**BEFORE THE PENNSYLVANIA PUBLIC
UTILITY COMMISSION**

Pennsylvania Public Utility Commission, *et. al.*	:	R-2016-2537349, *et al.*
	:	
v.	:	
	:	
Metropolitan Edison Company	:	
Pennsylvania Public Utility Commission, *et. al.*	:	R-2016-2537352, *et al.*
	:	
v.	:	
	:	
Pennsylvania Electric Company	:	
Pennsylvania Public Utility Commission, *et. al.*	:	R-2016-2537355, *et. al.*
	:	
v.	:	
	:	
Pennsylvania Power Company	:	
Pennsylvania Public Utility Commission, *et. al.*	:	R-2016-2537359, *et al.*
	:	
v.	:	
	:	
West Penn Power Company	:	

SUPPLEMENTAL DIRECT TESTIMONY

OF

RALPH C. SMITH

**ON BEHALF OF THE
OFFICE OF CONSUMER ADVOCATE**

AUGUST 17, 2016

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I. INTRODUCTION

Q. What is your name, occupation and business address?

A. My name is Ralph C. Smith. I am a Certified Public Accountant licensed in the State of Michigan and a senior regulatory consultant in the firm Larkin & Associates, PLLC, Certified Public Accountants, with offices at 15728 Farmington Road, Livonia, Michigan 48154.

Q. Have you previously filed Direct Testimony before the Commission in this proceeding?

A. Yes, I previously filed Direct Testimony on behalf of the Pennsylvania Office of Consumer Advocate ("OCA") in this proceeding on July 22, 2016.

Q. What is the purpose of your Supplemental Direct Testimony?

A. On page 111 of my Direct Testimony, I had discussed the Companies' proposed adjustments to normalize sales and revenues related to (1) the Phase III Energy Efficiency and Conservation Plan, and (2) the reflect the impacts of behind-the-meter generation. At the time my Direct Testimony was served on July 22, 2016, I had not yet received requested documentation in support of the Companies' proposed adjustments to base operating revenues, and thus my analysis of this issue was incomplete. I have since received and analyzed the requested documentation. The purpose of my Supplemental Direct Testimony is to address the Companies' proposed adjustments to normalize and annualize base operating revenues as it relates to each Company's Phase III EE&C Plan.

Q. Are you presenting any exhibits with your supplemental direct testimony?

A. Yes. Confidential Exhibits LA-ME-2, LA-PN-2, LA-PP-2, and LA-WP-2 quantify the recommendations discussed in my Supplemental Direct Testimony for Met-Ed, Penelec, Penn Power, and West Penn, respectively.

II. REVENUE NORMALIZATION AND ANNUALIZATION RELATED TO THE COMPANIES' PHASE III ENERGY EFFICIENCY AND CONSERVATION PLAN (ALL FOUR FE UTILITIES)

Q. What is the Phase III Energy Efficiency and Conservation Plan?

A. On October 15, 2008, House Bill 2200 was signed into law as Act 129, which had an effective date of November 14, 2008. Among other things, Act 129 directed that the Commission adopt an Energy Efficiency and Conservation ("EE&C") program. Pursuant to this program, the Commonwealth's largest electric utilities were required to implement a cost effective EE&C plan to reduce energy consumption and demand. Met-Ed, Penelec, Penn Power, and West Penn were among the electric utilities required to adopt EE&C Plans. The EE&C Plans are being implemented in phases.

On January 15, 2009, in Docket No. M-2008-2069887, the Commission adopted an Implementation Order ("Phase I Implementation Order"), which established the standards that each EE&C plan must meet. The Phase I Implementation Order also provided guidance with regard to the procedures required for the submittal, review, and approval of the EE&C plans.

On August 2, 2014, in Docket Nos. M-2012-2289411 and M-2008-2069887, the Commission issued another Implementation Order ("Phase II Implementation Order") which established the incremental reductions in consumption required of electric utilities and also provided guidance with regard to the procedures required for the submittal, review, and approval of the Phase II EE&C plans.

On June 19, 2015, in Docket No. M-2014-2424864, the Commission issued a third Implementation Order ("Phase III Implementation Order"). In the Phase III Implementation Order, the Commission set forth the standards for each EE&C plan and provided guidance on the procedures to be followed with respect to the submittal, review, and approval of the EE&C plans. In addition, the Phase III Implementation Order established that the Phase III EE&C Plan would be in effect for the five-year period June 1, 2016 through May 31, 2021.

The Commission ultimately approved the Companies' Phase III EE&C Plans in its Order dated March 10, 2016 in Docket Nos. M-2015-2514767, M-2015-2514768, M-2015-2514769, and M-2015-2514772.

Q. Did the Companies' proposed adjustments to base operating revenues include an adjustment to normalize and annualize revenue as it relates to each Company's Phase III Energy Efficiency and Conservation Plan?

A. Yes. As discussed in the Direct Testimony of Companies' witness Kevin M. Siedt, the Companies have proposed adjustments to normalize and annualize revenues for conservation measures pursuant to the Companies' Phase III EE&C Plans. As shown on each Company's Exhibit RAD-2 (page 7), Adjustment No. 1, the impact of the Companies' proposed adjustments reduce 2017 FPFTY base operating revenue by the following amounts[1]:

- Met-Ed: $7,274,232;
- Penelec: $10,738,149;
- Penn Power: $1,398,404; and
- West Penn: $5,314,673

Q. Were you able to understand and replicate how the Companies derived those adjustment amounts to reduce 2017 FPFTY operating revenue?

A. Not initially. However, through discovery responses, such as OCA-XIII-7, and follow up calls with the Companies, we obtained that understanding and could follow the Companies' adjustment calculations.

Q. Please describe the Companies' proposed adjustments to normalize and annualize revenues related to the Phase III EE&C.

A. The usage reduction adjustments proposed by the Companies reflect projected energy sales reduction targets that each Company must achieve through May 31, 2021 from energy efficiency measures pursuant to each Company's Phase III EE&C

[1] The Companies' proposed adjustments to base operating revenue also include a component that relates to Behind-the-Meter generation.

Plan. The FPFTY period in this case is January through December 2017. On page 7 of his Direct Testimony, Mr Siedt stated: "The revenue reductions for the entire FPFTY were calculated by annualizing the usage reduction targets that the Company must achieve by the end of its Phase III EE&C Plan (May 31, 2021). The annualized amount was netted against the monthly savings already included in the FPFTY sales forecast to derive the additional energy efficiency normalization adjustment."[2] Thus, the Companies have reduced 2017 FPFTY revenue at current rates by annualized energy sales reductions that are projected to occur through May 2021.[3] In other words, although the Companies' proposed revenue requirements in the current case are based on a 2017 FPFTY, the Companies' proposed revenue reduction for EE&C is based on the 12-month period May 2021 through April 2022. Consequently, this FirstEnergy-proposed adjustment creates a mismatch with the 2017 FPFTY.

Q. Do you agree with the Companies' proposed adjustments to normalize and annualize revenue to the May 2021 annualized levels specified in each Company's Phase III EE&C Plan?

A. No. While I agree that the impact of the Phase III EE&C Plan is known and measurable and should be reflected, I disagree with imposing annualized energy sales reductions through May 2021 upon the 2017 FPFTY results. Specifically, in deriving the energy efficiency normalization component of their proposed revenue

[2] Mr. Siedt filed Direct Testimony on behalf of each of the four FirstEnergy Companies. As such, he included a similar statement for each Company in his separately filed Direct Testimonies.

[3] The May 2021 annualization used by the FirstEnergy Companies essentially reflects conditions for the 12-month period, May 2021 through April 2022.

adjustments, the Companies' annualized the projected usage reduction targets (in kWh) at May 31, 2021 (the last year of the five-year Phase III EE&C Plans), and netted these amounts against the projected base kWh amounts for the FPFTY ended December 31, 2017.[4] I disagree with the Companies' proposal to reduce the 2017 FPFTY revenue by the projected May 31, 2021annualized usage reduction targets. The Companies' approach is not reasonable as it creates a significant time period mismatch since there is over a three-year difference between the two sets of projected kWh energy sales reductions for energy efficiency.

Q. Is the end of the Phase III EE&C Plan May 31, 2021?

A. Yes. The Commission's Phase III Implementation Order dated June 19, 2015 and its Order approving the Companies' Phase III EE&C Plans, which is dated March 10, 2016, clearly state that the Phase III EE&C Plan ends at May 31, 2021.

Q. What approach do you recommend to derive the revenue normalization adjustment for EE&C in the current FirstEnergy rate cases?

A. The average usage reduction during the estimated rate effective period should be used to quantify the impact on revenue.

Q. What calculations are you presenting?

[4] According to the response to OCA-XIII-5, the base kWh amounts reflect the amount of energy efficiency savings assumed in the 2017 FPFTY before normalization adjustments.

A. I am presenting two calculations of the revenue adjustments for each Company. One reflects a two-year rate effective period. The other reflects a five-year normalization period.

Q. Please explain the basis for the two and five year periods.

A. The two and five-year periods are based on the estimated rate case filing interval for the Companies. For the reasons discussed in my Direct Testimony that was served on July 22, 2016, as it relates to rate case expense, I recommend that each Company's claimed rate case expense be normalized over a period of five years.[5] In contrast, the Companies have proposed that claimed rate case expense be normalized over a period of two years. The recommended use of a five-year average or a two-year average is based on the timing of the rate case normalization periods proposed by OCA and the FirstEnergy Companies, i.e., the approximate rate case filing interval. In other words, the use of a five-year average of usage reduction targets or a two-year average of usage reduction targets should be predicated on the rate case expense normalization period that is ultimately adopted by the Commission in this proceeding.

Q. Please explain your recommended adjustment to normalize and annualize base operating revenues as it relates to each Company's Phase III EE&C Plan.

A. Confidential Exhibits LA-ME-2, LA-PN-2, LA-PP-2, and LA-WP-2 present the impact of reflecting the projected usage reduction targets for energy efficiency based

[5] See the Direct Testimony of Ralph C. Smith at pages 86-90.

on (1) a five-year average and (2) a two-year average. This approach nets the average projected annualized usage reduction targets for energy efficiency that are based on (1) the five years 2017 through 2021 and (2) the two years 2017 and 2018, respectively, against the projected 2017 FPFTY base kWh amounts. The adjustment increases each Company's adjusted base operating revenues at current rates by the following amounts:

	5 Year Avg	2 Year Avg
• Met-Ed:	$3,903,480	$7,366,686
• Penelec:	$5,077,472	$9,638,975
• Penn Power:	$788,308	$1,507,306
• West Penn:	$2,771,202	$5,181,862

This adjustment properly reflects known and measurable sales adjustments for EE&C in the context of using the 2017 FPFTY. For purposes of establishing the FirstEnergy Companies' revenue deficiencies in the current rate cases that are based upon using a 2017 FPFTY, either the five-year average amounts or the two-year average amounts should be added to 2017 test year revenue at current rates, depending on the Commission's ruling with regard to the normalization period for claimed rate case expense. This adjustment will reduce the Companies' proposed revenue deficiencies for each Company by the above amounts.

Q. Did another intervenor in this proceeding also address this issue?

A. Yes. Jeffry Pollock submitted Direct Testimony on behalf of (1) Met-Ed Industrial Users Group, (2) Penelec Industrial Customer Alliance, and (3) West Penn Power

Industrial Intervenors in this proceeding. In his Direct Testimony, Mr. Pollock recommended that the Commission reject the Companies' proposal to set rates based on projected usage levels for the period May 2021 through April 2022.

Q. Do you agree with the adjustment calculated by Mr. Pollock?

A. Not entirely. I agree with his conclusion that the FirstEnergy Companies' proposal effectively uses reduced sales based on the period May 2021 through April 2022, which is a severe mismatch with the 2017 FPFTY, and would likely result in the Companies earning in excess of their authorized rate of return. However, rather than the recalculation of the Companies' proposed adjustments that Mr. Pollock recommended, I recommend using the average known and measurable EE&C usage reduction impacts during the expected rate effective period, explained above and as shown on Confidential Exhibits LA-ME-2, LA-PN-2, LA-PP-2, and LA-WP-2.

Q. Does this conclude your Supplemental Direct Testimony?

A. Yes, it does.

OCA Statement No. 1-Suppl

BEFORE THE PENNSYLVANIA PUBLIC UTILITY COMMISSION

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EXHIBITS ACCOMPANYING THE

SUPPLEMENTAL DIRECT TESTIMONY

OF

RALPH C. SMITH

ON BEHALF OF THE
OFFICE OF CONSUMER ADVOCATE

JULY 22, 2016

PUBLIC VERSION

Metropolitan Edison Company
Revenue Normalization Adjustment - Phase III EE&C Plan

Exhibit LA-ME-2
Docket No. R-2016-2537349
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Fully Projected Future Test Year Ended 12/31/2017
(Thousands of Dollars)

Line No.	Description	OCA Adjustment Using a 5-Year Avg (A)	OCA Adjustment Using a 2-Year Avg (B)	
1	Revenue Normalization Adjustment Related to the Phase III EE&C Plan - Per Met-Ed	$ (7,274,232)	$ (7,274,232)	
2	Revenue Normalization Adjustment Related to the Phase III EE&C Plan - Per OCA	$ (3,370,752)	$ 92,454	
3	OCA Adjustment to Base Operating Revenue	$ 3,903,480	$ 7,366,686	L2 - L1

Notes and Source
Cols A&B, Line 1: Amount from Company Exhibit RAD-2, Adjustment No. 1
Col A, Line 2: See page 2
Col. B, Line 2: See page 4

Pennsylvania Electric Company
Revenue Normalization Adjustment - Phase III EE&C Plan

Fully Projected Future Test Year Ended 12/31/2017
(Thousands of Dollars)

Line No.	Description	OCA Adjustment Using a 5-Year Avg (A)	OCA Adjustment Using a 2-Year Avg (B)	
1	Revenue Normalization Adjustment Related to the Phase III EE&C Plan - Per Penelec	$ (10,738,149)	$ (10,738,149)	
2	Revenue Normalization Adjustment Related to the Phase III EE&C Plan - Per OCA	$ (5,660,677)	$ (1,099,174)	
3	OCA Adjustment to Base Operating Revenue	$ 5,077,472	$ 9,638,975	L2 - L1

Notes and Source

Cols A&B, Line 1: Amount from Company Exhibit RAD-2, Adjustment No. 1
Col A, Line 2: See page 2
Col. B, Line 2: See page 4

Exhibit LA-PN-2
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Pennsylvania Power Company
Revenue Normalization Adjustment - Phase III EE&C Plan

Exhibit LA-PP-2
Docket No. R-2016-2537355
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Fully Projected Future Test Year Ended 12/31/2017
(Thousands of Dollars)

Line No.	Description	OCA Adjustment Using a 5-Year Avg (A)	OCA Adjustment Using a 2-Year Avg (B)	
1	Revenue Normalization Adjustment Related to the Phase III EE&C Plan - Per Penelec	$ (1,398,404)	$ (1,398,404)	
2	Revenue Normalization Adjustment Related to the Phase III EE&C Plan - Per OCA	$ (610,096)	$ 108,902	
3	OCA Adjustment to Base Operating Revenue	$ 788,308	$ 1,507,306	L2 - L1

Notes and Source
Cols A&B, Line 1: Amount from Company Exhibit RAD-2, Adjustment No. 1
Col A, Line 2: See page 2
Col. B, Line 2: See page 4

West Penn Power Company
Revenue Normalization Adjustment - Phase III EE&C Plan

Fully Projected Future Test Year Ended 12/31/2017
(Thousands of Dollars)

Line No.	Description	OCA Adjustment Using a 5-Year Avg (A)	OCA Adjustment Using a 2-Year Avg (B)	
1	Revenue Normalization Adjustment Related to the Phase III EE&C Plan - Per Penelec	$ (5,314,673)	$ (5,314,673)	
2	Revenue Normalization Adjustment Related to the Phase III EE&C Plan - Per OCA	$ (2,543,471)	$ (132,811)	
3	OCA Adjustment to Base Operating Revenue	$ 2,771,202	$ 5,181,862	L2 - L1

Notes and Source
Cols A&B, Line 1: Amount from Company Exhibit RAD-2, Adjustment No. 1
Col A, Line 2: See page 2
Col. B, Line 2: See page 4

Exhibit LA-WP-2
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v.	:	
Pennsylvania Electric Company	:	
Pennsylvania Public Utility Commission, *et. at.*	:	R-2016-2537355, *et. al.*
v.	:	
Pennsylvania Power Company	:	
Pennsylvania Public Utility Commission, *et. al.*	:	R-2016-2537359, *et al.*
v.	:	
West Penn Power Company	:	

VERIFICATION

I, Ralph C. Smith, hereby state that the facts above set forth in my Supplemental Direct Testimony, OCA Statement No. 1-Suppl, are true and correct and that I expect to be able to prove the same at a hearing held in this matter. I understand that the statements herein are made subject to the penalties of 18 Pa.C.S. § 4904 (relating to unsworn falsification to authorities).

Signature: Ralph C. Smith
Ralph C. Smith

Consultant Address: Larkin & Associates
15728 Farmington Road
Livonia, MI 48154

DATED: August 17, 2016