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December 31, 2013

VIA ELECTRONIC FILING

Rosemary Chiavetta, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street, 2nd Floor North
P.O. Box 3265
Harrisburg, PA 17105-3265

Re: Pennsylvania Public Utility Commission v. PPL Electric Utilities Corporation
Docket No. R-2012-2290597

Dear Secretary Chiavetta:

Enclosed for filing are the Replies of PPL Electric Utilities Corporation in Response to the Comments of Other Parties Regarding the Storm Damage Expense Rider, for the above-referenced proceeding. Copies will be provided as indicated on the Certificate of Service.

Respectfully Submitted,

John H. Isom

JHI/jl
Enclosures

cc: Honorable Susan D. Colwell
Certificate of Service

CERTIFICATE OF SERVICE

I hereby certify that true and correct copies of the foregoing have been served upon the following persons, in the manner indicated, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant).

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Date: December 31, 2013

John H. Isom

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:	Docket No. R-2012-2290597
v.	:	
PPL Electric Utilities Corporation	:	

REPLIES OF PPL ELECTRIC UTILITIES CORPORATION TO THE COMMENTS OF OTHER PARTIES REGARDING THE STORM DAMAGE EXPENSE RIDER

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I. INTRODUCTION

On March 28, 2013, pursuant to the Pennsylvania Public Utility Commission's ("Commission") Order entered in this proceeding on December 28, 2012 ("*Rate Case Order*"). PPL Electric Utilities Corporation ("PPL Electric") filed Supplement No. 130 to its Tariff – Electric Pa. P.U.C. No. 201. There, PPL Electric proposed the Storm Damage Expense Rider ("SDER") to provide for recovery of operating expenses caused by storms that are reportable under the Commission's regulations at 52 Pa. Code § 67.1(b). The purpose of the SDER was to replace storm damage insurance that PPL Electric's insurer, PPL Power Insurance, Ltd., and its reinsurers had refused to renew due to extreme losses that they had incurred under the storm insurance policies, most recently from Hurricane Sandy in October, 2012. PPL Electric Exceptions, pp. 20-23.

Pursuant to a secretarial letter dated April 5, 2013, parties were permitted to submit comments and reply comments regarding PPL Electric's proposed SDER. Upon consideration of the comments and reply comments, the Commission entered a further order on November 15, 2013 ("*November Order*"). There, the Commission invited further comments and replies regarding the SDER. The Commission explained that the further comments and replies were being permitted in order to ensure all parties due process rights and provide the Commission with the benefit of additional substantive input. *November Order*, p. 5. In order to guide the comments of the parties, the Commission asked the parties to address nine subjects that were set forth in Appendix A to the *November Order*.

PPL Electric, the Commission's Bureau of Investigation and Enforcement ("I&E"), the Office of Consumer Advocate ("OCA") and PP&L Industrial Customer Alliance ("PPLICA") submitted comments in response to the Commission's *November Order*. Below, PPL Electric

replies to the comments of other parties. Before responding specifically to the comments of other parties, however, several observations are appropriate.

In the *November Order*, the Commission emphasized that: "Attempts to relitigate the appropriateness of allowing an **alternative funding mechanism** to replace the disallowed storm damage insurance will be **disregarded**." *November Order*, p. 5 (emphasis added). Despite the Commission's specific admonition, all other parties devoted a substantial portion of their comments to arguments that the Commission should reject any form of alternative funding mechanism.

These arguments took several forms. I&E urged that the Commission defer consideration of a rider until PPL Electric's next base rate case. I&E Comments, p. 7. Under I&E's position, no funding mechanism would be adopted, which would be directly contrary to the Commission's order. I&E argued that the Commission at this time should require reserve accounting for storm damage expenses, but I&E offers no funding mechanism. Instead, I&E proposes that the reserve balance be reviewed and alternative funding mechanisms be considered in future base rate cases. I&E Comments, p. 8. I&E's position is directly contrary to the Commission's admonition that it will disregard arguments that it should reject alternative funding mechanisms.

OCA argued that "there is no need to implement PPL's proposed SDER or any type of special recovery mechanism." OCA Comments, p. 10. In essence, OCA proposes to continue the recovery of storm damage expenses through base rates with the possibility of amortization of expenses from extraordinary storms. Under OCA's position, there would be no alternative funding mechanism.

PPLICA recommends that "the Commission deny recovery of additional storm damage expenses through an automatic adjustment clause, consistent with Section 1307 of the Public

Utility Code, and limit approval of an alternative funding mechanism to establishment of a storm damage reserve account." PPLICA Comments, p. 2. Of course, the problem with only establishing a reserve account is that it is simply an account; it would provide no funding mechanism at all, alternative or otherwise.

The other parties offer several rationales for disregarding the admonition in the Commission's *November Order*. I&E argues that consideration of a rider should be deferred so it could be more thoroughly vetted in the next base rate case. In making this argument, I&E ignores the following conclusion in the Commission's *November Order*. At pages 4-5, the Commission states:

> All parties shall be afforded due process when property interests such as those at issue here are implicated: however, the required level of due process must be determined. As the Commonwealth Court has held, "when there are no disputed questions of fact and the issue to be decided is purely one of law, a case may be disposed of without resort to an evidentiary hearing." Rather, in such cases, a "paper hearing" is sufficient to protect the due process rights of the participants." (Footnotes omitted.)

In reaching this conclusion, the Commission relied on *Dee Dee Cab, Inc. v. P. P.U.C.*, 817 A.2d 593, 598 (Pa. Cmwlth. 1995; *Lehigh Valley Power Committee v. Pa. P.U.C.*, 563 A.2d 548, 556 (Pa. Cmwlth. 1989); *Diamond Energy, Inc. v. Pa. P.U.C.*, 653 A.2d 1360, 1367 (Pa. Cmwlth. 1995). The Commission is holding a "paper hearing" now; the comments and reply comments are integral components of that process. I&E ignores the fact that, in this proceeding, it will have had four opportunities to comment on and air its views on alternative funding mechanisms for storm damage expenses.

OCA argues similarly that the evidentiary record in the rate case proceeding in 2012 did not address the SDER and therefore, the SDER or similar funding mechanisms should not be adopted without further hearings. Like I&E, OCA ignores the "paper hearing" process that the

Pennsylvania courts have repeatedly approved and that the Commission is currently providing to the parties. Like I&E, when this proceeding has been completed, OCA will have had four opportunities to comment on PPL Electric's proposed SDER and any other alternative funding mechanism. The Commission is providing ample due process for all the parties.

OCA in its comments also rehashed some of the evidence from the rate case regarding PPL Electric's now unavailable storm damage insurance program. OCA Comments, pp. 4-7. Although the purpose of this discussion is unclear, OCA seems to imply that no alternative funding mechanism should be adopted because the former storm damage insurance program did not benefit ratepayers. OCA's argument is meritless for several reasons. First, the issue of whether the former storm damage insurance program benefitted ratepayers is completely different from what form of funding mechanism should be adopted at this time. Second, of course, the evidentiary record in the base rate portion of this proceeding does not address alternative funding mechanisms in detail. The principal issue in the base rate case was whether the insurance program should be continued. As explained above, that issue became moot as a result of losses incurred by insurers, the most recent of which resulted from Hurricane Sandy. Third, in contending that the evidentiary record in the base rate portion of the proceeding is not sufficient, OCA ignores that the Commission is presently creating the record regarding alternative funding mechanisms in the current "paper hearing" process. No one is relying on the evidentiary record in the base rate case because the issue there was entirely different. There, although I&E discussed the possibility of a reserve account, the primary issue was whether PPL Electric should continue its use of insurance as one means of dealing with storm damage expenses. Fourth, OCA's summary of the rate case evidence is unbalanced, at best. OCA simply reiterates evidence submitted by I&E that was critical of the storm damage insurance

program. OCA ignores the explanations provided by PPL Electric that the insurance program benefitted ratepayers. PPL Electric explained that I&E's position was erroneous because it was largely driven by a misinterpretation of an interrogatory response which led I&E to double count sources of funds available to pay for storm damage expenses. PPL Electric St. 2-R, pp. 2-4. In fact, the losses sustained by the insurers drove PPL Electric's affiliated insurer to the brink of losing its license to provide any insurance and caused the reinsurer to refuse to offer such insurance. PPL Electric St. 14-RJ, pp. 10-13; PPL Electric Exceptions, pp. 22-23. Ratepayers in fact paid far less than PPL Electric's actual storm damage expense while the insurance program was in effect. PPL Electric St. 2-R, pp. 2-3. OCA's one-sided summary of the rate case evidence on the storm damage insurance program should be disregarded.

All three of the other parties recommended that the Commission should either do nothing or at most require the establishment of a reserve account mechanism. I&E Comments, p. 8, OCA Comments, p. 10, PPLICA Comments, p. 2. These recommendations are directly contrary to the Commission's express decision that an alternative funding mechanism should be adopted. A reserve account obviously is not a funding mechanism. It provides no funds for payment of expenses. It merely provides, under limited circumstances, a place to track revenues available to pay storm damage expenses and such expenses.

Indeed, unless PPL Electric is permitted to establish a regulatory asset, a storm damage reserve account might not even protect PPL Electric from financial consequences of large storms when storm damage expenses exceed revenues for their payment. The basis for the reserve account is FERC Account No. 228.1, Accumulated provision for property insurance. The instructions for that account provide that "Charges shall be made to this account for losses covered, not to exceed the account balance." In other words, when expenses exceed revenues,

the difference must be charged to expense on a current basis. PPL Electric's earnings and credit ratings could be adversely affected by a large storm when losses exceed the balance in the reserve account, unless the Commission allows PPL Electric to record a regulatory asset on its books to offset any negative amount.

The other parties also contend that no alternative funding mechanism should be adopted in responding to the Commission's questions. PPL Electric will respond to those contentions below.

As a practical matter, in answering the Commission's list of questions in its comments submitted on December 16, 2013, PPL Electric has responded to many contentions of other parties. In these Reply Comments, PPL Electric will minimize repetition of its previous comments to the extent possible.

Below, PPL Electric responds to comments of other parties that were made in response to the Commission's questions set forth in Appendix A to the *November Order*.[1] PPL Electric's responses are set forth beneath each of the Commission's questions.

1. Does the proper test for an automatic adjustment clause include expenses that are "substantial, variable, and beyond the utility's control?" If so, do all storm related operating expenses meet the standard?

OCA and I&E agree that the "substantial, variable and beyond the utility's control" standard applies to automatic adjustment clauses. OCA Comments, p. 11, I&E Comments, p. 8. PPLICA appears to argue that the standards for automatic adjustment clauses, that are not mandated by statute, are that the expenses must be easily identifiable and beyond the utility's control. PPLICA Comments, pp. 2-4. No party contends that storm damage expenses are not highly variable. Similarly, no party contends that storm damage expenses are not readily identifiable.

[1] PPLICA did not respond to all of the Commission's questions. It responded to questions 1, 6 8 and 9.

The other parties, however, all contend that storm damage expenses are subject to PPL Electric's control. I&E Comments, p. 9; OCA Comments, pp. 12, 15; PPLICA Comments, pp. 2-3. These contentions are erroneous for two principal reasons – first, they are founded on exaggerated notions of how much control PPL Electric has over storm damage expenses and second they understate public utilities' control over expenses that, as other parties concede, are properly subject to automatic adjustment clauses.

PPL Electric, like other public utilities, has a statutory duty to restore service as promptly as practical after a storm event. All public utilities are required by law to take all reasonable steps to restore service which must be without "unreasonable interruption." 66 Pa.C.S. § 1501. PPL Electric believes that the Commission would not look favorably upon a public utility that allowed customers to experience a prolonged service outage in order to reduce costs. Thus, a public utility's realistic discretion to limit costs of restoring service is very limited.

Conversely, public utilities' control over costs that other parties concede are properly recovered through automatic adjustment clauses is greater than other parties suggest. Other parties have used fuel costs as an example of an expense beyond the control of a utility. PPLICA Comments, p. 4; OCA Comments, p. 12; I&E Comments, p. 9. Contrary, to other parties' contentions, before industry restructuring, electric utilities could influence fuel costs.

For example, electric distribution companies can enter into long term contracts or short term contracts, fixed price contracts or contracts with prices floating on any number of different indices, purchase financial hedges or physical hedges, or enter into contracts with demand charges or contracts with only energy charges. Electric utilities can own their own generation facilities or they could construct transmission facilities to reduce congestion. All of these decisions influence fuel costs. The simple facts are that PPL Electric, like all electric distribution

companies, has a statutory obligation to restore service following an outage as promptly as reasonably practical, and therefore, it has only limited discretion in controlling storm damage service restoration costs. Further, no party has contended that the costs of restoring service following a reportable storm are not identifiable. PPL Electric should be permitted to recover storm remediation costs through an automatic adjustment clause.

I&E and OCA also contend that storm damage expenses may not be "substantial." I&E Comments, p. 11; OCA Comments, pp. 15-16. In making this contention, I&E and OCA observe that, while the totality of annual storm damage expenses can be substantial, damage from individual storms may not be. I&E's and OCA's argument is little more than semantics. It is true that, if total expenses are divided into enough pieces, the pieces may not be substantial, but that is not the applicable test, which considers the total expense. It would be equally invalid to argue that fuel costs are not substantial because the cost of a single kWh of energy is not substantial. These contentions are meritless.[2]

As explained above and in PPL Electric's Comments, its expenses for remediation of damages from reportable storms meet the standards for recovery through an automatic adjustment clause pursuant to Section 1307(a) of the Public Utility Code.

2. Does Section 1307 authorize "one-way" reconciliation provisions? Is I&E's storm damage reserve proposal contrary to statutory requirements?

As PPL Electric explained, it is uncertain whether "one-way" reconciliation is permissible under Section 1307(e) of the Public Utility Code. It is impossible to determine definitively whether "one-way" reconciliation is lawful without appellate review of such an

[2] I&E also contends that PPL Electric should be denied an automatic adjustment clause because it has disregarded the difference between the standards for extraordinary rate relief and eligibility for an automatic adjustment clause. I&E suggests that somehow, because PPL Electric has received relief in base rates in the past for extraordinary storms, it is precluded from utilizing an automatic adjustment clause to recover expenses from reportable storms in the future. Although PPL Electric will agree that the standards for extraordinary rate relief through base rates are somewhat different from standards for use of an automatic adjustment, that difference presents no barrier to the prospective use of an automatic adjustment clause.

automatic adjustment clause. To avoid this uncertainty, it would be more prudent to follow the well-traveled, tried and true path of a standard automatic adjustment clause under Section 1307 of the Public Utility Code with "two-way" reconciliation, especially where substantial expenses would be recovered through the clause. Uncertainty regarding the legality of the recovery mechanism would expose PPL Electric to risk regarding recovery of storm damage expenses in the event of a successful appellate challenge to the mechanism approved by the Commission. No party has suggested that storm damage expenses should not be recovered. Such recovery should not be placed at risk.

In its comments, I&E explained that it does not propose an automatic adjustment clause with "one-way" reconciliation. Instead, I&E suggested a reserve account in which any "overcollection" would be flowed back to ratepayers by means of a credit in a subsequent base rate case. I&E Comments, p. 13. Unfortunately, in attempting to resolve one legal issue, I&E's current base rate/reserve account proposal may create other problems. Apparently, I&E proposes that, in a subsequent base rate case, the Commission compare actual, historic storm damage expenses with revenues for recovery of storm damage expenses by reviewing the level of the storm damage reserve and adjust base rates prospectively to refund or recover from customers the difference between actual storm damage expenses and the estimates included in setting base rates. OCA seems to support this approach to storm damage expenses. OCA Comments, p. 16.

The first problem with this base rate/reserve account approach to recovery of storm damage expenses is that it could be construed to be "line item" ratemaking. In *National Fuel Gas Distribution Corporation v. Pa. P.U.C.*, 76 Pa. Cmwlth. 102, 146-47, 464 A.2d 546, 567 (1983) ("*National Fuel*"), the Commonwealth Court held that:

> If a utility's rates are, as in this case, lawful and in conformance with the applicable tariff, Code *Section 1312*

> authorized retroactive rate relief in the form of a refund only if the utility's rates are unreasonable or unjust. So far as we are able to discern, there is no warrant in *Section 1312* for a line-by-line examination of the utility's expenses and revenues actually incurred or received under rates previously in force and the Code does not authorize the imposition of a refund of excess revenues and improvident expenditures without consideration of the reasonableness of rates as a whole. . . .
>
> The Legislature's failure to authorize refunds in case an item of the utility's revenue is greater than anticipated at the time of the tariff approval or an item of expense is or should have been less than anticipated and approved, is sensible and equitable. It is equitable because the utility may not receive retroactive rate relief on account of expense items which are greater than anticipated or of revenue items which are lesser. It is sensible because the consideration of expense and revenue items in isolation and the requirement of refunds based only on such narrow consideration could result in the setting of confiscatory rates.

I&E's and OCA's proposed base rate/reserve account treatment of storm damage expenses may contemplate the type of line item analysis that the Court prohibited.

The second problem with the base rate/reserve account is that it is simply provides for recovery of storm damage expenses through base rates. It is only a little different from the existing system for recovering storm damage expenses which the Commission has determined to be unsatisfactory. The current system is unsatisfactory because it entails long delays between the incurrence and recovery of storm damage expenses. The base rate/reserve account ratemaking treatment of storm damage expenses proposed by I&E and OCA would perpetuate this problem. The proposed base rate/reserve account treatment of storm damage expenses should be rejected.

3. Under a storm damage expense rider ("SDER") or similar mechanism, what is the appropriate period to amortize a "major storm"? Provide statistical data or other relevant factors that the Commission should consider to support the appropriate amortization period. Should the Commission establish one amortization period that applies to all "major storms" or a sliding scale of amortization periods based on the expense levels or other factors?

In its Comments, PPL Electric explained that all storm damage expenses should be recovered over a single twelve-month period. PPL Comments, pp. 14-16. More specifically, PPL Electric showed that recovery of annual storm damages expenses of $60 million, an amount greater than any annual level of such expenses that PPL Electric had ever incurred in its history, would increase bills to residential customers by only 1.7 percent on a total bill basis. Under these circumstances, no extended period for recovery of such costs would be warranted.

No other party provided any analysis of the impact of storm damage expenses on customers. I&E and OCA, instead simply argue that a sliding scale would be appropriate to reduce impacts on bills to customers. I&E Comments, 14-16; OCA Comments, pp. 17-18. I&E and OCA provided no analysis of what whose impacts would be.

I&E also argues that the period for recovery of storm costs should be considered in a base rate case, and therefore, consideration of a rider should be deferred to the next base rate case. Thus, in responding to the Commission's third question, I&E has again contended that the Commission should postpone its consideration of an "alternative funding mechanism," which is exactly what the Commission stated in its *November Order* that it did not wish to do.

4. For purposes of the SDER, should the Commission establish a different definition for "major storm" to comply with "extraordinary, non-recurring, and unanticipated" criteria?

Based on the comments submitted by the parties, there is no need for the Commission to establish a different definition of "major storm" with regard to recovery of storm damage expenses. PPL Electric Comments, pp. 16-17; I&E Comments, p. 17; OCA Comments, p. 18-20.

5. What regulatory precedent, both in PA and in other states, exists for a "replenishing" storm reserve fund? How do other jurisdictions provide for recovery in excess of the reserve funding amounts? Should other over-recovery amounts be included, such as above authorized actual returns, in such cost recovery reserve funds?

Other parties concede that there is no precedent in Pennsylvania for storm reserve funds and replenishing such funds. I&E Comments, p. 18; OCA Comments, p. 20. PPL Electric agrees.

Regarding other states, PPL Electric reviewed the manner in which other jurisdictions provide for recovery of storm damage expenses in its Comments, pp. 17-20, relying substantially on summaries provided by the Edison Electric Institute in a publication entitled "Before and After the Storm" (January 2013). Based on this EEI summary, in states where electric utilities are permitted to establish storm reserve accounts, deficits resulting from actual expenditures in excess of reserve assets are funded by special riders or surcharges, by securitized bonds repaid through specific riders or surcharges, or through base rates. There is no predominant method for replenishing storm reserve fund deficits.

It must be emphasized, however, that many storm expense recovery mechanisms in other jurisdictions are based upon specific statutory provisions. Of course, statutes in other jurisdictions provide no authority for this Commission to adopt similar measures in Pennsylvania. For example, in certain states, securitized bonds may be used to pay for storm damages, including both expensed and capitalized costs. However, if securitized bonds were to be used in Pennsylvania for recovery of storm damage expenses, an automatic adjustment clause to repay principal and interest on those bonds would be unlawful because, absent specific statutory authority, automatic adjustment clauses may not be used to pay for capitalized costs. *Popowsky v. Pa. P.U.C.,* 869 A.2d 1144 (Pa. Cmwlth. 2005), *appeal denied*, 895 A.2d 552 (Pa. 2006) ("*Popowsky*"); *Pennsylvania Industrial Energy Coalition v. Pa. P.U.C.*, 653 A.2d 1336 (Pa. Cmwlth. 1995), *aff'd per curium*, 670 A.2d 1152 (Pa. 1996) ("*PIEC*"). Precedents from other states must be reviewed carefully in light of specific statutes in those states to determine

whether they can be applied in Pennsylvania. I&E and OCA have provided no authority for their proposed use of a base rate/reserve account method for recovery of storm damage expenses.

In responding to the Commission's question, both I&E and OCA offer the possibility of using excess earnings to pay for storm damage expenses. I&E Comments, p. 27, OCA Comments, p. 24. Neither I&E nor OCA, however, addresses the legal issues regarding such proposals under Pennsylvania law. Significantly, neither I&E nor OCA provides any Pennsylvania example of using excess earnings produced by just and reasonable rates to offset past expenses. PPL Electric believes that no such examples exist. Nor has I&E or OCA provided any Pennsylvania legal support for such an earnings sharing mechanism. PPL Electric believes that no such support exists.

Returns in excess of authorized returns should not be used to fund storm damage expenses for several reasons. First, any such action would violate the Commission-made rate doctrine. Under this doctrine, base rates, once established by a Commission order at the conclusion of a base rate proceeding, such as the Commission's determination in the *Rate Case Order*, may not be modified retroactively. No refund of a Commission-made rate is lawful. *Duquesne Light Co. v. Pa. P.U.C.*, 507 A.2d 433 (Pa. Cmwlth. 1986); *Cheltenham & Abington Sewerage Co. v. Pa. P.U.C.*, 344 Pa. 366, 25 A.2d 334 (1942); *Peoples Natural Gas Co. v. Pa. P.U.C.*, 34 A.2d 375 (Pa. Super. 1943); *West Penn Power Co. v. Pa. P.U.C.*, 100 A.2d 110 (Pa. Super. 1953).

Under this doctrine, the utility is at risk for most variances between actual and projected costs and revenues until the conclusion of the next base rate proceeding.[3] For example, if the summer air conditioning and the winter heating loads are less than projected in the prior base rate

[3] I&E states that the amount of the reserve and funding level could be reviewed in PPL Electric's next base rate proceeding and that the next base rate proceeding is expected in or before 2014. I&E Comments, p. 24. At this time, however, PPL Electric does not foresee a need to file a base rate case in or before 2014.

proceeding, the electric distribution company is not likely to achieve its allowed rate of return. The electric distribution company has no recourse for such shortfalls in revenues. Conversely, if the summer cooling and the winter heating loads are greater than projected in the prior base rate proceeding, it is possible that the electric distribution company could achieve more than its allowed rate of return. It is only fair that such risks be borne symmetrically; since the utility bears the risk of revenue shortfall, it should also realize the benefit of greater revenues. *See National Fuel, supra.*

Second, the Commonwealth Court has held that return is generally not to be reflected in automatic adjustment clauses. *See Popowsky* and *PIEC, supra.* Pursuant to these holdings, under Section 1307 of the Public Utility Code, which authorizes the establishment of automatic adjustment clauses or sliding scales of rates, return may not be considered in setting an automatic adjustment clause unless there is specific statutory authorization to do so, such as Section 1357(c) of the Public Utility Code, 66 Pa.C.S. § 1357(c), which authorizes return to be recognized in distribution system improvement charges. No such authority is contained in the Public Utility Code for storm damage reserve surcharges.

For these reasons, returns in excess of authorized levels should not be used to fund storm damage reserves.

6. Should there be a cap on the amount of costs recoverable under a storm rider or reserve account in order to insure rates are "just and reasonable?" If so, what should the amount of the cap be?

Of the parties to this proceeding, only PPLICA contends that a cap on recovery of storm damage expenses would be appropriate. PPLICA arbitrarily suggests one percent of annual distribution revenues as the cap on revenues to be charged through the SDER. PPLICA Comments, pp. 6-7. A cap of one percent of annual base rate distribution revenues, excluding

revenue for Rate Schedule LP, would be about $8 million, which is clearly inadequate based on historical annual losses, which have exceeded $57 million. I&E Statement 2, p. 35.

PPLICA's contentions are meritless for several reasons. Initially, PPLICA claims that many riders approved by the Commission incorporate upper limits. In support of this proposition, PPLICA cites page 10 of its earlier Comments that were filed in this proceeding on April 18, 2013. There, PPLICA refers to the smart meter rider and the Act 129 compliance rider. These riders contain no such limitation as PPLICA suggests. To the contrary, they use budget amounts for the initial estimate of costs to be recovered through the rider but they also contain an E or experience factor to reflect the difference between actual and estimated costs. Therefore, under these riders, the only limitation on amounts to be recovered is actual costs. The same limitation, however, would apply to the SDER. PPL Electric has proposed that actual expenses be recovered – no more and no less.

PPLICA also points to the example of the DSIC as a rider with a cap. PPLICA is correct that the DSIC contains a cap of 5 percent of total distribution revenues, not 1 percent of distribution revenues as PPLICA proposes. PPLICA, however, disregards the fact that the DSIC is an unusual rider that contains a cap and also permits recovery of capital costs, contrary to more general expense riders under Section 1307(a) of the Public Utility Code.

Nor does PPLICA address the provisions of the Public Utility Code which authorize automatic adjustment clauses. Section 1307 of the Public Utility Code makes unlawful any cap on covered expenses. Section 1307(e) requires that a public utility with an automatic adjustment clause report to the Commission annually all revenues received pursuant to the clause and "the total amount of that expense or class of expenses incurred which is the basis of the automatic adjustment clause." It does not call for the reporting of any portion or subset of an expense or

class of expense recovered through the clause. It then provides that the difference between revenues and expenses be recovered from or refunded to customers through the reconciliation process. It does not call for some portion of the expenses to be reflected in the reconciliation; it calls for the total of such expenses to be reconciled. The SDER reflects these statutory requirements; PPLICA's comments do not.

A cap on amounts to be recovered through the SDER would be inappropriate because there is no cap on the amount of storm damage expenses that PPL Electric might incur. If a cap on recovery of storm damage expenses through the SDER were imposed, the resulting recovery mechanism could not be just and reasonable.

7. Why is it appropriate to charge interest on any amortized expenses? Provide pertinent case histories on where the Commission has permitted collections of interest on similar expenses. Under PPL's Proposal, does interest accrue to customers on the $14.7M reserve as it is collected in rates?

I&E and OCA object to PPL Electric's proposal that interest be paid symmetrically on both over and undercollections of storm damage expenses. In support of their positions, they observe that interest is not accrued on damage from extraordinary storms that are recovered through base rates as an exception to the general rule against retroactive ratemaking. They also imply that symmetrical payment of interest is somehow anti-ratepayer. I&E Comments, pp. 28-29; OCA Comments, p. 25. Such contentions are incorrect.

I&E and OCA disregard the fact that the Commission is considering using a method for recovery of storm damage expenses that is different from base rates. PPL Electric has proposed an automatic adjustment clause under Section 1307 of the Public Utility Code. Automatic adjustment clauses are different from base rates, and it is typical in recent years for interest to be applied to both over and undercollections of expenses recovered through automatic adjustment

clauses.[4] There is simply no reason for the constraints of base rates to be applied to automatic adjustment clauses.

More importantly, symmetrical payment of interest on both over and undercollections of storm costs is fair to both PPL Electric and its customers. When there is an undercollection of storm damage expenses, PPL Electric should receive interest to offset the carrying costs of funds used to restore service before the costs are recovered from customers. Similarly, when there is an overcollection of storm damage expenses, PPL Electric should compensate customers for the use of their money until it is either refunded to customers or used to pay storm damage expenses. PPL Electric's proposal regarding interest is not in any way anti-ratepayer. Instead, it is fair and even-handed to ratepayers and the Company alike.[5]

8. SDER Rate Filings: Should the Commission require review and approval of the annual rates before taking effect? What precedents exist for review of similar expenses? What service requirements, comment opportunities and reporting requirements could be required in such rate filings? Should only actual or estimated expenses be included?

I&E, OCA and PPLICA all support review of rates. I&E Comments, p. 30, OCA Comments, pp. 26-28; PPLICA Comments, p. 8. These parties, however, ignore the fact that the Commonwealth Court and the Supreme Court of Pennsylvania have held that other automatic adjustment clauses with procedures identical to the proposed SDER procedures meet all statutory and due process requirements. Specifically, the Commonwealth Court and the Supreme Court of

[4] *See, e.g.*, the following automatic adjustment clauses in PPL Electric's Tariff – Electric Pa. P.U.C. No. 201: Transmission Service Charge, Generation Supply Charge – 1, Generation Supply Charge – 2, Smart Meter Rider, Universal Service Rider and the Competitive Enhancement Rider. In all of these automatic adjustment clauses, interest is applied to both over and under collections.

[5] OCA states also that the SDER "is silent on whether interest will accrue to customers on the $14.7 million of annual operating expense related to storm damage that PPL collects in base rates." OCA Comments, p. 25. OCA is incorrect. As explained in PPL Electric's Comments, p. 25, the proposed SDER provides that interest is to be computed "from the month the over or under collection occurs to the effective month that the over or under collection is recouped or refunded." Thus, each month, PPL Electric will review storm damage expenses incurred and revenues for recover of storm damage expenses under both base rates and the SDER and apply interest to the net difference.

Pennsylvania concluded that the Energy Cost Rate ("ECR") met all statutory and due process requirements.

In *Alleghany Ludlum Steel Corp. v. Pa. P.U.C.*, 67 Pa. Cmwlth. 400, 447 A.2d 675 (1982), the Commonwealth Court rejected Alleghany Ludlum's claim that the ECR, under Section 1307 of the Public Utility Code, did not provide due process to customers, even though the proposed rate became effective without Commission review or any prior hearing or opportunity for customer input. The Court concluded that the ECR was lawful because Section 1307(e) provides for review of the ECR following a public hearing with provision for refunds with interest to consumers in the event the Commission ordered downward revisions of the ECR. Due process requirements were not violated because letting the ECR become effective without prior approval does not constitute to Commission approval, and refunds are available if the increase is later held to have been unjustified. In reaching this conclusion, the Court relied on *City of Pittsburgh v. Pa. P.U.C.*, 55 Pa. Cmwlth. 177, 184-85, 423 A.2d 454, 457 (1980).

The Commonwealth Court in *Alleghany Ludlum* also relied upon Section 1312(a) of the Public Utility Code, which allows customers to bring complaints against rates set pursuant to Section 1307(e) of the Public Utility Code for up to four years after the rate was charged. Therefore, customers have protections not only through the public hearing requirement of Section 1307(e) of the Public Utility Code but also through their right to bring complaints under Section 701 of the Public Utility Code, 66 Pa.C.S. § 701, coupled with the statutory right for refunds with interest under Section 1312 when customers prove that the rate charged by the utility violated the Public Utility Code.

Alleghany Ludlum appealed the Commonwealth Court's determination to the Pennsylvania Supreme Court in *Alleghany Ludlum Steel Corp. v. Pa. P.U.C.*, 501 Pa. 71, 459 A.2d 1218 (1983). In affirming the Commonwealth Court, the Supreme Court noted that:

> [S]afeguards are, however, afforded through a subsequent, year-end automatic proceeding for final determination and adjustment of rate increases allowing full participation by all interested parties, and requiring refunds, with interest, calculated at the prevailing rate, of overpayment in the event previous ECR increases are determined to have been excessive.

Alleghany Ludlum, 501 Pa., *supra*, at 77, 459 A.2d at 1221 (footnote omitted).

The Supreme Court also noted that due process requires a balancing of competing interests. In determining that the ECR met due process requirements, the Supreme Court considered the interests of public utilities.

> The need for a public utility to receive a fair rate of return on its property to assure its continued financial integrity, necessary to achievement of the important goal of preserving modern, efficient, and dependable public service, consonant with rights of consumers, is not to be ignored. The legislature, seeking to balance these competing interests, has authorized the PUC to employ an automatic fuel cost adjustment, the ECR, to maintain a just and reasonable return.

Id. Thus, the hearing process under Section 1307(e) of the Public Utility Code and customers' rights to file complaints for refunds under Sections 701 and 1312 of the Public Utility Code, fully protect customers' rights consistent with the needs of EDCs, such as PPL Electric, to recover of storm damage expenses.

The procedures proposed for the SDER are the same as those used for many automatic adjustment clauses under Section 1307(a). Conspicuous by their absence in other parties' Comments is any mention of any problem that has arisen under automatic adjustment clauses using the review procedures proposed by PPL Electric for the SDER.

Several more specific comments are appropriate. I&E argues that the SDER should be subject to refund or recoupment. I&E Comments, p. 30. I&E's argument is curious because PPL Electric never suggested anything different. The E or experience factor is to be used to refund or recoup amounts that differ from the amount of storm damage expenses actually incurred by the Company. SDER, page 19Z.22.

PPLICA argues that the Commission should adopt procedures like those used for review of purchased gas cost recovery under Section 1307(f) of the Public Utility Code. PPLICA Comments, p. 8. PPLICA ignores the fact that those procedures are specifically mandated by statute for purchased gas costs and do not apply to storm damage or any other expenses. The statutes that do apply provide for rate filings, reports of actual expenses and revenues, hearings, and customer complaints. 66 Pa.C.S. §§ 701, 1307(a), Sectin 1307(e), 1312. In addition, the proposed SDER permits the Commission to conduct audits of the revenues and expenses. SDER, p. 19Z.24. These procedures are more than sufficient.

PPLICA also contends that further review is necessary for the Commission to review PPL Electric's "procedures and policies for projecting storm damage costs." PPLICA Comments, p. 8. PPLICA's concern is misplaced because the SDER does not contemplate any projection of storm damage expenses. Instead, it compares actual, experienced storm damage expenses with the actual level of revenues for recovery of storm damage expenses through base rates and the SDER. No projections are involved. PPLICA's contention is baseless.

9. How should storm damage rider cost be allocated among the rate classes? Should the allocation factors be included in the Tariff?

PPL Electric proposed that storm damage expenses be allocated among the rate classes based on the cost of service study approved by the Commission in the *Rate Case Order* establishing base rates effective January 1, 2013. In the base rate proceeding, issues regarding

the allocation of costs of service were thoroughly litigated by all parties, including I&E, OCA and PPLICA. PPL Electric sees no reason to revisit the allocation of storm damage expenses so soon after the Commission has thoroughly and definitely addressed exactly the same issues. Significantly, expenses from Hurricanes Ike and Lee and expenses from the October "Halloween" snow storm were reflected in the cost of service studies in that proceeding. Therefore, the allocation of storm damage expenses was subject to the Commission's *Rate Case Order*.

I&E agrees that storm damage expenses should be allocated based on the cost of service study approved by the Commission in the *Rate Case Order*. I&E Comments, p. 31.

PPLICA's position is internally inconsistent. It supports use of the rate case cost of service study. It states that use of the study represents principles of causation. PPLICA Comments, p. 9. PPLICA continues, however, by proposing that customers under Rate Schedule LP-5, who receive service at 69 kV or higher, be exempted from the SDER, even though the cost of service study it supports allocates a small amount (0.2%) of storm damage expenses to that rate class. Although PPLICA seems to support allocations based on principles of cost causation, it also advocates a materiality test for large customers under Rate Schedule LP-5. Although PPLICA asks for exemption of the portion of the SDER applicable to customers under Rate Schedule LP-5, it offers no alternative suggestion as to how or from whom costs properly allocable to customers under Rate Schedule LP-5 should be recovered. PPLICA's contention, that the cost of service study should be used only when it benefits its members and should be rejected when PPLICA perceives it as adverse to its members, is meritless and should be rejected.

OCA is the only party which asks that the Commission discard the very same cost of service study that it approved for PPL Electric in the *Rate Case Order*, and instead allocate storm damage expenses on the basis of Kwh or energy. Obviously, the effect of using an energy allocation would be to shift much more revenue requirement to the large industrial customers who use substantial amounts of energy, which would benefit residential customers.

OCA's rationale for its proposal is that: "All customers benefit from the operation of the distribution system." OCA Comments, p. 28. OCA's rationale, however, makes little sense. If OCA's proposal had validity, there would be no reason to conduct a cost of service study. The entire cost of service could by allocated on an energy basis, but such an allocation would clearly be contrary to cost causation principles. Such an allocation was not even presented in the rate proceeding.

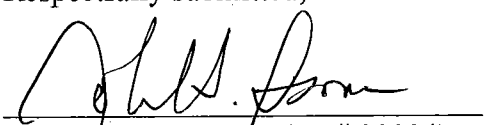
Further, although all customers may benefit from the operation of the distribution system, that observation provides no basis for allocating storm damage expenses on an energy basis. The observation could just as easily justify allocation on a customer basis, which would not be beneficial to residential customers.

Most importantly, OCA's proposal would be directly contrary to the holding of the Commonwealth Court in *Lloyd v. Pa. P.U.C.*, 904 A.2d 1010 (Pa. Cmwlth. 2006), *appeal denied*, 591 Pa. 676, 916 A.2d 1104(2007) ("*Lloyd*"), where the Court held that the "polestar" of allocating costs of service must be cost causation principles. OCA's suggestion that the Commission disregard the cost of service study it approved so recently in another phase of the same proceeding should be rejected.

II. CONCLUSION

PPL Electric appreciates this opportunity to submit these Reply Comments in response to the Comments of other parties. For the reasons fully explained above and in PPL Electric's earlier Comments, PPL Electric believes that its proposed Storm Damage Expense Rider, as modified by its earlier Comments, is in the public interest and is consistent with sound ratemaking principles, all applicable provisions of the Public Utility Code, and the Commission's orders in this proceeding. Therefore, PPL Electric respectfully requests that the Commission adopt the modified Storm Damage Expense Rider.

Respectfully submitted,



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