assessment of jobs being flawed as set forth in the previous paragraph, OPC claims that the other four employment commitments also lack substance.[392]

150. OPC asserts first that the Joint Applicants have not shown that the commitment to use good-faith efforts to hire 102 new union workers will result in any *incremental* increase in the workforce.[393] Second, while Mr. Crane claims that the commitment to hire 102 new union employees is a benefit of the transaction because Pepco does not "have the resources" to hire these employees,[394] OPC submits that there is no basis for Mr. Crane's claim, because Mr. Rigby confirmed that Pepco has never represented that it lacks the resources to hire new employees.[395] Third, there are costs associated with these employees.[396] To the extent the 102 new employees reflect incremental additions to the workforce (*i.e.*, the new employees are not simply replacing employees that have retired), the Joint Applicants will seek to recover the costs of the new employees through rates.[397] If the 102 new employees are simply filling vacancies that are caused by retirements, the costs associated with the new employees are already reflected in Pepco's current budgets.[398] Thus, to the extent the commitment to hire 102 new employees is an incremental benefit of the transaction; OPC claims it is a ratepayer-funded benefit for which Exelon is seeking to take credit.

151. Regarding the Joint Applicants' commitment to relocate at least 50 employees of PES to the District of Columbia, OPC alleges that the Joint Applicants: (1) have not quantified the alleged benefit of this proposal; (2) have not established qualitatively what this alleged benefit is; and (3) have not established a time commitment for this alleged benefit.[399] OPC notes further that only two of the 50 PES employees are District residents. Thus, according to the

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389 OPC's Br. at 42-43, citing Joint Applicants (4A)-2 at 4, Commitment 18.

390 OPC's Br. at 43, citing Joint Applicants (4A)-2 at 3, Commitment 15.

391 OPC's Br. at 43.

392 OPC's Br. at 42-43.

393 OPC's Br. at 43.

394 OPC's Br. at 44, citing Tr. at 115:16-20 (Crane).

395 OPC's Br. at 44, citing Tr. at 628:22 to 629:4 (Rigby).

396 OPC's Br. at 44, citing Tr. at 2874:7-9 (McGowan).

397 OPC's Br. at 44-45, citing Tr. at 113:17-21 (Crane).

398 OPC's Br. at 45, citing Tr. at 2874:11-16 (McGowan).

399 OPC's Br. at 45, Tr. at 1846:11-17.

Office, this commitment does not have a substantial impact on the important consideration of creating or maintaining jobs for District residents. To the extent these two District residents are terminated as part of the effort to achieve labor synergy savings, OPC contends that this aspect of the proposal could have a negative impact on the District.[400]

152. OPC also questions the motives of the Joint Applicants in committing to no net voluntary attrition for only two years, especially since it committed to a longer period in New Jersey. OPC concludes that the Joint Applicants have not provided substantial evidence to support a finding that a two-year commitment is in the public interest. Rather, according to OPC, the basis for the two-year period is simply that Exelon used a two-year period in its acquisition of Constellation Energy and "that met the test."[401] The Office maintains that, under this logic, there is no basis for not using the longer period that "met the test" in New Jersey.[402] As for the Joint Applicants' commitment that, for a period of two years after the transaction is consummated, Exelon will provide Pepco employees with compensation and benefits that, in the aggregate, are at least as favorable as compensation and benefits that employees received immediately before the Application was filed, OPC again asserts that the Joint Applicants do not provide any evidence supporting the adequacy of this two-year period. In fact, OPC argues, the only evidence that the Joint Applicants did supply, the New Jersey Settlement, which ensures comparable compensation and benefits for a period of at least five (5) years, demonstrates that a two-year period is inadequate.[403]

153. **AOBA.** AOBA submits that the Joint Applicants' charitable contributions commitment is particularly problematic since this Commission does not presently regulate Pepco's charitable contributions and there is no evidence that it would be in the public interest for this Commission to exercise oversight or review authority with respect to charitable contributions made subject to the Joint Applicants' proposed charitable contributions commitment.[404] Further, AOBA submits that the parameters of the Joint Applicant's proposed charitable contributions commitment are constructed in a manner that would include contributions made by Exelon and by Exelon affiliates that are not subject to any form of regulation by this Commission. In addition, the commitment is made to the achievement of a ten-year average level of charitable contributions, as opposed to an annual minimum level of contributions.[405] AOBA also states that no procedures are proposed for review of contributions actually made or guidelines established for compensation of the District if the committed ten-year average level of contributions is not achieved and that substantial unanswered questions remain with respect to the manner in which this Commission would be able to ensure that the proposed commitment

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[400] OPC's Br. at 46.

[401] OPC's Br. at 47, citing Tr. at 76:19 to 77:4 (Crane).

[402] OPC's Br. at 47.

[403] OPC's Br. at 47-48.

[404] AOBA's Br. at 86-87.

[405] AOBA's Br. at 87.

was satisfied.[406] AOBA also asserts that the proposed charitable contributions commitment has no direct relationship to Pepco's provision of utility services in the District and offers no clear and discernible value to the District of Columbia. Rather, it suggests that this Commission may need to engage in reviews of contributions made by Exelon affiliates over which it has no regulatory authority, and that could arguably represent an inappropriate and unwarranted distraction from the Commission's legislative established regulatory responsibilities.[407]

154. Concerning the Joint Applicants' commitment to low-income programs,[408] AOBA contends Pepco's existing low-income assistance programs are fully funded by Pepco ratepayers in the District and not financially supported by PHI or PHI shareholders, and nothing in the Joint Applicants' offered commitment with respect to low-income programs in this proceeding would change the funding of Pepco's low-income programs.[409] AOBA concludes that the Joint Applicants' Low-Income Assistance commitment represents nothing more than the recognition of an element of Pepco's continuing service obligation as a franchised utility in the District of Columbia.[410]

155. Responding to the Joint Applicants' commitment to support and promote energy efficiency and demand response programs,[411] AOBA states that, in the District of Columbia, energy efficiency programs are the responsibility of the SEU, which is funded through ratepayer assessments. AOBA claims that what Pepco or Exelon would do to "*support and promote*" energy efficiency is at best unclear.[412] As for demand response, AOBA avers that Pepco presently has only one demand response program, the residential "Kilowatchers" program. According to AOBA, the Joint Applicants propose no modifications or expansion of that program or the promotion of that program, nor do they propose any new demand response programs.[413] Moreover, AOBA points out that in response to questioning by Chairperson Kane, witness Crane testified that the Joint Applicants are not committing to anything in the area of demand response that Pepco is not already required to do.[414] Concerning the Joint Applicants' commitments to the provision of Standard Offer Service ("SOS"),[415] AOBA claims that the commitments are designed simply to maintain the continuity and integrity of the existing SOS procurement process. It states that these commitments are necessary to ensure that the Proposed

406 AOBA's Br. at 87.

407 AOBA's Br. at 88.

408 Joint Applicants (4A)-2 at 4, Commitment 21.

409 AOBA's Br. at 88.

410 AOBA's Br. at 88.

411 Joint Applicants (4A)-2 at 4, Commitment 23.

412 AOBA's Br. at 89.

413 AOBA's Br. at 90.

414 AOBA's Br. at 90-91, quoting Tr. at 522:21-523:18.

415 Joint Applicants (4A)-2 at 3, Commitment 9.

Merger does not adversely impact District ratepayers who rely on the Pepco-provided SOS service. Thus, AOBA contends, the Joint Applicants' SOS commitments are simply necessary "*hold harmless*" provisions that do nothing to enhance the value of services presently provided by Pepco for District of Columbia ratepayers.[416]

156. AOBA contends that Exelon's commitment to honor Pepco's existing collective bargaining agreement simply reflects a business reality that has the effect of maintaining the status quo. It does not represent a benefit to Pepco ratepayers, Pepco's union, or the District of Columbia. AOBA notes that, subsequent to the filing of their Application in this proceeding, the Joint Applicants have agreed to extend the existing contract and have indicated a desire to hire additional union workers.[417]

157. **District Government.** The District Government asserts that the claims of positive economic impacts on the District that the Joint Applicants asserted primarily through the testimony of Dr. Tierney are specious, incomplete and unreliable.[418] District Government witness Comings testified that Dr. Tierney's economic impact analysis suffers from three, equally fatal flaws:

> 1. The economic impacts presented in the application ignore job losses from merger synergies—presenting only a positive, lop-sided view of the merger.
> 2. The presentation of economic impacts is misleading because it counts cumulative jobs in every year as "new jobs."
> 3. The economic impacts from reliability improvements are overstated and based on a [faulty] premise that the District of Columbia's reliability standards would not be met by Pepco without the merger.[419]

158. The District Government briefly summarizes other adverse impacts on ratepayers and the District's economy as a result of the Proposed Merger as follows: (1) higher and more frequent rate case filings in the District;[420] and (2) the potential adverse impact of the Merger on District tax revenues, and the adverse impact of the Proposed Merger on local presence and responsiveness of the District of Columbia's electric utility.[421] In summary, the District Government states that the Joint Applicants have failed to show that the net effect of their

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416 AOBA's Br. at 91.

417 AOBA's Br. at 91-92.

418 District Government's Br. at 26.

419 District Government's Br. at 26, citing District Government (C) at 4:14-24 (Comings).

420 District Government's Br. at 28, citing District Government (A) at 57:7-61:2 (Smith).

421 District Government's Br. at 28-29, citing District Government (A) at 57:7-61:2, 92:-98:17 (Smith).

Proposed Merger on District ratepayers and the District's economy is positive. The District Government maintains that:

> the single most financially significant transfer of benefits of the merger – the exchange of a $1.6 billion premium over the market price of PHI stock for the acquisition of a return-based revenue stream in a transaction in which the former shareholders' dividend funds $3.5 billion in acquisition-related debt – receives no attention at all from the Joint Applicants. Perhaps this should not be surprising, as the benefits to the shareholder are so clearly achieved at the expense of the ratepayers.[422]

Summary of Community Comments Pertaining to Factor No. 1: the Economy of the District

159. A wide range of organizations - youth groups, art organizations, social service organizations, trade associations, etc. – highlighted Pepco's philanthropic support throughout the District. While many community organizations expressed support for the Proposed Merger noting in particular the commitment to fund philanthropic work at an average annual level of $1.6 million over the next ten years, some residents expressed disappointment in the show of support from numerous community organizations and noting that the organizations were all past recipients of contributions from Pepco and PHI.

Discussion Pertaining to Factor No. 1: the Economy of the District

160. The effects of the Proposed Merger on the economy of the District are mixed. The Joint Applicants represent that the CIF and "enhanced reliability," discussed under Public Interest Factor No. 3, will lead to an additional $168.4 million to $260.5 million in economic value and 1,506 to 2,407 new *job-years*.[423] Although the parties dispute the magnitude of the economic value of the impact that the Proposed Merger will have on the economy of the District and seek to clarify how many new jobs will be created in the District and for District residents, some positive benefits for the District of Columbia economy will occur in the short term immediately after the Proposed Merger closes.

161. OPC argued that the employment impacts frequently quoted by the Joint Applicants were misleading. The record reveals that Joint Applicants witness Dr. Tierney's job estimates relate to job-years, not to total number of actual jobs. For clarity, one full time job-year is equivalent to one full-time job lasting one year or two half-time jobs lasting one year of 50 jobs lasting 30 years each.[424] The Joint Applicants did not put on the record the actual number of new full time jobs that would comprise the 1,500 to 2,407 new job years that are

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422 District Government's Br. at 29.

423 *See* Joint Applicants (3G) at 16:10-17:4 n. 22 (Tierney).

424 Tr. at 2464:2–2465:8 (Tierney).

referenced by its witness Dr. Tierney when she is addressing the impact of the merger on the economy.

162. The record reflects that the Joint Applicants have agreed "to hire within two years of the Merger closing date at least 102 union workers in the District of Columbia" and to transfer 50 Pepco Energy Services Employees from Arlington, VA to the District of Columbia.[425] Regarding the 102 union employees, the record indicates the 102 employees may not all be new employees; some may be union workers who are filling vacancies caused by retirements or replacing contractors.[426] The Joint Applicants clarified that there are no requirements that a person working for Pepco must live in D.C;[427] and there is no specific commitment to hire a specific number of District residents for these union positions. Mr. Crane testified that Pepco does not have the resources to hire these new employees and suggested that but for the Proposed Merger, these hires would not be made.[428] The Commission is skeptical of this claim. To the extent these employees are replacements, the costs associated with them are already imbedded in existing Pepco rates; to the extent these employees are new hires, there is no commitment for the Joint Applicants to absorb the cost. Mr. Rigby agreed that some training costs are needed for these new hires; however, no cost was provided.[429] It is more likely that Pepco will seek to recover the costs in a future Pepco rate case.[430] Since the cost of incremental new hires will be recovered in rates, this commitment to hire 102 new union workers at ratepayers' expense must be viewed as a cost associated with the Proposed Merger. Mr. McGowan stated these jobs would be "cable splicers, field workers, overhead line workers, testers, substation workers, those types of jobs."[431] If we use a conservative estimate of $87,750 (including all overhead costs)[432] per worker per year, 102 jobs amount to a total of $8,950,000 or roughly $9 million a year. Given that Mr. Crane indicated that some of these workers might replace contractor work or retirements, we will conservatively estimate $4.5 million, or 50% of 102 union workers.[433] The only way this benefit of new jobs to the District economy would not be at a cost to ratepayers would be if the Commission decided to allocate the CIF to cover some of the increased labor costs. Even at the 50% level, the proposed $33.75 million CIF would only take care of roughly 7

[425] *See* Joint Applicants' (4A)-2 at 4, Commitments 17-18.

[426] Tr. at 115:4-7 (Crane).

[427] Tr. at 631:5-11 (Rigby).

[428] *See* Tr. at 115:16-20 (Crane).

[429] Tr. at 750:14-753:8 (Rigby).

[430] *See* Tr. at 2874:11-16 (McGowan), Tr. at 113:17-21 (Crane).

[431] *See* Tr. at 2866:14-18 (McGowan).

[432] Bureau of Labor Statistics, Occupational Employment Statistics, average salary for an Electrical Power-Line Installer and Repairer is approximately $65,000. http://www.bls.gov/oes/current/oes499051.htm. If we calculate the "fully loaded" cost of that employee we increase that number by 35% as outlined in Mr. Khouzami's testimony on the stand. *See* Tr. at 1844:18-20 (Khouzami).

[433] *See* Tr. at 114:16-115:7 (Crane).

to 8 years of the costs for new hires plus training cost to maintain the status quo (no net loss) with respect to jobs.

163. The Joint Applicants also commit to transfer 50 Pepco Energy Services employees from Arlington, Virginia to the District.[434] The Commission recognizes that the transfer of any additional employees to the District provides some benefits to the District economy, especially when District residents are hired.[435] The record shows that currently, only two out of the 50 PES employees live in D.C.[436] It is not clear whether these PES positions will prove to be long-term jobs in the District. Moreover, the Joint Applicants are not committing to maintain at least 50 PES employees in the District.[437] Evidence was submitted to indicate that some of the 50 PES employees are among the 257 positions in PHI that are scheduled to be terminated as a result of the merger.[438] While the Commission is pleased that the Joint Applicants have confirmed that zero Pepco jobs will be eliminated if the Proposed Merger is finalized;[439] the evidence confirms that a number of positions at the PHISCo that is headquartered in the District are being eliminated as part of the synergy savings produced by the Proposed Merger. The Commission notes that the merger synergies will be shared equally with all of Exelon's regulated and non-regulated entities, even though the impact of the resulting job losses at PHI headquarters may have more focused impacts on the District, given that PHI headquarters is here.

164. The other employment-related impact of the Proposed Merger relates to the timing of the job reductions that are expected following the consummation of the Merger. In "the two years following consummation of the Merger, Exelon commits to ensure no net reduction in the employment levels at Pepco due to involuntary attrition resulting from the Merger integration process."[440] We note, first, that this commitment is for Pepco only;[441] there is no similar commitment that relates to PHI's 586 employees who work in PHI's District of Columbia headquarters.[442] We also note that there is no explicit commitment to retain current employees beyond the initial two-year post-merger no net reduction period, which is different than the New Jersey settlement no net reduction period of three to five years.[443] At the hearing,

434 *See* Joint Applicants' (4A)-2 at 4, Commitments 17-18.

435 Tr. at 1839:7-13 (Khouzami).

436 Tr. at 1846.

437 Tr. at 1846:11-17.

438 Tr. at 1847.

439 Tr. at 1842.

440 Joint Applicants (4A)-2 at 3, Commitment 15.

441 Tr. at 1842:16-18.

442 District Government Cross Examination Exhibit No. 121.

443 Joint Applicants (4A)-1 at 13 of 42; Tr. at 75:2-77:7.

Mr. Khouzami testified that there are "200 currently filled positions. And that's across all of PHI" that would be eliminated;[444] he was unable to respond to how many of those reductions would come from PHI's District of Columbia headquarters.

165. After considering the entire record of evidence regarding the employment picture in the District for Pepco and PHI following the close of the Proposed Merger, the Commission concludes that the overall effect of the Proposed Merger on the economy of the District appears to be neutral or slightly positive for the immediate term with the addition of the new union jobs and the transfer of the PES employees to the District, but the economic picture is almost certain to trend negative within two or three years as the protections for job retention are lifted at PHI and Pepco. The District would also stand to lose the additional tax revenues that are associated with higher levels of employment and from a larger PHI organization operating in the District.

166. In addition to the employment-related benefits for the District economy, the Proposed Merger would have tax-related impacts for the District that were not addressed by the Joint Applicants, but were raised by other parties and the Commission. At the hearing, Chairman Kane asked Joint Applicants witness Khouzami and District Government witness Smith whether ratepayers would still be able to receive their proper share of any tax refund, relating to the divestiture of Pepco's generating assets and the refiling of its DC corporate income taxes, in 2018. Joint Applicants witness Khouzami believed that such a refund would still be shared with ratepayers, while District Government witness Smith thought that a condition should be included to ensure that any refund was preserved.[445]

167. The Joint Applicants have made two additional commitments that could have a beneficial impact on the District and its economy even though they are not necessarily benefits for District ratepayers. The first is the commitment to retain the PHI corporate headquarters in the District for an unspecified period of time; and the second is the Joint Applicants' commitment of an average annual $1.6 million charitable contribution from Pepco to local charitable organizations for the next 10 years. Having the PHI headquarters remain in the District at its present downtown location is clearly a benefit to the District and its economy although we note that there was no specified term associated with that commitment. With respect to the second commitment, we note that many non-profits have urged the Commission to approve the merger so the charitable donations being tendered will become available. These voluntary donations for charitable contributions do not come from ratepayers and the regulated side of Pepco. Rather, they are funded exclusively by the Joint Applicants from their profits. Pepco has been a generous corporation with respect to the charitable donations that it has made in the past; we are pleased to hear that it would continue to support local non-profits if the merger is approved, as charitable contributions are purely a discretionary activity of any utility and are made with shareholder funds, there is a clear benefit derived from the certainty of this commitment. To the extent that there is a commitment from the Joint Applicants to donate a specific amount of funding on an annual average basis to charitable organizations located in the

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444 Tr. at 1842:1-12 (Khouzami).

445 *See* Tr. at 2136:12-2137:17 (Commission Cross of Khouzami) (Mr. Khouzami also deferred to Joint Applicants witness McGowan), Tr. at 3068:12-3069:21 (Commission Cross of Smith).

District or that support charitable activities that benefit District residents, this commitment is one that will benefit the District's economy. We note, however, that the dollar amount of the commitment which is made by Exelon and its subsidiaries is lower than the amount of Pepco-DC's 2014 charitable contributions of around $1.9 million[446] -- a figure that does not take into account any donations made separately by PHI.

2. FACTOR 2: The effects of the transaction on utility management and administrative operations

Summary of Joint Applicants' Position Pertaining to Factor No. 2

168. The Joint Applicants state that "[they] have proposed several commitments to ensure that the Merger will not affect access to and accountability of the management of PHI and Pepco, but will instead improve utility management . . ."[447] The Joint Applicants have committed that PHI and Pepco will continue, as before the merger, to maintain their headquarters in Washington, D.C. at Edison Place.[448] They further commit "that Pepco will maintain appropriate levels of senior management" and that PHI will have a President/CEO, Chief Financial Officer, and Treasurer and a number of other officers.[449] The Joint Applicants state "[t]hese commitments ensure that the Commission and stakeholders will continue to have access to those senior-level individuals making decisions that impact customers within the District of Columbia."[450] Mr. Crane testified "the Merger will not create multiple tiers of management that have to be penetrated to access the decision-makers in the organization."[451] The Joint Applicants state, "Following the Merger, Pepco, PHI and Exelon Utilities will remain 'accessible and accountable to regulators in the District of Columbia as well as all other applicable jurisdictions.'"[452]

169. The Joint Applicants assert that decision making for PHI and Pepco will continue at the local level. They emphasize that "Pepco's Regional President will 'continue to provide a strong local connection and maintain relationships with the District of Columbia.'"[453] The Joint Applicants point out that:

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446 Tr. at 3261 (McGowan).

447 Joint Applicants' Br. at 62.

448 Joint Applicants' Br. at 62, citing Joint Applicants (4A)-2 at 3, Commitment 10.

449 Joint Applicants' Br. at 62, citing Joint Applicants (4A)-2 at 3, Commitments 11, 12.

450 Joint Applicants' Br. at 62, citing Joint Applicants (4A)-2 at 3, Commitment 13.

451 Joint Applicants' Br. at 62, quoting Joint Applicants (A) at 21: 18-21 (Crane).

452 Joint Applicants' Br. at 62-63, quoting Joint Applicants (A) at 21: 9-12 (Crane). (The quotation in Joint Applicants' Br. at 62-63 does not accurately reflect underlying quotation. Mr. Crane's actual quote is, "both Mr. O'Brien, who leads Exelon Utilities, and [Mr. Crane, the CEO of Exelon] are committing to being accessible and accountable to regulators, state and local governments, and all of the utilities' other constituencies.")

453 Joint Applicants' Br. at 63, quoting Citing Joint Applicants (4A)-2 at 3, Commitment 13.

> First, they commit that PHI's senior management "will continue to establish priorities and respond to local conditions as it does today." Second, they commit that "PHI's local management will continue to have the authority and responsibility to provide input into the development of Pepco's capital and operating and maintenance expense budgets and implement the approved budgets." Finally, they clarify that "[w]hile Pepco's budgets will be reviewed by Exelon's CEO and Executive Committee, they will have to be approved by the PHI board of directors."[454]

170. The Joint Applicants state, "Exelon's current management structure provides that the senior management of each of its subsidiary utilities has the authority to develop its business plan and O&M budget."[455] Referencing the testimony of Mr. O'Brien, the Joint Applicants state, "[w]hile such plans and budgets are reviewed at the Exelon Utilities and Exelon levels by Mr. O'Brien, Mr. Crane, and the Executive Committee of Exelon, it is the individual utility boards that have ultimate approval authority of both."[456] Further, after quoting BGE's CEO Mr. Butler's explanation of how BGE develops its budget, the Joint Applicants state, "[f]ollowing the Merger, the PHI board of directors will have the same authority to approve its utility subsidiary budgets and business plans that they have today, and the same authority that Exelon's utility subsidiaries currently have."[457] The Joint Applicants go on to state, "[a]s with Exelon's utilities, while the CEO of Exelon Utilities, Mr. O'Brien, will review the proposed PHI utility budgets, and while the aggregated budgets will be approved by the Exelon board as part of Exelon's overarching budget, PHI's board of directors will have final approval over its utility budgets and business plans."[458] Finally, the Joint Applicants state, "PHI and Pepco will retain local control of decisions such as when and how to file a rate proceeding, including the testimony to be presented in such a proceeding, and the management of activity following a major event."[459]

171. The Joint Applicants commit that, "following the Merger, the authority and responsibility delegated to PHI's local management 'will be clearly delineated in two formal, written documents consisting of a statement of Corporate Governance Principles and a Delegation of Authority . . . [that] will demarcate, among other things, levels of expenditures and defined categories of decisions that can be authorized solely by the utility's CEO or by the utility CEO with utility board of directors' approval.'"[460] The Joint Applicants identify a proposed

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454 Joint Applicants' Br. at 63, quoting Citing Joint Applicants (4A)-2 at 4, Commitment 24.

455 Joint Applicants' Br. at 63.

456 Joint Applicants' Br. at 63-64, citing Joint Applicants (C) at 8:1-4 (O'Brien).

457 Joint Applicants' Br. at 64, referencing Tr. at 1202:12-15 and 1202:20-1203:05. (Commission Cross of Butler).

458 Joint Applicants' Br. at 64.

459 Joint Applicants' Br. at 64, citing Tr. at 1074:9-1075:2 and 1080:22-1082:7. (Commission Cross of O'Brien).

460 Joint Applicants' Br. at 65, citing Joint Applicants (4A)-2 at 5, Commitment 27.

DOA, included with their commitments and as a separate exhibit, and indicate that "[d]ecisions such as the issuance or redemption of debt, the construction of a substation, energy procurement contracts, and the sale or divestiture of assets including real estate would be governed by the final DOA following the close of the Merger."[461]

172. In support of their assertion concerning local decision-making, the Joint Applicants, through Mr. O'Brien, point out that they have committed to a "proposed management structure to ensure local control for PHI and Pepco."[462] Under the proposed structure:

> PHI will have a seven-member board of directors. At least three members must be independent, as defined by New York Stock Exchange rules, and of the four remaining directors, at least one will be selected from the officers or employees of PHI or a PHI subsidiary. The PHI board will also include three outside directors from the service territories of PHI's three utility subsidiaries. The PHI board will select Pepco's board of directors, and the Pepco board will choose Pepco's officers. PHI's officers will include a President/CEO (Mr. David Velazquez will serve in this role following the Merger), Chief Financial Officer and Treasurer. Each of PHI's utilities will retain its Regional President, who will continue the role he or she currently plays in the management of each utility.[463]

The Joint Applicants state, "[t]he CEOs of BGE, ComEd and PECO are currently members of Exelon's Management Executive Committee. Following the close of the Merger, the CEO of PHI will also become a member of that Committee," which meets at least monthly with Exelon's CEO Mr. Crane, and will "'have direct and frequent access to him and other members of Exelon's senior management team.'"[464] The Joint Applicants assert these provisions "will ensure that PHI and Pepco retain local management and control of their operations, which Exelon believes is critical to the successful management of its utility subsidiaries."[465] The Joint Applicants state, "Exelon does not exercise 'hierarchical control' over its subsidiary utilities, but rather provides them with additional resources, including the development of best practices as

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461 Joint Applicants' Br. at 65, citing Joint Applicants (4A)-2 at 13, Table Two. Table Two was also included as Joint Applicants (3C)-5.

462 Joint Applicants' Br. at 65.

463 Joint Applicants' Br. at 65-66, citing Joint Applicants (4A)-2 at 6, Commitment 38; Joint Applicants (3C) at 14:8-18 (O'Brien).

464 Joint Applicants' Br. at 66, citing Joint Applicants (3C) at 15:3-10 (O'Brien). *See also*, Joint Applicants (4A)-2 at 5, Commitment 25.

465 Joint Applicants' Br. at 66, citing Joint Applicants (3C) at 9:6-7 (O'Brien).

discussed below, to improve their ability to provide safe, reliable and efficient service to their customers."[466]

173. The Joint Applicants state, "[t]he Exelon Utilities organization, the implementation of the Exelon [Utilities] Management Model and the sharing of best practices will drive overall improved and cost-effective utility operational performance at Pepco following the Merger."[467] In support of this, they state, "[t]he sharing of best practices and implementation of the Management Model following the Exelon-Constellation merger in 2012 have helped BGE achieve uncontroverted high performance in safety and reliability."[468] The Joint Applicants explain:

> in connection with the 2012 Exelon-Constellation merger, Exelon Utilities was developed by Exelon to facilitate the distribution of knowledge, expertise and sharing of best practices across all of Exelon's utilities. Exelon Utilities is an operational organization, not a legal entity. It is led by Mr. Denis O'Brien, and is staffed by approximately 40-50 individuals who facilitate operational excellence at Exelon's utilities. Under the current organizational reporting structure, each of Exelon's utility company CEOs report directly to Mr. O'Brien.[469]

The Joint Applicants state, "[p]ost-Merger, PHI's CEO, David Velazquez, will also report directly to Mr. O'Brien" and "[t]he reporting relationship of Pepco's Regional President, Donna Cooper, will not change after the Merger."[470]

174. The Joint Applicants assert, "[t]he implementation of the Management Model and the sharing of best practices at Pepco is critical to realizing the benefits expected from the Merger, including the reliability commitments."[471] The Joint Applicants state, "[the Management Model] is the management system in place to define and drive high operating and financial performance across Exelon's utilities."[472] They go on to state:

> The Management Model encompasses multiple system-wide core functions (such as Operate and Restore, Customer Care, Cost

466 Joint Applicants' Br. at 66-67, citing Joint Applicants (3C) at 16:1-2 (O'Brien).

467 Joint Applicants' Br. at 67.

468 Joint Applicants' Br. at 67.

469 Joint Applicants' Br. at 67-68, citing Joint Applicants (3C) at 9:19-21, 9:2-3 (O'Brien); Tr. at 994:10-11, 987:18-19, 988:6-7 (O'Brien Cross); Joint Applicants Cross Examination Exhibit No. 49 at 2 of 2.

470 Joint Applicants' Br. at 68, citing Commission Cross Examination Exhibit No. 1, Tr. at 989:19-21 (O'Brien Cross); Joint Applicants (B) at 6:18-7:5 (Rigby).

471 Joint Applicants' Br. at 68, citing Joint Applicants (C) at 4:2-4 (O'Brien); Tr. at 997:1-5 (O'Brien Cross).

472 Joint Applicants' Br. at 68, citing Tr. at 974:7-12 (O'Brien Cross).

> Management, Safety, and System Performance), each of which are directed by senior leaders and staffed by managers leading the particular functional area at each utility, with over 3,800 policies, programs, processes and procedures that document the output of the Management Model.[473]

The Joint Applicants, in response to parties questioning the value of sharing best practices, state "it has been Exelon's experience that individual utilities cannot identify and implement best practices as effectively or efficiently on their own or through the use of an outside consultant."[474] Joint Applicants witness Alden, Exelon's Vice President, Utility Oversight and Integration, explains:

> You can hire a consultant to do anything. I think we have the wherewithal within the company, the horsepower within the Exelon Utilities, to do just about anything that a consultant could do for us in this area, and the implementation management controls in place to ensure that it gets applied and implemented at the utility.[475]

With regard to potential best practices at Pepco, the Joint Applicants state "[w]hile Exelon has preliminarily identified some potential best practices it expects to implement at Pepco post-Merger, there are many other areas where best practices may be identified once the companies are combined and the type of detailed analysis discussed above is completed, that Exelon expects will result in improved reliability and enhanced customer service and satisfaction for Pepco and its customers."[476]

175. The Joint Applicants state further, "BGE's experience following the Exelon/Constellation merger provides the Commission with a real-world example of the benefits attainable through joining the Exelon family of utilities."[477] They assert that "[t]he implementation of the Management Model and the sharing of best practices played a part" in BGE's "significant improvements" in its reliability metrics from 2012 through 2014.[478] The

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473 Joint Applicants' Br. at 69, citing Joint Applicants Confidential Cross Examination Exhibit No. 48 at 2 of 166. (Submitted in response to Commission Cross Examination of Mr. O'Brien.)

474 Joint Applicants' Br. at 69, citing Tr. at 1357:20-1358:20 (Commission Cross of Alden); Tr. at 1005:13-1006:8 (O'Brien Cross).

475 Joint Applicants' Br. at 70, citing Tr. at 1358:4-11 (Commission Cross of Alden).

476 Joint Applicants' Br. at 70-71, citing Tr. at 1293:13-16 (Alden Cross); Joint Applicants (C) at 6:10-13 (O'Brien).

477 Joint Applicants' Br. at 71.

478 Joint Applicants' Br. at 71, citing Joint Applicants (H) at 5:20-23 (Butler); Joint Applicants (D) at 5:12-18 (Alden); Tr. at 1198:22-1199:7, 1238:14-17, 1360:17-19; Joint Applicants Cross Examination Exhibit No. 50 at 3 of 4.

Joint Applicants point out that "Between 2012 and 2013, the average time to restore service to BGE customers who sustained an interruption was reduced by 29.4 percent; which, as Mr. Alden explained, was due to a combination of 'work that had been done prior to the [Exelon-Constellation] merger as well as an acceleration that took place in that improvement as a result of the merger itself.'"[479]

176. The Joint Applicants also highlight that "these reliability improvements were accomplished without any increases in BGE's capital or O&M budgets."[480] The Joint Applicants state "BGE is now fully aligned with ComEd and PECO in its response to major storms, which facilitates the deployment of Exelon utility crews quickly and safely between the utility service territories."[481] Further, the Joint Applicants point to improvements in BGE's rankings in 2013 on the Customer Satisfaction Index, J.D. Power rankings of best utilities.[482] Finally, the Joint Applicants point out that "in addition to improved performance at BGE, BGE's shared service company costs actually were $10 million less in the first full year after the merger than they were in the last full year before the merger."[483]

Summary of OPC's and Intervenors' Position Pertaining to Factor No. 2

177. OPC states it has "serious concerns with the ambiguity and lack of specificity" with regard to "several commitments [the Joint Applicants] claim will enable Pepco to maintain a local presence in the District."[484] OPC raises what it terms "evasive and non-responsive answers Exelon witnesses gave at the evidentiary hearing regarding the degree to which Exelon senior management would be involved in reviewing and potentially modifying or rejecting Pepco's operational plans and budgets after the transaction closes."[485] OPC asserts "the Joint Applicants' commitments in this important area fall far short of what is needed to provide meaningful assurance that local control would in fact be maintained should Exelon's acquisition of Pepco be approved."[486]

178. Regarding the Joint Applicants' commitment to maintain PHI's and Pepco's headquarters in the District, OPC asserts "assuming that such language constitutes an enforceable commitment, it certainly provides no affirmative benefit to the District, as there is no evidence in the record that either PHI or Pepco, before the proposed transaction was announced,

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479 Joint Applicants' Br. at 72 n. 309, citing Tr. at 1237:4-11 (Alden Cross).

480 Joint Applicants' Br. at 71, citing Joint Applicants (D) at 6:2-8 (Alden).

481 Joint Applicants' Br. at 71, citing Joint Applicants (D) at 6:11-15, 7:16-20 (Alden).

482 Joint Applicants' Br. at 72, citing Joint Applicants (D) at 6 (Alden); Joint Applicants (3C) at 3:11-13 (O'Brien).

483 Joint Applicants' Br. at 72, citing Tr. at 2097:1-8 (Commissioner Cross of Khouzami).

484 OPC's Br. at 58, citing Joint Applicants (4A)-2 at 3, Commitments 10-14.

485 OPC's Br. at 58.

486 OPC's Br. at 58-59.

had planned or intended to move their headquarters outside the District, in either the short-term or long-term."[487] Regarding the Joint Applicants' commitment for PHI to have a President/CEO, Chief Financial Officer [CFO], Treasurer and a number of other officers and for Pepco to maintain appropriate levels of senior management at its District of Columbia headquarters, OPC asserts:

> neither of these two commitments provides any affirmative benefit whatsoever to the District. There is no evidence in the record that either PHI or Pepco, before the proposed transaction was announced, had planned or intended to no longer have a President, CEO, CFO, Treasurer or any other senior managers, or that Pepco would cease to maintain appropriate levels of senior management in the District. At best, this commitment evidences an intent to maintain the *status quo* to the maximum extent possible.[488]

OPC goes on to quote Mr. O'Brien's testimony that "PHI will have a President/CEO, [CFO] . . . Treasurer and a number of other officers, *although likely fewer than there are now*."[489] OPC observes that this statement "identifies the obvious point that things will be different if the transaction is approved" and that the commitments made are "far too vague to be meaningful."[490]

179. Next, OPC takes issue with how the Joint Applicants propose to restructure the boards of directors for PHI and Pepco. OPC asserts the Joint Applicants' commitment for a PHI board consisting of seven or more people with at least three members of the PHI board being "independent" (as defined by the New York Stock Exchange rules), "would represent significant back-sliding" in terms of maintaining independence and local control.[491] OPC points out that at least seven of the current 13 members of the PHI board are independent, and the PHI board proposed by the Joint Applicants will be "decidedly less independent" because it shifts from a majority of independent members pre-merger to a minority of independent members post-merger.[492] OPC states:

> such changes in PHI's board would be a step backwards for the District, since the less independent PHI's board is, the more likely that the board will simply act as a rubber stamp that routinely approves the decisions of Exelon's and PHI's senior management without vigorous analysis and debate.

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487 OPC's Br. at 59, citing Tr. at 594: 12-17. (Mr. Rigby confirmed there are no plans to move PHI's or Pepco's headquarters).

488 OPC's Br. at 60.

489 OPC's Br. at 60-61, citing Joint Applicants (3C) at 14:12-14 (O'Brien) (emphasis added in OPC's Brief).

490 OPC's Br. at 61.

491 OPC's Br. at 62, citing Joint Applicants (4A)-2 at 6, Commitments 38.

492 OPC's Br. at 62, citing OPC Cross Examination Exhibit No. 11 at 3.

180. Further, OPC states "[s]uch diminished independence of the PHI board would be compounded by the fact that PHI itself, post-transaction, would cease to be a publicly-traded company, instead becoming a private entity with but *one* shareholder—Exelon."[493] OPC expresses concern "that the Exelon board would appoint all members of the PHI board."[494] OPC cites statements of Mr. O'Brien indicating that "Exelon CEO Crane would likely become chairman of both PHI's board and Pepco's board, while Exelon Senior Executive Vice President O'Brien would likely become vice-chairman of both PHI's and Pepco's boards."[495] OPC asserts that contrary to the Joint Applicants claims about maintaining local control, "the transaction would result in both PHI and Pepco having boards whose members are appointed, controlled and directed by Exelon, all of which would undeniably constitute major changes in the *status quo*."[496] OPC made "recommendations that would strengthen the independence of the PHI and Pepco boards and ensure that those boards had stronger ties to the District," which the Joint Applicants rejected, including:

> recommendations that: (1) at least one-third and no fewer than two Pepco board members be independent, (2) the majority of Pepco's Board members reside in DC, (3) the majority of PHI's Board be independent, and (4) the PHI and Pepco CEOs reside in Pepco's service territory.[497]

OPC points out that "[t]he Joint Applicants rejected all of those OPC recommendations as "simply not tenable," because, as Mr. O'Brien stated, "Exelon, as a practical matter, must have the ability to exercise control over its subsidiaries," including Pepco.[498] OPC concludes that "[a]ny 'commitment' to local control is illusory as Exelon will be in control . . . [and] OPC fails to see any compelling basis to cede authority over the District's distribution utility to decision makers in Chicago."[499]

181. Regarding the Joint Applicants' commitment that "'[w]hile Pepco's budgets will be *reviewed* by Exelon's CEO and Executive Committee, they will have to be *approved* by the PHI board of directors,'" OPC states "[t]his so-called commitment is misleading, and ultimately meaningless for the District and Pepco's ratepayers."[500] First, OPC asserts that due to the proposed structure of PHI's board, "for all intents and purposes, there would appear to be little

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493 OPC's Br. at 62, citing OPC Cross Examination Exhibit No. 11 at 2.

494 OPC's Br. at 63, citing OPC Cross Examination Exhibit No. 11 at 2.

495 OPC's Br. at 63, citing OPC Cross Examination Exhibit No. 13 at 7, Tr. at 904:18-905:8.

496 OPC's Br. at 63.

497 OPC's Br. at 64, citing OPC (A) at 136-137 (Dismukes).

498 OPC's Br. at 64, citing Joint Applicants (3C) at 11:9-19 (O'Brien).

499 OPC's Br. at 64.

500 OPC's Br. at 64, quoting Joint Applicants (4A)-2 at 4, Commitments 24 (emphasis added in OPC Brief).

practical difference between Pepco's budgets being reviewed and approved by the PHI board versus being reviewed and approved by Exelon. In other words, it would be a PHI board in name only."[501] Second, OPC argues that, "while the Joint Applicants have gone out of their way to emphasize that Pepco's budgets will simply be 'reviewed' by Exelon's CEO and Executive Committee, the record indicates such review power necessarily includes the ability to approve, disapprove and/or require changes to Pepco's budgets."[502] OPC concludes that the budget review process proposed by the Joint Applicants "would increase the possibility that Exelon could require changes to Pepco's proposed business plans or budgets for the primary purpose of conforming such documents to accomplishing an Exelon objective—an objective which of course may not be in the best interest of the District."[503]

182. Finally, OPC raises concerns that Exelon will assume strategic planning on behalf of Pepco. OPC highlights that prior to the Proposed Merger, PHI had been in the process of developing a "Utility 2.0" plan, but as Mr. Rigby said PHI "hit the pause button" on Utility 2.0 after the Merger was proposed.[504] OPC points to Mr. Rigby's conclusion "that the matter would heretofore likely 'fall under [Exelon's] strategic planning process.'"[505] OPC concludes, "Exelon, with its enormous investment in generation assets, is likely to address the prospect of competing generation sources, in contrast to a wires-only utility like PHI."[506]

183. **AOBA.** AOBA raises concerns that although Exelon currently operates utilities in three jurisdictions, "it has never previously dealt with [ ] utilities, such as Pepco and Delmarva, that operate in multiple jurisdictions."[507] AOBA asserts "that Exelon's lack of sensitivity to inter-jurisdictional issues is particularly adverse to the interest of the District of Columbia in this proceeding."[508] AOBA goes on to highlight numerous issues, including "[t]he Joint Applicants failure to offer to this Commission and Pepco's District of Columbia ratepayers terms of settlement[ ] relevant to this jurisdiction that were accepted by Exelon and/or the Joint Applicants in other jurisdictions;" "Exelon's failure to ensure substantial representation of the District in its proposed structuring of the post-Merger Boards of Directors for PHI and Pepco;" and "Exelon's failure to include the substantial numbers of District residents that live in master-metered apartments in its allocation of CIF dollars among jurisdictions, despite the long history in the District of recognizing residential dwelling units in master-metered apartment building as

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501 OPC's Br. at 65.

502 OPC's Br. at 65, citing Joint Applicants (4A)-2 at 4, Commitment 24.

503 OPC's Br. at 66.

504 OPC's Br. at 67, citing Tr. at 797:2-14, 803:14-18 (Rigby); OPC (2E)-3 at 6.

505 OPC's Br. at 67, citing OPC (2E)-3 at 4-5.

506 OPC's Br. at 67.

507 AOBA's Br. at 15.

508 AOBA's Br. at 16.

distribution customers."[509] AOBA concludes that these failings stem from Exelon's "attempt[] to leverage the settlement it negotiated in . . . New Jersey (without any input from the District of Columbia interests) to force a "one size fits all" approach to resolving a number of Merger-related issues for all the jurisdictions served by the PHI utilities."[510]

184. The District Government states, "[t]he proposed merger would unquestionably change Pepco's relationship within its utility holding company's hierarchy."[511] They point out that "PHI's decisions that are made in the District today concerning issues that affect the District would be made, post-merger, by Exelon in Chicago . . . but clearly with a less District-centered focus than has been the case historically."[512] The District Government asserts, "[t]he record in this proceeding suggests that the approval of the proposed merger would bring a number of other changes with it that may be less consistent with implementation of District public policy than has been the case thus far with PHI."[513] First, the District Government, based on Exelon's confidential 2013 Strategic Plan, states:

> The evidence indicates that, aspirations toward local autonomy notwithstanding, Exelon tends to enforce a hierarchical orthodoxy directed toward ensuring that perceived threats to its existing business – including such developments as net metering, community renewable resources and imports that compete with Exelon's incumbent generating fleet – do not stay threats for long.[514]

Pointing to Exelon's roll in planning BGE's 2014 Maryland legislative agenda and lobbying against a merchant transmission project that would import Canadian hydroelectric power, the District Governments states "[t]hese examples (and others) represent an approach to management that contrasts unfavorably with PHI's comparatively more open-handed interaction with various communities within the District, and with the fact that PHI and its subsidiaries divested their generation assets years ago, eliminating competitive conflict between owned generation resources and other resources that seek to displace them."[515] Second, referencing Exelon's Management Model and Exelon's best practices, the District Government asserts that

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509 AOBA's Br. at 16-18, citing Joint Applicants (4A)-2 at 6, Commitment 38, AOBA (A) at 7:4-11 n. 4 (Oliver).

510 AOBA's Br. at 196.

511 District Government's Br. at 30.

512 District Government's Br. at 30.

513 District Government's Br. at 30.

514 District Government's Br. at 31, referencing District Government Confidential Cross Examination Exhibit No. 14 at 80.

515 District Government's Br. at 31, citing District Government Confidential Cross Examination Exhibit No. 37 at Attachment 2; District Government Cross Examination Exhibit No. 18 at Attachment A; Tr. at 1048:1-1060:14 (O'Brien); Tr. at 3573:21-3575:12 (Schoolman).

"there is no evidence on this record showing that any of these Exelon policies or practices produce measurable benefit to consumers that is attributable to this proposed merger."[516] Finally, the District government concludes "certain capital expenditure plans that are today made in the District of Columbia by PHI would, in a post-merger world, require approval from the Exelon CEO or Board of Directors."[517]

Discussion Pertaining to Factor No. 2

185. **Utility Management.** The Commission agrees with the District Government that, "[t]he proposed merger would unquestionably change Pepco's relationship within its utility holding company's hierarchy."[518] Pepco, which is currently the largest single utility in PHI, is on equal footing with the two other PHI utilities, *i.e.*, Delmarva Power and ACE, in terms of reporting structures within its current utility holding company, PHI.[519] Pepco's Region President is currently part of the PHI senior executive team and participates in decision-making on issues involving rate cases and budgets and legislative policy. Pepco's Region President would lose their seat at the table of the new utility holding company's decision makers if the merger is consummated. The post-Proposed Merger organization places Pepco in a clear second-tier status, relying on PHI to represent Pepco's interests along with those of Delmarva Power and ACE within the Exelon Management Committee.[520] Such a management structure fundamentally disadvantages Pepco, and by extension District ratepayers, in terms of having a voice within the Exelon holding company structure.

186. Exelon CEO Mr. Crane asserted, "the Merger will not create multiple tiers of management that have to be penetrated to access the decision-makers in the organization."[521] He claims that the Pepco Regional President will still have a strong voice in local decisions – a position that Joint Applicants argue was supported by the testimony of BGE CEO Calvin Butler. The Commission notes, however, that the BGE CEO, unlike the Pepco Region President, has a seat on the Exelon Executive Committee that reports to Exelon CEO Crane.[522]

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516 District Government's Br. at 31-32, citing District Government Cross Examination Exhibit No. 34, District Government Cross Examination Exhibit No. 39, Subpart D.

517 District Government's Br. at 32, referencing Joint Applicants (3C)-5, Joint Applicants (4A)-2 at 13, Tr. at 1040:3-1044:8 (O'Brien).

518 District Government's Br. at 30.

519 *See Formal Case No. 1119*, Joint Application at 5 and Exhibit 4. *See also*, Commission Cross-Examination Exhibit No. 1 (indicating all three legacy PHI utilities on same reporting level.)

520 *See* Joint Applicants (3C) at 15:3-10 (O'Brien). *See also*, Joint Applicants (4A)-2 at 5, Commitment 25.

521 Joint Applicants (A) at 21: 18-21 (Crane).

522 The Exelon Executive Committee consists of about 15 people and includes the EU CEO, the CEOs of the Exelon Utilities, the Exelon Head of Strategy, Exelon General Counsel, Senior Vice President of Exelon Generation, Senior Vice President of Constellation, and others. Tr. 1008:8-21.

187. The Commission reviewed and questioned the Joint Applicants on Exelon's Delegation of Authority (referenced in the Joint Application and presented as an exhibit during the hearings). This document dictates the hierarchy of decision-makers whose approval is needed for key management and policy decisions based upon dollar amount thresholds. The day-to-day administration of business affairs is governed by the Delegation of Authority, which demarcates levels of expenditures and defined categories that are authorized by EU CEO O'Brien or EU CEO O'Brien with the EU Board.[523] This adds additional layers of administrative decision-making processes that involve Pepco operations. However, rate case decisions are not listed on the Delegation of Authority because, according to the testimony of Joint Applicant witness O'Brien, the decision to file a rate case is made by the local utility's board, similar to what is currently undertaken at PHI.[524]

188. In response to questioning by Commissioner Fort, Mr. Crane testified that if the D.C. PLUG project were proposed and being developed within a post-merger Pepco, the $1 billion undergrounding project "would get the PHI CEO and PHI utility board [approval], then jump the rest [chain of delegated authority] because of the size of the project, and it goes directly to the Exelon board" for approval.[525] That extra layer of decision making stands in contrast to the current arrangement where the funding and the approval of Pepco's participation in the D.C. PLUG initiative was directly facilitated by the active participation of the President and CEO of PHI, Mr. Rigby, who as described by Chairman Kane, "sat there personally as – co-chairing of the task force, and, you know, it was clear, he was the one who was speaking for the company and could make those decisions."[526]

189. When asked by Chairman Kane if the Joint Applicants' commitment regarding policy, legislative, or other non-budgetary decisions for "PHI senior management will continue to establish priorities and respond to local conditions as it does today," Exelon CEO Crane indicated that the Pepco Region President and PHI CEO would be as involved in the future as today; however he went on to clarify the procedure that would be used stating:

> If there is a policy issue, a national policy issue or something that we think – as an executive committee, we have a lot of dialogue. So all the utilities heads are – sit on the executive committee. And if there's something like net metering – and I think that's probably the only thing that we're very concerned about – as we expand distributed generation, you know, we do come up with company policies. They're never disagreed upon, and we make sure that the local needs are taken care of.[527]

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523 Joint Applicants (3C) at 9:11-16 (O'Brien); Joint Applicants (3C)-5.

524 Tr. at 1078:3-17; Tr. at 1080:8-16 (Commission Cross of O'Brien),

525 Tr. at 494:12-495:3 (Commission Cross of Crane).

526 Tr. at 544:12-15 (Commission Cross of Crane).

527 Tr. at 544:16-546:2.

190. Chairman Kane also questioned Mr. Crane about Exelon's knowledge of how energy efficiency programs in the District operate to better understand the impact of the Joint Applicants' commitment to "maintain and promote existing energy efficiency and demand response programs" under the Proposed Merger. Mr. Crane was unaware of the unique structure of the District's energy efficiency programs, with the Sustainable Energy Utility determining these programs under contract with the District Department of the Environment, not the Commission.[528] Additionally, when questioned about the Community Renewable Facilities Act, and how such facilities were paid for, Mr. Crane stated, "it was almost like a net metering provision."[529] This prompted Chairman Kane to explain that this was incorrect and that it "was established so that there really was no subsidy that the price paid for the output of those facilities is the – it's a tariffed price, the same price at which the SOS provided would be buying electricity."[530] In each of these instances, the Joint Applicants demonstrated a distinct lack of knowledge concerning important District energy policies and funding mechanisms that are distinct from other jurisdictions.

191. Mr. Crane's responses and the record evidence about the management and decision making authority within Exelon and Exelon Utilities ("EU") confirms that under the Proposed Merger, certain budget and policy decision making will operate differently for Pepco. The Commission has concerns about whether the needs of the District will be properly raised and addressed with the hierarchy within EU. Mr. Crane has testified that David Velazquez, someone who has a great deal of knowledge about Pepco and the District, will become the PHI CEO if the Proposed Merger is consummated; however, Mr. Velazquez's appointment and the term of his appointment is not contained in any of the commitments provided by the Joint Applicants. Under the proposed management structure, the PHI CEO is a position that is filled by the PHI Board of Directors. Should the PHI Board of Directors decide to change its CEO and place in that position someone without the same knowledge of Pepco and Pepco's District of Columbia's operations, the position of the District and its ratepayers would be further harmed.

192. This Proposed Merger will result in Exelon exercising control over PHI and Pepco.[531] Much of this control will be exercised by persons outside the District of Columbia. EU CEO O'Brien will have a "direct role in the management of Pepco."[532] The record indicates that the PHI Board currently approves the overall power delivery budget for Pepco.[533] Post-merger, budgets for Exelon utility operating companies are developed in the operating company and approved by the operating company's board.[534] The record indicates that Pepco rate case

528 Tr. at 521:3-527:8 (Commission Cross of Crane).

529 Tr. at 527:3-13 (Commission Cross of Crane).

530 Tr. at 527:14-20 (Commission Cross of Crane).

531 Tr. at 892:13-17.

532 Joint Applicants (C) at 3:13-17 (O'Brien); Tr. 989:13-990:3.

533 Tr. at 833:11-834:4; 839:20-840:6.

534 Tr. at 915:18-917:3.

decisions are currently made at the Pepco executive leadership team level rather than at the PHI Board level.[535] Post-merger, it is unclear whether these activities will take place on the Pepco or the PHI board level initially. The record is clear that EU CEO O'Brien will be involved in reviewing rate cases before filing in the District, thus adding an additional layer of management oversight in the decision to file a rate case.[536] Pepco's business plans will be reviewed by Exelon CEO Crane, EU CEO O'Brien, and the Exelon Executive Committee with the PHI (not Pepco) Board making the final approval decision of such plans..[537] While EU CEO O'Brien would look to PHI CEO Velazquez to make most decisions, Exelon CEO Crane and EU CEO O'Brien may make some decisions.[538] There is no indication that the Pepco Region President will be making any of these key decisions.

193. **Post-Merger Boards.** Another change in the management structure under the Proposed Merger that has raised concerns is the change to the boards of directors of Pepco and PHI. OPC, AOBA, and the District Government all raised concerns with regards to the representation of the District's interest given the proposed composition of the PHI and Pepco boards under the proposed Merger. As OPC correctly points out, the PHI Board of Directors proposed by the Joint Applicants will be "decidedly less independent" because it shifts from a majority of independent members pre-merger to a minority of independent members post-merger.[539] Specifically, PHI will have a board of directors consisting of 7 or more people of which at least 3 members will be independent outside directors from the PHI utility service territories.[540] Thus at least one board member will be from the Pepco service area, *i.e.*, from either Maryland or the District of Columbia.[541] Of the remaining 4 directors, at least one will be selected from among the officers or employees of PHI or a PHI subsidiary and the remainder will initially be appointed by the Exelon Board and will consist of some combination of Exelon officers and directors.[542] Exelon CEO Crane will likely be the PHI Board Chairman.[543] EU CEO O'Brien will likely become PHI Board Vice Chairman.[544] Mr. Velazquez would also be one of the PHI Board members.[545] If the number of PHI Board members is increased, there is no

535 Tr. at 827:16-20; 824:13-826:1; 8351-10.

536 Tr. at 945:2-15.

537 Joint Applicants (3C) at 15:11-15 (O'Brien); Tr. 928:7-20.

538 Tr. at 853:19-854:2.

539 OPC's Br. at 62, citing OPC Cross Examination Exhibit No. 11 at 3.

540 Joint Applications (C) 7:2-7.2 (O'Brien).

541 Tr. at 019:7-16.

542 OPC Cross Examination Exhibit No. 11, p.2.

543 Tr. at 903:3-16; 904:18-22.

544 Tr. at 905:5-8.

545 Tr. at 906:3-6.

commitment by the Joint Applicants that additional board members would be independent.[546] Regarding the alignment of PHI and Pepco with BGE, ComEd and PECO in the Exelon management structure, PHI, with its three utilities—Pepco, Delmarva Power, and ACE—will become the fourth utility operating as an Exelon utility.[547] Pepco and the other PHI subsidiaries will not be on the same level.

194. **Administrative Operations.** With respect to administrative operations, the Proposed Merger would also result in Pepco being subject to both a new management model, and a second service company sharing allocated costs. With respect to the new management model and its best practices, the Joint Applicants assert that the Exelon Management Model is responsible in part for the improvement in the performance shown by BGE after the Exelon Constellation merger. The Joint Applicants assert "[t]he implementation of the Management Model and the sharing of best practices at Pepco is critical to realizing the benefits expected from the Proposed Merger, including the reliability commitments."[548] However, despite the fact that the Exelon Integration team has been working with PHI for almost a year, the Joint Applicants were not able to provide examples on the record of the areas of operations at Pepco that would be changed by these best practices. Additionally, there is a question about how EU will be tailoring its model to address the PHI structure since none of the current regulated utilities under the model operate within a separate holding company. Another difference, as noted by AOBA, is that none of the existing Exelon regulated utilities operate in multiple jurisdictions and have to deal with inter-jurisdictional issues as is the case with Pepco and Delmarva Power. AOBA noted further that inter-jurisdictional issues could be particularly adverse to the interest of the District of Columbia. The Joint Applicants were silent on whether aspects of the Exelon Management Model or the best practices will need to be further tailored to operate under the PHI structure and if so, how that will be done.

195. A similar administrative operational question arises with respect to the fact that there would be two service companies under the Proposed Merger. The Proposed Merger retains the PHISCo while adding Exelon's service company – Exelon Business Services Company ("EBSC") – to the mix.[549] The Commission has had a continuing concern about appropriate cost allocations for Pepco-DC under the PHISCo. As two service companies will be present after the Proposed Merger closes, ensuring that the proper allocation of service company costs will be passed on to Pepco-DC and to District ratepayers will require increased time and scrutiny on the part of the Commission and all of the companies involved.

196. The new structure places Exelon company leaders with a fiduciary interest and obligation to protect Exelon's generation business above PHI and Pepco in the new hierarchy. Such interests may be at odds with the interests of Pepco and District ratepayers in favor of Exelon's substantial generation component. The Joint Applicants have not explained how it

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546 Tr. at 1016:2-1017:9.

547 Tr. at 1008:7-10.

548 Joint Applicants (C) at 4:2-4 (O'Brien); Tr. at 997:1-5 (O'Brien Cross).

549 *See* Commission's discussion of multiple service companies in paragraphs 268-270.

currently operates when it is faced with conflicting business interests, such as when discussing issues around distributed generation and how it would operate if the Proposed Merger is consummated. Moreover, if Pepco has no seat at the table where these decisions are being made, at best, the Pepco Region President would have only a limited opportunity to identify where potential conflicts impacting plans related to Pepco are being made, raise an objection or influence the decision.

197. In summary, the proposed transaction makes numerous changes for the management of Pepco. It places Pepco-DC in a second-tier position within the EU' decision making management structure; removes the Pepco Region President from the decision making table; adds at least two additional levels of approval for large budget decisions; results in Exelon selecting all Pepco and PHI board members; reduces the number of independent directors on the Pepco and PHI boards of directors; includes Mr. Crane and Mr. O'Brien as the Chairs and Vice Chairs of the PHI and Pepco boards; does not ensure that there will be a board member from the District on the Pepco Board of Directors; introduces a new Management Model that has not previously been used with distribution companies that operate in multiple jurisdictions or that operate as part of a holding company with their own shared services company and that utilize unspecified best practices; adds a second service company that operates differently from PHISCo; and will operate pursuant to a new Delegation of Authority that governs certain budget expenditures. The Joint Applicants have not persuaded the Commission that District ratepayers will be benefited by the change in management structure that is being proposed nor will the change benefit the Commission as it performs its administrative duties. The Commission concludes that these changes, especially the ones that place Pepco on an unequal footing with other Exelon Utilities, will minimize Pepco-DC's voice and role within EU while changing how Pepco-DC operates within the proposed merged organization in a manner that has not been shown to be beneficial to the District and its ratepayers. Indeed, the proposed management structure will potentially harm Pepco and the ratepayers that it serves by diminishing Pepco's role and its ability to make decisions that are responsive to the needs of its ratepayers and the policy directives of the District.

3. FACTOR 3: The effects of the transaction on public safety and the safety and reliability of services

Summary of Joint Applicants' Position Pertaining to Factor 3

198. The Joint Applicants recognize that under D.C. Code §34-1101, "[e]very public utility doing business within the District of Columbia is required to furnish service and facilities reasonably safe and adequate and in all respects just and reasonable."[550] In addition, under the Commission's Electricity Quality of Service Standards ("EQSS"),[551] the utility "shall not exceed the reliability performance standards established for the following indices, calculated using District of Columbia data: System Average Interruption Frequency Index ("SAIFI") (stated in

[550] D.C. Code § 34-1101(a) (2015).

[551] 15 DCMR §§ 3600–3699.

interruptions) and System Average Interruption Duration Index ("SAIDI") (stated in hours),"[552] which are set forth in 15 DCMR § 3603.11. Mr. Alden testified on behalf of the Joint Applicants that, "[w]e have an obligation to meet the EQSS standards and we'll do what it takes to do that."[553] Thus, the Joint Applicants conclude, "the Merger will allow Exelon and Pepco to combine resources, knowledge and experience to expand on the success that Pepco recently has experienced and meet the EQSS requirements on an annual basis."[554] The Joint Applicants submit that their "stated intention to meet the Commission-imposed annual reliability standards should remove any doubt that the Merger will not have an adverse impact on reliability in the District of Columbia."[555]

199. The Joint Applicants are also proposing an independent three-pronged reliability performance commitment, which, as a whole, provides benefits that otherwise would not be available absent the merger:

- Reliability performance in the District of Columbia to meet or exceed the three-year average of the Commission's EQSS annual targets for the years 2018 to 2020.[556] Specifically, the Joint Applicants commit that Pepco will achieve a SAIFI of 0.66 interruptions and a SAIDI of 90 minutes.[557]
- A cap on the aggregate reliability-driven capital and O&M spending levels for the period 2015 to 2020.[558]
- A voluntary 50 basis point reduction to the return on equity that Pepco would otherwise be entitled to in its first distribution rate case filed after January 1, 2021, to the extent that the reliability performance targets are not met.[559]

The Joint Applicants have conditioned the spending commitment on there being no changes in law, regulations, or extreme weather events requiring increases in reliability-related spending to restore service and facilities or variations in the schedule of the DC PLUG that are outside of Pepco's control.[560]

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552 15 DCMR § 3603.10.

553 Joint Applicants' Br. at 73, citing Tr. at 1138:14-15 (Alden Cross).

554 Joint Applicants' Br. at 73.

555 Joint Applicants' Br. at 73-74.

556 Joint Applicants' Br. at 74, citing Joint Applicants (4B) at 2:12, Table 1 (Rigby).

557 Joint Applicants' Br. at 74, citing Joint Applicants (4A)-2 at 2, Commitment 7.

558 Joint Applicants' Br. at 74, citing Joint Applicants (4A)-2 at 2, Commitment 7, Table 1.

559 Joint Applicants' Br. at 74, citing Joint Applicants (4A)-2 at 3, Commitment 8.

560 Joint Applicants' Br. at 74, citing Joint Applicants (4A)-2 at 2, Commitment 7. The DC PLUG schedule to which the Joint Applicants refer is that which is referenced in the February 17, 2015 Supplemental Direct Testimony

200. As part of its three-pronged reliability commitment, the Joint Applicants claim that Pepco's District of Columbia customers can expect average reliability performance for the period 2018 through 2020 that is equal to or better than the three-year average EQSS reliability performance measured over the same period.[561] According to the Joint Applicants, the proposed commitment, coupled with Mr. Alden's acknowledgement that Pepco must meet the annual EQSS, establishes that reliability performance post-merger will be equal to or better than that which can be expected if Pepco were to remain a stand-alone company.[562] The Joint Applicants recognize OPC's argument that the Commission has already rejected an averaging approach in setting the EQSS standards, and therefore any commitment that relies on an averaging is not in the public interest.[563] However, because the Joint Applicants' proposal here includes an averaging of continuously improving targets, the Joint Applicants submit that it should address any concerns the Commission raised in the EQSS proceeding. The Commission's order in the EQSS proceeding is clear that the Commission did not desire standards that would reset annually based on actual historical performance because such a procedure could reward poor performance by making the standards less stringent in subsequent years.[564] The Joint Applicants are not proposing to reset performance targets based on past, actual performance. Rather, the Joint Applicants' proposal is based on a three-year average of increasingly demanding future reliability targets.[565]

201. The Joint Applicants submit that this commitment enhances the status quo by incorporating a voluntary spending cap. If the Proposed Merger is approved, the Joint Applicants commit to a cap on the aggregate reliability-driven capital and O&M spending levels for the period 2015 to 2020.[566] The Joint Applicants state that Pepco's current obligation to meet the Commission's EQSS targets does not include pre-established spending constraints.[567] They point to Mr. Gausman's explanation that Pepco's achievement of the "the EQSS SAIDI standard

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of Mark Alden at page 3 n.2 (*Formal Case No. 1116, In the Matter of Applications for Approval of Triennial Underground Infrastructure Improvement Projects Plan* ("*Formal Case No. 1116*"), Pepco and DDOT's Ninety Day Supplemental Report to the Joint Underground Infrastructure Improvement Projects Plan, filed February 10, 2015) not the schedule referenced in Joint Applicants (4A)-2.

561 Joint Applicants' Br. at 75.

562 Joint Applicants' Br. at 76.

563 Joint Applicants' Br. at 76, citing OPC (B) at 15:8-10 (Mara).

564 Joint Applicants' Br. at 76, citing Joint Applicants Cross Examination Exhibit No. 51 at 21 of 30.

565 Joint Applicants' Br. at 76.

566 The Joint Applicants state that the reliability-related capital and O&M spending cap is a District of Columbia-related commitment and is not intended to be applied to Pepco on a system-wide basis. With respect to the System Scheduled Maintenance, which appears in Commitment 7 as a system-wide number, the District of Columbia allocated portion of the budgeted spending caps and the actual spending would be determined in a future rate proceedings for purposes of evaluating whether the commitment has been met. Joint Applicants' Br. at 77 n. 331, citing Joint Applicants (4E) at 1-4 (Gausman).

567 Joint Applicants' Br. at 77, citing Tr. at 1379:8-13 (Gausman Rejoinder); Tr. at 3203:15-31 (Mara Cross).

may very well require an increase in expenditures, and that is a concern as we move out further into the lower values of SAIDI."[568] According to the Joint Applicants, while Pepco has made great strides in improving its reliability performance since the passage of the EQSS reliability targets, including in 2014, such improvement does not guarantee future performance improvements, let alone within budgeted spending levels. In fact, during the hearing, Mr. Gausman testified that after a company achieves overall system improvement such as that which Pepco has achieved, it becomes increasingly difficult to continue to realize even minimal SAIDI and SAIFI improvements at the dollar levels forecasted to be spent.[569] Mr. Gausman explained that as reliability performance improves, a company must continue to incur costs to ensure that the reliability improvements achieved are not lost, even if overall system performance does not improve over current levels.[570]

202. The Joint Applicants further submit that, unlike the Commission's EQSS regulations, the reliability commitment also includes an automatic voluntary financial penalty if the level of reliability improvement proposed is not achieved for either SAIFI or SAIDI.[571] The commitment calls for a 50 basis point reduction to the authorized rate of return on equity to which Pepco would otherwise be entitled in its next electric distribution rate case filed after January 1, 2021 if either target is not met.[572] The financial penalty proposed could be as much as about $5.6 million annually, which is a meaningful amount for Pepco-DC. This penalty, if imposed, would be in addition to any penalty that the Commission could otherwise choose to impose under its existing regulations and it would remain in place until such time as Pepco successfully obtains a Commission order approving new rates that end the return on equity penalty.[573]

203. Joint Applicants contend that, following the close of the Proposed Merger, Pepco will have access to more extensive Exelon utility resources for storm restoration, and together, Exelon's sister utilities form a broad regional network with the ability to dedicate and mobilize storm restoration resources, thereby reducing reliance on third-party mutual-assistance programs.[574] Joint Applicants witness Alden testified that, under utility mutual assistance agreements, there is no guarantee that other utilities will provide resources during or after a storm event, particularly when those other utilities may also be facing a large number of actual or potential outages from a large regional storm. By contrast, the Joint Applicants aver that Exelon utilities are committed to making their storm restoration resources available to their affiliates on a priority basis and are able to pre-position Exelon affiliated crews before actual storm events to

568 Joint Applicants' Br. at 78, quoting Tr. at 1379:12-19 (Gausman Rejoinder).

569 Joint Applicants' Br. at 78, citing Tr. at 1379:8-1380:3 (Gausman Rejoinder).

570 Joint Applicants' Br. at 78, citing Joint Applicants (3E) at 11:15-12:4 (Gausman).

571 Joint Applicants' Br. at 80, citing Joint Applicants (4A)-2 at 3, Commitment 8.

572 Joint Applicants' Br. at 80, citing Joint Applicants (4A)-2 at 3, Commitment 8.

573 Joint Applicants' Br. at 80.

574 Joint Applicants' Br. at 80, citing Tr. at 1225:9-1226:4 (Commission Cross of Butler).

ensure that those crews are ready to go to work immediately.[575] According to the Joint Applicants, the post-Merger enterprise will have substantially greater combined resources to respond promptly and effectively to major storms and other emergencies.[576] The fact that Pepco's service territory is geographically contiguous or close to the service territories of PECO and BGE will allow BGE and PECO crews to respond quickly to events in Pepco's service territory to assist Pepco's crews in expeditiously restoring power to District of Columbia customers.[577] The Joint Applicants maintain that these enhanced emergency response assistance benefits will be made possible, at least in part, by the implementation of common procedures shared across Exelon's and PHI's utilities post-Merger, such [as] "lock out" and "tag out" ("LOTO") procedures. Pepco's customers will directly benefit from a common LOTO procedure through the elimination or reduction of training and preparatory hours resulting in faster restoration and reduction in overall outage duration,[578] and elimination of time spent on permitting, assistance and supervision of non-affiliate utility crews.[579] As Joint Applicant witness Gausman explained, "[t]imely, adequate and efficient storm preparedness and response cannot be downplayed as a benefit of this Merger."[580]

204. Finally with regard to the Joint Applicants' commitment to safety and reliability, the Joint Applicants state that public and workplace safety will continue to be a core value for PHI and Pepco.[581] They also state that another important aspect of the merger is the shared focus that Exelon and PHI have in prioritizing cyber security at their operating utilities.[582]

Summary of OPC's and Intervenors' Position Pertaining to Factor No. 3

205. OPC argues that since 2011, when Pepco's poor reliability performance resulted in Pepco being identified as the "Most Hated Company in America,"[583] the Commission, OPC, and Pepco have worked diligently to improve Pepco's reliability performance. For its part, the Commission established the EQSS, which require Pepco to meet annual SAIFI and SAIDI metrics or face financial penalties. OPC quotes Mr. Rigby's statement that improving reliability

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575 Joint Applicants' Br. at 81, citing Joint Applicants (D) at 7:6-15 (Alden).

576 Joint Applicants' Br. at 81, citing Joint Applicants (A) at 11:1-2 (Crane); Joint Applicants (B) at 9:14-17 (Rigby).

577 Joint Applicants' Br. at 81-82, citing Joint Applicants (H) at 2:8-13 (Butler).

578 Joint Applicants' Br. at 82, citing Joint Applicants (3E) at 16:22-17:2 (Gausman).

579 Joint Applicants' Br. at 82, citing Tr. at 1029:9-13 (O'Brien Cross).

580 Joint Applicants' Br. at 82, quoting Joint Applicants (3E) at 18:5-6 (Gausman).

581 Joint Applicants' Br. at 82, quoting Joint Applicants (A) at 7:17-19 (Crane) (Exelon is "committed to maintaining the highest standards of safety and reliability for our people, our customers and the communities in which we work."); Joint Applicants (B) at 3:14 (Rigby) ("we make safety the most important part of everything we do.").

582 Joint Applicants' Br. at 83.

583 OPC's Br. at 68, citing OPC Cross Examination Exhibit No. 3.

performance was not simply an important goal, but it "dominated our focus."[584] OPC maintains that Pepco developed a Reliability Enhancement Plan and an Emergency Restoration Improvement Plan, which included hundreds of millions of dollars in capital and O&M expenditures that were designed to improve Pepco's reliability performance, and by implementing its improvement plans, Pepco has met the Commission's EQSS performance requirements each year. In fact, OPC asserts, excluding Major Service Outages, Pepco's SAIFI and SAIDI performance has improved year-over-year from 2011 through 2014.[585]

206. Given the importance of reliability in the District, OPC submits that the Commission should find that the public interest requires the Joint Applicants to demonstrate that the proposed transaction will result in net benefits in terms of reliability performance. OPC asserts "[c]omparing Exelon's reliability commitment against Pepco's standalone reliability performance in a no-transaction future demonstrates that the proposed transaction provides no meaningful benefits to ratepayers in terms of reliability performance."[586] OPC claims that the Joint Applicants' reliability commitment, as revised, remains unacceptable for numerous reasons, including that it would yield no benefits to ratepayers above and beyond the benefits ratepayers would enjoy in the absence of the proposed transaction.[587]

207. OPC asserts that the Joint Applicants' reliability commitment: (1) contains exceptions that essentially excuse Pepco from meeting the SAIFI and SAIDI targets; (2) does not include a commitment to hold spending at certain levels and does not include a commitment to forego seeking recovery in Pepco's District customers' rates, of reliability spending in excess of the levels shown in Table 1 of Item 7 of Exhibit Joint Applicants (4A)-2; and (3) does not include subjecting Pepco to the Return on Equity ("ROE") penalty if actual spending exceeds the levels shown in Table 1 of Item 7. OPC states that these three revelations completely eviscerate the Joint Applicants' claim that their reliability commitment provides a benefit to Pepco's ratepayers that they would not realize absent the proposed transaction.[588] First, OPC argues, the reliability commitment improperly excludes non-compliance for weather-related reasons, ignoring that the EQSS already exclude the impact of Major Service Outages.[589] Second, OPC submits that contrary to their explicit representations, the Joint Applicants' modified reliability commitment does not: (1) include a cap on spending; (2) include a pledge to forego rate recovery of reliability-related spending; or (3) include any penalty for exceeding spending levels.[590] Third, the Office avers that the Joint Applicants' proposed ROE penalty provides no measure of

584 OPC's Br. at 68, quoting Tr. at 582:18-22 (Rigby).

585 OPC's Br. at 68-69.

586 OPC's Br. at 69.

587 OPC's Br. at 71.

588 OPC's Br. at 74.

589 OPC's Br. at 74.

590 OPC's Br. at 75-83.

protection because the Joint Applicants could avoid the penalty at will, to the extent the penalty even applied at all.[591]

208. OPC goes on to argue that the Joint Applicants' reliability commitment either ignores or improperly takes credit for Pepco's substantial improvement in reliability performance – improvement that is likely to continue in the absence of the proposed transaction.[592] OPC claims that the Joint Applicants conveniently ignore irrefutable evidence of Pepco's recent and on-going impressive gains in reliability;[593] accomplished with no help from Exelon.[594] Furthermore, according to the Office, the Joint Applicants produced no evidence that Pepco's reliability improvements and continued compliance with the EQSS would cease if the transaction is not approved and Pepco moved forward on a stand-alone basis.[595] In fact, OPC submits, the only record evidence suggests the opposite is true. OPC witness Mara noted that "Pepco's reliability has been steadily improving since 2010 and as demonstrated by these graphs [at page 160 of Pepco's 2014 Consolidated Report] Pepco expects such improvements to continue absent the proposed merger."[596] Mr. Mara added, "[i]f Pepco's current reliability improvement programs and increased focus on reliability improvement continue, reliability in the District will improve even absent the merger."[597]

209. Continuing its criticism of the Joint Applicants reliability commitments, OPC asserts that the Joint Applicants: (1) have no plan for actually improving Pepco's reliability performance; (2) have not identified any best practices that might be deployed post-transaction; (3) have not quantified the benefits of that deployment; and (4) have not explained why Pepco could not implement best practices on its own.[598] In addition, OPC claims that the Joint Applicants: (1) have not identified any specific project that Exelon would modify in order to improve reliability performance;[599] and (2) reliability commitment (a) undervalues DC PLUG's likely contribution to Pepco's future reliability performance;[600] (b) rests on a flawed averaging

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591 OPC's Br. at 83-86.

592 OPC's Br. at 86.

593 OPC's Br. at 86-87, citing OPC Cross Examination Exhibit No. 2 (Joint Applicants' Response to PSC Staff Data Request No. 6-1) (setting forth Pepco's 2014 SAIFI and SAIDI performance, which reflect significant improvement from 2013). Mr. Crane testifies that Pepco's significant improvement in reliability must be acknowledged. Joint Applicants (A) at 14:1-3 (Crane).

594 OPC's Br. at 86-87.

595 OPC's Br. at 89.

596 OPC's Br. at 89, citing OPC (B) at 10:15-19 (Mara).

597 OPC's Br. at 89, citing OPC (B) at 6:3-5 (Mara).

598 OPC's Br. at 91-94.

599 OPC's Br. at 95-96.

600 OPC's Br. at 96-98.

method rather than annual compliance with the EQSS; and (c) provides no spending-related or rate-related benefits to Pepco's customers in the District.[601]

210. **AOBA**. AOBA asserts that the levels of SAIDI that Exelon initially proposed to guarantee did not meet the Commission's established EQSS for SAIDI for the years 2018-2020,[602] and, although Exelon has subsequently proposed to modify its SAIDI commitment to more closely approximate the Commission's reliability standards, it did so in conjunction with an adjustment to its proposed SAIFI commitment that noticeably dilutes the value of that commitment. Further, AOBA contends that Exelon maintains the use of a three-year average measure for assessing its performance despite the fact that the EQSS are established on a year-by-year basis.[603]

211. AOBA submits that the Joint Applicants' reliability-related commitments as currently presented: (1) provide no assurance of reliability performance beyond the levels that can reasonably be expected of Pepco in the absence of the proposed merger; (2) are premised on reliability-related budgets for capital expenditures and O&M costs that have not been properly justified, are over inflated, are not adequately tied to the achievement of reliability improvements, and/or are not presented on a basis that clearly identifies budgeted costs for Pepco's District of Columbia operations; and (3) offer essentially meaningless reliability guarantees that would be applicable only on a one-time basis and would have no impact on rates for at least six years after the merger even if the Joint Applicants' reliability commitments are not met.[604]

212. Concerning the Joint Applicants' reliability-related budget commitments, AOBA submits that the record of this proceeding lacks adequate and appropriate justification for any action by this Commission that would give credibility to the Joint Applicants reliability-related capital and O&M Budgets. AOBA contends that no linkage has been established between service reliability improvements that can or will be achieved and Pepco's budgeted reliability-related capital and O&M expenditures.[605] AOBA asserts further that, although Pepco's actual SAIFI and SAIDI results for 2014 improve upon the Commission's EQSS for 2018, those better than expected reliability results for 2014 were achieved despite the fact that Pepco substantially underspent its reliability-related capital and O&M budgets for 2014. Thus, AOBA claims that, in this context, the Commission has substantial reason to question the levels of reliability-related expenditures that the Joint Applicants suggest Pepco will require over the years 2015-2020.[606]

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[601] OPC's Br. at 99-103.

[602] AOBA's Br. at 49, citing AOBA (A) at 34 (Oliver).

[603] AOBA's Br. at 49-50.

[604] AOBA's Br. at 50-51.

[605] AOBA's Br. at 52.

[606] AOBA's Br. at 52.

213. AOBA maintains that the record of this proceeding also demonstrates that the reliability-related O&M expenditures the Joint Applicants have budgeted for Schedule System Maintenance are improperly premised on estimates of system-wide costs (*i.e.*, combined costs for DC and MD), and their proposed approach for identifying the portion of those O&M costs applicable to the District of Columbia does not provide the Commission with adequate basis for assessing compliance with the Joint Applicants commitment to not exceed the budgeted costs presented in Joint Applicants' Exhibit (4A)-2, Commitment 7.[607] According to AOBA, the O&M budget the Joint Applicants present also does not ensure that Pepco's District of Columbia customers will only be held responsible for costs actually incurred to provide service in the District. AOBA asserts that if a reliability-related O&M budget commitment is to be meaningful for Pepco's District of Columbia operations, then a separate O&M budget must be established for Pepco's operations in the District, and the reasonableness of the budget must be clearly demonstrated, and the Joint Applicants have done neither.[608]

214. AOBA argues that the Commission should reject the reliability related capital and O&M budgets the Joint Applicants have presented in this proceeding. In this regard, AOBA submits that Pepco's actual reliability driven capital expenditures for the District were $22.0 million or about 16.5% below the Company's 2014 budget, and Pepco's actual O&M expenditures for 2014 were $8.5 million or 20.5% below the levels the Company had budgeted for 2014. AOBA also notes that Joint Applicants' 2020 capital budget is 3% above the 2019 budget. But for the other years, the budget did not reflect a simple inflation adjustment[609]. Yet, according to AOBA, despite significantly under spending its 2014 budgeted costs, Pepco was able to achieve significant improvements in its 2014 SAIFI and SAIDI metrics for the District. AOBA contends that this basic observation raises substantial concerns regarding the appropriateness of the cost estimates that underlie the Joint Applicants budget commitments since those commitments appear to be built off of the 2014 budgets that appear to have been significantly overstated. Furthermore, according to AOBA, Pepco's actual 2014 results, which advance by several years Pepco's SAIFI and SAIDI achievements, strongly suggest that Pepco may not need the level of expenditures previously budgeted to achieve either the Commission's EQSS for future years or the three-year average SAIFI and SAIDI levels to which the Joint Applicants commit.[610]

215. **District Government.** The District Government alleges that the first flaw in the Joint Applicants' argument that its reliability commitments confer a benefit is the extent to which Pepco has advanced, and is likely to continue to advance, towards compliance with the Commission's EQSS on a stand-alone basis, without the Proposed Merger.[611] The District Government avers that the record demonstrates three failures of proof in the Joint Applicants'

[607] AOBA's Br. at 53.

[608] AOBA's Br. at 53.

[609] AOBA's Br. at 55-57.

[610] AOBA's Br. at 55.

[611] District Government Br. at 33.

claim that their merger reliability commitments actually confer any benefit on the District of Columbia's retail electricity consumers: (1) the evidence establishes that Pepco is likely to have attained the "three-year average" SAIDI and SAIFI levels promised in that commitment without the Proposed Merger; (2) the Joint Applicants' failure to quantify any estimate of Pepco's stand-alone cost of compliance with the Commission's EQSS forecloses their claim that the budgetary component of their reliability commitment offers District of Columbia retail electricity customers any genuine benefit; and (3) the commitment is contingent on maintenance of a construction schedule for the DC PLUG undergrounding initiative that is unlikely to be maintained and as to which the Joint Applicants' own witnesses are unable to agree on which construction schedule establishes the benchmark for triggering the Joint Applicants' contingency.[612]

216. According to the District Government, the SAIDI level promised in these commitments (an average interruption duration of 90 minutes over the period 2018 through 2020) is substantively identical to that required by the Commission's EQSS and that achieving that level of performance is incumbent on Pepco with or without the Proposed Merger.[613] In contrast, the District Government asserts that "the Joint Applicants' SAIFI level commitment represents an improvement over the EQSS requirement; however, the frequency of 0.66 interruptions on average between 2018 and 2020 is only 0.03 interruptions better than Pepco's stand-alone performance in 2014, and only 0.04 interruptions better than Pepco forecasted in 2014 achieving on a standalone basis by year-end 2017, without considering the effects of undergrounding projects such as DC PLUG."[614] Thus, the Joint Applicants' proposed SAIFI level really offers Pepco's District of Columbia customers nothing that Pepco was not well on its way to attaining on a pre-merger, standalone basis.[615]

Discussion Pertaining to Factor 3

217. Public Interest Factor 3 requires the Commission to assess the effect of the Proposed Merger on public safety and the quality and reliability of services. The Joint Applicants have made a commitment with regard to reliability and quality of service, as set forth in Joint Applicants (4A)-2. The Joint Applicants, "commit that Pepco will achieve reliability performance for 2018-2010 at a level equal to or better than the corresponding levels in the Commission's current EQSS averaged over the same three-year period."[616] Specifically, the Joint Applicants commit to meet the SAIFI and SAIDI averages without exceeding the aggregate capital and O&M spending levels listed in Table 1 of Commitment 7.[617] The Joint Applicants submit that their "stated intention to meet the Commission-imposed annual reliability standards

612 District Government Br. at 33-34.

613 District Government R.Br. at 26.

614 District Government R.Br. at 26.

615 District Government R.Br. at 26-27.

616 Joint Applicants (4A)-2, p. 2, Commitment 7.

617 Joint Applicants (4A)-2, p. 2, Commitment 7.

should remove any doubt that the Merger will not have an adverse impact on reliability in the District of Columbia." [618]

218. While the Joint Applicants concede that the Proposed Merger is not a necessary pre-condition to Pepco achieving improvements in SAIDI and SAIFI, they contend the Proposed Merger "will build upon Pepco's efforts to improve its reliability. These additional improvements would not be expected to occur without increasing reliability-related capital and operations and maintenance expenditures above the levels in Pepco's existing long-range plans. By implementing Exelon's best practices, the combined companies will achieve these improvements without increasing Pepco's planned expenditure levels. In addition, Exelon has committed to achieve the improvements by the end of 2020 and if the improvements have not been achieved, Exelon has committed as part of the Merger commitments to pay a penalty."[619]

219. The Commission notes that "[t]he Joint Applicants are not proposing a reliability commitment for the period 2015-2017; however, the EQSS performance standards will continue to apply to Pepco."[620] Thus, the Joint Applicants are not committing to enhancing the quality and reliability of services beyond meeting the current EQSS from 2015-2017.

220. The Joint Applicants state, "Pepco will achieve reliability performance for 2018-2020 at a level equal to or better than the corresponding levels set forth in the . . . EQSS averaged over the same three-year period."[621] The Joint Applicants have not committed to meeting any particular SAIFI or SAIDI metrics on an annual basis for those three years, or, for that matter, for any specific year.[622] Rather, the Joint Applicants' commitment is strictly limited to meeting only the <u>average</u> of those three years.[623] Use of a three-year average to measure compliance with reliability performance is directly contrary to the current EQSS. The Joint Applicants ignore the fact that, prior to the adoption of the current EQSS, reliability for the District was based on a five-year average of Pepco's Outage Management System data, but the Commission then rejected continued use of an averaging method when it established the EQSS and determined that annual compliance would be required.[624]

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[618] Joint Applicants' Br. at 73-74.

[619] DC Government Cross Examination Exhibit No. 48 (Joint Applicants Response to DC Government DR 1-75).

[620] AOBA Cross Examination Exhibit 41.

[621] Joint Applicants (4A)-2 at 2, Commitment 7.

[622] *See also* AOBA Cross Examination Exhibit No. 41 (Joint Applicants Response to AOBA DR 6-5: "Joint Applicants are not proposing a reliability commitment for the period 2015-2017; however, the EQSS performance standards will continue to apply to Pepco.")

[623] Joint Applicants (4A)-2 at 2, Commitment 7; OPC Br. at 99-100 ("The commitment is the mathematical average of the annual figures in columns 2-4, and it is misleading to juxtapose the words 'Exelon Commitment' with annual SAIFI and SAIDI metrics that are *not* part of the commitment.") (emphasis in original).

[624] OPC (B) at 15:13-16 (Mara).

221. The record evidence confirms that Pepco's SAIDI and SAIFI improved from 2011 to 2014.[625] In its 2013 Annual Report, PHI indicated that its utilities achieved one of the best reliability performances ever.[626] In addition, the Joint Applicants produced no evidence that Pepco's reliability improvements and continued compliance with the EQSS would cease if the Proposed Merger is not approved and Pepco continued to operate on a stand-alone basis. In fact, as pointed out by OPC, the record evidence suggests the opposite is true. OPC witness Mara noted that "Pepco's reliability has been steadily improving since 2010 and as demonstrated by these graphs [at page 160 of Pepco's 2014 Consolidated Report, showing actual data through 2013] Pepco expects such improvements to continue absent the proposed merger."[627] Mr. Mara added, "[i]f Pepco's current reliability improvement programs and increased focus on reliability improvement continue, reliability in the District will improve even absent the merger."[628] While Joint Applicant witness Gausman testified that Pepco could use some assistance, especially addressing the SAIDI requirement, he also concedes that there is nothing in his direct testimony intended to imply that Pepco would be unable to meet the EQSS standard for SAIDI and SAIFI if the Proposed Merger is not approved.[629]

222. The record confirms that Pepco met its 2014 EQSS requirements without spending the full amount of its capital spending/reliability budget. Spending was $22,006,712 below budget of $133,716,207 for reliability driven expenditures for Pepco-DC <u>and</u> $8,510,817 below the $41,552,005 for O&M reliability expenditures for Pepco-DC & MD.[630] However, testimony from Joint Applicant witness Rigby indicates that Pepco as a stand-alone company is not committing to the current capital budget.[631] Testimony by Joint Applicant witness Gausman at the evidentiary hearing confirmed that Commitment 7 is not a commitment to achieve currently existing EQSS targets because Pepco is under an obligation to achieve the EQSS standards.[632] Joint Applicant witnesses Alden and Gausman stated that Joint Applicants' Commitment 7 with respect to the three-year averaging of SAIFI/SAIDI achievement is in addition to Pepco's continuing obligation to meet the SAIDI and SAIFI requirements of the EQSS each and every year.[633] In 2014, Pepco already exceeded the 2018 SAIDI EQSS target and the 2020 SAIFI EQSS target.[634]

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625 Tr. at 588:6-10; OPC Cross Examination Exhibit No. 2.

626 Tr. 587:15-588:2.

627 OPC (B) at 10:15-19 (Mara).

628 OPC (B) at 6:3-5 (Mara).

629 Joint Applicants (E) 7:10-20 (Gausman); Tr. 1683:11-1684:13.

630 *See* AOBA Cross Examination Exhibit No. 38 (Joint Applicants Response to OPC DR 20-10).

631 Tr. at 737:8-738:1.

632 Tr. at 1389:4-1939:11.

633 Tr. at 1131:18-1132:4; 1383:15-17.

634 *See* AOBA (2A) at 36-37 (Oliver).

223. The Commission notes that the Joint Applicants reliability commitments include the effects of the DC PLUG that are not in any way connected with the Proposed Merger. The Commission agrees with OPC that Joint Applicants' claim that the Proposed Merger would improve Pepco's reliability is "heavily dependent upon the positive effects of the proposed DC PLUG undergrounding initiative, which predates, and is entirely independent of, the proposed merger."[635] OPC witness Mara explains that DC PLUG will underground approximately 21 feeders in the first three years, with more feeders in subsequent years.[636] Of critical importance, Pepco's 2013 projections for reliability, which reflect continued improvements and compliance with the EQSS through at least 2016, "do not include any improvements in reliability that may stem from DC PLUG."[637] The DC PLUG projects "will have a significant impact on improving reliability in the District in the future, above and beyond Pepco's existing reliability-related projects undertaken to meet the EQSS."[638] Thus, the Joint Applicants' reliability commitments "improperly include[s] the effect of the DC PLUG program."[639] We agree, as OPC witness Mara summarized, "it is obvious that reliability improvements resulting from DC PLUG are in no way products of, or benefits from, the proposed merger and, therefore, should be excluded from Exelon's projections regarding merger-related reliability benefits." [640]

224. As AOBA further explained, using 2014 as the baseline, after factoring in the DC PLUG impact, Pepco's resulting performance will exceed the 2018-2020 average for SAIFI and SAIDI listed in Joint Applicants (4A)-2. Thus, the Joint Applicants are not providing any additional benefit for reliability performance that Pepco is not already providing on a stand-alone basis, especially when factoring in the impact that the DC PLUG will have on enhancing system reliability.[641]

225. Although Pepco's performance is laudable, the record highlights that Pepco's required performance can be achieved at less cost. The Reliability Capital Budget and Forecast in the 2015 Annual Consolidated Report ("ACR") referenced by Joint Applicants witness Gausman is below the reliability driven capital budget levels contained in Joint Applicants' Commitment 7, Table 1.[642] We recognize that, in order to sustain its reliability performance, Pepco must continue to incur costs. However, because the Joint Applicants, when presenting their proposed reliability budget commitment in Table 1, did not take into consideration the

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635 OPC (B) at 5:15-17 (Mara).

636 The Commission notes that feeders running in parallel to the 21 selected feeders will also be undergrounded.

637 OPC (B) at 13:4-6 (Mara).

638 OPC (B) at 3:10-12 (Mara).

639 OPC (B) at 13:13-14 (Mara).

640 OPC (B) at 14:5-8 (Mara).

641 *See* AOBA (2A)-5, at 1.

642 Tr. at 1381. "And, in fact, the consolidated report that we just filed a few days ago, I believe there's about 40 pages of budget project-related information dealing with the reliability work that is planned for this year."

substantial under spending in reliability that occurred during 2014,[643] Table 1, which contains no corresponding adjustment for this under spending, may be overly inflated.[644] Thus, the Joint Applicants' characterization in their initial brief that the Proposed Merger will produce equal and perhaps greater levels of reliability at a lower cost to customers is not supported by the record evidence.[645] Accordingly, we conclude that the inflated budget offered in Joint Applicants' (4A)-2, Table 1, when compared to Pepco's 2015 ACR budget, is in fact a harmful effect on ratepayers which would result in higher than necessary rates for District ratepayers.[646]

226. Moreover, Joint Applicant witness Alden testified that assuming the Proposed Merger is approved, as filed, Exelon would perform a circuit-by-circuit review of Pepco's system and determine whether more work is needed to be done than initially anticipated to meet reliability standards. If the extra unanticipated work requires Exelon to exceed capital and O&M budgets it committed to not exceed he stated, "We would do what it took to meet the EQSS standards as required, and would manage those costs as best we could not to exceed the [budget] limits."[647] When asked by OPC whether Joint Applicants were guaranteeing that they will not exceed the aggregate capital and O&M spending levels, Mr. Alden responded: "What we're committing to is to meet the three-year average with a 50 basis points penalty associated with it for the capital dollars as committed to in our reliability spending."[648] Alden further stated, "If we exceed the spending levels that we've committed here to meet the commitment standards, then those additional expenditures would be subject to approval through [the] normal ratemaking process."[649] Thus, even assuming the Proposed Merger were approved, the record suggests it is possible that even with the Joint Applicants commitment to cap on the aggregate reliability driven capital and O&M spending levels from 2015-2020, District ratepayers could actually pay more than the capped amounts.

227. While the Joint Applicants have committed to meet a three-year average SAIDI and SAIFI performance measure at a capped budget under certain conditions and offer to take a 50 basis point reduction in the first rate proceeding after January 1, 2021 as a financial penalty if the commitment is not met between 2018-2020 could be viewed as a direct and traceable benefit of the Proposed Merger, are not persuaded that the claimed benefits are as direct or tangible as

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643 "The Merger commitment is guaranteeing reliability improvement while also guaranteeing that the reliability-related capital and O&M budgets set forth in the 2014-2018 budget would not increase." Joint Applicants' (3E) at 4:3-5 (Gausman). [*See also*, page 38 of Pepco's Capital Budget and Forecast 2014-2018 for reliability, filed *Pepco's Annual Consolidated Report* ("*PEPACR-2014*"), Potomac Electric Power Company's 2014 Annual Report, filed on February 18, 2014, supplemented on June 2, 2014.] *See also*, AOBA (2A) at Attachment 1 (Joint Applicant Response to DR AOBA 3-13) (Oliver). Such a budget was maintained in Joint Applicants (4A)-2.

644 AOBA Cross Examination Exhibit No. 58 (Gausman capital budget work papers).

645 Joint Applicants' Br. at 27.

646 *See* Paragraph 221, *supra*.

647 Tr. at 1137:13-1138:9.

648 Tr. at 1141:19-1142:6; *see also* Joint Applicants (4D) 2:1-9 (Alden).

649 Tr. at 1150:21-1151:3.

the Joint Applicants represent. Under Factor Nos. 3 and 1, the Joint Applicants argued that they would improve Pepco's reliability performance, which would in turn benefit ratepayers to the tune of $121.6 million. However, the Commission finds that the Joint Applicants' reliability commitments are no better than what the Commission's EQSS requires Pepco to achieve on a stand-alone basis. We also find that based on the 2014 actual performance of Pepco and the projected DC PLUG efforts, Pepco's current reliability performance exceeds what is being offered as a Proposed Merger commitment for a 3-year average from 2018-2020. Thus, the Joint Applicants do not offer any direct or tangible benefit above that provided by Pepco on a stand-alone basis because the Joint Applicants' quantification of projected reliability improvements do not take into account what Pepco would achieve absent the Proposed Merger.[650] Consequently, we cannot conclude that the Joint Applicants' commitment in this regard constitutes a benefit directly arising from the Proposed Merger transaction. A benefit, for reliability purposes, could have been an offer to enhance Pepco's ability to achieve reliability performance targets beyond Pepco's current performance levels on a stand-alone basis or lower the costs of achieving the EQSS targets. No such offers were made in this proceeding.

228. Joint Applicants Commitment 8 indicates that if the level of reliability improvement set forth in Commitment 7 is "not achieved across either SAIFI and SAIDI, the return on equity to which Pepco would otherwise be entitled in its next electric distribution rate case filed after January 1, 2021, will be reduced by 50 basis points."[651] We note that testimony at the hearing indicates there are qualifiers to this commitment. First, Joint Applicants witness Crane testified that the ROE penalty would not apply if Pepco met the reliability targets in Commitment 7 but exceeded the spending levels set forth in Table 1 of Commitment 7.[652] Second, Joint Applicants witness Gausman indicated the ROE penalty applies to meeting reliability targets, and not to holding spending to certain levels.[653] Third, the ROE penalty is not automatic or self-executing. Instead, assuming Pepco does not meet the three-year average, the penalty would not actually be imposed unless and until Pepco voluntarily decided to file its next rate case. Such a rate filing might not occur until late 2021, or in 2022, or even later. As OPC witness Mara pointed out, this lengthy delay in potential imposition of a financial penalty represents greater risk to ratepayers than would a penalty imposed one or two years post-transaction.[654] That risk "is particularly problematic given that shareholders will have received their share of benefits in the early years following consummation of the transaction (assuming the transaction is approved)."[655] Fourth, the ROE penalty would not apply if Pepco were under-earning its authorized ROE by 50 basis points or more. Joint Applicants witness Crane agreed that, if Pepco is under-earning its authorized ROE by 50 basis points or more, the ROE penalty

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650 *See* Paragraph 222, *supra*.

651 Joint Applicants (4A)-2 at 3, Commitment 8.

652 Tr. at 97:21-98:22 (Crane).

653 Tr. at 1408:4-16.

654 OPC (2B) at 7:14-17 (Mara).

655 OPC (2B) at 7:17-19 (Mara).

would have no financial impact.[656] Mr. Crane also agreed that, in fact, Pepco has under-earned its authorized ROE by 50 basis points or more several times during the last five years.[657] Joint Applicants witness Rigby also conceded "our [PHI] utilities are currently under-earning fairly significantly their allowed return."[658] The Joint Applicants presented no evidence that Pepco's historical trend of under-earning its ROE would change after the Proposed Merger closes. Moreover, Joint Applicant witness Alden does not recall whether the Joint Applicants have prepared an assessment of the likelihood that they would incur a non-performance penalty under the revised commitments and revised penalty structure that the Joint Applicants now propose.[659] Thus, the ROE penalty would provide little meaningful financial incentive to meet the EQSS standards.

229. The Joint Applicants have conditioned commitments 7 and 8 on there being no changes in law, regulations, or extreme weather events requiring increases in reliability-related spending to restore service and facilities or variations in the schedule of DC PLUG that are outside Pepco's control.[660] The Commission notes that the bulk of the testimony regarding this condition centered on DC PLUG. When it adopted the EQSS, the Commission stated, "[i]f Pepco can show that its failure to meet a specific benchmark was truly a result of conditions beyond Pepco's control, then the Commission may relieve Pepco of the requirement."[661] The DC PLUG was not contemplated as being a reliability improvement undertaking that would create a set of exceptions beyond Pepco's control. Providing Pepco with another "beyond control" exception would, at best, create confusion as to the meaning of that exception within the EQSS and its meaning within the reliability commitment. More likely, the extra layer of exception would pose the risk that, post-Proposed Merger, Pepco could identify new and unexpected factors that it claims excuses slippage in reliability performance. At a minimum, such language raises questions as to the true contours and limits of the Joint Applicants' reliability commitment. The Commission does note that there has been no criteria identified by the Joint Applicants that would be used to determine when a delay in the DC PLUG construction schedule is "outside Pepco's control."[662] Moreover, a delay in the DC PLUG construction schedule has already occurred, so the offer as it was made on the record, is already voided.

230. In this public interest factor, the Commission also explores what effect the sharing of best practices will have on public safety and reliability of services. The Joint Applicants contend that "[t]he sharing of resources and best practices among the combined companies, as well as their comparable business models, ***will produce*** direct and traceable financial benefits to

656 Tr. at 104:18-105:7 (Crane).

657 Tr. at 105:8-11 (Crane).

658 Tr. at 756:1-2 (Crane).

659 Tr. at 1260:18-1262:16-22.

660 Joint Applicants (4A)-2, p. 2, Commitment 7.

661 *Formal Case Nos. 766, 982, 991, 1002*, Order No. 16427, ¶ 38, rel. July 7, 2011.

662 Tr. at 1728:3-15; Joint Applicants (4E) 4:12-14 (Gausman).

District of Columbia customers . . ."[663] They further contend that approval of the proposed transaction will enhance Pepco's reliability because "the Merger ***will*** . . . allow Pepco to leverage best practices shared across the Exelon enterprise."[664]

231. However, the record does not provide any meaningful details regarding the best practices that Exelon is offering. Nor does the record show what the effects those best practices would have on public safety and the reliability of services if they were deployed. The Joint Applicants have not identified any best practices that might be deployed after the Proposed Merger closes, have not quantified the benefits of that deployment, and have not explained why Pepco could not implement best practices on its own. In fact, during the hearing, Joint Applicant witness O'Brien maintained his position that identifying best practices and determining how they can be implemented to create value cannot be done in any meaningful way until after the transaction closes.[665] Mr. O'Brien only discussed areas where best practices "might" be targeted at Pepco following the transaction.[666] However, he left no doubt that the Joint Applicants have not yet identified, and could not possibly identify, the specific best practices that would in fact be deployed at after the Proposed Merger closes, much less determine what the reliability and other impacts of that deployment might be. Mr. O'Brien's responses to data requests also confirmed that Exelon has not yet identified any specific best practices that might be deployed at Pepco following consummation of the transaction, and has not performed any assessment of what benefits (reliability-related or otherwise) might result from implementation of such yet-to-be-identified best practices.[667] Because of these deficiencies, Joint Applicants have presented no evidence that demonstrates that the sharing of best practices will produce direct, traceable, or tangible benefits to D.C. customers.

232. The Commission acknowledges that, following the close of the Proposed Merger, Pepco will have access to more extensive Exelon utility resources for storm restoration, and together, Exelon's sister utilities form a broad regional network with the ability to dedicate and mobilize storm restoration resources, thereby reducing reliance on third-party mutual-assistance programs.[668] Joint Applicants witness Alden testified that, under utility mutual assistance agreements, there is no guarantee that other utilities will provide resources during or after a storm event, particularly when those other utilities may also be facing a large number of actual or potential outages from a large regional storm. By contrast, the Joint Applicants aver that Exelon

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663 *Formal Case No. 1119*, Joint Application at 19 (emphasis added).

664 *Formal Case No. 1119*, Joint Application at 20 (emphasis added).

665 Joint Applicants (3C) at 5:11-15 (O'Brien); Tr. at 954:8-11.

666 Joint Applicants (3C) at 6:5-8 (O'Brien).

667 *See, e.g.,* OPC Cross Examination Exhibit No. 13 (Joint Applicants' Response to OPC Data Request No. 5-39(C) and (D)). Mr. O'Brien answered multiple data requests asking which Exelon best practices would be deployed at Pepco, and the effect of such deployment, with essentially the same response that "no determination has been made at this time regarding which best practices will be implemented at Pepco following the merger." Are these in the record?

668 Joint Applicants' Br. at 80, citing Tr. at 1225:9-1226:4 (Commission Cross of Butler).

utilities are committed to making their storm restoration resources available to their affiliates on a priority basis and are able to pre-position Exelon affiliated crews before actual storm events to ensure that those crews are ready to go to work immediately.[669] According to the Joint Applicants, the post-Merger enterprise will have substantially greater combined resources to respond promptly and effectively to major storms and other emergencies.[670] The Commission does find that the Proposed Merger will provide a bigger pool of affiliated crews that could streamline the process of restoring electric service after major system damage occurs.

233. Finally, the Commission points out that the record is practically silent with regard to the Joint Applicants' commitment to safety. The Joint Applicants do state that public and workplace safety will continue to be a core value for PHI and Pepco[671] and that Exelon and PHI share a focus in prioritizing cyber security at their operating utilities.[672] The record is devoid of any details explaining or supporting these assertions.

4. FACTOR 4: The effects of the transaction on risks associated with all of the Joint Applicants' affiliated non-jurisdictional business operations, including nuclear operations

Summary of Joint Applicants' Position Pertaining to Factor No. 4

234. Noting that the Commission has held that customers must be "compensated for the risks inherent in the companies' decision to merge,"[673] the Joint Applicants assert that the Proposed Merger poses no such risk to Pepco or its customers. In fact, according to the Joint Applicants, affiliation with Exelon will reduce risks to Pepco's customers.[674] In addition, to the extent the Commission finds that there are some risks inherent in the Joint Applicants' decision to merge, the Joint Applicants assert that "any such risks will be completely eliminated by the ring-fencing measures the Joint Applicants will put in place."[675] The Joint Applicants also assert that there similarly is no risk that Pepco's District of Columbia customers will bear any of the

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669 Joint Applicants' Br. at 81, citing Joint Applicants (D) at 7:6-15 (Alden).

670 Joint Applicants' Br. at 81, citing Joint Applicants (A) at 11:1-2 (Crane); Joint Applicants (B) at 9:14-17 (Rigby).

671 Joint Applicants' Br. at 82, quoting Joint Applicants (A) at 7:17-19 (Crane) (Exelon is "committed to maintaining the highest standards of safety and reliability for our people, our customers and the communities in which we work."); Joint Applicants (B) at 3:14 (Rigby) ("we make safety the most important part of everything we do.").

672 Joint Applicants' Br. at 83.

673 Joint Applicants' Br. at 83, citing *Formal Case No. 951*, Order No. 11075, p. 18, rel. October 20, 1997.

674 Joint Applicants' Br. at 83-84. As recently as January and April 2015, the credit rating agencies have concluded that joining the Exelon family is viewed positively for Pepco. *See* Joint Applicants Confidential Cross Examination Exhibit No. 17 at 1, 3 of 7; Joint Applicants Confidential Cross Examination Exhibit No. 18 at 1, 5 of 9.

675 Joint Applicants' Br. at 84, citing Joint Applicants (4A)-2 at 5-12, Commitments 28-72.

ongoing operational or future decommissioning costs associated with Exelon's nuclear facilities.[676]

235. In support of its position, the Joint Applicants point out that Exelon is considered by investors to be no more risky than PHI and, by many measures, Exelon's operating subsidiaries are less risky than PHI's operating subsidiaries.[677] The Joint Applicants add that each of Exelon's operating subsidiaries holds a solid investment-grade rating from each rating agency.[678] The Joint Applicants cite Ms. Lapson's testimony to contend that, in assessing risk, investors consider Exelon as a whole and take into consideration many factors, including "the size and diversity" of Exelon's business mix, its "conservative financial policies with regard to maintaining relatively low leverage and prudent decisions regarding dividend policy, and the conservative stance that Exelon's management has taken with regard to its business."[679]

236. The Joint Applicants claim that since the announcement of the Proposed Merger, none of the three rating agencies – Moody's, Standard and Poor's, and Fitch – placed a negative watch on or downgraded the ratings of PHI or its utilities.[680] Instead, the Joint Applicants maintain that the rating agencies view the Proposed Merger as credit positive for Pepco, which poses no added risk of financial harm to PHI or its utilities.[681] In fact, the Joint Applicants represent that long-term issuer ratings of Exelon and PHI are identical.[682] The Joint Applicants assert that, post-merger, with the proposed ring-fencing measures in place, PHI and its utilities likely will be treated much like BGE is now.[683] In support of this assertion, the Joint Applicants state that recently Fitch upgraded BGE's credit rating to BBB+ citing ring-fencing as one of the key rating drivers for the upgrade.[684] Thus, the Joint Applicants contend that Pepco's ratings

[676] Joint Applicants' Br. at 84.

[677] Joint Applicants' Br. at 84.

[678] Joint Applicants' Br. at 84, citing Joint Applicants (3K) at 5:11-14 (Lapson), which states: "[T]here is no real difference between the long-term credit ratings of PHI and its utility subsidiaries and the long-term credit ratings of Exelon and its utility subsidiaries. In other words, the Merger will not expose Pepco or its customers to any additional financial risks."

[679] Joint Applicants' Br. at 84, citing Joint Applicants (3K) at 11:5-9 (Lapson).

[680] Joint Applicants' Br. at 84, citing Joint Applicants (2K) at 26:15-17 (Lapson).

[681] Joint Applicants' Br. at 84, citing Joint Applicants Confidential Cross Examination Exhibit No. 17 at 1, 3 of 7; Joint Applicants Confidential Cross Examination Exhibit No. 18 at 1, 5 of 9.

[682] Joint Applicants' Br. at 85, citing Joint Applicants (3K) at 7:9 (Lapson).

[683] Joint Applicants' Br. at 85, citing Joint Applicants (2K) at 26:2-6 (Lapson).

[684] Joint Applicants' Br. at 85, citing *Fitch Downgrades Exelon Generation; Upgrades BGE; Revises ComEd's Outlook to Positive,* Apr. 29, 2015, *available at* https://www.fitchratings.com/creditdesk/press_releases/detail.cfm?pr_id=983866. The Joint Applicants state "The upgrade to BGE's credit rating occurred on April 29, 2015, after the evidentiary hearing closed, and pursuant to Federal Rule of Evidence 201, Joint Applicants respectfully request that the Commission take official notice of the upgrade. In the same report, Fitch downgraded Exelon Generation to BBB, demonstrating conclusively that ring-

will not be constrained to be identical, or narrowly tied, to the ratings of Exelon or Exelon Generation.[685] Further, the Joint Applicants maintain that support for this conclusion is evidenced by the fact that, today, Exelon's utility subsidiaries are not burdened by lower credit ratings because of the business risk of Exelon; rather, BGE, PECO and ComEd "enjoy credit ratings that are either the same or slightly higher than those of Pepco, [Delmarva Power and ACE]."[686]

237. The Joint Applicants submit that, in addition to comparable credit ratings, there is other objective market-driven evidence that investors view Exelon and PHI to be similar in risk. For example, the Joint Applicants claim that Exelon's bond spreads and credit default swap ("CDS") spreads are also comparable to, and in some cases more favorable than, those of PHI.[687] Further, Joint Applicants argue that there is compelling evidence that Pepco will not be increasing its relative "riskiness" through the Proposed Merger, and confirm Ms. Lapson's conclusion that "the Merger will not expose Pepco or its customers to any additional financial risks."[688]

238. The Joint Applicants submit that neither Pepco nor its Customers will be obligated to pay for costs associated with Exelon's nuclear operations as the result of the merger. To that point, the Joint Applicants state that the Proposed Merger will not expose Pepco or its customers to additional financial risks from Exelon's nuclear generation.[689] The Joint Applicants add that Exelon Generation, a separate subsidiary of Exelon that is structurally and legally separate from Exelon and its other subsidiaries, owns Exelon's nuclear generating assets.[690] The Joint Applicants allege that hypothetically financial distress at Exelon Generation might affect the consolidated earnings of Exelon but would not otherwise have a direct effect on the rest of Exelon.[691] The Joint Applicants state that creditors of Exelon Generation would have to pierce the Exelon Generation corporate veil in order to hold Exelon responsible for the acts, errors, omissions and obligations of Exelon Generation.[692] The Joint Applicants also state that even assuming this occurs, it would not have any effect on PHI or a PHI subsidiary. The Joint Applicants conclude that a creditor of Exelon Generation seeking access to PHI's and its

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fencing measures clearly separate the credit ratings of the utility subsidiaries from that of Exelon's unregulated businesses." Joint Applicants' Br. at 85 n. 377.

685 Joint Applicants' Br. at 85, citing Joint Applicants (2K) at 26:2-6 (Lapson).

686 Joint Applicants' Br. at 85, citing Joint Applicants (3K) at 7:15-17 (Lapson) (emphasis omitted).

687 Joint Applicants' Br. at 85, citing Joint Applicants (3K) at 8:21-23 (Lapson).

688 Joint Applicants' Br. at 86, citing Joint Applicants (3K) at 5:13-14 (Lapson).

689 Joint Applicants' Br. at 95 citing Joint Applicants (3A) at 10:23-24 (Crane).

690 Joint Applicants' Br. at 95, citing Joint Applicants (3A) at 11:17-19 (Crane); Joint Applicant (3K) at 11:12-13 (Lapson).

691 Joint Applicants' Br. at 95.

692 Joint Applicants' Br. at 95.

subsidiaries' assets to satisfy an Exelon Generation obligation would have to overcome a very high hurdle to reach up from Exelon Generation, over and down through the Exelon organization to get to the assets of a PHI utility subsidiary, such as Pepco.[693] The Joint Applicants believe that such a scenario is so remote as to be fanciful.[694] Further, the Joint Applicants represent that ring-fencing measures proposed by the Joint Applicants will isolate and protect Pepco and its customers from these types of extremely unlikely liabilities.[695]

239. Moreover, the Joint Applicants assert that contrary to the arguments made by some parties and the public, the early retirement of one or more of Exelon's nuclear units would not impose material financial stress on Exelon for two reasons.[696] First, decommissioning trusts have been established for all of Exelon's nuclear units and are, with one exception, fully funded.[697] The Joint Applicants state that while Exelon monitors the decommissioning trust investments to ensure it is getting an adequate return on those investments, when the plants are to be decommissioned, there will be adequate funding to bring them to a greenfield site.[698] Second, the Joint Applicants submit that any such units, in all likelihood, would be placed in cold storage and the actual physical dismantling and decommissioning of the facilities would not happen for many years into the future during which time the funds in the decommissioning trusts would continue to grow.[699] The Joint Applicants state that, most importantly, however, under no scenario would nuclear decommissioning costs be recoverable from PHI, Pepco, or Pepco's customers.[700] Nor would any other operational costs associated with Exelon's nuclear facilities be recovered from Pepco's customers, according to the Joint Applicants.[701] In short, the operation of and/or early retirement of one or more of Exelon's nuclear facilities would not have a significant financial impact on Exelon and would not have any impact on Pepco or its customers, given Exelon Generation's separate corporate existence and the proposed ring-fencing protections.[702]

240. The Joint Applicants explain why the proposed ring-fencing measures will insulate Pepco from any perceived risk of harm resulting from the Proposed Merger.[703] The

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693 Joint Applicants' Br. at 95.

694 Joint Applicants' Br. at 95, citing Joint Applicant (3K) at 11:13-22 (Lapson).

695 Joint Applicants' Br. at 95, citing Joint Applicants (3A) at 12:13-16 (Crane).

696 Joint Applicants' Br. at 95.

697 Joint Applicants' Br. at 95-96, citing Joint Applicants (3A) 13:1-4 (Crane).

698 Joint Applicants' Br. at 96, citing Tr. at 162:14-20 (Crane Cross).

699 Joint Applicants' Br. at 96.

700 Joint Applicants' Br. at 96, citing Joint Applicants (3A) at 13:4-8 (Crane).

701 Joint Applicants' Br. at 96.

702 Joint Applicants' Br. at 96, citing Joint Applicants (3A) at 14:14-17 (Crane).

703 Joint Applicants' Br. at 86.

Joint Applicants maintain that the objective of their proposed ring-fencing measures is to eliminate the perceived risks associated with the acquisition of PHI by Exelon – namely, those associated with Exelon's non-regulated activities.[704] The Joint Applicants claim that, currently, Pepco is not protected by any ring-fencing measures and that will remain true in the absence of the Proposed Merger.[705] The Joint Applicants submit that ring-fencing measures also operate to preserve the viability of an operating subsidiary in the unlikely event of its parent corporation experiencing corporate distress or entering bankruptcy.[706] According to the Joint Applicants, Ms. Lapson's testimony supports Exelon's view that their proposed package of ring-fencing measures "represents the leading edge in utility ring-fencing, and it will become the industry standard for providing the highest degree of protection going forward,"[707] which "should give the Commission a high degree of confidence that Pepco will be protected from any adverse effects relating to affiliation with Exelon and its non-PHI affiliates."[708] The Joint Applicants state that the ring-fencing measures they propose are essentially the same as those adopted by the Maryland Public Service Commission in the Exelon-Constellation merger and that the Maryland Commission described those measures as the "gold" or even "platinum" standard in ring-fencing.[709]

241. In further support of the protection that ring fencing provides, the Joint Applicants note that ring-fencing is widely used in banking, real estate, leasing and the financial services industries and there is vast experience in the financial marketplace and bankruptcy practice with ring-fencing protections.[710] For example, the Joint Applicants point out that due to effective ring-fencing measures put in place at Portland General Electric Company when Enron Corporation acquired the utility, Portland General avoided harm and was not a party to its

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[704] Joint Applicants' Br. at 86 n. 385, where the Joint Applicants also submit that by ring-fencing PHI, the Joint Applicants have taken concrete steps to ensure investors will view PHI and its utility subsidiaries, including Pepco, on a stand-alone basis in the unlikely event of financial or operational distress at Exelon or any of its non-PHI affiliates.

[705] Joint Applicants' Br. at 86-87, citing Tr. at 722:22-723:3 (Rigby Cross) ("I wouldn't anticipate that Pepco or PHI on a stand-alone would introduce ring-fencing unless, for some reason, we decided to get back into non-regulated generation.").

[706] Joint Applicants' Br. at 87, citing Joint Applicants (2K) at 5:14-16 (Lapson). As Ms. Lapson explained, a utility that is ring-fenced from its parent is more likely to retain debt ratings based on its individual credit condition, thereby avoiding a downgrade to the same rating as its weaker parent or affiliates. Joint Applicants (2K) at 10:4-7 (Lapson).

[707] Joint Applicants' Br. at 87, citing Joint Applicants (4K) at 3:7-9 (Lapson).

[708] Joint Applicants' Br. at 87, citing Joint Applicants (4K) at 3:12-14 (Lapson).

[709] Joint Applicants' Br. at 87, citing AOBA Cross Examination Exhibit No. 11 at 84-85 of 122.

[710] Joint Applicants' Br. at 88, citing Joint Applicants (2K) at 4:17-5:12 (Lapson).

parent's bankruptcy.[711] In the Joint Applicant's view, the ring-fencing measures they propose "are far in excess of the measures that existed at Portland General Electric."[712]

242. The Joint Applicants' contend that their ring-fencing commitments are comprehensive, detailed, specific, and transparent.[713] They also contend that, while it is plausible that one could suggest other additional or different ring-fencing conditions, or variations upon these conditions, such additional conditions would not afford Pepco or its customers any additional protections.[714] Most importantly, the Joint Applicants state that their proposed ring-fencing commitments will maintain the stand-alone financial condition and the business and financial viability of PHI and Pepco post-Merger.[715] The Joint Applicants also state that their measures include, among others: the creation of a bankruptcy-remote SPE, restrictions on PHI's ability to issue additional long-term debt, prohibitions on the payment of dividends that would cause Pepco's common equity to fall below 48%, and the transfer of most of PHI's non-regulated subsidiaries to Exelon or an Exelon affiliate so that they will be outside the PHI ring-fence.[716] The Joint Applicants add that they will ensure that Pepco and its customers are protected from financial harm as a result of the Proposed Merger by, among other things, not applying "push-down" purchase accounting to PHI's and Pepco's books, and ensuring no goodwill or other fair value adjustments will be recorded at Pepco post-Merger.[717]

243. The Joint Applicants submit that their ring-fencing (and corporate governance) measures will continue indefinitely unless and until the Joint Applicants petition the Commission for a change to identified measures and the Commission approves the requested change.[718] The Joint Applicants claim that it is important to recognize that they in all likelihood would not be petitioning for the removal of all ring-fencing measures.[719] The Joint Applicants also claim that the utility industry is rapidly changing, and some of the Joint Applicants' ring-fencing

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711 Joint Applicants' Br. at 88, citing Joint Applicants (2K) at 7:1-6 (Lapson).

712 Joint Applicants' Br. at 88-89, citing Tr. at 2642:14-16 (Commission Cross of Lapson).

713 Joint Applicants' Br. at 89.

714 Joint Applicants' Br. at 89.

715 Joint Applicants' Br. at 89, citing Joint Applicants (2K) at 25:7-9 (Lapson). In addition, as Ms. Lapson confirmed, the Joint Applicants' proposed ring-fencing measures include all of the elements of the ring-fencing measures that protected Portland General from consolidation in the bankruptcy of its parent Enron Corporation; indeed there are more and stronger commitments here. Tr. at 2644:9-18 (Commission Cross of Lapson).

716 Joint Applicants' Br. at 89.

717 Joint Applicants (4A)-2 at 1, Commitments 1 and 2.

718 Joint Applicants' Br. at 92, citing Joint Applicants (4A)-2 at 11-12, Commitment 72. Notably, this is not an all or nothing proposition. Rather, this commitment simply permits the Joint Applicants, after having had time to evaluate the necessity and usefulness of the ring-fencing measures, to determine whether a particular measure or measures may no longer be needed.

719 Joint Applicants' Br. at 92.

commitments may prove to be unnecessary for the protection of Pepco and its customers.[720] The Joint Applicants assert that this commitment allows the Joint Applicants to petition the Commission to remove or alter a particular provision or provisions – after a period of five years has passed.[721]

244. Finally, the Joint Applicants submit that Pepco and its customers will benefit from the Joint Applicants' ring-fencing measures.[722] To be more specific, the Joint Applicants state that in addition to preventing harm, some of the proposed ring-fencing commitments will provide Pepco and its customers with an affirmative benefit. For instance, not only will the Joint Applicants' proposed ring-fencing measures protect Pepco and its customers from any risks associated with Exelon's non-regulated businesses, they will remove a risk that Pepco faces today with respect to PHI's non-regulated business.[723] As Joint Applicants witness Mr. Khouzami explained:

> [T]he ring-fencing provisions are put in place to ensure that the non-regulated operations of Exelon would not cause harm to any of the customers of any of the PHI utilities.
>
> The ring-fencing structure we've put in place is at the PHI entity level, includes the three PHI utilities. It takes out what is currently, under PHI, the non-regulated businesses; it takes that and moves it to the non-regulated side of Exelon.
>
> So, in fact, the ring-fencing provisions . . . protect PEPCO D.C. customers even more so than what PHI has today, given that it has exposure to non-reg[ulated] operations underneath their structure now.[724]

In sum, the Joint Applicants represent that following the Proposed Merger, Pepco will be protected by some of the industry's leading, and most stringent, ring-fencing measures, which do not currently exist at Pepco today.[725]

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[720] Joint Applicants' Br. at 92.

[721] Joint Applicants' Br. at 92, citing Tr. at 2489:9-20 (Lapson Rejoinder).

[722] Joint Applicants' Br. at 94.

[723] Joint Applicants' Br. at 94 citing Joint Applicants (4A)-2 at 9, Commitment 57 ("PHI subsidiaries, other than PHISCo and the PHI utilities, that are currently engaged in operations that are not regulated by a state or local utility regulatory authority will be transferred to Exelon or an Exelon affiliate; . . . .").

[724] Joint Applicants' Br. at 94, citing Tr. at 2045:18-2046:10 (Khouzami Cross).

[725] Joint Applicants' Br. at 95.

Summary of OPC and Intervenors' Position Pertaining to Factor No. 4

245. OPC argues that the Commission should find that the proposed transaction poses risks to Pepco and its District of Columbia customers associated with all of the Joint Applicants affiliated non-jurisdictional business operations, including its nuclear operations and urges the Commission to conclude that "even if some of these risks are subject to mitigation, there is no incremental benefit inherent in such mitigation measures."[726] According to OPC, its witness, Dr. Woolridge, evaluated the proposed transaction with a focus on three distinct areas: (1) the capital markets perceptions of Exelon's proposed acquisition of PHI; (2) the relative riskiness of Exelon and PHI, and how these risks are viewed in the combined Exelon-PHI entity; and (3) the ring-fencing measures and financial commitments proposed by the Joint Applicants in light of this relative riskiness.[727] OPC states that Dr. Wooldridge's analysis was driven and measured by the prevailing standard which must be satisfied in order for a transaction to be approved, *i.e.*, that the transaction "must produce a direct and traceable financial benefit to ratepayers" and, "any savings that result must be shared with ratepayers, and be shared in such a proportion that ratepayers are compensated for the risks inherent in the companies' decision to merge."[728] OPC concludes that the Joint Applicants are unable to satisfy this standard, as the proposed transaction would expose ratepayers to more risk than would otherwise be present absent the transaction.[729]

246. **AOBA.** AOBA asserts that Exelon's substantial investment in nuclear generation and competitive energy markets engender a level of risk not found in regulated distribution utility operations. AOBA states that a number of issues have been raised in this proceeding with regard to the risks associated with Exelon's nuclear operations.[730] In that vein, AOBA stresses that Exelon owns the largest fleet of nuclear generation units in the U.S., and the ownership and operation of that fleet involves several elements of risk not found in electric distribution utility operations and to which electric distribution utilities would not otherwise be exposed.[731] For example, AOBA claims that Exelon has had to abandon plans to up-rate four nuclear facilities due to changing market conditions, and those abandoned projects have led to significant cost write-offs.[732] AOBA also claims that Exelon incurred losses in excess of $100 million in 2013 associated with its Clinton nuclear power station in Illinois.[733] AOBA notes that Exelon only has partial nuclear insurance and is required to self-insure if losses exceed the insured amount and is also exposed to risk on portions of claims that fall within insurance policy deductible amounts.[734]

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726 OPC R.Br. at Appendix B, Paragraph 48 at B-11.

727 OPC's Br. at 107.

728 OPC's Br. at 107, citing *Formal Case No.* 951, Order No. 11075, p. 18, rel. October 20, 1997.

729 OPC's Br. at 107.

730 AOBA's Br. at 46.

731 AOBA's Br. at 46.

732 AOBA's Br. at 46-47, citing Tr. at 180-183 (Lapson).

733 AOBA's Br. at 47, citing Tr. at 183 (Lapson).

AOBA contends that Joint Applicants witness Crane acknowledges that such losses could have a material adverse impact on Exelon's financial condition.[735]

247. AOBA argues that Exelon is further exposed to the potential that Électricité de France ("EDF"), a 49.99% owner of the Constellation Energy Nuclear Group ("CENG"), may exercise a "put option" within the next several years that would require Exelon to purchase EDF's share of CENG ownership. AOBA asserts that the large amounts of capital that would be required to support such a transaction could place considerable strain on Exelon's financial resources and limit Exelon's ability to provide needed equity support for Pepco's aggressive capital spending plans.[736] Thus, AOBA submits that if the proposed transaction is approved, ring-fencing of their operations from Exelon's more risky nuclear generation and energy marketing activities is a necessity both for protection against possible bankruptcy by Exelon, a much more diverse parent company, and for protection against potential adverse impacts that Exelon's non-regulated activities may have on Pepco's credit ratings and costs of debt if not properly ring-fenced.[737]

248. AOBA states further that the assessment of the relative risks of distribution utility operations and the risks of Exelon's more diverse utility holding company operations is eminently apparent in S&P evaluations of utility credit risk for Exelon's current utility subsidiaries, as well as its evaluations of numerous other utilities.[738] With regard to the issue of Credit Risk, AOBA states that as demonstrated through AOBA's cross-examination of Joint Applicants witness Lapson, S&P notes that the credit ratings of ComEd and PECO are limited to the lower of their stand-alone credit quality or that for their parent Exelon "where Exelon's credit quality is affected by its non-regulated generation and retail business that are directly affected by low power prices."[739] However, S&P's assessments for ComEd and PECO contrast with its post-Merger assessment of BGE's credit. S&P's assessment of BGE states:

> We base the company's rating on its stand-alone credit quality and we rate the company one notch higher than its parent, Exelon Corp. due to the insulation measures the company has implemented and maintained.[740]

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[734] AOBA's Br. at 47.

[735] AOBA's Br. at 47, citing Tr. at 184-185.

[736] AOBA's Br. at 47.

[737] AOBA's Br. at 47.

[738] AOBA's Br. at 43, citing AOBA Cross Examination Exhibit No. 99, (S&P report) pages 13, 27, 11; Tr. at 2537–2539.

[739] AOBA's Br. at 44, citing Tr. at 2537 to 2538.

[740] AOBA's Br. at 44, citing Tr. at 2538.

249. AOBA submits that the difference in these credit assessments is indicative of the influence of the more well-devised ring-fencing arrangement adopted for BGE.[741] AOBA further submits that the S&P assessments of credit ratings for Exelon's utility subsidiaries provide strong evidence that ring-fencing measures are necessary and meaningful. Moreover, AOBA argues that a well-devised ring-fencing arrangement does more than just protect the ring-fenced entities from a bankruptcy of the parent company.[742] AOBA adds that a well-devised ring fencing arrangement can also serve to lower a utility's cost of debt by enabling rating agencies, such as S&P, to assign a higher credit rating to a distribution utility subsidiary than it assigns to a parent company engaged in more risky generation and/or energy marketing activities.[743] For example, AOBA points out that S&P credit assessments for each of FirstEnergy's utility subsidiaries include the statement, "[t]he utility's ratings continue to be affected by FirstEnergy's nonrated-regulated generation and retail business that are materially pressured by the low price of electricity."[744]

250. AOBA further asserts that a similar statement is found in S&P's assessment of Public Service Electric and Gas Company ("PSE&G") even though Public Service is part of a wholly separate holding company. For PSE&G the S&P report states, "[t]he utility's ratings continue to be affected by its parent's nonrated-regulated generation business that is directly affected by the low price of electricity."[745] AOBA represents that the S&P utility credit assessments also offer explicit recognition of the comparatively low risk nature of distribution utility operations.[746] For example, in its assessment of Massachusetts Electric Company, S&P states, "[t]he Company has an excellent business risk profile, reflecting relatively low operating risk of electric distribution operations."[747] Likewise, AOBA points out that S&P offers the following assessment of Potomac Edison Company:

> Despite Potomac's 'excellent' business risk profile - reflecting its low risk, rate regulated distribution electric utility - credit quality is

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[741] AOBA's Br. at 44.

[742] AOBA's Br. at 44.

[743] AOBA's Br. at 44.

[744] AOBA's Br. at 45, citing the statement regarding credit assessments that the First Energy utility subsidiaries specifically addressed in the S&P report and the page of the S&P report (AOBA Cross Examination Exhibit No. 99) on which each utility is addressed, including: Cleveland Electric Illuminating Co. (page 13 of 42); Jersey Central Power & Light Company (page 20 of 42); Metropolitan Edison Company (page 22 of 42); Monongahela Power Company (page 23 of 42); Ohio Edison Company (page 26 of 42); Pennsylvania Electric Company (page 28 of 42); Pennsylvania Power Company (page 28 of 42); Toledo Edison Company (page 35 of 42); and West Penn Power Company (page 36 of 42).

[745] AOBA's Br. at 45, citing AOBA Cross Examination Exhibit No. 99, page 28 of 42.

[746] AOBA's Br. at 45.

[747] AOBA's Br. at 45, citing AOBA Cross Examination Exhibit No. 99, page 22 of 42.

> pressured by FirstEnergy's merchant businesses that continue to be pressured by low-electricity prices.[748]

251. As illustrated by the credit assessments offered for numerous utilities in the referenced S&P report, AOBA submits that in the absence of well-developed ring-fencing arrangements, the credit ratings of utility subsidiaries are frequently constrained by the parent company's credit.[749] According to AOBA, S&P assessments also contrast with Joint Applicants witness Lapson's Rebuttal Testimony in which she asserts: "There is no real difference between the long-term credit ratings of PHI and its utility subsidiaries and the long-term credit ratings of Exelon and Exelon's utility operating subsidiaries."[750] AOBA argues that Ms. Lapson's observation appears to represent a point in time observation regarding relative credit ratings.[751] However, during cross-examination by counsel for AOBA, Joint Applicants witness Lapson agreed that although Exelon and PHI may have similar credit ratings at a point in time, that is not necessarily a sound basis for a conclusion that their credit ratings will remain similar over time.[752] AOBA argues that an effective ring-fencing arrangement must address the potential that credit rating differences that could adversely affect customers of the PHI utilities, and more specifically Pepco customers in the District of Columbia, may occur in the future even if they do not exist at a given point in time.[753]

252. **District Government.** The District Government takes the position that, in light of the fact that the PHI operating utilities divested their generation assets years ago, any Proposed Merger that involved re-affiliating with generating assets would create additional risk.[754] The District Government also submits that District witnesses Dr. Wilson and Mr. Chang highlight the potential risks imposed on District of Columbia retail electricity consumers by Exelon's exposure from various aspects of its nuclear fleet.[755] The District Government asserts that Exelon itself acknowledges the economic difficulties presently associated with at least some of its nuclear assets.[756]

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[748] AOBA's Br. at 45 citing AOBA Cross Examination Exhibit No. 99, page 29 of 42.

[749] AOBA's Br. at 45-46.

[750] AOBA's Br. at 46, citing Joint Applicants (3K) at 5:10-13 (Lapson).

[751] AOBA's Br. at 46.

[752] AOBA's Br. at 46, citing Tr. at 2523:8-17.

[753] AOBA's Br. at 46.

[754] District Government's Br. at 35.

[755] District Government's Br. at 35; District Government Confidential Cross Examination Exhibit No. 17 (Confidential Joint Applicants' Response to DC SUN 5-7) at Attachment A, slide 15 "Combined Asset Value for Exelon's Generating Fleet".

[756] District Government's Br. at 35.

253. The District Government states that, as a result of some convergence of understanding about the economic risks associated with merchant generation generally, and merchant nuclear generation in particular, the issues under this Factor narrows to the question of what ring-fencing conditions are necessary and appropriate to insulate the District of Columbia's retail electricity consumers from those economic risks.[757] Even more specifically, the District Government submits that the debate between the Joint Applicants and the District appears to have narrowed to three issues: (1) whether the SPE that is integral to ring-fencing arrangements should reside at the holding company level or the operating company level; (2) whether a five-year or a ten-year "stay out" period (*i.e.*, ban on the merged company seeking modification or elimination of ring-fencing conditions, which otherwise remain subject to modification by the Commission on its own motion or at the request of a Joint Applicant) is appropriate; and (3) what showing ought to be required in order to obtain modification or other relief.[758]

254. As District Government witness Wilson explains, the District believes that effective ring-fencing requires the following.[759] First, the SPE should be lodged at the operating company level (Pepco), rather than at the holding company level (PHI).[760] Second, the District Government contends that a ten-year stay out period is more appropriate to consumer protection and the magnitude of the potential harm sought to be avoided by ring-fencing.[761] Finally, the merged company seeking relief from ring-fencing conditions should be required to show why changed circumstances have made modification or elimination of a ring fencing condition necessary in order to create or preserve a substantial benefit for District of Columbia customers.[762]

255. **DC Water.** DC Water comments briefly on Factor No. 4 stating: (1) all parties have acknowledged the need for the Commission to put in place ring fencing measures should it decide to approve the merger;[763] (2) in light of the financial and business risk differences, strong ring-fencing measures should be adopted to mitigate against the potential for harm to District ratepayers;[764] and (3) now that the Joint Applicants will adopt the ring-fencing measures set forth in Exhibit Joint Applicants (4A)-2; not seek to change the ring-fencing measures prior to 5 years after the merger closes; and make no changes in the ring-fencing measures unless and until the Commission makes a finding in a formal proceeding that such changes will not result in any

[757] District Government's Br. at 35-36.

[758] District Government's Br. at 36.

[759] District Government's Br. at 36, citing District Government (2F) at 15:1-17:18 (Wilson).

[760] District Government's Br. at 36

[761] District Government's Br. at 36.

[762] District Government's Br. at 36.

[763] DC Water Br. at 24-25.

[764] DC Water Br. at 26.

harm to ratepayers, DC Water does not oppose the Joint Applicants' ring fencing measures.[765] Further, DC Water states:

> Ring-fencing measures are useful tools for ensuring against certain risks, such as Pepco being affected by the bankruptcy of its parent corporate or an affiliate. Ring fencing measures do not, however, ensure that Pepco's customers will affirmatively benefit from the proposed transaction. OPC (D) at 24 (Woolridge). Nor do they guarantee that Pepco will be perceived by financial markets and ratings agencies as the same low risk transmission and distribution utility it is today. Thus, ring fencing does not eliminate all risks associated with the merger for ratepayers.[766]

Summary of Community Comments Pertaining to Factor No. 4

256. The Commission also received comments from members of the public concerning the risks posed by the Proposed Merger as a result of Exelon's ownership of nuclear plants. Some residents expressed concern that the Proposed Merger will result in increased rates for ratepayers to support Exelon's aging nuclear plants. Other commenters feared that District ratepayers would be forced to subsidize the losses incurred by Exelon if it had to close or repairs its aging nuclear plants and losses being experienced as customers move to lower cost renewable energy sources and away from uncompetitive merchant nuclear plants. Some expressed the concern that "acquiring PEPCO is one of [Exelon's] schemes to fix" the problem with its aging nuclear facilities.

Discussion Pertaining to Factor No. 4

257. Public Interest Factor No. 4 requires the Commission to assess the impact of the proposed transaction on risks associated with all of the Joint Applicants' affiliated non-jurisdictional business operations, including nuclear operations. Certain facts about Exelon are not in dispute. It is well known that Exelon owns the largest fleet of nuclear generation units in the United States.[767] Additionally, in the record, Exelon itself acknowledges there are economic difficulties presently associated with some of its nuclear assets.[768] Specifically, Exelon has had to abandon plans to upgrade four nuclear facilities due to changing market conditions, and those abandoned projects have led to significant cost write-offs.[769] Moreover, Exelon incurred losses

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765 DC Water Br. at 26.

766 DC Water Br. at 25 n. 36.

767 AOBA (A) at 71-72 (Oliver).

768 Tr. at 307:13-313:11,399:21-403:14 (Crane); District Government Confidential Cross Examination Exhibit No. 17 (Confidential Joint Applicants' Response to DC SUN 5-7) at Attachment A, slide 15 "Combined Asset Value for Exelon's Generating Fleet".

769 Tr. at 180 to 183 (Crane).

in excess of $100 million in 2013 associated with its Clinton Nuclear Power Station in Illinois.[770] Finally, it was revealed that Exelon only has partial nuclear insurance and is required to self-insure if losses exceed the insured amount as well as pay any portions of claims that fall within insurance policy deductible amounts.[771] Joint Applicants witness Crane acknowledges that such loses could have a material adverse impact on Exelon's financial condition.[772] Exelon is also responsible for decommissioning costs when any of its nuclear units are retired. Joint Applicants witness Crane stated that the decommissioning funds for all of these plants are fully funded, with one exception.[773] At issue as we consider Factor No. 4 is how Exelon's ownership of these additional business interests, especially the ownership of nuclear operations, would impact the proposed acquisition, Pepco, and by extension, District ratepayers. We begin by addressing and dispensing with a concern that was frequently raised by community commenters, *i.e.*, that Pepco, at the direction of Exelon will attempt to recover in the rates of District ratepayers the costs associated with its aging nuclear fleet. While this was an issue for the Commission in *Formal Case No. 951* when we were considering the proposed merger between Pepco and BGE as two vertically integrated companies where BGE owned a nuclear plant, the costs and assets of which could potentially be incorporated into the new company's cost of service and rate base, it is not a major issue here. Under the existing restructured electricity market, our current ratemaking procedures do not consider inclusion of any costs from generating plants in the cost of service or the rate base of the local distribution company. In any event, Exelon's nuclear generating assets are owned by Exelon Generation, an Exelon subsidiary that is structurally and legally separate from Exelon and its other subsidiaries.[774]

258. There are still two ways that District ratepayers could be financially harmed by Exelon's ownership of these generation assets. First, as we noted in our discussion of Factor No. 2, *supra*, and in our discussion of Factor No. 5, *infra*, under the proposed transaction, PHI and its subsidiaries, including Pepco, will share some of the costs for the work provided by the EBSC to other Exelon entities, including Exelon Generation. If the Proposed Merger were consummated, the Commission would direct the Joint Applicants to put in place protective measures to ensure that Exelon Generation or another Exelon subsidiary properly allocates all service costs from the EBSC so as to prevent District ratepayers from incurring unrelated service costs.

259. Second, District ratepayers could be impacted if the cost of capital available to Pepco, as a subsidiary of Exelon, is higher because of Exelon's ownership of non-jurisdictional business operations in general and nuclear operations in particular. As we were urged to do by all parties, the Commission has reviewed the record evidence addressing how credit rating agencies in general assess the risks of a parent company's non-jurisdictional business operations and the impacts of any such risk on a subsidiary electric distribution company; how credit rating

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[770] Tr. at 183 (Crane).

[771] Tr. at 184 to 185 (Crane).

[772] Tr. at 184 to 185 (Crane).

[773] Tr. at 315.

[774] Joint Applicants (3A) at 11:17-19 (Crane); Joint Applicant (3K) at 11:12-13 (Lapson).

agencies have assessed the risks of Exelon in particular especially in light of its large fleet of nuclear generation units; and how any perceived risk has or would impact an electric distribution subsidiary. That evidence shows that credit agencies may take into account the business operations of an electric distribution company's parent and any steps that have been taken to protect a subsidiary company from any added risks from a parent's operations.

260. AOBA cited several examples where S&P conducted such an analysis. AOBA noted that the S&P assessment for each of the First Energy subsidiaries[775] include the statement "[t]he utility's ratings continue to be affected by FirstEnergy's nonrated-regulated generation and retail business that are materially pressured by the low price of electricity."[776] AOBA noted that a similar statement is found in S&P's assessment of PSE&G even though Public Service is part of a wholly separate holding company. Concerning PSE&G, the S&P report states, "[t]he utility's ratings continue to be affected by its parent's nonrated-regulated generation business that is directly affected by the low price of electricity." [777] Yet another example is in S&P's assessment of Potomac Edison Company:

> Despite Potomac's 'excellent' business risk profile – reflecting its low risk, rate regulated distribution electric utility – credit quality is pressured by FirstEnergy's merchant businesses that continue to be pressured by low electricity prices.[778]

261. AOBA then focused the Commission's attention on an S&P discussion that compared the credit ratings of ComEd and PECO with its assessment of BGE after the Exelon-Constellation merger. That discussion noted ComEd and PECO are limited to the lower of their stand-alone credit quality or that for their parent Exelon, "where Exelon's credit quality is affected by its non-regulated generation and retail business that are directly affected by low power prices."[779] By contrast, S&P's assessment of BGE states:

> We base the company's rating on its stand-alone credit quality and we rate the company one notch higher than its parent, Exelon Corp. due to the insulation measures the company has implemented and maintained.[780]

262. AOBA submits that the difference in these credit assessments is indicative of the influence of the more well-devised ring-fencing arrangement adopted for BGE as a condition of

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[775] *See* footnote 746, *supra*.

[776] AOBA Cross Examination Exhibit No. 99, page 28 of 42.

[777] AOBA Cross Examination Exhibit No. 99, page 28 of 42.

[778] AOBA Cross Examination Exhibit No. 99, page 29 of 42.

[779] AOBA's Br. at 44, citing Tr. at 2537 to 2538.

[780] AOBA's Br. at 44, citing Tr. at 2538.

the Exelon-Constellation Merger;[781] and argues that the S&P assessments of credit ratings for Exelon's utility subsidiaries provide strong evidence that ring-fencing measures are necessary and meaningful. Moreover, AOBA argues that a well-devised ring-fencing arrangement does more than just protect the ring-fenced entities from a bankruptcy of the parent company.[782] AOBA adds that a well-devised ring fencing arrangement can also serve to lower a utility's cost of debt by enabling rating agencies, such as S&P, to assign a higher credit rating to a distribution utility subsidiary than it assigns to a parent company engaged in more risky generation and/or energy marketing activities.[783]

263. Another important area of consideration under Factor No. 4 is the ring-fencing measures the Joint Applicants have proposed to safeguard Pepco post-Merger from any perceived risk of harm resulting from the merger. OPC,[784] AOBA,[785] District Government,[786] and DC Water[787] have also indicated that appropriate ring-fencing measures are primarily meant to maintain the status quo and will provide the protection necessary against perceived risks of harm resulting from the merger. These parties argue that the ring-fencing measures will not produce benefits for ratepayers. Indeed, but for the Proposed Merger, the ring-fencing measures proposed by the Joint Applicants would be unnecessary. In any event, the purpose of implementing ring-fencing measures is to prevent harm, not to produce a benefit. Ring-fencing measures operate to preserve the viability of an operating subsidiary in the unlikely event of its parent corporation experiencing corporate distress or entering bankruptcy.[788] The Joint Applicants' proposed package of ring-fencing measures represents the leading edge in utility ring-fencing.[789] While some parties have suggested additional or different ring-fencing conditions, including those that would extend the length of time that the provisions are in place and provide for Pepco to be spun off from Exelon in the event that the ring fencing provisions are triggered, we acknowledge, as argued by Grid2.0 that ring-fencing does not protect against all risks.[790]

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781 AOBA's Br. at 44.

782 AOBA's Br. at 44.

783 AOBA's Br. at 44.

784 OPC's Br. at 109-110.

785 AOBA's Br. at 43-47.

786 District Government's Br. at 36.

787 DC Water's Br. at 24-26.

788 Joint Applicants' (2K) at 5:14-16 (Lapson).

789 Joint Applicants' (4K) at 3:7-9 (Lapson).

790 GRID2.0 (A) at 89 (Hempling). Those risks were listed by GRID2.0 as follows: (i.) the possibility that Exelon's acquisition of Pepco will reduce Pepco's access to equity capital (GRID2.0 (A) at 90-91(Hempling)); (ii.) potential increases in Pepco's cost of capital due to affiliation with Exelon; (GRID2.0 (A) at 92-94(Hempling)); (iii.) the risk that Exelon's' business failures could push Pepco into bankruptcy; (GRID2.0 (A) at 95-97 (Hempling)); (iv.) ring-fencing does not prevent Exelon from controlling or otherwise interfering with Pepco's activities in carrying out

264. While the ring-fencing provisions that were initially offered by the Joint Applicants in this proceeding were robust, they have been further strengthened by modifications made in subsequent settlements with the New Jersey Board of Public Utilities as well as settlements reached with the Delaware Public Service Commission and the Maryland Public Service Commission because of the Joint Applicants' offer of most-favored nation status to the District.[791] Indeed, in the Joint Applicants' list of its final commitments for this Proposed Merger, 43 of the 91 commitments relate to their ring-fencing commitments.[792] The Joint Applicants' ring-fencing commitments shield Pepco and protect District ratepayers include but are not limited to the following: 1) Pepco will maintain its separate existence as a separate corporate subsidiary and its separate franchises, obligations and privileges; 2) Pepco will maintain separate books and records; and 3) Pepco will not incur or assume any debt, including the provision of guarantees or collateral support, related to this Proposed Merger or any future Exelon acquisition.[793]

265. Based on the record of this proceeding, the Commission concludes that Exelon's ownership of additional non-jurisdictional business interests in general and its ownership of nuclear operations in particular, will have an impact on Pepco and could have an impact on District ratepayers, if the Proposed Merger is approved. The Commission recognizes the concern that District ratepayers could potentially be financially harmed as a result of Exelon's non-utility holdings, especially its nuclear operations. While some have urged us to consider the mere presence of the Joint Applicants' unregulated business to be a harm that cannot be mitigated, the Commission declines to do so. The Commission concludes that there is no way that losses incurred by Exelon's aging nuclear fleet would be included in the rate base of Pepco as a local distribution company. The Commission recognizes, however, that there is a possibility that Pepco's cost of capital could be affected if there were no ring-fencing provisions to assure investors that the finances of Pepco and PHI were separate from the obligations of Exelon. The Commission accepts the fact that the Joint Applicants' multiple commitments to implement numerous ring-fencing provisions would insulate Pepco and PHI from most, if not all, of the business risks associated with Exelon's non-regulated businesses and would provide a level of protection to District ratepayers in the event that Exelon's finances are placed in jeopardy by events that impact its unregulated businesses. For those reasons, we have concluded that District ratepayers and Pepco could be protected from any harmful effects of the Proposed Merger in the face of Exelon's unregulated business. At the same time, we see no added benefit that inures to District ratepayers or the District from Exelon's other businesses.

266. Whether additional provisions are necessary for the proposed ring-fencing commitments to provide additional protections to District ratepayers as urged by the Intervenors and some community commenters as additional terms or conditions to the approval of the

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its public service obligations; (GRID2.0 (A) at 97-98 (Hempling)); and (v.) does not ensure arm's-length relationships between Pepco and Exelon's many affiliates (GRID2.0 (A) at 98-104 (Hempling)).

791 *See also* Tr. at 70:14-71:1; Tr. at 108:18-21; Tr. at 136-138; Tr. at 139:22-140:20; Tr. at 141:1-5.

792 *See* Joint Applicants (4A)-2 at 4-12, Commitments 24-72.

793 *See* Joint Applicants (4A)-2 at 5, Commitments 28-30.

Proposed Merger is a decision that the Commission will defer until we have examined the remaining Public Interest Factors and made a determination of whether the Proposed Merger, taken as a whole, is in the public interest.

5. FACTOR 5: The effects of the transaction on the Commission's ability to regulate the new utility effectively

Summary of Joint Applicants' Position Pertaining to Factor No. 5

267. The Joint Applicants state that "[they] have made several commitments to ensure, following the Merger, PHI and Pepco retain local control over decisions impacting the District" and that "the Joint Applicants have structured the transaction so that the Commission will retain the same level of oversight and regulatory authority over Pepco, and the entities, such as service companies, which supply services to Pepco, as it has today."[794] The Joint Applicants state such oversight "includes access to and oversight of the individuals making decisions that impact Pepco's District of Columbia customers."[795] The Joint Applicants also state, "Exelon has submitted to the jurisdiction of the Commission for all matters related to the Merger and the enforcement of the commitments . . . and all matters relating to affiliate transactions between Pepco and Exelon or its affiliates."[796]

268. The Joint Applicants explain that PHISCo is the entity that currently provides business services to PHI's subsidiary utilities. Post-Merger, PHISCo will remain a subsidiary of PHI and will continue to perform functions and maintain assets for PHI's utilities.[797] They go on to explain that "[o]ther functions currently provided by PHI Service Company that will be available to other Exelon subsidiaries in addition to the PHI utilities will be transferred to and consolidated under the [EBSC]."[798] They explain:

> EBSC is Exelon's PHISCo counterpart, an organization that houses specific support functions for provision to the affiliates under Exelon's corporate umbrella, "designed to provide a range of what would typically be regarded as in-house services in the case of a stand-alone utility." EBSC is subject to the rules and regulations of the Federal Energy Regulatory Commission (FERC), and complies with the individual state regulatory commission requirements related to associate transactions in the jurisdictions in which Exelon's utilities operate. EBSC services

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[794] Joint Applicants' Br. at 96-97.

[795] Joint Applicants' Br. at 97, referencing Joint Applicants (A) at 27:7-12 (Crane); Tr. at 1080:8-16 (O'Brien).

[796] Joint Applicants' Br. at 97, citing Joint Applicants (4A)-2 at 14, Commitment 73.

[797] Joint Applicants' Br. at 97, citing Joint Applicants (F) at 30:16-20 (Khouzami); Joint Applicants (3F) at 24:10-15 (Khouzami).

[798] Joint Applicants' Br. at 97, citing Joint Applicants (4A)-2 at 9, Commitment 56.

> include information technology, supply, finance, human resources, government and environmental affairs and public policy, general counsel and legal services, corporate secretary services, and communications.[799]

The Joint Applicants state, "[c]urrently, EBSC provides these services to Exelon's utility operating subsidiaries: PECO, ComEd and BGE. This structure allows Exelon's utilities 'to realize economies of scale and scope that could be very difficult to achieve on an individual-company basis."[800]

269. The Joint Applicants further state that following the close of the Proposed Merger, "[u]nder the terms of Exelon's existing General Services Agreement ("GSA") . . . PHI and Pepco will have the discretion to determine whether and to what extent they will utilize EBSC's services, with the exception of corporate governance services that EBSC provides to each party to the GSA."[801] The Joint Applicants commit that "[s]ervices furnished by EBSC to Pepco will be billed at EBSC costs, with direct charges of those costs made wherever possible."[802] According to the Joint Applicants, "EBSC directly bills approximately 70% of its costs . . . [and i]f direct billing of costs is not possible, EBSC's costs will be allocated through the FERC–approved Modified Massachusetts allocation method identified in EBSC's Associate Transaction Procedures Manual."[803]

270. Finally, the Joint Applicants commit that Commission Staff and OPC "shall be assured reasonable and convenient access to the books and records of EBSC."[804] The Joint Applicants reference Mr. Khouzami's testimony and state, "the Commission will have the same access to EBSC's books and records as it currently has with PHISCo to ensure that there is no change in the transparency of the operation of the entity providing Pepco with services."[805] The Joint Applicants assert, "[t]his is consistent with the Commission's requirement in Formal Case No. 951 that the Commission retain access to books, accounts, records and papers in connection with its supervision of Pepco."[806] The Joint Applicants make the following two additional commitments:

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799 Joint Applicants' Br. at 97-98, citing Joint Applicants (F) at 29:10-15 (Khouzami); Joint Applicants (F)-3 at 2.

800 Joint Applicants' Br. at 98, citing Joint Applicants (F) at 29:18-21 (Khouzami).

801 Joint Applicants' Br. at 98, citing Joint Applicants (F)-3 at pp. 8-26; Joint Applicants (F) at 30:1-4 (Khouzami).

802 Joint Applicants' Br. at 98, citing Joint Applicants (F) at 30:6-8 (Khouzami); Joint Applicants (4A)-2 at 15, Commitment 78.

803 Joint Applicants' Br. at 99, citing Joint Applicants (F) at 30:8-11 (Khouzami); Joint Applicants (F)-3.

804 Joint Applicants' Br. at 99, citing Joint Applicants (4A)-2 at 16, Commitment 90.

805 Joint Applicants' Br. at 99, citing Joint Applicants (F) at 30:12-14 (Khouzami).

806 Joint Applicants' Br. at 99, citing *Formal Case No. 951*, Order No. 11075, pp. 80-81, rel. October 20, 1997.

> that Pepco will provide copies of any portions of external audit reports performed for EBSC pertaining to the determination of direct billings and cost allocations to Pepco-DC no later than 30 days after the final report is completed, and that the Commission under its authority pursuant to its affiliate transactions rules may "review the allocation of costs in sufficient detail to analyze their reasonableness, the type and scope of services that EBSC provides to Pepco and the basis for inclusion of new participants in EBSC's allocation formula."[807]

Summary of OPC's and Intervenors' Position Pertaining to Factor No. 5

271. OPC states, "[c]ommon sense dictates that it is more difficult to regulate a larger entity (an Exelon-owned Pepco) than a smaller one (a PHI-owned Pepco)."[808] OPC states "it will be more difficult for the Commission to regulate the District's electric provider if its CEO and home office are based in Chicago rather than in the District."[809] OPC incorporates by reference its earlier discussion under Public Interest Factor No. 2 regarding loss of local control, summarized in paragraphs 177-182.

272. OPC asserts Pepco's participation in Exelon's GSA will have negative implications on the Commission's ability to effectively review and monitor the costs being charged to Pepco.[810] Since Pepco will be receiving charges from both PHISCo and EBSC, OPC asserts "the information and reporting concerns raised by OPC in prior rate cases, many of which have been shared by the Commission will be amplified."[811] OPC quotes the Commission's Order in *Formal Case No. 1103*, Pepco's last distribution rate case, wherein the Commission states that it "shares OPC's concern that the amount of information about the District of Columbia-specific PHISCo costs that are allocated to the District is inadequate."[812] OPC goes on to quote at length the details of additional reporting requirements mandated by the Commission in that case regarding the Cost Allocation Manual and service agreement between PHI and Pepco.[813] OPC expresses concern that the Joint Applicants did not make a formal commitment to comply with the requirements of that Order.[814]

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807 Joint Applicants' Br. at 99, citing Joint Applicants (4A)-2 at 15, Commitment 79, Commitment 80. [The Joint Applicants appear to be referencing Commitment 89 not Commitment 80.]

808 OPC's Br. at 113.

809 OPC's Br. at 113-114.

810 OPC's Br. at 114.

811 OPC's Br. at 114, citing OPC (C) at 32:5-8 (Ramas).

812 OPC's Br. at 114-115, citing *Formal Case No. 1103*, Order No. 17424, ¶ 373, rel. March 26, 2014.

813 OPC's Br. at 115, citing *Formal Case No. 1103*, Order No. 17424, ¶ 374, rel. March 26, 2014.

814 OPC's Br. at 115.

273. OPC states "additional complications could arise simply due to the fact that Pepco's rate cases would involve costs being allocated from two different entities using two different cost allocation manuals."[815] They note that PHISCo uses 70 unique allocation factors for Pepco and the EBSC has approximately 60 different factors.[816] OPC asserts "[t]here is no dispute that the time associated with analyzing individual allocation ratios will increase as the number of ratios is expected to increase."[817] OPC also points to statements by Joint Applicants witness Khouzami concerning the absence of the reporting of other affiliate charges to Pepco.[818]

274. Finally, OPC argues that Exelon's conduct in this proceeding underscores OPC's position that it will be more difficult to effectively regulate an Exelon-owned Pepco than it is to regulate a PHI-owned Pepco. OPC states, "both the public and the Commission should be comfortable with the new players the proposed transaction would introduce into the District."[819] Further, OPC states "the public must have confidence in administrative processes, and Exelon's approach to administrative processes is an important part of that consideration."[820] OPC, quoting testimony from Joint Applicants witness Crane, goes on to discuss how the Joint Applicants revised their testimony and exhibits, but not their Application as support for the proposition that Exelon "played fast and loose with due process in order to gain a procedural advantage" and engaged in "questionable procedural gamesmanship."[821] Additionally, OPC points to the Joint Applicants non-compliance with the Commission's discovery rules, specifically Rules 122.4 and 122.13, regarding the handling of data responses.[822]

275. **AOBA.** AOBA asserts that Exelon is "insensitive" to the District's interests because the Joint Applicants are unwilling "to commit to provide access to Pepco's books and records in the District of Columbia upon request unless the[y] can have up to 20 days to produce those books and records."[823] AOBA notes that the Joint Applicants provide "[n]o explanation for why 20 days might be required to produce such documents."[824] Further, AOBA points out that Exelon only committed "to notify this Commission on an after-the-fact basis (*i.e.*, within 10 days

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815 OPC's Br. at 115, citing AOBA Cross Examination Exhibit No. 106.

816 OPC's Br. at 115 n. 421, citing AOBA Cross Examination Exhibit No. 106.

817 OPC's Br. at 115-116, citing AOBA Cross Examination Exhibit No. 106 at 2.

818 OPC's Br. at 116, citing Tr. at 1837:2-7, 1837:17-20 (Cross Examination of Khouzami).

819 OPC's Br. at 117.

820 OPC's Br. at 117.

821 OPC's Br. at 117, quoting Tr. at 238:7-13.

822 OPC's Br. at 117, citing OPC Cross Examination Exhibit No. 1 at 2; OPC Cross Examination Exhibit No. 18.

823 AOBA's Br. at 16-17, citing Joint Applicants (4A)-2 at 5, Commitment 29.

824 AOBA's Br. at 17 n. 10.

after the event) of any material change in the administration of Pepco's books and records."[825] AOBA concludes "[t]his commitment implies that Pepco's books and records could be moved to locations outside of the District of Columbia and this Commission would only be informed of a relocation of Pepco's books and records on an after-the fact basis."[826]

276. **District Government.** The District Government expresses a primary concern with the potential for Exelon to use "its core competencies in regulatory and legislative affairs" to shape how Pepco is regulated in the District.[827] The District Government states, "this merger [ ] could affect the Commission's ability to regulate Pepco effectively under Exelon . . . [because] (1) the size and complexity of Exelon's corporate structure (2) the geographic scope of Exelon's operations, and (3) the multiplicity of state regulatory authorities involved in regulating the merged company's operating affiliates."[828] The District Government states, "the presence of significant merchant generation assets within Exelon Corp. and one or more of its affiliates intending to participate in the SOS auction will require the Commission to develop, implement, and enforce the Code of Conduct required by D.C. Code § 34-1513 (c)."[829]

<u>Discussion Pertaining to Factor No. 5</u>

277. D.C. Code §§ 1-204.93 and 34-301 give the Commission plenary authority to regulate public utilities in the District of Columbia. Each public utility is subject to all applicable laws codified in Title 34 of the District of Columbia Code, any corresponding regulations promulgated by this Commission as codified in Title 15 of the D.C. Municipal Regulations, and all applicable Commission orders. Since this Proposed Merger involves a change of control over Pepco, the public utility that we regulate, we view this public interest factor with elevated scrutiny. In *Formal Case No. 1002*, the Commission approved the merger that caused Pepco to become a subsidiary of a public utility holding company with many regulated and non-regulated subsidiaries. During the hearing, Chairman Kane read a passage from *Formal Case No. 1002* where the benefits of that proposed merger were touted.[830] The arguments there sounded strikingly like the arguments in this proceeding. Because of the similarities, we bring our experience to this discussion of this public interest factor because we have experienced some challenges from the PHI construct that have, at times, impeded our ability to effectively regulate Pepco as a subsidiary of PHI.

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825 AOBA's Br. at 17, citing Joint Applicants (4A)-2 at 5, Commitment 29.

826 AOBA's Br. at 17 n. 11.

827 District Government's Br. at 37, citing Tr. at 3041:6-3047:6, 3060:11-3065:2 (Smith); District Government Confidential Cross-Examination Exhibit No. 14 at 80; District Government Cross-Examination Exhibit No. 37 (DC SUN Cross-Examination Exhibit No. 1).

828 District Government's Br. at 37-38.

829 District Government's Br. at 38, citing Tr. at 528:1-538:13 (Crane), and citing Joint Applicants (4A)-2 at 3, Commitment 9.

830 Tr. 872:6 -873:11 (colloquy by Chairman Kane quoting *Formal Case No. 1002*, Order No. 12395, ¶ 30, rel. May 1, 2002).

278. The record raises several issues when describing the effect of the Proposed Merger on the Commission's ability to regulate the new utility effectively: the Commission's timely and complete access to information related Pepco and all relevant affiliates of Exelon; additional tasks related to the presence of two shared services companies to ensure that District ratepayers are not paying costs that should be allocated to the unregulated businesses of the Joint Applicants and are being fairly charged for services that are being provided for Pepco-DC; new management tools and agreements that may raise additional auditing and enforcement issues; and the need to review and possibly strengthen Commission rules and procedures dealing with conflicts of interest between affiliates and enhance the Commission's ability to oversee and investigate potential conflicts issues if they arise.

279. With respect to the Commission's timely and complete access to information related to Pepco and all relevant affiliates of Exelon, AOBA raises concerns regarding the Commission's access to Pepco's books and service company cost allocation manuals.[831] Joint Applicants' Commitment 29 states that the Joint Applicants will provide the Commission and OPC access to Pepco's books "within twenty working days after such a request."[832] Joint Applicants' Commitment 29 also states that the Joint Applicants will "notify the Commission of any material change in the administration, management or condition of Pepco's books and records within ten days after the event."[833] However, D.C. Code § 34-1112 requires each public utility to keeps its books in an office within the District, "except as prescribed by the Commission" and "produce before the Commission such books . . . from time to time *as the Commission may order*."[834] Additionally, Commission Rule 3904.3 requires a utility company to "file amendment(s) to the cost allocation manual within 30 days from the effective date of the change." The Joint Applicants contend their 10-day notice period for changes to the cost allocation manual is a benefit as 10 days is substantially shorter than the 30-day notice period required under our rules.[835] However, the Joint Applicant's commitment that seeks to delay access to the books and records of Pepco is not beneficial because delayed access to necessary books and records will negatively impact the Commission's ability to effectively carry out its oversight role. Additionally, it raises a concern about the future intended location of Pepco's books and records of Pepco as well as the process of quickly accessing them when they are needed for regulatory oversight purposes or when they are needed for Commission proceedings.

280. The introduction of a second shared services company also raises a concern for the Commission. OPC and the District Government assert that the effect of the Proposed Merger on the Commission's ability to regulate the new utility will be harmful because of the increased regulatory complexity inherent in scrutinizing two distinct sets of service company charges under different service agreements. It is undisputed on the record that both PHISCo and EBSC will

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831 *See* AOBA's Br. at 16-17.

832 *See* Joint Applicants (4A)-2 at 5, Commitment 29.

833 *See* Joint Applicants (4A)-2 at 5, Commitment 29.

834 D.C. Code § 34-1115 (2015). (Emphasis added).

835 *See* 15 DCMR § 3904.3 (2011).

allocate costs to Pepco; that PHISCo and EBSC have their own cost allocation manual; and that the two companies use different methods of cost allocation.[836] PHISCo uses 110 allocation ratios of which 30 are based on the same ratio and 80 are unique allocation factors for Pepco. EBSC uses approximately 60 allocation factors, the majority of which are billed to Exelon's regulated utilities.[837] The Joint Applicants do not address how or when these two different cost allocation manuals will be harmonized to ensure the transparency of intercompany charges. It is beyond dispute, however, that the Commission and OPC and any Intervenor in a rate case where service costs are at issue will face an additional regulatory burden if they have to learn and work with two systems of service charges that are being imposed on Pepco and District ratepayers. The Commission agrees that "the information and reporting concerns raised by OPC in [*Formal Case No. 1103*] . . . will be amplified."[838] The Joint Applicants suggest that District ratepayers could see a benefit because certain service company functions will be transferred from PHISCo to EBSC following the merger and would allow Pepco to "realize economies of scale and scope" by sharing such services with other Exelon affiliates.[839] While the Commission recognizes that this is a possibility that could occur, the Joint Applicants provided no quantitative evidence to support this conclusion nor did they quantify the cost decrease that Pepco could expect to receive under this scenario.

281. The parties also note that the Proposed Merger would result in the introduction of several new agreements that would govern some of the activities of Pepco and of PHI as they relate to Pepco. These include the General Services Agreement, the Delegation of Authority document and the Exelon Management Model. The Commission, its staff, and the parties in Commission proceedings will need to become familiar with these new documents and may determine that these documents raise additional auditing and enforcement issues for the Commission in the future. Additionally, we note that the managers who will be administering these documents under the new management structure may be located outside of the District of Columbia which again raises access issues for the Commission. We note, however, that the Joint Applicants, in their written commitments, have agreed to make both their personnel and their documents accessible.

282. The final effect that the Proposed Merger may have on the Commission's regulatory duties is the need to review and possibly strengthen Commission rules and procedures dealing with conflicts of interest between the Joint Applicants and their affiliates and the need to enhance the Commission's ability to oversee and investigate potential conflicts issues if they arise. In Paragraphs 298 and 299 of this Order, we address this issue in more detail as it relates to the SOS process and to local retail competition.

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836 Tr. at 2896:21-2897:10; OPC Cross Examination Exhibit No. 106 (Joint Applicants' Response to OPC Data Request 18-107).

837 *See* AOBA Cross Examination Exhibit No. 106.

838 OPC's Br. at 114, citing OPC (C) at 32:5-8 (Ramas).

839 *See* Joint Applicants (F) at 29:18-21 (Khouzami).

283. OPC also sees fault in the Joint Applicants' failure to specifically commit to complying with the additional service company reporting requirements in the Commission's *Formal Case No. 1103*, Order No. 17424.[840] While OPC's sentiment is understandable, the Commission does not consider the lack of a specific commitment to comply with reporting requirements to be problematic because Pepco would remain bound to fully comply with all prior Commission orders, unless specifically and explicitly excused from doing so. Similarly, while the District Government sees regulatory risks in Exelon's lobbying efforts, such efforts are outside the scope of this Commission's regulatory reach; therefore, it is not an issue that we will consider in assessing the impact of the Proposed Merger.

284. Given the above, the Commission concludes that while the Proposed Merger would not -- indeed cannot -- change our regulatory oversight over Pepco, it would impact the manner in which the Commission's regulatory oversight is administered. More specifically, we conclude that the Proposed Merger would not have a beneficial effect on the Commission's ability to regulate the new utility effectively. To the contrary, the Proposed Merger would make regulatory tasks more complex; more time-consuming and more costly. In addition, the introduction of a second shared services company would produce mixed results. On the one hand, it offers the possibility of reduced costs through "economies of scale" as the Joint Applicants have argued but have not proven on the record; but also offers the possibility that District ratepayers will be charged costs that are not related to regulated services being provided by Pepco-DC. Services. In any event, the presence of two service companies will increase the need for regulatory oversight, reporting and auditing to ensure that Pepco and District ratepayers are being allocated the correct costs.

6. FACTOR 6: The effects of the transaction on competition in the local retail and wholesale markets that impacts the District and District ratepayers

Summary of Joint Applicants' Position Pertaining to Factor No. 6

285. The Joint Applicants begin by stating that the Commission, in Order No. 17597, specifically excluded competition issues that are not focused on the effects in the District of Columbia and issues related to the need to change the Commission's SOS rules as a consequence of the Merger, which would be addressed in a separate proceeding.[841] According to the Joint Applicants, "the merger creates no competition concerns in the District" because "[m]ost of the competition issues raised by other parties in this proceeding consist of issues that are beyond the scope of this proceeding as defined by the Commission" and "[t]he few competition concerns raised that fall within the scope of the proceedings are unsupported and have no merit."[842]

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[840] *See* OPC's Br. at 115, citing *Formal Case No. 1103,* Order No. 17424, ¶ 373, rel. March 26, 2014.

[841] Joint Applicants' Br. at 100, referencing *Formal Case No. 1119*, Order No 17597, ¶ 118, rel. August 22, 2014.

[842] Joint Applicants' Br. at 100-101.

286. The Joint Applicants point out that the Proposed Merger does not increase Exelon's wholesale market share because"[n]either Pepco nor any of its affiliates owns or controls any generation capacity that is located in the District of Columbia, and they control only 17 MW of capacity located elsewhere."[843] Moreover, as the Joint Applicants note, FERC has already found that the Proposed Merger "does not raise any horizontal or vertical market power concerns in wholesale markets."[844] Similarly, the Joint Applicants state the Proposed Merger "cannot reduce competition to provide SOS service in the District . . . because neither Pepco nor any of its affiliates currently participate in the District of Columbia's SOS auctions."[845]

287. Similarly, the Joint Applicants state the Proposed Merger "will have no effect on competitive retail markets in the District of Columbia."[846] In support, the Joint Applicants first state the Proposed Merger "has no effect on the ability of competitive retail suppliers to access wholesale supplies to meet retail load."[847] Second, the Joint Applicants state, "neither Pepco nor any of its affiliates competes in the competitive retail market in the District of Columbia, and, therefore, the Merger will not eliminate any competition in that market."[848] Third, the Joint Applicants state "the fact that the Merger will eliminate the possibility that in the future a Pepco affiliate could re-enter the competitive retail market as an independent competitor has no material effect because there already is robust competition in the District of Columbia."[849] In support, the Joint Applicants state:

> There currently are 50 approved competitive retail suppliers, 30 of which currently are supplying residential and/or commercial customers. Furthermore, customer switching to competitive suppliers in 2013 reached 14% for residential customers in the District of Columbia and over 80% for commercial customers.[850]

The Joint Applicants assert that OPC witness Dismukes agreed with their analysis that "the Merger should not have any negative effect on wholesale markets, competitive retail markets or the SOS procurement process."[851] Additionally, the Joint Applicants point out that the Market

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843 Joint Applicants' Br. at 101, citing Joint Applicants (2J) at 3:8-21 (Solomon).

844 Joint Applicants' Br. at 101, citing Joint Applicants (3J)-1 (*Exelon Corporation & Pepco Holdings, Inc.*, 149 F.E.R.C. ¶ 61,148 (2014)).

845 Joint Applicants' Br. at 101, citing Joint Applicants (3J) at 5:1-6:8 (Solomon).

846 Joint Applicants' Br. at 101.

847 Joint Applicants' Br. at 101, citing Joint Applicants (2J) at 14:10-14 (Solomon).

848 Joint Applicants' Br. at 101, citing Joint Applicants (2J) at 14:15-22 (Solomon).

849 Joint Applicants' Br. at 101-102.

850 Joint Applicants' Br. at 102, citing Joint Applicants (2J) at 15:1-13 (Solomon).

851 Joint Applicants' Br. at 102, citing OPC (A) at 128:18-20, 128:18-131:21 (Dismukes).

Monitor agreed that there are no competition concerns "resulting from the combination of the Joint Applicants' generation capacity."[852]

288. To address concerns that "Pepco could unduly favor Exelon's merchant generation business, either through the conduct of the SOS auctions or in the conduct of retail competition in the District" the Joint Applicants make two commitments.[853] First, the Joint Applicants commit that "Pepco will continue to provide SOS to its customers in the District of Columbia consistent with the District of Columbia Code and Affiliate Code of Conduct; and [ ] Exelon intends to continue participating in SOS auctions after the Merger."[854] Second, the Joint Applicants commit "that Exelon will comply, and cause Pepco and other Exelon affiliates to comply, with the statutes and regulations applicable to Pepco regarding affiliate transactions, including without limitation 15 D.C.M.R. §§ 3900-3999."[855] Since these commitments rely on the Commission's existing rules and regulations governing the SOS auctions and affiliate transactions, the Joint Applicants state "[t]o the extent . . . that the Commission or any party believes that the existing rules are inadequate, that does not constitute grounds for rejecting the Merger. As noted above, the Commission held in Order No. 17597 that the issue of whether these rules should be modified as a result of the Merger will, if necessary, be addressed in a separate rulemaking proceeding."[856]

289. With regard to SOS procurement in the District, the Joint Applicants, relying on Mr. Gausman, state:

> Pepco provides SOS in the District of Columbia through Request For Proposals (RFPs) conducted pursuant to the District of Columbia's SOS rules and the Commission's rules and orders. These rules provide the detailed structure for conducting supply procurements and standardizing all non-price terms and conditions, which are approved by the Commission each year. All suppliers bid on the same products, and contract evaluations and awards for those products are made on a lowest-price basis.[857]

The Joint Applicants point out that the procurement of SOS is monitored by an Independent Market Monitoring Consultant who reports to the Commission and OPC and that "the rules

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852 Joint Applicants' Br. at 102, citing PJM-IMM (A)-1 at 2.

853 Joint Applicants' Br. at 102-103.

854 Joint Applicants' Br. at 103, citing Joint Applicants (4A)-2 at 3, Commitment 9.

855 Joint Applicants' Br. at 103, citing Joint Applicants (4A)-2 at 14, Commitment 74.

856 Joint Applicants' Br. at 103, citing *Formal Case No. 1119*, Order No 17597, ¶ 118, rel. August 22, 2014.

857 Joint Applicants' Br. at 103-104, citing Joint Applicants (2E) at 3:3-18 (Gausman).

prevent Pepco from providing information to affiliated competitive providers unless such information is provided to all competitive bidders."[858]

290. The Joint Applicants, based on the above, explain "that these statutory and regulatory provisions were in effect at a time when PHI-owned generation facilities and a competitive retail electric and gas supply business. They were promulgated to address the concern that Pepco might act to favor its affiliates that competed to provide SOS and competitive retail service."[859] The Joint Applicants also point out that "no concerns [were] raised regarding the integrity of the SOS arising from Pepco's affiliation with Conectiv Energy, which was, at times, a participant in the SOS process, and PES, which was a competitive retail energy supplier active in the District of Columbia."[860] Regarding "the issue of a distribution utility potentially favoring an affiliated merchant generation company," the Joint Applicants point out this "is not unique to the District" and "[e]very state that has shifted to retail competition and conducts an SOS auction – including Pennsylvania, Maryland, Delaware, and New Jersey – faces the same concern."[861] The Joint Applicants assert "[t]hese states have implemented affiliate regulations that are very similar to the provisions that are in place in the District of Columbia, and none of them have encountered any problems with respect to affiliated merchant generation companies being favored in any respect" and that no witness in this case "has identified any aspect of the Commission's affiliate rules that they believe to be inadequate."[862]

291. The Joint Applicants assert that the competition issues raised by the PJM Market Monitor are outside the scope of this proceeding. The issues raised by the PJM Market Monitor do not address "'competition in the local retail, and wholesale markets that impacts the District and District ratepayers,'" rather they are the comments originally submitted to FERC and address "'the impact of the merger on the regional transmission organization, PJM, or on the PJM region as a whole.'"[863] The Joint Applicants state "those arguments were addressed by FERC and were, without exception, rejected as having no merit."[864]

292. Regarding Mr. Hempling's contention "that the Merger will harm competition in the competitive retail market because, '[a]bsent this merger, Pepco could change its mind, for a new affiliate, and enter the competitive market,'" the Joint Applicants highlight the speculative nature of the argument and state "'any theoretical loss of a hypothetical supplier in a market with so many competitors and low barriers to entry does not signal an adverse competitive effect of

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858 Joint Applicants' Br. at 104, citing 15 DCMR §§ 4109, 4108.3 (d) (2015).

859 Joint Applicants' Br. at 105, citing Joint Applicants (2E) at 5:17-7:7 (Gausman).

860 Joint Applicants' Br. at 105, citing Joint Applicants (2E) at 6:1-5 (Gausman).

861 Joint Applicants' Br. at 105, citing Joint Applicants (3J) at 28:1-6 (Solomon), Joint Applicants (2E) at 5:12-16 (Gausman).

862 Joint Applicants' Br. at 105, citing Joint Applicants (3J) at 28:1-6 (Solomon).

863 Joint Applicants' Br. at 106, citing *Formal Case No. 1119*, Order No 17597, ¶ 118, rel. August 22, 2014.

864 Joint Applicants' Br. at 107, citing Joint Applicants (3J)-1 at ¶¶ 45-49, 80-83.

the Merger.'"[865] Regarding Mr. Hempling's contention "that the Merger could have a negative effect on 'benchmark competition,' which he defines as the ability of 'commissions and customers to compare adjacent companies based on price and quality, and then take action,'" the Joint Applicants state "Pepco is the only electric distribution utility located in the District of Columbia. As a consequence, the Commission and Pepco's customers—to the extent they compare Pepco's rates and service with any other utility—must compare Pepco with utilities in other jurisdictions outside of the District of Columbia."[866] Finally, Regarding Mr. Hempling's contention "that the Merger will affect 'franchise competition,' which he describes as competition 'for the franchise, should either jurisdiction invite franchise competition,'" the Joint Applicants state "[t]o the extent that Mr. Hempling is correct, it is the *threat* of a takeover, not the *identity* of the entity replacing Pepco as the franchise holder, that would affect Pepco's performance."[867]

<u>Summary of OPC's and Intervenors' Position Pertaining to Factor No. 6</u>

293. OPC states that if the Proposed Merger is granted, "Exelon will be in a position to exercise a great degree of influence on policy discussions that shape [the] District's utility landscape for decades to come."[868] OPC asserts "the record in this case contains substantial evidence demonstrating that, if the Commission approves the transaction, Exelon will exercise its influence [over the local distribution company] to the detriment of District and Pepco's ratepayers."[869] OPC states, "the record demonstrates that Exelon intends to control the pace of development of distributed energy resources within the footprint of its distribution utilities in order to protect its substantial merchant generation function."[870] OPC concludes that "[i]f implemented, this intention would be harmful to consumers because [it] would hamper the ability of distribution-level generation and storage technology systems to develop naturally through healthy competition and innovation."[871]

294. OPC asserts that "[i]n policy debates about demand response or energy efficiency, the Commission at present simply does not have to worry about PHI or Pepco taking actions that are based on the need to protect central station generation. This is because, by its own design, PHI is fundamentally a regulated distribution utility company. As

[865] Joint Applicants' Br. at 107-109, citing GRID2.0 (A) at 154:2-3 (Hempling), Joint Applicants (3J) at 151-7-9 (Solomon).

[866] Joint Applicants' Br. at 109-110, citing GRID2.0 (A) at 151:7-9 (Hempling), Joint Applicants (3J)-5 at 2.

[867] Joint Applicants' Br. at 109-110, citing GRID2.0 (A) at 152:18-19, 153:1-3 (Hempling), Tr. at 3511:6-10 (Hempling Cross).

[868] OPC's Br. at 118-119.

[869] OPC's Br. at 119.

[870] OPC's Br. at 119, citing Tr. at 3559:19-3560:16 (DC SUN witness Schoolman).

[871] OPC's Br. at 119.

such, PHI is largely agnostic to central station generation."[872] OPC states, "Exelon has already taken positions that are different from (at best) or not consistent with (at worst) the agnostic nature of a wires-only company."[873] OPC concludes, "Exelon's enterprise-wide business strategy would need to change in order for this harm to dissipate."[874]

295. **District Government.** The District Government contends that the "proposed merger adversely affects competition on both the wholesale and retail levels."[875] At the wholesale level, the District Government states, "a post-merger Exelon would have the ability to exercise leverage over the entire PJM RTO by threatening to leave" and that the Proposed Merger will require additional "market monitoring, investigative, and reporting activities" by the Commission and OPC pursuant to D.C. Code § 34-1512.[876] At the retail level, the District Government states, "[t]he merger sets up a conflict between a utility holding company with a vast fleet of fossil and nuclear generation and a sense of its entitlement to control the electric distribution system within the District of Columbia, and District policies favoring the development of localized, renewable generation within the District of Columbia." The District Government sees the change in control of the local distribution system, inherent in the Proposed Merger, as "fundamentally inconsistent with the advancement of localized renewable generation and energy efficiency."[877] Moreover, the District Government is concerned that:

> if the merger is permitted to proceed before future policies with regard to direct access to the distribution network are resolved, Exelon's demonstrated proclivity for reshaping the legislative and regulatory landscape in ways that it finds congenial is likely to mean that the development and implementation of the policies that the Commission envisions establishing in the future proceeding discussed in Order No. 17851 may well end up being subject to the outcome of this proceeding, rather than the other way around. In the District's view, this is neither a desirable outcome nor one that the Commission ought to entertain.[878]

296. **GRID2.0.** GRID2.0 sees an inherent conflict between Pepco and Exelon stating that "[b]ecause Pepco does not own generation it has no reason to support higher cost[s] for electric supply, and should pursue policies that result in improved quality and lower [costs] for

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872 OPC's Br. at 119-120, citing OPC Cross Examination Exhibit No. 8 at 2-4; OPC Cross Examination Exhibit No. 9 at 2.

873 OPC's Br. at 120, citing Tr. at 3580:6-18.

874 OPC's Br. at 120.

875 District Government's Br. at 38.

876 District Government's Br. at 38-39, citing District Government (F) 56:1-63:13 (Wilson).

877 District Government's Br. at 40.

878 District Government's R.Br. at 31.

ratepayers. Exelon in contrast, has a fiduciary responsibility to maximize profits from its merchant generation fleet."[879] GRID2.0 states: "[g]ranting the Joint Applicants' desire to merge . . . will run counter to the PSC's rational[e] [for] Pepco's generation divestiture in 1999."[880] GRID2.0 asserts that the difference between Pepco's interest in procuring low-cost electricity and Exelon's affiliates' interest in high prices for the electricity they sell "can cause conflict in five policy areas: transmission access to lower cost generation suppliers, wind and solar displacing nuclear and fossil, distributed energy resources, retail competition, and Standard Offer Service."[881] In discussing retail competition, GRID2.0 raises the possibility of Pepco discouraging or delaying customers from switching to a third-party supplier as a means of supporting Exelon's generating affiliate.[882] Moreover, Exelon has stated that: "(a) it supports customer switching to alternative electric generation suppliers, and (b) its acquisition of Constellation's competitive retail operations provides another outlet for Exelon to 'grow its business in competitive markets.'"[883] GRID2.0 goes on to say that, "[c]ertainly in markets where Exelon's affiliates compete for retail sales, it will support customer switching (at least, switching to Exelon's affiliates [such as Constellation]). But Exelon will not necessarily support switching in markets where the switching is away from an incumbent utility Exelon controls."[884] As for SOS, GRID2.0 states "[h]aving a supplier that corporately controls the buyer is the definition of conflict of interest. Exelon recognizes this problem, but merely promises not to break the law," which leads them to argue for the Commission to "make clear that Pepco's continuing role as the SOS provider is not a foregone conclusion."[885]

297. The PJM Market Monitor argues for numerous actions at the wholesale level that would mitigate their concerns about the functioning of the PJM market.[886] The PJM Market Monitor states "[t]he FERC's decision not to include the mitigation measures is not explained."[887]

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879 GRID2.0's Br. at 13, citing Tr. at 437:1-14 (Crane).

880 GRID2.0's Br. at 13, referencing *Formal Case No. 945*, *In the Matter of the Investigation Into Electric Service Market Competition and Regulatory Practices* ("*Formal Case No. 945*"), Order No. 11576, p. 10 n. 32, rel. December 30, 1999.

881 GRID2.0's Br. at 14.

882 GRID2.0's Br. at 19-20.

883 GRID2.0's Br. at 20, citing *Formal Case No. 1119*, Joint Application, Exhibit No. 1 (Exelon 2013 10-K) at 84.

884 GRID2.0's Br. at 20.

885 GRID2.0's Br. at 20-21.

886 PJM Market Monitor's Br. at 1-12.

887 PJM Market Monitor's R.Br. at 2, citing *Exelon Corporation & Pepco Holdings, Inc.*, 149 F.E.R.C. ¶ 61,148, ¶¶ 76-83 (2014).

Discussion Pertaining to Factor No. 6

298. The record is clear that the Proposed Merger will have an effect on wholesale competition in the District by raising the potential for conflicts of interest in the procurement of SOS. As OPC pointed out, "Exelon actively participates in the SOS procurement process in the District through the subsidiary, Exelon Generation. Currently, Exelon Generation provides electricity to Pepco to serve SOS customers in addition to being selected as a supplier of electricity for the 2014-2015 term."[888] The Commission's notice of Winning Wholesale Suppliers for Standard Offer Service confirms that Exelon continues to serve our SOS load at this point.[889] The Joint Applicants point out that numerous other jurisdictions with retail competition, such as Pennsylvania, Maryland, Delaware, and New Jersey, face similar concerns.[890] They assert further that this will not be an issue because they commit to comply with the statutes and regulations applicable to Pepco regarding affiliate transaction.[891] This would not be the first time that an affiliate of the SOS Administrator has participated in the SOS procurement. [892] Our affiliate transaction rules which are referenced in our procurement documents anticipate such transactions and set out the applicable guidelines. Our Independent Market Monitor oversees the procurement process and provides assurance to the Commission that the process has taken place consistent with our rules. Moreover, given the prevalence of distribution utilities with affiliated generation and the Commission's decision in Order No. 17597 to review our SOS rules in a separate proceeding, we conclude that any concerns about the participation of the Joint Applicants in the SOS procurement process as both the SOS Administrator and a bidder can be adequately addressed by modifying the rules for the procurement procedures so that there could be no harm to District ratepayers under the wholesale SOS model adopted by this Commission.[893] Consequently, on the SOS side, we conclude that the effect of the Proposed Merger would be to leave wholesale market competition unharmed but with no noticeable benefits.

299. The Proposed Merger's effects on the local retail market are more ambiguous. It is clear to the Commission, and not seriously challenged by any party, that the electricity retail market is competitive with about 50 approved competitive retail suppliers (excluding brokers/aggregators and entities that have withdrawn), roughly 30 of which currently are supplying residential and/or commercial customers. In 2013, these suppliers served 14% of the residential customers and over 80% of the commercial customers in the District.[894] There is

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888 *See* OPC (A) at 125 (Dismukes).

889 "Winning Wholesale Suppliers for Standard Offer Service," Public Service Commission of the District of Columbia, available at http://www.dcpsc.org/customerchoice/whatis/electric/winning_wholesale_bkp_9apr15.asp .

890 *See* Joint Applicants (3J) at 28:1-6, Joint Applicants (2E) at 5:12-16 (Gausman).

891 *See* Joint Applicants (4A)-2 at 3, Commitment 9, Joint Applicants (4A)-2 at 14, Commitment 74.

892 The Joint Applicants are correct that at one point Conectiv participated in the SOS bidding. However, Conective has not been a SOS market participant for at least 9 years.

893 *Formal Case No. 1119*, Order No 17597, ¶ 118, rel. August 22, 2014.

894 *See* Joint Applicants (2J) at 15:1-13 (Solomon).

some concern about just how aggressive an Exelon-owned Constellation would be at recruiting customers when an Exelon-owned Pepco is also the SOS Administrator, and an Exelon-affiliate is also supplying energy for the SOS program. This would not be the first time, however, that the SOS Administrator is also affiliated with a retail electric supplier. We note that when Pepco affiliate Pepco Energy Services was active in the District there were no retail competition issues and we would not expect to see any if the Proposed Merger is consummated.

300. Concern has been expressed about the ability of an Exelon owned Pepco to fairly operate the distribution system in a manner that would not discourage distributed generation, especially for solar systems. We do not share that concern. In any event, D.C. Code § 34-1506 mandates that Pepco "provide distribution services to all customers and electricity suppliers on rates, terms of access, and conditions that are comparable to the electric company's own use of its distribution system" and "not operate its distribution system in a manner that favors the electricity supply of the electric company's affiliates;"[895] and the Commission stands ready to enforce these mandates if there is a problem.

301. The Commission therefore concludes that the Proposed Merger provides no additional benefits with respect to wholesale competition or with respect to retail competition. Because an Exelon-owned affiliate is a major player in the SOS wholesale SOS procurement process, the Commission would need to review both its affiliate transaction rules, the SOS procurement rules and the Wholesale Full Requirements Service Agreement would need to be reviewed and possibly amended to make certain that they fairly and reasonably address any concerns about conflicts of interest or procedural fairness to prevent any potential harm to District ratepayers and the Commission's SOS Program. Additionally, the Proposed Merger raises a potential harm in that there is a potential conflict of interest if the company that controls the local distribution company seeks to delay changes necessary to encourage additional distributed generation because of its ownership of alternative generation sources.

7. FACTOR 7: The effects of the transaction on conservation of natural resources and preservation of environmental quality

Summary of Joint Applicants' Position Pertaining to Factor No. 7

302. In response to the Commission adding Public Interest Factor No. 7 to look at the impact of the Proposed Merger on the "conservation of natural resources and preservation of environmental quality," in accordance with the Clean and Affordable Energy Act,[896] the Joint Applicants submitted the testimony of Christopher Gould, Exelon's Senior Vice President of Corporate Strategy and Chief Sustainability Officer, who described Exelon's long-standing commitment to a sustainable energy future and how that commitment is reflected across an

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[895] D.C. Code § 34-1506 (a) (2015).

[896] Joint Applicants' Br. at 111, citing *Formal Case No. 1119*, Order No 17597, ¶ 116, rel. August 22, 2014. D.C. Code Section 34-808.02 provides that "In supervising and regulating utility or energy companies, the Commission shall consider the public safety, the economy of the District, the conservation of natural resources, and the preservation of environmental quality."

extensive range of industry-leading programs at Exelon's utilities and in Exelon's own low-carbon generation portfolio.[897] Through Mr. Gould's testimony, and other evidence (including testimony of witnesses appearing on behalf of intervenors), the Joint Applicants claim to have shown that the Proposed Merger will have a decidedly positive impact on the conservation of natural resources and preservation of environmental quality in the District of Columbia.[898] The Joint Applicants also claim that the record demonstrates Exelon's leadership in renewable energy, distributed generation, energy efficiency, and innovative energy technologies. Examples include:

> Exelon is the eleventh largest producer of wind energy in the United States and continues to develop new wind projects across the country – including in areas where Exelon owns competing nuclear generation assets;[899]
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> * * *
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> Exelon's subsidiary, Constellation New Energy, Inc., is the country's seventh largest developer of commercial distributed solar projects and the largest solar developer in Maryland;[900]
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> * * *
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> Each Exelon utility has facilitated the interconnection of distributed generation systems, with thousands of customers (and over 100 MW of distributed generation) now participating in net metering programs;[901]
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> * * *
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> Each Exelon utility has been in full compliance with escalating renewable and alternative energy portfolio standards (RPSs) in Pennsylvania, Maryland and Illinois, procuring millions of renewable energy credits (RECs) created by renewable energy generators each year;[902]
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> * * *
>
> Exelon's venture investing arm, Constellation Technology Ventures, is making non-utility investments to drive renewable energy innovation – including investments in start-up companies focused on improvements in wind technology, solar panel efficiency, batteries and storage, and biomass fuels – which are

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[897] Joint Applicants' Br. at 111.

[898] Joint Applicants' Br. at 111.

[899] Joint Applicants' Br. at 111, citing Joint Applicants (3I) at 4:10-14 (Gould); Tr. at 1559:6-21 (Gould Cross).

[900] Joint Applicants' Br. at 111, citing Joint Applicants (3I) at 4:15-19 (Gould); Tr. at 1541:7-13 (Gould Cross).

[901] Joint Applicants' Br. at 112, citing Joint Applicants (3I) at 4:29-31 (Gould).

[902] Joint Applicants' Br. at 112, citing Joint Applicants (3I) at 4:24-27 (Gould).

> new technologies that can be leveraged for use across Exelon's portfolio of companies, including its utilities.[903]

303. According to the Joint Applicants, there is a complete lack of any credible evidence that Exelon will not be a good partner in the District of Columbia's implementation of renewable energy requirements and broader sustainability goals (including those of the Sustainable DC Plan).[904] The Joint Applicants allege that OPC and the intervenors who still question Exelon's commitment to the environment do so based on speculation unsupported by substantial evidence.[905] The Joint Applicants add that these parties raise two primary objections to the Proposed Merger under Factor No. 7: (1) that Exelon has not included any specific commitment related to renewable energy or other sustainability goals of the District of Columbia; and (2) that Exelon's past position on the now expired federal wind production tax credit ("PTC") and other issues reflect a preference for traditional, central station nuclear generation that will result in a post-Merger Pepco at odds with the District's renewable energy and sustainability goals, particularly increased distributed generation.[906] The Joint Applicants argue that these objections are entirely without merit and that this proceeding is not the place to pursue or resolve all environmental or "utility of the future" issues facing the District.[907] According to the Joint Applicants, the intervenors' broad assertions regarding Exelon's legislative positions are largely irrelevant and without foundation, and the actual record in this proceeding demonstrates that the Proposed Merger will substantially enhance the District's opportunity to realize its sustainable energy goals and the benefits of a transforming energy system.[908]

304. With respect to the first objection, the Joint Applicants submit that any suggestion that Exelon has not made a renewable energy or sustainability "commitment" under Factor No. 7 as part of the Proposed Merger misstates the purpose and rationale of the Joint Applicants' proposed CIF.[909] As Mr. Crane explained, the CIF can be used to advance conservation of natural resources and environmental quality through energy efficiency programs, demand response programs, or any other program which the Commission determines will be the most effective use of all or a portion of the CIF funds in light of existing District of Columbia laws

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903 Joint Applicants' Br. at 112, citing Joint Applicants (3I) at 5:1-6 (Gould).

904 Joint Applicants' Br. at 113.

905 Joint Applicants' Br. at 113.

906 Joint Applicants' Br. at 113.

907 Joint Applicants' Br. at 113 n. 509, stating that as Chair Kane noted at the conclusion of hearings, the Commission will be opening a new docket to address issues relating to grid modernization, microgrids, and storage. *See* Tr. at 3581:7-10 (Commission Cross of Schoolman).

908 Joint Applicants' Br. at 113.

909 Joint Applicants' Br. at 113.

and programs and the wide variety of District of Columbia stakeholder goals.[910] The Joint Applicants state that the lack of specific program options proposed by Exelon does not reflect an absence of a commitment to the District under Public Interest Factor No. 7 but, rather, evidences a firm belief that the District and its stakeholders – either through a separate proceeding, or potentially through a settlement approved by the Commission – will reach the best result for using the CIF to advance sustainability in the District.[911]

305. The Joint Applicants submit that the intervenors' second objection – that Exelon is biased towards traditional nuclear generation and opposes distributed generation and "utility of the future" developments, as purportedly reflected in Exelon's positions on certain policies – is similarly unsupported by the record in this proceeding.[912] The Joint Applicants argue that what the record shows is that Exelon's actual views on distributed generation and other energy developments will enhance the opportunities for the District and for Pepco customers to benefit from increased distributed generation and effective deployment of new technologies and are consistent with ensuring that clean energy is affordable and cost-effective for all customers.[913] The Joint Applicants add that both Mr. Crane and Mr. Gould emphasized the opportunities associated with distributed generation.[914]

306. The Joint Applicants represent that no intervenor witness contested Mr. Gould's explanation that projected retirements of other types of generation will create "an enormous amount of opportunity" for both centralized and distributed generation; indeed, DC SUN witness Schoolman conceded that she had done no quantification of whether even the full 250 MW of distributed solar required by the District's RPS in 2023 would have any actual material effect on wholesale electricity prices in PJM, with its 180,000 MW of generating capacity, or the

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910 Joint Applicants' Br. at 113-114, citing Tr. at 442:9-443:3 (Crane Cross); *see also* Tr. at 2279:16-21 (Tierney Cross) (discussing Factor No. 7 and explaining that "certainly part of what has been offered as a monetary benefit could be used by the Commission affirmatively to create a benefit from the customer investment fund for energy efficiency or for renewable energy development or anything else related to sustainability").

911 Joint Applicants' Br. at 114-115 n. 513, wherein the Joint Applicants state that should the Commission choose not to allocate any portion of the CIF to programs that will impact conservation of natural resources and environmental quality, that decision will not preclude approval of the Merger. The Joint Applicants note that some intervenors sought to condition Merger approval on additional "benefits" that appear to require the Commission to impose conditions that would be inconsistent with competitive markets and the laws governing the District's Standard Offer Service procurements. *See, e.g.*, Tr. at 2777:1-2779:14 (Burcat Cross) (proposing 10 to 20-year renewable energy contracts); Tr. at 2820:8-19 (Commission Cross of Burcat) (proposing that Exelon be required to explore new transmission in PJM); Tr. at 3179:4-3182:10 (Commission Cross of Chambers) (proposing that Exelon be required to construct distributed generation on District facilities, potentially through a sole source procurement). Aside from the legal flaws that these proposals appear to present, the witnesses did not provide any quantification of the costs of these proposals – either to the Joint Applicants or to District customers. The Commission should reject these additional proposed Merger conditions. *See, e.g.*, OPC (2E) at 6:9-29 (Morgan); DC Sun (A) at 43: 3-18 (Schoolman).

912 Joint Applicants' Br. at 115.

913 Joint Applicants' Br. at 115.

914 Joint Applicants' Br. at 115-116.

wholesale generation assets owned by Exelon.[915] The Joint Applicants add that, while OPC witness Morgan quoted a few excerpts from an early draft of an Exelon strategic plan in an attempt to support his allegations that Exelon opposed distributed generation, he then highlighted only a single sentence from Exelon's final strategic plan – ignoring entire sections which discussed Exelon's belief that distributed generation can provide a great deal of value for both Exelon and its customers.[916]

307. The Joint Applicants submit that, to the extent the Commission believes that such issues as the expired federal wind PTC or Exelon's views of legislation in other jurisdictions nevertheless have relevance to its consideration of this Merger, an examination of the evidence regarding Exelon positions on such issues demonstrates the reasonable bases for Exelon's views, as well as support from other stakeholders and experts. The Joint Applicants then proceeded to explain Exelon's views with regard to the Federal Wind Production Tax, the Maryland RPS and Community Solar Legislation, and the New York "Reforming the Energy Vision" ("New York REV") proceeding to counter attacks by several parties that its views reflected animosity towards renewable energy and sustainability.[917] The Joint Applicants also refuted MAREC witness Burcat's assertions that Exelon was hypocritically looking for a market subsidy for nuclear generation for its Ginna nuclear plant in New York and for nuclear plants in Illinois while opposing subsidies for renewables.[918] The Joint Applicants also allege that other witnesses raising concerns about Exelon's interest in, and support for, microgrids, customer data transparency, and smart grid technologies ignored actual programs in these areas at Exelon utilities in their testimony.[919]

308. The Joint Applicants submit that Exelon's leadership in each of these areas is well established and recognized. Moreover, in the area of energy efficiency, Exelon fully understands that the District's approach to designing, managing and funding energy efficiency programs through the SEU is different from the legal frameworks in the other states in which Exelon utilities operate.[920] The Joint Applicants assert that Exelon is committed to working closely with the SEU upon approval of the Merger to ensure that the experience of Exelon utilities in the

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[915] Joint Applicants' Br. at 116-117, citing Tr. at 3559:2-3560:21 (Schoolman Cross).

[916] Joint Applicants' Br. at 117, citing OPC (2E) at 6:9-29 (Morgan); Tr. at 2184:9-2188:21 (Morgan Cross). Exelon's final strategic plan is attached to Mr. Morgan's Supp. Direct Testimony, and contains an extensive discussion of Exelon's views on distributed generation. *See* Confidential OPC (2E)-5 at 32-34 of 36.

[917] Joint Applicants' Br. at 118-120.

[918] Joint Applicants' Br. at 120-121.

[919] Joint Applicants' Br. at 121-122, referencing District Government (G) at 8:1-4 (Chambers) (stating DGS is "heavily invested in the smart grid "and "does not know what type of partner the Joint Applicants will be" without any discussion of Exelon smart meter deployment or $1.2 million U.S. Department of Energy award to ComEd for microgrid controller development described by Mr. Gould); District Government (E) at 19:10-23 (Shane); Tr. at 3093:3-94:14 (Shane Cross) (discussing Pepco provision of data to customers participating in energy performance disclosure programs as "example of good collaboration" by Pepco in Direct Testimony but only discussing participation by Exelon utilities ComEd and PECO on cross-examination).

[920] Joint Applicants' Br. at 122.

development and implementation of energy efficiency programs is also available to the SEU for its development and administration of energy efficiency programs consistent with its statutory responsibilities.[921] The Joint Applicants also reference the testimony of their witness, Mr. Gould, to explain how Exelon's comprehensive sustainability experience and commitment will benefit the District.[922] The Joint Applicants conclude that the evidence relating to Factor No. 7 demonstrably establishes substantial benefits of the Merger for District customers and will help the District achieve compliance with its RPS and future sustainability initiatives.[923]

309. The Joint Applicants indicate that, consistent with the multi-party settlement agreement in Maryland, the Merger will ensure that part of the Green Sustainability Fund will be available to directly support and promote investment in District of Columbia sustainability projects, including solar and other renewable resources. As originally agreed to in the Maryland settlement, the portion of the Green Sustainability Fund allocable to the District of Columbia was \$7.1 million. The Maryland Order approving the Merger reduced the amount of the Fund allocable to Maryland from \$19.8 million to \$14 million but added an additional 5 MW of renewable generation to be developed by Exelon. As revised, the proportional share of the Green Sustainability Fund that would flow to the District of Columbia would be \$5.2 million together with 2 MW of solar or other renewable resources. Since the Joint Applicants initially offered the former option, the Commission can elect either the original \$7.1 million Green Sustainability Fund or \$5.2 million in the Green Sustainability Fund plus 2 MW of solar and other renewable resources.[924]

<u>Summary of OPC and Intervenors' Position Pertaining to Factor No. 7</u>

310. OPC asserts that Public Interest Factor No. 7 is one of the most significant points of focus for the Commission in this proceeding.[925] OPC submits that major environmental concerns, such as greenhouse gas emissions from conventional fossil fuel energy sources and climate change, have forced society to rethink the way we produce and consume energy.[926] In response to these concerns, OPC states that the District has made significant progress in addressing these pressing issues through the collaborative effort of dedicated citizens, energy stakeholders, and government officials who want to protect the environment and reshape the District's energy future.[927] OPC submits that over the past decade, several pieces of legislation have been adopted and implemented that have positioned the District of Columbia at the forefront of national leadership in the area of sustainability, renewable energy generation and

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921 Joint Applicants' Br. at 122.

922 Joint Applicants' Br. at 122, citing Joint Applicants (3I) at 23:4-15 (Gould).

923 Joint Applicants' Br. at 123.

924 Joint Applicants' R.Br. at 99.

925 OPC's Br. at 121.

926 OPC's Br. at 121.

927 OPC's Br. at 121.

distributed generation.[928] Therefore, OPC argues that this transaction presents a pivotal moment for the Commission, as the decision in this case will determine how the District's electric infrastructure will evolve and will impact District residents for generations to come.[929]

311. OPC asserts that after careful consideration of the Joint Application and testimony concerning Public Interest Factor No. 7, as well as the evidence adduced at the evidentiary hearing, OPC has reached two conclusions.[930] First, OPC argues that the issues covered by Public Interest Factor No. 7 are so important, the proposed transaction as a whole cannot be deemed to be in the public interest unless the Commission finds net benefits on this specific factor.[931] Second, OPC argues that there is no substantial record evidence that would support a finding that the proposed transaction is in the public interest with respect to the conservation of natural resources and the preservation of environmental quality.[932] In short, OPC submits that the Joint Applicants' proposed transaction fails to meet the Commission's evidentiary standard based upon its interpretation of D.C. Code § 34-504 with respect to this key issue.[933] OPC adds that Exelon's corporate philosophy regarding renewable energy generation and distributed generation is not consistent with the District's vision for locally generated renewable energy and environmental quality.[934]

312. OPC argues that as the proponent of the proposed transaction, the Joint Applicants are required to present evidence that the transaction will leave the District of Columbia and ratepayers better off than they would be absent the transaction *(i.e.*, the transaction must result in net, direct, traceable, financial benefits).[935] OPC states that contrary to the Joint Applicants' claim that the transaction would enhance environmental quality in the District; substantial record evidence demonstrates that the proposed transaction would not leave the City

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928 OPC's Br. at 121 n. 437, wherein OPC cites example, the Renewable Energy Portfolio Standard of 2004, D.C. Code § 34-1431.0 to 34-1431.10 (2012); the Clean and Affordable Energy Act of2008, D.C. Law 17-250 (codified in scattered sections of§ 8 of the D.C. Code, among others); the Distributed Generation Amendment Act of 2011 , D.C. Code § 34-1432 to 34-1436 (2012); the Sustainable DC Amendment Act of2012, D.C. Law 19-262 (codified in scattered sections of§ 8 of the D.C. Code, among others); the Community Renewable Energy Amendment Act of2013, D.C. Law 20-47 (codified in scattered sections of § 34 of the D.C. Code); and the Sustainable DC Omnibus Amendment Act of 2014, D.C. Law 20-142 (codified in scattered sections of § 8 of the D.C. Code, among others).

929 OPC's Br. at 121.

930 OPC's Br. at 122.

931 OPC's Br. at 122.

932 OPC's Br. at 122.

933 OPC's Br. at 122.

934 OPC's Br. at 122.

935 OPC's Br. at 122.

and ratepayers better off and would not provide a benefit to the District's efforts to deploy renewable energy generation.[936]

313. OPC asserts that Joint Applicants witness Gould speaks exhaustively about Exelon's achievements in the area of energy efficiency, but he offers little to nothing in the way of proof that the transaction will benefit the District's efforts in terms of renewable energy and distributed generation.[937] Specifically, OPC claims that Mr. Gould's testimony did not present any ideas or proposals that would advance – or even merely comply with – the significant and hard-fought policies that stakeholders have established to make renewable energy and distributed generation available and affordable throughout the District of Columbia.[938] In fact, according to OPC, the Joint Applicants witness Tierney – the only witness who attempted to quantify the benefits of the proposed transaction on the Joint Applicants' behalf – explained that the extent of the Joint Applicants' proposal on Pubic Interest Factor No. 7 was a solar-financing provision from a pending *(i.e.*, not yet approved) settlement in Maryland and the potential for the Commission to deploy the CIF in a manner that addresses Public Interest Factor No. 7.[939] In this manner, OPC contends that the Joint Applicants have not adequately responded to Public Interest Factor No. 7, nor have they provided any evidence to support their claim that the transaction will enhance environmental quality in the District.[940]

314. OPC submits that similar to the important issues surrounding reliability, Public Interest Factor No. 7 is so significant that the Joint Applicants' failure to demonstrate benefits on this particular Factor should compel a finding that the transaction as a whole is not in the public interest.[941] OPC also submits that the Commission should not feel compelled to fashion a set of conditions to fill the Joint Applicants' void for this Factor nor should any weight be given to proposals the Joint Applicants may introduce during the briefing stage of this proceeding.[942] OPC argues, instead, that the Commission should note this deficiency along with the other shortcomings included in this brief as a basis for denying the proposed transaction.[943]

315. OPC maintains that Pepco, unlike Exelon, does not have this inherent conflict because Pepco does not own generation plants and is therefore not focused on the impact the implementation of distributed generation will have on its revenues.[944] OPC argues that this

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936 OPC's Br. at 122.

937 OPC's Br. at 123.

938 OPC's Br. at 123.

939 OPC's Br. at 123, citing Tr. at 2268:9-17 (Tierney).

940 OPC's Br. at 123.

941 OPC's Br. at 125.

942 OPC's Br. at 125.

943 OPC's Br. at 125.

944 OPC's Br. at 127.

distinction is important to the District as the Commission recently announced that it was going to establish a proceeding similar to the New York REV here in the District "to address in a more global way the future outlook for energy growth in the District, the feasibility of deploying more energy storage facilities and increased distribution generation, and the impact of these new technologies on Pepco's load forecasting and construction plans for the city."[945] OPC asserts that the decisions that come out of that future proceeding will determine how the District's electric infrastructure will operate and will define a number of policies that will impact the manner in which consumers use and produce energy.[946] OPC adds that, if the Commission approves this transaction, there is substantial evidence to support a finding that Exelon's dominant corporate priority of revenue generation from nuclear energy will crowd out established District policies that benefit consumers, leaving the District and its electric future at a disadvantage.[947] Therefore, OPC submits Exelon is not the right utility partner for the District as many of the achieved sustainability gains stand to be compromised. OPC declares that in the absence of an affirmative proposal to offset these concerns, the proposed transaction cannot meet the public interest standard.[948]

316. **AOBA.** AOBA submits that the Joint Applicants commit to support and promote energy efficiency and demand response programs. However, AOBA adds, in the District, energy efficiency programs are the responsibility of the SEU, which is funded through ratepayer assessments.[949] AOBA states that what Pepco or Exelon would do to *"support and promote"* energy efficiency is at best unclear. Based on the testimony of Joint Applicants witnesses McGowan and Gould, AOBA argues that Exelon's intent is to work closely with the SEU to ensure that Exelon's experience in the area of energy efficiency is available to the SEU. However at the time of hearings in this proceeding, roughly eleven months following the announcement of the Proposed Merger, AOBA contends that there is no evidence that Exelon has had any substantive discussions with SEU representatives regarding opportunities for Exelon and/or Pepco to participate in the SEU's energy efficiency programs.[950]

317. AOBA asserts that, although the testimony of Joint Applicants witness Tierney includes a scenario under which CIF dollars would be used for funding energy efficiency programs, increased funding of energy efficiency programs is not a Proposed Merger-related commitment of the Joint Applicants in this proceeding.[951] AOBA declares that the scenario that

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945 OPC's Br. at 127-128, citing *Formal Case No. 1123*, *In the Matter of the Potomac Electric Power Company's Notice to Construct a 230 kV/138 kV/13 kV Substation and Four 230 kV/138 kV Underground Transmission Circuits on Buzzard Point*, Order No. 17851, ¶ 78, rel. April 9, 2015 (emphasis added).

946 OPC's Br. at 128.

947 OPC's Br. at 128.

948 OPC's Br. at 128.

949 AOBA's Br. at 89.

950 AOBA's Br. at 89, citing Joint Applicants (3L) at 19:11-18, 20:12-21 (McGowan); and Tr. at 2997-2998.

951 AOBA's Br. at 89.

Ms. Tierney presents is simply a hypothetical example of a possible use of the CIF dollars the Joint Applicants have offered to the District, and according to the Joint Applicants, all decisions regarding the manner in which CIF dollars would be used will be left to the Commission.

318. AOBA asserts that with respect to demand response, Pepco currently has only one demand response program, the residential "Kilowatchers" program.[952] AOBA contends that the Joint Applicants propose no modifications or expansion of that program or the promotion of that program, and they do not propose any new demand response programs, and in support of that contention refers to Joint Applicants witness Crane's response to questioning by Chairperson Kane that the Joint Applicants are not committing to anything in the area of demand response that Pepco is not already required to do.[953]

319. **District Government.** The District Government submits that, so far as it has been able to determine, the Joint Applicants propose nothing at all with respect to the conservation of natural resources and the preservation of environmental quality.[954] The District Government states that the record in this case shows Exelon to be poorly suited to cooperate in the implementation of District public policy concerning the conservation of natural resources and the preservation of environmental quality, while PHI presents no such obstacles.[955] In support of this assertion, the District Government points out that Pepco owns no generation, and therefore, confronts no inherent conflict between its business interests and promoting equitable access to the distribution system for local renewable resources.[956] While Exelon owns approximately 22,845 MW of nameplate generating capacity in 14 nuclear generating stations located in Illinois, New Jersey, New York and Pennsylvania; approximately 10,000 MW of fossil fuel generating capacity; and approximately 1,400 MW of various types of renewable generation,[957] the District Government declares that only ten (10) MW of the Exelon-owned renewable generation is located within areas in which an Exelon affiliate also owns the electric distribution system, which following the Merger would include the District.[958] Although various Exelon affiliates hold contractual interests in distributed renewable generation, the District Government claims that most of that generation is also located in areas where Exelon affiliates do not own the

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952 AOBA's Br. at 90.

953 AOBA's Br. at 90-91, citing Tr. at 522:21-523:18.

954 District Government's Br. at 41, citing *Formal Case No. 1119*, Order No. 17597, rel. August 22, 2014 ¶¶ 115-116, 124. *See also*, D.C. Code § 34-808.02 (2015).

955 District Government's Br. at 41, n. 91, wherein the District Government states that the record also offers numerous examples of Exelon's resistance, at both regulatory and legislative levels, to integration of renewable and distributed generation that it does not own or control. *See, e.g.* District Government Confidential Cross Examination Exhibit No. 13 at Bates page EXC-PHI-MD 031004; District Government Confidential Cross Examination Exhibit No. 14 at 80; District Government Confidential Cross Examination Exhibit No. 18; District Government Confidential Cross Examination Exhibit No. 37.

956 District Government's Br. at 41.

957 District Government's Br. at 41.

958 District Government's Br. at 41.

distribution system.[959] According to the District Government, the District has a strong and settled public policy favoring renewables and distributed generation and that Exelon's business model and philosophy are likely to prove fundamentally incompatible with the implementation of that policy.[960]

320. **DC SUN.** DC SUN submits that Exelon's overriding financial interest in protecting its merchant nuclear generation cannot be reconciled with bedrock District policies or with the interests of all electric customers in lower rates, better reliability, greater system resilience, and more sustainable energy.[961] DC SUN claims that, by statute, conservation of natural resources and preservation of environmental quality are on a par with public safety and the economy of the District as factors the Commission must consider in accordance with the Clean and Affordable Energy Act ("CAEA").[962] DC SUN states that the District's policy makers have adopted sustainable energy principles as a linchpin for the city's growth and prosperity.[963]

321. In addition to the renewable energy requirements set forth in the CAEA, DC SUN emphasizes that the Council affirmed its commitment in this regard by bolstering the District's RPS, including the local solar component, through passage of the Distributed Generation Amendment Act of 2011 ("DGAA").[964] DC SUN declares that on one hand the CAEA increased the alternative compliance payments that energy suppliers must furnish for failure to meet the solar carve-out in their RPS requirements, thus creating an effective incentive for suppliers to acquire the required levels of solar energy[965] and providing a robust market for solar renewable energy credits ("SRECs") that solar customers can sell to offset the capital costs of solar installations.[966] DC SUN submits that the CAEA's and DGAA's targeted support for localized

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959 District Government's Br. at 41, citing Tr. at 305:8-327:10 (Crane); District Government Cross Examination Exhibit No. 36.

960 District Government's Br. at 42.

961 DC SUN's Br. at 2.

962 DC SUN's Br. at 12, citing D.C. Code § 34-808.02 (2015).

963 DC SUN's Br. at 14, citing DC SUN (A)-3 at 56 (Schoolman).

964 DC SUN's Br. at 15-16, citing Clean and Affordable Energy Act of 2008, D.C. Law 17-250, § 301 (b) (codified as amended at D.C. Code § 34-1432 (c)(13) (2013 Repl.)), 55 D.C. Reg. 9225 (2008) (requiring 20% of energy to come from tier one renewable sources by 2020, not less than .4% from solar energy); District of Columbia Distributed Generation Amendment Act of 2011, D.C. Law 19-36, § 2 (a) (codified at D.C. Code § 34-1432 (c) (13) (2013 Repl.)), 55 D.C. Reg. 6837 (2011) (requiring 2.5% of energy to come from solar); *see* DC SUN (A) at 10:13-11:6 (Schoolman).

965 DC SUN's Br. at 16, citing DC SUN (A) at 13:15-14:6 (Schoolman) (CAEA doubled the alternative compliance payments for each Tier 1 renewable energy credit shortfall from $0.025 kWh to $0.050 kWh and increased the payments for each SREC shortfall from $0.30 kWh to $0.50 kWh. Further underscoring the central role of local distributed solar generation, energy suppliers could only meet the solar RPS requirement by purchasing SRECs from District of Columbia solar energy systems.).

966 DC SUN's Br. at 16, citing DC SUN (A) at 23:4-12 (Schoolman).

distributed solar generation through carefully tailored incentives and mandates clearly reflects the District's determination that local distributed solar generation is an indispensable part of its renewable initiatives and policies.[967]

322. DC SUN also submits that the District subscribes unequivocally to net metering for residential-scale distributed solar generation.[968] For the last decade, DC SUN claims that it has been undisputed that, at least for smaller distributed generation installations, any moment-to-moment excess energy that the customer produces will be credited to the customer at the full retail rate, including energy, distribution, and transmission.[969] DC SUN argues that this policy lowers customers' costs by ensuring that they get credit for all of the power they produce and makes solar a reasonable alternative.[970]

323. DC SUN submits that the District reaffirmed its commitment to distributed solar generation with its enactment of the Community Renewable Energy Act of 2013 ("CREA"), which removed many of the remaining obstacles to the smooth implementation of solar by operationalizing "virtual" net metering in the District.[971] DC SUN asserts that the CREA has four central pillars that are designed to extend the reach of distributed generation within the District.[972] DC SUN represents that the CREA also cleared many roadblocks to distributed solar generation and is only the most recent legislative addition to the District's robust renewables policy framework.[973] It points out that the District has taken a firm stance on the status of renewables in meeting its energy consumption needs, and distributed solar generation is an indispensable part of the District's vision.[974]

324. According to DC SUN, the enactment of CAEA, DGAA, and CREA, coupled with implementation of the Sustainable DC Plan, has created a firm, tightly knit structure in the

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967 DC SUN's Br. at 16-17.

968 DC SUN's Br. at 17.

969 DC SUN's Br. at 17, citing *Formal Case No. 945*, Notice of Final Rule Making, 55 D.C. Reg. 1327-1331 (February 8, 2008) (amending Chapter 9 of Title 15 DCMR to establish policies and procedures to implement net energy metering); 15 DCMR § 903-5 (2015) (providing that "a customer-generator with an electric generating facility that has a capacity less than or equal to 100 kilowatts, if the electricity generated during the billing period by the customer-generator's facility exceeds the customer-generator's kWh usage during the billing period (excess generation), the customer-generator's next bill will also be credited for the excess generation at the full retail rate for transmission and distribution service").

970 DC SUN's Br. at 17, citing DC SUN (A) at 23:13-19 (Schoolman).

971 DC SUN's Br. at 17, citing DC SUN (A) at 15:18-16:4 (Schoolman); D.C. Law 20-47, *Community Renewable Energy Amendment Act of 2013*, D.C. Law 20-47, 60 D.C. Reg. 15138 (2013); *see* Tr. at 849:16-850:3 (Pepco did not oppose the Community Solar legislation in the District and participated in a working group to shape the final outcome).

972 DC SUN's Br. at 17-18, citing DC SUN (A) at 16:10-18 (Schoolman).

973 DC SUN's Br. at 18.

974 DC SUN's Br. at 18.

District that has woven local distributed solar generation into the fabric of the District's approach to the conservation of natural resources and the preservation of environmental quality. DC SUN believes that the District and its residents, through the vehicle of local distributed solar generation, are well on their way to fulfilling a comprehensive vision of sustainability, and the Commission should not condone any action that would risk unraveling years of legislative work and collaboration.[975]

325. DC SUN submits that Exelon has made no commitments that would assist the District in promoting its distributed generation policies or that would provide a benefit with respect to conservation of natural resources or preservation of environmental quality.[976] DC SUN adds that nothing in this evidentiary record identifies any tangible environmental benefit to the District from the proposed acquisition.[977] Despite the District's unequivocal support for distributed solar generation and sustainability, DC SUN contends that Exelon ignores those topics entirely in its commitments or offers only meaningless bromides in the place of genuine promises.[978] DC SUN states that, at best, Exelon proposes to maintain the status quo with respect to Public Interest Factor No. 7. DC SUN adds that the Commission cannot rely on Exelon's track record or its dissemination of "best practices" among its utilities because Exelon's performance on environmental metrics does not match Pepco's. In short, DC SUN believes that Exelon brings nothing to the District in this acquisition, and will likely backslide from the progress Pepco has made in protecting the environment.[979]

326. In line with other intervenors, DC SUN argues that the Joint Applicants' witnesses identified only two of these commitments that relate to conservation of natural resources or preservation of environmental quality.[980] DC SUN contends that neither of these "commitments" has any substance.[981] First, DC SUN submits that with respect to Commitment

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975 DC SUN's Br. at 19.

976 DC SUN's Br. at 36.

977 DC SUN's Br. at 36, citing n. 150 wherein DC SUN states, to the extent that Exelon relies on its development of renewables in jurisdictions where it does not own a distribution utility (*see* Joint Applicants (3I) at 3:22-5:13 (Gould); Joint Applicants (3I)-1; Tr. at 1551:1-1552:18 (Gould) (identifying jurisdictions where Exelon claims some renewable facilities but does now own a utility)) or on its extensive fleet of low-carbon emission nuclear plants (*see* Joint Applicants (2I) at 6:3-14(Gould)), any purported benefits to the District are illusory. All of those generation facilities will continue to exist and continue their contributions to conservation of natural resources or preservation of environmental quality regardless of whether Exelon acquires Pepco. The District receives no incremental benefit from the proposed transaction that it would not continue to receive even if the Commission denies the Application.

978 DC SUN's Br. at 36.

979 DC SUN's Br. at 36.

980 DC SUN's Br. at 36, citing Tr. at 442:4-14, 445:20-446:6 (Crane), and citing Joint Applicants' (4A)-2 at 1, Commitment 6, at 4, Commitment 23.

981 DC SUN's Br. at 37 n. 155 wherein DC SUN states "Dr. Tierney did not know whether the Joint Applicants are proposing that the acquisition will create a benefit under Public Interest Factor [No.] 7 or whether they are representing that there is no harm with respect to this Factor. Tierney, Tr. at 2279, lines 9-15. If the Joint

6 and the Customer Investment Fund, Mr. Crane acknowledged that the Joint Applicants have only *suggested* potential uses for the Fund, but it "is not a commitment." [982] DC SUN also maintains that without deciding on a possible allocation of the Fund among the many competing demands – and the evidentiary record contains no basis for any apportionment – there is zero quantifiable benefit for the environment. Thus, DC SUN declares that this "commitment" is illusory as it relates specifically to Public Interest Factor No. 7.[983] Second, according to DC SUN, Commitment 23 is equally disingenuous. DC SUN submits that because the commitment is only to "maintain and promote" the "existing" programs that Pepco is already implementing, by definition, there can be no benefit to customers from the acquisition.[984] DC SUN states that as Joint Applicants witness Mr. Rigby admitted, "they're really aren't any" Pepco-sponsored energy efficiency programs, "[s]o maintaining those programs is really not providing any benefit . . ."[985] Additionally, DC SUN further states that with respect to demand response programs, as Mr. Crane conceded in response to the Chair, "these are commitments to obey the [Commission's] order. I mean it's a flash of the obvious that we're going to do that . . . [I]t does sound like we're overstating or stating something that's a flash of the obvious." [986] DC SUN notes that Mr. Rigby testified that Pepco will also maintain its existing energy efficiency and demand response programs pursuant to the Commission's orders without the merger, so there can be no benefit from this commitment.[987]

327. **GRID2.0.** Similar to other parties in this proceeding, Grid2.0 does not believe that Joint Applicants have adequately addressed Factor No. 7.[988] Moreover, GRID2.0 believes that Exelon's policies are diametrically opposed to the District's interests related to Factor No. 7.[989] GRID2.0 asserts that the Exelon acquisition of Pepco would leave District ratepayers worse

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Applicants are merely arguing that they will cause no harm, they have not met their burden with respect to this Factor, and the Application should be rejected, as a matter of law." Tr. at 2279:12-14 (Tierney).

982 DC SUN's Br. at 37, citing Tr. at 443:4-8 (Crane).

983 DC SUN's Br. at 37.

984 DC SUN's Br. at 38.

985 DC SUN's Br. at 39, citing Tr. at 818:6-819:1 (Rigby); *see* Tr. at 521:15-522:9 (Crane) (admitting in response to the Chair's questions that he was aware that energy efficiency programs in the District were run by the Sustainable Energy Utility, not by the utility, but that he was not aware that energy efficiency programs are determined by the Sustainable Energy Utility, not the Commission); Tr. at 3098:4-3099:7 (Shane) (the Sustainable Energy Utility, not the utility, develops the District's energy efficiency programs); OPC Cross Examination Exhibit No. 37 at 1 ("Pepco does not offer energy efficiency programs.").

986 DC SUN's Br. at 39, citing Tr. at 518:14-21, 520:2-8 (Crane).

987 DC SUN's Br. at 39, citing Tr. at 616:8-617:4 (Rigby) (agreeing that, on a stand-alone basis, it would be Pepco's intention to maintain the programs referenced in the Joint Applicants' Commitment 23); *see* Tr. at 523:6-11 (Crane) (Exelon was not committing to do anything in the area of demand response, energy efficiency or customer assistance that Pepco is not already required to do and would be required to do if there were no acquisition.).

988 GRID2.0's Br. at 25.

989 GRID2.0's Br. at 27, citing Tr. at 439:7-12, at 440:2-11 (Crane); OPC Cross Examination Exhibit No. 14 at 99, 106, and 107 of 178.

off in the protection of environmental quality and conservation of natural resources. GRID2.0 claims that this is a result of both conflicts of interest and motivations that are incompatible.[990] GRID2.0 contends that the advance of smart grid, in effect the adoption of technology that will permit and promote demand side management and distributed generation in DC leading to energy conservation and local generation of electricity, will be poorly served by the acquisition.[991] According to GRID2.0, if the acquisition proceeds, all evidence points to Exelon's corporate guiding principles – shown to be antithetical to the District's energy policies, as directing a retreat from the progress DC has made in shaping a clean and efficient energy future. Exelon's corporate "Guiding Principles are a smoking gun that institutionalizes the anti-efficiency and anti-renewable behavior demonstrated by Exelon and its subsidiaries."[992]

328. GRID2.0 argues that unless provisions can be incorporated into the proposal that establishes performance standards that ensure the new entity will meet DC goals for energy efficiency, use of renewable power, and design and investment into smart grid technology, and stipulates that the utility will be spun off into a separate entity should expressed conditions not be met within an established timeframe, then the request by the Joint Applicants should be denied.[993] Moreover, GRID2.0 asserts that the performance standards must also *specify* how Pepco's business plan will be modified to perform in accordance with maximum demand-side conservation and energy efficiency best practices.[994]

329. **MAREC.** MAREC submits that the District's commitment to renewable energy development is reflected in various statutes. In addition to the CAEA, MAREC points to the District's RPS, and MAREC submits that for the 2014 compliance year, electric suppliers must obtain at least 8% of their supply sold from Tier I resources, like wind, solar, geothermal, biomass, landfill gas, fuel cells, and 2.5% from Tier II resources, like hydropower and municipal solid waste. MAREC states that the solar set aside for 2014 is 0.60%. MAREC also states that the Tier I and solar requirements increase each year until 2020 when at least 20% of the supply sold must come from Tier I resources. MAREC states that the 20% requirement for Tier I will remain consistent until 2023. MAREC also states that the solar set aside will continue to increase until 2023 when it reaches 2.5%, and that the Tier II requirements will completely phase out after 2019.[995]

330. Notwithstanding the District's commitment to renewable and clean energy, MAREC argues that Exelon failed to propose any conditions to address Public Interest Factor No. 7. In support of this argument MAREC cites to the testimony of OPC witness Rick Morgan, who testified that the issues covered under that factor "involve an established of the District" and

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[990] GRID2.0's Br. at 28.

[991] GRID2.0's Br. at 28.

[992] GRID2.0's Br. at 28.

[993] GRID2.0's Br. at 29.

[994] GRID2.0's Br. at 29.

[995] MAREC Br. at 7, citing MAREC (A) at 6:22-7:14 (Burcat).

are "[p]arallel with net quantifiable financial benefits of ratepayers and incremental benefits on reliability performance" such that "approval of the [M]erger without an affirmative proposal from the JAs on these issues would not be in the public interest."[996] MAREC contends that even Exelon's own witnesses were challenged when asked to describe how the merger would address Public Interest Factor No. 7.[997] For example, MAREC claims that Dr. Tierney could not identify specific benefits offered to support Factor No. 7 but instead suggested that the Commission could, in its discretion, apply some of the monetary commitments for this purpose at its discretion.[998]

331. Similar to other parties, MAREC contends Exelon's failure to address Factor No. 7 is indicative of its lack of familiarity with the District's clean energy policies – which does not bode well for future compliance if the merger is approved.[999] MAREC represents that the record contains other evidence of Exelon's failure to "do its homework" to understand the District's clean energy landscape. For example, MAREC points to Joint Applicants witness Gould, who is responsible for Exelon's sustainability programs, but was not aware that the District is not subject to EPA's 111(d) Clean Power Plan program because there are no fossil fuel plants within its borders.[1000] MAREC further stresses that after being confronted with a lack of knowledge with respect to several District clean energy programs, Mr. Gould tried to justify Exelon's failure to gather information on these programs by stating that doing so in advance of the merger "would have been presumptuous."[1001] MAREC retorts however that, given Factor No. 7 requires Exelon to address the impact of the Proposed Merger on clean energy and natural resources, gathering information on the District's programs would not have been presumptuous, but prudent – not to mention a good faith showing of intent to comply in the future.[1002]

332. MAREC asserts that Exelon's failure to educate itself regarding the District's clean energy programs is one matter. However, MAREC emphasizes that the far greater danger posed by the merger is Exelon's open hostility to renewables, a policy stance that Exelon has adopted to protect its nuclear assets which are currently struggling to succeed in the competitive "free markets" that Exelon itself purports to endorse.[1003] MAREC argues that Exelon's entire strategic plan revolves around opposition to renewables and distributed generation because it conflicts with their business plan that involves creating a favorable economic environment for

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996 MAREC Br. at 8, citing OPC (2E) at 6 (Morgan).

997 MAREC Br. at 8.

998 MAREC Br. at 8, citing Tr. at 2270:4-16.

999 MAREC Br. at 9.

1000 MAREC Br. at 9, citing Tr. at 1594:1-15.

1001 MAREC Br. at 9, citing Tr. at 1516:7-1517:9.

1002 MAREC Br. at 9.

1003 MAREC Br. at 9.

nuclear generation.[1004] For this reason, MAREC argues that Exelon has made nuclear energy one of the centerpieces of its EPA Section 111(d) compliance program in other jurisdictions.[1005] However, MAREC maintains that this will not aid compliance with the District's renewable energy goals – as Exelon witness Gould conceded, nuclear power does not satisfy the District's RPS program.[1006]

333. **NCLC/NHT.** NCLC/NHT submitted related comments on energy efficiency and low-income ratepayers, which was summarized in paragraphs 63-65 under Public Interest Factor No. 1. Regarding Factor No. 7, NCLC/NHT contends that threshold questions can be raised as to whether CIF funds should be devoted to anything other than ratepayer credits, and why investments in energy efficiency or renewable energy should be considered.[1007] NCLC/NHT claims that that the answer is clear: allocating a portion of any CIF funds to programs that promote energy efficiency and renewable energy would help carry out the District's overall energy policies and help meet the requirements of Factor No. 7. NCLC/NHT argues that the CAEA[1008] and other policy initiatives make it abundantly clear that the District intends to be a leader in addressing the threats that climate change poses and, consistent with that goal, promoting energy efficiency and renewable energy.[1009] NCLC/NHT argues that the Commission should ensure that, in addition to providing immediate financial benefits, the CIF should provide for longer-term investments that strongly support the District's sustainability, energy efficiency and renewable energy goals.[1010] NCLC/NHT submits that the proposed CIF of $33.8 million provides the Commission with a unique opportunity to provide meaningful ratepayer credits, which are tangible and immediate - but also evanescent - as well as to direct investments to energy efficiency and renewable energy programs that will provide longer-term value and help the District meet its climate change and energy policy goals.[1011] NCLC/NHT concludes that between the CAEA itself and Factor No. 7, there are strong policy reasons why the Commission should allocate more than half of any CIF towards longer-term investments, and slightly less than half to immediate ratepayer credits.[1012]

Summary of Community Comments Pertaining to Factor No. 7

1004 MAREC Br. at 10, citing Tr. at 2192:16-2193:3 (Morgan).

1005 MAREC Br. at 10, citing Tr. at 188:11-19 (Crane) (testifying that nuclear power plants will meet carbon reduction requirements of proposed Illinois legislation).

1006 MAREC Br. at 10, referencing Tr. at 1591:20-22.

1007 NCLC/NHT Br. at 12.

1008 NCLC/NHT Br. at 12-13, citing D.C. Law 17-250.

1009 NCLC/NHT Br. at 13.

1010 NCLC/NHT Br. at 13.

1011 NCLC/NHT Br. at 15.

1012 NCLC/NHT Br. at 18.

334. Many community commenters, including 26 out of 42 Advisory Neighborhood Commissions, expressed pride in the District's progressive and innovative approaches to promoting renewable energy and expressed concern that these accomplishments will be undone if the merger is approved because of what they understand to be Exelon's opposition to the expansion of renewable energy generation. The Commission received hundreds of comments which read:

> The merger would also take us a step backwards on our progress towards renewables and efficiency. DC has made a significant commitment to our renewables and efficiency and Exelon won't meet them. The Mayor's Sustainability Plan has set the goals of increasing the use of renewable energy to make up to 50% of the District's energy supply, and cutting citywide energy use by 50% by 2032. However, Exelon's track record demonstrates that they are hostile to these goals, and highly unlikely to help the District achieve either of these goals. In fact Exelon has a history of fighting against renewable energy and efficiency at the state and national level. And there's no reason to think that they won't do the same in DC.

<u>Discussion Pertaining to Factor No. 7</u>

335. In Order No. 17597, the Commission added Factor 7 to evaluate the impact of the Proposed Merger on the "conservation of natural resources and the preservation of environmental quality," [1013] in accordance with the CAEA.[1014] As this is the first opportunity to review a merger using this factor, the Commission has been asked to provide a further explanation of how this factor will be assessed. With respect to the determination of the effect of the Merger on the "conservation of natural resources and preservation of environmental quality", several parties have suggested that the Commission should look at how the Proposed Merger will further the District's efforts to address climate change, environmental sustainability goals, energy reduction goals, rising energy costs and the preservation of the natural environment as these goals have been set out in the enactment of key legislation like the CAEA, DGAA, and CREA, coupled with implementation of the Sustainable DC Plan that was developed by the District Department of the Environment and released in 2013.[1015] We agree that these statutory

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[1013] D.C. Code § 34-808.02 provides that "In supervising and regulating utility or energy companies, the Commission shall consider the public safety, the economy of the District, the conservation of natural resources, and the preservation of environmental quality."

[1014] The Clean and Affordable Energy Act of 2008, D.C. Law 178-0250 ("CAEA") (October 22, 2008). The pertinent part of the CAEA for the purposes of this memo is the CAEA § 401 amending Section 8 of An Act Making appropriations to provide for the expenses of the government of the District of Columbia for the fiscal year ending June thirtieth, nineteen hundred and fourteen, and for other purposes, approved March 4, 1913 (37 Stat. 974; codified in scattered sections of the Title 34 of the District of Columbia Official Code) by adding a new paragraph (96A), which is now codified as D.C. Code § 34-808.02.

[1015] *See* District Government (G) at 3:3-7 (Shane).

and policy documents provide an appropriate framework against which to measure the effects of the Proposed Merger on conservation of natural resources and preservation of environmental quality in the District, given specific goals and objectives that the District has adopted.[1016]

336. The Joint Applicants argue that the Proposed Merger will have a beneficial effect on the conservation of natural resources and preservation of environmental quality in part because Exelon has made carbon-free nuclear energy that supports clean power production one of the centerpieces of its Clean Air Act Section 111(d) compliance program in other jurisdictions.[1017] We acknowledge that nuclear power has positive benefits over fossil fuels for the environment and the District's fuel mix contains about 30% nuclear power. The Commission also acknowledges that 81% of Exelon's total generation output comes from nuclear plants that support clean power production. At the same time, however, we note that the District is exempt from the requirement to produce a program complaint with Clean Air Act Section 111(d). Consequently, while nuclear power is beneficial as a source of clean power for the District, it has not been a primary focus of the sustainability concerns in the District. As Exelon witness Gould conceded, nuclear power does not satisfy the District's RPS program under the DGAA;[1018] nor can an increased use of nuclear power help the District satisfy its goal of obtaining 50% of its power from renewable sources by 2032.

337. The Joint Applicants also argue that Exelon and its subsidiaries have an impressive record in the support of renewable energy and distributed generation – two issues that are the focus of District legislation. They submit that this record provides further evidence that the proposed Merger would have a positive effect on environmental quality in response to Factor 7. The record evidence in this proceeding shows that Exelon is the eleventh largest producer of wind energy in the United States and continues to develop new wind projects across the country – including in areas where Exelon owns competing nuclear generation assets;[1019] that Exelon's subsidiary, Constellation New Energy, Inc., is the country's seventh largest developer of commercial distributed solar projects and the largest solar developer in Maryland;[1020] that Exelon-owned utilities have facilitated the interconnection of distributed generation systems, with thousands of customers for over 100 MW of distributed generation who are now

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1016 District Government's Br. at 41 n. 91 wherein District Government states that the record also offers numerous examples of Exelon's resistance, at both regulatory and legislative levels, to integration of renewable and distributed generation that it does not own or control. *See, e.g.* District Government Confidential Cross Examination Exhibit No. 13 at Bates page EXC-PHI-MD 031004; District Government Confidential Cross Examination Exhibit No. 14 at 80; District Government Confidential Cross Examination Exhibit No. 18; District Government Confidential Cross Examination Exhibit No. 37.

1017 Tr. at 188:11-19 (Crane) (testifying that nuclear power plants will meet carbon reduction requirements of proposed Illinois legislation).

1018 Tr. at 1591:20-22.

1019 Joint Applicants' Br. at 111, citing Joint Applicants (3I) at 4:10-14 (Gould); Tr. at 1559:6-21 (Gould Cross).

1020 Joint Applicants' Br. at 111, citing Joint Applicants (3I) at 4:15-19 (Gould); Tr. at 1541:7-13 (Gould Cross).

participating in net metering programs;[1021] and that BGE in Maryland approved 4,237 interconnection requests (and over 40 MW of nameplate net metering capacity) in 2014 alone. In addition, according to Joint Applicants witnesses Crane and Gould, Exelon has recognized that renewable energy and distributed generation are business elements that will continue to grow both within the Exelon generation mix and nationally. While acknowledging the fact that Exelon has a small but growing amount of renewable energy in its generation mix, several parties have criticized the Joint Applicants' Application for the lack of any substantive commitments focused on Pepco as the local distribution company and the support that could be expected to further the development of renewable energy and distribution generation on a going forward basis. These parties argue, and the record in this proceeding shows, that the Joint Applicants made no specific commitment to support the growth of distributed generation and the use of renewables within the District in its original or supplemental testimony with one exception. In a provision in the Maryland settlement, a separate Green Sustainability Fund was established for the PHI utilities, which included Pepco-DC; however, that provision was not accepted as submitted by the MD PSC and only formally introduced in the District as part of the Joint Applicants' Reply Brief as two different options – preventing parties from commenting on the offer.[1022] Besides the limited new proposal in the Reply Brief, the Joint Applicants simply committed to providing a CIF that could be used to fund energy efficiency or renewable energy efforts should the Commission so choose and Commitment No. 23, which says the Joint Applicants, will continue to maintain and support its current work on energy efficiency.[1023]

338. Regarding the Joint Applicants' commitments to "maintain and promote existing energy efficiency and demand response programs," Mr. Crane was unaware of the unique structure of the District's energy efficiency programs, with the SEU determining these programs under contract with the District Department of the Environment, not the Commission.[1024] When questioned about the CREA, and how such facilities were paid for, Mr. Crane stated, "[i]t was almost like a net metering provision."[1025] This prompted Chairman Kane to explain that this was incorrect and that it "was established so that there really was no subsidy that the price paid for the output of those facilities is the – it's a tariffed price, the same price at which the SOS provided would be buying electricity."[1026] In each of these instances, the Joint Applicants demonstrated a distinct lack of knowledge about important District energy policies. Each represents a management and funding mechanism that is very different from other jurisdictions. If the District's needs and programs were not heard and understood during this merger application process when Exelon executives are most focused on Pepco and the District, it raises

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1021 Joint Applicants' Br. at 112, citing Joint Applicants (3I) at 4:29-31 (Gould).

1022 *See* Joint Applicants' R.Br. at 99.

1023 Tr. at 520:2-11.

1024 Tr. at 521:3-527:8.

1025 Tr. at 527:3-13.

1026 Tr. at 527:14-20.

a question about whether the needs of the District will be properly addressed when the attention of Exelon management is focused elsewhere.

339. Many commenters have expressed a concern about the inherent conflict that a changing generation mix poses for the Joint Applicants because 81% of Exelon's total generation output comes from nuclear plants giving Exelon a "fiduciary responsibility to maximize profits for [its] generation business" and an incentive to pursue business practices to achieve that objective.[1027] They note that Exelon's investment in the nuclear market places its nuclear operations in competition with the District's efforts to promote renewables and distributed generation and with the generation of wind resources that can satisfy the District's RPS requirements. Testimony was given on the record and in community comments that the Joint Applicants have opposed efforts to expand generation from renewables through the use of expanded tax credits, net metering or other favorable tariff schemes. Exelon counters that it has a constitutional right to express its views and that the Commission should not consider these expressions when evaluating the Joint Applicants responses to Factor No. 7.

340. In assessing the impact of the Proposed Merger, we have looked to see whether the Application as amended, including the commitments set out in Joint Applicants (4A)-2 would produce a direct and traceable positive impact with regard to advancing the District's effort to improve environmental quality and sustainability and protect the environment. The record in this proceeding reveals that despite our designation of Factor 7 in response to both District legislation and active community encouragement, "[t]he Joint Applicants have not proposed any specific energy efficiency measures to be implemented in the District of Columbia. Rather, the Joint Applicants have stated that the CIF can be allocated at the Commission's discretion and could include energy efficiency measures."[1028] As for Commitment 23 in Exhibit (4A)-2, Joint Applicant witness Crane confirms that the Joint Applicants have not proposed any additional programs for the District of Columbia beyond what already exists.[1029] The record also reveals that Exelon has not specifically identified or quantified any incremental improvements the Proposed Merger will have on Exelon's, Pepco's or other subsidiary's renewable energy efforts, distributed energy efforts, and smart grid initiatives, and has not yet decided if and when such determination would be made.[1030]

341. While the Joint Applicants' Application does not contain any proposals that would be harmful to the District's efforts to protect the environment and promote sustainability, it does not contain any specific commitment(s) to enhance the District's existing programs for energy efficiency, sustainability and conservation which could be construed as a benefit. It should have been clear from the fact that the parties urged the Commission to add Factor No. 7

[1027] Tr. at 437:1-14 (Crane).

[1028] AOBA Cross Examination Exhibit No. 82 (Joint Applicants Response to AOBA DR 4-6).

[1029] Tr. 444:4-7 (Crane).

[1030] *See* OPC Cross Examination Exhibit No. 32 (Joint Applicants Response to OPC DR 13-2), OPC Cross Examination Exhibit No. 34 (Joint Applicants Response to OPC DR 13-4), and OPC Cross Examination Exhibit No. 35 (Joint Applicants Response to OPC DR 13-5).

in response to a statutory mandate that these were issues of importance to the District, its ratepayers, and the Commission. The lack of any commitments by the Joint Applicants for the advancement of the statutory and policy agendas that have been set in the District for the incorporation of a growing amount of renewables and distributed generation within our local distribution system, combined with Exelon's documented history of opposing certain programs that promote renewables, leaves us uneasy concerning the District's smooth transition to clean and green fuel sources if this Proposed Merger is approved. That transition will require a partner that is willing to make changes to the local distribution system to accommodate new generation sources. While the Joint Applicants have demonstrated that they have experience in renewable generation and have, through BGE, interconnected solar customers to its distribution system, they chose not to make any commitments related to incorporating renewables and distributed generation as part of the proposed transaction. The Commission does note the Joint Applicants acknowledge that the SEU runs energy efficiency programs in the District of Columbia, on which Pepco provides assistance, and Pepco has no direct operational responsibility for energy efficiency programs in the District of Columbia.[1031] However, the Joint Applicants offer to do nothing more than fund the CIF. The Commission finds no direct and tangible evidence of how, separate and apart from what could be funded with the CIF, this Proposed Merger advances the conservation of natural resources and the preservation of environmental quality in the District of Columbia. On balance, therefore, we are not persuaded that there has been a showing that the Proposed Merger would advance the conservation of natural resources and the preservation of environmental quality in the District of Columbia.

342. After considering the entire record evidence presented, the Commission concludes that the Proposed Merger would bring to the District a company that is knowledgeable and involved in renewable energy generation and that has at least one subsidiary, BGE, that is experienced in interconnecting renewable generating facilities to the distribution system which are benefits. But the record shows that Exelon has been less than enthusiastic about embracing distributed generation and has taken positions on net metering and community net metering programs that are contrary to programs that promote the use of renewable resources that have already been enacted into law in the District or that are reflected in the Sustainable DC policy adopted by the Mayor. The Commission has been urged to reject the Proposed Merger on these grounds alone but we decline to do so. The Joint Applicants have maintained that they have a Constitutional right to express a different opinion with respect to policy and legislative matters without being penalized for doing so. Our standard requires that we find that the District and its ratepayers would be benefited by the Proposed Merger not merely left unharmed. On the record in this proceeding, we cannot find that the District and its ratepayers would be benefited by having the Joint Applicants as a partner as the District moves forward to embrace a cleaner and greener environment and pursues its goals of having 50% renewable energy sources by 2032. For purposes of our evaluation, we consider the effect of the Proposed Merger on this factor to be neutral.

[1031] *See* OPC Cross Examination Exhibit No. 46 (Joint Applicants Response to OPC DR 14-38).

C. Assessment of Whether the Proposed Merger Taken as a Whole is in the Public Interest and Leaves the Public Benefited, and Not Just Unharmed

343. The Commission must consider whether the Proposed Merger, when taken as a whole, is in the public interest under D.C. Code §§ 34-504 and 34-1001 and leaves the public benefited and not just unharmed. We make our decision based on our review of the Application including the 91 Commitments filed by the Joint Applicant as part of their Supplemental Direct Testimony, the pre-filed testimony of all parties, the hearing record and the comments of interested persons and the effect of the Proposed Merger on the seven public interest factors.

344. Several parties have urged us to make the effect of the Proposed Merger on Public Interest Factor No. 7 controlling or to give it more weight than the other factors. We decline to do that. First, there is nothing in the language of D.C. Code § 34-808.02 that directs us to take that action.[1032] The statute reads:

> In supervising and regulating utility or energy companies, the Commission shall consider the public safety, the economy of the District, the conservation of natural resources, and the preservation of environmental quality.[1033]

Second, D.C. Code § 34-808.02 addressed more than Factor No. 7; it also directed the Commission to consider "the local economy," which we have done under Factor No. 1 and "public safety," which we have done under Factor No. 3.[1034] Consequently, we conclude there is no reason to make Factor No. 7 dispositive or controlling. Nor do we find every factor to be equally relevant and therefore to carry equal weight, in part because each merger is different and presents a variety of facts and circumstances and in part because the various factors themselves cover a range of issues and impacts. As explained in this Order, we have taken our findings about the effects that the Proposed Merger has on each factor and determined which ones produce a direct and tangible benefit to District ratepayers and the District rather than leave them merely unharmed. Our goal is to ensure that the transaction properly balances the interest of shareholders and investors with the interest of ratepayers and the community so that the benefits to the shareholders do not come at the expense of District ratepayers.

345. The Commission has determined that the proposed transaction would have a range of impacts on the seven public interest factors. We identified in our discussion of some of the sub-issues in Public Interest Factor 1 that there were several direct and tangible financial benefits of the Proposed Merger, including the $1.6 billion premium for the current PHI stockholders and the $33.75 million Customer Investment Fund, the specific use of which has yet to be determined. However, for the reasons we have set out in our discussions of the effects of the Proposed Merger on various aspects of Public Interest Factors Nos. 1, 2, 3, 4, 5 and 7, we

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1032 *See* D.C. Code § 34-808.02 (2014).

1033 D.C. Code § 34-808.02 (2014).

1034 *See Formal Case No. 1119,* Order No. 17597, ¶ 116, rel. August 22, 2014.

have concluded that the Proposed Merger has a number of mixed impacts on District ratepayers. We recognize that there may be beneficial or potentially beneficial effects for the local distribution company, and by extension District ratepayers, as a result of having access to greater financial resources from an experienced operator with a record of increasing the reliability of BGE post-merger by implementing certain best practices and a new Management Model. District ratepayers could potentially see rates that are lower than they otherwise would be if the promise of substantial synergy savings is realized, and the District's economy could be strengthened by 102 new union jobs, 50 transferred jobs from PES, an annual average of $1.6 million in charitable contribution to non-profits serving the District, and the retention of the PHI headquarters in the District. If each of these promises were to come to fruition, the public would indeed be benefited.

346. But the record of this proceeding confirms that there are harms or potential harms that come along with these benefits or potential benefits. Rates for District ratepayers will be increased by transition costs and costs to achieve the merger, including regulatory costs for the merger proceedings, before many of the synergy savings are realized. The ability of our local distribution company to act independently and control its own operations will be further curtailed as it is subjected to additional levels of managerial review, oversight and control. Our Commission will need to develop new regulatory procedures to monitor charges from two service companies, to make certain that all necessary information for regulatory purposes and proceedings are locally available and timely provided and to ensure that Pepco, in its roles as the local distribution company and the SOS Administrator, is not negatively impacted by its parent company's ownership of generation facilities. There is concern that the potential conflicts of interest inherent in Pepco's role and its parent company's policy positions and interests might inhibit our local distribution company from moving forward to embrace a cleaner and greener environment in the District and pursue its goals of having 50% renewable energy sources by 2032. This list of harms and potential harms, in our opinion, makes it difficult to conclude the Proposed Merger would benefit the District ratepayers and not merely leave them unharmed.

347. It is difficult to make a final decision about whether the Proposed Merger is in the public interest without taking into account, in some manner, the wishes of the public. In this case, a large component of the public, more than 3,200 interested persons, have made their opinions known to the Commission. While there was some support for the Proposed Merger from the public, the vast majority of the public expressed widespread public dissatisfaction with, and opposition to, the Proposed Merger. A majority of the local ANCs (*i.e.*, 26 out of 42) adopted resolutions against the Proposed Merger; and six of the thirteen Councilmembers provided written comments to the Commission in opposition to the Proposed Merger as submitted in the Joint Application. The Commission has reviewed and considered all of these public comments in our decision-making process, and we thank each person who submitted comments and/or testified at the community hearings for expressing their opinions in this case.

348. Exelon is a company with many positive attributes and a recent track record of bringing operational success to BGE; however the model that it has proposed for this merger as explained on this record further weakens Pepco as a company in control of its operations in the District as our local distribution company and is not one that is beneficial to District ratepayers or the District. Additionally, while the Joint Applicants throughout this case have attempted to minimize the corporate differences between Exelon on the one hand and PHI and Pepco on the

other, the record makes it clear that post-Merger, Exelon management intends to have a heavy hand in Pepco's operations and decision making. Given the well-publicized views of Exelon with respect to its opposition to certain tax credits to support renewable generation, parties in the proceeding and community commenters have questioned whether the Joint Applicants will be an enthusiastic partner to carry out policies and operations for a local distribution system with a greater amount of distributed generation. While this Commission has the authority to compel performance by utilities in support of District policies, recent experiences with DC PLUG and the Community Renewable Energy Act have demonstrated that a utility that is a partner in the District is vastly preferable to a utility that must be continually compelled to further important District goals. We are not persuaded by the record before us that the Joint Applicants will be the enthusiastic supporter and facilitator necessary to lead the District and its local distribution franchise in the future. Based on the foregoing, the evidence presented at the hearing, and the entire record in this matter, we conclude that the Proposed Merger, when taken as a whole, is not in the public interest because it does not benefit District ratepayers and the District rather than merely leave them unharmed.

D. Treatment of Conditions for the Proposed Merger

349. Our fellow Commissioner has argued that the Commission should have made additional efforts to craft conditions that could be added to the Joint Applicants' Application to approve this Proposed Merger. The Commission considered whether to adopt any of the various conditions proposed by OPC, the Intervenors and the public but has declined to do so. We note that the position taken by OPC and the Intervenors was to reject the Proposed Merger; but if the Proposed Merger was approved, then consider any of a number of conditions. Because the majority concluded that the Proposed Merger was not in the public interest and therefore should be rejected, there was no need to consider the conditions that were proposed by the parties and that had been objected to by the Joint Applicants.

350. Additionally, as we read the statute governing mergers and change of control proceedings, our role as a Commission is to determine whether the Proposed Merger that is presented to us is in the public interest. It is not our obligation to craft conditions to make a proposed transaction that does not satisfy our public interest standard into one that meets that statutory test. In this proceeding, Exelon had ample opportunity to submit a proposal that addresses the various weaknesses that were pointed out by parties and members of the public. Those opportunities have included: (1) the submission of numerous updates and clarifications to their Joint Application; (2) the submission of three additional rounds of testimony, on September 19, 2014, December 17, 2014, and February 18, 2015, since the filing of the Joint Application and its Direct Testimony on June 18, 2014; and (3) the presentation of live testimony on behalf of the Joint Applicants by twelve witnesses responding to OPC, Intervenor, and Commissioner questions regarding the Joint Application and adopting or accepting as evidence for the record numerous Data Responses and Cross Examination Exhibits. The Joint Applicants chose, instead, to present a proposal that, as OPC asserts, was "intended to get their foot in the door. At that point, the Joint Applicants seemed willing to roll the dice and accept whatever proposal the Commission is inclined to craft."[1035] Essentially, the Joint Applicants gambled that either the

[1035] OPC's Br. at 26.

parties to this proceeding would be willing to work with them to craft a proposed Settlement Agreement with conditions that the Commission would accept, as was the case in *Formal Case No. 1002* and in other jurisdictions where the Joint Applicants have sought approval of the Proposed Merger on behalf of other PHI companies, or that the Commission would, *sua sponte*, shore up any weaknesses in the Joint Application by adding terms and conditions of its own making -- something that our fellow commissioner promotes based on what was done in *Formal Case No. 951*.

351. The Commission said that each merger application is different and must be considered on its facts and circumstances. *Formal Case No. 951* was different from this Proposed Merger in several ways. First, that case involved two vertically integrated companies coming together to form a single merged company and took place before the electric market in the District of Columbia was restructured. It did not involve one parent company with distribution subsidiaries and no generation being acquired by another parent company with regulated and unregulated businesses. Consequently, the Commission was not faced with a proposed merger that raised a serious concern about Pepco's role within the management structure that was being proposed, as is the case here or had to deal with duplicate service companies that would make the Commission's oversight role more complex or that raised potential conflict of interest issues as a result of two different lines of business that are potentially in conflict. Second, the initial offer that was made in the merger application in *Formal Case No. 951* had a larger base of benefits for ratepayers. These benefits included a rate cap for two and half (2.5) years and four and half (4.5) years depending on the rate class. In any event, the applicants did not accept the conditions that the Commission crafted and the merger was not consummated

352. Furthermore, in this proceeding, the Joint Applicants have already argued against the Commission posing most of the conditions that our fellow commissioner lists in his dissent. For example, the Joint Applicants called the District Government's list of conditions "extraordinary and inappropriate on a number of levels;"[1036] and argued that, due to the existence of the "most favored nation" clauses in the Joint Applicants' settlements in New Jersey, Delaware, and Maryland, if the District Government's recommendations were implemented, then PHI-wide the total cost of the proposed transaction for the Joint Applicants would be between approximately $7.35 billion and $8.75 billion. Joint Applicants also opposed the Commission adopting any of the recommendations to increase the CIF for the District because it would be too costly on a PHI-wide basis as a result of "most favored nation clauses" that were incorporated into various settlement agreements. Similarly, Mr. Crane testified Exelon was not willing to make the boards of PHI and Pepco more "independent" because it "is simply not tenable given the nature of the transaction and the business in general. If these or similar conditions were attached to the Merger approval, I could not recommend to my board that I close the deal."[1037]

353. For the Commission to be obligated to establish conditions that would modify a merger application to make the resulting proposed transaction in the public interest, we would

[1036] Joint Applicants (3L) at 4:7-8 (McGowan).

[1037] Joint Applicants (3A) at 23-24 (Crane).

create a situation where every merger application would be found to be in the public interest merely because the Commission would be adding conditions that will make it so. That is not our obligation; nor is it in the best interest of the public for such a scenario to occur. The burden of persuasion to demonstrate that the proposed transaction is in the public interest and will benefit the public rather than merely leave them unharmed falls on the proponent seeking approval of the transaction. Until that threshold is met, the Commission is not required by our statute to determine and record the terms and conditions for the proposed transaction. Indeed, from a policy perspective, if the Commission were to take on the task of shoring up every proposal that it received, we would run the risk of undermining the public's confidence in the fairness of this review process. As OPC posits, "[i]n effect, it would allow the Joint Applicants in this case, and other applicants in the future, the ability (if not incentive) to present a flawed and deficient application for the Commission to fix and approve."[1038] The Commission has long expected applicants in the proceedings before it to meet the applicable legal standard by putting forward their best proposal and relying on the merits of that proposal. It is a tradition and a practice that is worth keeping.

V. FINDINGS OF FACT AND CONCLUSIONS OF LAW

A. Findings of Fact

354. Based on the foregoing, the evidence presented at the evidentiary hearing, and the entire record in this proceeding, the Commission makes the following findings:

A. On June 18, 2014, the Joint Applicants filed the Joint Application for approval by the Commission, pursuant to D.C. Code §§ 34-504 and 34-1001, for a change of control of Pepco to be effected by the Proposed Merger of PHI with Purple Acquisition Corp., a wholly owned subsidiary of Exelon.

B. PHI is the public utility holding company with headquarters in the District of Columbia, which, through its regulated subsidiaries, delivers electricity in the District of Columbia, Maryland, Delaware, and New Jersey.

C. Pepco is a wholly owned subsidiary of PHI and is the public utility regulated by this Commission pursuant to D.C. Code § 1-204.93 and D.C. Code § 34-101 *et seq.*

D. Exelon is a utilities services holding company with headquarters in Chicago, Illinois, which, through its subsidiaries, delivers electricity and natural gas to customers in Illinois, Pennsylvania and Maryland and generates electricity for sale throughout the United States.

E. Under the terms of the Merger Agreement entered into between Exelon, PHI and Merger Sub, PHI will merge with Merger Sub., and, as the surviving corporation,

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[1038] OPC's Br. at 27.

PHI will become an indirect, wholly owned subsidiary of Exelon and PHI's stock will no longer be publicly traded.

F. Merger Sub is a Delaware corporation and a wholly owned subsidiary of Exelon that was formed for the sole purpose of affecting the Proposed Merger.

G. Under the terms of the Proposed Merger Agreement, PHI will become the subsidiary of Special Purpose Entity ("SPE"), and SPE will be a subsidiary of EEDC, which owns Exelon's regulated public utility companies.

H. Upon completion of the Proposed Merger, PHI's subsidiaries, including Pepco, will operate as part of Exelon's holding company system.

I. The Proposed Merger is structured as an all-cash transaction for approximately $6.8 billion.

J. Upon consummation of the Proposed Merger, Exelon will purchase the stock of the PHI shareholders for the price of $27.25 per share; that share price represents a $1.6 billion stock acquisition premium.

K. The Proposed Merger Agreement provides for a $180 million reverse break-up fee whereby Exelon will purchase up to $180 million of non-voting preferred stock in PHI. Under certain conditions, PHI will retain the $180 million reverse break-up fee proceeds if the Proposed Merger does not close.

L. The Joint Applicants have made 91 commitments to the District of Columbia that are listed in Joint Applicants' (4A)-2.

M. The total Proposed Merger synergies, including both regulated and non-regulated affiliates, is $225 million over the first 5 years.

N. The Joint Applicants' original synergy study estimated that the net cost savings for PHI utility operating companies resulting from the Proposed Merger would approximate $92 million over the first five years.

O. The Joint Applicants created a Customer Investment Fund based on PHI's allocated amount of the anticipated synergy savings using the "Modified Massachusetts Formula," and then allocated a portion of that savings to each PHI utility operating company based on the ratio of that company's meter accounts to the total number of meter accounts in all PHI utility operating companies.

P. The initial Customer Investment Fund allocation to the District of Columbia based on a 5-year synergy savings of $100 million and the District's meter accounts was $14 million based on a 14 percent allocation.

Q. The Joint Applicants increased the District of Columbia Customer Investment Fund to $33.75 million following the Joint Applicants' settlement with the New

Jersey Board of Public Utilities and asserted that the amount was based on estimated total 10-year synergy savings for the District of $51 million.

R. There is no record evidence that establishes the 10-year synergy savings for all Exelon regulated and unregulated business or the amount of the synergies that is allocated to PHI.

S. The record evidence does not support the Joint Applicants' assertion that the $33.75 million Customer Investment Fund represents a net present value of 94% of the 10-year synergy savings.

T. The $33.75 million Customer Investment Fund for the District of Columbia represents the same $128 per customer meter calculation that was included in the New Jersey Settlement.

U. The Proposed Merger contains no commitment by the Joint Applicants to pass on 100% of allocable achieved synergy savings to Pepco-DC nor does it contain any documentation of the specific allocation factors that will be used to determine the District of Columbia's share of any future synergy savings that might be achieved.

V. Pepco's District of Columbia operations represent 23 percent of all PHI electric utility operating company sales, 25 percent of total rate base for all PHI utility operating companies, and 24 percent of net income for all PHI electric utility operating companies, in a system where almost all rates are volumetric.

W. The customer count number of 264,384 that was used by the Joint Applicants is lower than the District's actual meter count of 281,540, thereby lowering the initial percentage used to calculate the Customer Investment Fund for the District of Columbia.

X. Based on the actual number of meters in the District of Columbia, the direct and traceable financial benefit from the Customer Investment Fund per customer drops from $128 to approximately $120 per customer.

Y. The Joint Applicants have not included any new or incremental benefits for, or any specific provisions for assistance to, low-income customers in its application or its commitments.

Z. The record evidence contains no documentation of the specific allocation factors that will be used to determine the District of Columbia's share of any future synergy savings that might be achieved.

AA. The Joint Applicants estimate the total cost to achieve the Proposed Merger for Pepco-DC is $11 million, which includes the transition costs and regulatory support costs of the Proposed Merger.

BB. The estimated portion of the $15 million in total regulatory support costs included in transition costs attributed to Pepco-DC is less than $2 million.

CC. The fair market value of PHI was determined based on the totality of the circumstances by the PHI board of directors through a competitive bidding process. Ratepayer benefit was not considered as an element of the competitive bidding process for the purchaser of PHI.

DD. The record evidence does not clearly demonstrate that the Proposed Merger will add to Pepco's financial strength, nor does it show an immediate harm either.

EE. The immediate financial impact of the Proposed Merger on Pepco with respect to its cash flow after the Proposed Merger closes was not established on the record because the testimony was inconsistent.

FF. The Proposed Merger changes how Pepco will access capital. Decision will be as set out in the Delegation of Authority document.

GG. The Proposed Merger would result in Pepco competing with a larger pool of companies (*i.e.*, seven regulated distribution companies and Exelon's unregulated generation affiliates as compared to PHI's four regulated utilities) for additional investment dollars.

HH. Pepco's ability to use its net operating loss carry overs will be enhanced by the Proposed Merger to the benefit of District ratepayers; however the amount of the purported benefit has not been quantified on the record.

II. There would be no significant improvement in Pepco's credit ratings due to the Proposed Merger.

JJ. Pepco and PHI, as subsidiaries of Exelon, will be exposed to additional financial risks from the Proposed Merger due to Exelon's unregulated businesses.

KK. The Joint Applicants have proposed 45 ring-fencing commitments in Attachment 4(A)-2 to mitigate the financial risks from Exelon's unregulated businesses and provide a level of protection for PHI, Pepco and Pepco's ratepayers.

LL. The Joint Applicants have made a commitment to hire 102 new union workers for Pepco-DC; some unspecified number of the new union workers will replace existing workers and contractors; there is no commitment to include a certain number of District residents in the new hires.

MM. The cost to hire and train new workers at Pepco-DC who will be performing duties for the regulated company will be a ratepayer expense; any such expenses is a cost associated with the Proposed Merger

NN. The Joint Applicants have committed to transfer 50 employees from Pepco Energy Services in Arlington, Virginia to PHI Headquarters in the District. The transfer would provide some benefits to the District economy, especially if District residents are hired; however the record did not establish whether these would be long term positions.

OO. There are 257 positions at the PHI Service Company scheduled to be eliminated as part of the Proposed Merger.

PP. The Joint Applicants commit to ensure no net reduction in the employment levels at Pepco due to involuntary attrition resulting from the Proposed Merger integration for two years; in the New Jersey Settlement, the commitment for no net reduction is for a period of three to five years.

QQ. There is no commitment with respect to the retention of PHI's 586 employees who work in PHI's District of Columbia headquarters.

RR. Exelon and its subsidiaries commitment to donate an annual average of $1.6 million to charitable organizations located in the District or to organizations that support charitable activities that benefit District residents will benefit the District's economy.

SS. The charitable contribution dollar amount commitment is lower than the amount of Pepco-DC's 2014 charitable contributions of around $1.9 million; there is no record evidence of the amount of donations made separately by PHI.

TT. PHI is financially healthy as a standalone company and would continue to be so if the merger is not consummated.

UU. The PHI utilities will enhance Exelon's earnings picture for the future; this enhancement is a major reason for the acquisition.

VV. The credit rating agencies give similar ratings to Exelon, PHI and Pepco.

WW. Exelon will be able to use Pepco's net operating loss carry forward ("NOLCs") more quickly than PHI providing a benefit to District ratepayers; however the amount of the benefit has not been quantified on the record.

XX. The management structure included in the Proposed Merger organization places PHI, with its three utilities—Pepco, Delmarva Power, and ACE—as the fourth utility operating as an Exelon utility along with BGE, ComEd and PECO. Pepco and the other PHI subsidiaries will not be on the same level nor have full participation in the Exelon Utilities management meetings.

YY. Exelon's Delegation of Authority sets forth the hierarchy of decision makers based on set dollar amount thresholds for key management and policy decisions. There is minimal management and budget authority delegated to Pepco.

ZZ. After the Proposed Merger closes, Exelon Utilities CEO O'Brien will be involved in reviewing rate cases before filing in the District, thus adding an additional layer of management oversight in the decision to file a rate case.

AAA. The PHI Board of Directors proposed by the Joint Applicants will be decidedly less independent because it shifts from a majority of independent members pre-merger to a minority of independent members post-merger.

BBB. After the Proposed Merger is consummated, the Joint Applicants testified that David Velazquez would become the PHI CEO; however his appointment is not included in any commitment.

CCC. Exelon Utilities CEO O'Brien asserts that he would look to PHI CEO Velazquez to make most decisions, however, he notes that Exelon CEO Crane and Exelon Utilities CEO O'Brien may also make some decisions.

DDD. With respect to administrative operations, the Proposed Merger would result in Pepco being subject to both a new management model, and a second service company.

EEE. None of the current Exelon distribution companies operate within a separate holding company or in multiple jurisdictions.

FFF. The Proposed Merger retains the PHI Service Company while adding Exelon's service company to the mix.

GGG. The Joint Applicant's reliability performance offer is based on a three-year average rather than annual compliance as required under the Commission's EQSS; the use of an averaging method was rejected by the Commission when it established its EQSS.

HHH. In 2014, Pepco already exceeded the 2018 SAIDI EQSS target and the 2020 SAIFI EQSS target. There is no evidence that Pepco's reliability improvements and continued compliance with the EQSS would cease if the Proposed Merger is not approved and Pepco continued to operate on a stand-alone basis.

III. Reliability improvements resulting from DC PLUG cannot be considered products of, or benefits from, the Proposed Merger and must be excluded from Exelon's projections regarding merger-related reliability benefits.

JJJ. The 50 basis point reduction to the return on equity penalty commitment for failure to meet a 2018-2020 reliability performance average that would go into effect in the first rate proceeding after January 1, 2021 that was offered by the Joint Applicants provides little meaningful financial incentive to meet either the EQSS standards or Exelon's proposed standards after the Proposed Merger closes.

KKK. The Joint Applicants have proposed a spending cap commitment, but have conditioned Commitment 7 on there being no changes in law, regulations, or extreme weather events requiring increases in reliability-related spending to restore service and facilities or variations in the schedule of the DC PLUG that are outside of Pepco's control. However, the Joint Applicants have identified no criteria that would be used to determine when a delay in the DC PLUG construction schedule is outside Pepco's control.

LLL. The Joint Applicants have provided no meaningful details regarding the best practices that Exelon is offering to provide Pepco nor has it demonstrated the effects those best practices would have on public safety and the reliability of services if they were deployed or shown how the sharing of best practices will produce direct, traceable, or tangible benefits to D.C. customers.

MMM. Unlike in *Formal Case No. 951*, when Pepco was vertically integrated, the Commission's current ratemaking procedures do not consider inclusion of any costs from generating plants in the cost of service or the rate base of the local distribution company.

NNN. Credit agencies may take into account the business operations of an electric distribution company's parent and any steps that have been taken to protect a subsidiary company from any added risks from a parent's operations.

OOO. The Commission concludes that Exelon's ownership of additional non-jurisdictional business interests in general and its ownership of nuclear operations in particular, will have an impact on Pepco and could have a negative impact on District ratepayers, if the Proposed Merger is approved.

PPP. The Commission declines to find that the mere presence of the Joint Applicants' unregulated business to be a harm that cannot be mitigated.

QQQ. There is no way that losses incurred by Exelon's aging nuclear fleet would be included in the rate base of Pepco as a local distribution company. However, there is a possibility that Pepco's cost of capital could be affected if there were no ring-fencing provisions to assure investors that the finances of Pepco and PHI were separate from the obligations of Exelon.

RRR. The Joint Applicants' multiple commitments to implement numerous ring-fencing provisions would insulate Pepco and PHI from most, if not all, of the business risks associated with Exelon's non-regulated businesses and would provide a level of protection to District ratepayers in the event that Exelon's finances are placed in jeopardy by events that impact its unregulated businesses.

SSS. The Joint Applicant's commitment that seeks to delay access to the books and records of Pepco is not beneficial; delayed access to necessary books and records will negatively impact the Commission's ability to effectively carry out its oversight role.

TTT. It is undisputed on the record that both PHISCo and EBSC will allocate costs to Pepco; that PHISCo and EBSC each have their own cost allocation manual; and that the two companies use different methods of cost allocation.

UUU. The Joint Applicants provided no quantitative evidence to support the conclusion that District ratepayers could see a benefit because certain service company functions will be transferred from PHISCo to EBSC following the merger and would allow Pepco to "realize economies of scale and scope" if the Proposed Merger is approved nor did they quantify the cost decrease that Pepco could expect to receive under this scenario.

VVV. While the Proposed Merger would not, and cannot, change our regulatory oversight over Pepco, it would impact the manner in which the Commission's regulatory oversight is administered.

WWW. The Proposed Merger would make regulatory tasks more complex; more time-consuming and more costly by increasing the need for regulatory oversight, reporting and auditing to ensure that Pepco and District ratepayers are being allocated the correct costs.

XXX. Any concerns about the participation of the Joint Applicants in the SOS procurement process as both the SOS Administrator and a bidder can be adequately addressed by modifying the rules for the procurement procedures so that there could be no harm to District ratepayers under the wholesale SOS model adopted by this Commission. Consequently, on the SOS side, we conclude that the effect of the Proposed Merger would be to leave wholesale markets competition unharmed but with no noticeable benefits.

YYY. We agree that the District's efforts to address climate change, environmental sustainability goals, energy reduction goals, rising energy costs and the preservation of the natural environment as these goals have been set out in the enactment of key legislation like the CAEA, DGAA, and CREA, coupled with implementation of the Sustainable DC Plan that was developed by the Department of the Environment and released in 2013 provide an appropriate framework against which to measure the effects of the Proposed Merger on conservation of natural resources and preservation of environmental quality in the District, given specific goals and objectives that the District has adopted.

ZZZ. The Commission also acknowledges that 81% of Exelon's total generation output comes from nuclear plants that support clean power production.

AAAA. Nuclear power does not satisfy the District's RPS program under the DGAA;[1039] nor can an increased use of nuclear power help the District satisfy its goal of obtaining 50% of its power from renewable sources by 2032.

1039 Tr. at 1591:20-22.

BBBB. The Joint Applicants demonstrated a distinct lack of knowledge about important District energy policies.

CCCC. Exelon has not specifically identified or quantified any incremental improvements the Proposed Merger will have on Exelon's, Pepco's or other subsidiary's renewable energy efforts, distributed energy efforts, and smart grid initiatives, and has not yet decided if and when such determination would be made.

DDDD. The Commission finds no direct and tangible evidence of how, separate and apart from what could be funded with the CIF, this Proposed Merger advances the conservation of natural resources and the preservation of environmental quality in the District of Columbia.

EEEE. The Commission cannot find that the District and its ratepayers would be benefited by having the Joint Applicants as a partner as the District moves forward to embrace a cleaner and greener environment and pursues its goals of having 50% renewable energy sources by 2032.

B. Conclusions of Law

355. Based on the foregoing, the evidence presented at the evidentiary hearing, and the entire record in this proceeding, the Commission makes the following conclusions of law:

A. The Commission has jurisdiction to render a decision on the Joint Application's request for a change of control of Pepco.

B. The Commission has both express and implied statutory authority to review an application for authority to merge, and to set forth the terms and conditions upon which a merger may be approved or denied.

C. The Commission must consider whether the Proposed Merger, when taken as a whole, is in the public interest under D.C. Code §§ 34-504 and 34-1001 and leaves the public benefited and not just unharmed.

D. In determining whether a Proposed Merger is in the public interest, the Commission must (1) balance the interests of a utility's shareholders and investors with the interests of ratepayers and the community; (2) determine whether the benefits to the shareholders do or do not come at the expense of the ratepayers; and (3) determine whether the proposed merger produces a direct and tangible benefit to ratepayers.

E. The Joint Applicants, as the proponent of the order, bear the burden of persuasion. Thus, the Joint Applicants have the burden of convincing the Commission that the Proposed Merger is in the public interest under D.C. Code §§ 34-504 and 34-1001.

F. There is no reason to make Factor No. 7 dispositive or controlling under the CAEA. Nor do we find every factor to be equally relevant and therefore to carry equal weight, in part because each merger is different and presents a variety of facts and circumstances and in part because the various factors themselves cover a range of issues and impacts.

G. Unless the Proposed Merger is determined to be in the Public Interest, the Commission is not required by our statute to record the terms and conditions for the proposed transaction.

H. The Joint Applicants have not persuaded the Commission that taken as a whole, the Proposed Merger will benefit District ratepayers, and the District rather than merely leave them unharmed and, therefore, is in the public interest.

THEREFORE IT IS ORDERED THAT:

356. MAREC's Motion for Leave to File Post-Hearing Brief Two Days Out of Time is **GRANTED**;

357. MAREC's Initial Post Hearing Brief is **ACCEPTED**;

358. Because, taken as a whole, the Proposed Merger is not in the public interest, the Proposed Merger is **NOT APPROVED**;

359. The Joint Application filed by Exelon, Pepco Holdings, Inc., Pepco, Exelon Energy Delivery Company, LLC, and New Special Purpose Entity, LLC for a change of control of Pepco to be effected by the Proposed Merger of Pepco Holdings, Inc. with Purple Acquisition Corp., is, as filed, **DENIED** pursuant to D.C. Code §§ 34-504 and 34-1001.

A TRUE COPY: **BY DIRECTION OF THE COMMISSION:**

Brinda Westbrook-Sedgwick

CHIEF CLERK: **BRINDA WESTBROOK-SEDGWICK**
COMMISSION SECRETARY

PUBLIC SERVICE COMMISSION OF THE DISTRICT OF COLUMBIA
1325 G STREET, N.W., Suite 800
WASHINGTON, D.C. 20005

August 27, 2015

OPINION OF COMMISSIONER WILLIE L. PHILLIPS, CONCURRING, IN PART, AND DISSENTING, IN PART, FORMAL CASE NO. 1119, ORDER NO. 17947

I. INTRODUCTION

1. Today, I join the rationale articulated by the majority that the merger application as filed by the Joint Applicants is not in the public interest.[1040] I agree with the findings that the management structure proposed by the Joint Applicants could potentially harm ratepayers, and that the Customer Investment Fund ("CIF") is inadequate. However, the merger application should not be viewed in a vacuum. Instead, the merger deal must be viewed in a manner that considers the regulatory landscape of electric utilities and with a perspective that changes in innovation, technology, and the environment are transforming the electric industry. Therefore, I must respectfully concur, in part, and dissent, in part, from the majority opinion.

2. As utility regulators, our mission is to serve the public interest by ensuring that financially healthy utilities provide safe, reliable, and quality services at reasonable rates for the District of Columbia. In order to accomplish that mission, it is also our job to help bring certainty to a rapidly changing industry. Accordingly, I believe the Commission's evaluation of the proposed merger should have been a two-step process: 1) review of the proposed merger commitments; and 2) review of potential merger conditions.

3. Because it is the public interest that drives the Commission, the goal of a two-step process is not to guarantee approval, but to ensure that we give full consideration to all of the potential benefits of the proposed merger. If we determine that the public interest standard cannot be satisfied, even with conditions, and that the proposed merger is still a bad deal, then the merger application should be rejected. The majority stops at step one. Consequently, the Commission has missed a unique opportunity to consider potential benefits for the District of Columbia in this case.[1041]

[1040] Potomac Electric Power Company ("Pepco"), Exelon Corporation ("Exelon"), Pepco Holdings, Inc. ("PHI"), Exelon Energy Delivery Company, LLC, and New Special Purpose Entity, LLC (collectively, the "Joint Applicants") filed their initial merger application on June 18, 2014, pursuant to D.C. Code §§ 34-504 and 34-1001. By Order No. 17597, the Commission, among other things, amended the public interest factors that will be considered to evaluate whether the approval of the merger application is in the public interest. With this amendment, seven factors were considered in this case. *See Formal Case No. 1119*, Order No. 17597 at 61.

[1041] This Commission is the last state jurisdiction to consider the merger, which has been approved by the Delaware Public Service Commission, Maryland Public Service Commission, New Jersey Board of Public Utilities,

II. DISCUSSION

4. The Commission is tasked with deciding whether the Pepco/Exelon merger application should be approved pursuant to D.C. Code §§ 34-504 and 34-1001. As noted, the approval of the merger application hinges on whether the proposal taken as a whole is in the public interest. Like all cases, the starting point for my review is relevant Commission precedent.

A. Prior Merger Decisions

5. This Commission has previously considered two merger cases. In 1997, in *Formal Case No. 951*, the Commission considered and approved with conditions a merger between Baltimore Gas & Electric ("BGE") and Pepco that was ultimately not consummated.[1042] In 2002, in *Formal Case No. 1002*, the Commission considered and approved an unopposed Settlement Agreement regarding the merger between Pepco, Conectiv and the new RC (the company that eventually became PHI, which is the public utility holding company that now directly owns Pepco).[1043]

6. In *Formal Case No. 951*, which is the most analogous case to the Pepco/Exelon merger, the Commission determined that the merger "as proposed" could not be approved. However, the Commission's analysis did not stop there – the Commission weighed the opportunities that conditional approval of the merger would provide ratepayers as well as shareholders, whose interests the Commission is charged with protecting, and the Commission found it appropriate to approve the merger with additional conditions.[1044]

> In balancing the relative interests of all involved, we conclude that the merger *as proposed* by PEPCO and BGE exposes District of Columbia ratepayers to unacceptable risks and inequitably shares the savings likely to be realized. Nonetheless, we are mindful of the opportunity for savings and growth the merger offers to the ratepayers as well as the shareholders of both companies. Furthermore, a financially stronger, more efficient electric company will better serve the needs of ratepayers of this region, now and in the future. However, the merger plan *as proposed* by the applicants is not one that we will approve.[1045]

Virginia State Corporation Commission, and the Federal Energy Regulatory Commission. Maryland and New Jersey both approved the merger with additional conditions.

[1042] *See Formal Case No. 951*, Order No. 11075, at 3, rel. October 20, 1997.

[1043] *See Formal Case No. 1002,* Order No.12395, rel. May 1, 2002.

[1044] *Formal Case No. 951*, Order No. 11075, at 3, rel. October 20, 1997, citing *Washington Gas Light v. Baker*, 188 F.2d 11 (D.C. Cir. 1950), *cert. denied*, 340 U.S. 952, (1951) (the Commission must determine justness and reasonableness to the customer as well as to the investor).

[1045] *Formal Case No. 951*, Order No. 11075, at 3, rel. October 20, 1997. (Emphasis added).

The Commission reasoned that, "this case is perhaps one of the most difficult, yet important decisions in the history of electric utility regulation in the District of Columbia." The Commission also framed its decision as, "whether to approve a merger that may offer the Nation's capital a more efficient, lower-cost electric company, but which may also expose the District and D.C. ratepayers to all of the risks inherent in the proposed reorganization."[1046] The Commission finds itself in a very similar situation in the present case.

7. In *Formal Case No. 1002*, in examining shareholder and ratepayer benefits under a proposed Settlement Agreement, the Commission assumed, "that merging companies would not venture into a transaction if there were no benefits to be accrued by the merging companies' shareholders."[1047] Therefore, the Commission's review of the Settlement Agreement focused on whether the proposed merger would, "produce direct and traceable financial benefits to District ratepayers."[1048] However, the Commission noted that, "such benefits need not be profound."[1049] In the end, the Commission determined that the proposed Settlement Agreement was in the public interest.

B. Proposed Merger Commitments

8. The Joint Applicants included 91 commitments in their merger application.[1050] One of the most significant benefits of the proposed merger, according to the Joint Applicants, is their commitment to establish a $33.75 million CIF for use in the District of Columbia.[1051] The Joint Applicants also find benefits in their commitments to hire within two years at least 102 union workers, and to transfer 50 Pepco Energy Services Employees from Arlington, Virginia, to the District of Columbia.[1052] In addition, the Joint Applicants state that they will maintain PHI's supplier diversity programs and current level of charitable giving for at least ten years following consummation of the merger at an annual average of at least $1.6 million.[1053]

9. With regard to ring-fencing measures, the Joint Applicants provide a number of commitments to insulate Pepco from any perceived risk of harm resulting from the merger,

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1046 *Formal Case No. 951*, Order No. 11075, at 3, rel. October 20, 1997.

1047 *Formal Case No. 1002*, Order No. 12395, ¶ 24, rel. May 1, 2002.

1048 *Id*.

1049 *Formal Case No. 1002*, Order No. 12395, ¶ 24, rel. May 1, 2002, citing *Formal Case No. 951*, Order No. 11075, ¶ 18, rel. October 20, 1997.

1050 *See* Joint Applicants (4A)-2. On February 4, 2015, the Joint Applicants filed supplemental rebuttal testimony, which included additional commitments as a part of their merger application.

1051 Joint Applicants' Br. at 33, citing Joint Applicants (4A)-2 at 1, Commitment 6; Joint Applicants (4F) at 4:11-15 (Khouzami).

1052 Joint Applicants (4A)-2 at 4, Commitments 17-18.

1053 The Commission held four community hearings in this proceeding, where numerous community advocates and organizations submitted comments on the record in support of the commitment regarding charitable giving.

including risks associated with non-jurisdictional operations (*i.e.*, Exelon's nuclear facilities).[1054] The Joint Applicants also claim that they "have made several commitments to ensure, following the Merger, PHI and Pepco retain local control over decisions impacting the District" and that "the Joint Applicants have structured the transaction so that the Commission will retain the same level of oversight and regulatory authority over Pepco, and the entities, such as service companies, that supply services to Pepco, as it has today."[1055]

10. I believe that the principal deficiencies in the Joint Applicants' commitments include: 1) the allocation of the CIF; and 2) local control and regulatory oversight of Pepco post-merger. First, I agree with the majority's finding that the proposed CIF amount is inadequate, given the allocation methodology, which awards only 14 percent of the synergy-based CIF to the District of Columbia, which represents almost 25 percent of the sales, total rate base, and net income for all PHI electric operating companies.[1056] I also agree with the majority's finding that the proposed management structure could potentially harm District of Columbia ratepayers by diminishing their ability to be heard and by raising regulatory barriers. Under the proposed management structure, the Pepco Region President would effectively be removed from the decision-making process, and saddled with at least two additional levels of approval for large budget decisions. Moreover, the number of independent directors on the Pepco and PHI boards of directors would be reduced, and Pepco, the largest single utility in PHI, would be relegated to second-tier status within the Exelon decision-making management structure. For these reasons, I concur that the merger application *as filed* is not in the public interest.

C. Potential Merger Conditions

11. The impact of the proposed merger on ratepayers, the local economy, and the environment of the District of Columbia is vital to my consideration in this proceeding. Although the majority rejects the merger application as filed – without considering additional conditions that could benefit the District of Columbia – the majority's decision today is a clear departure from the approach taken in *Formal Case No. 951*. While the Commission is not bound by the approach taken in *Formal Case No. 951*, the Commission is required to reasonably explain its departure from Commission precedent. With today's decision, it is not clear why the majority is taking an approach different from *Formal Case No. 951* and from the practice of considering conditions in the overwhelming number of mergers that are reviewed by commissions throughout the country on both the state and national level. Therefore, in accordance with *Formal Case No. 951*, my preference would have been to not only set forth the proposed merger's defects, but to also offer, when appropriate, how the defect can be cured either by proposing conditions or providing guidance for future transactions.

12. Generally, the parties to this proceeding agree that the merger application as filed by the Joint Applicants should be rejected. Even though the parties request that we reject the

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[1054] Joint Applicants (4A)-2 at 4-12.

[1055] Joint Applicants' Br. at 96-97.

[1056] *See* Majority Opinion at ¶ 95.

merger application, many of those same parties advance conditions that they request the Commission impose should the merger be approved by the Commission. Nothing precludes the Commission from considering such conditions and we have considered conditions in the past.[1057]

13. For example, the District of Columbia Government ("District Government") argues that the proposed merger fails to pass muster under the Commission's established criteria, but the District Government also asks the question, "Can Conditions Save the Proposed Merger?"[1058] The District Government then proposes over 40 conditions including additional ring-fencing protections, a requirement to keep Pepco headquartered in the District of Columbia, and funding sustainable development and energy efficiency programs.[1059] The District Government finally concludes that unless similar conditions are adopted by the Commission, as those proposed by the District Government, the merger application must be rejected.

14. The Office of the People's Counsel ("OPC") contends, among other things, that commitments designed by the Joint Applicants to ensure local control and regulatory oversight do not go far enough.[1060] Rather, OPC argues that if the merger is approved it should include the following conditions: [1061]

- at least one-third and no fewer than two Pepco board members be independent,
- the majority of Pepco's Board members reside in DC,
- the majority of PHI's Board members be independent, and
- the PHI and Pepco CEOs reside in Pepco's service territory.

15. Regarding energy efficiency and renewable programs, the National Consumer Law Center, National Housing Trust, National Housing Trust Enterprise ("NCLC/NHT") argues that a similar approach to the Pepco/Exelon Multi-Party Settlement in Maryland should be taken in the District of Columbia. The NCLC/NHT also offers a specific proposal to fund energy

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1057 *See, e.g., Formal Case No. 951*; *see also Formal Case Nos. 1093 and 1115,* Order No. 17431, rel. March 31, 2014 (granting Washington Gas Light's Application for Approval of its Revised APRP subject to conditions).

1058 District Government's Br. at 42.

1059 District Government's Br. at 42.

1060 OPC's Br. at 64, citing OPC (A) at 136-37 (Dismukes).

1061 The Joint Applicants rejected these recommendations as "simply not tenable." OPC's Br. at 64, citing OPC (A) at 136-37 (Dismukes).

efficiency programs (taken out of the CIF amount)[1062] and the NCLC/NHT supports specific benefits for low-income ratepayers.[1063]

16. DC Solar United Neighborhoods ("DC SUN") argues that the proposed merger "does not pass the public interest test and cannot be effectively redeemed."[1064] DC SUN then goes on to state that, "if the Commission were to approve Exelon's acquisition of PHI, it would need to ameliorate the negative environmental impact by imposing strict conditions to counterbalance Exelon's keen financial incentive to protect its merchant generation fleet."[1065] The conditions put forth by DC SUN to accomplish that goal include specific steps that Pepco/Exelon should be required to undertake:

- accepting a financial penalty tied to achieving the District's overall solar goals,
- developing initiatives to provide financing for rooftop solar installations in low-income neighborhoods,
- streamlining the process for organizing and subscribing to community solar facilities,
- identifying the most favorable locations for distributed generation and where distribution grid upgrades are needed to accommodate solar installations, and
- helping to develop and support innovative regulatory structures that will permit distributed solar generation to thrive.

DC SUN also comments on the Commission's new grid modernization proceeding, which we opened to identify technologies and policies that can help modernize the District's energy delivery system for increased sustainability.[1066]

17. Additionally, the Commission could have considered such issues as a "most-favored-nation provision" to ensure District ratepayers receive equal benefits to other jurisdictions, a moratorium on rate increases, funding for increased low-income energy assistance, green jobs for District of Columbia residents, increased penalties for reliability standards, investments in energy efficiency programs, and an increase in or reallocation of the

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1062 NCLC/NHT Br. at 9-10, citing OPC Cross Examination Exhibit No. 7, pp. 24-26 of 70 (Multi-Party Settlement pp. 5-7). The Pepco-Maryland service territory falls completely within Prince George's and Montgomery Counties, so that all of the customers of the Pepco-Delmarva-Maryland are covered among paragraphs 5-7 of the Multi-Party Settlement.

1063 NCLC/NHT Br. at 9, citing OPC Cross Examination Exhibit No. 7, p. 20 of 70 (Multi-Party Settlement Commitment ¶ 3). The comparable dollar amount is $33.8 million for Pepco's customers in the District, and is also equivalent to approximately $128 per customer (Joint Applicants (4A)-2, at 1, Commitment 6; Joint Applicants (A) at 12:23 (Crane)).

1064 DC SUN's Br. at 6.

1065 DC SUN's Br. at 7.

1066 *See Formal Case No. 1130*, Order No. 17912, rel. June 12, 2015.

CIF amount.[1067] Based on Commission precedent, the Commission could have used any of these issues as a starting point, as well as certain conditions proposed by the District Government, OPC, NCLC/NHT, DC SUN, and others presented on the record, to potentially mitigate deficiencies in the merger.[1068] Instead, it appears the majority limited its evaluation of the merger to only consider the proposed merger *as filed*, neglecting to consider potential merger conditions.

18. Some have argued that the Commission should not feel compelled to fashion a set of conditions that may satisfy the public interest standard, and that it is not the obligation of the Commission to review conditions because undertaking such a review could burden the Commission's limited resources. To the contrary, I believe that it is the Commission's obligation to consider what a merger deal might look like that would benefit the public – before making our final determination. I also believe it is this sense of obligation that has compelled the Commission to consider conditions in the past.[1069] Still, to be clear, I dissent not because I favor any particular conditions. I simply disagree with the majority's apparent decision to not evaluate potential conditions that could benefit the District of Columbia, which is a stark contrast to the approach taken in *Formal Case No. 951*.

III. CONCLUSION

19. The majority today opines that the merger *as filed* is unacceptable. I agree. However, I am disappointed in the loss of the many opportunities inherent in the proposed merger that could have achieved benefits for ratepayers, the local economy, and the environment of the District of Columbia. It is unfortunate that the majority decided not to consider these opportunities with this decision, even though nothing precludes the Commission from doing so.

20. For the aforementioned reasons, I respectfully concur, in part, and dissent, in part, from the majority opinion.

Willie L. Phillips

Willie L. Phillips, Commissioner

[1067] In Delaware, the Joint Applicants negotiated a settlement agreement that included $2 million in funding for a workforce development program with Delaware State University, the Delaware Technical Community College, and other community based organizations specifically focused on energy-efficiency, renewable energy and Science, Technology, Energy and Math ("STEM") education. *In the Matter of the Application of Delmarva Power & Light Company, Exelon Corporation, Pepco Holdings, Inc., Purple Acquisition Corporation, Exelon Energy Delivery Company, LLC and New Special Purpose Entity for Approvals Under the Provisions of 26 DEL.C.§§ 215 and 1016*, Order No. 8746, rel. June 2, 2015.

[1068] The 91 commitments to the merger application included in Joint Applicants' Exhibit (4A)-2 were not updated to reflect settlements reached in other jurisdictions because it would "restart the clock" and delay the Commission's schedule. Tr. at 110:13-22 (Crane); *see also* Tr. at 138:15-20 (Crane), Tr. at 222:18 to 223:3 (Crane), Tr. at 238:11-18 (Crane), Tr. at 241:8 to 242:3 (Crane), and Tr. 550:4-12 (Crane).

[1069] *See, e.g., Formal Case No. 951*; *see also Formal Case Nos. 1093 and 1115*, Order No. 17431 (granting Application of Washington Gas Light Company for Approval of its Revised APRP subject to conditions).