

COMMONWEALTH OF PENNSYLVANIA



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February 17, 2010

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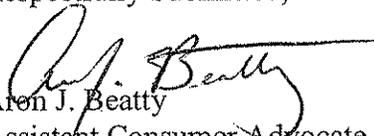
RE: Joint Petition of Metropolitan Edison
Company, Pennsylvania Electric Company
and Pennsylvania Power Company for
Approval of Smart Meter Technology
Procurement and Installation Plan
Docket No. M-2009-2123950

Dear Secretary McNulty:

Enclosed for filing are the Exceptions of the Office of Consumer Advocate to the Initial Decision issued on January 28, 2010 by the Honorable Susan D. Colwell, in the above-referenced proceeding.

Copies have been served as indicated on the enclosed Certificate of Service.

Respectfully Submitted,


Aren J. Beatty
Assistant Consumer Advocate
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Enclosures

cc: Honorable Susan D. Colwell

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CERTIFICATE OF SERVICE

Joint Petition of Metropolitan Edison :
Company, Pennsylvania Electric Company :
and Pennsylvania Power Company for : Docket No. M-2009-2123950
Approval of Smart Meter Technology :
Procurement and Installation Plan :

I hereby certify that I have this day served a true copy of the foregoing document, the Exceptions of the Office of Consumer Advocate to the Initial Decision issued on January 28, 2010 by the Honorable Susan D. Colwell, upon 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:

Dated this 17th day of February 2010.

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BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Joint Petition of Metropolitan Edison :
Company, Pennsylvania Electric Company :
and Pennsylvania Power Company for : Docket No. M-2009-2123950
Approval of Smart Meter Technology :
Procurement and Installation Plan :

EXCEPTIONS OF THE
OFFICE OF CONSUMER ADVOCATE

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Dated: February 17, 2010

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I. INTRODUCTION

On August 14, 2009, Metropolitan Edison Company, Pennsylvania Electric Company and Pennsylvania Power Company (collectively FirstEnergy Companies or Companies) filed a Joint Petition for Approval of Smart Meter Technology Procurement and Installation Plan (Joint Petition) pursuant to Act 129, 66 Pa.C.S. § 2807, and the Public Utility Commission's (Commission) Implementation Order.¹ In addition to the Office of Consumer Advocate (OCA), the following parties participated in this proceeding: The Office of Trial Staff (OTS), Department of Environmental Protection (DEP), Met-Ed Industrial Users Group, Penelec Industrial Customer Alliance, and Penn Power Users Group (collectively MEIUG *et al.*), Office of Small Business Advocate (OSBA), the Pennsylvania Association of Community Organizations for Reform Now (ACORN), and Constellation NewEnergy, Inc. and Constellation Energy Commodities Group, Inc. (collectively Constellation).

Comments to the FirstEnergy Companies' Joint Petition and proposed Smart Meter Technology Procurement and Installation Plan (SMIP) were filed by the OCA, OTS, DEP and ACORN on September 25, 2009. An Initial Prehearing Conference was convened by Administrative Law Judge Susan D. Colwell (ALJ) on September 28, 2009. A technical conference was held in this matter before ALJ David A. Salapa on October 20, 2009.

Hearings were held before ALJ Colwell on November 19, 2009. During hearings, the following testimonies of the OCA's witnesses were admitted into the record: Direct Testimony

¹ Re: Smart Meter Procurement and Installation, Docket No. M-2009-2092655 (Order entered June 24, 2009) (Implementation Order).

of J. Richard Hornby² (OCA St. 1); Direct Testimony of Nancy Brockway³ (OCA St. 2); Surrebuttal Testimony of J. Richard Hornby (OCA St. 1S); and Surrebuttal Testimony of Nancy Brockway (OCA St. 2S). Main Briefs were submitted by various parties, including OCA, on December 11, 2009, and Reply Briefs were submitted on December 31, 2009.

On January 28, 2010, ALJ Colwell issued her Initial Decision in this matter. With regard to matters of concern to the OCA, ALJ Colwell rejected the OCA's recommendation for the Companies to further consider mitigation efforts to address the burdens of smart meter deployment on low-income and otherwise vulnerable customers. Further, ALJ Colwell approved the Company's proposal to allocate the common costs among the classes based on the number of customers in each class. Finally, the ALJ approved the Companies' rate design as filed, allowing the Companies to collect smart meter and smart meter-related costs through a fixed customer charge. The OCA submits these Exceptions to the ALJ's Initial Decision on these points.

II. EXCEPTIONS

OCA Exception No. 1: The Commission Should Reject The Conclusion That Mitigation Of The Impacts Of Smart Meter Deployment On Vulnerable Customers Be Addressed Only Through Traditional Means, Such As Customer Assistance Programs. (I.D. at 29-30; OCA M.B. at 17-19; OCA R.B. at 3-5).

² Mr. Hornby is a Senior Consultant at Synapse Energy Economics, Inc., specializing in planning, market structure, ratemaking, and gas supply/fuel procurement in the electric and gas industries for more than 20 years. He has presented expert testimony and provided litigation support in approximately 100 proceedings in over 30 jurisdictions on behalf of state energy offices, consumer advocate offices, marketers and staff of public utility commissions. Mr. Hornby is a former Assistant Deputy Minister of Energy for the Province of Nova Scotia. He has a Master of Science in Energy Technology and Policy from the Massachusetts Institute of Technology (MIT) and a Bachelor of Industrial Engineering from the Technical University of Nova Scotia, now merged with Dalhousie University.

³ Ms. Brockway heads her own consulting firm specializing in the energy and utility industries, with particular attention on the role of regulation in the protection of consumers and the environment. She has over 25 years of experience and is a former Commissioner of the New Hampshire Utilities Commission. She was also formerly a hearing officer and advisor to the Maine Public Utilities Commission and General Counsel of the Massachusetts Department of Public Utilities. Ms. Brockway earned a Juris Doctor degree from Yale Law School and a Bachelor of Arts degree from Smith College.

In her Initial Decision, ALJ Colwell concludes that “there is no exception or accommodation for low-income or otherwise vulnerable customers in either the Act or the Implementation Order.” See I.D. at 30. However, a lack of specific exception in Act 129 for low-income and otherwise vulnerable customers⁴ does not require rejection of the OCA’s recommendations regarding the need for the Companies to address mitigation of the impacts of smart meter deployment on these customers. Therefore, the conclusion that the impacts of smart meter deployment on low-income and otherwise vulnerable customers shall be addressed only through traditional means, such as customer assistance programs, should be rejected.

In its Main Brief, the OCA outlined specific actions the Companies should take during the Assessment Period in order to mitigate the financial impacts of Act 129’s smart meter deployment requirements on those customers least able to absorb them – low-income and otherwise vulnerable customers. See OCA M.B. at 17-19. Specifically, the OCA recommended the following be included in the Companies’ SMIP:

- The Companies should particularly assess the impacts of their proposed SMIP on vulnerable customers. Working with community groups, the Company should identify to what extent their customers are low-income, low-use, medically challenged, or otherwise at risk, and develop plans to mitigate the risks to such customers of smart metering costs, including consideration of smart metering technologies, price and program designs, and equipment specification. This assessment should include a granular analysis of load shapes and usage characteristics of a sample of identified vulnerable customers before the end of the grace period to ensure sufficient reliable data and understanding of the needs of these customers.

See OCA M.B. at 17-18, citing OCA St. 2 at 3-4;

- [The Companies should] keep the costs of the deployment down as much as possible. This will help mitigate the bill impacts on customers who cannot necessarily participate in programs or rate offerings that may be enabled by smart meters. Requiring a robust benefit/cost ratio will help to

⁴ Vulnerable customers include low-income customers, customers with disabilities, the elderly, and others who cannot afford bill increases but may not enjoy many of the benefits of smart meter implementation. See OCA M.B. at 17, citing OCA St. 2 at 11.

keep the pressure on deployment costs and ensures that the optimal plan is chosen.

See OCA M.B. at 18, citing OCA St. 2 at 12; and

- In order to mitigate the burdens of smart meter deployment on vulnerable customers who cannot take advantage of SMIP rebates is to recover SMIP costs primarily on a volumetric rather than fixed basis.

See OCA M.B. at 18, citing OCA St. 2 at 13.

To be clear, the OCA does not recommend that low-income and otherwise vulnerable customers be excluded from the Companies' SMIP. Instead, the OCA's recommendations are intended to minimize any possible adverse impacts of smart metering deployment on such customers through analysis and consideration of the needs of low-income and otherwise vulnerable customers at all stages of program design and deployment.

ALJ Colwell accepts the Companies' argument that the consumer education and tools outlined in their SMIP, along with their already established customer assistance and universal service programs, will be adequate to address any adverse financial impacts of smart metering on their low-income and otherwise vulnerable customers. See I.D. 29-30. This argument fails to take into account two key facts. First, as stated by OCA witness Brockway:

With respect to the CAP programs, their budgets may not be sufficient to address the needs that may arise if vulnerable customers experience adverse bill impacts. LIHEAP, for its part is a federal program not within the control of the Commonwealth, whose budget (and thus availability) fluctuates. LIHEAP is only available for home heating applications. For the energy efficiency and smart meter program, while available to low income customers, many such programs require the customer to make an investment to be able to take advantage of the programs.

See OCA St. 2S at 2. Further, all of these programs are already being stretched to their limits, and any increased costs of these programs place additional burdens on other residential customers that support the programs.

Second, the Companies' SMIP provides a time-frame to assess the usage of their low-income customers to better understand the impact of the smart meter technology. This time-frame and the additional information allows for the designed programs to assist all low-income and otherwise vulnerable customers, not just payment-troubled customers that are served by CAP.

In this scenario, an ounce of prevention really does equal a pound of cure. The Companies can mitigate the adverse financial impacts of smart metering by, *inter alia*, studying their vulnerable customers, assessing their needs and usage and keeping their study findings in mind in choosing smart meter program design and technology. The Companies have already committed to a certain level of data collection and analysis during the Assessment Period, so it is not burdensome to require that they collect and analyze additional data regarding their low-income and otherwise vulnerable customers and work with interested stakeholders and community groups to develop appropriate plans.

The Companies can also prevent adverse financial impacts of smart metering by keeping smart meter deployment costs as low as possible. The Companies already have the burden of showing the Commission that they chose the most cost-effective, reasonable approach for implementation of smart meters in their service territories when submitting their Deployment Plan at the end of the Assessment Period. It naturally follows that the Companies should take into particular consideration the most cost-effective, reasonable approach for their low-income and otherwise vulnerable customers. Last, the OCA recommends mitigating the financial impacts of smart metering on low-income and otherwise vulnerable customers by recovering SMIP costs from residential customers primarily on a volumetric rather than fixed basis. This issue is discussed in more detail *infra*.

The fact that Act 129 and the Implementation Order are not specific with regard to minimizing the financial impacts of smart metering on low-income and otherwise vulnerable customers is not sufficient reason to ignore the steps that can readily be taken to mitigate the adverse financial impacts that this legislatively mandated program could have on the customers that are least equipped to handle them. The OCA's recommendations regarding data collection and analysis and program design are reasonable extensions of the data collection and analysis outlined in the Companies' SMIP. As discussed *infra*, the OCA's recommendation to recover SMIP costs for the residential class primarily on a volumetric rather than fixed basis is also reasonable and fair to all residential customers. Therefore, the OCA's recommendations regarding mitigation of the adverse impacts of smart metering on low-income and otherwise vulnerable customers should be accepted.

OCA Exception No. 2: The ALJ Erred In Approving The Companies' Proposal To Allocate SMIP Common Costs Based On The Number Of Customers In Each Class (I.D. at 48-55; OCA M.B. at 22-32; OCA R.B. at 6-18).

As part of their Smart Meter Plans, the Companies will incur approximately \$29.5 million in costs during the Assessment Period for overall Plan development which they classify as common costs that must be allocated among classes. I.D. at 48. The Companies, joined by the OSBA and MEIUG *et al.*, support the allocation of these costs on a per meter basis. The OCA supports the allocation of these costs on a demand and usage basis.

In her I.D., the ALJ detailed the Companies' position with regard to the allocation of these costs. I.D. at 49-55. The ALJ found that the Companies' allocation was reasonable and concluded as follows:

By proposing that the Companies allocate their SMIP costs on the basis of energy usage and demand, the OCA is ignoring long-standing principles of cost causation. As the Companies point out,

these costs “are akin to traditional metering and meter-related costs” because they will be incurred to determine the best way for the Companies to comply with the metering requirements mandated by Section 2807(f) of the Public Utility Code and the Commission’s Implementation Order.” (Companies Stmt. 3-R, pp. 2-3). Because these costs will be incurred without regard to energy consumption or customer demand, and because the smart meter technology will be provided to all metered customers, any costs relating to the Companies’ SMIP that cannot be directly assigned to a specific customer class should be allocated based on the number of customers in each class, as the Companies propose.

I.D. at 55 (Emphasis added).

The OCA excepts to the ALJ’s finding that an allocation of common Assessment Period costs on a customer basis is required in this case. The ALJ agreed with the Companies that the SMIP costs are “akin to traditional metering.” I.D. at 55. The OCA strongly opposes such a depiction of the SMIP costs in question. These are not traditional meters and the common costs associated with the Smart Meter Implementation Plan are not simply for the purpose of counting kilowatt hours and billing customers. The OCA submits that the reasons for incurring the costs imposed by the implementation of the Smart Meter Plans and by a specific directive of the General Assembly, diverge widely from the reason that “traditional metering” costs are incurred. The costs here are incurred to forward the purposes of Act 129 to provide benefits to customers in energy price reduction and stability through energy and demand savings. As such, looking simply at how outdated meters and meter-related costs were allocated in past decades produces an unreasonable result – especially when the ultimate purpose of smart meter installation is taken into consideration.

The OCA submits that the ALJ’s position overlooks the true cost causation of the Companies’ smart meter network – and the benefits anticipated by the General Assembly in passing Act 129. The cause of these costs is Act 129. The primary purpose of installing a smart

meter network pursuant to Act 129 is to impact the energy usage and peak demand of customers to reduce and stabilize energy prices. Act 129, 66 Pa.C.S. § 2806.1 *et seq*, pmb1.; OCA St. 1S at 5. The benefit of that impact will accrue to all customer groups, based on those customers' total energy usage and the demand they place on the system. The common costs arising during the Assessment Period, therefore, should be allocated on a usage and demand basis, as proposed by OCA witness Hornby and detailed in the OCA's Main and Reply Briefs. See OCA M.B. at 22-32; OCA R.B. at 6-18.

As further detailed below, and as explained in the OCA Main and Reply Briefs, the allocation of common SMIP costs on a demand and energy basis reflects cost causation and is consistent with traditional ratemaking principles. As such, the OCA submits that the ALJ's decision on this issue should be rejected and an allocation of these costs that reflects causation and benefits should be adopted.

A. Smart Meter Common Costs Are Being "Caused" By The Requirements Of Act 129 In Order To Benefit Customers Through Reductions In Demand And Energy Costs.

The OCA does not support the Companies' proposal to allocate the Assessment Period costs incurred by the Companies on a per customer basis. The costs that the Companies will incur during the Assessment Period will result in the development and construction of a smart meter network in accordance with Act 129 designed to drive down peak demands, produce energy savings opportunities, and reduce or stabilize wholesale costs of power.

OCA witness Hornby addressed the causes of cost incurrence in this proceeding noting that smart meter costs are being incurred, or "caused," primarily in anticipation of substantial savings in electricity supply costs. See OCA St. 1 at 15. Mr. Hornby explained the principles of cost causation that are at issue here, as follows:

[T]he Companies are incurring these costs solely to comply with the smart meter plan requirements of Act 129 and the primary goals of that Act are to reduce annual energy use, peak load and the costs and environmental impacts associated with those two factors.

Act 129 is clearly “causing” the Companies to incur incremental costs to deploy smart meter technology. The Companies note that they are submitting a smart meter plan to comply with the Act in their petition on page 3, in their Plan on pages 1 and 3, in the Direct Testimony of Mr. Paganie on page 7 at lines 7 and 8 and in the Direct Testimony of Mr. Mills on page 12 at lines 16 to 18.

See OCA St. 1S at 4-5. For example, the Companies’ Smart Meter Plan begins by acknowledging the impact of Act 129 on the filing, as follows:

1.1 Introduction

On October 15, 2008, Governor Rendell signed House Bill 2200 into law as Act 129 of 2008 (“Act 129”), which became effective on November 14, 2008. Among other things, Act 129 directed each electric distribution company (“EDC”) with more than 100,000 customers to file with the Pennsylvania Public Utility Commission (“Commission”) by August 14, 2009, its Smart Meter Technology Procurement and Installation Plan (“Plan”).

See ME/PN/PP Exh. JEP-2 at 4. In addition, the Companies’ witness, Robert A. Mills, noted:

The [Assessment Period] costs identified above represent costs that are necessary to prepare the Deployment Plan for deploying smart meters in Pennsylvania in order to meet the Companies’ statutory obligations under Act 129.

See ME/PN/PP St. 2 at 12.

The Companies’ cost recovery witness, Raymond I. Parrish, explained the purpose of their proposed rate recovery mechanism, as follows:

The purpose of my testimony is to introduce and explain the Companies’ proposed cost recovery mechanism that will be used to recover the costs incurred by the Companies during the planning and implementation of the Companies’ Smart Meter Technology Procurement and Installation Plan (“Plan”) that is

being filed pursuant to Act 129 of 2008, 66 Pa. C.S. §2807(f) (“Act 129”).

See ME/PN/PP St. 3 at 2. (Emphasis added). As Mr. Parrish testified, the Companies have developed a cost recovery plan to collect those costs that they are required to incur due to the passage of Act 129. As explained by OCA witness Hornby and acknowledged by the Companies’ witnesses, Act 129 is the direct cause of the current filing.

Reasonable cost of service practices require that costs be allocated among rate classes according to cost causation. See OCA St. 1 at 15; OCA St. 1S at 3. These costs are caused by compliance with Act 129. The preamble to Act 129 states that one of the main goals of the Act is to reduce the cost and price instability of electric energy:

The General Assembly recognizes the following public policy findings and declares that the following objectives of the Commonwealth are served by this act:

(1) The health, safety and prosperity of all citizens of this Commonwealth are inherently dependent upon the availability of adequate, reliable, affordable, efficient and environmentally sustainable electric service at the least cost, taking into account any benefits of price stability over time and the impact on the environment.

Act 129, 66 Pa.C.S. § 2806.1 *et seq*, pmbl.

The purpose of this massive new investment is not simply to count kilowatt hours and provide accurate monthly bills to each individual customer. Act 129 was passed for the purpose of reducing and stabilizing the cost of energy, to the benefit of all customers. Act 129, 66 Pa.C.S. § 2806.1 *et seq*, pmbl. Importantly, the Companies do not dispute this fact. Mr. Hornby testified that the Companies have acknowledged that the purpose of Act 129 is to drive down costs to the benefit of all customers, noting:

Act 129 is also explicitly trying to achieve important public policy goals of reducing annual energy use, reducing the air emissions

associated with that annual energy use, and reducing peak load. The General Assembly obviously expects that achieving these public policy goals will provide benefits to all customers in all rate classes. The joint and common costs associated with smart meter technology and energy efficiency are ultimately being caused by current levels of energy and demand, and the goal of Act 129 to reduce those current levels. For example, Mr. Paganie lists "...achieving Energy Efficiency and Demand Response" as the first benefits of the Companies' Plan (Paganie Direct, page 7 at line 23).

See OCA St. 1S at 5.

The purpose of the smart meter network required under Act 129 is to reduce costs and improve reliability to the benefit of all classes. As Mr. Hornby testified:

[S]ince these AMI related costs are being incurred, or "caused", primarily in anticipation of substantial savings in electricity supply costs they should be allocated in a manner that reflects those anticipated benefits. Allocating based on number of customers does not properly reflect the fact that the majority of the benefits are savings related to reductions in either demand or energy.

See OCA St. 1 at 15.⁵

The OCA submits that it is wholly unreasonable to allocate the common costs of the Companies' program based on the number of customers. Instead, these common costs should be allocated to customer classes in some reasonable proportion to the benefits received by each class from the planning and implementation of the smart meter system.

⁵ The ALJ cited the Companies' Main Brief, where they argued that the OCA's proposed allocation would be a "value of service" allocation. I.D. at 49-52. The Companies and Industrials argue that the OCA's position is a "value of service" allocation. See ME/PN/PP M.B. at 38; Industrials M.B. at 12-16. This argument is without merit.

Contrary to these arguments, the OCA's proposal is not based on value of service. The Companies have acknowledged that the Assessment Period costs at issue here are required to effectuate Act 129. Costs are being incurred to meet this legislative mandate in order to reach the goals established in the Act – costs are not being incurred to meet an unknown "value of service" placed on the SMIP by the Companies' customers.

B. The Benefits Of Smart Metering Accrue To All Classes, And The Bulk Of Costs Should Not Be Placed On Residential Customers.

In Exhibit JRH-3, OCA witness Hornby detailed the energy consumed by each major customer class for each of the three Companies. The following chart shows the percentage of each company's total energy usage:

	Met-Ed	Penelec	Penn Power
Residential	39.4%	31.6%	35.5%
Commercial	33.6%	36.0%	29.9%
Industrial	27.0%	32.4%	34.6%

Source: OCA St. 1, Exh. JRH-3 (page 2 of 2).

As the chart demonstrates, the energy consumed by each Company is spread somewhat evenly among the customer classes. This is the case despite the fact that residential customers represent 88%, 86%, and 87% of Met-Ed, Penelec and Penn Power's total customer number base, respectively. See ME/PN/PP St. 1 at 4-5. The industrial customers also account for between 21 percent and 29 percent of the peak demand placed on the Companies' system. See OCA St. 1S, Exh. JRH-3. The commercial customers account for between 29 percent and 40 percent of peak demand. Id.

As a result, to the extent each FirstEnergy Company's Plan achieves the General Assembly's goals and produces energy and demand savings, those savings will be spread among all of the customer classes in proportion to their energy usage and demand. Under the Companies' proposed allocation, however, the residential class will pay by far the lion's share of the costs. It simply defies logic that residential customers, who are responsible for only 31.6% to 39.4% of the Companies' energy usage, should pay for 86% to 88% of these costs.

By allocating on a purely customer count basis, the Companies will not be collecting the appropriate level of common costs from those customers causing such costs. As OCA witness Hornby explained:

Allocating based on number of customers does not properly reflect the fact that the majority of the benefits are savings related to reductions in either demand or energy. Therefore the allocation factor should be based upon demand (kW), energy (kWh) or some combination of both.

See OCA St. 1 at 15. The OCA submits that the Companies' proposal to allocate costs based on the number of customers is not appropriate given the anticipated benefits of the Plan. As such, the ALJ's decision on this issue should be rejected.

C. Allocating Common Costs On An Energy And Demand Basis Is Consistent With Accepted Ratemaking Principles.

In her I.D., the ALJ finds that the OCA is "ignoring long-standing principles of cost causation." I.D. at 55. The OCA respectfully submits, however, that the ALJ erred by failing to recognize that SMIP common costs are being incurred, not for the sake of placing basic kilowatt hour meters in service, but for the benefits that will result from the creation of a fully integrated smart meter network and the corresponding reduction in energy and capacity prices. In this way, the ALJ erred by finding that the costs at issue are "akin to traditional metering and meter-related costs." I.D. at 55.

The allocation of costs based on the causal relationship between costs and benefits is an accepted cost of service principle that is directly applicable here. This treatment is in keeping with the language of Act 129 itself, as well as with the Commission's Implementation Order.⁶ The Commission clearly evidenced its intention to assign costs to the classes which derive the benefit when it stated:

⁶ As noted below, this more reasonable methodology has been proposed in neighboring Maryland by BG&E. See OCA St. 1S at 4.

...we will require the EDC to allocate those costs to the classes whom derive the benefit from such costs.

Implementation Order at 32. The Commission went on to say:

Any costs that can be clearly shown to benefit solely one specific class should be assigned wholly to that class. Those costs that provide benefit across multiple classes should be allocated among the appropriate classes using reasonable cost of service practices.

Id.

The relationship between cost and benefits is an accepted and recognized ratemaking principle.⁷ For example, in the recent case Illinois Commerce Commission v. FERC, hereinafter ICC, the Seventh Circuit stated:

FERC is not authorized to approve a pricing scheme that requires a group of utilities to pay for facilities from which its members derive no benefits, or benefits that are trivial in relation to the costs sought to be shifted to its member...Not surprisingly, we evaluate compliance with this unremarkable principle by comparing the costs assessed against a party to the burdens imposed or benefits drawn by that party.

Illinois Commerce Commission v. FERC, 576 F.3d 470, 476 (Seventh Cir. 2009) (citing KN Energy, Inc. v. FERC, 968 F.2d 1295, 1300 (D.C. Cir. 1992); Transmission Access Policy Study

⁷ In her I.D., the ALJ quotes the Industrial customers' position that the Commonwealth Court's decision in Lloyd v. Pa. Public Utility Commission requires that the OCA's cost allocation should be rejected. I.D. at 53-54; See Lloyd v. Pa. Public Utility Commission, 904 A.2d 1010 (Pa. Commw. Ct. 2006) (Lloyd). The OCA submits, however, that rather than preclude consideration of the OCA's allocation proposal, the Lloyd decision supports its implementation.

While the Industrials cited Lloyd for the proposition that cost of service is the "polestar" of utility ratemaking and argue that allocating costs on the basis of benefits violates cost of service principles, the Court's decision in Lloyd does not support this argument. Notably, another section of the Lloyd decision upholds the allocation of Sustainable Energy Fund (SEF) costs to all classes of distribution customers on the basis that all ratepayers benefit from the Fund's activities. Lloyd at 1024-1027. The SEF costs were charged to all customers through a uniform per kWh charge. In the face of an argument by industrial customers that the SEF provides no demonstrable benefits to ratepayers, the Court stated: "What the core of that argument ignores is that the General Assembly has specifically authorized that public service programs such as SEF be funded." Lloyd at 1025. The Court noted that the purpose of the SEF is "to promote the development and use of renewable energy and clean energy technologies, energy conservation and efficiency which promote clean energy." Lloyd at 1024. Act 129, which established the smart metering program, likewise seeks to further the availability of adequate, reliable, affordable, efficient and environmentally sustainable electric service at the least cost, taking into account the benefits of price stability over time and the impact on the environment. Act 129, 66 Pa.C.S. § 2806.1 *et seq.*, pmb1.

Group v. FERC, 225 F.3d 667, 708 (D.C. Cir. 2000); Pacific Gas & Elec. Co. v. FERC, 373 F.3d 1315, 1320-21 (D.C. Cir. 2004); Midwest ISO Transmission Owners v. FERC, 373 F.3d 1361, 1368 (D.C. Cir. 2004)); see also Alcoa Inc. v. FERC, 564 F.3d 1342, 1346-47 (D.C. Cir. 2009); Federal Power Act, 16 U.S.C. § 824d. In ICC, the Court heard an appeal by various state Commissions and utilities in PJM regarding the financing of new transmission facilities. ICC, 576 F.3d at 474. The PJM-proposed and FERC-approved method at issue would have required all utilities in PJM’s region to contribute pro rata for facilities of over 500kV. Id. In overturning this treatment, the Seventh Circuit noted that not even the roughest estimate of likely benefits to the objecting utilities was presented. Id. at 475. In fact, FERC counsel conceded that Commonwealth Edison would derive only \$1 million in expected benefits from the project for which it was being asked to pay \$480 million. ICC, 576 F.3d at 478. The Court specifically stated that the disparity between benefit and costs would be unreasonable. Id.⁸

OCA witness Hornby recommended that a reasonable cost allocation methodology would distribute costs based on both customer usage and demand. See OCA St. 1 at 15. Mr. Hornby explained his alternative allocation methodology, as follows:

⁸ It should be noted that, in another context, the PJM Interconnection and the Midwest Independent Transmission System Operator (MISO) have proposed a methodology for allocating the costs of projects built into one regional transmission organization that also provided benefits to another Regional Transmission Operator (RTO). These benefits are referred to as “economic cross-border projects.” In its Order addressing this issue, the FERC described the methodology it then approved as follows:

If a project qualifies as an economic cross-border project, its costs will be allocated to each RTO in proportion to the present value of the RTO’s share of the annual benefits that are calculated for the proposed project...

We accept the RTO’s proposal as just and reasonable and in compliance with the Commission’s directives to revise the JOA [Joint Operating Agreement] to include a methodology to allocate between the RTOs, the costs of economic cross-border transmission projects.

We find that the proposed JOA economic cross-border benefit formula is a just and reasonable method of allocating costs since it is based on criteria that the Commission previously accepted for use by each RTO to measure the benefits of adding new transmission within its footprints.

Order on Cross-Border Facilities Cost Allocation, 129 F.E.R.C. ¶ 61,102 at ¶¶ 9, 26-27 (2009).

[I]t is reasonable for the Companies to allocate Assessment Period costs using a simple allocator consistent with the anticipated benefits which are driving, or causing, the implementation of AMI and to collect those costs through a charge consistent with the categories of those costs.

See OCA St. 1 at 16. Mr. Hornby further explained his recommendation for allocating Assessment Period costs, as follows:

I am proposing that they be allocated based upon the Companies' current levels of energy and demand which I consider to be the factors causing or underlying the Act's requirement that the Companies incur these costs.

See OCA St. 1S at 9.

A more reasonable allocation, similar to that proposed by OCA witness Hornby, has been proposed in other jurisdictions. Mr. Hornby testified as follows:

In Maryland, Baltimore Gas and Electric is proposing to allocate all smart meter costs among electric rate classes using a demand allocation factor, i.e. a three year average of weather normalized peak load contribution by class measured as an average of five coincident peaks.

See OCA St. 1S at 4.

The OCA submits that a part demand, part energy allocation of Assessment Period costs, as proposed by Mr. Hornby, is reasonable and should be adopted in this proceeding. A reasonable allocation factor for the Assessment Period costs would be a composite factor that is a weighting of energy and demand. See OCA St. 1S at 6. Mr. Hornby calculated the allocation factors for each Company using a 50% energy, 50% demand factor in his Exhibit JRH-3. See OCA St. 1S, Exhibit JRH-3.

The Companies' Plan is intended to provide economic benefits to all customers. Indeed, the purpose of the pending filing is to reduce total usage and peak usage, to the benefit of all

ratepayers. The OCA submits that an allocation based on both energy usage and demand properly recognizes why costs are being incurred and should be adopted in this case.

OCA Exception No. 3: The ALJ Erred In Approving The Companies' Fixed Customer Charge For Residential Customers (I.D. at 31-32, 58; OCA M.B. at 37-39; OCA R.B. at 21-22).

In her I.D., the ALJ ordered the approval of the Companies' Smart Meter Plan, pursuant to the modification contained in her decision. I.D. at 58. The ALJ did not expressly address the issue of residential rate design. The ALJ noted that the SMT-C rate, designed for the collection of SMIP costs, will be expressed as a monthly customer charge. I.D. at 31. The ALJ also noted that the parties are not in agreement regarding cost recovery. I.D. at 32. The OCA does not agree with the Companies' proposal to collect SMIP costs from residential customers through a fixed monthly charge. The OCA files this Exception to the ALJ's approval of the Company's plan on this issue.

The OCA submits that the Companies' Assessment Period costs should be recovered from residential customers on a per kWh, or usage, basis. The Companies' proposal to collect all smart meter costs through fixed customer charges is not consistent with the Commission's ratemaking standards.

Utilizing traditional ratemaking principles, the Commission has limited the costs that can be included for recovery in the customer charge to "basic customer costs" necessary to customer service. See e.g., Pa. PUC v. West Penn Power Co., 69 PUR4th 470, 521 (1985) (West Penn); Pa. PUC v. West Penn Power Co., 1994 Pa. PUC LEXIS 144, 154 (1994). The Commission has defined "basic customer costs" to include the costs for the meter and service drop, meter reading and billings. See West Penn at 521. OCA witness Hornby testified that the Companies' proposal would improperly collect common costs through a customer charge, as follows:

The Companies' proposal to apply the SMT-C as a customer charge is not reasonable for the Assessment Period. As noted above, the Companies consider the costs it will incur to be joint and common costs rather than customer-related costs. There is no support for recovering costs that are classified as joint and common via a customer charge.

See OCA St. 1 at 16. The OCA submits that a proper recognition of basic customer costs will result in a cost recovery scheme that collects indirect smart meter network costs through a usage based charge. See also OCA St. 1S at 9.

In addition to these traditional ratemaking principles regarding customer charges, the collection of all smart metering costs through a fixed charge is antithetical to the guiding principles of Act 129. A major purpose of Act 129 is the reduction of energy consumption, both on an annual basis and with regard to peak energy usage. As the Commission is well aware, the use of fixed charges for the recovery of a utility's costs reduces customers' incentives to decrease usage. If all of the smart meter costs are collected through a fixed customer charge, the incentive to reduce usage will decrease to the detriment of the energy efficiency goals of Act 129.

OCA witness Brockway also testified that the Companies should move to a volumetric approach in order to benefit more vulnerable customers. Ms. Brockway testified as follows:

SMIP costs should be recovered primarily on a volumetric rather than fixed basis. In this way, low-use customers who cannot take advantage of SMIP tariff benefits will not be as burdened with costs of the new system as they would be under fixed charge cost recovery.

See OCA St. 2 at 13. As Ms. Brockway explained, certain vulnerable customers are unable to respond to peak pricing signals obtained through smart metering. The OCA submits that a volumetric charge will provide more assistance to low-use vulnerable customers who cannot take advantage of peak pricing programs.

The OCA submits that recovery of the Assessment Period costs on a per kWh basis is reflective of the greater benefits that residential customers with greater usage stand to realize from smart meter capabilities. Finally, because the FirstEnergy Companies will be allowed to fully reconcile smart meter costs and revenues, the Companies bear no risk of under-recovery if actual sales are less than projected. For these reasons, the OCA submits that the ALJ's decision regarding the Companies' proposed residential design should be rejected and SMIP costs allocated to the Residential classes should be collected on a volumetric basis.

III. CONCLUSION

The Companies have developed a generally reasonable approach for the development and installation of a smart meter network as required under Act 129. The OCA supports the ALJ's decision, to the extent that it approves the general framework under which the Companies will implement their smart meter plan. The OCA submits, however, that the ALJ erred in failing to address issues regarding vulnerable customers and in approving the Companies' cost allocation and rate design proposals.

Of particular importance, traditional cost allocation principles, the language of Act 129, and the Commission's Implementation Order all support the OCA's position that the common costs of the FirstEnergy Companies' smart meter system cannot reasonably be allocated on the basis of the number of customers. The number of customers is neither a measure of the benefits derived from the smart meter system, nor the cause of common system costs. Accordingly, the OCA respectfully submits that the ALJ's I.D. should not be adopted with respect to the issues

identified in these Exceptions and that the Commission should approve the OCA's proposals concerning customer protections, common cost allocation, and residential rate design.

Respectfully Submitted,



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