BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Petition of UGI Utilities, Inc. – Electric Division for Approval of its Energy Efficiency and Conservation Plan	: : :	Docket No. M-2010-2210316

EXCEPTIONS OF UGI UTILITIES, INC. – ELECTRIC DIVISION TO RECOMMENDED DECISION OF ADMINISTRATIVE LAW JUDGE SUSAN D. COLWELL DATED JULY 15, 2011

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GLOSSARY OF TERMS

Act 129	Act 129 of 2008, P.L. 1592, 66 Pa.C.S. §§ 2806.1 and 2806.2.
ALJ	Administrative Law Judge Susan D. Colwell.
ARRA Investigation	*American Recovery and Reinvestment Act of 2009 Investigation*, Docket No. I-2009-2099881 – Final Report confirms that the Commission is not precluded from approving revenue decoupling mechanism or other lost revenue recovery mechanism.
CD Rider	Section 1307(a) surcharge mechanism proposed by UGI Electric to recover revenues lost as a result of Plan-related reductions in electric consumption.
EDC	Electric Distribution Company.
EE&C Plan	Energy Efficiency & Conservation Plan.
NGDC	Natural Gas Distribution Company.
R.D.	Recommended Decision of Administrative Law Judge Susan D. Colwell, Docket No. M-2010-2210316 (July 15, 2011).
Section 1301	66 Pa.C.S. § 1301 – Requiring all rates charged to be just and reasonable
Section 1307	66 Pa.C.S. § 1307(a) – Allowing for utilities to recover certain costs through a sliding scale or automatic adjustment of rates.
Section 1319	66 Pa.C.S. § 1319 – Directing the Commission to allow the recovery of all prudent and reasonable costs associated with an energy conservation or load management program.
Section 2806.1	66 Pa.C.S § 2806.1 – Section 2806.1 of Act 129, subjects only those EDCs with 100,000 or more customers to the requirements of Act 129.
TRC Test	Total Resource Cost Test, defined in Section 2806.1(m) and applied by Commission Order in Docket M-2009-2108601, is used to determine the cost-effectiveness of EE&C Plans.
TRM	Demand Side Management Resources Technical Reference Manual, Docket No. M-00051865, establishes the deemed savings standard for measuring EE&C Plan effectiveness.
UGI Electric	UGI Utilities, Inc. – Electric Division

UGI ELECTRIC EXCEPTION 1:

LOST REVENUE RECOVERY: THE R.D.'S REJECTION OF NON-ACT 129 EE&C PLAN LOST REVENUE RECOVERY THROUGH EITHER A SURCHARGE OR A REGULATORY ASSET ERRS AS A MATTER OF LAW AND POLICY.

A. Summary Of Exception

The R.D. rejects, on legal and policy grounds, UGI Electric's proposal to recover lost revenues as part of its voluntary EE&C Plan. R.D. at 28-31. This was error. Although Act 129 prohibits lost revenue recovery for the large EDCs (to which it applies), there is no legal impediment, either in Act 129 or elsewhere, to the Commission's adoption of a lost revenue recovery mechanism for smaller non-Act 129 EDCs such as UGI Electric. Given that the measure of a successful EE&C plan is the extent to which it reduces consumption and thus correspondingly reduces a utility's revenues, if the Commission wants smaller EDCs to implement EE&C plans voluntarily, it must permit a mechanism to recover revenues lost to successful EE&C measures during the interim between implementation of the EE&C plan and the Company's next base rate proceeding. The record in this case supports lost revenue recovery through either a Section 1307(a) surcharge mechanism or through regulatory asset treatment. UGI Electric proposed the former as part of its Plan (the "CD Rider"), but would accept the latter. Either mechanism would quantify lost revenues to be recovered in the same way EE&C plan conservation success is quantified: "deemed savings." If the Commission is "deeming" a particular level of energy in kWh to be saved when a particular EE&C measure is adopted, the same calculation also necessarily quantifies the revenue lost when such "saved" kWhs are not distributed by the EDC. To do anything less would call into question the accuracy of the Commission's own method of measuring Act 129 energy savings to determine compliance with the General Assembly's mandated reduction goals.

Conservation-related lost revenue recovery is not new to the Commission. When the Commission sought to "jump start" demand side management efforts in the early 1990s, it readily recognized in the order resolving the lengthy investigation ("*1993 DSM Order*") that it is essential in any voluntary conservation program that the utility be "made whole ... for lost revenue costs."[1] The same concerns are now being addressed in the context of the "ARRA" investigation, where, whatever their position on the issue, all commenters recognize that, in order for voluntary EE&C plans to work, society's conservation goals must be aligned with the utility's financial incentives.[2]

For smaller EDCs such as UGI Electric, nothing has changed from either a legal or a policy perspective since the *1993 DSM Order*. Without some form of lost revenue recovery, the "disincentive to implement" an EE&C plan may be insurmountable, and the company will be forced "to choose between implementing the Plan without lost revenue recovery (and thereby accelerating the filing of a base rate case) or withdrawing the Plan altogether." UGI Electric Statement No. 3-RJ at 7:2-5. Under either of these alternatives that assume rejection of any lost revenue recovery mechanism, ratepayers will lose, "because they will either lose the benefits of [the] proposed EE&C Plan or they will end up paying higher rates sooner than they otherwise would have paid them" because UGI Electric will be forced to accelerate the filing of a base rate case. *Id.* at 7:6-9. Under UGI Electric's CD Rider proposal, the average residential customer bill would reflect a $0.37 charge per month during the first year of the Plan, and would be reconciled and adjusted to precisely track actual deemed savings and corresponding lost revenues.

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[1] *Investigation Into Demand Side Management By Electric Utilities Uniform Cost Recovery Mechanism*, 80 Pa. P.U.C. 608, 641 (1993) ("*1993 DSM Order*").

[2] *American Recovery and Reinvestment Act of 2009 Investigation*, Docket No. I-2009-2099881 ("ARRA Investigation").

The Commission should reject the R.D.'s disallowance of a lost revenue recovery mechanism and approve one of the mechanisms proposed by UGI Electric so that this significant disincentive to voluntary EE&C plan implementation is removed.

B. Lost Revenue Recovery Is Lawful For A Non-Act 129 EDC.

Although Act 129 expressly prohibits large EDCs from recovering revenues lost due to reduced energy consumption other than prospectively through a Section 1308 base rate proceeding, neither Act 129 nor Act 129's lost revenue recovery prohibition applies to UGI Electric, because UGI Electric is an EDC "with fewer than 100,000 customers." 66 Pa.C.S. § 2806.1(l) ("This section [*i.e.*, the entirety of Section 2806.1] shall not apply to an electric distribution company with fewer than 100,000 customers."). The statute could not be clearer in this regard, and the R.D.'s attempt to amend the statute by extending the prohibition on lost revenue recovery to UGI Electric violates fundamental rules of statutory construction. If the legislature had wanted to require smaller EDCs to file EE&C plans and to prevent them from recovering the resulting lost revenues outside of the context of a base rate case, it would have drafted the statute to include smaller EDCs within the provisions of Section 2806.1. It did not. Rather, it expressly excluded smaller EDCs from the provisions of the Act.

The inapplicability of Act 129 does not leave a legal void, however. Section 1319 of the Public Utility Code, 66 Pa.C.S. § 1319, which directs the Commission to allow the recovery of "all prudent and reasonable costs associated with the development, management, financing and operation" of a "conservation or load management program," provides all the legal authority necessary for the Commission to approve recovery of lost revenues as part of a voluntary EE&C plan. Indeed, the Commission's *1993 DSM Order* did just that. In that case, the Commission expressly relied on Section 1319 as the proper statutory vehicle to "in effect, jump start the DSM process" by removing the "significant disincentives to the initiation of DSM programs" by

adopting a "special rate making mechanism" that featured a lost revenue recovery component. *1993 DSM Order*, 80 Pa.P.U.C. 608, 623.[3] As the Commission held concerning lost revenue recovery:

> [W]e will permit the utilities to use a balancing account for the lost revenue costs, and they will be treated as regulatory assets. ...We will permit the utilities to accrue interest on these funds at the same annual percentage rate allowed for their individual AFUDC accrual .... In this manner, the utilities would be able to recover the time value of money during the deferral period. This will ensure that the utilities will be "made whole" for their DSM lost revenue costs, even though they will not be permitted to collect them upfront through the surcharge.

Id. at 641.

The Commission's *1993 DSM Order* was reviewed and for the most part[4] affirmed by the Commonwealth Court in *Pennsylvania Industrial Energy Coalition v. Public Utility Commission*, 653 A.2d. 1336, *aff'd per curium*, 670 A.2d. 1152 (1996) ("*PIEC*"). On the question whether Section 1319 permits the recovery of lost revenues in the context of a base rate proceeding, as the Commission in that case contended, the Court declined to reach the issue, finding it unripe because no utility had yet made a regulatory asset claim in the context of a base rate proceeding pursuant to the *1993 DSM Order*. *PIEC* at 1352-53. Although the Court remanded to the Commission for further development of the issue, that opportunity never arose, and the issue was never revisited by an appellate court.

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[3] Specifically, the Commission decided in the *1993 DSM Order*, discussed more fully below, to permit lost revenue recovery through a regulatory asset, in part because, unlike the situation presented here where it is easy to quantify lost revenues through the "deemed savings" values for each plan program, the Commission in 1993 was less certain about how to calculate lost revenues ("[L]ost revenues are, by their nature, much more difficult to measure than DSM program costs. Therefore, we feel it necessary to require that these costs be recovered through a base rate proceeding so that they are based on actual program results, as verified through the rate making process."). *Id.* at 641.

[4] The court upheld the Commission's reliance on Section 1319 to allow special ratemaking treatment (*i.e.*, outside of the context of prospective-only base rate case treatment) for the recovery of direct and collateral electric utility conservation or load management program costs, so long as the costs incurred are "prudent and reasonable." *Id.* at 1346-47. The court also expressly held that it is appropriate to recover direct and collateral conservation program costs through a 1307(a) surcharge. *Id.* at 1349.

The lost revenue issue has arisen again in the context of the Commission's ongoing "ARRA" investigation. There, the Commission is considering potential rate mechanisms that might be needed to satisfy the ARRA federal funding requirement that the state implement appropriate rate making policies for electric and gas utilities to align their financial incentives with the promotion of energy efficiency and conservation, including lost revenue recovery and revenue decoupling mechanisms.[5] The ARRA Final Report confirms that, on the issue of lost revenue recovery, "no legal precedent exists that would preclude the Commission from reviewing/approving an RDM [revenue decoupling mechanism] or similar rate making change [*e.g.*, a lost revenue recovery mechanism] for gas utilities under 66 Pa.C.S. § 1307(a)." ARRA Final Report at 31 n. 42. The same legal conclusion applies to UGI Electric, because, given that Section 2806.1 does not apply to EDCs with fewer than 100,000 customers, UGI Electric is in the same legal position as an NGDC for purposes of lost revenue recovery.

Put simply, there is no legal impediment to the Commission's adoption of UGI's lost revenue recovery proposal, either in the form of the CD Rider 1307 surcharge or in the form of a regulatory asset. The Commission already has decided in the *1993 DSM Order* that lost revenue recovery is both legally permissible under Section 1319 and desirable as a matter of policy, and selected the regulatory asset mechanism to do it because, at that time before adoption of the "deemed savings" approach to measuring energy savings, it was difficult to quantify the lost revenue associated with those energy savings. The ARRA Final Report likewise concludes that, notwithstanding enactment of Act 129 and court cases decided since the *1993 DSM Order*, there

[5] The PUC initiated the ARRA Investigation on May 6, 2009, solicited and received comments and reply comments, held a technical conference on November 19, 2009, established a working group to further discuss issues and to prepare a report regarding potential policies on December 18, 2009, and tasked the working group with submitting a final report. The ARRA Investigation Final Report ("ARRA Final Report") was issued January 24, 2011. The Final Report provides positions of working group members regarding the requirements of the ARRA, as well as extensive analysis regarding aligning energy conservation goals with utility ratemaking policies. Comments have been filed on the Final Report and the matter awaits further Commission action.

is no legal impediment to lost revenue recovery for non-Act 129 entities; the Final Report expressly contemplates a 1307(a) surcharge for lost revenue recovery, *i.e.*, the CD Rider concept that UGI Electric proposes here.

As a matter of law, therefore, lost revenue recovery is permissible. The R.D. thus errs in adopting the legally incorrect and unsupported arguments of the public advocates and the *Amicus*,[6] and in failing to even refer to the extended discussion of the issue in the *1993 DSM Order* where the Commission expressly endorsed the legality (and desirability) of lost revenue recovery in the context of encouraging energy conservation plans. Specifically, the R.D. erroneously concludes that lost revenue recovery is unlawful because it: (1) is not permitted under Section 1307(a) and the Commonwealth Court's decision in *Popowsky v. Pa. Pub. Util. Comm'n.*, 13 A.3d 583, 593 (Pa. Cmwlth. 2011) ("*Popowsky 2011*"); (2) is contrary to the express policy of the Commonwealth as articulated in Act 129; (3) results in impermissible single-issue ratemaking; and (4) is barred by Section 1301. None of these arguments has merit.

1. Section 1307(a)/*Popowsky 2011*

The R.D.'s assertion that permitting surcharge recovery of lost revenues "would be directly contrary to the express language of the Commonwealth Court in *Popowsky 2011*," because "the proposed mechanism is not expressly authorized by the General Assembly," R.D. at 29, gets it exactly wrong. In *Popowsky 2011*, which merely summarized and applied existing law relating to permissible surcharges under Section 1307 (including the Court's *PIEC* decision on appeal from the *1993 DSM Order*), the Court expressly recognized that Section 1319 of the

[6] *Amicus* is a group of groups of industrials, including the Industrial Energy Consumers of Pennsylvania ("IECPA"), Duquesne Industrial Intervenors ("DII"), Met-Ed Industrial Users Group ("MEIUG"), Penelec Industrial Customer Alliance ("PICA"), Penn Power Users Group ("PPUG"), Philadelphia Area Industrial Energy Users Group ("PAIEUG"), PP&L Industrial Customer Alliance ("PPLICA") and West Penn Power Industrial Intervenors ("WPPII"). *Amicus'* only participation in the proceeding was the filing of a brief addressed to the lost revenue issue.

Code authorizes a Section 1307(a) surcharge in this very context for "all prudent and reasonable costs associated with the development, management, financing and operation" of a "conservation or load management program:"

> In *PIEC*, this Court addressed the issue of whether Section 1307(a) of the Code permits electric utilities to recover demand-side management (DSM) program costs by surcharge. Rejecting the argument that Section 1307(a) of the Code applied only to costs beyond the control of the utility, such as fuel costs and certain taxes, this Court held that a surcharge was available. Critical to our holding was the statutory authority for the surcharge found in Section 1319 of the Code, 66 Pa. C.S. § 1319. ... Because Section 1319 [of the Code] directs the PUC to allow recovery of all prudent and reasonable costs for developing, managing, financing and operating DSM programs and because Section 1307 [of the Code] gives the PUC the discretion to establish by either regulations or order the manner in which automatic adjustment recovery may be instituted and when such automatic adjustment of rates should be mandated, the surcharge method is permitted. *PIEC*, 653 A.2d at 1349.

Popowsky 2011, 13 A. 3d at 589 (footnote omitted).

Moreover, although the *PIEC* Court did not have the opportunity to expressly consider whether Section 1319 authorizes Section 1307(a) recovery for lost revenue costs, the Commission itself clearly held in the *1993 DSM Order* that lost revenues are "costs" recoverable under Section 1319,[7] and, although the Court did not reach the issue for procedural reasons, the Court noted the Commission's vigorous defense of that decision on appeal: "the PUC contends that the allowance of lost revenue recovery is authorized under Section 1319 of the Code, which states 'the commission shall allow the public utility to recover all prudent and reasonable costs associated with the development, management, financing and operation of the program.'" *PIEC*

[7] *See, 1993 DSM Order* at 641 ("we feel it necessary to require that these *costs* [*i.e.*, lost revenues] be recovered through a base rate proceeding"; "we will permit the utilities to use a balancing account for the *lost revenue costs*, and they will be treated as regulatory assets"; "this will ensure that the utilities will be 'made whole' for their DSM *lost revenue costs*," even though they will not be permitted to collect them up front through the surcharge.) (Emphasis supplied).

at 1352. The 2011 ARRA Final Report noted above takes the identical position on the legal authority for lost revenue surcharge recovery: "no legal precedent exists that would preclude the Commission from reviewing/approving an RDM [revenue decoupling mechanism] or similar rate making change [e.g., a lost revenue recovery mechanism] ... under 66 Pa.C.S. § 1307(a)." ARRA Final Report at 31 n. 42.

The R.D.'s reasoning that lost revenues from UGI Electric's voluntary EE&C Plan are "not easily identifiable" and not "beyond the utility's control," or "extraordinary" because they are voluntarily incurred, R.D. at 29, fares no better. Lost revenues *are* easily identifiable because they are quantified directly by the "deemed savings" recorded in kWh for each conservation measure implemented. As for whether a voluntary conservation program's costs are "beyond the utility's control," or "extraordinary," the Commission already decided in the *1993 DSM Order*, and the Commonwealth Court affirmed that holding in *PIEC*, that costs incurred to implement voluntary conservation plans that arise between rate cases may be recovered outside of the usual base rate recovery regime. *1993 DSM Order* at 619-20 ("Thus, a utility is entitled to recover all prudent and reasonable costs [including lost revenue costs] associated with these programs, if it voluntarily establishes a conservation or load management program and the Commission approves that program as prudent and cost-effective....").

Finally, even if the R.D. were correct (and it is not) that the law prohibits Section 1307(a) surcharge recovery of lost revenues, such a prohibition would not apply to the alternative regulatory asset treatment UGI Electric proposed, which the Commission expressly approved in the *1993 DSM Order*.

2. Act 129

The R.D. concedes, as it must, that Act 129 does not apply to smaller EDCs such as UGI Electric. It therefore is difficult to understand the R.D.'s adoption of the argument advanced by the public advocates that lost revenue recovery is "contrary to the express policy of the Commonwealth" as articulated in Act 129, and therefore prohibited by law. R.D. at 30. Necessarily, if Act 129 and its ban on lost revenue recovery does not apply to smaller EDCs, allowing smaller EDCs to recover lost revenues cannot be contrary to Act 129 or its policies.

Act 129, which added Section 2806.1 to the Public Utility Code, prohibits large EDCs from recovering lost revenues due to reduced energy consumption, other than prospectively through a Section 1308 base rate proceeding. But the legislature expressly stated that Section 2806.1 "shall not apply to an electric distribution company with fewer than 100,000 customers." 66 Pa.C.S. § 2806.1(l). Therefore, although Act 129 changed the law (as established in the *1993 DSM Order*) with respect to the Act 129 activities of large EDCs, the legislature consciously chose to leave undisturbed that same law concerning smaller EDCs not covered by the provisions of Act 129.

It is thus clear on the face of Act 129 that the legislature intended to leave the law undisturbed with respect to smaller EDCs not covered by Act 129. When a statute is clear in this manner, it is dispositive of legislative intent and there is no need for further interpretation. *Lynnebrook & Woodbrook Assoc. L.P. v. Millersville*, 600 Pa. 108, 115, 963 A.2d 1261, 1265 (2008). If the Commission nonetheless were to apply principles of statutory construction, however, the result would be the same. Where, as here, a statutory provision such as Section 1319 is interpreted by an agency as it was in the *1993 DSM Order*, and the legislature thereafter

has the opportunity to amend the statute to negate the interpretation, but does not do so, an implied legislative approval of the interpretation arises. *Hospital Ass'n of Pa. v. MacLeod*, 487 Pa. 516, 523 n.10, 410 A.2d 731, 734 n.10 (1980). The Commission clearly interpreted Section 1319 in the *1993 DSM Order* to permit recovery of lost revenues. The legislature is presumed to know of that interpretation, but never amended Section 1319. Instead, it amended the Public Utility Code to add Section 2806.1, but expressly chose not to apply that new provision to smaller EDCs such as UGI Electric. The necessary conclusion, therefore, is that Section 1319 and the *1993 DSM Order* interpreting it, except as modified in Act 129 for EDCs with 100,000 or more customers, remain enforceable law and stand for the proposition that recovery of lost revenues associated with energy conservation measures is permissible. If the legislature had intended to proscribe lost revenue recovery associated with conservation measures for all natural gas and all electric public utilities covered by Section 1319, it would have done so. It did not. Since it did not, allowance of lost revenues cannot be "contrary to the express public policy of the Commonwealth." R.D. at 30.

3. Single Issue Ratemaking

The R.D. appears to hold that allowance of lost revenue recovery violates the prohibition against single issue ratemaking. R.D. at 28-29. To the extent it does, it is in error.

Under traditional rate base/rate-of-return regulation, a utility's rates are fixed in the context of a "base rate" proceeding after an examination of expenses, revenues, taxes and return, and go into effect on a prospective basis; the rates themselves are not applied retroactively to past sales, and any changes to the rates as fixed occur only after a similar comprehensive re-examination in the context of a future base rate proceeding. *See, e.g., Popowsky v. Pa. Pub. Util. Comm'n.*, 869 A.2d 1144, 1152 (Pa. Cmwlth. 2005) ("*Popowsky 2005*"). It is within this

context that the alleged prohibition on "single-issue" ratemaking arises. The courts have held that, as a general matter, it is inappropriate to adjust rates to reflect a change in a single revenue or expense item, absent special circumstances. *See, e.g., PIEC*, 653 A.2d. at 1349-50 (1995).

Of course, the Commission and the courts have long recognized that, under certain circumstances, single-issue ratemaking that has a retroactive effect is a necessary and appropriate exception to the general rule that base rates may be changed prospectively only. *See, e.g., Popowsky v. Pa. Pub. Util. Comm'n.*, 868 A.2d 606 (Pa. Cmwlth. 2004) ("*Popowsky 2004*"). Where, as here, a utility can demonstrate a credible basis for recovering an extraordinary item between rate cases, the Commission has approved such recovery and the courts have affirmed it. In *Popowsky 2004*, where Pennsylvania-American Water Company claimed recovery of increased security expenses incurred between rate cases in the wake of the September 11 attacks, the Commission approved it and the Commonwealth Court affirmed because: (1) the cost did not arise as the result of inaccurate projections in a previous rate case; (2) the cost was extraordinary at the time incurred; and (3) the company had attempted promptly to recover the cost through a surcharge, which the PUC had denied in favor of deferred accounting treatment. *Id.* at 610-11.

To the extent that the Commission were to permit UGI Electric to recover lost revenues through its preferred method, a Section 1307 surcharge in the form of the CD Rider, the single-issue ratemaking claim is simply inapplicable. PIEC lost that argument in its appeal from the *1993 DSM Order*, where the Commonwealth Court held that single-issue ratemaking is an issue that arises in the context of base rate proceedings, whereas Sections 1307 and 1319 expressly authorize an automatic adjustment of rates for recovery of conservation-related costs outside of a base rate proceeding. *PIEC* at 1350.

UGI ELECTRIC EXCEPTION 1 – Lost Revenue

With respect to UGI Electric's alternative proposal for regulatory asset treatment of lost revenues, recovery is entirely appropriate under the controlling law. Applying the *Popowsky 2004* three-factor test here, and contrary to the reasoning of the R.D. at 29, UGI clearly is entitled to recovery of lost revenues. First, its lost revenue claim does not arise because of an "inaccurate" revenue projection in its previous base rate case that it seeks to correct, but instead arises from a wholly new event – revenue loss occasioned by its compliance with the Commission's desire to encourage smaller EDCs to file voluntary EE&C plans. Second, and for the same reasons, the lost revenues in question are "extraordinary" because, in contrast to all other situations in which a for-profit enterprise seeks to prevent loss of revenues, here UGI Electric is affirmatively and purposefully taking steps that will result in a loss in revenues by encouraging its customers to reduce their electricity consumption. The Commission decided long ago in the *1993 DSM Order* that lost revenues are recoverable as a regulatory asset for precisely this reason. *Id.* at 623 ("DSM activities are unique in that, if they are successful, the result will be a decrease in demand for electricity with a corresponding reduction in revenues. Under these circumstances, we consider it appropriate and necessary to , in effect, jump start the DSM process through the implementation of a special ratemaking mechanism...."). Third, UGI Electric's attempt to recover the revenues it will lose between the time of implementation of its EE&C Plan and its next base rate case obviously constitutes "immediate action," because it is seeking rate recovery in the very same filing in which it is proposing the Plan that will cause the loss.

Accordingly, should the Commission not approve UGI Electric's proposed CD Rider but allow the recovery of lost revenues in this case as a regulatory asset, it most assuredly would not constitute prohibited "single-issue ratemaking." UGI Electric's claim fits squarely within

Commission and court case law that permits recovery of extraordinary items between rate cases as an exception to the general rule that rates are set only in a base rate case with prospective-only application. The R.D.'s cursory analysis to the contrary is unsupported, unpersuasive, and contrary to Commission precedent.

4. Section 1301

The R.D. erroneously adopts arguments advanced by the OCA and the *Amicus* that lost revenue recovery violates the "just and reasonable" requirement of Section 1301 of the Public Utility Code because the impact of lost revenues is "highly speculative" and thus cannot be examined properly except prospectively in the context of a base rate proceeding. R.D. at 30-31 ("it would produce unjust and unreasonable rates because it is based on speculative estimates of energy savings"). PIEC challenged the Commission's *1993 DSM Order's* allowance of regulatory asset treatment of lost revenues on this same basis. *PIEC* at 1352-53. Although the Court declined to reach the issue on the grounds of ripeness due to the then-difficult task of accurately calculating the actual amount of revenue lost as a result of a conservation program, the Court recognized in remanding to the Commission "the possibility that a sufficiently reliable calculation could be developed." *Id.* at 1352.

The "deemed savings" values developed in the TRM to quantify electricity savings for Pennsylvania's conservations programs now provide all the specificity and reliability needed that was lacking at the time the Commission adopted the *1993 DSM Order*. "Deemed savings" are the basis upon which the Commission is measuring saved kilowatt hours; all stakeholders have agreed to use that metric as the cornerstone of conservation plans. If it is reliable for that purpose, it necessarily is sufficiently reliable for purposes of measuring the revenues lost

associated with the kilowatt hours saved. *See* UGI Electric I.B. at 25-26; UGI Electric R.B. at 12-14.

The R.D. bases its conclusion that UGI Electric's quantification of lost revenues is "highly speculative," on the OCA witness's mere assertion (without any factual support) that even though "deemed savings" are an acceptable method for measuring reduced electricity consumption, they are only a "coarse indicator" of the revenues directly associated with that reduced consumption that will be lost. *See* OCA I.B. at 14 (quoting OCA Statement No. 1 at 22-24). This refusal to acknowledge the inescapable relationship between specific levels of energy savings and specific amounts of lost revenues, now adopted by the R.D., is simply not credible. The Section 1301 "just and reasonable" requirement means that lost revenues must be determined with a "sufficiently reliable calculation." *PIEC* at 1352. If the "deemed savings" values for specific conservation measures as set forth in the TRM are not "sufficiently reliable" to calculate revenues lost associated with kWhs saved, it invites questions as to how they can be reliable to calculate kWhs saved.

C. Lost Revenue Recovery Is Desirable As A Matter Of Policy For A Non-Act 129 EDC.

Given that, by definition, a successful EE&C plan will erode a utility's revenues, the central policy issue the Commission needs to address if it wants smaller EDCs to implement *voluntary* EE&C plans is whether it will permit recovery of lost revenues during the interim between implementation of the EE&C plan and the Company's next base rate proceeding. Perplexingly, the R.D. adopts as "logical" the view held by the public advocates and *Amicus*: given Act 129's prohibition on lost revenue recovery for the *mandatory* EE&C plans of large EDCs, smaller EDCs should expect the same prohibition in their *voluntary* plans. "It is far more logical to expect that, if the smaller EDCs decide to participate in energy conservation programs

similar to the large EDCs, they can expect to recover their costs in a manner similar to the large EDCs." R.D. at 30. But there is nothing logical about this expectation.

Logic dictates that a for-profit enterprise will not *voluntarily* reduce its profits by reducing its sales. That is why the Commission decided in the *1993 DSM Order* that utilities had to be "made whole" for their lost revenue costs if voluntary DSM programs were to succeed. *1993 DSM Order* at 641. That is why Congress, through ARRA, is requiring states to have appropriate rate making policies for electric and gas utilities to align their financial incentives with the promotion of energy efficiency and conservation in order to receive federal stimulus funds; the statutory presumption, entirely logical, is that under traditional regulation a utility's financial incentives are *not* aligned with promoting energy efficiency by reducing sales and thereby reducing revenues. ARRA Final Report at 1. That is why the ARRA Final Report reflects on virtually every page the working group's active consideration of ways to remove financial disincentives to the promotion of energy savings, including lost revenue recovery mechanisms. And that is why numerous Commissions across the country, including Oregon, California and Maryland, have adopted ratemaking mechanisms that in fact remove the economic disincentive. UGI Electric I.B. at 23-24.

There can be no dispute that utilities face an economic disincentive to implement conservation plans, and that voluntary plans will never be viable unless the disincentive is removed. This Commission recognized the point as early as 1993, and other jurisdictions and industry commenters have supported lost revenue recovery since. *Voluntary* plans continue to need a "jump start." *1993 DSM Order* at 623.

Aside from its adoption of the public advocates' and the *Amicus'* misguided "logic" as its point of departure, the R.D. offers several other policy reasons why rejection of UGI Electric's

lost revenue recovery proposal allegedly is good regulatory policy: (1) UGI Electric's revenue reductions will be offset by revenue increases for other UGI affiliates because of UGI Electric's fuel switching proposals; (2) rejection of lost revenue recovery will "not necessarily" lead to an earlier UGI Electric base rate case; and (3) UGI Electric's estimates of energy savings are "speculative," based as they are on a document "not intended for ratemaking purposes." R.D. at 30-31. None of these has merit.

1. "Offsetting" revenues to affiliates

The public advocates' often-stated but never-supported concern that lost revenue recovery is unnecessary because UGI Electric revenue losses will be "offset by revenue increases for other UGI affiliates" as the result of fuel switching, R.D. at 31, has no basis at all in the record. The affiliates OCA claimed would benefit are: (1) PNG, the Company's affiliated NGDC whose service territory partially overlaps with UGI Electric's; (2) AmeriGas, UGI Electric's affiliated propane supplier; and (3) UGI Energy Services, Inc. ("UGIES"), UGI Electric's affiliated natural gas supplier. OCA I.B. at 17. Even if this argument had conceptual merit (and it does not, as discussed below), it is factually incorrect.

The total potential first year increase in PNG's natural gas distribution revenues would be no more than $38,000, less than 10% of the revenues that UGI Electric anticipates to lose in the first year of the Plan. UGI Electric Statement No. 3R at 6:1-15; UGI Electric Exhibit No. WJM-4. There is no other evidence on the record attempting to quantify this amount, and no party challenged UGI Electric's computation in surrebuttal testimony or on cross-examination.

With respect to AmeriGas, an unregulated propane supplier that participates in a highly competitive market, the only record evidence indicates that there will be little, if any, fuel switching from electric to propane. As UGI Electric Witness Raab explained:

> [p]ropane has a relatively low benefit to cost ratio of 0.49. ...[T]he relative cost-ineffectiveness of conversions to propane will significantly limit the number of such conversions, so that they are unlikely to have a signficant (or any) impact on the Plan's overall positive TRC result.

UGI Electric Statement No. 2RJ at 3:17-21. Moreover, even if a customer switched to propane, there is no evidence to support the assertion that the customer would be supplied by AmeriGas given the highly competitive market for propoane in UGI Electric's service territory in which AmeriGas competes.

With respect to UGIES, the Commission's own website confirms that UGIES faces competition from in excess of 35 other natural gas suppliers that are licensed to provide NGS service in the area of UGI Electric's service territory that overlaps with PNG.[8] Given that these 36 suppliers are competing to provide fewer than 10,000 mcf in annual natural gas volumes in the first year of the Plan, *see* Exhibit WJM-5, the level of potential new revenue, if any, to UGIES, is barely measureable and speculative at best.

Accordingly, other than the bald accusations accepted in the R.D., there is no factual basis for the conclusion that UGI Electric's fuel switching programs will enrich its affiliaties.Even if there were such evidence, however, it would not be a principled basis for denying lost revenue recovery. As Mr. McAllister explained, it would be inappropriate to impute any increase in revenues to UGI Electric's affiliates to UGI Electric, because UGI Electric is a separate legal entity whose rates and revenue requirements are determined by its own revenues and expenses, and not those of its affiliates. UGI Electric Statement No. 3R at 5:11-13. Moreover, as Mr. Raab explained, from the policy perspective, it is *desirable* for there to be an increase in end-use gas load as part of a conservation plan, because fuel switching to decrease

[8] http://www.puc.state.pa.us/naturalgas/naturalgas_suppliers_list.aspx.

electric load "is at the heart of the full-fuel-cycle concept that has been so widely endorsed [by DOE, NARUC, AGA and NRDC]." UGI Electric Statement No. 2R at 18:2-12.

2. Need to file base rate case

The R.D. adopts the OCA and OSBA argument that "there is no certainty" that denial of lost revenue recovery in this proceeding will advance the timing of UGI Electric's next base rate case. R.D. at 31. Surely, however, there can be no doubt that, all things equal, if UGI Electric were to implement its Plan without lost revenue recovery, doing so will significantly accelerate its need to file a base rate proceeding. UGI Electric's unchallenged estimate is that, by Year 3 of the Plan, annual lost revenue will be in excess of $1 million. Regardless of whether a base rate filing occurs immediately or the Company is able to hold out for some short period of time while suffering a substantial revenue loss, the filing of a base rate case will occur sooner (and likely much sooner) than later. In contrast, as Mr. McAllister explained, approval of either the CD Rider or regulatory asset treatment for recovery of lost revenue will, all things equal, allow UGI Electric to defer the filing of a base rate proceeding for a substantial period of time. UGI Electric Statement No. 3RJ at 6:22-7:1; Tr. at 109-115.

Denying recovery thus will either force the Company to withdraw the plan or dramatically accelerate the filing of a base rate case. As Mr. McAllister explained, UGI Electric customers will lose either way, because:

> [T]hey will either lose the benefits of our proposed EE&C plan or they will end up paying a higher rate sooner than they otherwise would have paid them because UGI Electric will be recovering in the new base rates the projected lost revenues, plus all of the other increases in base rate components it is entitled to recover, plus the cost of adjudicating the lost revenue claim and all of the other issues in a base rate case filed earlier than otherwise would have been necessary. There is just no question that it is far better for customers to compensate the Company for lost revenues

> through some mechanism that allows the Company to recover interim lost revenues and defer the filing of a base rate case.

UGI Electric Statement No. 3RJ at 7:6-14.

3. "Speculative" reliance on TRM and "deemed savings"

Finally, the R.D. adopts the public advocates' unsuported and erroneous view that UGI Electric's quantification of lost revenues is speculative because it uses as its base the TRM's "deemed savings" values, which "are not intended for ratemaking purposes." R.D. at 31. The quantification of lost revenues is not speculative, however, and the fact that "deemed savings" values were developed to quantify energy savings does not disqualify them as a measure for lost revenues associated with the energy saving measures adopted; the two are flip sides of the same coin. If anything, the technical energy efficiency pedigree actually enhances the reliability and credibility of deemed savings values for rate applications, because all stakeholders in the EE&C process have agreed that they accurately reflect actual energy consumption reduction. "Deemed savings" as developed in the TRM is the "gold standard" for measuring the effectiveness of Pennsylvania's conservation programs. If deemed savings is appropriate to use it to quantify the number of kilowatt hours saved, it is also appropriate to use it to quantify the lost revenues associated with those saved kilowatt hours. Failure to acknowledge this fundamental principle would make a mockery of Act 129 and the Commission's entire EE&C program approval and monitoring process.

Moreover, as UGI Electric Witness McAllister explained, the Company's proposal to use deemed savings to quantify lost revenues is customer and measure-specific, so that the quantification of revenues lost matches precisely to deemed savings in energy:

> We propose to quantify the lost revenues associated with the conservation programs that we are proposing on the basis of the deemed savings that correlate with the conservation measures that our customers elect to implement. ... [I]f a UGI Electric customer

> participates in one of our programs, the deemed savings associated with that activity results in a specified loss in revenue and that specified loss in revenue is the amount we would be entitled to recover.

UGI Statement No. 3RJ at 5:18-6:3.

UGI Electric is not asking the Commission to guarantee that, notwithstanding implementation of its EE&C Plan, UGI Electric will continue to recover a "baseline" revenue amount. UGI Electric is not seeking to recover lost revenue associated with business downturns or non-Plan conservation reductions in electricity usage. Neither the proposed CD Rider, nor the proposed regulatory asset, is structured to capture such revenues. Rather, UGI Electric merely is proposing that for each conservation measure covered by the Plan that is implemented by a customer and produces "deemed savings" in electricity, UGI Electric will lose revenue in a corresponding amount that shall be recovered. This is nothing more than a simple identification and capture of revenues UGI Electric would have received but-for implementation of a particular Plan measure. It is a "make whole" provision of the type the Commission approved in the *1993 DSM Order*, only not in any way speculative and much easier to measure. It is not a "guarantee" of revenues that UGI Electric had hoped to achieve, but rather a payback of revenues that UGI Electric would have received but did not because of the implementation of a particular Plan measure by a particular customer.

D. Surcharge Recovery Of Lost Revenue Through The CD Rider Is Optimal.

UGI Electric's EE&C Plan as filed proposes recovery of lost revenues through the CD Rider, a reconcilable surcharge billed to all customers pursuant to Section 1307 of the Public Utility Code. UGI Electric Statement No. 3 at 13:10-13. *Pro forma* tariff pages to implement the proposed CD Rider are attached to UGI Electric's EE&C Plan as Appendix A. (Exhibit WJM-4 shows the calculation of the proposed annual CD Rider.) *Id.* at 16-20.

As with any other reconcilable surcharge, the CD Rider's initial surcharge amount would collect a projected level of costs (*i.e.*, in this case, lost revenues calculated on the basis of "deemed savings" of electricity produced by anticipated customer participation in particular Plan programs). In the unlikely event that UGI Electric customers opt to participate in Plan programs in precisely the way UGI Electric projects during the first year, the CD Rider will collect the precise amount of lost revenue associated with the collective "deemed savings" in kilowatt hours, and no reconciliation would be needed. Otherwise, the CD Rider surcharge amount will be adjusted to reflect actual revenue losses from the deemed savings achieved, flowing back to customers any over-collections of lost revenues, or recouping from customers any under-collections in lost revenues. UGI Electric Statement No. 3 at 14:19-15:11. In addition to adjusting for reconciliation, the CD Rider surcharge would also adjust to reflect the anticipated "ramp-up" in revenue losses associated with deemed savings from the first year to the second year, and from the second year to the third year of the Plan. *Id.* at 15:13-16:6.

As Mr. McAllister explained, recovery of lost revenues through a reconcilable surcharge such as the CD Rider "is the most administratively efficient and customer-friendly way to recover lost revenues because it does so as they are lost, a process that will occur gradually, reimbursing the Company and charging the customer on a close to real-time basis." UGI Electric Statement No. 3R at 7:5-8. In Year 1 of the Plan, the average residential customer bill would reflect a $0.37 charge per month for the CD Rider, and would increase each year to reflect additional projected savings in electric usage and thus associated lost revenues. *See* Exhibit WJM-4. At whatever time in the future UGI Electric would file a base rate case, the CD Rider would be rolled into base rates and, once all reconciliation was completed, set to zero. As discussed above, and contrary to criticisms by the public advocate witnesses adopted by the R.D.

at 30-31, there is nothing hypothetical or indefinite about lost revenue recovery through the CD Rider. UGI Electric Statement No. 3RJ at 5:18-6:3.

In the Commission's *1993 DSM Order*, the Commission expressed concern that lost revenues associated with DSM programs are difficult to measure, *1993 DSM Order* at 641, because, as the ALJ in the case concluded, there were insufficient monitoring and evaluation techniques for verifying that revenue loss. *1993 DSM Order* at 636. The TRC approach embodied in Act 129 and the TRM, however, eliminates this concern. As UGI witness Raab explained, the TRC is the single standard set by the Commission for determining cost-effectiveness. UGI Electric Statement No. 2R at 27:24-26. If a customer adopts a particular program measure, such as installing a CFL or switching from an electric water heater to a natural gas water heater, that conservation measure produces quantifiable electricity "deemed savings" that necessarily translate directly into quantifiable revenue losses. Accordingly, in the 20 years since the Commission considered the question in the *1993 DSM Order*, verification concerns associated with recovering lost revenues through a reconcilable surcharge have been addressed. As a consequence, the reconcilable surcharge approach to lost revenue recovery reluctantly rejected by the Commission in the *1993 DSM Order*, now has all the specificity and support it needs. It, therefore, deserves a second look.

E. Regulatory Asset Recovery Of Lost Revenue Is Consistent With Commission Precedent.

The alternative recovery mechanism proposed by UGI Electric, regulatory asset treatment, already has been approved by the Commission for lost revenue recovery in the *1993 DSM Order*. The R.D., which rejects the concept of lost revenue recovery generally, R.D. at 28-31, does not attempt to distinguish the *1993 DSM Order* (in fact, does not even cite it), and does not discuss in any way UGI Electric's regulatory asset proposal. *Id.* This is error.

Under UGI Electric's proposal, accrual of a regulatory asset that would reflect actual lost distribution revenues calculated on the basis of actual deemed or calculated electricity savings, as determined on the basis of installed and verified EE&C program participation (*i.e.*, the same method used under the CD Rider proposal). UGI Electric Statement No. 3R at 9:3-6. In addition to actual accrued lost revenues, UGI Electric would be permitted to accrue interest, consistent with the approach adopted by the Commission in the *1993 DSM Order*, and recover the regulatory asset beginning with the effective date of UGI Electric's compliance filing following its next base rate case. *Id.* at 8:18-9:12.

Regulatory asset treatment for lost revenues in the context of an energy conservation plan is a concept that the Commission embraced after full consideration of the issues in its *1993 DSM Order*. In adopting regulatory asset treatment in the *1993 DSM Order*, the Commission acknowledged concern that regulatory asset treatment would result in a delay in the utilities' recovery of lost revenues, but decided that allowing utilities to recover actual program costs up front through a surcharge, while also allowing them to recover interest on the regulatory asset, would suffice to make the utility "whole" and thereby remove the disincentive for utilities to implement conservation programs. *1993 DSM Order* at 641.

Accordingly, although UGI Electric continues to believe that gradual recovery of lost revenues on an as-incurred basis through a reconcilable surcharge is far preferable from the perspective of both ratepayers and shareholders than regulatory asset treatment, and further believes that the evolution in conservation plans that has occurred since 1993 resulting in the "deemed savings" measurement technique eliminates any concerns over monitoring and verification of actual revenue losses, UGI Electric would accept regulatory asset treatment as an acceptable alternative to the proposed (and preferred) CD Rider recovery of lost revenues.

UGI ELECTRIC EXCEPTION 2:

FUEL SWITCHING: THE R.D. ERRS IN REDUCING INCENTIVE PAYMENTS AND REQUIRING THE USE OF HIGH EFFICIENCY EQUIPMENT

A. Summary of Exception

UGI Electric has proposed incentive payments to customers who switch from electric for water heating and clothes drying that equal 100% of the anticipated incremental cost the customer will incur in making the fuel switch, and an incentive payment to customers who switch from electric for home heating of $4850, which equals 75% of the anticipated average incremental cost the customer will incur in making the fuel switch. The R.D. makes three very significant adjustments to the fuel switching incentive proposals, the net effect of which is to jeopardize the overall success of the Plan: (1) a drastic reduction (far higher than any proposed by any public advocate in the case) in the home heating incentive from $4850 to $1000, based solely on evidence apparently gathered by the ALJ after the record closed and UGI Electric had no opportunity to review or rebut – a palpable due process violation; (2) a reduction to the water heating and clothes dryer fuel switching incentive from 100% to 50%, based on similar extra-record evidence and an unsupported recommendation by the OCA; and (3) imposition of the requirement that incentive payments be conditioned on the customer's purchase of much more costly high efficiency equipment. Recognizing that much judgment is involved in setting the level of incentives needed to induce a customer to switch, UGI Electric urges the Commission to retain the incentives as proposed by UGI Electric, especially if the Commission is inclined to accept the high efficiency equipment requirement, so that the Plan's opportunity for a successful roll-out is maximized. That way, in the event that experience demonstrates that the incentive payments are too high, UGI Electric, the party in the best position to do so, will be able to make any necessary mid-course corrections to an already successful Plan.

B. Fuel Switching Incentive Payments Should Not Be Reduced, Especially If Costlier High Efficiency Equipment Is Required.

UGI Electric has proposed incentive payments to customers who switch from electric for water heating and clothes drying that equal 100% of the anticipated incremental cost the customer will incur in making the fuel switch, and an incentive payment to customers who switch from electric for home heating of $4850, which equals 75% of the anticipated average incremental cost the customer will incur in making the fuel switch. UGI Electric Exhibit 1 at 57. In each of its proposed fuel switching incentive programs, UGI Electric requires that the customer install standard efficiency replacement appliances, but does not require more expensive high efficiency appliances. A review of the details of the actual programs reveals that fuel switching measures are expected to produce slightly less than half of the Plan's total TRC Net Benefits of $15.2 million, and slightly less than half of the total $8.6 million in Plan costs over 3 years. These are good programs, with high TRC Benefit/Cost ratios. The electric to natural gas water heater switching program alone accounts for almost a third of the Plan's overall TRC Net Benefits, with a TRC Benefit/Cost ratio of 2.08. UGI Electric Exhibit 1 at 62. On an overall basis, the Plan's TRC Benefit/Cost ratio is 2.04, far in excess of the 1.0 minimum TRC test parameter applied to the larger EDCs' EE&C plans in the Act 129 proceedings. *See* UGI Exhibit 1 at 70. In short, the fuel switching programs within UGI Electric's overall Plan "pull their weight"; they are substantial contributors to the Plan's overall potential for success (in terms of "deemed savings"), yet do not monopolize the Plan's budget and leave ample room for the Plan's other seven programs.

The R.D. recommends three significant adjustments that adversely affect the proposed fuel switching incentives and jeopardize the success of the Plan on an overall basis. None of the

adjustments is supported or necessary. UGI Electric urges the Commission to reject the R.D.'s recommendations and approve the fuel switching programs as filed.

First, relying exclusively on comparison to an alleged smaller EE&C incentive payment for a home heating fuel switching program offered by PPL (information apparently gathered independently by the ALJ, never introduced into the record by any party, never discussed in any of the pre-filed testimony or in cross examination, never discussed by any participant in briefs, and cited for the first time in the R.D.) the R.D. arbitrarily recommends that the 75% incentive payment for home heating fuel switching be slashed from $4850 to "no more than $1000." R.D. at 39.[9] The Commission should reject this component of the R.D. out of hand, as it violates fundamental due process rights. The issue of incentive payments for fuel switching was hotly contested in this case, but no party recommended cuts for home heating incentive payments anywhere near as deep as those recommended by the R.D., and no party cited or relied on the fuel switching incentive payment apparently offered by PPL in its EE&C plan as a basis for arguing that UGI Electric's proposed incentive should be reduced. If they had, UGI Electric would have had the opportunity to review the particulars of PPL's incentive payments, offer expert testimony justifying the differences in UGI Electric's proposed incentives, and otherwise litigate the issue in an orderly fashion. Nor did the ALJ at hearing confront UGI Electric's expert witness on the issue, which at least would have provided UGI Electric an opportunity to be heard. Nor does the R.D. even attempt to demonstrate that the PPL incentive program to which it compares UGI Electric's is even remotely comparable. Under these circumstances, this recommendation of the R.D. is a blatant violation of due process that is clear reversible error,

[9] The R.D. text conflicts with the Ordering paragraphs on this issue. In the text at 39, the R.D. states that no incentive for home heating fuel switching should exceed $1000; in Ordering Paragraph 3.b, the directive is that the incentive level "shall not exceed 50% of the customer's cost," which on this item would be $2425. As discussed below, UGI Electric contests this reduction to the proposed incentive payment as well, and asks that the Commission approve the incentive payment as filed.

and must be rejected. *Ohio Bell Tel. Co. v Pub. Utils. Comm'n*, 301 U.S. 292 (1937) (where state public utilities commission, following on-the-record proceedings, based its decision on price trends that did not appear in the record and that the utility had no opportunity to examine or rebut before the commission's decision, fair hearing essential to due process was not afforded and commission action was reversed).

Second, relying again on extra-record information relating to the lower fuel switching incentives allegedly offered by PPL and Allegheny in their EE&C plans, and also in part on the recommendations of OCA Witness Crandall, the R.D. recommends that the 100% incentives UGI Electric proposes for water heating and clothes drying be cut in half so that no incentive payment exceeds "50% of the cost of the replacement." R.D. at 38-39. This basis for the R.D.'s recommendation on this issue suffers the same due process violation taint as the R.D.'s home heating incentive reduction recommendation – *i.e.*, it is based on information gathered by the ALJ after the close of the record with no opportunity for UGI Electric to review or rebut it. However, because the ultimate recommendation – a reduction in the incentive payment of 50% - is the same outcome recommended by the OCA, which UGI Electric did have an opportunity to contest, UGI Electric views the error as harmless as long as the Commission does not base its decision on the extra-record information supplied in the R.D.

Focusing on the OCA's criticisms and proposed 50% reduction of the incentive payment, UGI Electric urges the Commission to retain the 100% incentive for these two items as proposed. Most of the dollars allocated to this program are expected to be spent on the electric to natural gas hot water heater fuel switch incentive, and, as stated above, the program is expected to be a key element of the overall Plan's success -- it alone accounts for almost a third of the Plan's overall TRC Net Benefits, with a TRC Benefit/Cost ratio of 2.08. UGI Electric Exhibit 1 at 62.

Admittedly, much judgment is involved in attempting to predict what it will take to persuade a customer to switch from an electric water heater or clothes dryer. There is no direct experience with other plans that UGI Electric can use as a guide or benchmark. UGI Electric has given considerable thought to the level of incentives that will be necessary to induce customers to switch. As UGI Electric Witness Raab explained, the Company considered a variety of factors, mindful that under the status quo consumers rarely convert from an electric appliance to another fuel such as natural gas, even though the savings in energy costs alone could justify a switch:

> The Company's fuel switching programs are innovative and unique. While one may be able to borrow information and data about traditional conservation and energy efficiency programs from other utilities in other jurisdictions, this is not the case with the group of fuel switching programs included in UGI Electric's Plan. We do not precisely know the level of incentive required to move this market in a significant way.
>
> UGI Electric does know, however, that the likelihood of a customer who does not already have natural gas service converting from an electric appliance to a natural gas appliance is small, because this rarely occurs in practice. On the other hand, UGI Electric's customers regularly purchase high efficiency equipment. These observations suggest that larger incentives will be required to move the market from electric appliances to natural gas appliances than will be required to obtain participation in traditional conservation and energy efficiency programs, and explains why the incentives associated with the Company's fuel switching programs have been set at higher levels than the incentives associated with the Company's more traditional conservation and energy efficiency programs.

UGI Electric Exhibit No. 2RJ at 9:18-10:10.

Ultimately, there is no way to know precisely what incentive amount is required in order to induce a customer to switch. The smaller the incentive payment, the more likely it is that the only customers who will take advantage of the incentive will be free-riders who would have switched anyway. UGI Electric Statement No. 2R at 21:8-15. UGI Electric wants the Plan to succeed, and views "a successful roll-out of these [fuel switching] programs to be particularly

important." UGI Electric Statement No. 2R at 21:17-18. As Mr. Raab explained, to accomplish this goal, it makes sense to err if at all on the side of giving an incentive that turns out in retrospect to be too large, which the Company can scale back if it meets with too much success:

> In light of this, UGI Electric believes it is important that these programs, which have not been offered by the larger EDCs, get off to a successful start. The best way to ensure early success is by offering large incentives for customers to participate. If these incentives turn out to be larger than necessary, they can always be reduced as UGI Electric gains more experience with them.

Id. at 21:18-23.

Given that the Company has built its Plan from the ground up, filed it on a voluntary basis, has every reason to want it to succeed, and will be closely monitoring its implementation and the need for mid-course corrections, it deserves the benefit of any doubt on this issue. The size of the incentive needed to induce a customer to switch is a critical unknown; the only thing we know for sure is that the incentive will need to be very substantial for the program to be successful, at least initially.

Third, significantly exacerbating the damage to UGI Electric's Plan that would result from the first two recommended cuts in incentive payments, the R.D. calls for adoption of the OCA's proposal that incentive payments may be offered only for high efficiency natural gas appliances, which have a much higher cost than standard efficiency appliances. R.D. at 46. The R.D. relies heavily in this regard on the Commission's May 6, 2011 Tentative Order at Docket No. M-2009-2108601 ("TRC Tentative Order")[10] which proposes, but does not decide, to require a switch to "high efficiency" alternate fuel devices. R.D. at 43-46. UGI Electric offers three points in response.

[10] Implementation of Act 129 of 2008 - Total Resource Cost (TRC) Test, Docket No. M-2009-2108601 (May 6, 2011).

Point one is that the TRC Tentative Order is just that – something the Commission is considering to assist Act 129 electric companies as they amend and improve their plans. The Commission has not yet adopted it, and is presently considering comments to the TRC Tentative Order. Given that fact, and given that "high efficiency" water heaters, clothes dryers and gas furnaces are significantly more expensive than their standard efficiency counterparts, the Commission should not at this time, for a fledgling EE&C plan, "raise the bar" on inducing customers to switch from electricity to natural gas or some other alternate fuel by significantly increasing the customer contribution, but rather should approve the program as filed and consider an amendment to UGI Electric's Plan, if and when the Commission adopts the TRC Tentative Order.

Point two is that the Commission should reconsider its Tentative Order on this issue. There is no basis for requiring electric customers to pay incentives for devices that will decrease *natural gas* consumption that is the responsibility of the natural gas distribution company:

> If UGI Electric were to pay UGI Penn Natural Gas customers to install high efficiency natural gas appliances, this would be a clear case of UGI Electric subsidizing the conservation and energy efficiency activities of UGI Penn Natural Gas. This is because once the electric load has been removed from the UGI Electric system, UGI Electric customers get no additional electric load reduction from the more costly investment in a high efficiency gas appliance, and UGI Electric customers should not be expected to pay for that.

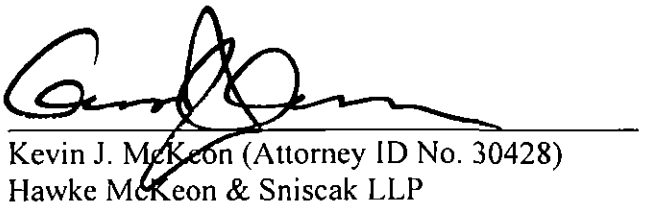
UGI Electric Statement No. 2R at 23:15-21.

Point three is that, in the event the Commission decides to amend UGI Electric's Plan to require "high efficiency" alternate fuel equipment as recommended in the R.D., doing so is one more reason the Commission should reject any reduction in proposed incentive payments for fuel switching, because the higher cost of high efficiency equipment, coupled with a dramatically lower incentive payment, surely will jeopardize the success of the fuel switching component of

the Plan, and, as a result, of the Plan itself. *See* UGI Electric Init. Br. at 42-43; UGI Electric Statement No. 2RJ at 13:17.

CONCLUSION

UGI Electric respectfully requests that the Commission grant these exceptions and approve the Plan as amended to reflect: (1) the addition of solar thermal water heating as per the SEF stipulation; (2) the revised 30-day notice provisions; and (3) the revised classes for cost on lost revenue rider recoveries.



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Dated: July 25, 2011

Counsel for UGI Utilities, Inc., Electric Division

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a true copy of the foregoing document upon all parties of record in this proceeding in accordance with the requirements of 52 Pa. Code Section 1.54 (relating to service by a participant), in the manner and upon the persons listed below:

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