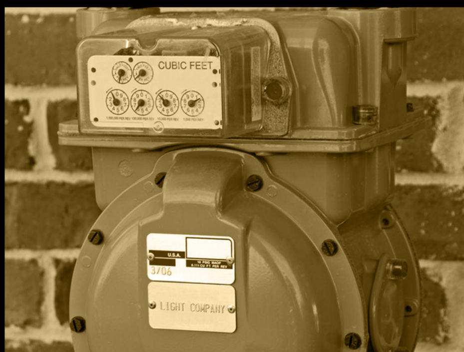
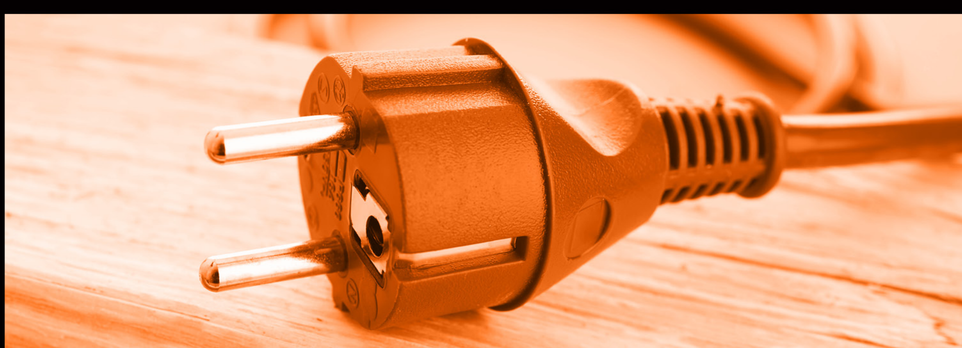
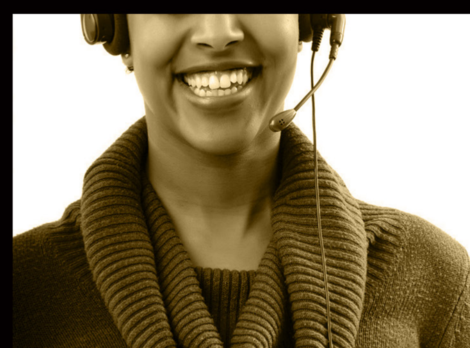


FISCAL YEAR 2010 2011

PENNSYLVANIA
PUC
PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission Annual Report





Our Mission

The Pennsylvania Public Utility Commission balances the needs of consumers and utilities to ensure safe and reliable utility service at reasonable rates; protect the public interest; educate consumers to make independent and informed utility choices; further economic development; and foster new technologies and competitive markets in an environmentally sound manner.

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Chairman Robert F. Powelson

Vice Chairman John F. Coleman Jr.

Commissioner Wayne E. Gardner

Commissioner James H. Cawley

Commissioner Pamela A. Witmer

The Honorable Tom Corbett
Governor of Pennsylvania

The Honorable Jim Cawley
Lieutenant Governor of Pennsylvania

Members of the General Assembly

We are pleased to submit the 2010-11 Annual Report for the Pennsylvania Public Utility Commission. As required by Section 321 of the Public Utility Code, 66 Pa. C.S § 321, this report highlights the accomplishments and challenges faced in fulfillment of our traditional mission as regulators and protectors of the public interest, and the new roles demanded by the changing utility marketplace. In the 21st century, we are not only utility regulators, but also market monitors, consumer protectors, advocates, educators, and promoters of new technology and economic development.

As part of this year's Annual Report, we have included a "State of the Public Utility Commission" - a summary of our work to balance the needs of utilities and their consumers.

We appreciate the opportunity to provide you with a snapshot of the issues and challenges facing the PUC.

Robert F. Powelson   John F. Coleman   Wayne E. Gardner   James H. Cawley   Pam Witmer

Legislative Priorities 2011-12

- Establish gas-safety authority over otherwise non-jurisdictional natural gas facilities
- Increase fines for natural gas pipeline safety violations
- Authorize gas safety jurisdiction over unregulated entities essentially providing public utility service with landfill gas and propane
- Authorize enforcement regarding payment of Unified Carrier Registration (UCR) fees paid by motor carriers that operate commercial vehicles in interstate commerce
- Authorize wastewater system improvements through an automatic adjustment clause or collection system improvement charge as well as natural gas and electric improvements through a distribution system improvement charge
- Provide for the Commission's exclusive jurisdiction over allocation of rail/highway crossing costs

Spending Reductions

- In each of the past two fiscal years, we managed our budget to achieve a savings of $3 million of the amount that was appropriated
- Savings used to offset additional assessments on the public utilities that fund our budget
- We plan to reduce our spending by at least $1.5 million during Fiscal Year 2011-12

PUC Reorganization

- Act 129 of 2008 granted the PUC flexibility to make major structural changes within the agency for the first time in decades
- Realigns the Commission's structure for greater efficiency and effectiveness moving forward
- Transparency and employee engagement remain top priorities
- New Executive Director hired to incorporate strategy and planning functions
- Other major changes we plan to implement include:
    - Affirmation of the centralization of administrative and personnel functions under the Director of Administration
    - Realignment of bureaus with regulatory functions under the Director of Regulatory Operations
    - Creation of Bureaus of Technical Utility Services and Investigation and Enforcement

Electric Shopping in PA as of November 2011

- 1,422,980 customers shopping statewide
- 25.2 percent of customers shopping statewide; 51 percent of the load shopping
- Nearly 226 suppliers are licensed by the PUC; 52 suppliers making offers to Pennsylvania electric customers on PAPowerSwitch.com

Investigation into PA's Competitive Electricity Retail Market

- En Banc Hearings and Technical Conferences held to gather comments and address issues
- Opportunity to assess the status of the market and to make the necessary adjustments for a more robust electricity shopping experience for PA consumers

PA PowerSwitch.com and Gas Switching Chart

- National model allows consumers to search for electric suppliers and competitive offers by zip code and make the switch
- New chart, updated weekly, tracks customer switching in every electric utility service territory, as well as the percent of customer load that has been switched to an alternate supplier
- Consumer educators partner with legislators, media, utilities and suppliers for educational events
- Monthly Gas Switching Chart developed to track customer switching in the natural gas industry

Implementation of Act 129 of 2008 (Energy Efficiency and Conservation)

- Approved the Energy Efficiency and Conservation, Smart Meter, and Time-of-Use Rate plans filed by Pennsylvania's seven major electric distribution companies
- Act 129 also sets forth mandated reductions in overall and "peak demand" electricity consumption by 2011 and 2013
- Examining if utilities met first reduction targets for May 2011

Marcellus Shale

- PUC Chairman serves on the Marcellus Shale Advisory Commission
- The Commission will undergo a comprehensive review of existing statutes, regulations and policies, and provide recommendations to develop a regulatory framework that is balanced and reasonable to ensure that PA maximizes the opportunity that Marcellus Shale presents in the most responsible manner possible
- Natural gas production volumes can be a game changer for Pennsylvania utility customers by providing low-cost energy
- With the huge boom in Marcellus Shale gas drilling, much of it in the Southwestern part of the state, the construction of a new training facility for natural gas pipeline inspectors to be located within Pennsylvania is being discussed internally by the Public Utility Commission

Pipeline Safety

- Unlike most other state commissions, the PUC does not have jurisdiction over all gathering and intrastate transmission pipelines
- Under Senate Bill 325 and House Bill 344, the PUC would gain jurisdiction over pipelines owned by cooperatives and municipalities, as well as those owned by propane, landfill gas and natural gas pipeline operators
- We strongly support the passage of a gas safety bill so the public can have the maximum confidence in the soundness and integrity of these systems
- Although we believe the natural gas transportation network in Pennsylvania as a whole is very safe, the recent tragic events in Allentown and Philadelphia have proven that we must take every step possible to replace vulnerable pipelines

Aging Infrastructure

- Unlike the roads and bridges we see every day, we cannot see the deterioration of underground pipes and wires that have delivered services to our homes for more than 70 years
- Because replacing this infrastructure is extremely expensive, it could take many years for utilities to make these replacements in an affordable manner through traditional ratemaking
- Based on PA's nationally recognized best-practice water distribution improvement service charge, House Bill 1294 would authorize the Commission to allow an automatic adjustment charge that enables natural gas, electric and wastewater utilities to recover certain infrastructure improvement costs between base rate cases through a surcharge on customers' bills
- Obtaining legislative approval to accomplish this is a priority for the PUC

Water Service Reliability and Infrastructure

- Implemented in 1997, the Distribution System Improvement Charge (DSIC) ensures the least possible rate impact on customers by evenly spreading out over time the cost of replacing and enhancing Pennsylvania's water system
- PA was the first state in the nation to enact and use the DSIC, and since that time, it has become a national "best practice"
- The PUC implemented a new water audit program to enhance tracking of levels of unaccounted-for water to enhance overall infrastructure reliability, help preserve water resources, limit water leakage and enhance customer service

Area Code Exhaustion

- Currently reviewing our decision to order a geographic split of the 814 area code, with technical conferences and additional public input hearings scheduled to further engage the public on this issue
- Working to address possible changes related to the existing 717 area code
- Currently monitoring the 570 area code and awaiting the latest exhaust data.

Public Utility Code Chapter 30 – Act 183 of 2004

- Establishing broadband availability throughout the Commonwealth by 2015
- Most rural telecommunications companies now make broadband available
- Embarq/CenturyLink and Windstream committed to 100 percent broadband availability by Dec. 31, 2013
- Verizon and Verizon North committed to 100 percent broadband availability by Dec. 31, 2015

Initiatives During 2011-12

- Expand eFiling
- Paper reduction measures to benefit external users
- Review of reporting requirements imposed on public utilities with the goal of streamlining, consolidating and eliminating
- Emerging Leaders Program to ensure succession planning


ONE WAY
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Introduction

Utility service is a critical element to the health and safety of Pennsylvania's residential and business customers. The Pennsylvania Public Utility Commission (PUC) ensures that electric, natural gas, water and telecommunications services are available upon request at a reasonable rate and provided safely with a reliable level of service. Similarly, customers using taxis, moving trucks or motor coaches expect fair rates and adequate service. The Commission also works to promote the safety of public highway-railroad crossings and compliance with railroad regulations.

With the restructuring of Pennsylvania's electric, natural gas and telecommunications industries, the Commission's role also is to oversee that transition and to educate customers so they may make informed utility choices.

Under the law, utilities are entitled to the opportunity to earn fair rates of return. The PUC recognizes that it is in the long-term public interest to permit a strong financial climate for investment in public utilities. By allowing a fair return to investors, companies can attract capital to provide and improve services for all customers.

Organization

The Commission is comprised of five full-time members nominated by the Governor for staggered five-year terms. The nominations must be approved by a majority of the state Senate. The Commissioners set policy on matters affecting utility base rates and services, as well as on personnel, budget, fiscal and administrative matters. Commissioners take official action on cases during regularly scheduled public meetings.

The Commission has its headquarters in Harrisburg with regional offices in Philadelphia, Pittsburgh and Scranton. In Fiscal Year 2010-11, the Commission continued to strive to create a more open and user-friendly PUC. Information about the PUC, including copies of documents filed with and produced by the Commission, audio of certain Commission proceedings, forms, applications and summaries of public meetings, is available at www.puc.state.pa.us.

The PUC oversees nearly 7,000 entities furnishing the following in-state services: electricity; natural gas; telephone; water and wastewater collection and disposal; steam heat; transportation of passengers and property by motor coach, truck and taxicab; pipeline transmission of natural gas; and public highway-railroad crossings. Municipal utility service is exempt from PUC regulation, with the exception of services furnished beyond a municipality's corporate boundaries. Rural electric cooperatives, school buses, bottled water, heating oil, cable television, Internet service providers and wireless telecommunications services also are exempt from PUC regulations.

There have been many significant changes to the utility industry and to the Commission's responsibilities since the last major reorganization in 1976. Act 129 of 2008 gives the Commission greater flexibility to develop a new organizational structure that will improve the operation of the PUC. Accordingly, the Commission reviewed the organizational structure and has begun to realign the bureaus to meet the new challenges efficiently and effectively, in a manner where transparency and employee engagement remain top priorities.

Among the major changes is the creation of an Executive Director position that incorporates both strategy and planning functions. In addition, agency bureaus will be more accurately aligned with regulatory functions through a consolidation of technical advisory staff into a single entity, Technical Utility Services. The agency's prosecutory and advisory functions now are clearly separated, as well. A separate bureau, Investigation and Enforcement, serves as the prosecutory bureau for purposes of representing the public interest in ratemaking and service matters before the Office of Administrative Law Judge, and enforcing compliance with the states and federal motor carrier safety laws and regulations. The bureau also will handle rail safety enforcement proceedings that are referred by the Bureau of TUS. The Commission also is centralizing administrative and personnel functions under the Director of Administration, and realigning bureaus with regulatory functions under the Director of Regulatory Operations who will oversee the Law Bureau, the Bureau of Audits, the Bureau of Consumer Services, Secretary's Bureau and the new Bureau of Technical Utility Services and Bureau of Investigation and Enforcement.

In order to maintain a smooth reorganization, the Commission has appointed a transition team of various bureau directors to implement the plan and keep the Commissioners apprised of the progress.

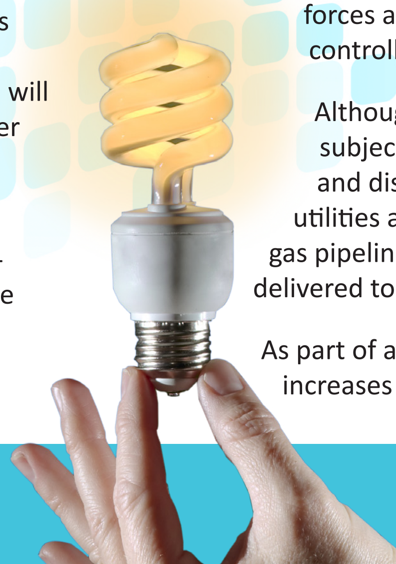
The Commission is funded by assessments of the regulated public utilities. The PUC may assess utilities up to three-tenths of 1 percent of gross intrastate revenue to cover the cost of regulation. Assessments are paid into the state Treasury's General Fund for use solely by the Commission.

The Public Utility Commission was created by the Pennsylvania Legislative Act of March 31, 1937, which abolished the Public Service Commission.

Broad Powers

The PUC exercises broad powers in meeting its regulatory obligations. In today's rapidly changing business environment, utilities must consider all of their options. Utility mergers, rate change requests, acquisitions and affiliated interest agreements continue to be filed before the Commission at a steady pace. With limited exceptions, utilities are required to obtain Commission approval for these transactions, as well as to operate, extend or abandon service. The PUC's responsibility is to ensure these actions are in the public interest.

The PUC also works diligently to ensure an effective transition to competitive markets in the electric, natural gas and telecommunications industries. The move toward competitive electricity markets through the passage of the Electricity Generation Customer Choice and Competition Act was based primarily on the legislative finding that "competitive market forces are more effective than economic regulation in controlling the cost of generating electricity."



Although the natural gas and electric supply markets are subject to competition, customers still receive transmission and distribution service from their local utilities. The local utilities also continue to maintain the electric lines or natural gas pipelines to ensure that safe, reliable utility service is delivered to customers.

As part of an overall strategy for preparing consumers for increases in electricity supply costs expected at the time of the expiration of rate caps, the Commission established regulations and policy statements that set the rules for default service for electric generation. The PUC has engaged consumer advocates and industry experts in efforts to mitigate any increases in future electric generation prices. The PUC worked to educate consumers; develop strategies to remove barriers for suppliers providing competitive electric service; approve phase-in or pre-payment plans and directed all utilities to file such programs if electric rates were expected to increase by more than 25 percent; update low-income programs that provide customer assistance; and implement default service pricing that reflects the least cost to consumers over the long term. We also are continuing to implement reasonable, cost-effective programs that consumers and companies can implement to conserve energy or use it more efficiently.

Over and above regulating rates for motor carriers that transport property, passengers and household goods, the PUC is responsible for enforcing rail and motor carrier safety laws. Motor vehicle, railroad facility and track inspections are important components of the PUC's safety program. The PUC also resolves complaints about unsafe conditions at rail crossings and enforces common carrier compliance with safety and insurance requirements.

If customers have complaints about a utility, they may seek help by calling a toll-free number and speaking with the PUC's Bureau of Consumer Services. Trained customer service representatives help to resolve billing and quality of service issues, establish payment plans or restore service. The toll-free number is 1-800-692-7380.

Rates

In order to provide economical and efficient service to Pennsylvania communities, the state grants electric distribution, natural gas distribution, steam heat, local telecommunications, water and wastewater companies the right to provide their service within a specified geographic area. History shows and economics dictate that the construction of energy and water distribution facilities by multiple utilities in the same location would be extremely costly and disruptive to communities. The utility is then regulated by the PUC to assure just and reasonable rates for safe and adequate service.

Competition is permitted in the supply of electricity and natural gas. Charges for the supply of electricity and natural gas by licensed competitors are not regulated and are based on market prices. The PUC exercises no jurisdiction over those market prices. Many electric utilities are operating under negotiated generation rate caps for supply services. As of Jan. 1, 2011, all of those rate caps expired. The prices for the delivery through the distribution system of electric and natural gas continue to be regulated by the PUC.

Competition also is permitted for telephone service. Most incumbent local telephone companies operate under a price stability formula that limits their ability to seek rate and revenue increases based on the rate of inflation and other factors. The rates for competitive local exchange carriers that are competing against the incumbent local telephone companies also require PUC approval. Legislation passed in 2004 categorized interexchange carrier services, such as long-distance toll, as competitive and subject to permissive tariffs. The long-distance company has the option of maintaining a tariff on file with the Commission or operating without a tariff subject to state contract law.

Filing for a Fixed Utility Rate Increase

When a regulated utility, other than telecommunications providers, seeks a distribution rate increase, it must file a request with the PUC that shows the proposed new rates and effective date, and must prove that the increase is needed. The utility also must notify customers at least 60 days in advance of the filing of the proposed effective date. The notice must include the amount of the proposed rate increase, the proposed effective date and how much more the consumer can expect to pay.

A handful of incumbent local exchange carriers have simplified ratemaking plans, similar to the regulatory regimes described above. However, a general rate increase for telecommunications utilities follows a different path due to the more advanced state of competition. Major rate revisions for incumbent local exchange carriers under price cap regulation are subject to a rate ceiling for residential dial tone, an inflation formula, and company-specific criteria and filing deadlines ranging from a 30-day Commission review period to a 90-day Commission review period. Competitive local exchange carriers, long-distance toll providers, and competitive access providers may file rate revisions under either a one-day or a 30-day notice period, depending on the type of filing.

How Are Rates Set?

The standard ratemaking process ensures the lowest reasonable rate for consumers while maintaining the financial stability of utilities. Under the law, the utility has the opportunity for recovery of its reasonably incurred expenses and a fair return on its investment. The PUC evaluates each utility's request for a rate increase based on those criteria.

How Long Does It Take?

By operation of law, the rate request for electric, natural gas, steam heat, water or wastewater companies is suspended for up to seven months if the PUC does not act before the proposed effective date. The PUC uses that time to investigate and determine what if any portion of the requested increase is justified. During the investigation, hearings are held before an Administrative Law Judge (ALJ), at which the evidence in support of the rate increase is examined and expert witnesses testify. In addition, consumers are offered an opportunity to voice their opinions and give testimony. Briefs may be submitted by the formal parties. A recommendation to the PUC is made by the ALJ. Finally, the matter is brought before the Commissioners for a vote and final decision. Including the 60-day notice period, the rate increase process can take about nine months.

Hearings and Recommendations

When the PUC investigates a rate increase, it is assigned to an ALJ, who is an attorney with experience in administrative law. The ALJ presides at formal hearings, which are open to the public and conducted like a formal court proceeding.

At the formal hearing, the company, the PUC's Bureau of Investigation and Enforcement (I&E) and other parties such as the state's Office of Consumer Advocate and the state's Office of Small Business Advocate present evidence, and their witnesses are subject to cross-examination. I&E reviews the company's records and requests, and presents its view regarding what is in the public interest. Individual consumers may become formal parties by filing a formal complaint. Consumers may speak for themselves, or an attorney may represent individual consumers or groups of consumers. Consumers also can have their say informally by writing or calling the PUC, or by testifying at a public input hearing, which may be conducted by the ALJ in the utility's service territory. By providing testimony, consumers place their views in the official file on the case. Consumer testimony becomes part of the record on which the PUC will base its decision.

After weighing the evidence and hearing the arguments, the ALJ writes a recommended decision addressing each issue in the case within the limits set by law. The recommended decision may approve, disapprove or modify the original request. Parties may file exceptions to the judge's decision. Subsequently, reply exceptions may be filed. Sometimes, rate cases are resolved after all of the parties reach a settlement on the issues. The entire matter is then sent to the Commissioners for a vote at a public meeting.

Final Order

The Commissioners make the final decision, authorizing rates that: (1) permit revenues that allow the company to meet its reasonable expenses, pay interest on its debt and provide a fair return to stockholders so it will continue to attract investment; and (2) assign the proper rate for residential, commercial and industrial customers that attempts to reflect the cost of service. The Order has the weight of law unless the PUC changes it in response to a petition for reconsideration, or it is successfully challenged in court.

Consumer Role

By law, consumers must pay for the service they use, which includes a share of the reasonable cost of utility company expenses such as operating and maintenance expenses, administrative expenses, depreciation and taxes. While the ratemaking process is complex, consumers have the right to be informed about the process, receive an explanation of their utility bills, have their complaints addressed in a prompt and fair manner, and receive continuous utility service if payment responsibilities are met.

Consumers have a right to participate in the ratemaking process and can do so by filing an informal complaint, which can include attending and/or testifying at a public input hearing. They also can file a formal complaint or complete an objection and comment form for rate cases. Forms and additional information about filing a complaint or an objection are available at www.puc.state.pa.us.

Multi-Utility Issues

The Commission deals with many issues that cross the boundaries of specific utilities. Those issues where significant changes occurred are highlighted below:

InfoMAP

An enhanced website search engine and an improved case management system have shaped a PUC that is more accessible than ever. The leading factor in this is the implementation of a new case and document management system – InfoMAP (Information Management and Access Project). The legislature provided funding for the replacement of the PUC computer system that dated from the late 1970s. InfoMAP automates workflows, reduces reliance on paper copies and improves public access to PUC information.

InfoMAP overhauled the PUC's case management system, improving the Commission's docketing, tracking and sharing of information. It also provides a single entry point to submit and access information, initiate transactions, and conduct business, thereby permitting electronic filings and giving the public electronic access to information filed with and produced by the PUC. InfoMAP went live in January 2008, and immediately the paper flurry within the Commission was significantly reduced.

Since the implementation of InfoMAP, access by external users to information maintained by the PUC has improved significantly, with most filings being eFiled or scanned and published to the website. This means interested parties can view filings made with the PUC online instead of coming to PUC offices to review paper files.

eFiling

During the fiscal year, eFiling gained popularity as more and more parties turned to filing electronically over traditional paper filings. A link to the eFiling system is available from the PUC website at www.puc.state.pa.us. The website includes instructions on how to set up an account, access the users' guide and preview the system.

On Feb. 17, 2009, the PUC began allowing all users including consumers, utilities and practitioners to begin eFiling. The widespread availability of eFiling was the latest step in creating a more open and transparent PUC.

Starting Jan. 19, 2011, the Commission expanded the size of documents that can be electronically filed from five megabytes to 10. The pilot has been so successful it was extended to Fiscal Year 2011-12. The Commission has also designated additional qualified documents acceptable for eFiling during this pilot. Pilot extensions will continue as the Commission plans to move forward with a proposed rulemaking to revise our regulations on electronic filing.

eFiling also allows users to pay PUC filing fees via the website using a credit card. Only “qualified documents,” designated by the Commission, are eligible for eFiling. Qualified documents include:

- Applications;
- Formal complaints;
- Comments;
- Exceptions;
- Reply exceptions;
- Petitions;
- Protests;
- Rate filings;
- Security certificates; and
- Supporting documents such as briefs, reply briefs and motions.

Public Meeting Summary

In fall 2008, the Commission began publishing summaries of each public meeting. In keeping with the mission to create a more open and transparent PUC, the summaries are designed to provide an overview of the action at each Commission Public Meeting. The summaries contain a brief overview of the cases considered, motions and final decision. In Fiscal Year 2010-11, the Commission issued 25 summaries, which are posted on the PUC website and e-mailed to members of the legislature.


PUC Public Meeting Summary

Homeland Security & Emergency Preparedness

When it comes to emergency preparedness and security, the Commission has a direct support relationship with the Pennsylvania Emergency Management Agency (PEMA) and other Commonwealth agencies and commissions.

During emergencies, a Commission team mobilizes at the Pennsylvania State Emergency Operations Center (SEOC) in Harrisburg. The PUC Emergency Management Response Team (ERT) under the direction of the Emergency Preparedness Coordinator provides assistance to utilities responding during an emergency, and coordinates with other state agencies to ensure that all available resources are being used. Its primary goal is to quickly and effectively meet the needs of those responding to an emergency. The team also makes sure a clear line of communication is available

from the utilities to the PUC, PEMA, the Governor and his staff, as well as other Commonwealth agencies and commissions.

The Commission also has liaisons from its bureaus of Technical Utility Services, Transportation and Safety, and the Office of Communications, who act as round-the-clock contacts for PEMA for utility-related emergencies on an ongoing basis. The PUC also has a seat on the Commonwealth Emergency Management Council.

In addition, throughout the stormy winter and summer months, the Emergency Preparedness Coordinator participates in conference calls and emergency meetings with PEMA, the National Weather Service, and other Commonwealth agencies and commissions to discuss the preparedness of the utilities and the ERT for the potential effects of an anticipated storm.

The Commission also works with the utility industry, state agencies and other stakeholders through several task forces and working groups, including the Drought Task Force, Pennsylvania One Call, Commercial Vehicle Safety Alliance, Federal Railroad Administration, Pennsylvania Water/

Wastewater Agency Response Network (PAWARN), 9-1-1 Task Force and several National Association of Regulatory Utility Commissioners (NARUC) committees. The Commission has developed relationships with the nine regional counter-terrorism task forces, and acts as a liaison among the utilities and county emergency management agencies when necessary.

The Commission ERT has undergone Homeland Security sponsored training, and is certified in the National Incident Management System (NIMS) and the National Response Framework. Throughout the year, the ERT participates with PEMA on developing and executing several training exercises, including winter weather drills and nuclear power facility emergency exercises.

The Commission also has developed a program to have all applicable Commission staff trained in NIMS. The Commission is NIMS compliant for Fiscal Year 2010-11 and will continue to maintain compliance for future years as requirements are updated and staff changes.

The Commission also has in place a self-certification regulation that requires each regulated utility to certify in an annual filing that it has reviewed its physical security, cyber-security, emergency and business continuity plans, as well as conducted tests or drills of these plans. This regulation followed a recommendation from the PUC's investigative report on House Resolution 361.

Federal Stimulus Funding

Commission Received $1 Million Federal Grant

The Commission received grant funding through the American Recovery and Reinvestment Act of 2009 (ARRA). Specifically, the PUC received $1,068,000 in funding through the Electric Regulation Assistance Program that is made available to state public regulatory agencies to help them deal with the increased caseload created by the ARRA in areas such as energy efficiency, smart grid, demand-response equipment, transmission, and electricity based renewable energy.

Using grant funds, the Commission hired two staff to handle inquiries and requests for information from the public, utility customers and customer-generators in the areas of Act 129 program implementation and measure installment; utility net metering; and interconnection;

Alternative Energy Portfolio Standards-solar installations (PA Sunshine Program); alternative energy credit certification; and the Generation Attribute Tracking System (GATS), the alternative energy credits registry designated by the PUC.

Also using grant funding, an additional staffer was hired to perform public outreach work focused on electric competition and rate caps, energy efficiency and conservation, and renewable energy initiatives.

Finally, also using grant funding, another staffer was hired to analyze electric-related issues that impact the rates that Pennsylvania electric consumers pay. This position investigates and analyzes electric utility claims that involve Act 129-related compliance filings and annual reviews.

Commission Completed an Investigation Required by the ARRA Regarding Aligning Utility Ratemaking Policies with Energy Conservation Goals.

A working group issued a Final Report on Jan. 21, 2011, in the investigation to ensure the Commonwealth's compliance with and eligibility for a portion of $3.1 billion in grants under the Federal State Energy Program. Those grants are contingent upon the states seeking to implement utility ratemaking policies to ensure that utility financial incentives are aligned with the promotion of energy efficiency and conservation. On April 16, 2009, the Commission initiated the investigation. Interested parties submitted comments on July 6, 2009, and reply comments on Aug. 6, 2009. The Commission held a technical conference on Nov. 19, 2009. Based on the discussions at the technical conference, the Commission formed a working group to further discuss issues regarding the ARRA and to prepare a report regarding potential policies that could be implemented by the Commission to ensure compliance with the ARRA. The working group was formed on Jan. 18, 2010, and held meetings in March, April and June. Comments were received and on July 28, 2011, the Commission issued an Order concluding the investigation.

Commission's Budget

Executive Government Operations

General Government Fund	General Fund	General Fund
	Estimated 2010-11 Expenditures	Approved 2011-12 Budget
State Funds:		
Personnel	$44,770,000	$45,889,000
Operating	10,767,000	12,485,000
Fixed Assets	120,000	124,000
Other	346,000	400,000
Total State Funds	**$56,003,000**	**$58,898,000**
Federal Funds:		
Personnel	$3,220,000	$3,005,000
Operating	1,037,000	1,119,000
Total Federal Funds	**$4,257,000**	**$4,124,000**
Total Commission Budget:	**$60,260,000**	**$63,022,000**

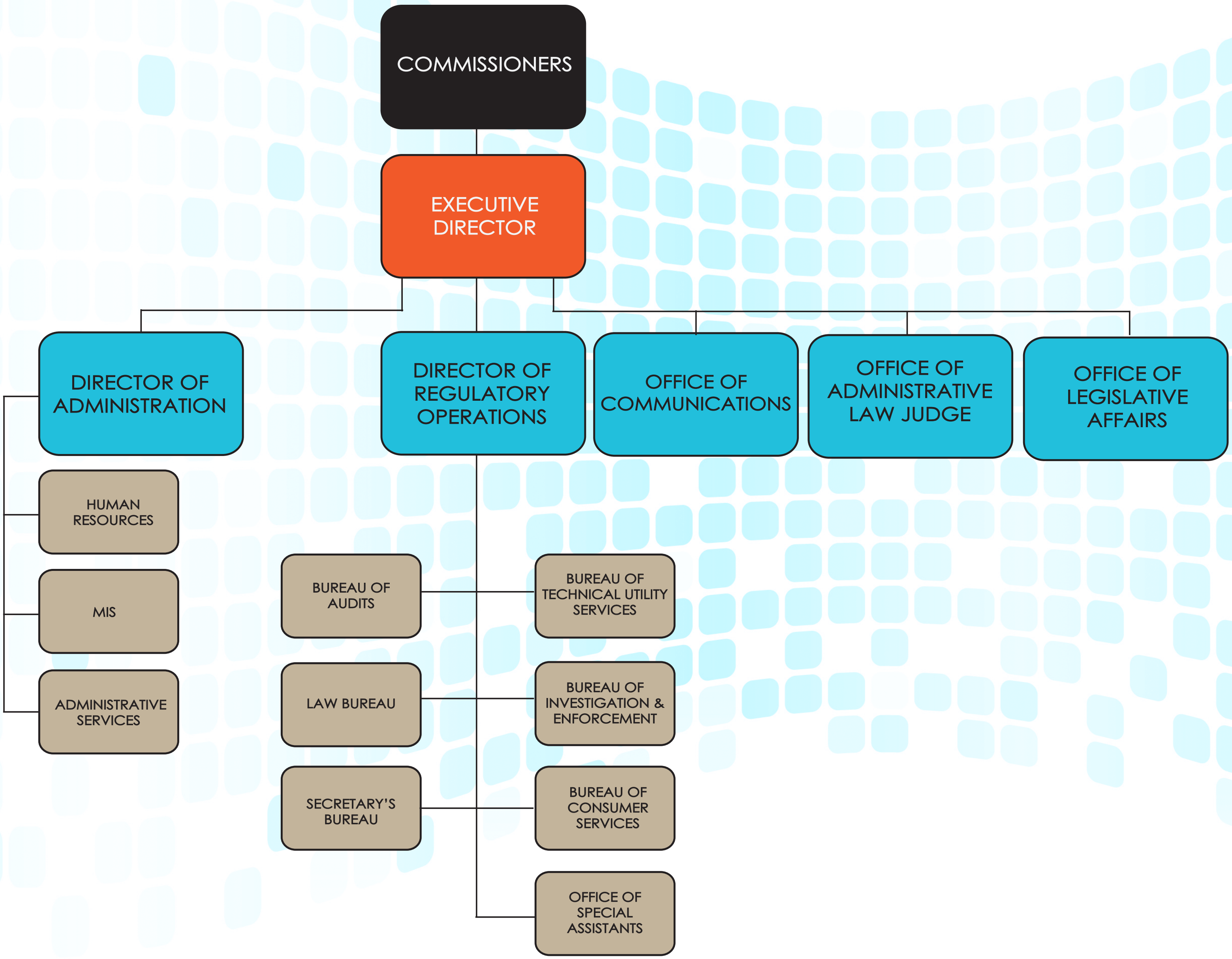
Other Revenue Sources

	2009-10 Receipts	2010-11 Receipts
Filing & Copy Fees	$196,937	$205,644
Electric Generation Application Fees	33,950	38,500
Fines	373,118	262,241
Federal - Gas Pipeline Safety	793,520	709,722
Federal - Motor Carrier (MCSAP)	1,043,849	1,275,396
Federal - ARRA Electric Reg. Asst.	-	272,231
Federal - ARRA Smart Grid	-	45,348
Total	**$2,441,374**	**$2,809,082**

2009-10 Application Fees, Filing & Copy Fees & Fines

	Electric Generation Application Fees	Fines	Filing & Copy Fees	Total
1st Quarter	$13,650	$36,717	$58,883	$109,250
2nd Quarter	10,850	68,429	40,730	$120,009
3rd Quarter	5,600	125,925	44,454	$175,979
4th Quarter	8,400	31,170	61,578	$101,148
Total	**$38,500**	**$262,241**	**$205,645**	**$506,386**

Organizational Chart



Bureau Directors

Jan H. Freeman

The Executive Director is responsible for the oversight of the day-to-day management of the Commission functions and staff. This position is responsible for the planning, direction and organization of the overall operations of the Commission.

Karen O. Moury
Director of Regulatory Operations

Robert C. Gramola
Director of Administrative Services

Tom Charles
Director of Communications

June Perry
Director of Legislative Affairs

Charles E. Rainey Jr.
Chief Administrative Law Judge

The Director of Regulatory Operations oversees the PUC's bureaus with regulatory functions, including the Law Bureau, the Bureau of Audits, the Bureau of Consumer Services, Secretary's Bureau, the Bureau of Technical Utility Services and the Bureau of Investigation and Enforcement.

The Director of Administration is responsible for overseeing administrative and personnel functions. The Office is comprised of the Office of Human Resources which is responsible for handling all personnel issues, and providing administrative and advisory services to all PUC management; Management Information Systems which oversees information and technology; and the Office of Administrative Services which is responsible for the preparation of the Commission's budget, collection of assessments, various fiscal operations, processing of contracts, and office services.

The Director of Communications is accountable for Commission media relations, employee communications and consumer education, in addition to acting as the lead staff for the Consumer Advisory Council.

The Director of Legislative Affairs acts as the liaison between the PUC and the Governor's Office, the General Assembly and the Pennsylvania Congressional Delegation. The Office identifies legislation that may affect the Commission or public utilities and obtains staff analysis; provides bill analysis and relevant information to the legislature; and promotes the Commission's position on legislation and issues with the General Assembly. The Office also handles requests for information from the Governor, legislators and constituents.

The Chief Administrative Law Judge fulfills a judicial role within the Commission by hearing cases, mediating cases through the alternative dispute resolution process and issuing decisions. The Bureau's primary duty is to provide fair and prompt resolution of contested proceedings before the Commission. The Administrative Law Judges (ALJs) are attorneys with experience in administrative law. They are independent judges who preside over the hearings in cases, which can include consumer complaints, rate filings, investigations, ability to pay/billing disputes and applications. ALJ decisions are based upon a record of evidence, legal precedent and policy.

M. Carl Lesney
Director of Audits

Johnnie E. Simms
Director of Investigation and Enforcement

Alexis Bechtel
Director of Consumer Services

Paul Diskin
Director of Technical Utility Services

The Bureau of Audits performs financial, management, operational and specialized audits on electric, natural gas, steam heat, wastewater, water and telecommunications utilities. It also reviews certain adjustment clause rate filings. The Bureau also conducts a limited number of reviews of the annual assessment reports for transportation companies. The audits may result in recommendations to refund over-recovered costs and/or to improve accounting or operational procedures that, if adopted, may save the utilities money, which may result in significant one-time savings for utilities or become annual savings. The Bureau also is responsible for auditing the annual reconciliation statements associated certain water companies authorized to use the distribution system improvement charge.

The Bureau of Investigation and Enforcement serves as the prosecutory bureau for purposes of representing the public interest in ratemaking and service matters before the Office of Administrative Law Judge, and enforcing compliance with the state and federal motor carrier safety and gas safety laws and regulations. The bureau handles rail safety enforcement proceedings that are referred by the Bureau of TUS. The Bureau also prepares reports for the Commission, provides technical support for other bureaus and participates in working groups on energy issues.

The Bureau of Consumer Services responds to and investigates informal complaints from residential and small commercial customers. The Bureau also serves as an intermediary between utilities and consumers, working to resolve complaints or develop payment arrangements. The Bureau provides consumers with utility-related information and monitors compliance with PUC regulations regarding consumers. The Bureau provides an analysis of utility performance when handling consumer complaints and issues.

The Bureau of Technical Utility Services serves as the principal technical advisory bureau to the Commission regarding fixed and transportation utility regulatory matters, as well as serves as an adviser to the PUC on technical issues for electric, natural gas, water and wastewater, and telecommunications utilities. The Bureau offers policy recommendations on rates, tariffs and regulatory matters, processes fixed utility applications, and coordinates emergency operations of utilities. The Bureau processes filings such as securities certificates and affiliated interest agreements. The Bureau also reviews and maintains county 911 system plans; telecommunications relay service reports; annual financial reports; and utility tariffs.

Bohdan R. Pankiw
Chief Counsel

Rosemary Chiavetta
Secretary

Cheryl Walker Davis
Director of Special Assistants

The Law Bureau acts as the Commission's in-house legal counsel, providing legal advice to the Commission. The Bureau's director serves as Chief Counsel to the Commission. Three main categories of legal services are provided by the Bureau: advisory and representational. The Law Bureau represents the Commission before state and federal courts when the Commission's decisions are challenged. The Bureau also represents the Commission before federal agencies such as the Federal Communications Commission and the Federal Energy Regulatory Commission on issues that impact Pennsylvania

The Secretary's Bureau is the PUC's official point of contact with the public. The Bureau receives all official documents and filings, serving as the prothonotary of the Commission. All official Commission actions and decisions are issued over the Secretary's signature. All correspondence and filings must be addressed to the Secretary to be considered filed before the Commission. The Bureau receives, enters, indexes and assigns all filings to appropriate bureaus through InfoMAP, which is the Commission's document and case management system. The Secretary's Bureau also is responsible for coordinating and monitoring all Public Meeting agendas and meeting minutes, and issuing all Commission Orders and Secretarial Letters.

The Office of Special Assistants, as the Commission's advisory support bureau, is comprised of attorneys, rate case review specialists and administrative support staff. The Bureau drafts Opinions and Orders for the Commission to vote on at Public Meetings, as well as reviews and offers recommendations on the exceptions to Administrative Law Judge decisions, petitions for reconsideration and requests for extensions of filing deadlines.


PAPowerSwitch
Pennsylvania Public Utility Commission
Shop
Switch
Save
Electric Bill
Understanding

Consumers

The Commission remains committed to monitoring and evaluating utility performance, as well as working aggressively to educate consumers about critical utility issues, including significant price increases for energy and their rights as utilities consumers.

During Fiscal Year 2010-11, the Commission focused on educating electricity customers about rising energy prices and the resources available to help them lower and pay their bills. In launching PAPowerSwitch.com, the Commission created a user-friendly tool to help consumers shop for their electric supplier and took the message to the community with consumer education events. The Commission continued with the implementation of the changes to the utility termination rules while working to educate consumers about these changes and their rights. Work continued on the rulemaking to bring the Standards and Billing Practices for Residential Utility Service (Chapter 56) in line with the Responsible Utility Customer Protection Act (Chapter 14). The Commission also continued to expand its consumer outreach activities by participating in the Commonwealth's annual Farm Show, hosting regional events and visiting local communities.

PAPowerSwitch.com

With PAPowerSwitch.com, the PUC is working to make sure consumers have the tools at their fingertips to make an informed decision about choosing an electric supplier. Just like consumers shop for other services, they can shop for the generation supply portion of their bill, making a decision based upon their needs and preferences. Generation supply costs comprise the majority of the average electric bill. When shopping for electricity, transmission costs are included in the "price to compare" that allows consumers to compare their utility's bill to that of a competitive supplier.

Putting the power in consumers' hands to choose their electric generation supplier began with the 1997 Electricity Generation Choice and Competition Act. Under the law, electric rates were

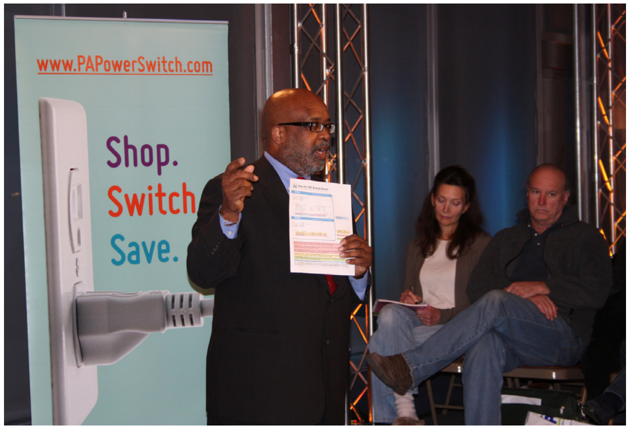
capped to ease the transition to competitive markets. As of Jan. 1, 2011, all rate caps expired. For many, the expiration of electric rate caps has brought an increase to electric rates. Consumers have the power to switch to a competing supplier who may offer the lowest price, or provide a specific service such as green/renewable energy.

Pennsylvania residents have the right to choose their electric supplier, but the ability to switch depends on whether competitive offers are available. The power to switch electric suppliers gives consumers greater control over their electric bill. Many consumers look for an impartial voice to put the offers being made by the electric suppliers at their fingertips in a user-friendly format. On PAPowerSwitch.com, the power is in the hand of consumers to shop for an electricity supplier – it's a zip. Consumers just click and enter their zip code to find electric suppliers making offers in their area. A tool also allows them to enter their monthly usage to get an even more precise estimate of their bills if they choose to stay with their utility or use a competitive electric supplier.

PAPowerSwitch.com gives consumers the information to "Shop. Switch. Save."

The PUC partnered with local television in southeast Pennsylvania to bring the power to switch electric suppliers directly to the community. To make the website "come alive" at the community outreach events, a bank of computers was made available for consumers to compare prices. Nine competitive electric suppliers, representatives from PECO, and the Office of Consumer Advocate participated in the events. Through its partnership with NBC 10 in Philadelphia, the Commission held three PAPowerSwitch events in the first quarter of 2011 in the PECO service territory. Approximately 2,000 electric shoppers turned out on January 19 at the King of Prussia Mall.

In February, NBC 10 staged an "in-studio" event for dozens of electric shoppers. Commissioners highlighted the benefits of electric competition and demonstrated how to shop on PAPowerSwitch.com, while PUC consumer educators walked consumers through the website.



More than one-million Pennsylvanians have now switched to a competitive electric supplier, and the number continues to grow each week. A surge in electric shopping in the PECO service territory during the First Quarter of 2011 propelled Pennsylvania past the one-million milestone. Rate caps on generation expired on Dec. 31, 2010, in PECO and three other service territories, opening the door to shopping for more than 60 percent of the Commonwealth's electric customers.

Since the beginning of the year, southeastern Pennsylvania has become the Commonwealth's "hot spot" for electric shopping, with up to 10,000 PECO customers switching to a competitive supplier on a weekly basis. Because of such robust activity, the statewide total grew more than a quarter million shoppers since the beginning of the year.

Other features of PAPowerSwitch.com:

- The PUC recently added a Spanish-language companion site.
- Suppliers now have the ability to update their own prices and company information.
- Consumer alerts are e-mailed to customers who plugged their zip codes and contact information into the site to receive weekly updates on suppliers and prices available in them.
- A new, larger, printable version of the zip-code-searchable supplier list is now available.

In addition to logging onto PAPowerSwitch.com, consumers can call 1-800-692-7380. The Commission's call center and consumer educators can print a list of suppliers in a consumer's zip code and mail it to those consumers without Internet access. The PUC has available a new "PA PowerSwitch" brochure and a post card designed to promote the new website and encourage people to Shop. Switch. Save.

Consumer Education on Electric Prices

Part of the Commission's policies to mitigate and prepare Pennsylvania electricity customers for price increases includes working with electric utilities to implement utility-sponsored consumer-education plans for their service territories.

Each of the state's electric distribution companies (EDCs) under the PUC's jurisdiction filed a proposed consumer-education plan that is tailored to their service territory as required under a May 17, 2007, Commission Order that established policies to mitigate higher electricity prices. The Commission approved each after ensuring the plans met the requirements. The Commission, along with the Office of Consumer Advocate and the Office of Small Business Advocate continue to review the consumer-education materials filed by utilities in accordance with their plans.

The utilities' plans contain provisions to educate consumers about price increases while providing information on electric competition, demand side response, low-income programs, and energy conservation and efficiency.

The plans also proposed appropriate budget levels and cost-recovery mechanisms. The intention of requiring these plans was to prepare Pennsylvanians for the removal of the electric rate caps and to enable customers to make informed decisions regarding their own levels of electric use. Each plan is posted on the PUC website, www.puc.state.pa.us, under the Electricity tab.

Consumer Outreach Summary

The PUC's consumer outreach specialists have provided utility education and outreach to thousands of consumers by working with health and human service providers, consumer advocates, utility community relations specialists, seniors and low-income consumers.

The outreach team travels the state to ensure consumers from all socioeconomic backgrounds are educated and understand their rights as utility customers. In Fiscal Year 2010-11, the outreach team hosted numerous workshops, free seminars and roundtable discussions throughout the state. Outreach specialists also support and participate in community fairs, legislative forums, senior expos, public input hearings and other educational events.

During those events, consumer-outreach specialists provide materials to consumers about complex utility issues, including shopping for a competitive electric generation supplier; fact sheets outlining the Responsible Utility Customer Protection Act; customer assistance programs; energy efficiency and conservation tips; transmission line siting; and rising energy prices.

The PUC's outreach specialists are committed to assisting consumers in addressing specific individual concerns and offering solutions to utility-related issues. In 2010-11, the team focused on educating Pennsylvanians and nonprofit, community-based organizations through the PUC's "Prepare Now" campaign, "Be Utility Wise" initiatives, and PAPowerSwitch.com's "Shop. Switch. Save."

Throughout the year, the consumer outreach specialists staffed a variety of public input meetings regarding base rate increase requests pending before the Commission, as well as plans to provide relief prior to area code exhaustion of the 814, 717 and 570 area codes.

Overall, the PUC consumer outreach specialists encouraged consumers to:

- Be aware of expiring electric rate caps and the associated increase in electric bills. Consumers were provided with information on the expiration of rate caps, and how to shop for electricity.
- Use electricity, natural gas and water wisely to conserve resources and save money. Consumers were given informational materials and fact sheets providing conservation tips on how to become more responsible and aware of their utility usage.
- Know their rights as responsible utility consumers and be aware of important changes in the law related to utility shut-offs (Chapter 14).
- Consider budget billing options as a way to make heating bills more predictable and affordable throughout the year.
- Understand area-code relief proposals.
- New partnerships and networking opportunities were developed by attending training sessions and informational meetings with other state agencies and community-based organizations.

PA Farm Show

In January 2011, the Commission participated in the 95th Annual Farm Show to inform thousands of visitors about the role of the PUC as an available resource to address utility questions or concerns.

Over 50 PUC employee volunteers at two locations staffed a table and spoke with consumers who had questions regarding various industries regulated by the Commission. The PUC booth contained information about energy, telephone, transportation, water and wastewater issues. The Commission's primary focus was to educate consumers to prepare now for higher energy costs, and provide tips for weatherizing homes and conserving energy.

With the expiration of rate caps statewide beginning Jan. 1, 2011, the PUC increased its education at this year's show, with a separate booth dedicated to the Commission's one-stop shop for electric shopping, www.PAPowerSwitch.com. Most of the questions fielded by volunteers at both booths involved the electric shopping process.

Information also was available on:

- Programs to help low-income consumers pay utility bills.
- How consumers can take advantage of the Alternative Energy Portfolio Standards Act of 2004.
- Act 183 of 2004, which requires telecommunications companies to provide access to high-speed Internet by 2015.
- Telecommunications Relay Service (TRS), which enables Pennsylvanians to communicate by telephone with people who are deaf, hard of hearing or speech disabled (*See Telephone*).

Prepare Now

During Fiscal Year 2010-11, the PUC continued to work with electric and natural gas companies to help consumers "Prepare Now" for the higher costs of winter heating.

In a November 2010 letter, the Commission asked electric and natural gas utilities under its jurisdiction to join the PUC in reaching out and educating consumers. The letter also stressed the importance of the Low-Income Home Energy Assistance Program (LIHEAP) and the impact the program has on helping low-income consumers restore and maintain their utility service. A new campaign called "Faces of LIHEAP," will feature remarks from utility representatives, government officials and National Football League Hall of Famer Franco Harris, who is honorary chair for Partners for Warmth. The letter also reminds the utilities of their responsibilities under the state's utility termination and reconnection law, also known as Chapter 14. In February 2011, the PUC reminded consumers at risk of termination to call their utility to seek resources to help maintain electric or natural gas utility service for the winter months. This year, the Pittsburgh natural gas companies continued their LIHEAP efforts and unified under a new brand name – called "Partners for Warmth"

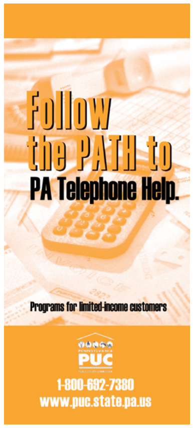
The winter of 2010 was the eighth winter that the Commission urged consumers to "Prepare Now." The message is simple: "Prepare Now" for higher energy costs this winter. Learn about changes in the law related to utility shut-offs and know your rights. Save money by learning how to conserve energy. Heat your home safely. Explore budget billing options. Look into programs that help low-income customers restore and maintain service. Visit www.puc.state.pa.us, and click on "Prepare Now" or call the PUC at 1-800-692-7380.

Lifeline Awareness Week

In conjunction with a national initiative to promote the awareness of Lifeline and Link-Up discount programs, the PUC joined other state agencies and industry representatives to help residents "stay connected" through various media events and community exposure.

Gov. Ed Rendell signed a proclamation designating Sept. 13 to 19, 2010, as Pennsylvania Lifeline Awareness Week. Through various media outlets, as well as consumer events, the Commission emphasized the importance of these assistance programs, which offer discounts to help residents gain access to basic local telephone service.

The Lifeline 135 program is available for customers of all qualified telephone service providers. Under the program, customers who participate in certain public assistance programs, or who have income at or below 135 percent of the federal poverty guidelines (currently $30,000 for a family of four) can receive a discount on their monthly local phone service for one telephone line. The discounts are paid out of the federal Universal Service Fund, which is subsidized by contributions from all telephone companies. The Link-Up provides a 50 percent reduction off the telephone installation charge, up to a maximum of $30, for qualifying households that do not currently have telephone service. In an effort to increase awareness about the program, the PUC developed an informational brochure, "Follow the PATH to PA Telephone Help" to provide information about Lifeline and other programs available to limited-income consumers.



Settlements with Utility Companies

In Fiscal Year 2010-11, the PUC approved settlements with utility companies following informal investigations into violations of the Public Utility Code or consumer complaints. In many cases, the companies agreed to improve communications with consumers.

■ **Aqua Pennsylvania Inc.** paid a $15,000 civil penalty and contributed $10,000 to the company's Helping Hands Fund, which helps low-income customers restore and maintain water service, after a settlement was reached between the company and the Commission. The settlement stemmed from an informal investigation of two incidents where employees hit utility lines during excavations.

■ **Telos II** paid a $1,250 fine after reaching a settlement with Commission staff as a result of violations including failure to have complete log sheets.

■ **Peoples Natural Gas Co.** paid an $80,000 civil penalty and agreed to establish several safety mechanisms as a result of a complaint against the company, which was triggered by an explosion and fire. A November 2008 National Transportation and Safety Board (NTSB) report determined that the probable cause of the incident was damage by a third party to Peoples' two-inch distribution line. The damage stripped the pipe's protective coating and made the pipe susceptible to corrosion and failure. The NTSB determined that Peoples was not at fault.

■ **UGI Utilities Inc.** spent $20,000 to utilize the services of an outside contractor to retain their work crews regarding excavation shoring safety. On April 24, 2009, a PUC inspector observed three holes at an excavation site in Bethlehem, where shoring was not being used. Shoring braces excavation sites to prevent cave-ins. The company also paid a $10,000 civil penalty.

The company has also paid a $17,500 civil penalty, after an informal investigation was launched as a result of a complaint raising concerns about a September 2009 outage and location of propane tanks that served the Farmington Way residential subdivision in Lititz, Pa.

■ **T.W. Phillips Gas and Oil Co.** implemented a two-pronged program designed to improve the company's public education on gas safety and preventing damage to gas lines, using $15,000 to expand and improve a company program to educate local firefighters in its service territory on the dangers of natural gas fires. The company also agreed to devote $15,000 to a new program designed to educate children on preventing damage to buried gas lines and introduce three initiatives to increase the number of leak repairs on its pipeline system, especially the bare steel pipe. The company agreed to the settlement after an investigation of a gas explosion in Ringgold, Jefferson County, on Feb. 17, 2008, that damaged a residence.

■ **Peoples Natural Gas Co.** paid a $1,500 civil penalty for allegedly violating the Public Utility Code or Commission regulations. Prosecutory staff alleged that the company failed to provide the customer with information about obtaining a medical certificate in order to restore service and failed to determine if the customer was satisfied with the calls to the company. The company also agreed to implement corrected procedures to prevent similar occurrences in the future.

Customer Assistance Program Review

The Commission continued with a review of the proposed Universal Service and Energy Conservation Reporting Requirements rulemaking which establishes a consistent process for reviewing CAP program funding levels and other CAP provisions while reviewing companies' three-year Universal Service Plans. Comments were invited on several topics, including the impact of Low Income Home Energy Assistance Program (LIHEAP) grant application changes, affordability of CAP costs in conjunction with the recent economic decline, cost recovery and rate effects of program modifications. The Commission intends to finalize the rulemaking prior to June 2012.

The Commission also suspended several sections of the Policy Statement pertaining to the application of LIHEAP grants to a distribution company's CAP as being inconsistent with the Department of Public Welfare's (DPW) proposed changes to its LIHEAP 2010 Final State Plan. The Commission has received comments from interested parties on both the proposed rulemaking and policy statement.

The state's electric and natural gas competition laws require that every electric utility and major natural gas utility establish a CAP. In considering CAP design, funding and cost

recovery simultaneously, the Commission's goal is to balance the interests of the low-income customers who participate in CAPs with interests of all residential consumers. The funding levels and program design vary from company to company.

As part of the Commission's comprehensive examination of universal service programs, the Commission issued for comment a proposed rulemaking and policy statement revisions in August 2007 that address CAPs, under which low-income customers receive financial assistance in paying utility bills.

Chapter 14 Impact Report

On Jan. 14, 2011, the Commission issued its third biennial report on the implementation of Chapter 14, which was added to the Public Utility Code under the Responsible Utility Customer Protection Act of 2004. The Commission is required to submit a biennial report to the Governor and legislature updating the effects of implementing Chapter 14. The Third Biennial Report concludes that the utilities have successfully implemented Chapter 14 since its passage in 2004. All reports are available on the Commission's website under Publications and Reports. The next report will be issued by Dec. 14 2012.

Chapter 14 seeks to eliminate the opportunities for customers capable of paying their utility bills to avoid doing so, and to provide utilities with the means to reduce their uncollectible accounts. The law changed the way regulated electric, water and major natural gas utilities handle cash deposits; termination of service; reconnection of service; payment arrangements; and the filing of termination complaints by residential customers.

The Commission implemented Chapter 14 in a manner that achieves the policy goals of increasing utility account collections and avoids passing along bad debt costs to paying consumers, while ensuring that service remains available to all consumers on reasonable terms and conditions. The Commission is dedicated to using a collaborative process that accounts for the needs of both utilities and consumers, and gives all parties an opportunity to participate.

Cold Weather Survey Results

Each year, prior to the winter heating season, the PUC requires electric and natural gas utilities to check residential properties where service has been terminated due to non-payment. The goal of the annual Cold Weather Survey is for the company to attempt to reach payment agreements with the occupants so service can be restored.

The Commission requests that utilities make four attempts to contact the consumer or a responsible adult occupant at the property where service has been terminated. These contacts include a combination of telephone calls and letters to establish contact, with the fourth attempt being a personal visit to the property.

In December 2010, the survey found that 17,294 occupied households were without heat-related utility service. An additional 2,363 homes were using potentially unsafe heating sources, bringing the total homes not using a central heating system to 19,657. The total number was 21,029 in 2009.

Residential electric households not using a central heating system totaled 4,499, while 15,158 natural gas households had no service. About 10,690 households – 54 percent of the total accounts without service – were in the Philadelphia area. The results also showed that an additional 19,323 residences where services were terminated appeared to be vacant.

The companies resurveyed the households without utility service in February 2011. At that time, the total number of homes not using a central heating system decreased by 29 percent to 13,859.

Universal Service Programs and Collections Performance

The PUC issued the 2009 annual summary of the universal service programs and collections performance of Pennsylvania's major electric distribution companies (EDCs) and natural gas distribution companies (NGDCs) in Fiscal Year 2010-11.

Universal service programs are designed to help ensure that all customers have access to utility service no matter what their income. Programs include the Low Income Usage Reduction Program (LIURP), Customer Assistance Programs (CAPs), Customer Assistance and Referral Evaluation Services (CARES), and Hardship Funds.

Generally, electric and natural gas customer households that are enrolled in universal service programs have average household incomes that are less than $15,700 per year.

According to the report, the gross write-offs ratio for the electric industry was 2.10 percent in 2009, compared to 1.85 percent in 2008, while the natural gas industry average was 3.92 percent in 2009 and 3.52 percent in 2008.

According to the report, EDCs used $189,171,318 to enroll 240,002 customers in CAPs where on average those customers pay 79 percent of their total bill.

NGDCs used $197,875,832 to enroll 192,924 customers in CAPs where on average those customers pay 85 percent of their total bill, according to the report.

EDC customers also received $63 million in total LIHEAP grants while NGDC customers received $107.5 million in total LIHEAP grants. The full report is available on the PUC website at www.puc.state.pa.us under Publications and Reports.

Utility Consumer Activities Report and Evaluation

Helping Pennsylvania consumers resolve utility problems remains a major concern for the Commission. Full-time investigators within the PUC's Bureau of Consumer Services (BCS) handle a variety of consumer contacts related to billing problems, service delivery and repairs. The 2009 Utility Consumer Activities Report and Evaluation (UCARE) shows that BCS investigated 18,147 consumer complaints in 2009, with 16,126 of those complaints coming from residential consumers and 2,021 from commercial consumers. The total number of consumer complaints declined by 11 percent from 2008-09.

BCS also handled 55,618 requests for payment arrangements from residential customers in 2009, a 9 percent decrease from 2008. The majority of requests for payment arrangements – 50,098 requests – involved electric or natural gas companies. In addition, 954 residential telephone consumers requested assistance in setting up payment arrangements in 2009, which is a 33 percent decrease from the number of payment arrangements requested in 2008.

From 2008 to 2009, terminations of natural gas service increased by 9 percent, while terminations for electric service decreased by 11 percent. Statewide, electric and natural gas terminations went from 294,682 in 2008 to 250,533 in 2009. Reconnections of electric and natural gas service decreased during the same period, going from 212,959 in 2008 to 197,938 in 2009.

At this time, water utilities are not required to report termination and reconnection data to the Commission, so BCS does not report this data in the UCARE report.

However, Aqua Pennsylvania Inc. and Pennsylvania American Water Co. (PAWC) voluntarily provide termination data to the Commission. Terminations for these companies increased from 35,227 in 2009 to 38,204 in 2010 – an 8 percent increase. Likewise, reconnections for Aqua and PAWC increased during the same period from 26,021 in 2009 to 28,659in 2010 – a 10 percent increase.

BCS also received 77,761 inquiries in 2010, a 3 percent increase from the previous year. Inquiries include information requests, requests for payment arrangements that BCS cannot accommodate and opinions from consumers. For the most part, these contacts did not require investigation by BCS. These inquiries came to the attention of BCS through the Commission's toll-free hotlines, other telephone numbers, the U.S. Postal Service and e-mail communication.

The PUC surveys consumers who have contacted BCS with a utility-related problem or payment arrangement request in order to monitor its own customer service. The 2010 survey results show that more than 82 percent of consumers said they would contact the PUC again if they were unable to resolve their problem by talking with the utility. Meanwhile, 77 percent of consumers rated the service they received from the PUC as "good" or "excellent."

This and other data appear in the Commission's 2010 UCARE report, which will be available on the Commission's website at www.puc.state.pa.us under Publications and Reports.

Customer Service Performance Report

Each year, the Commission prepares the Customer Service Performance Report. In addition to reporting company submitted data, the report provides information on how customers feel the major electric and natural gas companies are doing with customer service.

In 2009, the majority of electric and natural gas customers contacted said they were satisfied with the way company customer service representatives handled their calls.

Based on customer surveys, an average of 89 percent of electric and 80 percent of natural gas customers said they were either "satisfied" or "somewhat satisfied" with the ease of reaching their company. A greater percentage of customers said they were satisfied with the way company representatives handled their calls – 91 percent of electric customers and 85 percent of natural gas customers. A majority of the customers were satisfied with both the courtesy and level of knowledge demonstrated by customer service representatives.

The report also includes data provided by the utilities on the performance of the company's customer service operations. Two electric companies reported that their call abandonment rate had decreased from the previous year, indicating a performance improvement in this area. One increased, and three remained the same as the previous year. Abandoned calls are the number of customers who hang up while on hold to speak to a representative.

Four of the seven natural gas companies had a lower average call abandonment rate in 2009 than in 2008. Three of the major electric companies reported an improvement in the percentage of calls answered within 30 seconds, while three reported a decline.

After plummeting dramatically from 88 percent in 2007 to 58 percent in 2008, Allegheny Power's percent of calls answered within 30 seconds rose slightly to 60 percent in 2009. The average percentage of calls answered within 30 seconds for the electric companies in 2009 is 76 percent, down from 77 percent in 2008. All but one of the gas companies reported improved rates in the percentage of calls answered within 30 seconds. NFG answered 91 percent of its calls within 30 seconds in 2009, the highest percent of all the gas companies and better than the 73 percent reported for 2008. NFG attributes the improvement in telephone answering statistics primarily to a 4.6 percent reduction in call volume, as well as to assignment of additional staff to answer calls. The last time a company (gas or electric) reported over 90 percent of calls answered within 30 seconds was in 2002 when NFG reported 92 percent for this statistic. Columbia shows a marked improvement in its rate of calls answered within 30 seconds, from 69 percent to 82 percent. The average percentage of calls answered within 30 seconds for natural gas companies increased from 72 percent in 2008 to 78 percent in 2009.

The full report for 2009 is available on the PUC's website at www.puc.state.pa.us under Publications and Reports.

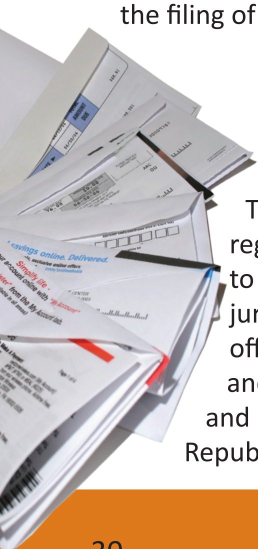
Chapter 56/Chapter 14 Rulemaking

In June 2011, the Commission approved a rulemaking, which addresses such provisions as winter termination; definition of customer; user without contract; application and credit standards; security deposits; the service termination process; medical emergency procedures; dispute procedures; protections for victims of domestic violence; electronic billing and payment; and medical certificates.

In September 2008, the Commission adopted a Notice of Proposed Rulemaking to amend 52 Pa. Code Chapter 56 to bring it into compliance with Act 201 of 2004 (Chapter 14 of Title 66). In March 2009, the PUC issued a Secretarial Letter to direct those utilities that had already adopted electronic billing programs to file comments regarding the successes and failures of their individual electronic billing programs.

Chapter 56 contains the Standards and Billing Practices for Residential Utility Service, and includes the regulations governing the termination process, credit, applications, billing, payment and dispute procedures.

Chapter 14 seeks to eliminate opportunities for customers capable of paying their utility bills to avoid payment, and to provide utilities with the means to reduce their uncollectable amounts. The law changed the way regulated electric, water, and major natural gas utilities handle cash deposits; reconnection of service; termination of service; payment arrangements; and the filing of termination complaints by residential customers.



Consumer Advisory Council

The Consumer Advisory Council (CAC) was created through a regulation in 1977 to advise the Commission on matters relating to the protection of consumer interests under the Commission's jurisdiction. CAC members are appointed by the following elected officials: the Governor; Lieutenant Governor; the Democratic and Republican Chairpersons of the Senate Consumer Protection and Professional Licensure Committee; and the Democratic and Republican Chairpersons of the House Consumer Affairs Committee.

PUC Consumer Advisory Council: Front row, let to right: Robert Christianson, Tim Hennessey, Cindy Datig. Back row, left to right: Lee Tolbert, Michael Bannon, George Silvestri, Tina Serafini, Tom LeCrone, John Detman, Harry Geller.

In addition, the Commission appoints "at-large" representatives that reflect a reasonable geographic representation of the Commonwealth, including low-income individuals, members of minority groups and various consumers. A person may not serve as a member of the Council if the individual occupies an official relation to a public utility or holds or is a candidate for a paid appointive or elective office of the Commonwealth. Council members serve two-year terms and may be reappointed. Council officers serve two-year terms. The Chairperson may not act for more than two consecutive terms.

The Council acts as a source of information and advice for the Commissioners. Interactions between the Council and the Commissioners occur through periodic meetings, and in writing via minutes of meetings and formal motions. Council meetings are generally held at 10 a.m. on the fourth Tuesday of the month in the PUC Executive Chambers in Harrisburg. The meetings are open to the public.

During this fiscal year, the CAC continued to focus on issues arising from the rate caps expiring, educating consumers statewide, proposed supplier marketing guidelines, the Marcellus Shale procedures, the Chapter 56 rulemaking and universal service programs.

The Council also received briefings on issues that the Commission has dealt with, including Chapter 14, the PUC's PAPowerSwitch website, Chapter 30, Cold Weather Survey, CAP policy, the legislative special session on energy, transmission lines, and the Alternative Energy Portfolio Standards Act.

PA Relay Service Advisory Board

In May 1990, the Commission established the Pennsylvania Relay Service Advisory Board. The purpose of the board is to review the success of the statewide Telecommunications Relay Service (TRS) and identify improvements that should be implemented. The board functions primarily as a TRS consumer group by providing feedback and guidance to the TRS providers and the Commission regarding communication assistant training, problem solving, outreach initiatives and service enhancements.

The board meets four times a year to advise the TRS providers on service issues, to discuss policy issues related to traditional TRS and Captioned Telephone Relay Service (CTRS), and to interact with Commission-appointed members. At each meeting, the traditional TRS provider and CTRS administrator give the board a status report of their activities. These reports focus on issues including call volumes, new service offerings, complaint handling equipment enhancements and outreach plans.

The 12 members of the board are appointed by the Commission and serve two-year terms. The Commission requires that the board consists of one representative from the Pennsylvania Telephone Association, the Office for the Deaf and Hard of Hearing (ODHH), and the traditional TRS provider (AT&T Communications of Pennsylvania LLC); two representatives from the Commission; and seven representatives from the deaf, hard-of-hearing and speech-disabled communities.

During 2009, board members from the deaf, hard-of-hearing and speech-disabled communities included representatives from the following organizations: the Hearing Loss Association of Pennsylvania; the Pennsylvania Society for Advancement of the Deaf; the Center for Independent Living of South Central Pennsylvania; Independent Living Program at the Western Pennsylvania School for the Deaf; Office for the Deaf & Hard of Hearing; and an individual from the deaf community.

As a user group, the board meeting agenda items primarily relate to quality of service and improving relay service. However, the board also has advised the Commission on many critical policy issues that affect TRS users.


Pennsylvania Relay Service Advisory Board: Front Row, left to right: Kristen Brandt, Pat Brockley and Melissa Sanders. Back row, left to right: Christa Cervantes, Leslie Kelly, Sharon Behun, Mina Knezevich, Shelia Brown, Todd Behanna, Eric Jeschke, Steve Samara and Chuck Hafferman.

Although the official consumer-education campaign has concluded, the Commission continues to work to educate consumers. Educators inform the hearing public about relay technology and enhance the opportunities of people with hearing loss and speech disabilities to communicate with the hearing public in their daily lives. They regularly provide TRS information and materials as they travel throughout the Commonwealth visiting numerous county fairs, festivals and other venues with large audiences.

Keystone Connection

The Commission continued its publication of the “Keystone Connection,” a newsletter that is released quarterly to about 1,200 subscribers, including news media and industry stakeholders. “Keystone Connection” provides a snapshot view of the utility markets under the Commission’s jurisdiction: electric, natural gas, transportation, telecommunications and water. The publication highlights the major issues that affect each industry, and includes coverage of all utilities, including news on consumer issues and general information on PUC happenings. Copies of the Keystone Connection are available on the PUC website at www.puc.state.pa.us under Publications and Reports.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Electric

The PUC regulates default service and distribution rates, ensures service reliability, and fosters the development of competitive electricity markets. The PUC participates in matters that impact the wholesale energy market. The PUC also regulates electric rates of some municipal systems that serve customers outside their boundaries. Since the implementation of Act 129 of 2008, the PUC reviews and approves energy efficiency and demand side response programs proposed by Pennsylvania's seven major electric utility companies.

The expiration of long-term electric generation rate caps, coupled with the implementation of Act 129 and its comprehensive energy efficiency and conservation measures, continues to change the way Pennsylvanians think about electricity consumption – an impact that is sure to be felt for years to come. In Fiscal Year 2010-11, electric generation rate caps expired for the remaining portions of Pennsylvania (West Penn Power, Met-Ed, Penelec and PECO). Currently, Pennsylvania has 11 electric distribution companies (EDCs) and 226 licensed electric generation suppliers (EGSs).

The Commission continued to move forward with efforts to mitigate the effects of rate cap expiration with a focus on developing strategies to remove barriers to competition; educating consumers; updating low-income programs that provide customer assistance; and implementing default service plans that reflect the least cost to consumers over time. The Commission's default service regulations and policy statement provide both guidance to the industry and suggested tools to mitigate the impact on consumers transitioning from capped rates for generation to rates based on wholesale market prices.

The main goal of Act 129 is to reduce energy consumption and peak demand throughout Pennsylvania. The Commission has worked to implement this groundbreaking legislation in phases, meeting all of the deadlines on its accelerated timetable.

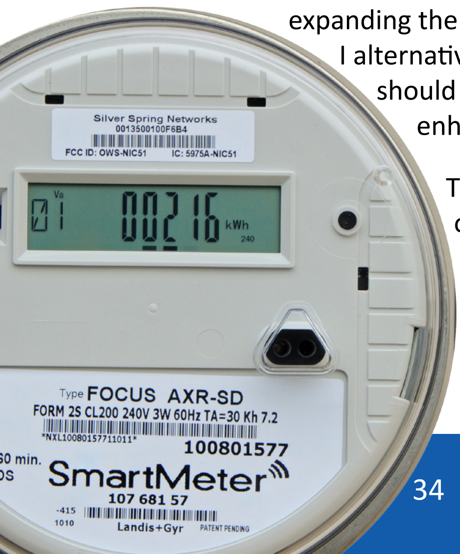
As the majority of the state's electric consumers transitioned to uncapped generation rates, the wholesale energy market rules continue to grow in importance. With that, the Commission has been increasingly focused on the effect of wholesale energy prices on retail electric rates, default service procurement practices, energy conservation, alternative energy and consumer education. Since a properly functioning and competitive wholesale market for electricity also is essential for reasonable retail rates, the Commission launched an investigation into Pennsylvania's electricity retail market in Fiscal Year 2010-11 to determine which aspects of the market are functioning properly and which issues may need to be addressed.

Act 129 of 2008 Implementation

The PUC continues to implement Act 129 of 2008, which expands the Commission's oversight responsibilities and imposed new requirements on EDCs, with the overall goal of reducing energy consumption and demand. Under Act 129, the state's seven largest EDCs must reduce electricity consumption with target dates of 1 percent by May 31, 2011, and 3 percent by May 31, 2013. The Act also requires a 4.5 percent reduction in peak demand by May 31, 2013.

All seven companies submitted reports for June 1, 2010, through May 31, 2011, providing the EDCs' energy and demand savings, as verified by their independent evaluators. This information will be reviewed by the statewide evaluator and Commission staff with a final report expected to be issued in the first quarter of 2012.

Other directives of Act 129 included deploying smart meter technology and time-of-use rates, modifying default service procurement strategies, and expanding the types of generating plants that qualify as Tier I alternative energy sources. The efforts under Act 129 should ultimately reduce the cost of electricity, and enhance safety and reliability of service.



The ongoing implementation of Act 129 is one of the most pressing responsibilities currently before the PUC. Throughout the implementation process, the PUC has provided the opportunity for stakeholders to take an active role. The Commission has engaged consumer advocates, energy efficiency and conservation experts, EDCs, customers, EGSs, and other interested groups, providing various opportunities for stakeholder comment in every aspect of the implementation of Act 129.

In creating the energy efficiency and conservation (EE&C) program guidelines, the Commission recognized a "one-size-fits-all" approach would not work. The PUC's program standards provided each EDC with the ability to tailor its EE&C plan to its service territory and consumers. The PUC will monitor the EE&C plan implementation to ensure the programs are cost-effective and achieving the intended results.

In general, the EDC plans for residential consumers include:

- Residential EnergyStar and high-efficiency appliance programs that provide rebates to customers for the purchase of certain energy efficient appliances.
- Residential compact fluorescent lighting (CFL) rewards programs that provide rebates and point of sale discounts for the purchase and installation of CFLs.
- Residential heating, ventilation and air conditioning (HVAC) efficiency programs that encourage consumers to purchase a high-efficiency central air conditioner or heating system.
- Residential home performance programs that provide for home audits and rebates toward implementing audit recommendations.
- Low-income home audit, and appliance and air conditioner replacement programs.

Act 129 also required EDCs with more than 100,000 customers to furnish smart meter technology upon request and in new building construction, and have a full deployment schedule not to exceed 15 years. The Commission approved smart meter plans for the seven largest EDCs that include:

- A summary of the EDCs' current deployment of smart meter technology, if any.

- A plan for future deployment, complete with dates for key milestone and measurable goals.
- A proposal for access to data for third parties, including electric generation suppliers, and providers of conservation and load management services.
- A plan for cost recovery either through base rates or a reconcilable automatic adjustment clause.

Act 129 defined smart meter technology as that capable of bidirectional communication that records electricity usage on at least an hourly basis, including related electric distribution system upgrades to enable the technology. The Act also directed that smart meter technology must provide customers with direct access to and use of price and consumption information, such as hourly consumption; the ability to support time-of-use rates and real-time price programs; and automatic control of customer's energy consumption.

The Commission also:

- Created a statewide registry for Conservation Service Providers (CSPs) that included the minimum experience and qualifications necessary to qualify as a CSP. Each EE&C plan must include a contract with one or more CSPs to implement the plan or a portion of the plan.
- Entered into a partnership with GDS Associates Inc. Engineers and Consultants to provide long-term, statewide evaluation of the EDC energy efficiency and conservation programs.
- Adopted a total resource cost test to analyze the costs and benefits of the EE&C plans.
- Updated the Technical Reference Manual, which is used to assess energy savings attributable to energy efficiency and demand response measures for Act 129, as well as the Alternative Energy Portfolio Standards Act.

The PUC has dedicated a section of its website to Act 129 information – under the Electricity tab, select Act 129 Information to view copies of all Orders, Secretarial Letters, comments and reply comments, and EE&C plan submissions.

Energy Efficiency & Conservation (EE&C) Plans for Smaller EDCs

On Dec. 17, 2009, the PUC set guidelines for the state's smaller electric distribution companies (EDCs) wishing to develop EE&C programs similar to those required for the larger EDCs under Act 129 of 2008. The smaller companies include: Citizens' Electric Co.; Pike County Light & Power Co.; UGI Utilities Inc.-Electric; and Wellsboro Electric Co. UGI Electric filed a voluntary EE&C plan which is under review.

The Commission asked that each of the plans include:

- A detailed description of EE&C measures to be offered;
- Sufficient supporting documentation and verified statements or testimony or both;
- Proposed energy consumption or peak demand reduction objectives or both, with proposed dates the objectives are to be met;
- A budget showing total planned expenditures by program and customer class;
- Tariffs and a Section 1307 cost-recovery mechanism; and
- A description of the method for monitoring and verifying plan results.

The PUC's program guidelines provide each EDC with the ability to adapt its EE&C plan to its service territory and consumers. While the Commission did not establish mandatory energy reduction targets as found in Act 129, it will monitor the each plan implementation to ensure the programs are cost-effective and achieving the intended results.

Rate Caps

Under the 1997 Electricity Generation Choice and Competition Act, electric rates -- which are comprised of generation, transmission and distribution -- were capped to ease the transition to competitive markets. The law provides a framework that allows all retail electric customers to have direct access to competitive suppliers of electricity.

Customers do not necessarily have to pay the utility prices for generation. They may have the ability to choose between an EDC and competitive supply prices for the generation portion of the bill. An electric generation supplier (EGS) may be able to offer a better price for generation or a green energy product. Customers will be able to compare the EDC price to a competitive supplier price to find the best option.

The amount consumers might save depends on issues such as:

How much they pay now for electric generation supply.

How much electricity they use.

How market prices change in the future.

The price offered by the suppliers serving in the area.

The 1997 law allows residential customers to purchase power from competitive EGSs, while still having their electricity physically delivered by the EDCs regulated by the PUC. The law also permitted the EDCs to recover "stranded costs," which were the existing investments in infrastructure that may have become uneconomic and unrecoverable in a competitive environment.

In exchange, generation, transmission and distribution rates were capped at 1996 levels. The caps on transmission and distribution rates all have expired. Through the settlement of litigated proceedings before the PUC, the generation rates were extended for many of the EDCs. As determined by those proceedings, all utility generation rate caps expired by Jan. 1, 2011.

While Pennsylvania consumers' rates were capped since 1997, the market prices for electricity have risen. The impact of those caps on prices reflected the market prices when the companies were acquiring their power. The companies purchased power for use in January 2011 through a series of auctions in accordance with their PUC-approved default service plans. Act 129 of 2008 required that the default price provide the "least cost to customers over time." The companies will continue to make some spot market purchases and all of the state's electric distribution companies may adjust their price to compare (PTC) quarterly based upon their purchases and default service plan.

With the caps for customers of PECO Energy Co., Metropolitan-Edison Company, Pennsylvania Electric Company and West Penn Power Co. expired, all Pennsylvania electric customers are now paying market-based prices for the generation portion of their bill.

To assist both residents and businesses with shopping, the PUC launched PAPowerSwitch.com. The website is a resource for residents and businesses to make informed decisions on which supplier to choose that will save them money while meeting all of their needs. *(See Consumers)*

Generation Price Mitigation Efforts

The Commission continues to engage consumer advocates and industry experts in efforts to mitigate any price increases in future electric generation prices. The Commission approved rate-mitigation plans such as phase-in or pre-payment plans, after directing all utilities to file such programs if electric generation prices increased by more than 25 percent when rate caps expired.

PPL, Met-Ed, Penelec and PECO all petitioned the Commission to allow customers to pre-pay in anticipation of price increases for supply service that could occur when their generation rate caps expire. All of the programs were voluntary for consumers. PPL and PECO offered customers 6 percent interest on their pre-payment, while Met-Ed and Penelec offered 7.5 percent. The amount plus interest was then paid back to those customers in the form of a credit once rate caps expire.

The Commission also approved a deferral program for PECO's residential and small commercial customers, which allows qualifying customers to voluntarily receive a credit on their bills in the first year to mitigate the initial financial impact of any rate increase, followed by higher payments in later years to make up the first year credits and accrued interest. PPL also was approved for a similar deferral program.

In addition, the PUC approved a demand side response rate for eligible PPL customers. The program enables certain customers to lower their electric bills by shifting electricity usage from on-peak periods when wholesale electricity prices and demand are higher to off-peak periods when demand and prices are lower.

A summary of other mitigation efforts follow:

Energy efficiency and conservation: Energy efficiency investments often are the most cost-effective means of reducing electricity bills. Examples include installation of high-efficiency lighting, such as compact fluorescent bulbs (CFLs), higher efficiency appliances, repair or replacement of heating or cooling systems, and weatherization of homes and businesses. (See Act 129 of 2008 Implementation)

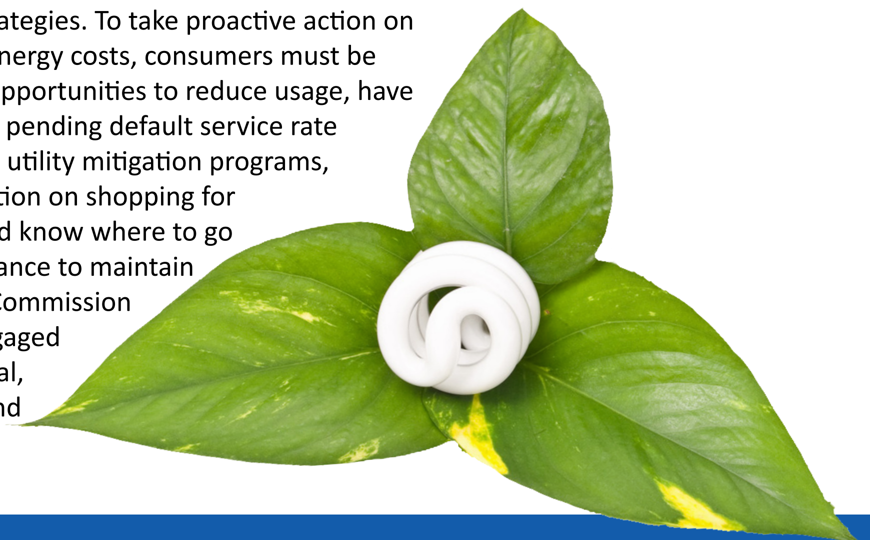
Smart Meters: Reducing usage or shifting load from periods when demand and prices for electricity are high, to periods when demand and prices are low, can have a decisive effect on reducing overall energy costs. (See Act 129 of 2008 Implementation)

Default Service Supply Procurement: The Commission has approved energy procurement rules that will reduce default service rate volatility by directing electric utilities to acquire a portfolio of energy products of different contract lengths and at different points in time. This portfolio approach will help insulate customers from large fluctuations in market prices.

Updated Low-Income Programs: Since electricity prices are likely to change with market prices, low-income programs that provide customer assistance and usage reduction must be adjusted accordingly to ensure that low-income customers are able to afford basic utility service.

Removal of Barriers to Retail Choice: The Commission has established a Retail Markets Working Group to examine existing barriers to the development of retail electricity markets and to recommend policies to the Commission to ensure customers have viable options for their electricity supply when rate caps expire.

Consumer Education: Education is the cornerstone of mitigation strategies. To take proactive action on their future energy costs, consumers must be informed of opportunities to reduce usage, have knowledge of pending default service rate increases and utility mitigation programs, have information on shopping for electricity, and know where to go to seek assistance to maintain service. The Commission is actively engaged in the approval, monitoring and



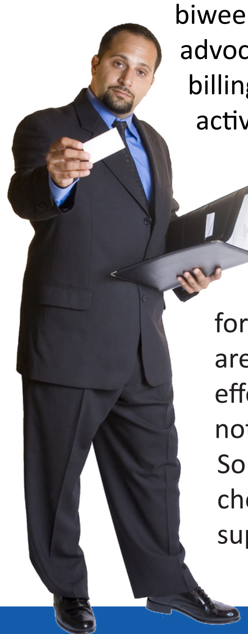
implementation of electric utility consumer-education materials. (*See Consumers*)

Improving Competition

During the fiscal year, the Commission has taken steps to better monitor the competitive environment for electric generation while at the same time moving forward with measures designed to remove barriers to competition.

The Commission established the Committee Handling Activities for Retail Growth in Electricity (CHARGE), to provide an informal forum for troubleshooting issues that are interfering with the ability of EGSs to participate in the retail market and with the overall success of Pennsylvania's electric choice program. The PUC's Office of Competitive Market Oversight (OCMO), whose role recently was expanded from monitoring the development of the natural gas market, serves as the Commission's electric choice ombudsman.

Since a kick-off conference call on Dec. 18, 2009, CHARGE has been holding biweekly conference calls, in which EGSs, EDCs and consumer advocates participate. Various issues are being addressed such as billing, taxes, price to compare, consumer protections, marketing activities and disclosure statements.



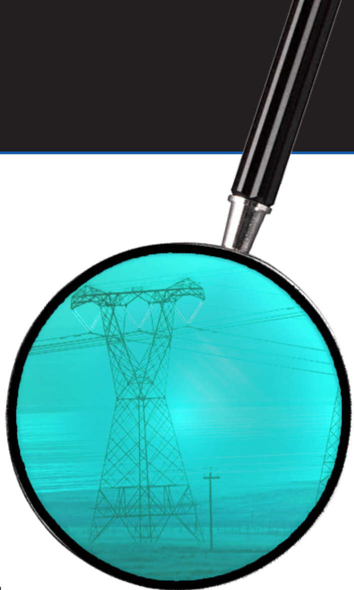
CHARGE has focused on draft guidelines addressing marketing and sales practices for EGSs in their interactions with residential customers. On Feb. 10, 2011, the Commission issued for comment a proposed rulemaking for marketing and sales practices of EGSs. These guidelines are viewed by many CHARGE participants as important to the effective operation of the retail market so that consumers are not discouraged by inappropriate marketing and sales practices. Some issues addressed by the guidelines include background checks, training and monitoring of agents, hours during which suppliers may conduct door-to-door marketing, and the details surrounding the verification process for a switch that is made during door-to-door marketing.

With the expiration of generation rate caps, more and more EGSs are entering the state's retail electric generation supply market. As a result, consumers are being exposed to unfamiliar marketing strategies and sales techniques including direct sales or door-to-door sales. As a result of this rulemaking suppliers will be expected to conduct themselves with the guidelines in mind so that their sales and marketing activities do not call into question the fairness and integrity of the competitive market.

CHARGE also addressed issues with the eligible customer lists provided by EDCs, including elements such as meter read cycle, customer name, customer address, utility rate class, load profile group indicator, load factor, telephone number, old account numbers, contact name and address, rate mitigation plan indicator, interval meter indicator, and capacity and transmission obligations. In Fiscal Year 2010-2011, the Commission issued for comment a reconsideration of the interim guidelines for the customer information to be provided by EDCs to EGSs contained in the eligible customer lists originally issued Nov. 12, 2010. The Commonwealth Court returned jurisdiction of this matter to the Commission following appeals by the Office of Consumer Advocate and the Pennsylvania Coalition Against Domestic Violence, both of which had concerns over privacy, specifically, a customer's ability to restrict the release of all customer data held by an EDC, not just the customer's telephone number and historical billing data. The court has also stayed the Commission's Nov. 12, 2010 Order.

The Commission will reconsider the guidelines in order to further address the rights of consumers to safeguard their customer information while also maintaining the Commission's obligations under Chapter 28 of the Public Utility Code.

Agendas and recaps of all CHARGE meetings that have been held are available on the Commission's website – click on Electric, then Electric Competitive Market Oversight.



Statewide Investigation of Competitive Retail Electric Market

On Feb. 24, 2011, the PUC announced plans to launch a statewide investigation to ensure that a properly functioning and workable competitive retail electricity market exists in the Commonwealth. This investigation was directed as part of the PUC's adjudication of the merger application of West Penn Power Co., Trans-Allegheny Interstate Line Company and FirstEnergy Corp. In that proceeding, representatives of EGSs who are active in Pennsylvania's retail market had urged the PUC to impose various conditions on the merger approval designed to ensure a fully functional and workably competitive retail market. Rather than addressing issues of potential harm to retail markets in the merged entity's distribution footprint in a piecemeal fashion as part of a litigated proceeding, the PUC opted to open this statewide investigation. The goal of the statewide investigation is for stakeholders and staff to make recommendations for improvements in the functioning of the retail market.

The statewide investigation will examine both the legislative and regulatory framework behind Pennsylvania's retail market, including an analysis of the current default service model and whether, as currently structured, that model is hindering competition. Additionally, the investigation will include a process to identify interested competitive suppliers who are qualified to provide default service throughout the state.

The Commission will conduct the investigation in two phases. The first phase is designed to assess the status of the current retail market and explore what changes need to be made to allow customers to best realize the benefits of competition. At the conclusion of this first phase the Commission will initiate the second phase to examine and address how to best resolve the issues raised and implement the prudent changes identified based upon its review of the comments received.

The Commission will hold en banc hearings during the investigation to allow invited parties the opportunity to discuss the topics raised in this proceeding. The first en banc hearing was held on June 8, 2011, with the second scheduled for later in Fiscal Year 2010-2011.

Default Service

The 1997 Electricity Generation Choice and Competition Act required electric companies, or a Commission-approved alternative supplier, to provide default electric generation service to customers who have not selected an alternative generation supplier. This is commonly called default service.

The default service regulations provide critical rules and guidance to the industry regarding pricing, terms and conditions of service to consumers who decline to choose a competitive supplier, or who are unable to continue service with a competitive supplier.

Act 129 of 2008 amended language concerning default service prices, requiring that the default service prices for electric generation service are required to reflect "the least cost to customers over time." The Commission is amending its default service regulations to ensure they are consistent with the changes in Act 129. Proposed regulations were issued in January 2010. Until final regulations are promulgated, the PUC is taking the amended language of Act 129 into its consideration of any EDC default service plans that come before the Commission for approval.

In establishing default service regulations, the Commission also recognized that some elements of default service should be addressed in a policy statement rather than a rulemaking, because changes in markets and technology may result in an approach that is too narrowly tailored or too unresponsive to serve the state's interests.

The policy statement provided procurement guidelines for default service providers to ensure competitive procurement practices; diversify generation supply risks; seek a variety of suppliers and contract terms; and comply with alternative energy requirements. It recommended that default service providers give customers the option to defer paying some portion of a rate increase for a period of time if the retail rate increases by more than 25 percent.

The Commission's role is to ensure that the process utilities use to establish the default service electricity generation prices achieves the lowest price over time. The generation prices are not set by the PUC, but rather are based on the wholesale market, over which the PUC exercises no jurisdiction.

The following is the status of default service plans for each of the EDCs:

West Penn Power Co.

A July 25, 2008, Order approved a default service plan for West Penn Power, which covers default service prices from Jan. 1, 2011, to May 31, 2013, and requires the company to purchase power for residential customers using 12-, 17- and 29-month contracts, and spot-market purchases to mitigate the impact of price spikes on the competitive markets.

On March 12, 2009, and May 14, 2009, the PUC approved plans for the company to accelerate the purchases of some electricity supply while wholesale energy costs were lower. Moving up the purchases of electric supply for residential customers was designed to allow the company to take advantage of favorable pricing available in the wholesale energy markets at that time.

On Sept. 8, 2010, the PUC granted a Petition from West Penn to modify its competitive procurement plan to acquire solar photovoltaic alternative energy credits and other Tier 1 alternative energy credits through long-term contracts rather than through spot-market purchases. As a result, West Penn will be conducting auctions for the purchase of these alternative energy credits.

Citizens' Electric Co. & Wellsboro Electric Co.

On Feb. 25, 2010, the PUC approved a default service plan covering June 1, 2010, through May 31, 2013. As part of the plan, the companies will choose a single portfolio manager to administer the schedules for competitive bid solicitations, and the schedules contained within the companies' stratified procurement plan.

The plan includes a Fixed Generation Supply Service Rate (GSSR) that may be adjusted quarterly. The changes to the Fixed GSSR reflect updated estimates to forecast costs and sales, which then are reflected in the rates. The Fixed GSSR is based upon the total amount of annual estimated purchased power costs, plus the total annual estimated administrative charges associated with purchasing generation supply to serve the default service customers, divided by the projected total kWh sales for the application period.

The Commission reviews the companies' filings to verify computations; ensure the proposed rates reflect the energy contract prices and the Federal Energy Regulatory Commission-approved tariff rates; and determine that the filings are in compliance with company tariffs and Commission Orders.

Duquesne Light Co.

The PUC approved a settlement for a default service plan for Duquesne on May 20, 2010. The default service plan covers service from Jan. 1, 2011, through May 31, 2013, and includes steps to obtain least-cost generation supply on a long-term, short-term and spot-market basis.

Metropolitan Edison Co. (Met-Ed)/Pennsylvania Electric Co. (Penelec)

On Nov. 6, 2009, the PUC approved a settlement for a default service plan for a 29-month term, beginning Jan. 1, 2011, and ending May 31, 2013. Under the plan, the companies will include competitive procurement plans that provide for a mix of spot purchases, and short- and long-term contracts, including using a descending clock auction to procure the full-requirements component of the supply mix and requests for proposals; a mix of supply resources that is designed to obtain least-cost generation supply contracts on a long-term, short-term and spot-market basis; and a separate solar procurement process designed to meet the solar photovoltaic requirement for the duration of the programs.

PECO Energy Co.

The PUC approved a default service plan for PECO on April 16, 2009, that provides for a mix of spot, one-, two- and five-year purchases of generation supply to establish the default service rates that will be in effect from Jan. 1, 2011, to May 31, 2013.

Pennsylvania Power Co. (Penn Power)

On Feb. 18, 2010, the Commission determined that the default service prices for Penn Power customers were transparent and non-discriminatory, and reflected market-based prices. This is the company's third default service plan since its rate cap expired Dec. 31, 2006.

The competitive bidding process was conducted by an independent group on behalf of Penn Power for the procurement of the commercial customers load for June 1, 2010, through May 31, 2011, and the residential customer load for June 1, 2010, through May 31, 2011.

Pike County Light & Power (PCL&P)

In July 2011, Pike County Light & Power petitioned the PUC to maintain its current default service procurement methodology through May 31, 2014. Specifically, Pike County filed for approval of a default service plan for the period June 1, 2012 through May 31, 2014 that would continue its current practice of procuring default supply on the New York ISO spot market. Pike County would also maintain its current generation rate structure, with the default service rate comprised of two components: (1) the Market Price of Electric Supply, and (2) the Electric Supply Adjustment Charge. The petition will be finalized in FY 2011-12.

PPL Electric Utilities Inc.

On June 18, 2009, the Commission approved a settlement for PPL's default service program and procurement plan that will establish the default service prices for Jan. 1, 2011, through May 31, 2013.

Under the plan, PPL also will convene a customer collaborative to discuss residential, small commercial and industrial direct mail referral programs. PPL also will convene a collaborative to discuss a retail aggregation program. The results will be considered as part of the company's next default service proceeding.

UGI Utilities Inc. – Electric Division

On July 17, 2008, the PUC approved a settlement for the default service procurement, implementation and contingency plan for UGI Electric. The company will rely on competitive wholesale market purchases to obtain power for its default service customers in an approach designed to provide better protection from congestion risk relative to the base filing. The generation rates resulting from the purchases took effect Jan. 1, 2010.

Distribution Rate Increase Requests

During Fiscal Year 2010-11, the Commission took the following actions related to about $349 million in rate increase requests:

PECO Electric

Customers Served: 1.6 million customers in six counties
Requested Rate Increase: $316.4 million (7 percent - total revenue)
Approved Rate Increase: $225 million (4.9 percent- total revenue)
Primary Reason: To cover a significant investment in distribution plant, as well as increases in operation and maintenance costs

PPL Electric Utilities

Customers Served: 1.4 million customers in 23 counties
Requested Rate Increase: $114 million (2.4 percent - total revenue)
Approved Rate Increase: $77.5 million (1.62 percent - total revenue)
Primary Reason: To cover distribution system improvements and expansions, as well as increases in operation and maintenance costs

Wellsboro Electric

Customers Served: 6,129 customers in two counties
Requested Rate Increase: $870,100 (23.7 percent - distribution only)
Approved Rate Increase: $700,000 (19.04 percent - distribution only)
Primary Reason: Recover costs of providing service and upgrades to the distribution system

Citizens Electric

Customers Served: 6,800 customers in two counties
Requested Rate Increase: $787,276 (21.5 percent - distribution only)
Approved Rate Increase: $600,000 (16.32 percent - distribution only)
Primary Reason: Recover costs of providing service and upgrades to the distribution system

Duquesne Light Co.

Customers Served: 586,800 in two counties
Requested Rate Increase: $87.3M (6.7 percent - total revenue)
Approved Rate Increase: $45.7M (3.5 percent - total revenue)
Primary Reason: To cover significant increases in operating and other costs, as well as new distribution plant investment

Smethport

Customers Served: 1,060 in McKean County
Requested Rate Increase: $239,876 (16 percent - distribution only)
Approved Rate Increase: $239,876 (16 percent - distribution only)
Primary Reason: To support long-term operations and maintenance costs of the electric department

Participation in Federal Proceedings

The Public Utility Code authorizes the Commission to appear before federal agencies such as the U.S. Department of Energy (DOE), the Federal Energy Regulatory Commission (FERC) and the federal courts. The Commission intervenes in wholesale market proceedings on behalf of Pennsylvania and in collaboration with other state commissions in proceedings before FERC which may have an impact on the decisions being made by FERC about wholesale electric markets and interstate transmission of electricity. Among other things, FERC administers the Federal Power Act and is charged by Congress with creating, maintaining and enforcing the essential conditions for a fully competitive, non-discriminatory wholesale electricity market.

Beyond its responsibility for the wholesale energy markets, FERC also seeks to create proper wholesale market conditions and incentives to ensure the timely construction of necessary generation and transmission facilities to serve anticipated future demand.

A highly competitive and efficient wholesale electric market is integral to the existence of a properly functioning Pennsylvania retail electric market that supplies retail power at reasonable prices for consumers. FERC delegates operational and market decisions to the Regional Transmission Organizations (RTOs). The PUC participates in many proceedings related to the design and operation of the RTO in which Pennsylvania is located.

The RTO in which Pennsylvania operates is the PJM Interconnection LLC (PJM). Pennsylvania is no longer part of the Midwest Independent Transmission System Operator Inc. (Midwest ISO) as of June 2011. The PUC is a member of one organization of state commissions jointly interested in wholesale market issues – the Organization of PJM States Inc. (OPSI). OPSI represents the interests of member states before the FERC.

The Commission has also been an active party in litigation in the federal courts to oppose federal policy initiatives that impinge on state jurisdiction.

The Commission also participates in various FERC proceedings that may be initiated by and against RTOs, generation owners, transmission owners, load-serving entities or end users. The Commission has increased both the number of staff and the extent of its involvement in monitoring and advocating Pennsylvania's views on federal and regional energy issues.

Reliability Pricing Model (RPM)

In December 2006, FERC found that PJM's existing generation capacity market was unjust and unreasonable, because it failed to procure sufficient capacity to enable PJM to attract sufficient new generation investment to support a reliable transmission system. To remedy its concern, FERC approved the highly controversial RPM program, a capacity market under which PJM purchases capacity on a multi-year forward-looking basis through an auction mechanism and allocates the costs to wholesale electricity customers.

The cost of capacity is determined by these forward auctions. On Dec. 12, 2008, PJM filed proposed amendments to RPM, and its filing was assigned by FERC to an intensive fast-track mediation process. The PUC and many other parties intervened and participated in the mediation process. On Feb. 9, 2009, PJM and most of the PJM wholesale market buyers, municipal and electric cooperatives, the Commission and other state commissions, state consumer advocates, and large end-user interests filed a proposed settlement, opposed by most of the generation owners in PJM. On March 26, 2009, FERC issued its Order, which took the proposed settlement as a starting point for disposition, while giving consideration to many of the objections of the PJM generators, and directed that certain issues be returned to PJM's stakeholders for further development.

Although the changes to RPM and recent economic events have resulted in a sharp decrease in capacity prices in many PJM sub-regions, RPM and its ongoing effect on wholesale markets and generation investment continue to be of regional concern. The Commission is actively participating in the ongoing RPM stakeholder process. Additional PJM-proposed modifications to RPM filings are expected to be filed at FERC.

FERC Order 719

FERC issued final rules directing all jurisdictional RTOs to convene stakeholder committees to discuss and to subsequently propose specific tariff changes regarding wholesale market demand response, "scarcity" pricing rules, long-term power contracting, RTO responsiveness and organization, market structure, and market monitoring. The Commission actively participated in the Order 719 stakeholder discussions. While the outcome of some of the stakeholder committee deliberations was favorable to Pennsylvania, PJM's subsequent compliance filings presented some major problems for Pennsylvania retail customers, resulting in the filing of protests by the Commission.The protests primarily dealt with PJM's proposed changes to scarcity pricing of wholesale electricity and the impact of the proposal on wholesale market prices.

Other Federal Court, Department of Energy and FERC proceedings the PUC is involved in include:

- California Wilderness Coalition et al v. US Department of Energy et AL (9TH Circuit Case No. 08-71074)
- P3 v. PJM (EL11-20-000) and PJM Minimum Offer Price Rule Filing (ER11-2875)
- PJM New Demand Response Products (ER11-2288)
- Eastern Interconnection States Planning Collaborative
- Potomac-Appalachian Transmission Project (ER08-386)
- Petition for Incentive Rate Treatment by Northeast Transmission Development (EL11-33-000)

Transmission Planning

The PUC continues to actively monitor federal legislation impacting transmission siting. Amendments to the Federal Power Act enacted as part of the Energy Policy Act of 2005 greatly expanded the authority of the federal government, through the Department of Energy (DOE) and FERC, to prescribe areas of the country where large transmission lines should be sited.

This legislation authorized DOE to conduct triennial congestion studies to determine where in the United States the greatest amount of transmission congestion and constraints are located. The study issued in 2006 designated the entire Mid-Atlantic Region as a National Interest Electric Transmission Corridor (NIETC). The result of the NIETC designation is that a transmission line must be processed through the state commission, if applicable, within one year of filing or the utility applicant can seek to have the transmission line sited under "backstop authority" given to FERC under the new FPA provisions. This expansion of federal authority greatly infringes on state commission processes to review and rule on a transmission siting application.

In March 2008, following DOE's formal designation of the Mid-Atlantic NIETC, the PUC together with six other states and/or state commissions, plus a number of environmental organizations, challenged the DOE NIETC designation in the U.S. Court of Appeals on a number of grounds. The 13 separate appeals, including the PUC's, were consolidated for argument in the 9th Circuit. The major issues are that the NIETC designation was overbroad and the methods utilized by DOE for determining areas of congestion were flawed. Briefing of the case occurred from September 2008 through April 2009. The case, after a year of delay, was argued on June 8, 2010. The appellants requested as relief that the NIETC designation be withdrawn and the matter returned to DOE for further consideration utilizing better data.

Since that time, DOE has issued a new congestion study for 2009 that makes no changes in the Mid-Atlantic designation. Also, DOE, as a result of the litigation, has initiated a multi-state process, funded by American Recovery and Reinvestment Act stimulus money and known as the Eastern Interconnection State Planning Council, which will work with transmission planning authorities such as PJM to develop recommendations on where future transmission lines should be sited. These recommendations will be reviewed and approved by FERC. The PUC is an active participant in this process.

Transmission Line Proceedings

The Pennsylvania Public Utility Code requires public utilities to furnish and maintain adequate, efficient, safe, and reasonably priced utility service and facilities. The Code permits public utilities to make the changes necessary to ensure the quality and safety of that service. The PUC is the agency charged with ensuring that public utilities are meeting those obligations. The Commission's jurisdiction includes oversight of the siting and construction of electric transmission lines.

On Nov. 4, 2010, the Commission adopted Interim Guidelines for transmission line siting in Pennsylvania. The Interim Guidelines provide guidance on the information that the Commission believes is relevant and critical to its evaluation of future transmission line siting applications. The Commission plans to initiate a rulemaking process to update existing regulations on the information that must be filed in support of transmission siting applications. Because the rulemaking process can take a year or more, the Interim Guidelines provide direction and will be effective until final regulations are completed.

Ongoing developments at the federal level affecting transmission line siting, as well as the Commission's obligation to maintain an adequate transmission infrastructure, impacted the decision to re-evaluate the relevancy and effectiveness of the Commission's current transmission siting regulations. As discussed earlier in this chapter, the Commission has been involved in preserving state jurisdiction over transmission line siting, taking an active role in the DOE's NIETC designation litigation.

The Interim Guidelines address public notice filing requirements; eminent domain filing requirements; exemption from municipal zoning standards; route evaluation and siting; environmental filing requirements; and health and safety considerations.

Transmission line siting cases present two distinct issues: whether the need for the line exists; and whether, considering the alternatives, the proposed route is in the public interest. When an application of this nature is received, the Commission is required to hold hearings to consider the necessity, safety and environmental impact of the proposed line. The Commission also considers a variety of other issues, including risk of danger to the health and safety of the public, compliance with applicable statutes, and regulations providing for the protection of natural resources and minimal adverse environmental impact. Additional information on the PUC process for transmission line siting is available on the Commission website under Consumer Education.

Some large transmission line proceedings recently considered by the Commission include:

Trans-Allegheny Interstate Line Co. (TrAILCo)

TrAILCo filed an application seeking Commission approval to locate, construct and operate a proposed transmission-line project in portions of Washington and Greene counties. More than 300 protests and interventions were filed on behalf of various parties. To provide adequate opportunities for community input, the Administrative Law Judges (ALJs) assigned to the case held 12 public input hearings in various locations of Washington and Greene counties in fall 2007. Evidentiary hearings were conducted in spring 2008, in which the legal, policy and evidentiary issues were addressed.

On Nov. 24, 2010, the Commission granted TrAILCo's amendment to application and granted a joint petition for settlement (joint petition) without modification. On Oct. 8, 2010, the ALJ had recommended that the amendment to the application be granted and further recommended that the joint petition be approved without modification. Pursuant to the Commission Order, the parties had convened a Collaborative to discuss the Prexy Facilities. As a result of the Collaborative, TrAILCo filed an

amendment to its application regarding the Prexy Facilities, along with the joint petition on Oct.13, 2009 with the ALJ. Under the joint petition, the Collaborative agreed that the transmission infrastructure alternative was the appropriate solution to prevailing reliability issues, in lieu of the Prexy Facilities solution. The Collaborative and the joint petition termed this the "S5" solution. The S5 solution as agreed by members of the Collaborative involves a split in the Woodville-Elrama line at the Peters-Bethel Park crossover, connection of Bethel Park to Elrama and connection of Peters to Woodville with reconductoring of Woodville-Collier and installation of capacitors at a number of locations at already existing substations.

On Nov. 13, 2008, the Commission approved an agreement that allowed a 1.2 mile portion (502 Junction Facilities) of the 37.2-mile transmission line proposed by TrAILCo and stayed the remainder of the proceeding for further consideration. The Energy Conservation Council (ECC) appealed the portion of the line involving the 502 Junction Facilities. On May 6, 2010, the Pennsylvania Commonwealth Court affirmed that decision. Although ECC filed a petition for reargument, Commonwealth Court denied ECC's Petition on June 30, 2010. A collaborative working group was established to consider other options for the remaining 36 mile portion of the TrAILCo line (Prexy Facilities).

PPL Susquehanna-Roseland

PPL filed the application on Jan. 6, 2009, to construct a new 500-kV transmission line. Known as the Susquehanna-Roseland project, the proposed Pennsylvania line is about 101 miles long and travels through portions of Lackawanna, Luzerne, Monroe, Pike and Wayne counties. PPL also requested authorization to construct a new substation in Blakely Borough, Lackawanna County, to connect the 500-kV line to the regional transmission system in that area. The Commission held four public input hearings in the area where the proposed line is to be constructed. The ALJ issued a Recommended Decision on Nov. 12, 2009 recommending the grant of the application. On Feb. 12, 2010, the Commission issued an Order affirming and modifying the ALJ's decision. The Commission disagreed with the ALJ requirement that all necessary permits be obtained prior to commencing construction.

Several parties appealed the Commission's decision to Commonwealth Court. The Commonwealth Court affirmed the PUC's decision. The decision was not appealed to the Supreme Court.

Alternative Energy Portfolio Standards Act of 2004

Signed into law on Nov. 30, 2004, the Alternative Energy Portfolio Standards Act (AEPS) requires EDCs and EGSs to include a specific percentage of electricity from alternative resources in the generation they sell to Pennsylvania customers. Since the passage of AEPS, the PUC has moved expeditiously to develop the rules and regulations necessary for fostering Pennsylvania's alternative energy market. Each year, the Commission continues to address the issues that arise as more EDCs, EGSs and alternative energy systems attempt to follow the mandates of the Act.

On June 3, 2010, the Commission re-approved Clean Power Markets (CPM) as the administrator of alternative energy credits (AECs) until Dec. 31, 2013, with the option for two one-year contract extensions. An AEC is created each time a qualified alternative energy facility produces 1,000 kWh of electricity. The AEC then is sold or traded separately from the power. This makes it easier for individuals and businesses to finance and invest in alternative energy.

Among the services CPM performs is the verification of electric distribution company and electric generation supplier compliance with the minimum portfolio requirements of the AEPS Act; the calculation of Tier I requirements on a quarterly basis; the review of applications for alternative energy system status; and the response to inquiries about alternative energy credits.

On Sept. 25, 2008, the PUC finalized the regulations that govern compliance with AEPS by the EDCs and EGSs. The regulations reflect the Commission's understanding that the Act is intended to promote the efficient utilization of the region's alternative energy resources, to yield significant economic and environmental benefits in Pennsylvania. Act 129 of 2008 expanded the definition of alternative energy sources that qualify as Tier I resources under AEPS. The PUC finalized procedures and guidelines to allow for the limited expansion of alternative energy sources that qualify in Tier I under AEPS to include Pennsylvania-based low-impact hydro-power facilities and generators utilizing by-products of pulping and wood manufacturing processes. The PUC also created reporting requirements and related procedures to adjust the AEPS Tier I requirements to account for the newly qualified resources.

The Commission also established the standard application forms and fees for customer-generators wanting to interconnect to the electric grid. A major component of AEPS includes directions for how customer-generators, who use technologies such as solar panels, fuel cells or biodigesters, can connect to the electric distribution system. The PUC had previously established the rules for those interconnections and how the customer-generators will be compensated by EDCs and EGSs for providing surplus energy to the electric grid. The forms are available on the PUC website under the Electricity tab, select Alternative Energy.

As the Act evolves and matures, the Commission will tackle the issues in a way that will facilitate implementation of this important component of the Commonwealth's overall energy policy. In its most recent performance audit of the PUC, the Legislative Budget & Finance Committee (LB&FC) said the Commission "made good progress" in implementing the requirements of the Act.

Reliability

Under the Customer Choice Act, each EDC is obligated to ensure that its service does not deteriorate below the level of service reliability that existed prior to the Jan. 1, 1997, effective date of the Act.

The monitoring efforts by the Commission are focused on reviewing annual and quarterly reports filed by the electric distribution companies. Large electric companies have to stay within 10 percent of a PUC-established benchmark for a rolling three-year period and within 20 percent of the benchmark during a rolling 12-month period. Four smaller electric companies – UGI Electric Co., Citizens' Electric Co., Pike County Light & Power and Wellsboro Electric Co. – also must

stay within 10 percent of their benchmark for a rolling three-year period, but will be allowed to go up to 35 percent of the benchmark for the rolling 12-month period. Benchmarks are the Commission's goals for each utility based on the number and duration of outages.

The Commission issued the annual reliability report – Electric Service Reliability in Pennsylvania – in June 2011. The report trends reliability performance from March 2004 through March 2011, and includes the causes of outages, by percentage, and information on all major events. It can be viewed at the Commission's website at www.puc.state.pa.us under Publications and Reports.

Electric Power Outlook

Each public utility that distributes or furnishes electricity must annually submit to the Commission information concerning its future plans to meet its customers' demands. The Commission is required to submit the report to the General Assembly, the Governor, the state's Office of Consumer Advocate and each affected public utility each year.

Regional generation adequacy and reserve margins of the Mid-Atlantic area have been maintained. While sufficient generation capacity is expected through 2014, the Commission will continue its current policy of encouraging generation adequacy within the region. With respect to transmission adequacy, the transmission system in the Mid-Atlantic Region has sufficient capacity to meet demand. Transmission expansions and upgrades are being planned for the next five years to reinforce the bulk of the power grid.

Inspection and Maintenance Standards

PUC regulations require EDCs to have a plan for periodic inspection and maintenance of poles, overhead conductors and cables, wires, transformers, switching devices, protective devices, regulators, capacitors, substations, and other facilities critical to maintaining an acceptable level of reliability. The regulation also sets forth minimum inspection and maintenance intervals for vegetation management, poles, overhead lines and substations.

Biennial plans for the periodic inspection, maintenance, repair and replacement of facilities, designed to meet performance benchmarks and standards, were filed with the Commission on Oct. 1, 2009, by FirstEnergy (Met-Ed, Penelec and PennPower), West Penn Power and UGI, became effective on Jan. 1, 2011. Inspection and maintenance plans were filed by Duquesne Light, PECO, PPL, Citizens', Pike County and Wellsboro on Oct. 1, 2010 to become effective Jan. 1, 2012.

Outage Response

The PUC initiated a rulemaking and proposed a policy statement on Nov. 6, 2009, to improve utility response to large-scale service outages. The goal was to amend existing regulations regarding service outages and reportable accidents. The Commission also proposed a policy statement to provide guidance to the industry regarding the types of public notice necessary.

The goal of the rulemaking is to have more effective responses to future unscheduled outages. The proposed amendments address accidents involving injury for the electric, natural gas, water and wastewater industries; service outages; the ability to capture more reportable events, such as cyber-security attacks and damages to a utility company by another utility company; deadlines for reporting accidents; the expansion of provisions regarding reporting service outages to include sustained outages; and reports to track the number of utility workers, contract and mutual aid workers assigned to repair work.

The proposed policy statement is intended to establish guidelines for how the utilities should communicate with the public during outages to ensure that actual, timely notice to customers is provided. The proposed policy statement contains a series of acceptable methods for improving the timeliness and effectiveness of notice to customers during an outage.

The proposed policy statement applies to electric distribution utilities. However, the Commission sought comment on whether the policy statement should apply to natural gas, water and wastewater utilities as well.

The proposed policy statement is designed to establish acceptable forms of notification to reflect technological advances; have the utilities strive to adopt the National Incident Management System (NIMS) and its public information system; ensure crisis communications plans are in writing and consistent with NIMS; and encourage utilities to work across geographic regions if applicable.

The proposed rulemaking and policy statement are the result of a statewide evaluation of EDC storm response tactics, including their power restoration practices and customer communications. The action followed residual storms from Hurricane Ike on Sept. 14-15, 2008, that mixed with a cold front to produce winds up to 80 mph in Western Pennsylvania, caused damage to the area's electric distribution system and left more than 450,000 customers without power. For some, power was not restored until Sept. 22, 2008.

Mergers and Acquisitions

In reviewing mergers and acquisitions, the Commission works to make certain that customers are protected and the company is a viable public utility and a good neighbor. The PUC gives each application a thorough and comprehensive review. In Pennsylvania, the legal standard asks whether an affirmative public benefit will result from the merger or acquisition. Public benefit is defined typically as protecting the public interest, encouraging economic development and safeguarding the environment. The following merger was approved in Fiscal Year 2010-11:

West Penn Power (Allegheny Power), Trans-Allegheny Interstate Line Company (TrAILCo) and FirstEnergy:

On Feb. 24, 2011, the Commission approved the joint application filed by West Penn Power (Allegheny Power), Trans-Allegheny Interstate Line Company (TrAILCo) and FirstEnergy to obtain approval for a change of control of Allegheny and TrAILCo. Allegheny and TrAILCo will become a wholly owned subsidiary of FirstEnergy.

As part of its review of the application, the Commission found that the merger would be in the public interest. Under the terms of a settlement agreement, West Penn Power will become a wholly owned subsidiary of FirstEnergy. FirstEnergy will remain the ultimate corporate parent of Met-Ed, Penelec and Penn Power and all other FirstEnergy subsidiaries, and will become the ultimate corporate parent of Allegheny and all of the Allegheny subsidiaries, including West Penn and TrAILCo. Following the merger, Met-Ed, Penelec, Penn Power, West Penn and TrAILCo will continue to operate as Pennsylvania public utilities and remain under the Commission's jurisdiction. The merger will not affect the day-to-day operations of these utilities.

Renewable and Sustainable Energy

The PUC monitors periodic board meetings held by the five sustainable energy funds. The PUC also chairs the Pennsylvania Sustainable Energy Board, which provides suggested operational and best practices for the regional funds, as well as promotes the transparency of the funds' activities and projects.

Various restructuring and merger settlements from electric competition allocated nearly $80 million of consumer funds, over about a 10-year period beginning in 1998, for regional plans to develop renewable and clean energy projects and technologies. The Commission is responsible for approving nominations to each fund's board of directors and changes to their governing bylaws. Examples of projects for which the regional boards have approved funding include wind farms, photovoltaic applications, efficiency loan programs and renewable energy education.

Electric Company Audits

The Commission periodically performs management and operations audits (MAs) or management efficiency investigations (MEIs) of the jurisdictional electric distribution companies.

In addition to the periodic MAs and MEIs, the PUC annually conducts a variety of other EDC audits. During the fiscal year, 14 audits, involving competitive/intangible transition charges, default service, purchased power, non-utility generation, transmission service costs, consumer-education programs and universal service programs, were completed.   Also, 82 filings requesting changes to established adjustment clause rates were reviewed and processed, implementing revised surcharge rates.

Among the MAs and MEIs completed within the 2010-11 fiscal year were:

PECO Energy Co. – Electric

An MEI released on July 29, 2010, showed that PECO Energy Co. – Electric could realize annual savings of up to $1.6 million by implementing recommendations contained in the report. These savings are in addition to the $8.1 million annual savings that the company has already realized by implementing recommendations from an August 2007 Focused Management and Operations Audit report.

The Commission examined the company's progress in implementing 27 of the 53 recommendations from the prior management audit report and its emergency preparedness efforts.

According to the MEI, PECO has effectively implemented 14 of the 27 prior recommendations reviewed and taken some action on the 13 remaining recommendations. Some of the changes made by the company include: completing implementation of the Mobile Dispatch System, resulting in annual savings of approximately $6,500,000; successfully reducing its energy-theft caseload by reorganizing its Revenue Protection Department and utilizing several reports to monitor for electric-theft, resulting in annual savings of approximately $1,200,000 since 2006; taking steps to improve the effectiveness of its Gas-Theft of Service Program, resulting in annual savings of approximately $35,000; reducing corrective maintenance costs over the 2005 to 2009 timeframe resulting in annual savings of $112,000; and implementing a process to compare cost of services provided to affiliates resulting in annual savings of $273,000.

In addition, the Audit Staff made five recommendations for further improvement that include: managing annual non-storm overtime spending through the use of proper controls, reviews and authorizations, including monitoring and tracking overtime, which should result in annual savings ranging from $500,000 to $1.5 million; allocating vegetation funding levels among operation regions to target areas experiencing prevalent tree-related outages; restructuring the reporting relationship of the Internal Audit function so that it no longer reports administratively, directly or indirectly, to management responsible for the financial accounting, or to the finance operation of the company; filling vacant Internal Audit Department positions in a more timely manner to reduce the need to augment audit services resulting in annual savings of $101,000; and striving to reduce the number of "at-fault" line hits attributable to inaccurate and no print causal factors resulting in annual savings of $50,000.

Duquesne Light Co.

An MEI examined the progress Duquesne Light Co. made in implementing 10 of the 15 original recommendations from the prior management audit released in May 2006. The MEI report was released on Nov. 19, 2010.

The Commission found that Duquesne effectively implemented all 10 of the prior recommendations reviewed. Among the more notable improvements achieved by the company are: implementing a succession planning process for senior management and management positions; filing and receiving commission approval of all required affiliated interest agreements; establishing procedures requiring documentation of Duquesne Light's Board of Directors' approval for all inter-company loans and amendments; significantly reducing its amount of accounts receivable write-offs resulting in an average annual savings of about $9.4 million; reducing long-term residential arrearages resulting in an average annual savings of $59,000; significantly reducing its justified payment arrangement request rate; reducing response times to consumer complaints; and conducting regular reviews of inactive inventory to identify, write off and dispose of obsolete inventory resulting in one-time savings of $1.2 million and annual savings of $117,400.

Additionally, the Commission's Audit Staff made recommendations for further improvement such as increased collection agency recovery rates for closed customer accounts that could increase its annual cash flow by about $186,000 and further reductions to the average response time to payment arrangement requests.

Electric Distribution System Improvement Charge

Based on experience in the water industry, the PUC urges the creation of a distribution system improvement charge (DSIC) to allow electric distribution companies to use a surcharge on customers' bills to accelerate the replacement of infrastructure improvements. System improvement charges reduce the frequency and the associated costs of base rate cases while maintaining a high level of customer protections. (*See Natural Gas*)

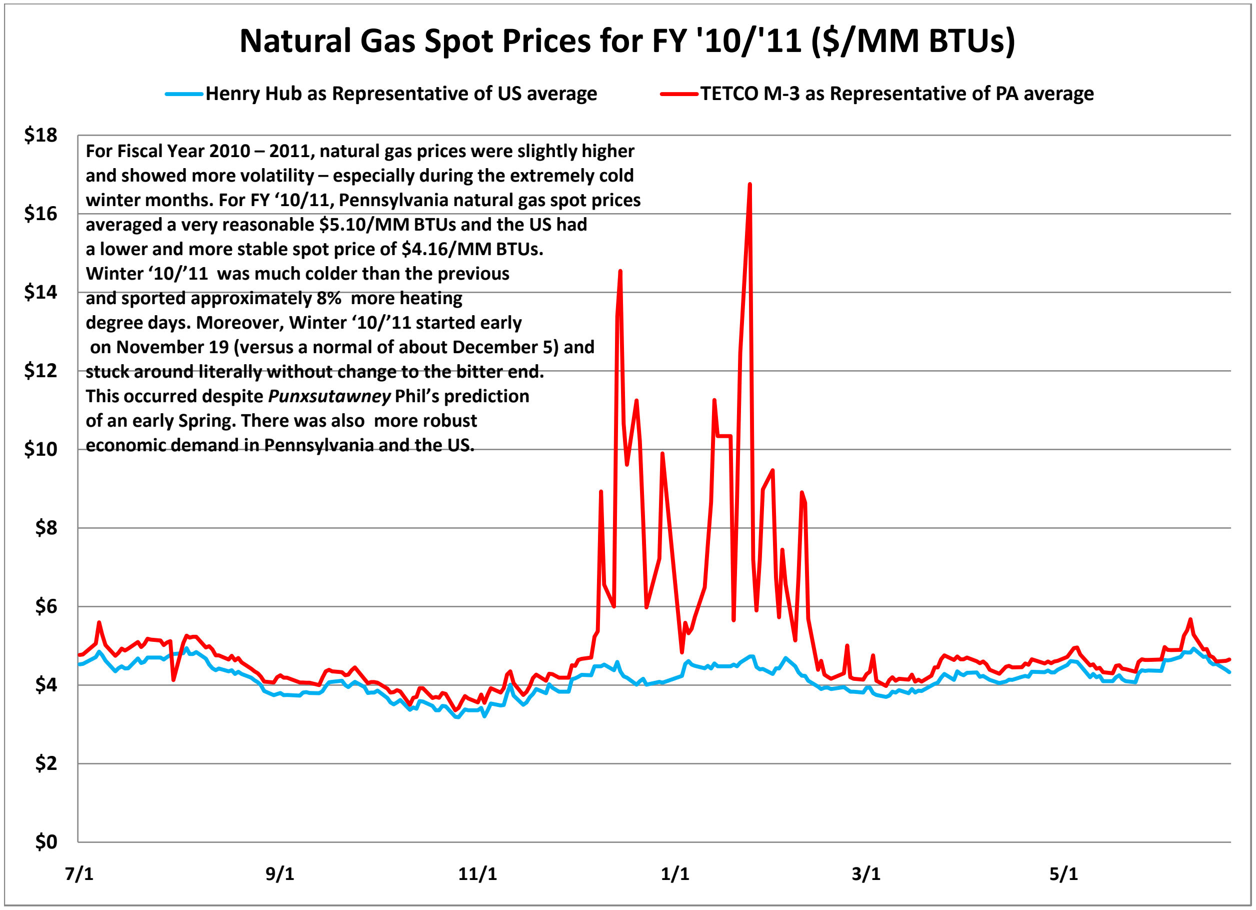
Natural Gas

Working to ensure safety, the PUC inspects the state's natural gas pipelines while regulating natural gas distribution company base rates and default service rates, and encouraging the development of competitive markets.

As the country began to see economic recovery, the fiscal year saw a slight increase in natural gas prices. The prices for the most part were steady from about $5/MM British Thermal Units (BTUs) to about $4/MM BTUs although winter weather did provide some limited volatility. In Fiscal Year 2010-11, the Commission continued its examination of the jurisdictional issues related to Marcellus Shale development. Also, the Commission moved forward on industry items designed to remove market barriers and increase competition in Pennsylvania's retail natural gas services market. Additionally, the PUC continued its support for legislative approval of a distribution system improvement charge that would facilitate the timely recovery of costs of infrastructure improvements and would promote increased safety in the state's natural gas distribution system. The PUC's Gas Safety Division continues to monitor the safety of the fuel that heats 51 percent of the homes in the state and oversees the transporting of gas and hazardous liquids resulting from the Marcellus Shale formation for non-public utility pipelines. Settlements for about $130,000 were reached with natural gas companies that were under informal investigation for violating portions of the Public Utility Code or PUC regulations. Currently, Pennsylvania has 32 regulated natural gas distribution companies (NGDC)and 110 licensed natural gas suppliers (NGS).

Wholesale Natural Gas Prices

For Fiscal Year 2010-11, natural gas prices were slightly higher and showed more volatility – especially during the extremely cold winter months. During the fiscal year, Pennsylvania natural gas spot prices averaged a very reasonable $5.10/MM BTUs and the United States had a lower and more stable spot price of $4.16/MM BTUs. The winter months of 2010-11 were much colder than the previous and sported approximately 8 percent more heating degree days. Moreover, the winter of 2010-11 started early on Nov. 19, 2010, compared to a normal start of about Dec. 5, and stuck around without change to the bitter end. This occurred despite Punxsutawney Phil's prediction of an early spring. There was also more robust economic demand in Pennsylvania and the country.



As shown in the graph above, prices spiked during extremely cold weather. This was not so much due to lack of production as due to pipeline constraints. These occasional price spikes occurred throughout the winter even with the increase in production in Pennsylvania from the Marcellus, and from the United States' other shale reserve production.

The U.S. Energy Information Administration (EIA) notes that natural gas production continues to grow at a strong pace despite a significant decline in gas-directed drilling activity. According to Baker Hughes, total working natural gas rigs now number 881, down 11 percent from the August 2010 level. However, growth in oil-directed drilling activity could lead to significant increases in associated natural gas production. EIA expects rising natural gas prices in 2012 to contribute to an increase in drilling activity.

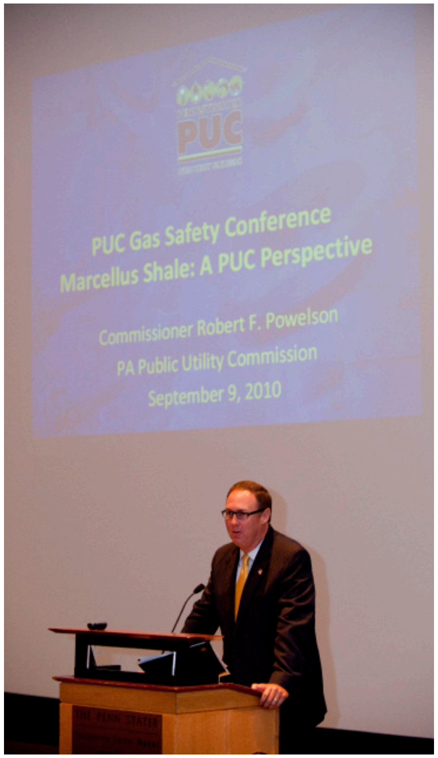
Growing domestic natural gas production has reduced reliance on natural gas imports, and contributed to increased exports. EIA expects that pipeline gross imports of natural gas will fall 4.2 percent to 8.7 billion cubic feet per day (Bcf/d) during 2011 and by 3.7 percent to 8.4 Bcf/d in 2012. Increased pipeline gross exports to Mexico and Canada during the first part of 2011 have led to an upward revision for both 2011 and 2012. Pipeline gross exports are expected to average 4.1 Bcf/d in 2011 and 3.9 Bcf/d in 2012, compared to just 3.1 billion cubic feet (Bcf) in 2010.

The United States marketed natural gas production in December 2010 of 64.0 Bcf/d - the highest rate since February 1973. The latest EIA data for monthly natural gas production show a decline in production in the lower-48 states for January 2011. Some of this decline is because of “freeze-offs” during the very cold weather that forced some producers to temporarily shut down some production. Production is expected to recover from these freeze-offs before beginning modest declines that will continue through the year because of a falling gas-directed drilling rig count.

At the end of the winter heating season on March 31, 2011, EIA expected that about 1,549 Bcf of working natural gas will remain in storage. Cold temperatures and production freeze-offs in February contributed to a larger-than-expected draw on inventories. EIA expects that inventories, though somewhat below their 2010 levels for the first half of the year, still will remain relatively robust.

Looking forward, EIA projects that total generation by the electric power sector during 2011 will remain close to last year’s level. Weather events have significantly affected generation dispatching patterns this spring. Preliminary data indicate that hydroelectric generation during March reached its highest level since 1999 as a result of heavy precipitation in the Northwest, while strong thunderstorms and tornadoes caused a number of unplanned nuclear plant outages during April. The increase in hydroelectric generation this year contributed to a decline in the share of total generation fueled by coal and flat natural gas generation during 2011. EIA expects a 2 percent increase in total electric power sector generation in 2012, fueled primarily by increases in coal- and natural gas-fired generation.

Marcellus Shale Issues



A Commission legislative priority is the extension of the PUC’s authority to inspect the remaining intrastate transmission and gas gathering lines within the state. The PUC believes this will ensure adequate protection against the risks of life, property and the environment, posed by pipeline transportation infrastructure that will be constructed from the development of Marcellus Shale gas reserves. The PUC is not seeking rate regulation associated with the recommended extension to Commission pipeline authority on otherwise non-jurisdictional pipelines. The Commission would continue to regulate rates of any pipeline that operates as a public utility.

In conjunction with the Commission making gas safety oversight a legislative priority, Senate Bill 325 and House Bill 344 were introduced to give the Commission

gas safety oversight of non-jurisdictional distribution systems and pipelines consistent with federal laws and regulation, such as those used in Marcellus Shale exploration. The Commission would also be able to respond to complaints, assess fines and penalties and enforce federal siting and construction standards under the measures. The PUC's jurisdiction would not extend to rates or ratemaking, and its jurisdiction in regard to landfill gas distribution systems is limited to pipelines outside the landfill boundaries. The regulations must be consistent with and no more stringent than federal laws and regulations.

The bills are currently pending before the state House and Senate.

As part of an ongoing dialogue, the PUC held two special *en banc* hearings on issues related to Marcellus Shale development, safety and PUC jurisdiction in Fiscal Year 2009-2010. Consumer advocates, the industry and the federal government were invited to testify before the Commission. Interested parties also were asked to submit comments.

In initiating the hearings, the Commission emphasized that the extraction of the natural gas associated with the Marcellus Shale has the potential to create hundreds of thousands of jobs while significantly stimulating the state's economy. At the same time, the PUC is striving to guard the public interest when it comes to ensuring that the natural gas, and the goods and services needed to extract it are being transported in a safe manner.

Marcellus Shale development creates numerous issues and unanswered questions, many of which impact the Commission's core functions. The *en banc* hearings examined these questions sooner rather than later so that the Commission can fully protect the public while not stifling economic growth. The hearings did not examine issues outside of the Commission's jurisdiction such as water quality or other environmental issues.

The PUC has created a page on its website on the topic -- click on Natural Gas, then Marcellus Shale.

The Public Utility Code identifies two types of natural gas public utilities. The first is the traditional natural gas distribution utility that delivers natural gas to homes, businesses and industrial customers. The second type of natural gas public utility is a type of common carrier. This type of gas utility transports natural gas, via a pipeline, for the public, for compensation. The PUC only has jurisdiction to regulate and inspect public utilities or "entities defined as public utilities."

Laser Northeast Application

On May 19, 2011, the Commission voted to remand the case of Laser Northeast Gathering Co. to the Commission's Office of Administrative Law Judge (OALJ) for further examination and the purpose of determining whether the granting of a certificate of public convenience is necessary or proper for the service, accommodation, convenience or safety of the public. A decision in the case is expected in 2011.

On Jan. 19, 2010, Laser Northeast filed a natural gas application to begin to offer gathering and transporting or conveying service by pipeline to the public in eight townships in Susquehanna County. The company has applied to be a public utility under the Public Utility Code, Title 66 of Pennsylvania's Consolidated Statues.

Two input hearings were held in July 2010 on the application. An administrative law judge (ALJ) recommended decision on Dec. 1, 2010, denied the application after finding that the service in question was not public utility service and that the applicant did not satisfy its burden of proving entitlement to a certificate of public convenience. The judge also ruled that the pipeline was being designed to serve only a specific group and not the entire public. The case was awaiting Commission action at the end of the fiscal year.

SEARCH

The Commission continues to move forward with an action plan that grew out of the efforts of the Stakeholders Exploring Avenues for Removing Competition Hurdles (SEARCH). SEARCH is a working group comprised of stakeholders representing residential, commercial and industrial customers, natural gas distribution companies, suppliers, and pipelines. SEARCH was created as a result of an October 2005 Commission report that found that effective competition did not exist in Pennsylvania's natural gas retail market.

The SEARCH action plan was designed to increase effective competition in the retail market for natural gas supply and includes three rulemakings: one that addressed market issues; one that addressed security requirements related to licensing natural gas suppliers (NGSs); and a third that addressed natural gas distribution company (NGDC) business practices.

The Commission expects to initiate a five-year review of efforts to remove barriers to effective competition in June 2013.

In June 2011, the Commission proposed changes to the final rulemaking to promote competition for natural gas suppliers. Based upon input from the Independent Regulatory Review Commission (IRRC) and the comments submitted to the IRRC, the Commission voluntarily withdrew the rulemaking in order to give consideration to the various clarification issues raised by IRRC and related comments. The goal of the rulemaking is to foster a competitive retail marketplace for natural gas service. The final rulemaking will: reformulate the "price to compare" used by consumers to judge whether the price offered by a competitive natural gas supplier (NGS) is better than the one being offered by the incumbent natural gas distribution company (NGDC); make permanent rules for establishing voluntary purchase of receivables programs (PORS); and provide guidance to ensure that the release, assignment or transfer of capacity by an NGDC to a NGS is nondiscriminatory and is at the applicable contract rate.

On June 17, 2010, the Commission issued a final rulemaking that addressed NGS creditworthiness and reasonable security requirements. The revised licensing regulations permit the use of NGS accounts receivable in a PUC-approved POR program to satisfy part of or all of a NGS's security requirement; and list possible triggering events for and reasonable criteria for adjusting the security amount. The regulation also was revised to list PUC procedures, both formal and informal, that a NGS may use to resolve a dispute over security with a NGDC, and to impose an annual reporting requirement for NGDCs on the adjustment of security amounts. The final regulation must be reviewed by the Office of the Attorney General, the Governor's Budget Office, and the designated standing committees of both houses of the General Assembly, and then approved by the

Independent Regulatory Review Commission. The final regulation will become effective upon publication in the Pennsylvania Bulletin.

The action plan's third rulemaking on NGDC business practices addressed the standardization of NGDC system operating rules; specific operation rules regarding nomination and delivery requirements, tolerance bands, cash out/penalties and standardization of electronic bulletin boards. On May 1, 2009, the Commission issued a Proposed Rulemaking Order that also directed the establishment of a stakeholders working group to develop these standards and a model Supplier Coordination Tariff format, and proposed the formation of a standing working group to develop standards for data exchange and communications, including electronic bulletin boards. The Order also directed that the stakeholders working group be run concurrently with the proposed rulemaking, and that the Commission's Director of Regulatory Operations convene the stakeholder working group.

The market issues rulemaking looked at the NGDC price to compare; reconciliation and quarterly adjustments; purchase of receivable programs; mandatory capacity release and non-discrimination; and cost recovery of competition-related activities. The Proposed Rulemaking Order was issued on March 27, 2009, with a Final Rulemaking Order being issued on Jan. 13, 2011.

The 1999 Natural Gas Choice and Competition Act allowed customers to purchase gas from independent suppliers, while still having their gas physically delivered by PUC-regulated distribution companies. In October 2005, a Commission report found that effective competition did not exist in the natural gas markets. SEARCH was formed and tasked with developing recommendations for legislative, regulation or policy changes that would increase competition in the retail natural gas market.

Small Natural Gas Company Task Force

On Jan. 15, 2009, the Commission formed a task force to review the operations of small natural gas utilities. Small natural gas utilities are defined as having intrastate operating revenues under $40 million. The PUC has 20 small natural gas companies under its jurisdiction.

The purpose of conducting a full-scale review of the small natural gas utilities is to ensure that customers of all natural gas companies are receiving safe and adequate services.

The task force is currently reviewing an application concerning the gas cost rate (GCR) for these small companies. Beginning in Fiscal Year 2011-12, the task force will informally investigate all aspects of the GCR, including examining the current inclusion of some gas costs or removal of all gas costs from base rates to result in an all-inclusive GCR. The task force also will review the appropriateness of current regulations that require the GCR companies to pay interest to customers on over-collected gas costs versus the prohibition of collecting interest from customers on under-collected gas costs. A report is expected in Fiscal Year 2011-12.

In June 2010 the task force issued a report on the operational and financial viability of these companies. The report noted the importance of all companies filing and maintaining a current gas cost rate; ordered the small gas utilities to improve their financial record keeping; and recommended that the small gas companies install proper metering equipment at the source of their natural gas, in order to be able to calculate the volume of gas entering their system and the associated losses sustained within the system. The report also suggested that utilities work on maintaining unaccounted for gas; recommended the Commission find ways to incent the larger gas distribution companies to assist the small gas companies with their operational issues; and instructed the creation of other revenue incentives such as a distribution surcharge or other ways to encourage those small gas companies at risk to file rate cases. The task force also recommends the restructuring of existing nonviable small gas systems and ordered a more rigorous financial and operational audit of those small gas companies that have been identified as being most at risk for possible failure.

Natural Gas Distribution System Improvement Charge

Based on experience in the water industry, the PUC urges the creation of a distribution system improvement charge (DSIC) to allow natural gas companies to use a surcharge on customers' bills to accelerate the replacement of infrastructure improvements. Otherwise, the utility must wait until the completion of a rate case to begin recovering its investment and receiving a return on its investment.

Legislation that would give the PUC authorization to institute a system improvement change for natural gas utilities was introduced in the General Assembly as House Bill 1294. The Commission has testified in support of the bill. The PUC has worked with members and staff on specific language to address their concerns, and believes that the bill, as currently drafted, would be a positive regulatory tool to help manage utility infrastructure costs and that the bill includes appropriate protections for all consumers. Those consumer protections include an opportunity to file complaints, a pre-established cap on the amounts that can be recovered, a provision to prevent excess earnings, and subsequent audits of the collections.

System improvement charges reduce the frequency and the associated costs of base rate cases while maintaining a high level of customer protections. The DSIC is designed to provide consumers with improved service quality; greater rate stability; fewer main breaks; fewer service interruptions; increased safety; and lower levels of unaccounted for natural gas. In light of today's difficult financial markets, DSICs and a Collection System Improvement Charge (See *Water/Wastewater*) are the type of innovative regulatory policies expected as rating agencies tighten ratings benchmarks and are a key element in maintaining access to capital markets on reasonable terms.

Section 1307 of the Public Utility Code authorizes the PUC to prescribe a mandatory system for automatic adjustment of a utility's rates by means of a sliding scale of rates. In 1997, the Public Utility Code was amended to add Section 1307(g), which specifically provided for an adjustment clause for the recovery of costs related to distribution system improvement projects designed to enhance water quality, fire protection reliability and long-term system viability.

The PUC has expressed support for a gas DSIC for NGDCs and testified before the House Consumer Affairs Committee. The PUC would like the legislation to authorize the Commission to establish reasonable parameters for use of the DSIC, via regulations, as is presently the case for water utilities. The PUC has indicated that it also should have oversight of the securitization process, which only would be available to PGW. The bill also brings treatment of natural gas service lines in line with industry practice relative to electric service lines, both of which present inherent risks to activity on and near such lines. The NGDC would be responsible for service lines and safety issues related to service line leaks, excavations and siting. The PUC also supports this aspect of the proposed legislation.

Base Rate Increase Requests

During the fiscal year, the Commission took the following actions related to about $102 million in rate increase requests:

PECO Gas

Customers Served: 480,000 customers in five counties
Requested Rate Increase: $43.8 million (5.28 percent - total revenue)
Approved Rate Increase: $19.6 million (2 percent - total revenue)
Primary Reason: To cover a significant investment in distribution plant, as well as increases in operating and maintenance costs

Valley Energy

Customers Served: 5,855 customers in Bradford County
Requested Rate Increase: $420,844 (11.2 percent - distribution only)
Approved Rate Increase: $235,000 (6.3 percent - distribution only)
Primary Reason: To cover substantial increases in operations and maintenance costs, and upgrades to its distribution plant

PGW

Customers Served: 494,400 customers in the City of Philadelphia
Requested Rate Increase: $42.5 million (4.8 percent - total revenue)
Approved Rate Increase: $16 million (1.8 percent - total revenue)
Primary Reason: To maintain the company's bond rating and fund its retirement program

Peoples Natural Gas Co.

Customers Served: 357,455 customers in 16 counties
Requested Rate Increase: $70.2 million (21.4 percent - total revenue)
Approved Rate Increase: $53 million (16.2 percent - total revenue)
Primary Reason: To allow the company the opportunity to recover sufficient revenue to cover its operating expenses and increases in rate base

Columbia Gas of Pennsylvania Inc.

Customers Served: 413,000 customers in 26 counties
Requested Rate Increase: $32.6 million (6.97 percent - total revenue)
Approved Rate Increase: $12 million (2.59 percent - total revenue)
Primary Reason: to cover its operating expenses and increases to rate base, and to provide a fair rate of return

At the end of Fiscal Year 2010-11, two natural gas rate increase requests for $54.26 million were pending before the Commission: Columbia Gas Co. ($37.8 million) and UGI Central Penn Gas Co. ($16.46 million).

PGW Working Group, Collaborative with Competitive Suppliers

On Dec. 18, 2008, in the context of approving emergency rate relief in the amount of $60 million, the Commission established a working group to examine PGW's financial situation. The group was directed to recommend improvements, solutions and other courses of action that can be implemented to maintain the company's financial viability. The Commission recognized that PGW's current management team has taken a number of steps to move PGW in a positive direction, but stated that other significant initiatives may be necessary to ensure that the company is able to provide safe, reliable and reasonably priced service to its customers.

The Working Group – comprised of representatives of the Commission, PGW and the City of Philadelphia Mayor's Office – has focused on PGW's overall cash flow position and the status of the rollover of two tranches of commercial paper (together totaling $148 million) during the first quarter of 2009. The group also has discussed PGW's remarketing efforts in connection with the 2006 bonds.

The Commission also ordered PGW to begin a collaborative process in February 2009 to explore options for transitioning some or all of its customers to an alternative default supplier. This proposal was raised by natural gas suppliers that participated in the company's emergency rate relief proceeding and was based on evidence that PGW purchases natural gas for its customers in the amount of $600 million to $700 million annually from borrowed funds.

As required, PGW submitted a report to the PUC in April 2010, detailing the progress made and identifying the areas of agreement among stakeholders; stakeholders are permitted to submit alternative reports recommending a course of action. This process is to continue until the stakeholders agree to submit a final action report, unless the Commission orders otherwise.

Mergers and Acquisitions

When reviewing mergers and acquisitions of utility companies, the Commission focuses on making sure that customers are protected and the company is a viable public utility and a good neighbor. Each application received by the Commission gets a thorough and comprehensive review. In Pennsylvania the legal standard asks whether an affirmative public benefit will result from the merger or acquisition. Public benefit is defined typically as protecting the public interest, encouraging economic development and safeguarding the environment.

On May 19, 2011, the Commission approved a change of control of T.W. Phillips and Oil Co. (T.W. Phillips) from TWP INC. to LDC Holdings II LLC, an indirect subsidiary of Steel River Infrastructure Fund North America LP (Steel River). The Commission approved the transfer by sale of 100 percent of the outstanding common stock of T.W. Phillips, currently owned by TWP to Holdings II. On Nov. 10, 2010, T.W. Phillips, TWP INC., and Holdings II filed a joint application requesting the transfer by sale. In addition to maintaining the corporate headquarters in Butler, the company committed to maintaining field offices in its service territory and staffing levels that are sufficient to provide safe, adequate and reliable service.

Gas-Safety Issues

The PUC is responsible for enforcing the Commission's pipeline safety regulations as they apply to natural gas and other public utilities transporting certain commodities by pipeline within Pennsylvania. Generally, the PUC ensures that pipeline utilities comply with the federal pipeline safety regulations that have been adopted by the PUC as its safety standards. The PUC monitors compliance with these regulations by conducting frequent inspections of pipeline facilities and examining safety records of regulated gas utilities. The inspectors also investigate incidents that include fires, explosions and major outages.

Natural Gas Pipeline Reportable Incidents

During the fiscal year, the Commission investigated three reportable incidents. During the previous three years, natural gas utilities reported 21 incidents, including eight in 2006, six in 2007, four in 2008, and three in 2009.

In 2011, two natural gas explosions in the Philadelphia and Allentown areas resulted in investigations of the companies by the Commission.

On Tuesday, Jan. 18, 2011, a Philadelphia Gas Works (PGW) employee was killed after an explosion while responding to a call of natural gas odor in the area. Crews were working to fix both a gas leak and a water main that was possibly damaged due to pressure from the break in the 12-inch gas main. As a result of the explosion, three other PGW workers and a firefighter were transported to local hospitals.

Five people were killed in a natural gas explosion on Feb. 9, 2011, in Allentown. An investigation into the explosion is focusing on a crack in a 12-inch natural gas main owned by UGI that was found after that explosion. Forty-seven homes were damaged in the explosion.

Both incidents remain under investigation at the Commission.

A reportable incident may involve an explosion, a release of gas, and, unfortunately, sometimes personal injury or loss of life. The PUC's regulations require a utility to submit a report of an accident involving facilities or operations that meet one or more of the following circumstances: 1) a release of gas involving death or injury; 2) a release of gas and $50,000 in property damages, including lost gas; and 3) a release of gas that results in an event considered significant by the operator. During the past five years, the most frequent causes of reportable incidents were facility damage, operator error and corrosion. A public utility also must immediately notify the federal government through the National Response Center of all reportable incidents.

The cause of pipeline incidents has varied during the past several years, but the PUC has identified the most frequent causes as excavation damage; natural causes such as flooding; automobile accidents; pipeline leaks caused by corrosion; and human error. The division has utilized information gathered from its incident investigations to ensure its inspection efforts focus particular attention on the areas that have previously resulted in reportable incidents.

Federal Initiatives

As a result of the two natural gas explosions, the Commission joined U.S. Secretary of Transportation Ray LaHood to call for a pipeline safety forum in Washington D.C. Sec. LaHood emphasized the importance of public safety and natural gas, and called for a forum where state officials, industry leaders and regulators would discuss improving pipeline safety. The forum was held on April 18, 2011, in Washington D.C. The Commission participated with several state and federal officials, as well as industry leaders.

LaHood is also supporting a bill that would add federal gas safety inspectors and increase penalties on companies that violate safety rules.

Natural Gas Safety Investigation Settlements

In Fiscal Year 2010-11, the PUC approved settlements with natural gas utility companies following informal investigations into violations of the Public Utility Code.

- **Peoples Natural Gas Co.** paid an $80,000 civil penalty and agreed to establish several safety mechanisms as a result of a complaint against the company, which was triggered by an explosion and fire. A November 2008 National Transportation and Safety Board (NTSB) report determined that the probable cause of the explosion and fire was damage by a third party to Peoples' two-inch distribution line. The damage stripped the pipe's protective coating and made the pipe susceptible to corrosion and failure. The NTSB determined that Peoples was not at fault.

- **UGI Utilities Inc.** spent $20,000 to utilize the services of an outside contractor to retrain their work crews regarding excavation shoring safety. On April 24, 2009, an inspector with the PUC's Gas Safety Division observed three holes at an excavation site in Bethlehem, Pa., where shoring was not being used. Shoring braces excavation sites to prevent cave-ins. The company also paid a $10,000 civil penalty.

The company also paid a $17,500 civil penalty, after an informal investigation was launched as a result of a complaint letter raised concerns about a September 2009 outage and location of propane tanks that served the Farmington Way residential subdivision in Lititz.

T.W. Phillips Gas and Oil Co. implemented a two-pronged program designed to improve the company's public education on gas safety and preventing damage to gas lines, using $15,000 to expand and improve a company program to educate local fire fighters in its service territory on the dangers of natural gas fires. The company also agreed to devote $15,000 to a new program designed to educate children on preventing damage to buried gas lines and introduce three initiatives to increase the number of leak repairs on its pipeline system, especially the bare steel pipe.

The company agreed to the settlement after an investigation of a gas explosion in Ringgold, Jefferson County, on Feb. 17, 2008, that damaged a residence.

Additional Gas Safety Activities Included:

- 1,336 inspections (compliance, regulator and relief station, discontinued service, corrosion control, transmission line, and compressor station inspections) ;
- Three investigations of reportable incidents;
- 102 non-compliance letters issued;
- 236 gas safety violations issued;
- 227 violations handled by non-compliance letters; and
- 23 violations pursued by enforcement staff

Gas Company Audits

During the fiscal year, the Commission completed 11 purchased gas cost audits (PGC), 14 gas cost rate audits and two consumer-education audits. The Bureau also reviewed 13 gas cost rate (GCR) adjustment clause filings implementing revised GCR rates. In addition, the Bureau performs periodic management and operations audits (MAs) and management efficiency investigations (MEIs) of natural gas companies. Among those MAs and MEIs completed during the 2010-2011 fiscal year were:

Columbia Gas of Pennsylvania Inc.

On Jan. 27, 2011, an audit report was released of Columbia Gas of Pennsylvania Inc. and contained recommendations that would result in an annual savings of up to $200,000 for the company. The MEI examined the company's progress in implementing 24 of the 30 recommendations from the prior management audit report released in August 2006 and its emergency preparedness efforts.

According to the MEI, Columbia Gas has effectively implemented 16 of the 24 prior recommendations reviewed and taken some action on the eight remaining recommendations. Some of the changes made by the company include: refinanced its long-term debt through NiSource Corporation which resulted in an annual interest savings of $4.275 million; increased its

capital investment for replacing its infrastructure; significantly decreased its residential receivable gross write offs resulting in an increased cash flow of approximately $3.1 million annually; implemented the process of allocating the customer call center expenses based upon the number of call minutes applicable to the distribution companies, resulting in an estimated $1.6 million annual savings; realized an annual increase in net collections; allocated charges to affiliates for the use of the main office; implemented controls to limit employee access to financial, customer, and employee data and revised contractor meter reading performance targets.

In addition, the Audit Staff made ten recommendations for further improvement that include: expedite the installation of dispatching software which accurately tracks dispatching time and has data archiving abilities; conduct an internal audit that specifically tests Columbia Gas' allocation process and the related charges to and from the affiliates; strive to control the high levels of overtime experienced by individual field employees; implement changes to decrease emergency response times after normal hours and during weekend/holidays periods; accurately and effectively track line hits and damage collection success; and continue to utilize newly formed collection practices and continue with the planned reinstitution of secondary collections.

Gas Beyond the Mains

Based on a Management Efficiency Investigation (MEI) of UGI Utilities Inc. and UGI Penn Natural Gas Inc., the Commission determined that many unanswered questions existed related to propane service in general and tariffed Gas Beyond the Mains (GBM) programs in particular that should be reviewed.

Specifically, the Commission was concerned about the GBM programs of jurisdictional gas utilities and PUC jurisdiction over other propane distribution systems. On Jan. 8, 2009, the Commission initiated an investigation to review the jurisdictional status of such systems and any other relevant issues. The investigation is to determine whether the GBM program of PUC jurisdictional utilities should continue, whether the program, as run, is cost-effective, whether UGI has been transitioning customers to gas service within a reasonable time period as it was designed, and any other issues relevant to GBM programs.

The Commission has made numerous data requests to some of our jurisdictional gas utility companies that have GBM programs and met with non-jurisdictional propane operators. Commission staff has circulated a preliminary report on the matter and is seeking further information from its jurisdictional natural gas utilities regarding GBM programs.

Steam Heat

Three steam heat utilities currently operate in Pennsylvania. Generally, steam heat is produced in central generation plants by heating water to its boiling point, and then distributing the steam heat to users through a series of underground pipes. In Fiscal Year 2010-11, the PUC's Bureau of Audits reviewed and processed 33 (monthly and annual) steam cost rate adjustment clause filings submitted by jurisdictional steam heat companies. In addition, eight steam cost rate audits were completed.


PUC

Telecommunications

In promoting a competitive telephone market, the PUC works to ensure reasonable local rates, accelerate the deployment of high-speed broadband access service, and make programs available so that no consumer is left without local telephone service.

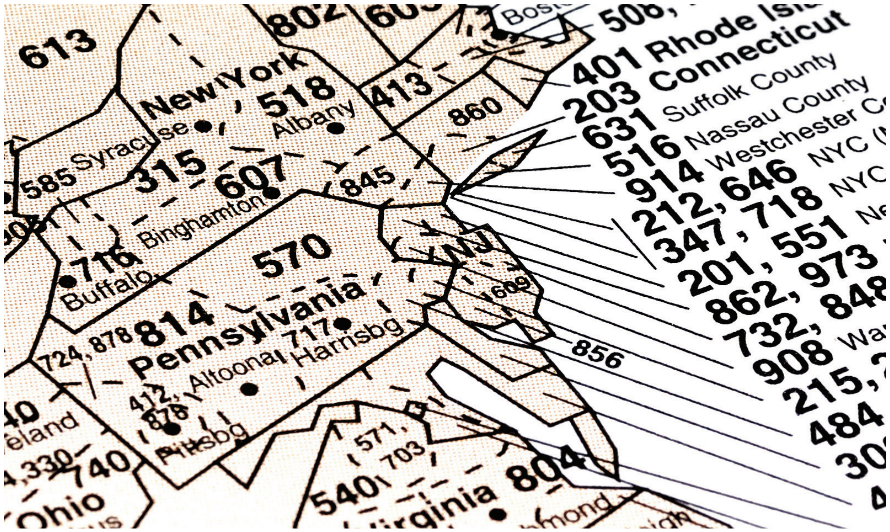
The Commission monitors the aggressive broadband deployment initiatives required by Act 183 of 2004 (Act 183 or Chapter 30), which will require regulated local exchange carriers to provide access to broadband service to all Pennsylvanians by 2015. The Commission also ensures services for low-income consumers meet or exceed national standards when determining whether a wireline or wireless carrier is entitled to federal funding as an Eligible Telecommunications Carrier.

Regulated Telephone Companies

The three largest incumbent local exchange carriers (ILECs) are Verizon Pennsylvania Inc., Verizon North Inc. and The United Telephone of Pennsylvania LLC d/b/a CenturyLink (CenturyLink). Currently, the number of telecommunications carriers certified by the Commission is as follows:

Telecommunications Carriers Total:	713
Competitive Local Exchange Carriers:	169
Incumbent Local Exchange Carriers:	37
Competitive Access Providers:	93
Interexchange Carriers, Toll Facilities-Based:	72
Interexchange Carriers, Toll Resellers:	342

Numbering Plans



The North American Numbering Plan Administrator, "NeuStar Inc" (Neustar), which is the neutral third party Number Planning Area (NPA) relief planner for Pennsylvania, petitioned the PUC on behalf of Pennsylvania's telecommunications industry because the 570, 814 and 717 area codes are projected to run out of telephone numbers. New area codes are needed when existing area codes exhaust their supply of "NXX" codes (which is the second set of three digits in a 10-digit telephone number, NPA-NXX-XXXX).

Different relief alternatives are suggested for ensuring adequate number resources. The alternatives include an overlay of a new area code and various geographic splits of the existing area codes. The petition filed by Neustar before the PUC recommended an "overlay" plan for each area code. With an overlay, the existing geographic area served by an area code is kept intact and a new area code is added to the same geographic area. New customers or existing customers adding additional lines could be assigned numbers from the new overlay area code. Ten-digit local dialing would then apply to all telephone calls per the FCC.

The 570, 814 and 717 area codes were originally expected to exhaust their supplies of telephone numbers by the third quarter of 2011, second quarter of 2012, and the fourth quarter of 2012, respectively. The Commission opened a public comment period on the issues and held public input hearings across the state on the plans.

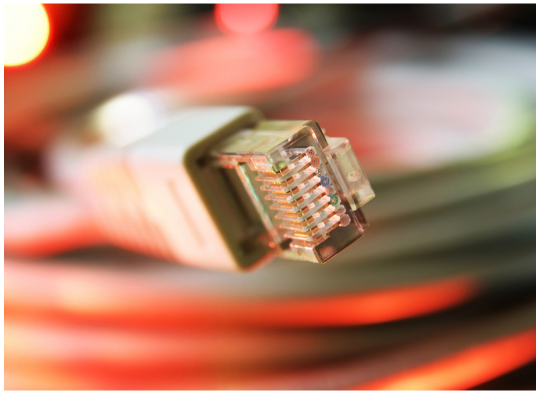
The Commission directed the implementation of an all-services distributed overlay as the form of area code relief for the 570 NPA. The number 272 will be the overlay area code for the 570 area code when the overlay code is implemented. The 570 area code was originally expected to exhaust its numbers in the third quarter of 2011. However, with the aid of numbering conservation which the PUC required carriers to implement, the expected exhaust date is now Fiscal Year 2011-12. NANPA will continue to monitor the 570 area code and provide projected exhaust updates to the Commission. NANPA is to alert us when the 570 area code is three months from exhaust at which time the carriers will begin their education and permissive dialing to implement the 272 area code.

In December 2010, the Commission approved a split of the 814 area code. Neustar assigned 582 to the northwestern area of the split, and the other would retain the 814 area code. Petitions of reconsideration were filed with the Commission on Jan. 3, 2011, to reconsider the split. On Jan. 13, 2011, the Commission granted in part the petitions of reconsideration in an order as well as a joint motion, which reopened the case for technical conferences and public hearings. Following an announcement by relief planner, Neustar, that the new projected exhaust date for the 814 area code is the first quarter of 2015, not the first quarter of 2013, the Commission is moving forward with technical conferences and public input hearings, and has suspended the timeline for implementation of area code relief.

In May 2010, the Federal Communications Commission (FCC) granted the Commission's petition to direct mandatory pooling in all area codes in Pennsylvania. The Commission implemented mandatory number pooling in all rate centers in the 215/267, 570, 610/484, 717 and 814 NPAs in June 2010. Mandatory pooling should extend the current numbering supplies within Pennsylvania's area codes.

Telephone Stimulus Monies in PA

The Commission continues to work with other Commonwealth agencies to obtain federal funding from the National Telecommunications Information Administration (NTIA) for telecommunications infrastructure and service projects for Pennsylvania. NTIA is the federal agency charged with dispsensing billions of dollars in federal funding under the American Recovery and Reinvestment Act of 2009 for those kinds of projects throughout the nation. The Commission has participated in successful efforts that have resulted in Pennsylvania being approved for more than $168 million in federal funding.



About $28.8 million was awarded to Pennsylvania to construct a "middle mile" project, which is essentially a network that will connect other networks, covering the Northern Tier Counties in Pennsylvania from Ohio to New York. NTIA also awarded Pennsylvania another $99.6 million in funding for a broadband network that will link Pennsylvania colleges and universities, research entities, and healthcare organizations.

The Commonwealth also received a $2.25 million grant to support a broadband data collection and mapping effort to identify the facilities providing broadband in Pennsylvania. Finally, the Commonwealth expects to receive a portion of the $3.7 million Latino Microenterprise TechNet and $28.5 million One Economy Corporation proposals to expand public computer access to the Latino population, as well as broadband outreach efforts for residents of public housing and low-income communities throughout the country.

The Governor established a Stimulus Oversight Commission to review, monitor and advise PA's plans for stimulus spending to assure that citizens get the best from the program. The Oversight Commission's website is www.recovery.pa.gov.

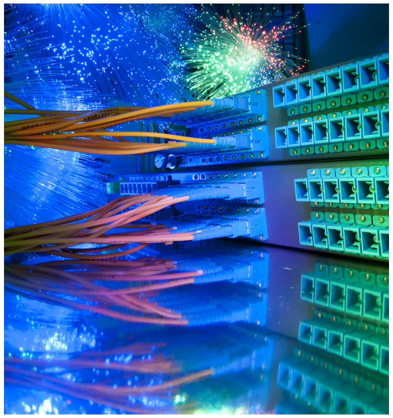
2-1-1 Three-Digit Dialing

On Feb. 11, 2010, the Commission approved the petition of the United Way of Pennsylvania (UWP), designating PA 2-1-1 as the lead implementing agency of the 2-1-1 abbreviated dialing code for providing information and referral services in Pennsylvania. During Fiscal Year 2010-2011, PA 211 began implementation of the system on a regional basis in Pennsylvania with the assistance of the telecommunications industry.

On July 21, 2000, the Federal Communications Commission (FCC) ruled that the 2-1-1 abbreviated dialing code should be used as a universally and easily recognizable number that would make it possible for callers in need to make critical connections with appropriate community-based organizations and government agencies more easily accessible. The FCC, acting on a petition filed in 1998 by the United Way of America, the Alliance of Information and Referral Services (AIRS) and several other partners, assigned the 2-1-1 abbreviated dialing code as the universal telephone number for non-emergency community information and referral services.

In 2006, the UWP and the Pennsylvania Association for Information & Referral (PAIR) joined forces and established a taskforce called the Pennsylvania 2-1-1 Collaborative that was made up of representatives from across Pennsylvania. In 2009, PA 2-1-1 was formed as an independently incorporated Pennsylvania not-for-profit organization dedicated to providing all Pennsylvanians with access to non-emergency community information and referral services.

Colocation/Wire Centers Federal Appeal



The Commission filed an appeal of the Federal District Court's decision in *Verizon PA Inc. & Verizon North Inc. v. PaPUC, et al.,* Docket No. 08-CV-3436 *(Broadview).* The *Broadview* decision reversed a 2008 Commission order that had determined that a competitive local exchange carrier (CLEC) that leases only a part of a fiber-optic cable from a competitive fiber provider (CFP) should not be counted as a fiber-based collocator when determining if a wire center is "impaired" under the FCC's *Triennial Regulatory Review Order of 2005 (2005 TRRO).* Impairment of a wire center affects certain rates Verizon may charge the CLECs. The 2008 Commission order further held that a CLEC with a fiber-optic cable that leased a competitive alternate transport terminal (CATT) from Verizon could be counted as a fiber-based collocator when determining if a wire center was "impaired." Verizon did not appeal this aspect of the 2008 Commission order.

Verizon's Performance Issues

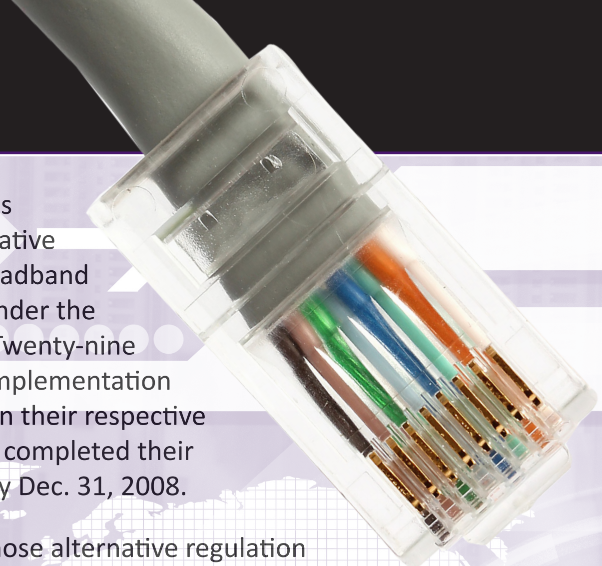
The PA Carrier Working Group (CWG) – comprised of Verizon PA, competitive local exchange carriers (CLECs), the Office of Consumer Advocate, the Office of Small Business Advocate, Commission staff, and other interested parties – focuses on the quality of the wholesale service (e.g., interconnection) that Verizon PA renders to the CLECs. The PA CWG also works with similar CWG groups throughout the Verizon multi-state footprint to resolve issues in a manner consistent with Verizon and CLEC multi-state operations. Work is ongoing in the PA CWG on PA-specific operations and problems, as well as incorporating footprint changes into the way service is measured in PA.

Verizon PA's wholesale service is evaluated using metrics that measure Verizon PA's wholesale service against Verizon PA's retail service or against benchmarks if there is no comparable retail service, as detailed in the PA Carrier-to-Carrier (C2C) Guidelines. Self-executing remedies, as detailed in the PA Performance Assurance Plan (PAP), are generated if it appears that the wholesale service was deficient. While the PA Guidelines and PA PAP are typically updated quarterly, the current metrics and remedies reflect the third major revision since inception in 1999. In April 2010, the Commission approved with modifications a financial remedy plan for Verizon PA directory listing errors that affect customers of CLECs, implemented in Pennsylvania as a result of PA CWG efforts.

In January 2011, the PUC voted unanimously to select Silverpoint Consulting LLC as the vendor to oversee the review of performance metrics and related remedies as they pertain to Verizon Pennsylvania Inc.'s wholesale interconnection devices. Silverpoint was notified of their selection, and final contract negotiations were initiated shortly thereafter. At this time, Verizon is reviewing the final contract, and the PUC's Law Bureau is waiting for signatures from all applicable parties. Once all parties have signed the final contract, a Notice to Proceed will be issued by the Bureau of Administrative Services. The parties expect work to begin on the audit in Fiscal Year 2011-12.

Chapter 30 Implementation

The Commission continues to implement key provisions of Act 183 of 2004, which modify the prior Chapter 30 provisions of the Public Utility Code. Compared to pre-existing Chapter 30 regulations, Act 183 provides more economic incentives to facilitate deployment of a Statewide Broadband Network compared to pre-existing regulations, encourages earlier completion of existing network modernization plans (NMPs) by incumbent local exchange carriers (ILECs), and provides for less Commission regulation. Chapter 30 authorizes the Commission to oversee the NMPs that provide for the deployment of broadband high-speed access connections to the Internet and other services. Act 183 also reduces filing and reporting requirements for incumbent local exchange carriers, and establishes a Bona Fide Retail Request program (BFRR), the Business Attraction or Retention Program (BARP), the Broadband Outreach and Aggregation Fund (BOAF) and the Education Technology Fund (E-Fund).



The Chapter 30 law provides three options for the alternative regulation and network broadband deployment for the ILECs under the Commission's jurisdiction. Twenty-nine ILECs proceeded with the implementation of broadband deployment in their respective networks. All these carriers completed their broadband commitments by Dec. 31, 2008.

The remaining four ILECs chose alternative regulation options. CenturyLink and Windstream Pennsylvania LLC elected to complete their broadband commitments by 2013 and invoked a zero percent inflation offset value in their respective price cap mechanisms, and also undertook the BFRR obligations. Verizon PA and Verizon North, the only non-rural ILECs, elected to complete their broadband deployment by 2015, which incurs a .5 percent inflation offset value in their respective price cap formulas, and requires a BFRR program and BARP obligations.

Broadband Deployment

Pennsylvania is home to one of the country's most aggressive broadband deployment initiatives as required by Act 183 of 2004. In a report released March 4, 2008, by the U.S. Internet Industry Association, Pennsylvania's Act 183 was cited as "the most aggressive broadband deployment plan in the nation." By 2015, Act 183 requires that every Pennsylvanian will have access to broadband services, even in the more rural areas.

Act 183 also contains several programs designed to accelerate broadband deployment. Currently, the Commission has examined the Federal Communications Commission's (FCC) National Broadband Plan and has filed comments in the various proceedings initiated by the FCC to emphasize Pennsylvania's advances in broadband deployment.

Bona Fide Retail Request Program

The Bona Fide Retail Request Program (BFRR) established by Act 183 of 2004 provides a means for customers to obtain broadband services sooner than they may otherwise receive them through their local telephone company's deployment schedule.

Through the BFRR, customers may demonstrate that sufficient demand for high-speed Internet service exists in their area by submitting applications to their local telephone company. When a minimum of 50 retail access lines or 25 percent of the retail access lines within a community service area (whichever is less) commit to purchase broadband services for a minimum of one year, the local telephone company must make those services available in that area within 12 months. Community service areas are geographic areas served by the same central office or remote terminal. Typically, a community service area will be all the homes and businesses within approximately two or three miles of one of these remote terminals or central offices.

Verizon Pennsylvania (Verizon PA), Verizon North Inc. (Verizon North), the United Telephone Co. of Pennsylvania LLC d/b/a CenturyLink and Windstream Pennsylvania Inc. are required to offer BFRR programs under the provisions of Act 183.

Each of these four companies maintains a required toll-free telephone number and website containing information about their respective BFRR program. Consumers also can find more information about the BFRR program through Pennsylvania's Department of Community and Economic Development (DCED) website at www.newpa.com/broadband.

The participating companies must provide semi-annual reports to the Commission consisting of the number of requests for high-speed access services to the Internet received during the reporting period by community service areas and the actions taken by the company on those requests. The Commission is required to monitor and enforce the compliance of the participating companies with their obligations to offer and administer a BFRR program.

Chapter 30 sets limits, under which, in any given 12-month period, a company is not required to work on more than 40 active BFRR requests and is not required to work on more than 20 such requests that "require property acquisition, including rights-of-way, or new construction." The two Verizon companies have filed certifications stating that they have met both the 40 overall and 20 major build statutory thresholds.

Business Attraction or Retention Program

Verizon PA, Verizon North, CenturyLink and Windstream Pennsylvania Inc. also are required to implement a Business Attraction or Retention Program (BARP). The BARP permits DCED to aggregate customer demand and facilitate the deployment of advanced or broadband services to qualifying businesses that DCED seeks to attract or retain in the Commonwealth. Under this program, DCED may submit requests to the applicable company on behalf of qualifying businesses in areas that DCED deems priority areas for economic development. The Commission is required to monitor and enforce the compliance of participating companies with their obligations under the BARP.

Education Technology Program

Act 183 requires the Department of Education to create the Education Technology Program to provide grants to school entities from the Education Technology Fund (E-Fund) to purchase or lease telecommunications services and equipment related to broadband. Applicant schools must be able to match their E-Fund grants.

Broadband Outreach and Aggregation Program

To further broadband deployment, this program was established by DCED as mandated in Chapter 30. This program makes expenditures and provides grants from the BOAF. The fund is for outreach programs -- for business and residential consumers, political subdivisions, economic development entities, schools, and healthcare facilities -- concerning the benefits, use and procurement of broadband services, and seed grants to aggregate customer demand.

The Commission receives an annual report from DCED to verify the accuracy of the contributions from the four participating ILECs.

Promoting Broadband Access and Education

In order to finance the E-Fund and BOAF, Act 183 requires the Commission to annually assess the four ILECs opting to complete their broadband buildout in 2013 or 2015; such assessments are established to be 20 percent of the first year's annual revenue effect of any rate increase gained from the elimination or reduction in the inflation offset in the carriers' NMP formula. The acquired funds are divided equally between the E-Fund and the BOAF until June 30, 2011, when the E-Fund is statutorily discontinued. Thereafter, the assessment is reduced to 10 percent until the participating ILEC achieves full broadband deployment or until the termination of the BOAF on July 1, 2016. At no time may the BOAF exceed $5 million.

The E-Fund also receives an assessment from the non-rural ILECs (Verizon PA and Verizon North) based on their access line apportionment. For the fiscal years 2005-06 and 2006-07, the annual assessments were $7 million. For the fiscal years 2007-08 through 2010-11, each year's assessment is the difference between $7 million and any unencumbered amount remaining in the E-Fund. In addition, the Verizon companies expressed a commitment in 2004 to Gov. Rendell that, if the assessment amounts for E-Fund were less than $10 million, the Verizon companies would provide an additional contribution of up to $3 million annually to make up the difference during the life of the fund.

In June 2011, the Commission approved the statutorily-mandated assessment on applicable ILECs for payment to the BOAF of $50,100 for the 2011-12 Fiscal Year. No assessment was made for payment to the E-Fund, as this fund expired on June 30, 2011.

Connect America Fund

On April 21, 2010, the Federal Communications Commission (FCC) released a Notice of Inquiry (NOI) and a Notice of Proposed Rulemaking (NPRM) that sought public comment on the FCC's effort to replace the legacy high-cost universal service fund (USF) with a broadband fund. In effect, the FCC seeks to eliminate USF funding and redirect it to promoting broadband in rural areas. The replacement for the USF will be called the Connect America Fund (CAF).

The NPRM seeks comments on a number of proposals to cut legacy universal service spending in high-cost areas and to shift support to broadband communications. These proposals include: 1) capping the overall size of the high-cost program at 2010 levels; 2) re-examining the current regulatory framework for smaller carriers in light of competition and growth in unregulated revenues, and 3) phasing out support for multiple competitors in areas where the market cannot support even one provider. Comments to the NPRM are due in Fiscal Year 2011-12.

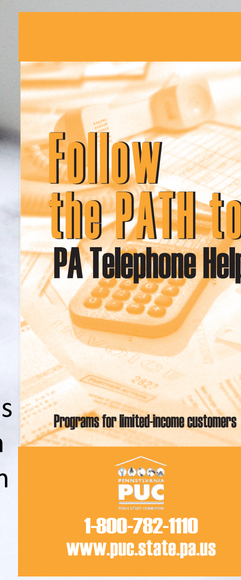
PUC-Approved Price Cap Filings

To date, 23 incumbent local exchange carriers (ILECs) adopted price caps using the gross domestic product price index (GDP-PI) outlined in Act 183 of 2004 as the inflation factor under the alternative regulation portion of their Chapter 30 Plans. As a result, the carriers file their annual price stability mechanism index either accompanied by tariffed rate changes and/or banked revenue increases/decreases. Through past settlements reached with the state's Office of Consumer Advocate, most of the ILECs are required to implement banked revenue changes in actual rates within four years or forego the revenue increase. Verizon PA, Verizon North and CenturyLink are required to immediately implement any rate decrease of more than $500,000. Pursuant to Chapter 30, during the period from 2005 to 2011, companies with price cap mechanisms collectively have been permitted to increase local service rates. As of the end of FY 2010-11, those were $123.379 million with total banked revenues of $22.197 million.

Bundled Services for Lifeline Participants

The Lifeline 135 program is available to qualified customers of eligible telecommunications carriers. Under the program, customers who participate in certain public assistance programs, or who have incomes at or below 135 percent of the federal poverty guidelines can receive a discount on their monthly local phone service for one telephone line. The discounts are paid out of the Federal Universal Service Fund, which is subsidized by contributions from all telephone companies.

As a result of a 2007 complaint filed by the Office of Consumer Advocate, the Pennsylvania Utility Law Project and AARP, the Commission ordered Verizon PA Inc. and Verizon North Inc. to also offer its customers enrolled in Lifeline 135 an opportunity to subscribe to bundled services. The companies' current tariffs permit Lifeline 135 customers to subscribe to three types of bundled services: local service with three vertical services; local service with three vertical services and regional toll; and local service with three vertical services, regional toll and long distance. In an effort to increase awareness about Lifeline, the PUC developed an informational brochure, "Follow the PATH to PA Telephone Help." The brochure provides information about Lifeline and other available programs for limited-income telephone customers. This program also is being examined by the FCC, who may take action in FY 2011-12.



PA Universal Service Fund

The PA Universal Service Fund (PaUSF) supports the affordability of basic local telephone service that is provided by rural ILECs in Pennsylvania. The Commission's third-party administrator of the PaUSF is Solix Inc. The company is under contract with the Commission to administer the fund through Dec. 31, 2011. Withum, Smith & Brown submitted an auditor's report dated June 2011. This report is on the PUC's website at www.puc.state.pa.us, under the Telecommunications tab, click on PA Universal Service Fund.

The Commission approved a state USF contribution rate for 2011 calculated to produce approximately $33.873 million to be distributed among recipient carriers. Of the $33.8673 million, $1.6 million is held in reserve for uncollectibles, and $155,778 is paid to Solix.

The amount is collected via assessments against telephone company intrastate retail revenues from the prior year. All PUC-jurisdictional telecommunications companies are assessed and file annual intrastate retail revenue reports with Solix that are used for calculating the assessment rate for the upcoming year. All incumbent LECs in Pennsylvania except Verizon PA, Verizon North (formerly GTE North), and Windstream D&E Inc. are annual net recipients from the Fund.

As part of the Commission's decision resulting from its investigation into further intrastate switched access charge reductions and the PaUSF, the Commission directed that a rulemaking proceeding be instituted to consider potential changes to the PaUSF Regulations in light of telecommunications market realities, including intermodal wireline and wireless competition, as well as changing policy goals before the FCC and this Commission which affect affordable service to end users.

The rulemaking will evaluate potential reforms to the PaUSF Regulations and the PaUSF itself. Certain determinations made by the Commission in the investigation that are relevant in considering potential PaUSF reforms in the PaUSF Rulemaking include: (1) the size of the PaUSF shall not increase; (2) RLECs will not receive financial support from the PaUSF by merely maintaining an $18.00/month local rate benchmark; and (3) an affordability rate of $23/line/month has been found to be reasonable.

At the same time, the following issues have been deferred to the PaUSF Rulemaking: (1) whether the PaUSF should be reformed; (2) a review of any anticompetitive effects that a reformed PaUSF may have with regard to the operation of the wireline and wireless telecommunications services marketplace within the Commonwealth; (3) whether a needs-based test should be established to determine if assistance should be provided to RLECs for service in high cost service areas and/or for assistance to low-income customers.

In December 2010, the Pennsylvania Telephone Association (PTA) filed a petition with the Commission that seeks to expand the base of contributors to the PaUSF. Currently, the PaUSF is funded by incumbent local exchange carriers, competitive local exchange carriers and interexchange carriers. The contribution rate for these carriers has been increasing from .075 percent in 2001 to 1.25 percent in 2011. PTA argues that, because they use the Public Switched Telephone Network, wireless carriers and Voice over Internet Protocol (VoIP) providers should be required to contribute to the fund. PTA notes that expanding the base of contributors would provide dramatic relief to the current contributors and remove a competitive disadvantage experienced by the traditional PaUSF participants.

Eligible Telecommunications Carriers

The Federal Universal Service Fund (FUSF) was established by the Federal Communications Commission (FCC) in 1983 to make local telephone service more affordable in a competitive telecommunications market by providing subsidies to carriers in high-cost areas. The federal fund is separate from the PA Universal Service Fund. Carriers operating in Pennsylvania that desire FUSF money must meet certain service obligations and offer discounted services to low-income consumers to be deemed an Eligible Telecommunications Carrier (ETC) by the Commission.

The Commission currently exercises its ETC designation authority with respect to incumbent local exchange carriers (ILECs), competitive local exchange carriers (CLECs) and wireless carriers. The Commission evaluates ETC requests to ensure that carriers seeking ETC status comply with public safety and other requirements consistent with the broader public interest.

On Oct. 1, 2010, the Commission adopted a policy statement regarding ETCs. The policy statement provides that, in order to obtain Pennsylvania ETC status, a company is expected to meet the FTC standards regarding ETCs and the FUSF and section 214(e) of the Telecommunications Act of 1934 (47 U.S.C. § 214(e). In addition, ETCs seeking low income support under Lifeline and Link-up America programs should satisfy the minimum standards established in 66 Pa. C.S. § 3019(f) (relating to Lifeline service) and comply with the Commission's Lifeline and Link-up Order dated May 23, 2005.

The Commission applied this policy in *Petition of Virgin Mobile,* Docket No. P-2010-2155915 in December 2010. There currently are ten outstanding ETC petitions.

Mergers and Acquisitions

In reviewing mergers and acquisitions, the Commission strives to ensure that customers are protected, and that the company has the requisite managerial, financial and technical capability to provide services. Commission staff works to provide a comprehensive and thorough review of each application. In Pennsylvania, the applicable legal standard mandates that an affirmative public benefit shall result from a utility merger or acquisition. Public benefit is defined typically as protecting the public interest, encouraging economic development and safeguarding the environment.

CenturyTel/Embarq Merger

On March 1, 2011, the Commonwealth Court affirmed the Commission's approval of a merger between CenturyTel and Embarq. The Court held that the Commission followed the precedent established by the Pennsylvania Supreme Court and properly evaluated the impact of the merger on competition. The Court further held that the substantial evidence supported the Commission's determination that the merger would provide affirmative benefits for the state's citizens and that the merger would positively affect competition in Pennsylvania.

In an order dated March 1, 2010, the Commission approved the merger of CenturyTel and Embarq, subject to conditions imposed by the FCC, which also approved the merger. The Office of Small Business Advocate (OSBA) appealed the Commission's order to Commonwealth Court, arguing that the Commission erred in concluding that financial strengthening and the post-merger company's resulting enhanced ability to compete was a public benefit of the merger.

OSBA also argued that as a result of the merger, an incumbent local exchange carrier (ILEC) would be strengthened, which hinders a competitive local exchange carriers (CLEC's) ability to compete and is thus anti -competitive.

CTC, et al/Earthlink

In April 2011, the Commission entered an Order approving an application for the transfer of indirect control of CTC Communications Corp. (CTC), Conversent Communications of Pennsylvania, LLC (Conversent), Lightship Telecom, LLC (Lightship), and Choice One Communications of Pennsylvania, LLC (Choice One) to EarthLink, Inc. (Earthlink).

Core Communications, Inc. (Core) filed a petition to intervene and protest the application. Core alleged that Choice One and CTC have a history of refusing to compensate carriers for services rendered although they are legally required to do so. It asked the Commission to impose sufficient conditions to assure the merger would not permit the Joint Applicants to engage in anticompetitive behavior.

The Commission acted to adopt the ALJ's decision to deny Core's Petition and to adopt the Merger. The Commission ruled that, based on the pendency of a prior complaint by Core, which included the same parties, the same rights asserted, and the same relief sought in each case, that Core's objection to the expedited treatment of the application was moot and did not affect the determination of whether to fully litigate the case. The Commission concluded that remanding the matter for a hearing before an ALJ would violate the lis pendens doctrine and require the applicants to be forced to defend itself against the same claims twice. The Commission ruled that the applicants should continue to be responsible for any liability that may arise for events that occurred prior to the merger but that a review of the document revealed that Choice One' and CTS' legal obligations to pay for services, will continue to exist after the transaction closes.

Under the merger, CTC, Convergent, Lightship and Choice One will become wholly-owned subsidiaries of EarthLink. The merger will create one of the largest nationwide competitive communications service providers serving Internet and business customers and position Earthlink, which currently has subsidiaries operating in all fifty states and the District of Columbia, to realize cost savings and achieve synergies expected to strengthen its ability to enhance service offerings and provide more advanced communications to a broader customer base. The transaction will be seamless to all of the applicants' customers as they will remain customers of their respective providers with no change in rates, terms and conditions of service after the merger.

CenturyLink/Qwest

On Oct.14, 2010, the Commission approved a Joint Settlement Agreement filed by all of the active parties regarding the joint application for the change of control of Qwest Communications Company LLC (Qwest) to CenturyLink (CL). The joint application filing was a consequence of a merger agreement between Qwest Communications International, Inc. (QCII), the holding company of Qwest and CL, whereby QCII will become a wholly-owned first tier subsidiary of CL. The settlement, among other things, will result in a savings of time and resources of the Parties and the Commission. CL's Pennsylvania customers will benefit from significant ongoing capital investment through the acceleration of CL's build out of its Pennsylvania facilities for broadband availability and limited increases to CL's local service rates and other non-competitive service rates in 2011 and 2012. In addition, the settlement requires CL to meet with the OCA and OSBA prior to making any pledges of its assets and any filing made under Chapter 19 of the Public Utility Code regarding securities. The approval by the Commission of the joint application and similar actions by regulatory agencies across the country resulted in CL becoming the third largest telecommunications company in the United States as of April 2011. The combined company will operate under the CenturyLink name and brand.

Access Charge Proceedings

Intrastate carrier access charges are a method of compensation between telecommunications carriers in the exchange of certain types of long-distance traffic. The Commission has carried out a series of intrastate carrier access charge reforms. These reforms have impacted at times local exchange rates that are charged by ILECs.

RLEC Access Charge Proceeding

On June 30, 2011, the Commission acted upon the Rural Local Exchange Company (RLEC) Access Charge Investigation by directing further reductions to intrastate access charges. All affected RLECs were ordered to rebalance their switched access charges with offsetting increases to local service rates so that the net effect of the access charge reductions would be revenue neutral.

The major rulings resulting from the investigation include the following:

- RLECs shall file tariffs to mirror their intrastate Traffic Sensitive (TS) switched access rates with their interstate TS switched access rates. In a few instances where certain RLECs' intrastate TS switched access rates are below their federal counterparts, those RLECs have the option of increasing their intrastate TS switched access rates to match their interstate TS switched access rates.

- RLECs with a Carrier Charge (CC) greater than $2.50/line/month are directed to decrease their CC to a rate not to exceed $2.50/line/month. The CC is a non-traffic sensitive monthly charge that carriers pay to RLECs in order to cover the joint and common costs of the local loop. Current CCs range from $0/line/month to $17.99/line/month. In the few instances where an RLEC's CC is less than $2.50/line/month, those RLECs have been given the option of maintaining their CC at the current level or increasing it to a rate not to exceed $2.50/line/month.

- Establishment of an access charge rate rebalancing schedule, which will provide an opportunity for the RLECs to increase their non-competitive service rates to produce a sufficient level of revenue to offset the lost revenue from decreases to their intrastate TS switched access rates. The rebalancing will be accomplished in three phases over a four-year period in a revenue-neutral manner as required by Chapter 30 of the Public Utility Code.

- Implementation of a rulemaking to evaluate potential reforms to the PaUSF Regulations and the PaUSF itself.

The RLEC investigation had been stayed for three years, from 2006 to 2009, because of uncertainties concerning intercarrier compensation issues pending before the Federal Communications Commission (FCC). FCC action had the potential to significantly affect intrastate access charges as well as federal Universal Service support for Pennsylvania telephone customers. After waiting for a decision from the FCC for some time, the Commission ultimately decided to lift the three-year stay in August 2009.

The Commission currently has the following related access charge proceedings before it:

- **Verizon Companies Access Charge Investigation** - In May 2010, the Commission lifted a three-year stay on the Verizon companies' (Verizon Pennsylvania Inc. and Verizon North Inc.) Access Charge Investigation. The stay was originally placed into effect pending the outcome of a decision by the FCC in its Unified Intercarrier Compensation proceeding. At the same time, the Commission also adopted an alternative time frame for the required adjudication of this investigation to begin after the issuance of a Recommended Decision by the Presiding Administrative Law in the RLEC Access Charge Investigation. The RLEC Recommended Decision was issued in August 2010, and the ALJ assigned to this investigation proceeded to develop the record which closed in June 2011. A Recommended Decision is expected to be issued in the third quarter of 2011.

- **Core Communications v. AT&T** - In May 2011, the Office of Administrative Law Judge (OALJ) issued an opinion addressing a dispute between two Competitive Local Exchange Carriers (CLECs), Core and AT&T. The decision addressed the Commission's authority to set the intercarrier compensation rate for local calls when those local calls are used to reach the internet. The OALJ decision relied on an FCC brief in a 10th Circuit proceeding in which the FCC claims that its *ISP Remand Order* includes disputes between CLECs over compensation for dial-up calls to the internet. The Federal Communications Commission (FCC) *ISP Remand Order* ruled that the FCC has authority to set the compensation rate for local calls between incumbent carriers (ILECs) and competitive carriers (CLECs) when those calls were used to access the internet. The Commission had challenged that FCC claim of authority but was ultimately unsuccessful in getting the U. S. Supreme Court to review the decision. The issue before the Commission is whether the *ISP Remand Order* includes CLEC-to-CLEC disputes over compensation when local calls are used to access the internet.

The dispute arose after Core filed a complaint that AT&T was refusing to remit compensation to Core for local calls when they were used to access the internet. There is an ongoing dispute nationwide between CLECs whether it is the states or the FCC that has jurisdiction over those local calls, what the compensation rate should be for those local calls, and whether any compensation is due at all. Some carriers have also refused to pay any compensation rate at all for these calls by citing an even earlier FCC decision that "exempted" Enhanced Service Providers (ESPs) from the obligation to pay access rates when interconnection to the telephone network is used to provide "enhanced" or "information" service. Those carriers claim that any local call that is part of an "information service" or is an "information service" is exempt from state commission authority and any access payment obligation. The matter is under Commission consideration.

In addition to the above major access charge investigations, litigation continues before the Commission for various complaints filed by both ILECs and CLECs concerning the application and payment of intercarrier compensation. Some cases hinge on whether intercarrier compensation can be assessed on certain types of traffic. Some carriers concede that some sort of payment may be appropriate but insist that the calls in question are not long distance toll and, therefore, intrastate access rates are inappropriate. Some carriers believe reciprocal compensation rates, a considerably lower rate applied to local calling, are more appropriate. These proceedings are being litigated before the Commission. In February 2010, the Commission addressed intercarrier compensation issues between Palmerton Telephone Company and Global NAPs South Inc.

PUC Involvement at the FCC

Federal telecommunications regulation by the FCC is playing an increasingly important role in the delivery of telephone service in Pennsylvania. This requires the Commission to expend resources and become actively involved in various proceedings at the FCC regarding several important issues that directly impact Pennsylvania consumers. These proceedings include:

The National Broadband Plan is a proceeding in which the FCC is seeking input from the public as part of an FCC report to Congress on what measures are needed to deploy broadband and support broadband services throughout the nation, particularly in rural areas. The FCC says that federal stimulus will probably be insufficient to attain rural broadband deployment so other support may be required, including support from the Federal Universal Service Fund (FUSF). The FCC submitted the report and is now in the process of issuing Notices of Proposed Rulemakings (NPRMs) and Notices of Inquiry (NOIs) to solicit comments on the national broadband initiatives.

The Commission has submitted comments to the FCC, particularly given the very large increase in the FUSF (conservatively estimated to range from $20 to $350 billion, depending on the speeds used to define broadband) that may be required as the FCC determines whether to support broadband deployment and services from the FUSF. Currently, Pennsylvania annually contributes $176 million more into the FUSF than it gets back. The Commission is concerned that this annual net $176 million contribution to support the current $7.1 billion FUSF fund may grow astronomically if $40 billion in additional broadband deployment and services costs are funded by the FUSF without reform of the FUSF.

The Commission urged the FCC to require that any state receiving any support for broadband deployment or services be required to implement measures similar to those undertaken in Pennsylvania under Chapter 30. Recipient carriers should be required to get support from end-users for broadband deployment as a precondition to getting FUSF support. The Commission has reminded the FCC that Pennsylvania has the nation's third largest rural population and successfully completed a broadband deployment program in all but two rural carriers' service territories by 2009. The Commission also has reminded the FCC that the remaining two rural carriers are on schedule to complete their broadband deployment programs no later than 2013 and that Verizon will complete their deployment by 2015.

Universal Service is the term used for the FCC's efforts to provide federal universal service fund (FUSF) support to carriers so that reasonable local rates can be maintained in high-cost areas, typically rural areas. The FUSF is supported by an assessment on carriers' interstate calling revenues. Those revenues have declined due to technological changes even as the FUSF support distributions have increased.

The four parts of the FUSF are High-Cost, Schools and Libraries, Rural Health and Low Income. Pennsylvania annually pays $176 million more into the FUSF than it receives although some rural carriers do receive more in support than they pay. The FCC is examining ways to limit burgeoning FUSF costs, particularly for the High-Cost and Low-Income programs. The FCC is also considering including broadband deployment as a new program initiative within the FUSF.

The Commission actively has participated in proceedings before the FCC in order to minimize increased costs to Pennsylvania, including costs for any national broadband deployment program. As mentioned previously, the Commission is particularly concerned that the current FUSF fund may grow by an additional $40 billion if broadband deployment and services are fully supported by the FUSF. The Commission also is concerned that any federally mandated reductions in carrier revenues may result in local rate increases, particularly if there are reductions in access rates that require revenue neutral recovery under Section 3017(a) of Chapter 30 within Pennsylvania.

Intercarrier Compensation is the term used for the payments that telephone companies and their competitors pay each other to use the other's networks. The three forms of compensation are interstate access rates (for interstate long-distance calls), intrastate access rates (for in-state long-distance calls), reciprocal compensation (for in-state local calls) and bill and keep compensation (each carrier pays its costs for call completion). Currently, reciprocal compensation is the lowest rate, interstate access rates are next, and intrastate access rates are the highest.

The FCC proposed establishing a national compensation rate for all calls at one rate, including the rate for local and in-state long distance calls traditionally set by the states. The FCC says this is necessary in order to prevent carriers from classifying calls in a way that permits carriers to receive a more favorable compensation. The Commission is active in this proceeding and awaiting further FCC action.

Forbearance is the term used for the authority the FCC has to "waive" or "set aside" federal laws and regulations on various regulatory mandates including reporting requirements and competitor access to facilities. The FCC recently granted forbearance from statutory obligations to report on customer satisfaction and carrier investment in their networks although, in that decision, the FCC also opened a new rulemaking. The Commission actively has opposed any forbearance that would undermine Pennsylvania's legislative authority to address its own state mandates provided by statute or regulation.

In June 2009, the FCC issued a series of rules outlining the procedure governing future forbearance proceedings. The FCC rules adopted a "complete as filed" regulation and put limits on a petitioner's ability to unilaterally withdraw forbearance requests. The FCC's final rules reflect many proposals submitted by the Commission in partnership with other state commissions in the Mid-Atlantic Region.

PA Telecommunications Relay Service Program (TRS and CTRS), Telecommunications Device Distribution Program (TDDP) and Print Media Access System Program (PMASP/Newsline)

The goal of TRS, CTRS, TDDP and PMASP is to provide functionally equivalent access to telecommunications and print media. These programs provide access to and from the special needs populations that they are designed to serve. The programs continue to be funded from the TRS monthly surcharge on wireline access lines, which is $0.08 per line for Fiscal Year 2011-12.

AT&T has provided traditional TRS as a certificated TRS provider since 1990. Captioned Telephone Relay Service (CTRS), which has been available in Pennsylvania since 2003 and is currently provided by Hamilton Relay under contract, is an alternative to traditional TRS for individuals with some degree of hearing and speech within the deaf and hard-of-hearing community.

TDDP, instituted in 1996, provides free telecommunications devices for consumers meeting eligibility requirements related to disability, income level, age and residence. PMASP (also known as Newsline) instituted in 2005, is an on-demand newspaper reading service, accessible via toll-free telephone lines for the blind and others who cannot physically read a newspaper. While funded by the TRS surcharge, TDDP and Newsline are coordinated by the Bureau of Labor and Industry.

During Fiscal Year 2009-10, the Bureau of Audits initiated the audit of the TRS program's receipt and distribution of funds received from the billing of the applicable TRS surcharge rates for the fiscal years ending April 30, 2007, and April 30, 2008, and the fiscal period ending Feb. 28, 2009. That audit is still being performed. Also, during this fiscal year, the Bureau of Audits completed the audit of the underlying costs of TDDP, as well as PMASP for the fiscal years ending June 30, 2008, and June 30, 2009. No irregularities were found. (*See also Consumers*).

Palmerton Telephone Company vs. Global NAPs

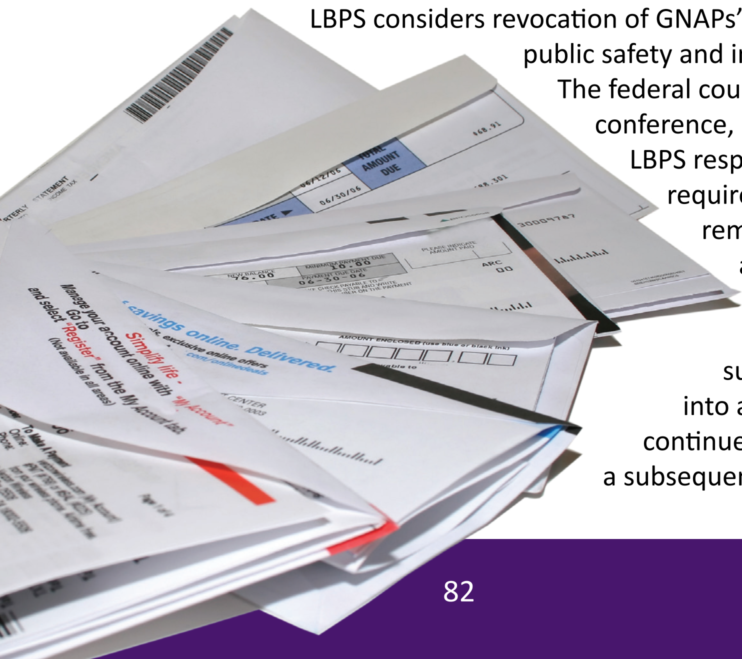
In a March 2010 Order, the Commission disposed of the intercarrier compensation dispute between Palmerton Telephone Company and Global NAPs South Inc. (GNAPs). Palmerton had filed a formal complaint with the PUC alleging that GNAPs did not pay intrastate carrier access charges for the indirect termination of certain network traffic. GNAPs justified its non-payment largely on the basis that this traffic was Voice over the Internet Protocol (VoIP) IP-enabled "enhanced" traffic that was not subject to intrastate carrier access charges and, broadly, not subject to the Commission's jurisdiction.

The Commission determined that GNAPs provides common carrier telecommunications services in its wholesale transport and indirect termination of traffic at Palmerton's facilities — inclusive of interexchange nomadic VoIP calls — that are subject to the Commission's intrastate jurisdiction on the basis of applicable Pennsylvania and federal law. Therefore, the Commission found that GNAPs was liable to Palmerton for the nonpayment of intrastate carrier access charges. The Commission ordered GNAPs to pay Palmerton the amount of access charges owed and assessed a $50,000 civil penalty on GNAPs for its lack of compliance with prior Commission orders. Subsequently, Global NAPs filed a Petition for Reconsideration of the Commission's March 2010 Order. In April 2010, the Commission granted the Petition subject to review on the merits. Final consideration of the matter will take place in Fiscal Year 2010-11.

In addition, Global NAPs filed with the FCC, a Petition for a Declaratory Ruling and for Preemption of the Pennsylvania, New Hampshire and Maryland State Commissions, filed March 5, 2010, to consider the effect of the FCC's 2004 Vonage ruling on the viability of imposing intrastate carrier access tariffs on long-distance VoIP traffic, and to determine whether to preempt the Commission's actions. The Commission, along with many other parties has filed comments and reply comments with the FCC. That case is still pending before the FCC.

The Commission's Law Bureau Prosecutory Staff (LBPS) then filed a formal complaint with the Commission seeking revocation of GNAPS' Certificate of Public Convenience for failure to comply with a Commission Order. A provider must have a Certificate of Public Necessity to operate as a public utility in Pennsylvania. In this case, GNAPs failed to remit the Commission-determined compensation to Ironton Telephone Company for interconnection services.

In January 2011, GNAPs responded by filing a pleading in the Federal District Court in Boston seeking invalidation of the LBPS complaint. GNAPs claimed that because they were in federal receivership, the state commission lack authority to take further enforcement actions. The LBPS challenged that claim based on federal law which exempts from state action bans in receivership situations involving public safety or the public interest. The LBPS considers revocation of GNAPs' authority a matter of public safety and in the public interest. The federal court, after a several hour conference, did not act on the LBPS response but went on to require GNAPS' receiver to remit compensation into a fund to compensate Pennsylvania carriers. The obligation to submit compensation into a federal fund will continue until the court acts on a subsequent purchaser of GNAPS' assets. The receiver indicated a new purchaser would be shortly identified. The LBPS has been waiting on further action since that February 2011 hearing.



Paper Billing Fee

When the Commission reviewed the petition of Cordia Communications Corp. for designation as an ETC in FY 2009-10, staff noted that Cordia's current tariff contained a provision for a paper invoice charge of $1.25 for customers who prefer to receive a paper invoice monthly billing statement. Under Section 1509 of the Public Utility Code, the Commission determined that the transmittal of, or sending, monthly bills to customers appears to be a public utility's statutory obligation. The Commission's regulations also contemplate that a monthly bill be mailed to customers. In June 2010, the Commission concluded that an investigation should be initiated by Law Bureau and the Bureau of Fixed Utility Services to make a recommendation on whether the practice of charging a fee for a paper bill by certain facility-based and non-facility-based telecommunications carriers is consistent with the Public Utility Code, Commission billing regulations and other relevant authority. The Commission expects the investigation to be concluded in Fiscal Year 2011-12.

Verizon Competitive Tariff

On May 31, 2011, Verizon Pennsylvania Inc. and Verizon North LLC each filed revisions to their respective Informational Tariffs for Competitive Services stating their intent to withdraw these tariffs effective June 1, 2011. In the alternative, the Companies indicated that they would maintain price lists and product guides on the non-tariffed sections of the Verizon website.

By Commission order entered June 24, 2011, the Commission addressed these filings and consolidated them for the purpose of further Commission inquiry. Because the Companies' respective Chapter 30 amended regulation and network modernization plans each currently contain language that states that the Companies will maintain informational tariffs for their competitive services, the Commission deemed each filing in potential violation of the companies' respective Chapter 30 plans and suspended the filings for a period not to exceed six months.

The Order also noted that the Companies' proposed withdrawal of their informational tariffs raised several other regulatory policy considerations. The Commission directed the Companies to file suspension supplements to their proposed filings, and to restore their informational tariffs to full force and effect. At the same time, the Commission treated the filings as letter petitions seeking modification of their respective Chapter 30 plans and provided a period of time for comment and reply comment opportunities by interested parties on the issues raised by the Companies' filings. Finally, the Order directed the Law Bureau to evaluate these comments and to prepare a recommendation for Commission consideration within 100 days of the entry of the June 24 Order.

Verizon (PA and North) Tandem Transit Traffic Filing

On April 5, 2011, Verizon Pennsylvania Inc. and Verizon North LLC (collectively the Verizon Companies) each made separate filings in which they introduced new tariffs for services for other telephone companies, namely tandem transit service. Each tariff was filed to become effective May 5, 2011. On April 22, 2011, the Pennsylvania Telephone Association (PTA) filed formal complaints against each tariff on behalf of its member companies. In its complaint, the PTA claimed that tandem transit traffic service should be negotiated between the parties seeking and offering such service rather than being something that is the subject of a tariff filing.

By Commission Orders entered May 19, 2011, the Commission suspended the Verizon Companies' proposed tariffs by operation of law until Dec. 4, 2011, and launched an investigation into the lawfulness, justness, and reasonableness of the Verizon Companies' existing rates, rules and regulations. The Commission assigned these filings to the Office of Administrative Law Judge for alternative dispute resolution or for the prompt scheduling of hearings culminating in the issuance of a Recommended Decision. These filings are currently in mediation before the Commission.

Merger Proceedings Rulemaking

On June 17, 2010, the Independent Regulatory Review Commission approved final Commission rules governing the review and approval of applications submitted by telephone companies to the Commission asking for a Certificate of Public Convenience approving a transfer of control. Section 1102 of the Public Utility Code requires an application for any transfer of control, typically with a merger.

Section 1102 had no time limit on Commission review of an application for these changes of control. The new rules establish specific timelines for Commission review and approval. This should shorten Commission review and give industry the needed approvals.

The final rules require publication of an application in the Pennsylvania Bulletin and establish a 15-day protest period. There are filing requirements and prior consumer notice mandates aimed at reducing the filing of formal protests.

The final rules establish three periods for Commission review and approval. Pro Forma Review will apply to an application that does not change rates, terms or conditions of service, or is a transfer of control that is less than 20 percent. Those will be reviewed and approved by the Commission through a staff-issued Secretarial Letter within 30 days after the protest period.

Abbreviated Review will apply to applications that change rates, terms or conditions of service, or is a transfer of control greater than 20 percent. Those will be considered by the Commission within 60 days after expiration of the protest period.

Finally, the rules conduct an unlimited administrative proceeding only when a party files a formal protest or the Commission determines that an unlimited Commission proceeding is necessary. This occurs if there are novel issues or a longer proceeding is required by the public interest.

Call Recording Rulemaking

Commission regulations prohibit a jurisdictional telecommunications utility from recording calls between its employees and customers. Several local exchange carriers received waivers of this regulation to allow recording of such calls for quality of service and training purposes. Rather than continue to address this issue in a case-by-case basis, on July 23, 2009, the Commission approved guidelines for utilities wishing to record calls with customers.

The Commission then initiated a rulemaking to replace the guidelines with regulations. Under the proposed terms of the rulemaking, a utility seeking to record calls would have to provide notice to the Commission, as well as provide its customers with a bill insert explaining the call recording process at least 30 days before the utility begins recording calls. Customers calling the telecommunications company would be provided a pre-recorded message to the effect that the call may be monitored or recorded for training or quality control purposes. The recorded calls would have to be erased after a 90-day (or shorter) retention period. Comments and reply comments have been received and IRRC has provided its comments. Commission staff is currently drafting a final rulemaking order.

Verizon's Initiative to Eliminate Hard Copies of White Pages

In an effort to be more environmentally friendly, beginning January 2011, Verizon ceased delivering paper copies of its residential white page listings, but rather made them available online. Customers may request free paper copies of the residential white pages listings by contacting an 800 number or by making a request online.

MACRUC and NARUC Involvement

Commission staff serves as lead on the Telecommunications Staff Committee, which is part of the Middle Atlantic Conference of the Regulatory Utility Commissions (MACRUC). As part of our participation, we monitor FCC developments and develop joint MACRUC recommendations for adoption by the MACRUC states on matters of joint state concerns.

Currently, several issues of concern being discussed include the FCC's use of forbearance of federal regulations and preemption of state authority over intrastate telecommunications historically regulated by the states.

The Commission also is actively involved with the National Association of Regulatory Utility Commissioners (NARUC) to ensure that Pennsylvania and MACRUC regional concerns are considered in making decisions about what services should be supported at what funding level.

MACRUC and NARUC involvement give the Commission an opportunity to present Pennsylvania concerns on national issues, particularly the costs related to the Federal Universal Service Fund. Commissioner James H. Cawley currently leads the NARUC Joint Federal-State Board on Universal Service as the State Chair.

Water/Wastewater

The PUC regulates the rates and service of investor-owned water and wastewater companies, along with some municipal systems that serve customers outside their boundaries. Since viable water systems are essential to strong Pennsylvania communities, rates must be set to reflect prudently incurred costs of providing service.

The Commission regulates the rates and service of about 185 water and wastewater companies, including a number of municipal water and wastewater systems, and continues its oversight of the water affected by Marcellus Shale drilling and its supply. In Fiscal Year 2010-2011, the Commission acted on 22 water and wastewater rate increase requests. The Commission also processed 21 applications for certificates of public convenience, including requests for additional territory, abandonments and formation of new companies.

The Commission continues to make the Legislative approval of a collection system improvement charge (CSIC) for wastewater companies a top priority.

The Commission also continues to implement a water audit pilot program, which is intended to enhance the companies' tracking of levels of unaccounted-for water. It is designed to provide an effective, standardized structure by guiding the water utility to quantify apparent and real loss volumes in a systemized approach and assigning cost impacts to the losses. Additionally, the Commission has focused on emergency response planning by requiring that companies annually certify that their physical and cyber security, emergency response and business continuity plans are current through ongoing audits of these plans.   These plans are also subject to periodic on-site reviews.

Marcellus Shale

The Commission continues to monitor the concerns about the availability of water supplies required for Marcellus Shale gas development as well as questions about disposal of the water used in hydraulic fracturing and any produced formation brines.

Water availability for hydraulic fracturing and the disposal of wastewater will be important factors affecting the growth of the Marcellus Shale gas industry and are of concern because of their impact on local water resources. Without an economical and sustainable water resource solution, further development of the Marcellus Shale basin will be at risk.

Marcellus Shale formations have very low permeability compared with most conventional gas-producing rocks. Currently, there is a mix of vertical and horizontal wells drilled in the Marcellus Shale bedrock. There appears to be a growing consensus that the share of horizontal wells will increase in the years ahead. Each well drilling and development requires substantial amounts of water. At issue is where the required large volumes of water are obtained.

The large regulated water utility companies have the expertise and experience to assist in developing the best management practices for water conservation with the goal of keeping pace of drilling and production activities within the bounds of sustainable water use. Their involvement will be necessary so possible consequences of competing water use does not become a major issue in locations with already stressed water supplies, or under drought conditions.

The second water resource issue of concern is the safe disposal of the large quantities of wastewater recovered during well development. The current disposal practice is processing it though a commercial or municipal wastewater treatment facility. The reports of high salinity in Pennsylvanian streams and rivers have been linked to this disposal practice. As a result, the Department of Environmental Protection (DEP) requires its approval before a municipal wastewater treatment facility can accept hydro fracturing fluids and brines for treatment. In addition, the future amounts of salts and minerals in a treated discharge to Pennsylvania rivers and streams has to be reduced. The Commission, the industry and DEP are working to determine the best available options to deal with the Marcellus Shale liquids.

In March 2011, Gov. Tom Corbett announced the formation of a Marcellus Shale Advisory Commission. The purpose of the Commission, Corbett said, is “to oversee how we can build around this new industry and how we can make certain we do this while protecting our lands, our drinking water, our air – all the time growing our workforce.’’

The commission is to address the needs and impacts of natural gas development on local communities, as well as promote the efficient, environmentally sound and cost-effect development of Marcellus Shale and other natural gas resources. Chairman Robert F. Powelson represents the PUC on the Advisory Commission *(See Natural Gas).*

Rate Increase Requests

During the fiscal year, the Commission took the following actions related to about $21.5 million in rate increase requests:

Acorn Water Company, LLC

Customers Served: 21 customers in portions of Earl Township, Lancaster County
Requested Rate Increase: $6,500 (215.6 percent)
Approved Rate Increase: $7,413 (245.9 percent)
Primary Reason: To provide the necessary revenues to cover operating expenses

City of Lock Haven – Water Department

Customers Served: 1,063 customers in portions of Allison, Castanea and Wayne Townships, Clinton County
Requested Rate Increase: $491,423 (41.60 percent)
Approved Rate Increase: $375,000 (31.75 percent)
Primary Reason: To provide for rates more closely related to the cost of providing services

Corner Water Supply & Service Corp.

Customers Served: 600 customers in portions of Paint and Elk townships, Clarion County
Requested Rate Increase: $42,771 (13.24 percent)
Approved Rate Increase: $17,347 (5.37 percent)
Primary Reason: To obtain a fair and reasonable rate of return on the shareholders' investment

Deer Haven Sewer Co.

Customers Served: 46 customers in portions of Palmyra Township, Pike County
Requested Rate Increase: $40,314 (373.3 percent)
Approved Rate Increase: $25,715 (133 percent)
Primary Reason: To provide additional funds for the company to pay its day to day operational expenses

Elverson Water Co. Inc.

Customers Served: 496 customers in Borough of Elverson and portions of West Nantmeal, East Nantmeal and Warwick townships, Chester County
Requested Rate Increase: $15,644 (11.6 percent)
Approved Rate Increase: $15,644 (11.6 percent)
Primary Reason: To recover the increase in the cost of operations

Kensington Water Co.

Customers Served: 62 customers in portions of Hamilton and Letterkenny townships, Franklin County
Requested Rate Increase: $11,303 (75 percent)
Approved Rate Increase: $11,303 (75 percent)
Primary Reason: To improve security and reliability and to improve water quality

Little Washington Wastewater Co. – Masthope Division

Customers Served: 1,211 customers in portions of Delaware, Bucks, Chester, Luzerne and Carbon counties
Requested Rate Increase: $181,426 (45.9 percent)
Approved Rate Increase: $115,000 (32.7 percent)
Primary Reason: To allow the company to continue to meet the needs of its customers, comply with state and federal environmental requirements and to earn a reasonable return on its investment

Little Washington Wastewater Co. – Southeast Consolidated Division

Customers Served: 4,349 customers in portions of Delaware, Bucks, Chester, Luzerne and Carbon counties
Requested Rate Increase: $1,079,436 (32.2 percent)
Approved Rate Increase: $999,000 (29.9 percent)
Primary Reason: To allow the company to continue to meet the needs of its customers, comply with state and federal environmental requirements and to earn a reasonable return on its investment

Manwalamink Sewer Co.

Customers Served: 1,238 customers in portions of the village of Shawnee-On-Delaware and portions of Smithfield and Middle Smithfield townships, Monroe County
Requested Rate Increase: $73,381 (14.7 percent)
Approved Rate Increase: $73,381 (14.7 percent)
Primary Reason: To cover lost revenue and a significant increase in operating expenses and to allow a normal rate of return on the utility's equity value of its plant

Manwalamink Water Co.

Customers Served: 1,238 customers in portions of the village of Shawnee-On-Delaware and portions of Smithfield and Middle Smithfield townships, Monroe County
Requested Rate Increase: $65,128 (19.92 percent)
Approved Rate Increase: $65,128 (19.92 percent)
Primary Reason: To cover lost revenue and a significant increase in operating expenses and to allow a normal rate of return on the utility's equity value of its plant

Pennsylvania Utility Co. Inc. (Wastewater)

Customers Served: 560 customers in portions of Lehman Township, Pike County
Requested Rate Increase: $369,827 (232.8 percent)
Approved Rate Increase: $275,000 (173.1 percent)
Primary Reason: To realize a reasonable rate of return on the company's fixed capital investment and to recover increased operating expenses

Pennsylvania Utility Co. Inc. (Water)

Customers Served: 561 customers in portions of Lehman Township, Pike County
Requested Rate Increase: $112,309 (69.4 percent)
Approved Rate Increase: $70,000 (43.3 percent)
Primary Reason: To realize a reasonable rate of return on the company's fixed capital investment and to recover increased operating expenses

Pennsylvania American Water Co. – City of Coatesville Division (Wastewater)

Customers Served: 6,035 customers in the City of Coatesville and certain municipalities and territories located in Chester County
Requested Rate Increase: $8,156,652 (197.3 percent)
Approved Rate Increase: $5,999,000 (145.16 percent)
Primary Reason: To recover the approximately $57.7 million that the company invested to improve wastewater service and reliability since the last rate case in 2008

Pennsylvania American Water Co. – Clarion Wastewater Operations

Customers Served: 2,215 customers in the Borough of Clarion and portions of Clarion and Monroe townships, Clarion County
Requested Rate Increase: $968,817 (83.61 percent)
Approved Rate Increase: $600,000 (51.78 percent)
Primary Reason: To recover additional investment

Pennsylvania American Water Co. – Claysville Wastewater Operations

Customers Served: 500 customers in the Borough of Claysville and portions of Donegal Township, Washington County
Requested Rate Increase: $487,486 (157.73 percent)
Approved Rate Increase: $360,000 (116.52 percent)
Primary Reason: To recover additional investment

Pennsylvania American Water Co. – Northeast Wastewater Operations

Customers Served: 3,911 customers in portions of Lehman Township, Pike County; and Smithfield, Middle Smithfield and Stroud townships, Monroe County
Requested Rate Increase: $2.09 million (240 percent)
Approved Rate Increase: $1.475 million (168.89 percent)
*Primary Reason:*To recover acquisition and capital improvements

Reynolds Disposal Co. (Wastewater)

Customers Served: 681 customers in Greenville and portions of Pymatuning, Delaware and Hempfield townships, Mercer County
Requested Rate Increase: $77,167 (20.5 percent)
Approved Rate Increase: $49,500 (13.2 percent)
Primary Reason: To realize a reasonable rate of return on the company's fixed capital investment and to recover increased operating expenses

Superior Water Co. Inc.

Customers Served: 3,626 customers in
Berks, Chester and Montgomery counties
Requested Rate Increase: $404,190 (18.81 percent)
Approved Rate Increase: $404,190 (18.81 percent)
Primary Reason: To restore the company's rate of return and net operating income to a more reasonable level to recover a return on and a return of the company's increase of investments

The York Water Co.

Customers Served: 62,714 customers in several
boroughs and townships in York and Adams counties
Requested Rate Increase: $6.2 million (15.9 percent)
Approved Rate Increase: $3.4 million (9 percent)
Primary Reason: To provide sufficient revenues to recover the cost to maintain its facilities properly, to afford the opportunity to more nearly approach a fair and reasonable rate of return on the original costs

Total Environmental Solutions Inc. – Treasure Lake Wastewater Division

Customers Served: 5,601 customers in
portions of Sandy Township, Clearfield County
Requested Rate Increase: $268,140 (25.6 percent)
Approved Rate Increase: $105,059 (10 percent)
Primary Reason: To realize a reasonable rate of return on the company's fixed capital investment and to recover increased operating expenses

Total Environmental Solutions Inc. – Treasure Lake Water Division

Customers Served: 5,561 customers in
portions of Sandy Township, Clearfield County
Requested Rate Increase: $376,120 (62.15 percent)
Approved Rate Increase: $244,917 (40.5 percent)
Primary Reason: To realize a reasonable rate of return on the company's fixed capital investment and to recover increased operating expenses

Wonderview Water Co.

Customers Served: 152 customers in portions of
Main and Catawissa townships, Columbia County
Requested Rate Increase: $21,025 (32.5 percent)
Approved Rate Increase: $21,025 (32.5 percent)
*Primary Reason:*To move the company toward a profitable position.

At the end of Fiscal Year 2010-2011, 11 rate increase requests for $85.3 million were still pending before the Commission including: City of Lancaster – Bureau of Water ($8.6 million); Tri-Valley Water Supply Inc. ($54,430); CMV Sewage Co. Inc. ($270,532); The Newtown Artesian Water Co. ($999,839); Pennsylvania American Water Co. ($70,676,379); United Water Pennsylvania Inc. ($2,832,179); Twin Lakes Utilities Inc. ($124,420); Corner Water Supply & Service Corp. ($38,719); CAN DO Inc. (wastewater) ($437,564); CAN DO Inc. (water) ($266,344); and City of Bethlehem – Bureau of Water ($996,710).

Distribution System Improvement Charge

The distribution system improvement charge (DSIC), currently utilized by six jurisdictional water utilities, is designed to provide consumers with improved water quality; greater rate stability; increased water pressure; fewer main breaks; fewer service interruptions; and lower levels of unaccounted-for water.

Implemented in 1997, the DSIC enables companies to recover certain infrastructure improvement costs between base rate cases through a surcharge on customers' bills. The cost is small when compared to the noticeable benefits, with approximate average monthly costs to consumers ranging from a few cents a month to $2.75. Today, because of the DSIC, projected timeframes for upgrades of entire distribution systems range from 117 years to 160 years to more closely match that of actual service lives. During the fiscal year, the Commission reviewed and processed 24 quarterly DSIC surcharge adjustment filings. Because of the success of the DSIC, one of the Commission's legislative priorities is to have a collection system improvement charge (CSIC) put into place for the wastewater companies.

PAWC Chloramine Settlement

On June 29, 2010, the Commonwealth Court issued a decision affirming the Commission's Order approving a settlement that allowed the use of chloramines in the Pennsylvania American Water Co. (PAWC) West Shore Regional Treatment Plant, York County, and the Silver Spring Water Treatment Plan, Cumberland County. The company began using chloramines in July 2010.

On May 14, 2009, the Commission approved a settlement between the company and the state's Office of Consumer Advocate (OCA). The Commission found that the settlement was in the public interest, because the company will take actions that address the concerns raised by the customers in a complaint proceeding.

In September 2007, several complaints were filed against PAWC by customers in response to the company's announcement that it intended to convert the facilities from chlorinated water to chloraminated water. The Pennsylvania Department of Environmental Protection (DEP) had issued permits to PAWC that approved the plan.

Water and Wastewater Plant Inspections

The Commission has conducted 24 plant inspections through Fiscal Year 2010-11. Random inspections are conducted at various times, usually to inspect companies that have not had any recent inspections. If violations are found, the company is directed to correct the problem. If the problem is not corrected, Commission staff conducts an informal investigation. The 24 inspections conducted this fiscal year included 22 random and two plant tours by Commission staff. 19 of the random inspections were completed in connection with Emergency Preparedness Audit inspections.

Water Audit Pilot Program

In December 2008, a water audit pilot program was implemented to enhance the companies' tracking of levels of unaccounted-for water, which is water that is lost between the treatment plant and sale to customers. The water audit was designed to provide an effective, standardized structure by guiding the water utility to quantify apparent and real loss volumes in a systemized approach and assigning cost impacts to the losses. The voluntary pilot program provides further ways to assess overall infrastructure reliability, help preserve water resources, limit water leakage and enhance customer service. The initial meeting was in February 2009 followed by a workshop in early Fiscal Year 2009-10, where presentations were provided by two individuals who have familiarity with the water audit software. A concluding order on the program is expected in Fiscal Year 2011-2012.

Mergers & Acquisitions

In reviewing mergers and acquisitions, the Commission works to make certain that customers are protected, and the company is a viable public utility and a good neighbor. The PUC gives each application a thorough and comprehensive review. In Pennsylvania, the legal standard asks whether an affirmative public benefit will result from the merger or acquisition. Public benefit is defined typically as protecting the public interest, encouraging economic development and safeguarding the environment.

During Fiscal Year 2010-11, the Commission did not approve any mergers in the water industry.

Policy Statement on Acquisition Incentives

The PUC continues to implement a longstanding policy on water and wastewater system acquisition incentives to promote water system viability and regionalization.

The policy statement provides additional guidance for companies acquiring small, chronically challenged or otherwise troubled water systems, while ensuring fair treatment of customers. It also provides direction on when and how utilities interested in making an acquisition should prepare and submit original cost documentation that determines the appropriate value of the assets of an acquired system.

The Commission has a policy of encouraging well-operated water and wastewater utilities to regionalize or consolidate with smaller systems. The limited resources — managerial, financial or technical — of these smaller systems can result in less than reliable service for consumers.

The policy statement supports the Commission's regionalization efforts, which in recent years have allowed consumers of the smaller, troubled systems to experience improved service after being acquired by a larger, more viable water or wastewater system.

Management Audits and Efficiency Investigations

The Commission periodically performs management and operations audits (MAs) or management efficiency investigations (MEIs) of the larger jurisdictional water companies. Among the MAs and MEIs completed within the 2010-11 fiscal year were:

Newtown Artesian Water Co.

On Nov. 19, 2010, the PUC released a Management and Operations Audit of Newtown Artesian Water Co. The Focused Management and Operations Audit analyzed and evaluated management performance in five areas; none of which were rated as needing major or significant improvement. The audit made 10 recommendations to the company for improvement, none of which were significant. The company indicated acceptance of all 10 recommendations in its implementation plan.

The audit recommendations included:

- Developing and maintaining a damage prevention program to include a damage statistic database and a pipeline awareness program for the Company's stakeholders;
- Issuing periodic reminder notices to commercial/industrial customers that are non-compliant with installing backflow prevention devices and implement measures to enforce installation of such devices for high risk customers and update the list of licensed testers sent to customers on an annual basis;
- Developing a central file to maintain annual main break and leak information and use this data to update the distribution maps in order to help make informed main replacement decisions;
- Developing and maintaining a Cyber Security Plan in accordance with Chapter 101 of 52 Pa. Code and test and update it on an annual basis;
- Examining opportunities including the associated costs and benefits of reducing the billing lag to a more reasonable level;
- Maintaining board of director fees at the current level until they more closely reflect the fees of similar size utilities; and
- Addressing all the external audit firm's management letter recommendations in a timely manner.

United Water Co.

On Jan. 13, 2011, the Commission released a report on the Focused Management and Operations Audit of United Water Pennsylvania, Inc. that contained recommendations that could save the company $315,500 annually and provide a one-time savings of $57,000. The Focused Management and Operations Audit analyzed and evaluated management performance in 10 functional areas.

The audit makes 17 recommendations to the company for improvement. The Company indicated acceptance of 16 recommendations in its Implementation Plan and rejection of one.

The accepted audit recommendations included:

- Correct the inventory turnover calculation and strive to achieve an inventory turnover of at least 2.0;
- Establish emergency stock and eliminate obsolete material;
- Enhance automation of the materials management system, document procedures, and strive to eliminate parts of the current process that may cause errors;
- Improve inventory accuracy and implement a cycle counting procedure;
- Accelerate the main replacement program to achieve long range main replacement rates of approximately 100 to 120 years;
- Develop a more proactive main replacement program; and
- Strive to reduce Unaccounted for Water (UFW) to or below Commission guidelines of 20 percent.

York Water Co.

On June 30, 2011, the Commission released a Management Efficiency Investigation (MEI) that examined York Water's progress in implementing 8 of the original 13 recommendations from a Focused Management and Operations Audit report released in October 2008. By implementing the recommendations contained in the October 2008 report, York Water is realizing annual savings of $26,000 and has realized a one-time saving of $174,000. The MEI found that the Company has effectively implemented all eight of the prior recommendations reviewed, making changes that include:

- Reducing its inventory and increasing its inventory turnover rates;
- Accelerating its main replacement rate from 232 years in 2008 to 143 years in 2010;
- Updating its emergency response plan;
- Educating its employees on proper treatment of confidential customer information; and
- Revising its vehicle replacement guidelines.

The Commission's Bureau of Audits staff further recommended that York Water should strive to achieve the Company's goal of attaining a main replacement rate and rehabilitation interval not to exceed 120 years. This follow-up recommendation was accepted in York Water's Implementation Plan, which included plans to achieve the goal starting in 2011.

Pennsylvania American Water Co.

On June 30, 2011, the Commission released a Management Efficiency Investigation (MEI) that contained recommendations that could save Pennsylvania-American Water Co. (PAWC) up to $2.6 million and $650,000 in one-time savings by implementing the recommendations contained in the report. These savings are in addition to the $223,500 to $323,500 annual savings and $67,000 in one-time savings already realized by implementing recommendations from a Stratified Management and Operations Audit report released in November 2008.

The MEI examined PAWC's progress in implementing 81 of the 114 original recommendations from the November 2008 audit report, finding that PAWC has effectively implemented 49 of the 81 prior recommendations and taken some action on 31 of the remaining 32 recommendations. Some of the changes made by the company include:

- Enhancing the Company's software to enable electronic deployment of software updates to remote workstations;
- Performing a server consolidation study and developing a long-range Information Technology (IT) plan, which is reviewed and updated annually;
- Updating its Information Technology disaster recovery plans and testing the plans on a regular basis;
- Implementing new financial monitoring processes to initiate actions to achieve improved profitability and financial health;
- Significantly reducing the number of billing over estimates;
- Allocating infrastructure improvement resources on a statewide basis rather than on a district by district basis;
- Reducing unplanned production overtime by approximately 11 percent;
- Improving the call centers' core infrastructure and introducing website self service capabilities and electronic billing; and
- Finalizing a supplier diversity program and significantly increasing diversity participation and contract awards.

In addition, the Audits staff made 47 follow-up recommendations for further improvement. The company indicated acceptance of 43 of recommendations, partial acceptance of three and rejection of one. The accepted or partially accepted recommendations include:

- Implement the procurement/materials management application of the new software system across the PAWC organization in a timely manner which should allow it to reduce its inventory on a one time basis by up to $650,000 with associated annual savings of up to $162,500;

- Conduct an internal audit of the smaller inventory locations to determine the accuracy of the inventory data and develop comprehensive materials management policies and procedures;

- Accurately report Unaccounted for Water (UFW) levels to the Commission and implement long term initiatives designed to achieve actual UFW levels of no more than 20 percent which could result in annual production cost savings of up to $2.1 million;

- File an updated affiliated interest agreement with the PUC for review and approval; and

- Create a comprehensive damage prevention manual and establish goals to strengthen the damage prevention program.

Statewide Water Resources

The PUC participates in the Statewide Water Resources Committee charged with carrying out Act 220 of 2002. This law requires the development of a statewide plan to manage the Commonwealth's water resources more effectively. Act 220 calls for the 25-year-old state Water Plan to be updated within five years, with regular updates every five years thereafter. The updated plan, issued in March 2009, addresses the quantity of water available in the Commonwealth, the amount used, and the amount needed.

Auditing Emergency Response Planning

The Commission requires that companies certify that their physical and cyber security, emergency response and business continuity plans are current. During Fiscal Year 2005-06, the PUC found deficiencies in several of the certified plans that had to be corrected to comply with Commission requirements. In some cases, the plans were outdated, and phone numbers for Commission contacts were obsolete. In March 2006, the Commission initiated an audit program to ensure that all water utilities' emergency response plans are current and in compliance with all applicable laws and regulations, including cyber and physical security along with business continuity. During Fiscal Year 2010-2011, emergency response plans were audited for 11 of the small water utilities, as well as six of the larger utilities during the course of routine management audits and management efficiency investigations.

Water and Wastewater System Viability

Pennsylvania has more than 2,200 community drinking water systems, many of which are small water systems serving less than 3,300 consumers. The PUC regulates the rates and service of about 185 water and wastewater companies. Many were built decades ago, and a number now face operational, technical and financial challenges that could affect customer service.

Many small water and wastewater systems have varying degrees of operational constraints that impact their viability. Operational constraints inherent to small systems typically include: compliance problems; limited technical and managerial expertise; lack of capital for improvements with a limited ability to borrow at reasonable rates; deferred maintenance; deteriorated and undersized infrastructure; and minimal sources of supply or storage.

A viable water/wastewater system is one that is self-sustaining, and has the financial, managerial and technical capabilities to reliably meet both PUC and DEP requirements on a long-term basis. The most recent Legislative Budget and Finance Committee (LB&FC) performance audit recognized the Commission's work in this area, highlighting efforts to encourage the commitments to enhancing water system viability to ensure that consumers of small water/wastewater systems receive the same quality of service provided by larger, viable water/wastewater companies.

Regionalization

Many of the water/wastewater mergers and acquisition applications that the Commission acts on are a form of regionalization. In general, regionalization is the consideration of water resources in terms beyond artificial boundaries (townships, boroughs, city limits, municipalities, service territories, etc.). Some water/wastewater systems in Pennsylvania lack the management and funding to stand alone as viable systems. Regionalization typically results in a cost-effective solution or alternative that works to ensure system reliability and water/wastewater standards.

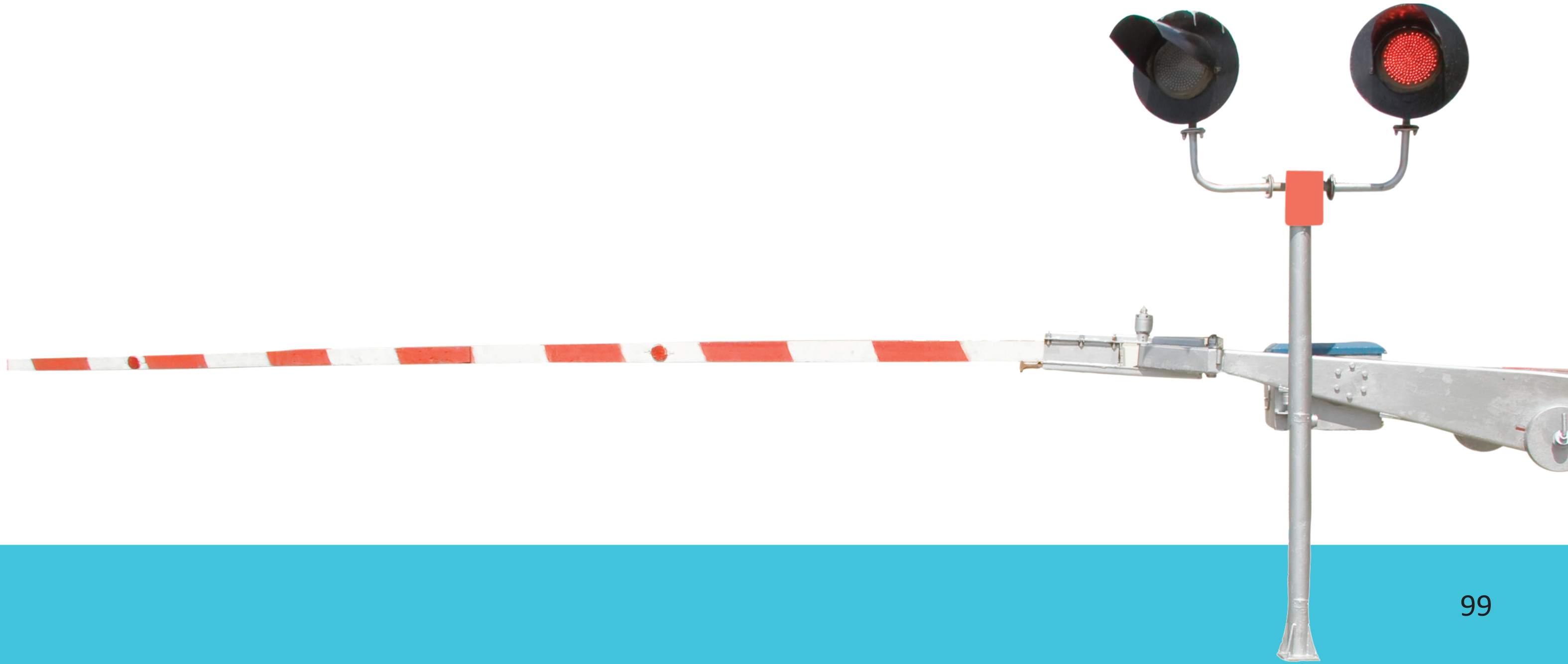
The benefits of regionalization include increased economies of scale and service efficiencies, improved operations, management, and technology. Approaches to regionalization can include mergers, acquisitions, physical interconnections, satellite management agreements and cooperative purchasing/operational pools. Regionalization is not limited to large jurisdictional companies buying or taking over smaller companies. In some cases, nearby non-jurisdictional water companies, such as municipalities or authorities, also have participated in regionalization efforts.

Transportation & Safety

Ensuring the provision of safe rail and motor carrier service, the PUC also handles rates of transportation companies. The PUC resolves complaints about unsafe conditions at rail crossings and enforces common carrier compliance with safety and insurance requirements.

During Fiscal Year 2010-11, the Commission continued to focus on passenger carrier safety compliance. As part of its enhanced oversight of the motorcoach industry, the PUC performed inspections of motor coaches at various destinations across Pennsylvania, conducted inspections of busses at motor coach carrier home offices, and completed post-accident motor coach inspections. During the year, the Commission conducted about 16,913 enforcement activities.

The Commission also processed applications to approve the construction, alteration and abolition of more than 138 rail-highway crossing cases. It completed informal investigations of complaints about unsatisfactory crossing surface conditions, as well as unsafe crossings. The PUC also conducted inspections of locomotives, rail cars, tracks and rail operations. Additionally, the Commission approved a proposed rulemaking order that takes into consideration the technological and operational changes of the rail industry over the last thirty years and reflects current Federal standards.



Marcellus Shale Enforcement

The PUC has increased its motor carrier enforcement presence in the areas of the commonwealth that are connected to the Marcellus Shale geologic formation.

The increase in motor carrier enforcement is a result of several complaints received by the Commission involving carriers transporting commodities without a PUC certificate, and some trucks are being operated in an unsafe manner. Increased inspections are taking place in many northern tier counties and southwestern counties of the State to ensure the motor carriers are complying with PUC regulations. The PUC has also been participating in joint inspection efforts with the PA State Police.

Trucking companies are required to have a certificate of public convenience for property carrier authority and proof of insurance if they are involved with transporting commodities related to the drilling operations, such as water, sand and stone. Carriers operating without the certificate and insurance can be subject to Commission penalties. Also, carriers violating the safety regulations that pertain to the drivers and equipment can be cited and the driver and equipment may be placed out of service.

The Commission completed 262 Marcellus Shale inspections during special inspection efforts with the PA State Police. As a result, 59 vehicles were placed out of service – most due to brake deficiencies and unsafe loading. Twelve drivers were placed out of service due to driver license problems, log book violations, and exceeding the hours of service limitations.

Annual Assessment Report Review of Motor Carriers

The Commission conducted a review of selected motor carrier Annual Assessment Reports. The Annual Assessment Report requires public utilities to submit operating revenues, including "total gross operating revenues" and "gross intrastate revenues" utilized to determine each public utility's appropriate annual assessment.

The review of assessable revenues within this industry includes verification of "excludable" revenues requiring an on-site visit. The PUC visited six motor carriers selected for 2009 revenue review and issued its report for each of the companies. The PUC will continue to conduct reviews of selected motor carrier Annual Assessment Reports.

The future reviews of selected motor carriers may result in adjustments to assessable revenues and/or recommendations for improved record keeping and reporting. In addition, the future reviews may provide the Commission the necessary information to determine what, if any, subsequent steps may be required to move toward consistency in claimed exemptions within each segment of the motor carrier industry. As of April 1, 2011, and part of the Commission's overall reorganization plan, all motor carrier filings are now made with the Secretary of the Commission.

Motor Coach Safety Program

The Commission has implemented an oversight plan to monitor the safety compliance of Pennsylvania's motor coach operators to ensure the public's protection.

The plan is a four-step approach to oversee the safety of bus companies operating in the state. First, all new bus carriers must satisfactorily complete a Safety Fitness Review (SFR) within the first 180 days of operation. The SFR is an evaluation of the bus company to determine if the carrier has implemented procedures and other controls to ensure compliance with the PUC's safety regulations. Annual fleet inspections are conducted on all new entrant motor coach carriers and a portion of existing bus companies that hold intrastate operating authority. Carriers with a previous history of safety violations also are subject to the fleet inspections. The Commission also conducts driver/vehicle inspections at various sites across the state where there is a high volume of busses transporting passengers, such as at amusement parks and other tourist locations.

The Commission is an active partner with the Federal Motor Carrier Safety Administration's (FMCSA) bus safety efforts through participation in the Motor Carrier Safety Assistance Program (MCSAP). The federal Compliance Reviews (CRs) entail a thorough audit of the carrier's safety records and safety management systems to identify violations. A safety rating based on the findings is one result of the CR, and the carrier may be subject to civil prosecution by the FMCSA and the PUC. In addition, the PUC works with the FMCSA to investigate carriers lacking valid operating authority to operate in interstate commerce. These bus carriers may be utilizing unqualified drivers and vehicles with safety deficiencies while transporting people to and from points in Pennsylvania.

As part of its participation in the MCSAP, the FMCSA asked Pennsylvania to enhance its oversight of the motor coach industry, following a number of significant crashes that resulted in injuries and fatalities across the state. In 2010, PUC officers conducted 1,349 bus inspections, 415 at terminals and 934 at destination inspection sites. As a result of these inspections, 61 buses were placed out of service and 29 drivers were placed out of service.

Also, as part of an agreement with the Pennsylvania State Police, the Commission's enforcement officers perform post-crash inspections of motor coach vehicles that were involved in serious accidents, i.e., those involving fatalities and, in some instances, injuries. The enforcement officers use specially equipped trailers that contain ramps and other equipment to thoroughly examine buses that were likely disabled during a crash.

Unified Carrier Registration (UCR)

The federal Unified Carrier Registration System Plan and Agreement (UCR Act) became effective Jan. 1, 2007. In accordance with the UCR Act, motor carriers that operate commercial motor vehicles in interstate commerce must pay a fee based upon the size of the carrier's fleet. For 2010, the fee structure included six brackets, ranging from \$76 to \$73,346. In addition, individuals and companies that provide freight forwarding, brokering or leasing services in interstate commerce must register their business and pay an annual fee of \$76. Motor carriers and the other businesses must register and pay the fee to the state in which they are headquartered.

The PUC has participated in the UCR program from 2008 through 2011. Thus far, the PUC has collected the following monies in the respective years: \$4.3 million for 2008, \$4.4 million for 2009, and \$4.95 million in 2010 and 2011. Although the registration and fee payment deadlines have expired for the 2009, 2010, and 2011 years, the PUC continues to pursue and collect delinquent fees.

Regulated Motor Carriers

- 5,932 properties
- 347 taxis
- 399 limousines
- 474 paratransit
- 67 airport transfer
- 499 group and party
- 54 scheduled route
- 287 household goods movers

2010-11 Enforcement Activities

- 8,143 truck, bus, small passenger vehicle inspections
- 361 informal complaint investigations
- 870 safety fitness reviews
- 811 federal safety audits

National Rail Plan

The Consolidated Appropriations Act of 2010 directed the Federal Railroad Administration (FRA) to establish strategic goals and deliver to Congress the first ever long range National Rail Plan (NRP) in the fall of 2010. When completed, the first-ever National Rail Plan will establish the framework necessary to begin laying a foundation that will improve our transportation network for future generations. The necessary improvements in passenger and freight mobility will lead to economic, environmental, and societal benefits for all Americans.

Rail transportation is one of the safest and most fuel-efficient transportation modes, but the National Rail Plan must allow rail transportation to be complimentary of the entire transportation system. Rail passengers and freight often travel between locations on the same corridors.
Many regions have pursued commuter rail as a low-cost way to improve transportation capacity, from suburban to central business districts using existing railroad corridors. The primary issue facing all three systems (intercity, commuter, and freight) is that limited capacity in existing corridors makes maintaining both reliability and safety a challenge. A high-performance freight system will require modernized corridors that have the capacity to allow both passenger and freight trains to operate without interfering with each other.

In the United States today, two distinctly different rail systems exist: freight railroads and passenger railroads. Freight railroads are privately owned and operated; they are in business to make a profit for their investors. Passenger railroads are publicly subsidized by taxpayers; they provide a public service by offering a safe and environmentally friendly travel option. These two different types of rail transportation usually occur in the same corridor and on the same infrastructure.

Our nation’s intercity passenger rail service is provided by the National Railroad Passenger Corporation (Amtrak), which was created in 1971 to relieve the freight railroads from their common carriage obligation to provide passenger service. The current passenger services, which serve as an important component of a national transportation system, must be improved and intermodal connections enhanced. To better develop high-speed rail service, whether operated by Amtrak or another entity, the Recovery Act, signed into law by President Obama on Feb. 17, 2009, contains funding and sets forth requirements for the development of high-speed intercity rail. The Recovery Act designated $8 billion specifically for the development of high-speed intercity rail transportation.

There are many challenges when operating a slow freight train and a fast passenger train on the same track and rail network. The FRA and the PUC are dedicated to providing the safest mode of transportation. There are several new safety requirements proposed and enacted to enforce and ensure compliance. New technologies will also enhance railroad safety such as positive train control to prevent collisions of two trains on the same track and electronically controlled pneumatic brakes which provide quicker stopping distance. Both of these safety improvements will be utilized on Pennsylvania's rail lines.

Smaller railroads also play a critical role in providing transportation services. These generally lower-cost railroads preserve transportation options for local shippers, and thus play an important part in the national transportation system by providing the link to connect local shippers with the larger, Class 1 carriers for efficient, long-haul service. Pennsylvania has more short-line railroads than any other state.

It is expected that the National Rail Plan will not only provide the framework for rail transportation improvements for the nation, but also important economic and social enhancements for the Commonwealth of Pennsylvania.

Rail Excursions in Pennsylvania

Pennsylvania is a very diverse state with cities, farm land, mountains and valleys, and most areas are accessible by railroads. These railroads were carved into the landscape as a means of commerce and travel. Thanks to many entrepreneurs, rail enthusiasts and government agencies, these rail lines provide freight service as well as passenger excursions.

The opportunity to ride these rail lines is located in many areas of the Commonwealth. There are more than 20 tourist rail lines that will take you back in history and provide a seldom seen look of the scenic landscapes of Pennsylvania. The excursions are family oriented and provide several options to explore. Many like to ride for the historic value, entertainment, and scenery. Another option for railroad enthusiasts is the State Railroad Museum in Strasburg, Steamtown in Scranton and attractions around Altoona such as the Horseshoe Curve museum.

The railroad, equipment and operational procedures are inspected by the PUC Rail Safety Division. They must comply with state and federal safety regulations. A few of the rail excursions include:

Stourbridge Line Rail Excursions located in Honesdale. This is the birthplace of the American railroad. On Aug. 8, 1829, the Delaware & Hudson operated the first commercial locomotive in the western hemisphere.

Strasburg Rail Road located in Strasburg. This steam operated railroad provides a ride through the farm lands of Lancaster County. There are gift shops, restaurants, entertainment and occasionally a visit from Thomas the Tank Engine.

Jim Thorpe Rail Tours located in Jim Thorpe. This excursion will take you from Jim Thorpe to Nesquehoning, Lake Hauto and Hometown trestle. You will ride in vintage 1920-30's era, fully enclosed passenger cars through the woodlands of Northern Pennsylvania.

Reading Blue Mountain & Northern Railroad located in Port Clinton. This rail line travels through the Lehigh Gorge and the anthracite coal region.

Middletown & Hummelstown Railroad located in Middletown. This rail excursion specializes in dinner trains, Santa Claus and Easter Bunny specials and rides to Indian Echo Caverns.

The Roadbed to Eliminating Human Factor Incidents in the Railroad Industry

The roadbed of a railroad track structure is the solid foundation on which the trains distribute their weight and provide a safe passage for train traffic. Railroad maintenance crews work daily to preserve the roadbed and track structure, but minimizing "human factor" incidents is just as important as a sound physical roadbed to provide a safe and efficient railroad system. The human factor causes a large percentage of railroad accidents, and the elimination of human factor incidents is a common priority shared between the Federal Railroad Administration (FRA), the PUC, and railroad industry.

Since rail accidents are most likely to occur in rail yards where there are many tracks, switches, and train movements, a voluntary, non-regulatory workplace safety partnership was created to develop safe practices that reduce fatalities and injuries in rail yard switching operations. This partnership, Switching Operations Fatalities Analysis (SOFA), is recognized and accepted throughout the country. SOFA identifies five "Lifesavers" – secure equipment before action is taken, protect employees against moving equipment, discuss safety at the beginning of a job or when a project changes, communicate before action is taken, and mentor less experienced employees.

PUC rail safety inspectors stringently enforce a wide array of regulations and safety procedures that specifically target operating practices involving train movements. For instance, regulations presently prohibit the use of electronic devices by transportation employees involved in train movements. These regulations eliminate potential distractions. Another regulation has also been proposed that would require certain railroads to develop Risk Reduction Plans. These plans will identify and analyze operational hazards and develop methods to mitigate those risks.

The development of new regulations and adherence with SOFA recommendations combined with labor and industry commitments will create a safety culture with increased communications and decreased rail accidents. With a dedication to safety, the FRA and PUC Rail Safety Inspectors work to enforce compliance with regulations and safety rules. This collective effort will provide a strong roadbed for reducing human factor incidents in the rail industry.

Operation Lifesaver

OPERATION LIFESAVER®
Pennsylvania

Operation Lifesaver is a nonprofit, national public education program dedicated to eliminating collisions, deaths and injuries at rail-highway crossings and on railroad rights-of-way. Operation Lifesaver strives to increase public awareness about the danger for motor vehicle operators and pedestrians at rail-highway intersections.

The program seeks to improve driver and pedestrian behavior by encouraging compliance with traffic laws relating to crossing signs and signals. It also points out the dangers on railroad rights-of-way. Designated PUC employees are certified to provide Operation Lifesaver presentations to various groups, such as school children, businesses and civic organizations. The Rail Safety Division's four trained presenters also provide information concerning railroad safety at outreach events. The Rail Safety Division has the expertise with regard to engineering at highway-rail crossings, and participation in the program complements the division's goals for the prevention of accidents and the promotion of public safety. Visit Pennsylvania's Operation Lifesaver's web site at www.paoperationlifesaver.org

2010-11 Inspections

- 23,150 railroad car
- 441 locomotive
- 3,089 miles of railroad track
- 2,424 Hazardous Materials Units

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