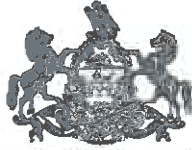


COMMONWEALTH OF PENNSYLVANIA

July 2, 2018

E-FILED

Rosemary Chiavetta, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street
Harrisburg, PA 17120

Re: Pennsylvania Public Utility Commission v. UGI Utilities, Inc. – Electric Division / Docket No. R-2017-2640058

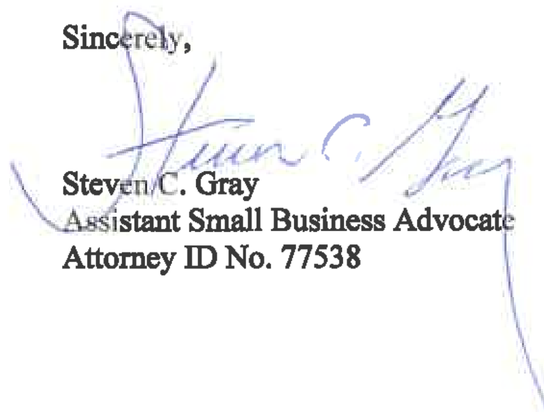
Dear Secretary Chiavetta:

Enclosed please find the Main Brief, on behalf of the Office of Small Business Advocate ("OSBA"), in the above-captioned proceeding.

Copies will be served on all known parties in this proceeding, as indicated on the attached Certificate of Service.

If you have any questions, please do not hesitate to contact me.

Sincerely,



Steven C. Gray
Assistant Small Business Advocate
Attorney ID No. 77538

Enclosures
cc: The Honorable Steven K. Haas
The Honorable Andrew M. Calvelli
Robert D. Knecht
Parties of Record

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:	
	:	
v.	:	**Docket No. R-2017-2640058**
	:	
UGI Utilities, Inc. – Electric Division	:	

MAIN BRIEF ON BEHALF OF THE OFFICE OF SMALL BUSINESS ADVOCATE

Steven C. Gray
Assistant Small Business Advocate
Attorney ID No. 77538

For:

John R. Evans
Small Business Advocate

Office of Small Business Advocate
300 North Second Street, Suite 202
Harrisburg, PA 17101

Date: July 2, 2018

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I. Introduction

A. UGI Electric

On January 26, 2018, UGI Utilities, Inc. – Electric Division ("UGI Electric" or the "Company") filed Tariff Electric – Pa. P.U.C. Nos. 6 and 2S with the Pennsylvania Public Utility Commission ("Commission"). The proposed Tariff, as originally filed, would increase UGI Electric's annual revenue by $9.254 million per year. The Company also proposed a new Storm Expense Rider, a Universal Service Program Rider, and a new Rate EV (for Electric Vehicle Services).

On March 12, 2018, UGI Electric submitted Supplemental Direct Testimony and Revised Exhibits.

B. History of the Proceedings

On February 12, 2018, the Office of Small Business Advocate ("OSBA") filed a Formal Complaint.

On March 1, 2018, the Commission entered an Order suspending the Tariffs and instituting an investigation before the Office of Administrative Law Judge ("ALJ").

On March 22, 2018, a Prehearing Conference was held before ALJs Steven K. Haas and Andrew M. Calvelli.

On March 30, 2018, ALJs Haas and Calvelli issued their Scheduling Order.

On April 26, 2018, the OSBA served the Direct Testimony of Robert D. Knecht.

On May 11, 2018, the OSBA served the Supplemental Direct Testimony of Mr. Knecht.

On May 25, 2018, the OSBA served the Rebuttal Testimony of Mr. Knecht.

On June 7, 2018, the OSBA served the Surrebuttal Testimony of Mr. Knecht.

On June 11 & 12, 2018, Evidentiary Hearings were held before ALJs Haas and Calvelli.

On June 20, 2018, the Company filed a Partial Stipulation Resolving Certain Contested Issues ("*Partial Stipulation*") with ALJs Haas and Calvelli.

The OSBA submits this Main Brief in accordance with the ALJs' March 30th Scheduling Order.

C. Legal Standards

Section 1301 of the Public Utility Code, 66 Pa. C.S. § 1301, provides that "every rate made, demanded, or received by any public utility, or by any two or more public utilities jointly, shall be just and reasonable, and in conformity with regulations or orders of the commission."

The burden of proof to establish the justness and reasonableness of every element of the utility's rate increase rests solely upon the public utility. 66 Pa. C.S. § 315(a). "It is well-established that the evidence adduced by a utility to meet this burden must be substantial." *Lower Frederick Township. v. Pa. PUC*, 409 A.2d 505, 507 (Pa. Cmwlth. 1980).

Although the burden of proof remains with the public utility throughout the rate proceeding, when a party proposes an adjustment to a ratemaking claim of a utility, the proposing party bears the burden of presenting some evidence or analysis tending to demonstrate the reasonableness of the adjustment. *Pa. PUC v. Aqua Pennsylvania, Inc.*, Docket No. R-00072711 (Order entered July 17, 2008). "Section 315(a) of the Code, 66 Pa. C.S. § 315(a), applies since this is a proceeding on Commission Motion. However, after the utility establishes a prima facie case, the burden of going forward or the burden of persuasion shifts to the other parties to rebut the prima facie case." *Pa. PUC v. Philadelphia Gas Works*, Docket No. R-00061931 (Order entered September 28, 2007), at 12.

Furthermore, Section 523 of the Public Utility Code, 66 Pa. C.S. § 523, requires the Commission to "consider . . . the efficiency, effectiveness and adequacy of service of each utility

when determining just and reasonable rates." In exchange for customers paying rates for service, which include the cost of utility plant in service and a rate of return, a public utility is obligated to provide safe, adequate and reasonable service. "[I]n exchange for the utility's provision of safe, adequate and reasonable service, the ratepayers are obligated to pay rates which cover the cost of service which includes reasonable operation and maintenance expenses, depreciation, taxes and a fair rate of return for the utility's investors . . . In return for providing safe and adequate service, the utility is entitled to recover, through rates, these enumerated costs." *Pa. PUC v. Pennsylvania Gas & Water Co.*, 61 Pa. PUC 409 (1986), at 415-16. *See also* 66 Pa. C.S. § 1501. As a result, the legislature has given the Commission discretionary authority to deny a proposed rate increase, in whole or in part, if the Commission finds "that the service rendered by the public utility is inadequate." 66 Pa. C.S. § 526(a).

II. Summary of Argument

The *Partial Stipulation* proposes to withdraw the Company's proposal for the EV Rider. This withdrawal is consistent with the OSBA's testimony on this issue.

The fully projected future test year ("FPFTY") rate base should be based on average net plant values throughout the year, and FPFTY depreciation should reflect forecast depreciation for the test year.

The rate base treatment of excess accumulated deferred income taxes ("Excess ADIT") should follow that of ADIT, and that Excess ADIT should be recognized as an offset to rate base.

Mr. Knecht's allocated cost of service study ("ACOSS") should be adopted for the purposes of revenue allocation and rate design in this proceeding. Mr. Knecht's ACOSS corrects several technical and methodological errors in the Company's original ACOSS. UGI Electric's

"rebuttal testimony" ACOSS is also acceptable, as it generally adopts the modifications proposed by Mr. Knecht.

Mr. Knecht's revenue allocation recommendation should be adopted. It moves rate classes closer to their respective cost of service and provides relief to rate classes that have been overpaying for decades.

Mr. Knecht's "directional" recommendations for rate design for the GS-1, GS-4, and LP-4 rate classes should be adopted. UGI Electric generally agrees with the OSBA's rate design proposals, and no party has voiced opposition to those proposals.

A traditional proportional scaleback should be applied only to those classes that are assigned rate increases if the Commission awards the Company an overall revenue increase less than requested.

III. Stipulation of Partial Settlement

C. EV Rider

In its original January 26th filing, UGI Electric proposed a rate for electric vehicle charging stations ("Rate EV"). OSBA witness Robert D. Knecht summarized the Company's Rate EV proposal, as follows:

> I begin by observing that the Company's proposal is unclear. With that caveat, my understanding is that the Company would purchase and maintain electric vehicle charging stations, and charge customers a monthly fixed fee for use of the station. Electricity supply and utility distribution service would be billed separately and are not reflected in the proposed Rate EV charges.

OSBA Statement No. 1, at 26.

Mr. Knecht identified a series of problems with the Company Rate EV proposal, including questionable estimated maintenance costs and understated lifespans of the charging stations, leading to excessive rates. *Id.*, at 26-27. Mr. Knecht recommended that the Commission reject the Company's Rate EV proposal. *Id.*, at 26.

The *Partial Stipulation* withdraws UGI Electric's Rate EV proposal from this proceeding. The OSBA supports this result as it is consistent with the recommendation in Mr. Knecht's testimony.

IV. Rate Base

The OSBA did not submit direct testimony relating to any revenue requirement issues in this proceeding. However, this proceeding involves certain methodological issues with respect to the derivation of the revenue requirement that the Commission has not previously addressed. Consequently, the Commission's resolution of these issues in this proceeding will likely serve as precedent for future base rates proceedings. The OSBA believes these issues are significant, and therefore addresses them in this brief.

These issues include whether an average year or end-of-year plant balances should be used to set fully projected future test year ("FPFTY") rate base (and associated depreciation expense); and whether excess accumulated deferred income taxes ("Excess ADIT") created by the Tax Cut and Jobs Act ("TCJA") should continue to be used as an offset to utility rate base as was the ADIT from which the Excess ADIT was transferred.

A. Original Cost Utility Plant in Service

1. End of Year vs. Average Rate Base Methodology

In 2012, Act 11 made certain amendments to the public utility code, including a provision giving public utilities the option of using a FPFTY for base rates proceedings:

> **Use of future test year.** — In discharging its burden of proof the utility may utilize a future test year or a fully projected future test year, ***which shall be the 12-month period beginning with the first month that the new rates will be placed in effect*** after application of the full suspension period permitted under Section 1308(d) (relating to voluntary changes in rates). The commission shall promptly adopt rules and regulations regarding the information and data to be submitted when and if a future test period or a fully projected future test year is to be utilized. Whenever a utility utilizes a future test year or a fully projected future test year in any rate proceeding and such future test year or a fully projected test year forms a substantive basis for the final rate determination of the commission, the utility shall provide, as specified by the commission in its final order, appropriate data evidencing the accuracy of the estimates contained in the future test year or a fully projected future test year, and the commission may after reasonable notice and hearing, in its discretion, adjust the utility's rates on the basis of such data. ***Notwithstanding section 1315 (relating to limitation on consideration of certain costs for electric utilities), the commission may permit facilities which are projected to be in service during the fully projected future test year to be included in the rate base.***

Section 315(e) of the Public Utility Code, 66 Pa. C.S. Section 315(e) (emphasis added).

Prior to the adoption of Act 11, Pennsylvania public utilities were permitted to use either a future test year ("FTY") or a historic test year ("HTY") for ratemaking, but were not permitted

to use a FPFTY. Under FTY regulation, rates did not go into effect until the end of the FTY. I&E Statement No. 3-SR, at 7. In effect, the FTY generally represented the 12 months prior to start of new rates. In that regulatory regime, however, the law and the Commission permitted utilities to make certain adjustments to the annual values for the FTY, in order to better align costs with the period in which rates would be in effect. These adjustments included allowing utilities to set rate base at FTY end-of-year plant values, and to calculate depreciation expense based on those year-end values. OCA Statement No. 1, at 7-8. Similarly, various revenue and cost parameters were all "annualized" at values representative of the end of the FTY, rather than being actual FTY values.

In effect, under the previous regime, rates and costs were implicitly derived on an annual basis *around* the end of the FTY, rather than representing the values for the test year calendar period. Of course, this method suffered from a certain amount of regulatory lag, in that rates and costs reflected a period around the end of the FTY, while the new rates did not go into effect until the end of the FTY. This regime was generally based on the used and useful principle, to avoid setting rates in any way based on the expectation for plant not yet in service. I&E Statement No. 3-SR, at 7.

One of the benefits of Act 11 and the use of a FPFTY is that this problem of regulatory lag can be addressed.

This proceeding, like many since the adoption of Act 11, involves a dispute between the parties as to whether rate base for the FPFTY should be set by porting the year-end methodology from the prior FTY regulatory regime to the new FPFTY and using year-end values, or whether the rate base for the FPFTY should be set based on an average of the forecasted rate throughout the FPFTY.

Since the passage of Act 11, the Commission has not determined whether the adjustments permitted under FTY regulation such as the use of year-end rate base are appropriate for FPFTY regulation. I&E Statement No. 3-SR, at 9. The OSBA respectfully submits that FTY adjustments are not appropriate for FPFTY regulation.

Simply put, the OSBA submits that both standard regulatory practice and basic common sense require a matching between the time period for which costs are incurred and the time period for which rates will be in effect. Given this simple principle, FPFTY ratemaking should be based on the costs incurred throughout the test year, because the rates will also be in effect for that same period. Significantly, Section 315(3) requires that ". . . a fully projected future test year, which shall be the 12-month period beginning with the first month that the new rates will be placed in effect after application of the full suspension period permitted under section 1308(d)."

Since rates go into effect in the first month of the FPFTY, the determination of utility costs should also begin in the first month of the FPFTY. Thus, since utility costs in the first month of the FPFTY are based on plant and depreciation in that month, the utility cost for the FPFTY should necessarily reflect the plant and depreciation values in the first month of the FPFTY. Of course, because utility rates will also be in effect in the last month of the FPFTY, the costs should also reflect plant and depreciation values for the last month of the year.

Thus, based on the simple principle of matching rates and costs, the OSBA respectfully submits that FPFTY rate base should be based on average net plant values throughout the year, and FPFTY depreciation should reflect forecast depreciation for the test year.

OCA witness Mr. Lafayette K. Morgan, Jr. explains the issue this way in his direct testimony:

> As I understand it, the use of a fully projected future test year or rate year is intended to allow rates to be set to reflect the costs that will be incurred during the first year the rates will be in effect. UGI-E has overstated its future rate year cost of service by reflecting costs at end of FPFTY levels rather than at the levels of costs that will be experienced during the rate year. Rather than reflecting costs that will be incurred during the rate year ending September 30, 2019, the use of the end of period means UGI-E has reflected costs that will be incurred as of October 1, 2019.

OCA Statement No. 1, at 6-7.

I&E reaches the identical conclusion. Mr. Ethan H. Cline stated, as follows:

> Under the FPFTY, the traditional interpretation of the 'used and useful' requirement for rate base inclusion of investments is unclear because when a company employs the use of a FPFTY in a base rate case, the new rates go into effect before the end of the Company's FPFTY. The inclusion of rate base added in a FPFTY necessarily means that customers will be paying a return on and a return of a utility's plant investment that has not yet been placed in service. By using an average of the rate base that is projected to be in service by the end of the FPFTY, rather than the full year-end amount, the impact of the necessary customer overpayment at the beginning of the year is mitigated. This results in rates that are more just and reasonable because ratepayers are not paying for approximately a year of plant that is not yet in service.

I&E Statement No. 3, at 5-6.

In rebuttal, UGI Electric appears to argue that use of year-end rate base is reasonable because it is likely that rates will be in effect for a period beyond the FPFTY. *See* UGI Electric Statement No. 4-R, at 3-4. In effect, the Company wants to extend the FPFTY beyond the 12-month term for rate base and depreciation costs (but, of course, not for revenue growth or other parameters). The OSBA observes that if the legislature had wanted to allow utilities to base their cost forecasts on a future period longer than one year, it would have done so. Because the test period is limited to one year, the Company's argument is without merit. Costs and volumes should be based on the FPFTY.

The Company also argued that the use of year-end rate base was permitted under FTY regulation. UGI Statement No. 4-R, at 4. The use of year-end rate base was permitted specifically because it resulted in a better matching of costs and rates, and because rates could not go into effect at the beginning of the FTY. *See* OCA Statement No. 1-S, at 4. In fact, as Mr. Cline pointed out, the prior practice only allowed utilities to include rate base that was in place at the time the new rates went into effect, and therefore served to *understate* the costs associated with the first year in which the rates would be in effect. I&E Statement No. 3-SR, at 7. The OSBA submits that resolving this regulatory lag problem was likely a reason for the adoption of Act 11. It is therefore difficult to understand how the Company can now try to claim that a past practice which was amended for good reason in Act 11 can reasonably serve as precedent for the going-forward implementation of Act 11.

The Company also refers to the specific language of Act 11 that:

> Notwithstanding section 1315 (relating to limitation on consideration of certain costs for electric utilities), the commission may permit facilities which are projected to be in service during the fully projected future test year to be included in the rate base.

66 Pa. C.S. Section 215(e). The Company concludes that this language requires that the rate base for the entire FPFTY be based on all plant put into place at any time during the FPFTY.

The use of average rate base for the FPFTY is fully compliant with Act 11. Facilities which are projected to be in service during the fully projected future test year are included in rate base for the specific period in which they are in place. *See* I&E Statement No. 3-SR, at 5-6. Thus, for example, facilities which go into service in the eighth month of the FPFTY are reflected in rate base only for the period in which they are used and useful, namely months 8 through 12 of the FPFTY. Act 11 in no way mandates that assets put in place at any time during the FPFTY must be fully reflected in the cost basis for service in every month of the FPFTY.

The Company also attempts to argue that the use of average rate base would complicate the issue of the distribution system improvement charge ("DSIC"), whereas the UGI Electric method is purportedly neutral. UGI Electric Statement No. 4-R, at 6-7. The OSBA rejects the illogic of this assertion. Essentially, the Company argues that it should be allowed to set rates on Day 1 of the FPFTY based on plant that will not be in place for up to 12 months, thus substantially over-recovering actual costs during the FPFTY. Then, under the Company's interpretation, it will be permitted to start raising rates under the DSIC mechanism as soon as the forecast year-end plant balance is exceeded. The Company has implicitly concluded that setting rates well in excess of costs for the FPFTY and at cost for subsequent years is a fair and reasonable ratemaking regime. Even if the use of average rate base may increase complexity related to the start-up of DSIC charges, that complexity is justified by avoiding the over-charging of ratepayers that comes with the Company's method. Moreover, the Company provides no explanation as to why starting up the DSIC based on a year-end methodology is materially less complex than starting up the DSIC under an average rate base approach.

In rejoinder testimony, the Company argued that the use of average rate base will cause the Company to begin using the DSIC mechanism sooner, and will thus file its next base rates case sooner than it would under the year-end approach. UGI Electric Statement No. 4-RJ, at 5. The OSBA acknowledges that a lower average rate base value will likely result in a DSIC going into effect earlier than under the year-end mechanism. However, the OSBA disagrees that allowing the use of year-end rate base will serve to defer future base rates proceedings. In its rejoinder, UGI Electric simply ignored the fact that if the Commission allows the use of year-end rate base as a regulatory mechanism, this will create an incentive for UGI Electric to file its next

base rates case sooner rather than later, because a rate increase would be justified by the higher rate base allowed under a year-end mechanism.

The OSBA therefore respectfully suggests that the period between rate cases would be more-or-less the same under the average and year-end methods, and would simply reflect the increase in costs from period to period based on the increase from average to average rate base, or the increase from year-end to year-end rate base. There is no merit to the Company's claim that the consistent use of average rate base will somehow shorten the periods between base rates proceedings.

VII. <u>Taxes</u>

B. Excess Accumulated Deferred Income Taxes

In developing the FPFTY revenue requirement, utilities include income tax costs based on revenues and expenses as recorded in their regulatory books, including normal depreciation expense. However, in practice, utilities (and of course other businesses) are allowed to use accelerated depreciation methods for computing actual tax liability. This reduces the cash cost for taxes. Since this tax bill will eventually come due (at least in theory), the difference in taxes between the two methods is recorded as a liability on the balance sheet called accumulated deferred income taxes ("ADIT"). In effect, accelerated tax depreciation provides a source of zero-cost financing to the utility. OCA Statement No. 1, at 12.

Ratepayers do not directly benefit from the lower cash taxes, so regulators generally require that ADIT be applied as an offset to utility claimed rate base. In effect, the financing benefits achieved by the Company through accelerated depreciation are passed back to ratepayers in the form of a lower rate base and thus lower financial costs.

The passage of the Tax Cut and Jobs Act ("TCJA") substantially lowered the federal statutory corporate income tax rate from 35 percent to 21 percent, which has significant implications for ADIT. For the period prior to the adoption of TCJA, the Company's financial statements essentially assumed that income tax expense was based on the statutory 35 percent rate, including the portion of the income taxes that were not paid in cash and deferred through the use of accelerated tax depreciation.

Because the statutory rate has been reduced, the Company has been recording a higher deferred expense than it will eventually bear, and thus the balance sheet needs to be corrected to reflect the lower tax obligation. Thus, lowering the statutory corporate tax rate means that the ADIT liability is overstated, and the Company's income/retained earnings are understated.

In effect, the impact of the TCJA was to convert a portion of the ADIT from being an interest-free loan from the government in the form of tax deferrals to being an interest free loan from ratepayers. I&E Statement No. 1-SR, at 37.

This overstatement in ADIT is therefore re-categorized into an excess accumulated deferred income tax ("Excess ADIT") account. Pursuant to the average rate assumption method ("ARAM"), this balance which will be phased out gradually as the income gain associated with the lower than expected tax bill is recognized on the income statement and in retained earnings. OCA Statement No. 1, at 11-12. The Excess ADIT account is a categorized as a regulatory liability, because the balances are gradually being returned to ratepayers. There does not appear to be any dispute that this accounting treatment is appropriate. OCA Statement No. 1, at 11

However, the Company proposed that this Excess ADIT *not* be included as an offset to utility rate base for the purpose of setting rates in this proceeding. This approach implies that the rate base offset related to ADIT will be substantially reduced as a result of the TCJA. In effect,

the Company is claiming that the rate base effect of the windfall it received from the TCJA should also result in an increase in both rate base and rates.

Experts for OCA and I&E both concluded that Excess ADIT should continue to serve as a credit to rate base in the same manner as ADIT.

OCA and I&E make simple, straight-forward arguments in support of their position. OCA witness Mr. Morgan explained that the shifting of balances from ADIT to Excess ADIT accounts is essentially that of a change in the name of the account, that the benefits of the TCJA reduction in the tax rate have not been fully returned to ratepayers, and therefore there is no reason to penalize ratepayers by changing the rate base treatment of these amounts. OCA Statement No. 1, at 12-13.

I&E witness Ms. Wilson explained that the funds in the ADIT account, including those shifted to the Excess ADIT account, were reflected in rates in prior years but not incurred by the Company as cash tax costs, making the funds available for investment. Ms. Wilson goes on to explain that these funds represented an interest-free loan from the government and now represent an interest-free loan from ratepayers. It is therefore inappropriate for the Company to charge ratepayers for interest on these balances.

In response, the Company appears to take the position that Commission precedent is that only ADIT should be reflected in a rate base credit, while all regulatory accounts are excluded from rate base and attract neither interest costs nor credits. UGI Electric Statement No. 9-R, a 4-5.

The Company's argument regarding precedent may be worth considering, but unless there is a specific case that is comparable to the current situation, precedent is unhelpful. For the Company's argument to have merit, UGI Electric should be required to demonstrate that there

were similar circumstances in which a particular rate base item (of significant cost) was effectively shifted to a regulatory account, and the Commission determined that it was initially appropriate to include the value in rate base and then excluded the value once shifted to the regulatory account. The OSBA observes that no such precedent was referenced in the Company's testimony, although the Company may do so in its briefs.

The OSBA submits that this issue boils down to a determination as to whether Excess ADIT is more like ADIT, or whether it is more like other regulatory liabilities. From that perspective, the matter is straightforward. These balances reflect costs that were at least implicitly included in rates but which were not actually paid in cash to the taxing authorities. This conclusion applies to both ADIT and Excess ADIT. The only change related to these balances is that before TCJA, the Company expected to eventually pay these costs in the future. After TCJA, the Company expects that it will need to eventually refund these costs to ratepayers. Thus, there is an extremely close parallel between ADIT and Excess ADIT.

In its rejoinder testimony, the Company offers the argument that, in the specific circumstances facing UGI Electric, the current ADIT balance does not reflect taxes that were reflected in rates because the accelerated depreciation which gave rise to the ADIT is related to assets placed in service since the Company's last base rates case in 1996.

The OSBA disagrees with the logic of this position, as it fails to recognize that the Company's rates for the past 22 years could have been adjusted to reflect the accumulation of deferred taxes, had the Company chosen to do so. But it did not. Assuming the Company is logical, in each year since the last base rates case it would compare the revenues that it was earning at approved rates with the revenues that it could justify if it were to file a base rates proceeding. And, of course, the revenues that the Company could earn in a base rates

proceeding would include corporate income taxes using normal depreciation, and would be offset by the ADIT rate base credit. Thus, the Company implicitly considered normal depreciation expense, normal corporate income tax expense and ADIT when it evaluated whether to file a base rates proceeding. In OSBA's view, this implies that the existing rates were sufficient to recover those costs, and thus ratepayers were implicitly being asked to contribute to those costs.

Therefore, the OSBA respectfully concludes that the rate base treatment of Excess ADIT should follow that of ADIT, and that Excess ADIT should be recognized as an offset to rate base.

IX. Rate Structure

A. Allocated Cost of Service Study

OSBA witness Robert D. Knecht described the three versions of an allocated cost of service study ("ACOSS") submitted by the Company in this proceeding, as follows:

> The Company's cost allocation methodology and the associated ACOSS are presented by Mr. John D. Taylor of Black and Veatch Corporation ('B&V'). The ACOSS model was originally submitted as Exhibit D, for the fully projected future test year ('FPFTY') ending September 30, 2019.
>
> It was subsequently updated to a 'revised' version on March 12, 2018 to reflect the implications of the Tax Cut and Jobs Act of 2017 on the Company's filing,
>
> and modified to a 'corrected revised' version on March 26, 2017 to reflect certain modest technical corrections.
>
> For the purposes of this testimony, I refer to the most recent 'revised corrected' version as the Company's filed ACOSS.

OSBA Statement No. 1, at 7 (formatting added).

In addition, Mr. Knecht explained that the Company's revised corrected ACOSS mostly conformed to Commission precedent:

> Mr. Taylor also prepared an ACOSS for PPL Electric Utilities Corporation ('PPL Electric') at Docket No. R-2015-2469275. This analysis [the PPL ACOSS] generally followed the earlier practices of PPL Electric, which have been substantially litigated over the past decade.
>
> In particular, the PPL Electric analysis used a minimum system methodology for classifying distribution system plant, and that method was explicitly approved by the Commission.
>
> In a couple of areas, my testimony contrasts the proposed approach offered by Mr. Taylor in this docket with the Commission-approved practices that he used for PPL Electric.

OSBA Statement No. 1, at 7 (footnote omitted) (formatting added).

Mr. Knecht identified eleven technical corrections to the Company's revised corrected ACOSS. *See Id.*, at 8-10. The eleven corrections had minimal impact on the overall results of the ACOSS. *Id.*

Mr. Knecht also identified six methodological modifications to the Company's revised corrected ACOSS:

> 1. The ACOSS should separately allocate costs to the GS-1 and GS-4 rate classes, in light of the substantial differences between the classes in terms of both customer characteristics and rate design;
>
> 2. The Company's minimum system calculations for classification of poles costs understate the customer component of costs;
>
> 3. Line transformers costs should be classified into both customer and demand components, as opposed to the Company's method which treats them as 100 percent demand-related;
>
> 4. The Company allocates line transformer costs using a primary system demand allocator. As line transformers generally serve to step down voltage from primary to secondary systems, these assets are used only by secondary customers, and costs should be allocated accordingly.

> 5. The meters allocator for the lighting class should be consistent with the Company's workpapers for the development of the meters cost allocator;
>
> 6. The methodology used to develop the Company's non-coincident peak demand allocator requires some additional clarification.

OSBA Statement No. 1, at 11 (footnote omitted).

The OSBA respectfully submits that the Company erred by combing the GS-1 and GS-4 rate classes in their revised corrected ACOSS. Mr. Knecht explained the issue, as follows:

> [T]he GS-1 and GS-4 classes have substantial differences in the nature of the businesses (and other entities), in the average customer size, and in the type and magnitude of tariff charges. In light of these differences, it would generally be logical to separate the classes for the purposes of cost allocation. For example, PPL Electric does so for its GS-1 and GS-3 classes, which have certain similarities to the UGI Electric rate categories. Moreover, my recollection is that UGI Electric separated these classes for cost allocation purposes in its last base rates case.

OSBA Statement No. 1, at 11-12 (footnote omitted).

UGI Electric's defense for combining GS-1 and GS-4 was that "it was deemed that current rate designs for GS-1 and GS-4 would likely be in relative alignment without further need for segregation." *Id.*, at 12 (footnote omitted). Mr. Knecht responded to the Company's argument, as follows:

> I respectfully disagree with that rationale for several reasons:
>
> First, this logic presupposes that the Company's cost allocation method will be approved by the Commission. I expect that some parties to this proceeding, myself included, may disagree.
>
> Second, ***simply because the combined revenues from GS-1 and GS-4 are basically in balance with the combined costs for those classes does not necessarily imply that each class is in balance.*** Without running the numbers, it is impossible to determine whether one class's revenues substantially exceeds costs while the other class's revenues fall short of costs.

> Third, both the GS-1 and GS-4 rate classes have both a significant customer base and a significant load. Specifically, the GS-1 class has a forecast load of about 26 GWh or about 2.5 percent of UGI Electric total. Furthermore, the GS-1 class represents a significant share of the non-residential/non-lighting service, at 66 percent of the customers, 5.7 percent of the load, and nearly 12 percent of the distribution revenues. Rate GS-4 represents approximately 30 percent of non-residential/non-lighting customer count and load, and some 44 percent of revenues.
>
> Fourth, rate design should be based, at least in part, on the results of the ACOSS. Thus, for example, setting the customer charge for the GS-1 class should reflect the customer-related costs assigned to that class in the ACOSS. Because meters and services costs tend to be lower for smaller customers in the GS-1 class than for the larger customers in the GS-3 class, the use of a combined class in the ACOSS is not useful for GS-1 rate design.

OSBA Statement No. 1, at 12-13.

The remaining five methodological issues identified by Mr. Knecht, set forth above, are addressed, in detail, in Mr. Knecht Direct Testimony. See OSBA Statement No. 1, at 13-17.

As a result of the technical corrections and methodological issues in the Company's revised correct ACOSS, Mr. Knecht created his own ACOSS:

> As I indicated in my direct testimony, I prepared an independent version of the Company's ACOSS spreadsheet model, which replicated the Company's calculations.
>
> I also identified a variety of relatively minor technical errors in the Company's model, as well as several areas of professional disagreement with respect to the Company's cost allocation methodology.
>
> I also explained why the 'General Service' rate class used in the UGI Electric ACOSS should be segregated into 'GS-1' and 'GS-4' categories.

OSBA Statement No. 1-SD (formatting added). Mr. Knecht created two versions of his ACOSS: one, a four-class model (with GS-1 and GS-4 combined); and a five-class model (with GS-1 and GS-4 separated). *Id.*, at 1-2.

Mr. Knecht explained the Table, set forth below, that illustrates the results of the Company's revised corrected ACOSS and Mr. Knecht's ACOSS:

> Table IEc-SD1 below shows the revenue shortfall and current rates for the Company's ACOSS and my two simulations. This shortfall depicts the magnitude of the rate increase (decrease) needed to bring current rates into line with allocated cost.

OSBA Statement No. 1-SD, at 2.

Table IEc-SD1 ACOSS Comparison: Current Revenue Shortfall $000			
	UGI ACOSS	RDK 4-Class ACOSS	RDK 5-Class ACOSS
Residential	9,782	10,372	10,372
GS-1	(708)	(787)	805
GS-4			(1,592)
Large Power	(374)	(785)	(785)
Lighting	(208)	(308)	(308)
System	**8,492**	**8,492**	**8,492**
Sources: RDK Workpapers			

OSBA Statement No. 1-SD, at 2. Note that this Table reflects the updated overall revenue requirement requested by the Company. Mr. Knecht prepared a second table, using a "normalized revenue-cost ratio." Mr. Knecht explained this metric, as follows:

> Because current revenues fall short of the revenue requirement in the ACOSS, the revenue-cost ratios are 'normalized' for that difference such that the average revenue-cost ratio at current rates is 100 percent. Revenue-cost differentials and revenue-cost ratios are vastly superior metrics of revenue-cost performance to the flawed 'indexed rate of return' metric often used by Pennsylvania utilities.

OSBA Statement No. 1-SD, at 2, footnote 1.[1] Mr. Knecht continued:

> Table IEc-SD2 below depicts the results of the same simulations, except it uses a normalized revenue-cost ratio at current rates rather than the difference between current revenues and allocated costs. A ratio of 100 percent implies that current revenues equal (normalized) current costs. A ratio above 100 percent indicates that class revenues are, on a relative basis, over-recovering allocated costs, and a ratio below 100 percent indicates relative under-recovery.

[1] The indexed rate of return metric, as well as the flat-earth theory, should be consigned to the dustbin of history.

OSBA Statement No. 1-SD, at 2-3. Table IEc-SD2 is set forth below:

Table IEc-SD2 ACOSS Comparison: Normalized Revenue-Cost Ratios			
	UGI ACOSS	RDK 4-Class ACOSS	RDK 5-Class ACOSS
Residential	86%	85%	85%
GS-1	134%	136%	83%
GS-4			165%
Large Power	130%	140%	140%
Lighting	153%	175%	175%
System	**100%**	**100%**	**100%**
Sources: RDK Workpapers			

The results of combing versus splitting the GS-1 and GS-4 classes is clearly seen both Tables IEc-SD1 and IEc-SD2, above. It would be a violation of Section 1502 of the Public Utility Code, 66 Pa. C.S. Section 1502 (Discrimination in service), to combine GS-1 and GS-4 as originally proposed by UGI Electric. The Company's revised corrected ACOSS, with the rate classes combined, created a substantial rate benefit for the GS-1 class at the expense of the GS-4. That is the definition of "unreasonable preference," as it is a straight forward mathematical exercise to separate the two.

Mr. Knecht's ACOSS does not change the basic revenue allocation patterns evident in the Company's revised correct ACOSS. For example, the Residential rate class still demonstrates a major revenue shortfall, while the Lighting rate class is over-recovering its cost of service. See OSBA Statement No. 1-SD, at 3-4.

In summary, Mr. Knecht's ACOSS corrects a series of technical errors, splits GS-1 and GS-4 into separate classes are required by Section 1502, and modifies the Company's revised corrected ACOSS so that it is more consistent with Commission precedent.

In its rebuttal testimony, the Company agreed with the vast majority of Mr. Knecht's technical recommendations, and it prepared an updated ACOSS based on that analysis. The Company's cost allocation expert Mr. Taylor stated:

> In short, OCA witness Mr. Mierzwa's suggested adjustments do not follow principles of cost causation whereas Mr. Knecht's suggested adjustments do follow these principles. As such, I have rejected all but one of Mr. Mierzwa's suggested adjustments and have updated the Company's rebuttal version of the allocated class cost of service study to take into account the suggestions provided by Mr. Knecht.

UGI Electric Statement No. 6-R, at 2.

In surrebuttal testimony, Mr. Knecht acknowledged that the adjustments made by the Company in its rebuttal ACOSS were reasonably consistent with his recommendations, and that any remaining disagreements had minimal quantitative impact. OSBA Statement No. 1-SR, at 1.

The OSBA therefore respectfully submits that the Commission should adopt either Mr. Knecht's ACOSS or the Company's rebuttal ACOSS for the purposes of revenue allocation and rate design in this proceeding.

B. Revenue Allocation

Mr. Knecht's ACOSS demonstrates that both the Residential and GS-1 customer classes are under-recovering their cost of service. Mr. Knecht also observed:

> [T]he very long period over which [the Residential class's] rates have been far below allocated costs. Based on the results of my cost allocation analysis, the same logic should apply to the GS-1 customers. I therefore recommend that an increase commensurate to that applied to the Residential class be assigned to the GS-1 class.

OSBA Statement No. 1, at 4. Mr. Knecht proposed the following revenue allocation:

Table IEc-SD3 UGI Electric Revenue Allocation Summary				
	UGI Revenue Allocation		RDK Revenue Allocation	
	$000	Percent*	$000	Percent*
Residential	8,476	39.9%	8,476	39.9%
GS-1	19	1.2%	622	39.9%
GS-4	(4)	-0.1%	(516)	-9.2%
Large Power	–	0.0%	–	0.0%
Lighting	–	0.0%	(91)	-9.2%
System	**8,491**	**24.2%**	**8,491**	**24.2%**

* Percent increase in current rates excluding electric supply costs.

Source: Corrected revised Exhibit D, revised Exhibit E; RDK Workpapers

OSBA Statement No. 1-SD, at 5.

Mr. Knecht explained, in detail, his revenue allocation recommendations, as follows:

> I am aware that the Commission has, in some proceedings, declined to assign an overall rate decrease to certain rate classes. The Commission has also, on occasion, approved average rate decreases to some classes in extraordinary circumstances. In this case, I believe the circumstances are extraordinary, in that there has not been a base rates proceeding for 22 years, and because the revenue-cost differences for the GS-4 and Lighting classes are very large.
>
> Moreover, assigning the additional revenues to offset the increase to the Residential class (and comparably reduce the GS-1 increase) would have only a small impact, as it would reduce the magnitude of the increase to those classes by only about 2.3 percentage points compared to a nearly 40 percent increase.
>
> Thus, assigning no decreases to the GS-4 and Lighting classes would require that the Commission forego an opportunity to make substantial additional progress toward cost-based rates in exchange for a relatively small benefit for the small-customer rate classes.

> In addition, I characterize my proposal as a revenue allocation issue for both Rate GS-1 and GS-4. In the Company's thinking, however, my proposal would involve only a small average increase for the combined 'General Service' rate class, and that how that revenue allocation is distributed among all of the General Service customers is a matter of rate design.
>
> As such, I conclude that the specific circumstances in this case justify the average rate decreases that I propose.

OSBA Statement No. 1-SD, at 5-6 (formatting added).

Furthermore, the revenue allocation proposed by Mr. Knecht complies with the decision of the Commonwealth Court in *Lloyd v. Pennsylvania Public Utility Commission*, 904 A.2d 1010, 1020 (Pa. Cmwlth. 2006). In *Lloyd*, the Court stated that cost of service is the "polestar" guiding rates cases such as this one. Therefore, using Mr. Knecht's accurate, just, and reasonable ACOSS, the rationale (set forth above) for his proposed revenue allocation, and the legal requirements of *Lloyd*, the OSBA respectfully submits that the ALJs and Commission adopt the OSBA revenue allocation.

C. Rate Design

1. Summary of Proposed Rate Design

The OSBA's proposed rate design for the GS-1 customer class is set forth below:

Table IEc-SD4 Pennsylvania EDC Tariff Rates for Small General Service Customers			
	Rate	Customer Charge ($/month)	Energy Charge (cents/kWh)
UGI Electric Current	GS-1	$6.75	4.035
UGI Electric Proposed	GS-1	$6.75	4.0725
RDK Directional	GS-1	$14.00	4.7025
PPL Electric	GS-1	$22.00	*
Metropolitan Edison	GS-Small	$21.88	4.069
Pennsylvania Electric	GS-Small	$18.33	3.624
Penn Power	GS-Small	$24.89	3.623
West Penn Power	Rate 20 GS	$9.52	3.529
PECO	GS**	$14.28	4.560

* PPL Electric applies a $4.361 per kW demand charge, as all customers have smart meters.

** Single-phase service without demand measurement; most PECO GS customers have demand meters.

Source: Utility tariff schedules on-line, reviewed April 23, 2018.

OSBA Statement No. 1-SD, at 7.

The OSBA's proposed rate design for the GS-4 customer class is set forth below:

Table IEc-SD5 UGI Electric Rate GS-4 Distribution Tariff Charges			
	Current	UGI Proposed	RDK Alternative
Customer Charge ($/month)	$0.00	$0.00	$15.00
First 20 kW Demand ($/kW/mo.)	$3.59	$3.59	$3.59
Over 20 kW Demand ($/kW/mo.)	$1.30	$1.30	$2.20
First 200 kWh/kW (cents/kWh)	3.033	2.982	2.222
Next 300 kWh/kW (cents/kWh)	2.303	2.303	1.533
Over 500 kWh/kW (cents/kWh)	2.031	2.031	1.261
Source: Exhibit IEc-SD1			

OSBA Statement No. 1-SD, at 8.

The OSBA's proposed rate design for the LP-4 customer class is set forth below: below:

Table IEc-SD6: CORRECTED UGI Electric Rate LP Distribution Tariff Charges			
	Current	UGI Proposed	Corrected RDK Alternative
Customer Charge ($/month)	$0.00	$0.00	$0.00
First 100 kW Demand ($/kW/mo.)	$1.358	$1.358	$2.00
Next 400 kW Demand ($/kW/mo.)	$0.940	$0.940	$1.60
Over 600 kW Demand ($/kW/mo.)	$0.690	$0.690	$1.40
First 100 kWh/kW (cents/kWh)	1.696	1.672	1.508
Next 200 kWh/kW (cents/kWh)	1.518	1.518	1.330
Next 200 kWh/kW (cents/kWh)	1.383	1.383	1.195
Over 500 kWh/kW (cents/kWh)	1.295	1.295	1.107
Source: Exhibit IEc-SR1			

OSBA Statement No. 1-SR, at 3.

It must, of course, be recognized that this rate design is based both on the Company's overall proposed increase in revenue and based on Mr. Knecht's proposed revenue allocation. If either of these parameters is modified by the Commission, the rate design must be adjusted accordingly. Mr. Knecht therefore characterized these rate design recommendations as "directional," and OSBA recommends that the Commission do the same. OSBA Statement No. 1-SD, at 6.

3. Non-Residential Customer Charges

In this proceeding, the Company proposed only very small overall changes in revenue from the non-residential rate classes. The Company implicitly concluded that because there was no need to change revenue, the existing rate design was reasonable. The OSBA respectfully disagreed, since it has been more than 20 years since the Company's last base rates proceeding

and its non-residential rate design reflects economic conditions in the era before the deregulation of generation services and rate unbundling. Mr. Knecht therefore offered detailed recommendations regarding both the strategy for rate evolution and for specific changes to non-residential tariff structure.

Mr. Knecht explained his proposed GS-1 customer class rate design, as follows:

> As I indicated in my direct testimony, the base distribution rates for GS-1 consist of a monthly customer charge, a flat per-kWh distribution energy charge, and the EEC Rider charge. I also indicated that the customer charge was far below both allocated customer costs for the class and the customer charges for small general service customers at all major Pennsylvania EDCs. I suggested that the customer charge be increased, with an offsetting reduction in the energy charge.
>
> However, in light of my revenue allocation recommendation, it would be necessary to increase both the customer charge and the energy charge in order to achieve the class revenue requirement. I suggest that the customer charge increase follow the Company's recommendation for the Residential class to $14.00 per month, and that the energy charge be increased as necessary to achieve the rate increase.

OSBA Statement No. 1-SD, at 6-7.

Mr. Knecht explained his proposed GS-4 customer class rate design, as follows:

> As I explained in my direct testimony, most other Pennsylvania EDCs have a distribution tariff for medium general service customers consisting of a customer charge and a flat demand charge. UGI Electric, by contrast, has a tariff with no customer charge, but with a two-block demand charge and a three-block 'Wright' energy charge. I recommended phasing out this tariff by adding a customer charge, increasing the demand charge, and decreasing the energy charges.

OSBA Statement No. 1-SD, at 8.

Finally, Mr. Knecht explained his proposed LP-4 customer class rate design, as follows:

> My recommendations for the LP tariff generally followed those for Rate GS-4. In my direct testimony I recommended including a customer charge or retaining a two-block demand charge, reducing

> demand charge block differentials (except as an alternative to the customer charge), and reducing the Wright energy charge.

OSBA Statement No. 1-SD, at 8.

The OSBA is cognizant that rate design is a complex issue in any base rates case, and that the 22 years between now and the time that UGI Electric last filed a base rates case makes these rate design issues even more complicated.

Mr. Knecht reviewed the rate design issues in detail in his Direct Testimony, and the OSBA is hesitant to include that level of detail in this Main Brief. For the convenience of the ALJs and the Commission, the OSBA will note that Mr. Knecht, in his Direct Testimony, describes the General Service rate classes on pages 2-4; addresses the GS-1 rate class on pages 21-21; addresses the GS-4 rate class on pages 22-24; and addresses the LP-4 rate class on page 24-25.

In its rebuttal testimony, the Company voiced general agreement with Mr. Knecht's "directional" rate design recommendations. UGI Electric Statement No. 8-R, at 12-13 and 14-15. The only area of disagreement resulted from inadvertent calculation errors in Mr. Knecht's LP-4 rate design analysis in direct testimony which implied that he favored an overall rate increase for that class. Mr. Knecht clarified this matter in surrebuttal, confirming that he did not propose an overall increase for that class, and adjusting the "directional" rate design calculations accordingly. OSBA Statement No. 1-SR, at 1-3.

The OSBA observes that no other party submitted direct or rebuttal testimony on the matter of non-residential rate design. As such, there appears to be general agreement with the direction that non-residential rate design should be headed.

Rate Design naturally flows out of the resolution of other issues in a base rates case: the overall revenue requirement awarded; the ACOSS selected; and the revenue allocation adopted.

The Rate Design proposals for the General Service classes, set forth above, are a just and reasonable method for recovering the costs assigned to those rate classes, and also will bring the Company's rate design into the 21st century.

Consequently, the OSBA respectfully requests that the ALJs and the Commission adopt the rate design proposals set forth in Mr. Knecht's testimony and this Main Brief.

D. Scale Back

OSBA's revenue allocation recommends rate increases only for the Residential and the GS-1 rate classes, of which the vast majority is assigned to the Residential class. The other classes are assigned rate decreases. Any reduction from the full revenue requirement requested by the Company should be proportionally assigned to the Residential and GS-1 classes. There is no overwhelming need to give classes that are assigned a rate decrease any additional relief.

Therefore, the OSBA recommends that any scaleback be a traditional proportional scaleback applied only to those classes that are assigned rate increases.

XII. Conclusion

Wherefore, based upon this Main Brief and the written testimony of the OSBA, the OSBA respectfully requests that the ALJs and the Commission decide these specific issues, as follows:

Approve the *Partial Stipulation* without modification;

Decide that the FPFTY rate base should be based on average net plant values throughout the year, and that FPFTY depreciation should reflect forecast depreciation for the test year;

Decide that the rate base treatment of Excess ADIT should follow that of ADIT, and that Excess ADIT should be recognized as an offset to rate base;

Adopt either Mr. Knecht's ACOSS or the Company's "rebuttal testimony" ACOSS for the purposes of revenue allocation and rate design in this proceeding;

Adopt Mr. Knecht's revenue allocation recommendations for the Company's rate classes;

Adopt Mr. Knecht's recommendations for the rate design of the GS-1, GS-4, and LP-4 rate classes; and

Employ a traditional proportional scaleback only to those rate classes that are assigned rate increases.

Respectfully submitted,

Steven C. Gray
Assistant Small Business Advocate
Attorney ID No. 77538

For: John R. Evans
Small Business Advocate

Office of Small Business Advocate
300 North Second Street, Suite 202
Harrisburg, PA 17101

Dated: July 2, 2018

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:	
	:	
v.	:	**Docket No. R-2017-2640058**
	:	**Docket No. C-2018-2647268**
UGI Utilities, Inc. – Electric Division	:	

CERTIFICATE OF SERVICE

I hereby certify that true and correct copies of the foregoing have been served via email and/or First-Class mail (*unless other noted below*) upon the following persons, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant).

The Honorable Steven K. Haas
The Honorable Andrew M. Calvelli
Pennsylvania Public Utility Commission
400 North Street
Commonwealth Keystone Building
Harrisburg, PA 17120
sthaas@pa.gov
acalvelli@pa.gov
(Email and Hand Delivery)

Scott B. Granger, Esquire
Bureau of Investigation & Enforcement
400 North Street
Commonwealth Keystone Building
Harrisburg, PA 17120
sgranger@pa.gov
(Counsel for BIE)
(Email and Hand Delivery)

Hayley E. Dunn, Esquire
Aron J. Beatty, Esquire
Office of Consumer Advocate
555 Walnut Street, 5th Floor
Harrisburg, PA 17101
HDunn@paoca.org
ABeatty@paoca.org
(Counsel for OCA)
(Email and Hand Delivery)

Jerome D. Mierzwa
Lafayette K. Morgan
Exeter Associates, Inc.
10480 Little Patuxent Parkway
Suite 300
Columbia, MD 21044
jmierzwa@exeterassociates.com
lmorgan@exeterassociates.com
(Expert Witnesses for OCA)

Michael J. Majoros, Jr.
James Garren
Snavely King Majoros & Associates, Inc.
PO Box 727
Millersville, MD 21108
mmajoros@snavely-king.com
jgarren@snavely-king.com
(Expert Witnesses for OCA)

Aaron L. Rothschild
Rothschild Financial Consulting
15 Lake Road
Ridgefield, CT 06877
aaron@rothschildfinancial.com
(Expert Witness for OCA)

Roger D. Colton
Fisher, Sheehan & Colton
34 Warwick Road
Belmont, MA 02478
roger@fsconline.com
(Expert Witness for OCA)

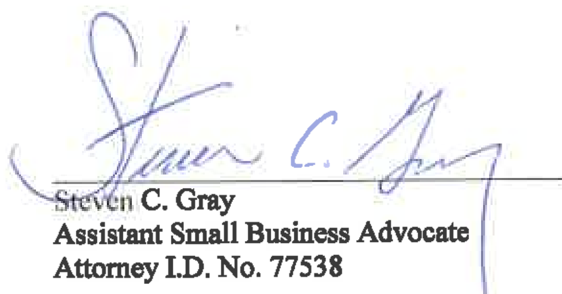
Mark C. Morrow, Esquire
Danielle Jouenne, Esquire
UGI Utilities, Inc.
460 North Gulph Road
King of Prussia, PA 19406
morrowm@ugicorp.com
jouenned@ugicorp.com
(Counsel for UGI)

David B. MacGregor, Esquire
Post & Schell, P.C.
Four Penn Center
1600 John F. Kennedy Boulevard
Philadelphia, PA 19103
dmacgregor@postschell.com
(Counsel for UGI)

Garret P. Lent, Esquire
Post & Schell, P.C.
17 North Second Street, 12th Floor
Harrisburg, PA 17101
glent@postschell.com
(Counsel for UGI)

Jessica R. Rogers, Esquire
Post & Schell, P.C.
607 14th Street NW
Suite 600
Washington, DC 20005
jrogers@postschell.com
(Counsel for UGI)

DATE: July 2, 2018



Steven C. Gray
Assistant Small Business Advocate
Attorney I.D. No. 77538