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STATE OF INDIANA

FILED

INDIANA UTILITY REGULATORY COMMISSION MAY 27 2005

INDIANA UTILITY
REGULATORY COMMISSION

PETITION OF PSI ENERGY, INC. FOR AUTHORITY)
TO INCREASE ITS RATES AND CHARGES FOR)
ELECTRIC SERVICE; FOR APPROVAL OF NEW)
SCHEDULES OF RATES AND CHARGES AND OF)
RULES AND REGULATIONS APPLICABLE TO SUCH)
RATES AND CHARGES; FOR THE AUTHORITY TO)
REFLECT ITS QUALIFIED POLLUTION CONTROL)
PROPERTY AND OTHER NEW PLANT AND)
EQUIPMENT IN ITS RATES AND CHARGES; FOR)
APPROVAL OF ITS IMPLEMENTATION OF THE)
FEDERAL ENERGY REGULATORY COMMISSION'S)
SEVEN-FACTOR TEST; FOR APPROVAL OF)
VARIOUS RATE TRACKING MECHANISMS,)
INCLUDING A PROPOSED MIDWEST)
INDEPENDENT TRANSMISSION SYSTEM)
OPERATOR MANAGEMENT COST ADJUSTMENT)
RIDER AND CONTINUED USE OF A PURCHASED)
POWER TRACKING MECHANISM; AND FOR)
APPROVAL OF RELATED ACCOUNTING)
TREATMENT AND DEPRECIATION RATES AND)
OTHER ACCOUNTING RELIEF RELATIVE TO ITS)
BUSINESS)

CAUSE NO. 42359

PSI ENERGY, INC. REPLY

PSI Energy, Inc. ("PSI") hereby respectfully submits to the Indiana Utility Regulatory Commission ("Commission") its Reply to the "Industrial Group's Response to PSI's Real Time Pricing Report and Objection to Proposed New RTP Rate", filed with the Commission on May 18, 2005, and in support hereof, states as follows:

1. **PSI Negotiated in Good Faith.** The overall purpose of the Real Time Pricing ("RTP") Collaborative was "...to design rate options which will be effective while providing value to PSI, its participating customers, and PSI's non-participating customers (these options

may or may not include some form of a real time pricing program).”¹ PSI has made a lengthy attempt to achieve that goal. It is indeed unfortunate that the PSI Industrial Group (“PSI-IG”) has chosen to characterize PSI’s participation in the collaborative process in the way that it has. PSI has consistently negotiated in good faith, put forth proposals in an attempt to address the concerns of the PSI-IG, and sought extensions of time to accommodate the process. Throughout negotiations, PSI made several changes to its proposal to meet the concerns raised by PSI-IG, such as adjusting energy delivery charges and ancillary service charges for differing load factor, billing such charges based on demand, and agreeing to allow customers to continue participation in PowerShare® for a limited time. PSI had solid reasons that served as a basis for the content of its proposals.

During the collaborative process, PSI-IG did not move from its position that PSI should maintain the lower of cost or market pricing – a pricing mechanism that the Commission had already found had “some serious flaws” and was not cost effective.² Regrettably, PSI-IG never meaningfully addressed PSI’s proposals nor engaged in any meaningful dialogue about the theoretical structure of RTP.

Finally, because the Commission found that PSI’s current RTP Rider was not reasonable and should be terminated, and because the collaborative parties never came to a conclusion on a revised RTP Rider, PSI could have legitimately let the program terminate and transition the customers to PowerShare®, as originally planned. However, PSI chose to offer for approval its latest offer of a revised RTP tariff. PSI firmly believes it has negotiated in good faith throughout the process and that our ultimate proposal is a reasonable compromise.

¹ Order in Cause No. 42359, p. 127.

² Order in Cause No. 42359, p. 126

2. **No Need For Further Delay.** PSI-IG proposes further postponement of this process. The RTP Collaborative Process began in earnest with the first meeting in July 2004, less than two months after the Commission's rate case order establishing the Collaborative. The goal at that time was resolution of the issue by January 31, 2005, the termination date for the existing RTP Rider originally set by the Commission. Throughout the process PSI has willingly and on its own initiative postponed due dates, including the termination date of the RTP Rider, in order to give the parties more time to negotiate. However, as both PSI-IG and PSI agree, the parties are fundamentally at odds over the generation pricing component that is appropriate for an RTP program.

PSI-IG claims that it wants to negotiate with Duke Energy, referencing the fact that PSI's parent company, Cinergy Corp., and Duke Energy Corporation have recently announced the intent to merge the two companies. PSI-IG's request for more time to negotiate with Duke implies that the entire pricing philosophy across three separate retail jurisdictions³ will be obliterated by the merger process, and is clearly premature. The merger was just announced less than three weeks ago, numerous regulatory approvals and likely more than 12 months will pass before the merger can be consummated. When this holding company merger is consummated in the future, it will not have any effect on the structure of PSI tariffs. PSI-IG's request is both unfounded and premature.

It is understandable that PSI-IG would request more time. The longer the current tariff is in place the longer the RTP customers will be receiving an unwarranted discount. The Commission has found the current tariff to be not cost effective, and therefore not reasonable and

³ PSI's treatment of commodity related costs for its RTP Programs has been approved for its affiliate companies The Cincinnati Gas and Electric Company and Union Light Heat and Power Company in Ohio and Kentucky, respectively.

subject to termination. RTP customers have already gained another 12 months under the current flawed RTP Rider. There is simply no basis to delay the termination of the current RTP Rider.

3. **Market Pricing.** PSI's primary concerns regarding the RTP program are that the commodity portion and energy delivery portions of its structure are significantly under-priced. The Commission agreed that PSI had met its burden of proof on these matters.⁴ With regard to the commodity portion of the price, the current RTP tariff takes the lesser of marginal cost or market cost which we contend substantially under-prices the cost of commodity services. PSI's proposal removes the "lesser of" test, and moves the commodity portion of the price to market. PSI believes this approach is the best representation of the real world⁵, and provides price signals that better reflect the long run marginal cost of providing this type of service. PSI's belief that market pricing is the right approach for the generation component of RTP was reaffirmed when the Midwest Independent Transmission System Operator, Inc. ("Midwest ISO") Day Ahead Energy Market began. An independent verifiable hourly day-ahead price is simply the right price to use for the generation component of a real time pricing program.

PSI-IG claims that PSI has not indicated how much it costs to serve RTP customers. PSI has presented evidence in the rate case and information in the collaborative that demonstrates that RTP customers have been receiving a discount that is disproportional to the benefit they provide. PSI demonstrated that under the current tariff, RTP customers are not even covering the marginal cost to serve them. PSI provided an analysis showing the cost of providing this service based on the cost of providing combustion turbines to serve incremental load along with the load impact of RTP customers. This analysis revealed that recovering the cost of a combustion

⁴ Order in 42359, pp. 126 - 127.

⁵ The Midwest ISO Day-Ahead hourly pricing is used for the RTP program, and the Midwest ISO represents a bona-fide clearinghouse for market prices.

turbine required a revenue stream that was remarkably close to what would have been provided had market costs been used.

PSI-IG has consistently resisted this notion, instead preferring to raise arguments that by pricing the commodity portion of RTP based on market, PSI would be deviating from economic dispatch. This, of course, is not true, and demonstrates a fundamental lack of understanding of the subject matter.⁶ There must be some “spread” between the cost of providing service and the final price customers pay to cover the marginal costs of service, make a contribution to fixed costs, and provide for a reasonable profit. PSI’s contention is that the best measure of this “spread”, for purposes of the RTP Rider, is the difference between the marginal cost and the market, and that this “spread” further, in the long run, represents the cost of combustion turbines.⁷ PSI presented calculations clearly showing this approach, and PSI-IG failed to formally or informally ask any questions – other than basic understanding of the approach - even though PSI has responded fully to any and all questions directed to PSI. It is disingenuous for PSI-IG to suggest such an approach is “in question” given its failure to ask any probing questions about it.

PSI-IG further assails PSI for its attempts to obtain a reasonable profit for the RTP Program, even though doing so will benefit non-participant customers. If PSI’s units are dispatched into the market, any profits from off-system sales will be shared with non-participant customers. Failure to restructure the RTP Program as proposed by PSI would continue to disadvantage non-participant customers. PSI-IG conveniently omitted this fact from its

⁶ This is why PSI responded to the PSI-IG by stating that economic dispatch is not germane to our discussions. PSI’s units have been, are, and will continue to be dispatched on a economic basis.

⁷ Even so, this allows RTP customers to “escape” a number of other charges normally paid by non-participating customers.

argument, even though this logic was presented by PSI in the very next sentence contained in PSI's response.

PSI-IG continues to complain about the subsidy levels discussed about the program. The record in Cause No. 42359 is clear that these customers are receiving an inordinate benefit under the program. In addition, all costs of the rate increase granted in Cause No. 42359 that would have been attributable to RTP customers are borne by the remaining customers under rates HLF and LLF; RTP customers, but for a small portion of distribution and transmission costs, receive a "free pass" on the generation related fixed costs. Any form of traditional cost studies will continue to show a substantial subsidy to these customers. Without substantial modification, the subsidy from other customers will continue to enlarge, particularly as pollution control equipment costs are included in rates.⁸

PSI-IG contends that it was unable to make detailed offers to PSI. However, PSI-IG could have engaged a consultant knowledgeable in RTP, as did PSI. But to the best of our knowledge, PSI-IG failed to do so, or at least it was not apparent in any discussions or requests. Had they done so, meaningful discussions could have been achieved and an attempt made at the appropriate modeling. At the very minimum, discussions at a theoretical level likely could have enhanced the process.

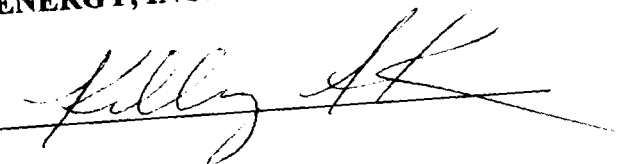
While PSI recognizes that RTP customers may be negatively impacted by the move to PSI's proposed Revised RTP Rider, PSI contends that such customers have received benefits under the current program which are disproportional to the value received for years.

WHEREFORE, in consideration of all the foregoing, PSI respectfully requests the Commission to replace the current Standard Contract Rider No. 21, which is due to terminate as

⁸ This will remain an issue with this program despite PSI's current proposal, and is one reason PSI proposes that the new RTP Rider be limited in time to three years.

of June 30, 2005, with the Revised Standard Contract Rider No. 21 filed by PSI in its April 29, 2005 RTP Collaborative Report, establishing an effective date of June 30, 2005.

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that copies of the foregoing Motion were delivered or mailed, postage prepaid, in the United States Mail, this 27th day of May, 2005, to the following counsel and parties:

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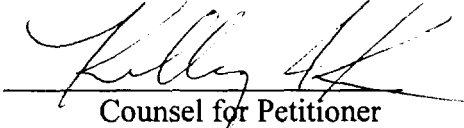
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