17 North Second Street
12th Floor
Harrisburg, PA 17101-1601
717-731-1970 Main
717-731-1985 Main Fax
www.postschell.com

Jessica R. Rogers

jrogers@postschell.com
202-661-6964 Direct
202-661-6944 Direct Fax
File #: 153583

January 4, 2017

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: Petition of UGI Central Penn Gas, Inc. for a Waiver of the Distribution System Improvement Charge Cap of 5% of Billed Distribution Revenues and Approval to Increase the Maximum Allowable DSIC to 10% of Billed Distribution Revenues - Docket No. P-2016-2537609

Dear Secretary Chiavetta:

Enclosed, for filing, please find the Exceptions of UGI Central Penn Gas, Inc. to the Recommended Decision of Administrative Law Judge Angela T. Jones Issued December 5, 2016, in the above-referenced proceeding. Copies will be provided as indicated on the Certificate of Service.

Respectfully submitted,

Jessica R. Rogers

JRR/jl
Enclosures

cc: Certificate of Service
Honorable Angela T. Jones

CERTIFICATE OF SERVICE

UGI Central Penn Gas, Inc.
(Docket No. P-2016-2537609)

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

VIA E-MAIL AND/OR FIRST CLASS MAIL

Erin L. Gannon
Darryl Lawrence
Office of Consumer Advocate
555 Walnut Street
Forum Place, 5th Floor
Harrisburg, PA 17101-1923

Steven C. Gray
Office of Small Business Advocate
Commerce Building
300 North Second Street, Suite 202
Harrisburg, PA 17101

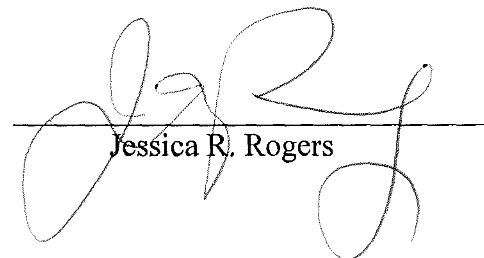
Carrie B. Wright
Bureau of Investigation & Enforcement
PO Box 3265
Harrisburg, PA 17105-3265

Jerome Mierzwa
Exeter Associates, Inc.
10480 Little Patuxent Parkway, Suite 300
Columbia, MD 21044

Pamela C. Polacek
Vasiliki Karandrikas
Alessandra L. Hylander
100 Pine Street
P.O. Box 1166
Harrisburg, PA 17108-1166

Robert D. Knecht
Consultant for OSBA
Industrial Economics Incorporated
2067 Massachusetts Avenue
Cambridge, MA 02140

Date: January 4, 2017



Jessica R. Rogers

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Petition of UGI Central Penn Gas, Inc. for a Waiver of the Distribution System Improvement Charge Cap of 5% of Billed Distribution Revenues and Approval to Increase the Maximum Allowable DSIC to 10% of Billed Distribution Revenues	:	Docket No. P-2016-2537609

EXCEPTIONS OF UGI CENTRAL PENN GAS, INC. TO THE RECOMMENDED DECISION OF ADMINISTRATIVE LAW JUDGE ANGELA T. JONES ISSUED DECEMBER 5, 2016

Mark C. Morrow (ID # 33590)
Danielle Jouenne (ID # 306839)
UGI Corporation
460 North Gulph Road
King of Prussia, PA 19406
Phone: 610-768-3628
Fax: 610-992-3258
E-mail: morrowm@ugicorp.com
E-mail: jouenned@ugicorp.com

David B. MacGregor (ID # 28804)
Jessica R. Rogers (ID # 309842)
Post & Schell, P.C.
17 North Second Street
12th Floor
Harrisburg, PA 17101-1601
Phone: 717-731-1970
Fax: 717-731-1985
E-mail: dmacgregor@postschell.com
E-mail: jrogers@postschell.com

Post & Schell, P.C.

Attorneys for UGI Central Penn Gas, Inc.

Date: January 4, 2017

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I. INTRODUCTION

UGI Central Penn Gas, Inc. ("UGI-CPG" or the "Company") files these Exceptions to the Recommended Decision ("RD") of Administrative Law Judge Angela T. Jones (the "ALJ") issued on December 5, 2016.

This case concerns the Petition of UGI-CPG for a waiver of the current 5% Distribution System Improvement Charge ("DSIC") rate cap, and its request to set the rate cap at 10%, pursuant to 66 Pa.C.S. § 1358(a)(1). The first findings in this proceeding were the determination of the appropriate standard for waiver of the 5% DSIC rate cap and whether UGI-CPG had met this standard. The RD found that the standard for waiver of the 5% DSIC rate cap is the same as the standard for granting a modified Long-Term Infrastructure Improvement Plan ("LTIIP") and that UGI-CPG met this standard and was entitled to waiver of the 5% DSIC rate cap. (RD at p. 28). The RD correctly rejects the absolute necessity standard advanced by the Office of Consumer Advocate ("OCA") and Office of Small Business Advocate ("OSBA"), which would require that a utility be granted a waiver only under "extraordinary circumstances". (RD at pp. 22, 28). The RD found that the standard proposed by the OCA and OSBA was not required by the statute or the Commission's regulations. (RD at pp. 22, 28). The Company strongly supports the standard articulated in the RD and does not take exception to the determination of the standard for waiver applied in the RD, nor the RD's determination that UGI-CPG was entitled to waiver per the application of this standard.

The next finding made in the RD sought to establish the appropriate revised DSIC rate cap. The RD rejected the Company's proposed 10% cap, and the Bureau of Investigation and Enforcement's ("I&E") proposed 7.5% cap, and instead developed a new methodology that captures a fraction of the Company's increased modified LTIIP spending resulting in a revised DSIC rate cap of 8.65%. The RD's methodology for calculating this new DSIC rate cap was not

proposed by any party to this proceeding nor adopted from a prior Commission determination. (RD at p. 31). The methodology adopted by the RD would limit the Commission's discretion by imposing a formula for calculating DSIC rate cap increases that would preclude the Commission from considering the totality of the circumstances in each fact-dependent case. UGI-CPG therefore takes exception to the calculation of the revised DSIC rate cap.

The Company also takes exception to the RD's description of the functioning of the DSIC mechanism - namely how costs are recovered by the DSIC and how to quantify the impact of granting the Company a lower DISC cap than the 10% cap requested. Importantly, the RD misstates the impact of a potential future base rate proceeding on recovery of prior uncollected DSIC revenue. (RD at pp. 29-32).

Lastly, the Company takes exception to the RD's findings on the effective date of the increased DISC rate cap. The RD does not provide a clear effective date for the increase in the DSIC rate cap. The Company encourages the Commission to make any increase in the DSIC rate cap effective upon one day's notice after a final order is issued in this proceeding and that any intent by the RD or Commission in effectuating recovery for past under collection that exceeds the increased DSIC rate cap is made explicit and executed in a similar manner to that of PGW, which was granted a temporary DSIC rate cap increase for that purpose.[1]

The Commission should adopt the RD's standard for determining that waiver was appropriate in this proceeding, but should not adopt the RD's calculation of the level of the increased DSIC rate cap. Instead, the Commission should grant UGI-CPG's request to increase

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[1] *See Petition of Philadelphia Gas Works for Waiver of Provisions of Act 11 to Increase the Distribution System Improvement Charge Cap and to Permit Levelization of DSIC Charges*, Docket No. P-2015-2501500, Orders entered on January 28, 2016 and July 6, 2016.

the DSIC rate cap to 10%, in order to enable the Company to accomplish the critical infrastructure work identified in its modified LTIIP.[2]

II. EXCEPTIONS

Exception No. 1: The RD erred in developing a new method for calculating the level of the applicable cap on the DSIC rate, which method is not supported by the record. (RD at p. 31).

Exception No. 2: The RD incorrectly states the implications of this proceeding on the Company's ability to recover revenue associated with DSIC related projects. (RD at pp. 29-32).

Exception No. 3: The findings in the RD regarding when the increased cap applies are unclear. (RD at p. 32).

III. ARGUMENT

A. EXCEPTION NO. 1 - THE RD ERRED IN DEVELOPING A NEW METHOD FOR CALCULATING THE LEVEL OF THE APPLICABLE CAP ON THE DSIC RATE, WHICH METHOD IS NOT SUPPORTED BY THE RECORD.

The RD incorrectly creates a mathematical equation for determining the level of the DSIC rate cap that is not supported by the record in this proceeding, or by the Commission's prior precedent. (RD at p. 31). The RD's proposal is in contrast to the approach adopted by the Commission in prior proceedings, in which the Commission employs its discretion to consider the individual circumstances of the requesting utility, to balance the interests of the customers and the utility, in order to effectuate the intent of the General Assembly in passing Act 11. For the reasons stated in this section, the Commission should not adopt the methodology developed in the RD, and should instead adopt the Company's proposed cap of 10%.

The RD arrives at a DSIC rate cap of 8.65% by applying a new method developed to calculate a DSIC rate cap that is associated with, but not directly correlated to, the increased spending in the Company's modified LTIIP. (RD at pp. 30-31). Instead of adopting a totality of the circumstances approach that considers the Company's current and future operational and

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[2] *See Petition of UGI Central Penn Gas, Inc. for Approval of their Modified Long-Term Infrastructure Improvement Plan,* Docket No. P-2013-2398835, (Order entered June 30, 2016) ("*UGI-CPG Modified LTIIP*").

financial needs, the impact on UGI-CPG's customers, and the total cost of the Company's identified DSIC-eligible plans as intended by Act 11 – the RD develops a calculation that relies on various sets of data that do not produce an outcome that is consistent with past Commission determinations in waiver proceedings. The RD's calculation is as follows:

> Statutory DSIC cap of 5% + (Difference between amount of projected DSIC charge at January 1, 2019 without cap less 5% current cap)*(Percent increase in LTIIP DSIC investment) = Increased DSIC rate cap
>
> 5% + (9*38.5%) = 8.65%

The RD does not provide any source for the methodology developed and applied in this proceeding. The RD acknowledges that this figure excludes 40% of the amount necessary to provide the Company with "full recovery" for DSIC eligible spending.[3] (RD at p. 31).

The RD errs in adopting a methodology that does not follow precedent and is not supported by record evidence. The Commission has consistently applied an increased rate cap in cases where utilities have demonstrated that the 5% DSIC cap is insufficient to facilitate infrastructure replacement programs, without relying on the methodology proposed in this RD.

In *Petition of Philadelphia Gas Works for Waiver of Provisions of Act 11 to Increase the Distribution System Improvement Charge Cap and to Permit Levelization of DSIC Charges*, Docket No. P-2015-2501500 (Opinion and Order entered January 28, 2016) ("*PGW DSIC Waiver*"), the Commission granted the utility's request for a waiver, and increased the DSIC rate cap to 7.5%. Further, on reconsideration, the Commission allowed PGW to reach up to a 10% DSIC rate to recover for undercollections. *PGW Reconsideration*, Docket No. P-2015-2501500 (Opinion and Order entered July 6, 2016.) In neither instance did the Commission employ a formula such as the one proposed in the RD in this proceeding, where the approved revised rate

[3] A full discussion of why the RD's description of DSIC recovery as "full recovery" is inaccurate is included in Exception No. 2, below.

cap was dictated by a percentage of the increase in betterment spending. Instead, the Commission considered the totality of PGW's financial circumstances, PGW's experience using its DSIC, and the impact increasing the DSIC would have on customers, and crafted a remedy that sought to balance these interests.

In the pre-Act 11 DSIC waiver proceedings, the Commission, as in *PGW DISC Waiver*, neither developed nor utilized a methodology such as the one proposed in the RD in this proceeding to support the 7.5% DSIC cap adopted therein. Instead, the Commission used its judgment and discretion to strike an appropriate balance between the interests of customers in getting safe, reliable, and affordable service, and providing utilities with adequate return on their investment to maintain economic stability as they spent millions of dollars per year in infrastructure repair and replacement. *See, e.g., Pa. Pub. Util. Comm'n v. Aqua Pennsylvania, Inc.*, Docket No. R-2008-2079310 (Order entered July 23, 2009); *Petition Of Pennsylvania-American Water Company For Approval To Implement A Tariff Supplement To Tariff Water-PA P.U.C. No. 4 Revising The Distribution System Improvement Charge*, 2007 Pa. PUC LEXIS 42 (Order entered August 14, 2007).

UGI-CPG's request of a 10% DSIC cap in this proceeding represents a comparable impact to customers as the 7.5% DSIC cap granted to the water utilities in the above-cited proceedings due to the differences between the operation of the water DSIC and the gas DSIC, which UGI-CPG enumerated in this proceeding. Specifically, the water DSIC is applied to 100% of the total water customer's bill, whereas the gas DSIC is not applied to commodity charges (*e.g.*, the purchased gas cost) for a gas customer's bill. (UGI-CPG St. 1-R, p. 15.) Commodity charges often constitute approximately one third to one half of customer bills. (UGI-CPG St. 1-R, p. 15.) Therefore, a gas DSIC at 10% recovers approximately the same total

percent of a customer's bill as a water DSIC operating at 5%. (UGI-CPG St. 1-R, p. 15.) UGI-CPG's proposal, therefore, considered both the Commission's historic approach to DSIC waivers and the constraints added to gas utilities by Act 11.

The Company proposed a 10% DSIC rate cap to balance its own financial interests with that of its customers. (UGI-CPG St. 1-R, pp. 5, 12, 15.) Unlike the cap proposed by the RD, which excludes 40% of the total DSIC-eligible investment, the Company's proposal of a 10% cap was near the mid-point between the existing capped charge to customers and the total charge if all DSIC-eligible projects were reflected as of January 1, 2019. (UGI-CPG Ex. WJM-3.) Thus, the Company's proposal of a 10% rate cap better reflects both the Commission's historical consideration of increased DSIC rate caps, and strikes a logical balance between the Company and customers.

The calculation adopted by the RD, however, deviates from Commission precedent, and limits the Commission's discretion in a way that does not further the policy goals of the General Assembly in passing, and the Commission in implementing, Act 11. There is no support for applying a percentage fraction of the increased spending reflected in the modified LTIIP to the total calculated change in potential DSIC charges. The RD correctly determined that no party had challenged the projects in the modified LTIIP, the inclusion of costs, or the cost estimates produced by the Company. (RD at p. 23). No party disputes that UGI-CPG had already exceeded the 5% DSIC rate cap, and by October 1, 2017, it would reach and exceed a 10% DSIC rate cap. (UGI-CPG Ex. WJM-3). The plain language of the RD, and an analysis of the calculation itself, show that the calculation provides the Company with only a fractional return on the investment required by the accelerated spending identified in the modified LTIIP. The RD's methodology should not be adopted absent evidence supporting the exclusion from DSIC

return on 40% of the DSIC-eligible projects identified in the modified LTIIP, and a finding on why that exclusion furthers the policy goals of the Commission and protects customers.

Not only is the methodology established in the RD inconsistent with Commission precedent, the new methodology is inconsistent with any theory of the case supported by the evidence and expert witnesses in this proceeding. Two parties to this proceeding provided evidence on where to strike the appropriate balance between customers and the Company. I&E's witness supported the adoption of a 7.5% DSIC rate cap. (I&E St. No. 1, p. 12.) However, the Company showed that a 7.5% DSIC cap would not be sufficient in light of the substantial acceleration under the modified LTIIP and that a 10% DSIC cap more appropriately balanced the Company's interest in remaining economically viable, with a minimal impact on customers' bills. (UGI-CPG St. No. 1-R, pp. 2-3; 5-6.) Increasing the DSIC rate cap to the Company's proposed 10% would only amount to an increase of $2.80 per month to the average residential heating customer once the Company reached the 10% cap, which would not occur until mid-2017. (UGI-CPG Ex. WJM-3). There is no record evidence to support the conclusion of the RD that its 8.65% is an appropriate cap.[4]

The methodology adopted in the RD does not achieve the goal of striking an appropriate balance between the interests of the customer and the Company. Specifically, the methodology does not appropriately consider customer impacts, or balance those impacts with the interests of the Company. The only point of customer reference in the RD is a confirmation that the per bill impact will be approximately $2.04 for the average residential heating customer, and that the calculated increase would reflect 60% of the amount of actual spend the Company would engage

[4] While the Company does not support adoption of the formula for calculating the rate cap developed in the RD, if the Commission determines to use that formula, it should modify the calculation to use the 54.3% increase from its *Modified LTIIP Order*. (RD at pp. 30-31; *UGI-CPG Modified LTIIP* at p. 5). Instead of using the 54.3% increase identified by the Commission, the RD utilizes 38.5% without providing a basis for deviating from the Commission's determination. (RD at p. 31).

in under its modified LTIIP. (RD at pp. 31-32). The RD does not provide any analysis as to why the $2.04 customer charge reaches a more appropriate balance than the per bill impact of the DSIC at 10% ($2.80). (UGI-CPG Ex. WJM-3.) From the analysis in the RD, the Commission cannot conclude that the methodology applied in this proceeding strikes the appropriate balance between customer and company interests. Therefore, the methodology should be rejected.

Rather than adopt the calculation in the RD, the Commission should instead retain its discretion and apply its traditional totality of the circumstances analysis. Not only would the Commission's traditional approach allow it to better effectuate the General Assembly's intent in Act 11 by considering the unique circumstances of individual utilities, but applying the RD's approach would provide a perverse incentive for utilities to start with a lower original LTIIP investment, and then adopt a higher percentage increase in order to manipulate the outcome of the methodology. For instance, a utility that showed a 60% increase in its original LTIIP, and only a 20% increase in its modified LTIIP, would receive a much lower DSIC rate cap than an identically situated utility that showed a 20% increase in its original LTIIP, and a 60% increase in its modified LTIIP. The Commission should not adopt a methodology that encourages gamesmanship, particularly where the methodology also fails to include any mechanism for ensuring that a proper balance between the interests of the customers and the utility is achieved.

For the reasons explained above and in UGI-CPG's Main and Reply Briefs, the RD errs in determining that the increase in the DSIC rate cap should be less than 10%.

B. EXCEPTION NO. 2 - THE RD INCORRECTLY STATES THE IMPLICATIONS OF THIS PROCEEDING ON THE COMPANY'S ABILITY TO RECOVER REVENUE ASSOCIATED WITH DSIC RELATED PROJECTS.

The RD incorrectly describes the impact of granting the Company's request on both the Company's continued use of the DSIC mechanism, and on its ability to recover lost revenues

through a base rate proceeding. These issues should be addressed by the Commission in its final Order.

The RD misstates the operation of the DSIC rate cap on recovery. Specifically, the RD states that "what is not recovered through any capped DSIC rate can be recovered through the means of a rate base proceeding" (RD at p. 30). This does not accurately reflect the operation of the DSIC mechanism. Act 11 allows utilities to collect through the DSIC mechanism what, in the past, was lost depreciation that occurred between base rate proceedings. For any quarter where revenue associated with DSIC-eligible plant exceeds the 5% DSIC rate cap, new plant placed in service is excluded from the DSIC calculation. When a utility eventually comes in for a base rate proceeding, it can include the plant that was excluded from the DSIC in rate base, however the recovery on that plant will be reduced by the depreciation that occurred during the period between the in-service date and the date of the fully projected future test year. Thus, anything that is not recovered through the DSIC in a particular quarter is foregone revenue that cannot be recovered later, as the RD incorrectly assumed.

In the case of UGI-CPG, any plant placed in service on or after the quarter ending May 30, 2016, is currently not reflected in the DSIC and no revenue is being recovered on that plant. (UGI-CPG Ex. WJM-3). The excluded revenue for the plant that is not currently reflected in the DSIC is $1.14 million. By January 1, 2019, UGI-CPG is projected to have more than $9 million of unrecoverable investment. (UGI-CPG Ex. WJM-3).

The RD also incorrectly describes the function of the DSIC mechanism and how the Company's proposal would recover revenue associated with DSIC-eligible projects. The RD finds that the Company's proposal of 10% is "about 70% of the projected DSIC rate of 14.49% needed for full recovery of the projected spending corresponding to the modified LTIIP." (RD at

pp. 31-32). The concept of "full recovery" through the DSIC is misleading. A 10% DSIC rate cap would not provide full recovery, but rather would allow the Company to reflect DSIC-eligible plant placed in service in its DSIC through the third quarter of 2017, when the DSIC is expected to reach the 10% rate cap. Once that cap is reached, the Company would again receive no new revenue associated with additional infrastructure replacement projects, despite having another entire year left in its modified LTIIP. Further, including plant in the DSIC does not provide for immediate recovery of the full costs of the plant. Rather, the DSIC recovers a return on and of DSIC eligible investments over time, broken down on a quarterly basis. An increased cap would reflect all eligible plant placed in service prior to reaching the cap, but "full recovery" for that plant will take many years of continuous operation of the DSIC.

In addition, the DSIC does not provide recovery for non-DSIC-eligible projects, increased operations and maintenance costs, or a variety of other costs that can only be recovered through the base rate process. (UGI-CPG St. 1-R, pp. 10-11.) In conjunction with the accelerated pace of replacement, which will inevitably drive the Company over the increased cap, whether it is at 8.65% or 10%, the combination of non-recoverable items will require regular base rate proceedings. (UGI-CPG St. 1-R, pp. 9-10.) Unless the DSIC continues to operate consistently for the entire depreciable life of a particular piece of plant, it is inaccurate to say that the DSIC with any rate cap provides for "full recovery". And that long-term operation will not occur, because the Company will eventually be driven in for a base rate case due to the accelerated replacement schedule that is required in order for it to have a DSIC at all.

The General Assembly adopted Act 11 with the intent of assisting utilities in accelerating replacement of infrastructure by allowing recovery of additional capital investments between base rate proceedings. Act 11 has been successful at encouraging gas utilities, such as UGI-

CPG, to adopt aggressive long-term accelerated plans that span two or more decades and encompass hundreds of millions of dollars' worth of infrastructure repair and replacement. The current LTIIP represents just a small segment of these long-term plans. Without an increase in the DSIC rate cap, the rate cap will limit much needed rate relief for utilities undertaking work that will ensure safe and reliable service for customers. Even if a utility seeks base rate relief, the accelerated replacement schedule and the constantly aggregating eligible plant total required by Act 11 will cause utilities to exceed the DSIC rate cap, whether it is at 5%, 7.5%, or 10%. To make the DSIC fully effective for gas companies undertaking significant long-term plans, an increase in the DSIC rate cap is appropriate, in the same way that the Commission recognized that the DSIC had to be modified for water companies undertaking substantial infrastructure work. Adoption of the analysis in the RD would undermine the intent of the General Assembly in adopting Act 11 by not acknowledging the very features of the DSIC mechanism that will ensure it operates effectively, even with a DSIC rate cap at 10%.

The Commission should not adopt the RD's recommendation to limit the DSIC cap to 8.65% because it is based on an incorrect analysis of the implications of providing the Company with a lower DSIC rate cap than what the Company has requested. For the reasons explained above and in UGI-CPG's Main Brief and Reply Brief, UGI-CPG's request for waiver to increase the DSIC rate cap to 10% of billed distribution revenue should be granted.

C. EXCEPTION NO. 3 - THE FINDINGS IN THE RD REGARDING WHEN THE INCREASED CAP APPLIES ARE UNCLEAR.

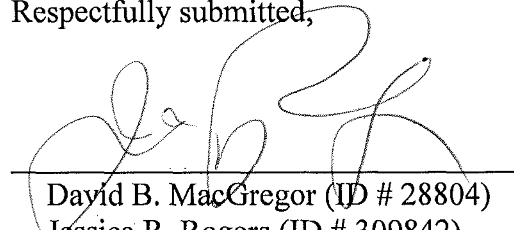
In the Company's view, the RD does not clearly articulate when the DSIC rate cap should be increased and what additional revenue can be collected. (RD at p. 32). The RD states that "Residential heating gas customer's bills will have an added (3.65 x \$0.56 = \$2.04) \$2.04 per month above what has been collected at the rate capped at 5% from April 2017 to the end of the

term of the LTIIP (end of year 2018)." (RD at p. 32). UGI-CPG encourages the Commission to clarify when the increased DSIC rate cap would be effective by adopting in its final order an effective date upon one day's notice. For the reasons explained in this Exception and Exception No. 1, the RD should be revised to adopt an effective date that implements a 10% DSIC rate cap based on one day's notice after a final order is issued, for prospective recovery only.

IV. CONCLUSION

For the foregoing reasons, the Commission should reject those portions of the RD identified in these Exceptions, and grant UGI Central Penn Gas, Inc.'s Petition for Waiver to increase the DSIC rate cap to 10% of billed distribution revenue.

Respectfully submitted,



David B. MacGregor (ID # 28804)
Jessica R. Rogers (ID # 309842)
Post & Schell, P.C.
17 North Second Street
12th Floor
Harrisburg, PA 17101-1601
Phone: 717-731-1970
Fax: 717-731-1985
E-mail: dmacgregor@postschell.com
E-mail: jrogers@postschell.com

Mark C. Morrow (ID # 33590)
Danielle Jouenne (ID # 306839)
UGI Corporation
460 North Gulph Road
King of Prussia, PA 19406
Phone: 610-768-3628
Fax: 610-992-3258
E-mail: morrowm@ugicorp.com
E-mail: jouenned@ugicorp.com

Post & Schell, P.C.

Attorneys for UGI Central Penn Gas, Inc.

Date: January 4, 2017