

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

ORDER

October 10, 2019

**FORMAL CASE NO. 1017, IN THE MATTER OF THE DEVELOPMENT AND
DESIGNATION OF STANDARD OFFER SERVICE IN THE DISTRICT OF
COLUMBIA, Order No. 20232**

I. INTRODUCTION

1. By this Order, the Public Service Commission of the District of Columbia (“Commission”) solicits comments from interested persons regarding the Commission’s long-term renewable energy power purchase agreement pilot program for Standard Offer Service (“SOS”), Potomac Electric Power Company’s (“Pepco” or “Company”) draft request for proposals (“RFP”), and the individual Working Group members’ comments on the draft RFP. Comments and reply comments are due within 30 and 45 days, respectively, from the date of this Order. In addition, Pepco shall file an analysis indicating the approximate level at which long-term power purchase agreements represent a material credit and capital structure issue for Pepco, along with supporting calculations, within 20 days from the date of this Order. Interested persons may address Pepco’s filing in their comments within 30 days of the date of this Order.

II. BACKGROUND

2. By Order No. 19897, issued April 12, 2019, the Commission, *inter alia*, established “a pilot program to procure renewable energy through long-term power purchase agreements (‘PPA’) for electricity generated by solar or wind power facilities located within the PJM Interconnection region (‘PJM’) with a target quantity of five (5) percent of the SOS load.”¹ In order to facilitate the establishment of this pilot program, the Commission directed that “a planning meeting be scheduled within 30 days, and that the SOS Working Group produce, by July 31, 2019, a draft request for proposals (‘RFP’) for long-term renewable energy PPAs, including the renewable energy credits (‘RECs’) associated with the energy... and draft revised SOS rules, if required, to accommodate this change in the SOS procurement portfolio.”² Order No. 19897 also directed Pepco to file

¹ *Formal Case No. 1017, In the Matter of the Development and Designation of Standard Offer Service in the District of Columbia (“Formal Case No. 1017”), Order No. 19897, released April 12, 2019 (“Order No. 19897”), ¶ 1.*

² Order No. 19897, ¶ 35.

an analysis regarding the impact of long-term renewable energy PPA obligations on imputed debt.³ On May 28, 2019, Pepco filed its response.⁴

3. The SOS Working Group held three meetings on May 1, June 7, and July 11, 2019.⁵ On July 31, 2019, Pepco, on behalf of the Working Group, filed a draft RFP; its comments addressing a number of issues affecting the PPA; redlined edits to and comments on the draft RFP from Commission Staff, the Center for Renewables Integration (“CRI”)⁶, and the Apartment & Office Building Association of Metropolitan Washington (“AOBA”); and comments from the Sierra Club and WGL Energy Services, Inc. (“WGL Energy”).⁷

III. DISCUSSION

A. Outstanding Issues Raised at Standard Offer Service Working Group Meetings

4. During the SOS Working Group meetings, stakeholders raised the following three (3) issues for which a consensus could not be reached: 1) which strategies/recovery mechanism should be employed to integrate the long-term renewable energy PPA into the SOS procurement portfolio; 2) what margin or return should Pepco receive; and 3) how the RECs generated as a result of the PPA are to be treated.

5. While Pepco already commented on which recovery mechanism should be employed to integrate the long-term renewable energy PPA into the SOS procurement portfolio,⁸ the Commission invites comments from all interested persons on the three outstanding issues.

³ Order No. 19897, ¶¶ 37, 45 (citation omitted).

⁴ *Formal Case No. 1017*, Potomac Electric Power Company’s (“Pepco”) Response to Paragraph 37 of Order No. 19897, filed May 28, 2019 (“Pepco’s Response to Paragraph 37”).

⁵ *See Formal Case No. 1017, First Standard Offer Service Working Group Meeting Regarding Long-Term Renewable Energy PPAs Meeting Minutes*, filed May 20, 2019 (“May 20th Minutes”); *Formal Case No. 1017, Second Standard Offer Service Working Group Meeting Regarding Long-Term Renewable Energy PPAs Meeting Minutes*, filed June 20, 2019 (“June 20th Minutes”); and *Formal Case No. 1017, Third Standard Offer Service Working Group Meeting Regarding Long-Term Renewable Energy PPAs Meeting Minutes*, filed July 23, 2019 (“July 23rd Minutes”).

⁶ CRI is a consultant for the District of Columbia Department of Energy & Environment (“DOEE”).

⁷ *Formal Case No. 1017*, Potomac Electric Power Company’s (“Pepco”) Response to Order No. 19897 at 2, filed July 31, 2019 (“Pepco’s Response”).

⁸ Pepco’s Response at 2-6.

1. Strategies/Cost Recovery Models to Integrate the Long-Term Renewable Energy PPA Into the SOS Procurement Portfolio

6. A key issue that arose during the SOS Working Group process was what strategies or cost recovery models should be employed regarding which customers pay for the energy purchased under the PPA and who consumes or buys that energy. Under the current SOS procurement regime, 100 percent of the SOS load is bid out as a full requirements product, requiring suppliers to provide not only the energy but also other components such as capacity, losses, congestion, load shaping, credit and risk, ancillary services, and the cost of compliance with the District's Renewable Energy Portfolio Standard.⁹ The SOS Working Group discussed three strategies or cost recovery models: the 95/5; Massachusetts; and Pepco's proposed Modified 95/5.

7. **The 95/5 Model.** Under the 95/5 Model, the long-term renewable energy PPA provides the renewable energy to satisfy five (5) percent of the SOS load including the environmental attributes¹⁰ associated with that renewable energy. Pepco, as the SOS Administrator, would have to procure the remaining components for that five (5) percent – capacity, losses, congestion, load shaping, credit and risk, and ancillary services – and provisions would have to be made to accommodate the intermittent nature of the renewable energy provided by the PPA since the energy from the PPA will not strictly follow load demand.¹¹ With this model, the cost of procuring the energy from the PPA, including the environmental attributes and the components listed above, would be borne by all SOS ratepayers. The SOS ratepayers would also consume the energy generated from the PPA.¹² The remaining 95 percent of the SOS load is bid out as a full requirements service or product in the same manner as the current SOS procurement process.¹³

⁹ "Full Requirements Service" is defined as meaning "all necessary Energy, Capacity, Transmission other than Network Integration Transmission Service, Ancillary Services, Renewable Energy Resource Requirement, transmission and distribution losses, congestion management costs, and such other services or products that are required to supply the Specified Percentage except for Network Integration Transmission Service and distribution service." See *Formal Case No. 1017*, Standard Offer Service Working Group's Proposed Wholesale Full Requirements Service Agreement ("WFRSA") and Request for Proposals for the 2019 to 2020 SOS Solicitation, WFRSA at 4 (Definition of Full Requirements Service), filed July 30, 2019.

¹⁰ "Environmental Attributes include Renewable Energy Credits ('REC') and any other federal, regional, state and other credits, certificates, benefits, emission reductions, offsets and allowances that are attributable, now or in the future, to the facility or the energy produced by the facility." Pepco's Response, Draft Request for Proposals at 3.

¹¹ Renewable energy, wind and/or solar systems, under a PPA, would not strictly follow the District of Columbia's SOS customers' load demand like the full requirements SOS product or service does. For example, solar energy is produced when the sun shines, and wind turbines turn when the wind blows. Provision needs to be made for the intermittent nature of solar and wind power generation not matching up with the constant and ever-changing nature of the District's SOS electricity demand and spot market purchases would make up for this mismatch.

¹² June 20th Minutes at 4-5.

¹³ June 20th Minutes at 4-5.

8. **Massachusetts Model.** Under this model, the current SOS procurement process remains unchanged since 100 percent of the SOS load would continue to be bid out as a full requirements service or product. The long-term renewable energy PPA would procure renewable energy, including the environmental attributes, equivalent to five (5) percent of the SOS load.¹⁴ Under the Massachusetts Model, because the renewable energy procured pursuant to the PPA would not serve SOS load, Pepco, as the SOS Administrator, would not have to procure the other components listed in paragraph 7.

9. With this model, the cost of procuring the renewable energy equivalent to five (5) percent of the SOS load, including the environmental attributes, would be borne by both SOS customers and customers of competitive electricity suppliers. Since the 100 percent of the SOS load would be procured as a full requirements product, the additional energy equivalent to five (5) percent of the SOS load generated from the PPA would be sold into the wholesale market at a gain or a loss. The net proceeds from those sales would appear as sur-credits or surcharges on all ratepayers' bills depending on whether those sales result in profits or losses.¹⁵

10. **Pepco's Proposal: Modified 95/5 Model.** Under this model, 95 percent of the SOS load would be bid out as a full requirements product, and the long-term renewable energy PPA would supply the remaining five (5) percent of the SOS load. The only difference between the 95/5 Model and the Modified 95/5 Model is who pays. Under this model, both SOS customers and customers of competitive electricity suppliers would be responsible for all costs. Whereas under the 95/5 Model, only the SOS customers are responsible for costs. According to Pepco, it would "act as an agent, collecting funds from customers in advance of paying the renewable developer, much like Pepco does for various taxes and surcharges it collects for the District of Columbia."¹⁶

11. The Commission invites comments from interested persons on the three models described above or any other recovery model that the Commission should adopt.

2. Margin or Return for Administering the PPA

12. At the July 11, 2019, SOS Working Group meeting, based on the assumption that Pepco would be the signatory on the PPA in the Company's role as the SOS administrator, the SOS Working Group discussed, but did not resolve, the issue of whether and how much of a margin or return Pepco should receive for administering the PPA, in addition to being reimbursed for the incremental costs incurred for administrating

¹⁴ June 20th Minutes at 5.

¹⁵ June 20th Minutes at 5.

¹⁶ Pepco's Response at 4 (citation omitted).

a long-term renewable energy PPA.¹⁷ Pepco currently receives a margin or return for its services as the SOS administrator, in addition to being reimbursed for the incremental costs Pepco incurred as the administrator.¹⁸ The Commission recognizes that, at a minimum, Pepco should be compensated for the incremental cost it would incur in administering the PPA. The Commission therefore invites comments on the appropriate margin or return, if any, Pepco should receive for administering the PPA, in the event that Pepco serves in this role.

3. Treatment of RECs Generated by the PPA

13. In Order No. 19897, the Commission directed the SOS Working Group “to produce... a draft request for proposals (‘RFP’) for long-term renewable energy PPAs, including the RECs associated with the energy, for solar or wind power generating facilities located within PJM...”¹⁹ The SOS Working Group did not resolve how the RECs associated with generation produced under the PPA should be treated or utilized. The Commission therefore invites interested persons to comment on this issue. In commenting on this issue, interested persons should consider whether and to what extent the treatment of the RECs “is consistent with the Clean Energy DC goal of a 50 percent reduction in greenhouse gas (‘GHG’) emissions by 2032...”²⁰ and with the Commission’s statutory mandate to preserve the environmental quality, including effects on global climate change and the District’s public climate commitments.²¹ Interested persons should also consider that, if all of the RECs are sold separately from the energy produced pursuant to the PPAs, that energy would no longer be considered to be clean or renewable energy as the renewable attributes associated with the energy have been sold. The energy would, instead, be rendered “null” energy.²² This would be the case no matter what recovery method the Commission chooses.

¹⁷ See *Formal Case No. 1017*, July 23rd Minutes at 4.

¹⁸ See generally Order No. 19897, ¶¶ 4-5.

¹⁹ Order No. 19897, ¶ 35.

²⁰ Order No. 19897, ¶ 22 citing Center for Renewables Integration, *Feasibility Study: Increasing the Renewable Energy Content of Standard Offer Service*, at 2 (September 28, 2019) (citation omitted in original); See also Sec. 301(B)(1)(c)(i) of D.C. Law 22-257, *CleanEnergy DC Omnibus Amendment Act of 2018* (March 22, 2019) (“*CleanEnergy Act*”); See DOEE and District of Columbia Office of the Mayor, *Clean Energy DC, The District of Columbia Climate and Energy Action Plan*, at v (August 2018), available at https://doee.dc.gov/sites/default/files/dc/sites/ddoe/page_content/attachments/Clean%20Energy%20DC%20-%20Full%20Report_0.pdf.

²¹ “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, including its effects on global climate change and the District’s public climate commitments.” D.C. Code § 34-808.02 (*as amended by CleanEnergy Act*). See also Order No. 19897, ¶ 22.

²² “Electricity use from a renewable resource in the absence of owning the associated RECs is not considered renewable electricity (referred to as ‘null power’) and has the same environment profile as the residual grid electricity mix – RECs make it renewable.” See Understanding Renewable Energy Certificates

B. Imputed Debt and Related Matters

14. On May 28, 2019, Pepco responded to Order No. 19897 regarding the impact of the PPA on the Company's imputed debt. Pepco notes that in Standard and Poor's ("S&P") most recent corporate ratings criteria, S&P states:

[u]nder lease arrangements, the lessee contracts for the use of an asset, entering into a debt-like financing obligation to make periodic rental payments. To account for this, we adjust debt, earnings, cash flows, and interest for comparability across accounting regimes. In certain cases, we may increase lease liabilities if we believe the reported lease disclosure does not adequately capture the lease leverage.²³

Pepco contends that imputing debt is S&P's way of transferring the PPA project risk from the renewable developer to the utility because the PPA obligation of the utility is essentially providing cash flow and credit support to the renewable developer. Pepco asserts that S&P and other rating agencies account for this transferred risk as a fixed debt obligation of the utility and impute or represent this risk to the utility's balance sheet.²⁴ According to Pepco, "S&P, as well as the other credit rating agencies, consider the strength of cost recovery mechanisms and assign the lowest risk factor to legislatively mandated cost recovery mechanisms."²⁵ Pepco also notes that "[t]he estimated notional value of this proposed PPA alone just 5% percent of SOS load could range from \$150-\$200 million over twenty years based on current calculations."²⁶ Specifically, Pepco stated that it "has not recently prepared any formal analysis that indicates the general level at which PPAs represent a material credit and capital issue or risk for the Company."²⁷ In addition, Pepco asserted that, "as a policy matter, the Commission should not allow a level of PPAs on the utility balance sheet up to the point where the PPAs become a material credit issue."²⁸

(RECs) and the Green Power Procurement Process at 6 (2015) at https://www.epa.gov/sites/production/files/2016-01/documents/webinar_20150415_critchfield.pdf.

²³ Pepco's Response to Paragraph 37 at 1, *citing to* Standard & Poor's Ratings Corporate Methodology: Ratios and Adjustments (April 1, 2019).

²⁴ Pepco's Response to Paragraph 37 at 2, *citing to* Moody's Investors Service Rating Methodology Regulated Electric and Gas Utilities (December 23, 2013).

²⁵ Pepco's Response to Paragraph 37 at 3.

²⁶ Pepco's Response to Paragraph 37 at 3.

²⁷ Pepco's Response to Paragraph 37 at 3.

²⁸ Pepco's Response to Paragraph 37 at 3.

15. Pepco contends that “there are viable alternatives to traditional PPAs that have been successfully implemented in other states that allow developers to finance renewable projects without negative credit implications for the utility. However, if the Commission requires the utility to enter into a PPA, there are minimum requirements that the Commission should require to protect the utility and its customers.”²⁹ Pepco recommends that “the PPA be structured such that the Company has explicit assurance that it will recover all costs associated with the PPA, and the PPA should include provisions to protect the Company from any potential default by the renewable developer(s).”³⁰ According to Pepco, it “knows from experience that the optimal method of recovery should be provided by statute as opposed to a method contained in Commission regulation or directive. Given that a statutory change is not imminent, changes to the SOS regulations, while not as certain as explicit as legislative requirements, would likely be viewed by the credit rating agencies as having greater certainty than Commission directive alone.”³¹ Pepco recommends that the Commission implement an explicit cost recovery mechanism in regulations, and that such a “cost recovery regulation should allow the Company to act as payment agent where funds are collected from customers via surcharge to cover all costs, thereby minimizing the risk associated with the use of any utility funds in the PPA process.”³²

16. Pepco also states that “requiring Pepco to act as a counter party to a long-term PPA could result in debt imputed to Pepco’s books, which could in turn affect Pepco’s credit rating and, ultimately, result in higher distribution rates if Pepco’s cost to borrow increases.”³³ Pepco cites these risks in opposing the adoption of the Massachusetts Model and resisting assuming the role of signatory to the PPA under that model.³⁴

17. Pepco maintains that changes to SOS regulations would likely be viewed by the credit rating agencies as having greater certainty (thus, lower risk to Pepco’s credit metrics) than Commission directive alone. While we recognize that imputed debt is a concern that may affect a utility’s financial ratios and credit rating, Pepco’s statements alone do not quantify the specific impact of long-term PPAs on the Company’s balance sheet. Absent this showing, the Commission is unable to assess the degree of risk that long-term PPAs would have on Pepco’s balance sheet. Accordingly, within 20 days of the date of this Order, Pepco is directed to file an analysis indicating the approximate level (percentage of SOS load) at which long-term PPAs represent a material credit and capital structure issue for Pepco and to provide supporting calculations. In addition, Pepco is

²⁹ Pepco’s Response to Paragraph 37 at 4.

³⁰ Pepco’s Response to Paragraph 37 at 4.

³¹ Pepco’s Response to Paragraph 37 at 4.

³² Pepco’s Response to Paragraph 37 at 4.

³³ Pepco’s Response at 2-3 (citation omitted).

³⁴ Pepco’s Response at 6-7 (citation omitted).

directed to provide at least one empirical example where S&P or another rating agency has imputed debt from such long-term PPAs onto a utility's balance sheet. Interested persons may comment on Pepco's filing in their comments. The Commission is concerned about the issue of imputed debt and the impact that it could potentially have on customer rates. Thus, the Commission also seeks comments as to whether changes to the SOS regulations adopting an explicit cost recovery mechanism are needed as recommended by Pepco to minimize the risk associated with the PPA.

C. Draft RFP

18. As previously indicated, on July 31, 2019, Pepco, on behalf of the SOS Working Group, filed its proposed draft version of the RFP; Commission staff's, CRI's, and AOBA's redlined edits and comments on Pepco's proposed draft RFP; its own comments addressing a number of issues affecting the PPA; and comments from the Sierra Club and WGL Energy regarding the PPA and RFP.³⁵ Pepco noted that there was no consensus within the SOS Working Group concerning a number of issues regarding the content of the RFP.³⁶ The Commission therefore invites interested persons to comment on all the documents that Pepco filed on behalf of the SOS Working Group.

THEREFORE, IT IS ORDERED THAT:

19. Consistent with paragraphs 6 through 11 of this Order, interested persons are invited to comment on which recovery mechanism or model to employ in the integration of the long-term renewable energy power purchase agreement into the Standard Offer Service procurement portfolio within 30 days and to file reply comments within 45 days of the date of this Order;

20. Consistent with paragraph 12 of this Order, interested persons are invited to comment on the issue of whether the Potomac Electric Power Company should receive a margin or return for the administration of the long-term renewable energy power purchase agreement within 30 days and to file reply comments within 45 days of the date of this Order;

21. Consistent with paragraph 13 of this Order, interested persons are invited to comment on the treatment of the renewable energy credits within 30 days and to file reply comments within 45 days of the date of this Order;

22. The Potomac Electric Power Company is directed to file, consistent with paragraphs 14 through 17 of this Order, an analysis indicating the approximate level (i.e. percentage of SOS load) at which long-term PPAs represent a material credit and capital structure issue for the Company, along with supporting calculations; and to provide at least one empirical example where Standard & Poor or another rating agency has imputed debt

³⁵ Pepco's Response.

³⁶ Pepco's Response at 2.

from such long-term PPAs onto a utility's balance sheet within 20 days from the date of this Order;

23. Interested persons are invited to address the Potomac Electric Power Company's analysis in their comments filed within 30 days of the date of this Order;

24. Consistent with paragraphs 15 and 17 of this Order, interested persons are invited to comment on whether the Commission's Standard Offer Service regulations should be revised to adopt an explicit cost recovery mechanism to minimize the risk associated with the integration of a long-term renewable energy power purchase agreement into the Standard Offer Service procurement portfolio within 30 days and to file reply comments within 45 days of the date of this Order; and

25. Consistent with paragraph 18 of this Order, interested persons are invited to comment on the Potomac Electric Power Company's proposed draft of the request for proposals; Commission staff's, the Center for Renewables Integration's, and the Apartment & Office Building Association of Metropolitan Washington's redlined edits and comments on the Potomac Electric Power Company's proposed draft request for proposals; the Potomac Electric Power Company's comments addressing a number of issues affecting the long-term renewable energy power purchase agreement; and comments from the Sierra Club and WGL Energy Services, Inc. regarding the power purchase agreement and the draft request for proposals within 30 days and to file reply comments within 45 days of the date of this Order.

A TRUE COPY:

BY DIRECTION OF THE COMMISSION:



CHIEF CLERK

**BRINDA WESTBROOK-SEDGWICK
COMMISSION SECRETARY**