

PENNSYLVANIA PUBLIC UTILITY COMMISSION

v.

METROPOLITAN EDISON COMPANY
Docket No. R-2016-2537349

PENNSYLVANIA ELECTRIC COMPANY
Docket No. R-2016-2537352

PENNSYLVANIA POWER COMPANY
Docket No. R-2016-2537355

WEST PENN POWER COMPANY
Docket No. R-2016-2537359

Surrebuttal Testimony

of

Lisa A. Gumby

Bureau of Investigation & Enforcement

Concerning:

OPERATING & MAINTENANCE EXPENSES
CASH WORKING CAPITAL

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1 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A. My name is Lisa A. Gumby. My business address is Pennsylvania Public Utility
3 Commission, P.O. Box 3265, Harrisburg, PA 17105-3265.

4
5 **Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

6 A. I am employed by the Pennsylvania Public Utility Commission in the Bureau of
7 Investigation and Enforcement (I&E) as a Fixed Utility Valuation Engineer.

8
9 **Q. ARE YOU THE SAME LISA A. GUMBY THAT SUBMITTED**
10 **TESTIMONY IN I&E STATEMENT NO. 2 AND I&E EXHIBIT NO. 2?**

11 A. Yes.

12
13 **Q. WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?**

14 A. The purpose of my surrebuttal testimony is to respond to the rebuttal testimony of
15 the First Energy companies' (First Energy or Company) witnesses Richard A.
16 D'Angelo (First Energy Statement No. 2-R) and Jeffrey L. Adams (First Energy
17 Statement No. 5-R).

18
19 **Q. DOES YOUR SURREBUTTAL INCLUDE AN ACCOMPANYING**
20 **EXHIBIT?**

21 A. Yes. I have an accompanying exhibit, I&E Exhibit No. 2-SR, included with this
22 surrebuttal testimony. However, I will also refer to my direct testimony and its

1 accompanying exhibit in this surrebuttal testimony (I&E Statement No. 2 and I&E
2 Exhibit No. 2).

3
4 **Q. HOW IS YOUR SURREBUTTAL TESTIMONY ORGANIZED?**

5 A. I will first respond to First Energy witness Richard A. D'Angelo on the subject of
6 my operating and maintenance (O&M) expense recommendations. I will then
7 respond to First Energy witness Jeffrey L. Adams on the subject of my cash
8 working capital (CWC) adjustment.

9
10 **Q. HAS THE COMPANY ACCEPTED ANY OF YOUR ADJUSTMENTS?**

11 A. Yes, to an extent. Mr. D'Angelo accepted a vacancy adjustment, in concept, but
12 with an alternate vacancy rate proposal (First Energy Statement No. 2-R, pp. 7-8,
13 24-25 and Exhibit RAD-72). Additionally, no Company witnesses responded to
14 my adjustments for Relocation Expense or Other Payroll, so in absence of a
15 rebuttal position, I assume that these adjustments are acceptable as recommended.

16
17 **SUMMARY OF O&M AND RATE BASE ADJUSTMENTS**

18 **Q. PLEASE SUMMARIZE YOUR ADJUSTMENTS.**

19 A. The following tables summarize my recommended adjustments.

Met-Ed

Met-Ed			
O&M	Company Claim	I&E Recommendation	Adjustment
Payroll Expense	\$30,987,000 ¹	\$29,875,856	(\$1,111,144)
Benefits Expense	\$4,488,000 ¹	\$4,482,482	(\$5,518)
Other Payroll Expense	\$219,303	\$134,777	(\$84,526)
Rate Case Expense	\$274,000	\$68,500	(\$205,500)
Advertising Expense	\$344,000	\$183,000	(\$161,000)
Relocation Expenses	\$146,822	\$16,324	(\$130,498)
Total O&M Adjustments:			(\$1,698,186)
Rate Base	Company Claim	I&E Recommendation	Adjustment
Payroll Capitalized	\$36,789,957 ¹	\$36,721,185 ²	(\$68,772)
Benefits Capitalized	\$5,328,637 ¹	\$5,322,454	(\$6,183)
Other Payroll Capitalized	\$260,362	\$160,011	(\$100,351)
Cash Working Capital	\$134,868,000	\$78,644,000	(\$56,224,000)
Total Rate Base Adjustments:			(\$56,399,306)

1. Met-Ed Claims for payroll and benefit costs are reduced by the Met-Ed vacancy adjustment (Met-Ed Exhibit RAD-72).
2. I&E Recommendation for capitalized payroll is increased to reflect removal of the capitalized payroll adjustment related to post-FPFTY payroll increases, \$790,317.

Penelec

Penelec			
O&M	Company Claim	I&E Recommendation	Adjustment
Payroll Expense	\$37,319,000 ¹	\$34,846,287	(\$2,472,713)
Benefits Expense	\$5,695,000 ¹	\$5,519,434	(\$175,566)
Other Payroll Expense	\$292,477	\$147,218	(\$145,259)
Rate Case Expense	\$285,000	\$71,250	(\$213,750)
Advertising Expense	\$405,000	\$159,000	(\$246,000)
Relocation Expenses	\$161,230	\$56,497	(\$104,733)
Total O&M Adjustments:			(\$3,358,021)
Rate Base	Company Claim	I&E Recommendation	Adjustment
Payroll Capitalized	\$37,982,128 ¹	\$36,824,845 ²	(\$1,157,283)
Benefits Capitalized	\$5,795,145 ¹	\$5,616,730	(\$178,415)
Other Payroll Capitalized	\$297,671	\$149,832	(\$147,839)
Cash Working Capital	\$177,979,000	\$95,370,000	(\$82,609,000)
Total Rate Base Adjustments:			(\$84,092,537)

1. Penelec Claims for payroll and benefit costs are reduced by the Penelec vacancy adjustment (Penelec Exhibit RAD-72).
2. I&E Recommendation for capitalized payroll is increased to reflect removal of the capitalized payroll adjustment related to post-FPFTY payroll increases, \$917,504.

Penn Power

Penn Power			
O&M	Company Claim	I&E Recommendation	Adjustment
Payroll Expense	\$8,277,813 ¹	\$8,023,363	(\$254,450)
Benefits Expense	\$1,699,341 ¹	\$1,711,954	\$12,613
Rate Case Expense	\$81,000	\$20,250	(\$60,750)
Advertising Expense	\$191,000	\$67,000	(\$124,000)
Relocation Expenses	\$40,782	\$6,849	(\$33,933)
Total O&M Adjustments:			(\$460,520)
Rate Base	Company Claim	I&E Recommendation	Adjustment
Payroll Capitalized	\$9,840,462 ¹	\$9,902,230 ²	\$61,768
Benefits Capitalized	\$2,019,463 ¹	\$2,034,456	\$14,993
Cash Working Capital	\$28,906,000	\$22,277,000	(\$6,629,000)
Total Rate Base Adjustments:			(\$6,552,239)

1. Penn Power Claims for payroll and benefit costs are reduced by the Penn Power vacancy adjustment (Penn Power Exhibit RAD-72).
2. I&E Recommendation for capitalized payroll is increased to reflect removal of the capitalized payroll adjustment related to post-FPPTY payroll increases, \$221,585.

West Penn

West Penn			
O&M	Company Claim	I&E Recommendation	Adjustment
Payroll Expense	\$33,734,485 ¹	\$31,226,316	(\$2,508,169)
Benefits Expense	\$5,040,474 ¹	\$4,851,029	(\$189,445)
Other Payroll Expense	\$194,579	\$24,879	(\$169,700)
Rate Case Expense	\$353,000	\$88,250	(\$264,750)
Advertising Expense	\$316,000	\$96,000	(\$220,000)
Relocation Expenses	\$151,018	\$16,447	(\$134,571)
Total O&M Adjustments:			(\$3,486,635)
Rate Base	Company Claim	I&E Recommendation	Adjustment
Payroll Capitalized	\$33,065,842 ¹	\$31,860,357 ²	(\$1,205,485)
Benefits Capitalized	\$4,940,683 ¹	\$4,754,989	(\$185,694)
Other Payroll Capitalized	\$190,725	\$24,386	(\$166,339)
Cash Working Capital	\$123,226,000	\$84,323,000	(\$38,903,000)
Total Rate Base Adjustments:			(\$40,460,518)

1. West Penn Claims for payroll and benefit costs are reduced by the West Penn vacancy adjustment (West Penn Exhibit RAD-72).
2. I&E Recommendation for capitalized payroll is increased to reflect removal of the capitalized payroll adjustment related to post-FPFTY payroll increases, \$725,670.

PAYROLL AND BENEFITS

Q. SUMMARIZE YOUR RECOMMENDATION IN DIRECT TESTIMONY FOR PAYROLL AND BENEFITS.

A. I addressed two issues affecting the Companies' payroll and benefit claims: (1) pay increases with effective dates beyond the end of the fully projected future test year (FPFTY) ending December 31, 2017; and (2) a vacancy rate adjustment based on historic vacancy levels. My recommended total allowances in direct testimony for payroll expense, benefits expense, capitalized payroll, and capitalized benefits are as follows:

Met-Ed

Met-Ed (I&E Statement No. 2, p. 3)			
O&M	Company Claim	I&E Recommendation	Adjustment
Payroll Expense	\$31,097,000	\$29,875,856	(\$1,221,144)
Benefits Expense	\$4,504,000	\$4,482,482	(\$21,518)
Total Payroll & Benefits O&M Adjustments:			<u>(\$1,242,622)</u>
Rate Base	Company Claim	I&E Recommendation	Adjustment
Payroll Capitalized	\$36,920,000	\$35,930,868	(\$989,132)
Benefits Capitalized	\$5,348,000	\$5,322,454	(\$25,546)
Total Payroll & Benefits Rate Base Adjustments:			<u>(\$1,014,678)</u>

1 **Penelec**

Penelec (I&E Statement No. 2, p. 4)			
O&M	Company Claim	I&E Recommendation	Adjustment
Payroll Expense	\$37,530,000	\$34,846,287	(\$2,683,713)
Benefits Expense	\$5,728,000	\$5,519,434	(\$208,566)
Total Payroll & Benefits O&M Adjustments:			<u>(\$2,892,279)</u>
Rate Base	Company Claim	I&E Recommendation	Adjustment
Payroll Capitalized	\$38,197,000	\$35,907,341	(\$2,289,659)
Benefits Capitalized	\$5,829,000	\$5,616,730	(\$212,270)
Total Payroll & Benefits Rate Base Adjustments:			<u>(\$2,501,929)</u>

2

3

4 **Penn Power**

Penn Power (I&E Statement No. 2, p. 5)			
O&M	Company Claim	I&E Recommendation	Adjustment
Payroll Expense	\$8,550,000	\$8,023,363	(\$526,637)
Benefits Expense	\$1,757,000	\$1,711,954	(\$45,046)
Total Payroll & Benefits O&M Adjustments:			<u>(\$571,683)</u>
Rate Base	Company Claim	I&E Recommendation	Adjustment
Payroll Capitalized	\$10,164,000	\$9,680,645	(\$483,355)
Benefits Capitalized	\$2,088,000	\$2,034,456	(\$53,544)
Total Payroll & Benefits Rate Base Adjustments:			<u>(\$536,899)</u>

5

West Penn

West Penn (I&E Statement No. 2, p. 6)			
O&M	Company Claim	I&E Recommendation	Adjustment
Payroll Expense	\$33,803,000	\$31,226,316	(\$2,576,684)
Benefits Expense	\$5,051,000	\$4,851,029	(\$199,971)
Total Payroll & Benefits O&M Adjustments:			<u>(\$2,776,655)</u>
Rate Base	Company Claim	I&E Recommendation	Adjustment
Payroll Capitalized	\$33,133,000	\$31,134,687	(\$1,998,313)
Benefits Capitalized	\$4,951,000	\$4,754,989	(\$196,011)
Total Payroll & Benefits Rate Base Adjustments:			<u>(\$2,194,324)</u>

Q. WHAT WERE YOUR ADJUSTMENTS FOR PAY INCREASES BEYOND THE END OF THE FPFTY?

A. The adjustments for pay increases beyond the end of the FPFTY are as follows:

O&M/Capital Allocations (I&E Statement No. 2, p. 10)					
Company	Category	Amount		O&M	Capital
Met-Ed Allocated Post-FPFTY Payroll Increases				\$1,053,683	\$ 790,317
Penelec Allocated Post-FPFTY Payroll Increases				\$1,335,496	\$ 917,504
Penn Power Allocated Post-FPFTY Payroll Increases				\$ 306,415	\$ 221,585
West Penn Allocated Post-FPFTY Payroll Increases				\$1,278,330	\$ 725,670

1 **Q. DID ANY FIRST ENERGY WITNESS SUBMIT REBUTTAL TESTIMONY**
2 **IN RESPONSE TO YOUR RECOMMENDATION TO DISALLOW PAY**
3 **INCREASES BEYOND THE END OF THE FPFTY?**

4 A. Yes. First Energy witness Richard A. D'Angelo (First Energy Statement No. 2-R,
5 pp. 16, 21-22) disagreed with my recommendation.
6

7 **Q. SUMMARIZE MR. D'ANGELO'S RESPONSE IN REBUTTAL**
8 **TESTIMONY.**

9 A. Mr. D'Angelo first addresses my adjustment for a capitalized portion of pay
10 increases beyond the end of the FPFTY. He argues that the Companies' post-
11 FPFTY pay increases were not included in capitalized wage claims and, therefore,
12 my recommendation to adjust for a capitalized portion of post-FPFTY wage
13 increases should be disallowed (First Energy Statement No. 2-R, p. 16).

14 Secondly, Mr. D'Angelo reiterates his position that the Commission has
15 held that known and measurable payroll increases beyond the test year that were
16 contractually required under collective bargaining agreements or were reasonable
17 management actions are appropriate adjustments (First Energy Statement No. 2-R,
18 pp. 21-22). He further opines that since these increases occur within a relatively
19 short time beyond the FPFTY ending December 31, 2017, the Companies'
20 proposed post-FPFTY pay increases fall well within reasonable bounds based on
21 prior Commission precedent (First Energy Statement No. 2-R, p. 22).

1 **Q. DOES MR. D'ANGELO'S REBUTTAL TESTIMONY REGARDING POST-**
2 **FPFTY PAY INCREASES AFFECT YOUR RECOMMENDATION IN**
3 **DIRECT TESTIMONY?**

4 A. Yes, in part. I agree with Mr. D'Angelo's recommendation to disallow my
5 capitalized portion of the post-FPFTY pay increases. Since the rate base additions
6 are claimed only to the end of the FPFTY, it is logical that the claimed plant
7 additions were not adjusted for pay increases subsequent to the conclusion of the
8 FPFTY ending December 31, 2017. My recommendation is adjusted in the
9 summary of adjustments herein to remove the claimed capitalized share of post-
10 FPFTY pay increases.

11 Regarding Mr. D'Angelo's opinion that the post-FPFTY pay increases
12 should be allowed based on prior Commission precedent, I disagree. Mr.
13 D'Angelo's references to Commission precedent predate the existence of the
14 FPFTY, which already allows annualization of pay increases that are not in effect
15 at the time rates go into effect (I&E Statement No. 2, pp. 11-12). It is
16 unreasonable to assess ratepayers the costs of post-FPFTY expenses when
17 ratepayers will already be paying rates in excess of actual expenses when rates go
18 into effect. Accordingly, I continue to recommend disallowance of all of the post-
19 FPFTY pay increases as summarized herein and as detailed in my direct testimony
20 (I&E Statement No. 2, pp. 7-12).

**Q. WHAT WERE YOUR PAYROLL AND BENEFIT ADJUSTMENTS TO
RECOGNIZE HISTORIC VACANCY LEVELS?**

A. The adjustments to recognize historic vacancy levels for payroll and benefits are
as follows:

O&M/Capital Allocations Payroll Vacancy Adjustment (I&E Statement No. 2, p. 13)					
Company	Category	Amount		O&M	Capital
Met-Ed Allocated Payroll Vacancy Adjustment				\$ 167,461	\$ 198,815
Penelec Allocated Payroll Vacancy Adjustment				\$1,348,217	\$1,372,155
Penn Power Allocated Payroll Vacancy Adjustment				\$ 220,222	\$ 261,770
West Penn Allocated Payroll Vacancy Adjustment				\$1,298,354	\$1,272,643

O&M/Capital Allocations Benefit Vacancy Adjustment (I&E Statement No. 2, p. 16)					
Company	Category	Amount		O&M	Capital
Met-Ed Allocated Benefit Vacancy Adjustment				\$ 21,518	\$ 25,546
Penelec Allocated Benefit Vacancy Adjustment				\$ 208,566	\$ 212,270
Penn Power Allocated Benefit Vacancy Adjustment				\$ 45,046	\$ 53,544
West Penn Allocated Benefit Vacancy Adjustment				\$ 199,971	\$ 196,011

1 **Q. WHAT WAS THE BASIS FOR YOUR HISTORIC VACANCY LEVEL**
2 **ADJUSTMENTS TO PAYROLL AND BENEFITS?**

3 A. I calculated an average historic vacancy adjustment based on data supplied by the
4 Companies for January 2014 through May 2016. I utilized the average vacancy
5 rate to establish anticipated FPFTY vacancies, which I multiplied by the average
6 salary and benefit costs to establish my recommended adjustments (I&E Statement
7 No. 2, pp. 12-17, I&E Exhibit No. 2, Schedule 2, Schedule 3).

8
9 **Q. DID ANY FIRST ENERGY WITNESS SUBMIT REBUTTAL TESTIMONY**
10 **IN RESPONSE TO YOUR RECOMMENDATION TO ADJUST PAYROLL**
11 **AND BENEFIT COSTS TO RECOGNIZE A HISTORIC VACANCY RATE?**

12 A. Yes. First Energy witness Richard A. D'Angelo (First Energy Statement No. 2-R,
13 pp. 24-25) responded to my recommendation.

14
15 **Q. SUMMARIZE MR. D'ANGELO'S RESPONSE IN REBUTTAL**
16 **TESTIMONY.**

17 A. Mr. D'Angelo agrees with the concept of a vacancy rate adjustment; however, he
18 opines that the Companies have enhanced the budgeting processes to reduce
19 shortfalls between budgeted and filled positions (First Energy Statement No. 2-R,
20 p. 24). It is Mr. D'Angelo's contention that to recognize an accurate vacancy
21 adjustment, a much shorter period of time should be utilized to capture the
22 Companies' enhanced budgeting processes. He proposes a vacancy adjustment

1 based only on staffing history from January 2016 through May 2016 (Met-
2 Ed/Penelec/Penn Power/West Penn Exhibit RAD-72).

3
4 **Q. DOES MR. D'ANGELO'S REBUTTAL TESTIMONY REGARDING**
5 **HISTORIC VACANCY RATES AFFECT YOUR RECOMMENDATION IN**
6 **DIRECT TESTIMONY?**

7 A. No. Historic vacancy rates have less to do with a company's budgeting process
8 than with the general employment and economic climate. I used the Companies'
9 historic staffed versus budgeted positions to capture the effect of the Companies'
10 ability to sustain full staffing through historic employment trends. While I used
11 the months' of data that I had available to me, January 2014 through May 2016, in
12 reality a longer period of time would provide a more accurate picture of the impact
13 of economic conditions on staffing over a historic period. If I had more data
14 available, I would actually recommend a longer period, five to ten years, to
15 establish a historic vacancy rate.

16 Interestingly, three of the four First Energy companies, Penelec, Penn
17 Power, and West Penn, had resulting vacancy rates of 3-4%, which is
18 extraordinarily close to the Bureau of Labor Statistics June 2016 reported total
19 separation rate of 3.4% (I&E Exhibit No. 2-SR, Schedule 1). Accordingly, I
20 continue to recommend the historic vacancy rate payroll and benefit adjustments
21 summarized herein and as detailed in my direct testimony (I&E Statement No. 2,
22 pp. 12-17).

1 **Q. DOES MR. D'ANGELO'S PROPOSED VACANCY ADJUSTMENT**
2 **AFFECT YOUR RECOMMENDATION IN DIRECT TESTIMONY?**

3 A. No. However, the net proposed claim reduction is reduced by inclusion of Mr.
4 D'Angelo's vacancy adjustments in the Companies' original claims. The impact
5 of the revised payroll and benefit claims are reflected in my summary of
6 adjustments herein.

7
8 **RATE CASE EXPENSE**

9 **Q. SUMMARIZE YOUR RECOMMENDATIONS IN DIRECT TESTIMONY**
10 **FOR RATE CASE EXPENSE.**

11 A. I recommended an eight-year normalization period based on the historic filing
12 record (I&E Statement No. 2, pp. 26-31). My recommended rate case expense
13 allowances for the Companies are as follows (I&E Statement No. 2, p. 26):

14	Met-Ed:	\$68,500
15	Penelec:	\$71,250
16	Penn Power:	\$60,750
17	West Penn:	\$88,250

18
19 **Q. WHAT IS THE BASIS FOR YOUR RECOMMENDATION FOR RATE**
20 **CASE EXPENSE?**

21 A. The basis of my recommendation is a result of revising the claimed rate case
22 interval from two years to eight years (I&E Statement No. 2, pp. 25-26).

1 **Q. DID ANY COMPANY WITNESS SUBMIT REBUTTAL TESTIMONY IN**
2 **RESPONSE TO YOUR RECOMMENDATION?**

3 A. Yes. First Energy witness Richard A. D'Angelo (First Energy Statement No. 2-R,
4 pp. 17-18) disagreed with my recommendation.
5

6 **Q. SUMMARIZE MR. D'ANGELO'S RESPONSE IN REBUTTAL**
7 **TESTIMONY.**

8 A. Mr. D'Angelo opines that the Companies' likelihood of reaching the distribution
9 system improvement charge (DSIC) cap within 2-3 years makes a rate case
10 interval of eight years unlikely (First Energy Statement No. 2-R, p. 18).
11 Additionally, Mr. D'Angelo cites to my direct testimony regarding the
12 Commission's December 28, 2012 Order in PPL Electric Utilities' (PPL) 2012
13 base rate case at Docket No. R-2012-2290597, which he opines supports a
14 normalization period far shorter than that calculated based on historical data (First
15 Energy Statement No. 2-R, p. 18).
16

17 **Q. DOES MR. D'ANGELO'S REBUTTAL TESTIMONY AFFECT YOUR**
18 **RECOMMENDATION IN DIRECT TESTIMONY REGARDING THE**
19 **RATE CASE INTERVAL?**

20 A. No. Despite Mr. D'Angelo's continued insistence that a two-year rate case
21 interval is appropriate, the Companies' historic record does not support
22 authorization of a two-year rate case interval. In fact, the recommended eight-year

1 rate case interval is generous with respect to Penelec's and Penn Power's historic
2 intervals, ten years and 14 years, respectively (I&E Statement No. 2, pp. 26-30).

3 Additionally, Mr. D'Angelo's reference to my testimony regarding the PPL
4 2012 base rate case as actually supporting the Company's claim is inaccurate. My
5 direct testimony indicates how the reliance on the company's stated intentions
6 failed in that instance. While the Commission accepted the PPL's stated intentions
7 in assigning the rate case interval, PPL did not, in fact, perform to its stated
8 intentions. Its subsequent base rate case did not occur at the stated two-year
9 interval, but rather 36 months after the 2012 base rate case, which was a full four
10 months longer than the interval recommended by I&E utilizing the historic record
11 (I&E Statement No. 2, pp. 31-33).

12
13 **Q. DO YOU HAVE ANY CHANGES TO YOUR RECOMMENDATION FOR**
14 **RATE CASE EXPENSE?**

15 A. No.

16
17 **ADVERTISING EXPENSE**

18 **Q. SUMMARIZE YOUR RECOMMENDATIONS IN DIRECT TESTIMONY**
19 **FOR ADVERTISING EXPENSE.**

20 A. I recommended an allowance for advertising expense equal to that claimed in the
21 historic test year (HTY) (I&E Statement No. 2, pp. 34-36). My recommended

advertising expense allowances for the Companies are as follows (I&E Statement No. 2, p. 35):

Met-Ed:	\$183,000
Penelec:	\$159,000
Penn Power:	\$67,000
West Penn:	\$96,000

Q. WHAT IS THE BASIS FOR YOUR RECOMMENDATION FOR ADVERTISING EXPENSE?

A. The basis of my recommendation is a result of excluding the large expense increases from the HTY to the FPFTY, which the Companies attributed to smart meter advertising. I do not believe it is reasonable to assess additional base rate expenses for smart meter advertising when the Companies admit that the amounts established in base rates at the last base rate case have not been utilized (I&E Statement No. 2, pp. 35-36).

Q. DID ANY COMPANY WITNESS SUBMIT REBUTTAL TESTIMONY IN RESPONSE TO YOUR RECOMMENDATION?

A. Yes. First Energy witness Richard A. D'Angelo (First Energy Statement No. 2-R, pp. 27-29) disagreed with my recommendation.

1 **Q. SUMMARIZE MR. D'ANGELO'S RESPONSE IN REBUTTAL**
2 **TESTIMONY.**

3 A. Mr. D'Angelo opines that the Companies are entitled to recover the costs of
4 Commission-mandated smart meter advertising costs and that disallowing only
5 this increase in smart meter advertising costs that is part of the new baseline is
6 unreasonable (First Energy Statement No. 2-R, pp. 27-28). He further opines that
7 implying that this one cost can be recovered via the SMT-C Rider exclusive of
8 other costs is a pointless anomaly outside of the intent of inclusion of smart meter
9 costs in base rates (First Energy Statement No. 2-R, pp. 28-29).

11 **Q. DOES MR. D'ANGELO'S REBUTTAL TESTIMONY AFFECT YOUR**
12 **RECOMMENDATION IN DIRECT TESTIMONY REGARDING**
13 **ADVERTISING EXPENSE?**

14 A. No. Mr. D'Angelo misconstrues my position that increases in advertising
15 expenses can ultimately be recovered via the SMT-C Rider. I was not implying
16 that the Companies activate the rider for this one cost element but rather that the
17 new baseline is adjusted by my recommended downward adjustment to advertising
18 expense. Since the SMT-C rider remains set to zero until the embedded base rate
19 revenue amounts are exceeded (Met-Ed/Penelec/Penn Power/West Penn Statement
20 No. 6, p. 7), it is feasible that through appropriate rate case timing, and the
21 corresponding baseline readjustment, that ratepayers may never receive any

benefit from the overcollections accumulating from smart meter excess revenue recovery.

Q. DO YOU HAVE ANY CHANGES TO YOUR RECOMMENDATION FOR ADVERTISING EXPENSE?

A. No.

CASH WORKING CAPITAL

Q. SUMMARIZE YOUR RECOMMENDATION IN DIRECT TESTIMONY CONCERNING CASH WORKING CAPITAL (CWC).

A. I recommended an allowance for CWC that excluded unamortized cash pension contributions from the CWC calculation (I&E Statement No. 2, pp. 40-43). My recommended CWC allowances for the Companies are as follows (I&E Statement No. 2, p. 40):

Met Ed:	\$78,644,000
Penelec:	\$95,370,000
Penn Power:	\$22,277,000
West Penn:	\$84,323,000

Q. WHAT IS THE BASIS FOR YOUR RECOMMENDATION FOR CWC?

A. The Companies did not obtain prior Commission approval to include a return on unamortized cash pension contributions, and neither the need to make such

1 prepayments nor the rationale for the proposed 10-year amortization period was
2 explained. Lastly, the Companies will receive more in pension expense recovery
3 amounts than will be paid in the FPFTY - none of the Companies plan to make an
4 actual payment in the FPFTY (I&E PROPRIETARY Exhibit No. 2, Schedule 13,
5 p. 3).
6

7 **Q. DID ANY COMPANY WITNESS SUBMIT REBUTTAL TESTIMONY IN**
8 **RESPONSE TO YOUR RECOMMENDATION?**

9 A. Yes. First Energy witness Jeffrey L. Adams (First Energy Statement No. 5-R, pp.
10 4-9) disagreed with my recommendation.
11

12 **Q. SUMMARIZE MR. ADAMS' RESPONSE IN REBUTTAL TESTIMONY.**

13 A. Mr. Adams opines that I misunderstand why unamortized cash pension
14 contributions are included in the Companies' CWC requirements as prepayments
15 in accordance with the Commission's approved normalization of cash pension
16 contributions in the 2006 Order.

17 Mr. Adams states that CWC represents the cash invested by a utility from
18 the time between when the expense payment is made to when the expenditure is
19 recovered in rates, and that the prepayment for cash pension contributions will not
20 be recovered from ratepayers until the Commission-approved normalization
21 completes its ten-year cycle.

1 Additionally, Mr. Adams opines that cash pension contributions are similar
2 to plant and equipment as they are made for the benefit of customers and should
3 receive a rate of return equal to the Companies' cost of capital. It is his opinion
4 that failure to do so would result in a loss based on the time from when the
5 payment is made to the time when it is recovered in rates.

6 Further, Mr. Adams opines that the 2006 Order for the normalization of
7 pension expense to the average ten years of actual contributions is the equivalent
8 of a ten-year amortization of each cash payment to the pension fund and represents
9 a regulatory prepayment. It is his opinion that ratepayers benefit by the "leveling"
10 effect of the amortization as it defers recovery for up to ten years.

11
12 **Q. DO YOU AGREE THAT THE UNAMORTIZED CASH PENSION**
13 **CONTRIBUTIONS SHOULD BE TREATED AS PREPAYMENTS FOR**
14 **CWC PURPOSES?**

15 A. No. While the Companies may determine that payments should be made which
16 exceed minimum funding requirements in certain years, those discretionary
17 payments are not properly classified as a component of CWC and thus should not
18 be eligible to earn a rate of return.

19
20 **Q. DOES THE 2006 ORDER SPECIFICALLY PERMIT THE COMPANIES**
21 **TO RECOVER A RETURN FOR UNAMORTIZED CASH PENSION**
22 **CONTRIBUTIONS?**

1 A. No. As I stated in my direct testimony, the Companies did not receive approval
2 from the Commission to receive a return on cash pension contributions. If they
3 had received such permission, it would have been in error as normalization of
4 expense does not result in permission to apply rate base treatment. The
5 Companies only received approval from the Commission to utilize a normalization
6 methodology for recovery of pension expense over a ten year period (Commission
7 Opinion and Order at Docket No. R-00061366, Issued on January 11, 2007, p. 93).
8 The Commission did not grant an amortization of any cash pension contributions.
9

10 **Q. IS MR. ADAMS MISCHARACTERIZING THE 2006 COMMISSION**
11 **ORDER?**

12 A. Yes. The Commission Order indicated that it was acceptable for the Companies to
13 utilize a normalization methodology based on a ten-year average of historic
14 pension contributions; however, what Mr. Adams fails to acknowledge is that
15 normalization of expenses generally does not provide for any portion of the
16 expense to be applied to rate base earning a rate of return.
17

18 **Q. IS IT ACCURATE TO COMPARE THE NORMALIZATION OF CASH**
19 **PENSION CONTRIBUTIONS TO PLANT AND EQUIPMENT?**

20 A. No. Unlike plant and equipment, cash pension contributions relate to an operating
21 expense which should not be subject to rate base treatment. The contributions
22 made to the pension funds are invested and receive a rate of return inside the

1 pension fund(s). Furthermore, while Mr. Adams is correct that ratepayers may
2 benefit from the leveling in cash pension contributions (expense) if actual
3 contributions are greater than the historic ten-year cycle used to determine pension
4 expense in a base rate case, the opposite could be said if the Companies make
5 smaller cash payments after a rate case than the ten-year historic average for
6 pension expense.

7 As Mr. Adams states in his testimony, "If future contributions differ from
8 the levelized expense amount, the calculation of the ten-year expense
9 normalization in a subsequent base rate case will adjust for that variance" (First
10 Energy Statement No. 5-R, p. 9). Thus, it is unnecessary for the Company to earn
11 a rate of return on cash pension contributions as the appropriate adjustments will
12 be made in the next base rate case.

13
14 **Q. DOES MR. ADAMS' REBUTTAL TESTIMONY AFFECT YOUR**
15 **RECOMMENDATION IN DIRECT TESTIMONY REGARDING CWC?**

16 A. No. I continue to recommend disallowance of the Company's inclusion of prepaid
17 cash pension contributions in CWC. The Company is already receiving an
18 appropriate amount of pension expense resulting in more money in rates than
19 actually necessary to fund the FPFTY contributions to its plan as none of the
20 Companies actually plan to make a payment in the FPFTY.

SUMMARY OF I&E'S LITIGATION POSITION

**Q. WHAT IS I&E'S TOTAL REVENUE REQUIREMENT
RECOMMENDATION?**

A. Met-Ed

I&E's total base rate revenue recommendation for Met-Ed is \$446,674,000, which represents an increase of \$93,118,000 to present rate revenues of \$353,556,000 (Met-Ed Ex. RAD-2, p. 1). This amount includes the recommendations of all I&E witnesses presented in direct testimony.

Metropolitan Edison Company
R-2016-2537349
INVESTIGATION & ENFORCEMENT

	12/31/17 Proforma Present Rates \$ (000)	Adjustments \$ (000)	Present Rates \$ (000)	Allowances \$ (000)	Proposed \$ (000)
Operating Revenue	353,556	0	353,556	93,118	446,674
Deductions:					
O&M Expenses	121,462	-1,699	119,763	0	119,763
Depreciation	118,205	0	118,205		118,205
Taxes, Other	23,472	0	23,472	5,494	28,966
Income Taxes:					
Current State	10,639	364	11,003	8,754	19,757
Current Federal	27,376	1,149	28,525	27,605	56,130
Deferred Taxes	12,561	0	12,561		12,561
ITC	-372	0	-372		-372
Total Deductions	313,343	-186	313,157	41,853	355,010
Income Available	40,213	186	40,399	51,266	91,665
Measure of Value	1,386,312	-56,399	1,329,913	0	1,329,913
Rate of Return	2.90%		3.04%		6.89%

Penelec

I&E's total base rate revenue recommendation for Penelec is \$474,861,000, which represents an increase of \$93,894,000 to present rate revenues of \$380,967,000 (Penelec Ex. RAD-2, p. 1). This amount includes the recommendations of all I&E witnesses presented in direct testimony.

Pennsylvania Electric Company
R-2016-2537352
INVESTIGATION & ENFORCEMENT

	12/31/17 Proforma Present Rates	Adjustments	Present Rates	Allowances	Proposed
	\$ (000)	\$ (000)	\$ (000)	\$ (000)	\$ (000)
Operating Revenue	380,967	0	380,967	93,894	474,861
Deductions:					
O&M Expenses	129,179	-3,359	125,820	0	125,820
Depreciation	111,276	0	111,276		111,276
Taxes, Other	25,706	0	25,706	5,540	31,246
Income Taxes:					
Current State	12,034	597	12,631	8,827	21,458
Current Federal	27,737	1,883	29,620	27,834	57,454
Deferred Taxes	19,675	0	19,675		19,675
ITC	-457	0	-457		-457
Total Deductions	325,150	-879	324,271	42,201	366,472
Income Available	55,817	879	56,696	51,693	108,389
Measure of Value	1,614,095	-84,092	1,530,003	0	1,530,003
Rate of Return	3.46%		3.71%		7.09%

Penn Power

I&E's total base rate revenue recommendation for Penn Power is \$121,626,000, which represents an increase of \$27,436,000 to present rate revenues of \$94,190,000 (Penn Power Ex. RAD-2, p. 1). This amount includes the recommendations of all I&E witnesses presented in direct testimony.

Pennsylvania Power Company
R-2016-2537355
INVESTIGATION & ENFORCEMENT

	12/31/17 Proforma Present Rates	Adjustments	Present Rates	Allowances	Proposed
	\$ (000)	\$ (000)	\$ (000)	\$ (000)	\$ (000)
Operating Revenue	94,190	0	94,190	27,436	121,626
Deductions:					
O&M Expenses	36,806	-460	36,346	0	36,346
Depreciation	26,087	0	26,087		26,087
Taxes, Other	6,222	0	6,222	1,619	7,841
Income Taxes:					
Current State	2,278	63	2,341	2,579	4,920
Current Federal	3,014	201	3,215	8,133	11,348
Deferred Taxes	6,351	0	6,351		6,351
ITC	0	0	0		0
Total Deductions	80,758	-196	80,562	12,331	92,893
Income Available	13,432	196	13,628	15,105	28,733
Measure of Value	413,424	-6,552	406,872	0	406,872
Rate of Return	3.25%		3.35%		7.07%

West Penn

I&E's total base rate revenue recommendation for West Penn is \$426,428,000, which represents an increase of \$56,121,000 to present rate revenues of \$370,307,000 (West Penn Ex. RAD-2, p. 1). This amount includes the recommendations of all I&E witnesses presented in direct testimony.

West Penn Power Company
R-2016-2537359
INVESTIGATION & ENFORCEMENT

	12/31/17 Proforma Present Rates	Adjustments	Present Rates	Allowances	Proposed
	\$ (000)	\$ (000)	\$ (000)	\$ (000)	\$ (000)
Operating Revenue	370,307	0	370,307	56,121	426,428
Deductions:					
O&M Expenses	139,587	-2,181	137,406	0	137,406
Depreciation	97,678	0	97,678		97,678
Taxes, Other	24,724	0	24,724	3,311	28,035
Income Taxes:					
Current State	11,170	319	11,489	5,276	16,765
Current Federal	19,808	1,011	20,819	16,637	37,456
Deferred Taxes	21,592	0	21,592		21,592
ITC	-795	0	-795		-795
Total Deductions	313,764	-851	312,913	25,224	338,137
Income Available	56,543	851	57,394	30,897	88,291
Measure of Value	1,364,177	-41,766	1,322,411	0	1,322,411
Rate of Return	4.14%		4.34%		6.68%

1 **Q. DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?**

2 **A. Yes.**