

**PECO ENERGY COMPANY
STATEMENT NO. 2**

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

**PETITION OF PECO ENERGY COMPANY
FOR EXPEDITED APPROVAL OF ITS
MARKET RATE TRANSITION PHASE-IN PROGRAM**

DOCKET NO. P- _____

DIRECT TESTIMONY

WITNESS: ALAN B. COHN

**SUBJECT: PECO ENERGY COMPANY'S MARKET
RATE TRANSITION PHASE-IN TARIFF RIDER**

DATED: SEPTEMBER 10, 2008

TABLE OF CONTENTS

I. INTRODUCTION AND PURPOSE OF TESTIMONY 1

**II. PECO’S PROPOSED MARKET RATE TRANSITION PHASE-IN
TARIFF RIDER..... 3**

**III. COST RECOVERY FOR THE MARKET RATE TRANSITION
PHASE-IN PROGRAM AND THE CUSTOMER EDUCATION
PLAN..... 15**

IV. CONCLUSION 18

1
2
3
**DIRECT TESTIMONY
OF
ALAN B. COHN**

4
I. INTRODUCTION AND PURPOSE OF TESTIMONY

5 1. **Q. Please state your full name and business address.**

6 A. My name is Alan B. Cohn. My business address is PECO Energy Company,
7 2301 Market Street, 15th Floor, Philadelphia, Pennsylvania 19103.

8 2. **Q. By whom are you employed and in what capacity?**

9 A. I am employed by PECO Energy Company (“PECO” or the “Company”) as
10 Manager of Revenue Analysis in the Regulatory group.

11 3. **Q. Please describe your educational background.**

12 A. I received a Bachelor of Science Degree in Commerce and Engineering from
13 Drexel University in 1980. I received a Masters Degree in Business
14 Administration from Drexel in 1985. In addition, I have completed the
15 American Gas Association (“AGA”) Gas Rate Fundamentals Course at the
16 University of Wisconsin and the AGA Advanced Gas Rate Course at the
17 University of Maryland.

18 4. **Q. Please describe your work experience in the energy industry.**

19 A. Upon graduation from college in 1980, I was hired by PECO as a Rate Analyst
20 in the Cost and Load Analysis Section of the Rate Division. In 1987, I was
21 appointed Supervisor of the Economic Analysis Section in PECO’s Rates and

1 Regulatory Affairs Division. Since that time, I have held various management
2 positions in PECO's Rates and Regulatory Affairs Department and Strategic
3 Planning Department, where I had responsibility for managing base rate case
4 filings, cost of service studies and financial and economic analyses.

5 **5. Q. Have you testified previously before this Commission or other regulatory**
6 **bodies?**

7 A. Yes. I have testified in regulatory proceedings before the Pennsylvania Public
8 Utility Commission (the "Commission"), the Federal Energy Regulatory
9 Commission and the Maryland Public Service Commission. A list of the
10 cases in which I have submitted testimony is attached hereto as Exhibit ABC-
11 1.

12 **6. Q. What is the purpose of your direct testimony?**

13 A. The purpose of my testimony is two-fold. First, I will explain PECO's
14 proposed Market Rate Transition Phase-In Tariff Rider (the "Phase-In Rider"),
15 which will offer eligible customers an option to mitigate the impact on their
16 electric bills of the increase in price for generation supply service that PECO
17 anticipates will occur as of January 1, 2011, when the caps on its generation
18 rates expire. As Mr. Webster explains, the Phase-In Rider is part of a larger
19 rate mitigation plan, which also includes PECO's proposed Market Rate
20 Transition Deferral Program (the "Deferral Program"), PECO's Market Rate
21 Transition Energy Efficiency Package ("EEP"), and PECO's Commission-

1 approved Customer Education Program.¹ The Deferral Program will be
2 included in the Company's default service plan ("DSP") filing, and the EEP
3 will be part of a separate but concurrent filing.

4 The second purpose of my testimony is to describe the rate mechanism PECO
5 proposes to establish under Section 1307 of the Public Utility Code to recover
6 the costs it will incur to implement and administer the Phase-In Rider and its
7 Consumer Education Program.

8 **7. Q. Are you sponsoring any exhibits?**

9 A. Yes, I am sponsoring the following exhibits:

- Exhibit ABC-1 List Of Prior Testimony
- Exhibit ABC-2 Tariff Supplement Per Phase-In Rider And Cost Recovery Mechanism
- Exhibit ABC-3 Calculation Of Phase-In Pre-Payment And Credit Factors
- Exhibit ABC-4 Illustrative Calculation Of Phase-In Plan Operation For Rate R
- Exhibit ABC-5 Estimated Plan Implementation And Administration Costs

10 **II. PECO'S PROPOSED MARKET RATE TRANSITION**
11 **PHASE-IN TARIFF RIDER**

12 **8. Q. Please explain the Phase-In Rider.**

13 A. The Phase-In Rider is a proposed addition to PECO's Tariff Electric – Pa.
14 P.U.C. No. 3 that will offer eligible customers a rate option designed to allow

¹ PECO's Customer Education Plan was approved by the Commission by Order entered August 8, 2008 at Docket No. M-2008-2032274.

1 them to transition to higher market-based prices for generation supply service
2 over a period of three and one-half years through a series of increases.²
3 Exhibit ABC-2 is a tariff supplement that sets forth the proposed Phase-In
4 Rider as “Original Page No. 96C.” Although the caps on PECO’s generation
5 rates for default service do not expire until January 1, 2011, the Phase-In Rider
6 will give eligible customers the option, beginning July 1, 2009, to make
7 advance payments to cover a portion of the increase expected to occur as of
8 January 1, 2011. A customer choosing this option will experience a gradual
9 series of increases in the price of generation service each year from 2009 to
10 2013. To make this happen, the pre-payments that customers make in 2009
11 and 2010, plus accrued interest on those pre-payments, will be applied to
12 customers’ bills as credits in 2011 and 2012. The credits will decline each
13 year and expire as of December 31, 2012, so that beginning January 1, 2013
14 these customers’ bills will reflect the cost of generation supply service.

² For most customer classes the phase-in period will be three and one-half years. However, for customers served on Rate RH (Residential Heating) and Rate OP (Off Peak) the phase-in period will be four and one-half years. PECO is proposing a somewhat longer phase-in for customers on Rates RH and OP because, as part of its DSP filing, PECO will also propose to phase-out the declining blocks and demand charges for the generation portion of these rates. The longer phase-in for these customers, combined with the phase-out of the current rate design, will provide a smoother transition. For purposes of this testimony, I will discuss the three and one-half year phase-in.

1 **9. Q. You indicated that interest would be paid on the pre-payments. Please**
2 **elaborate.**

3 A. During the period PECO is holding customers' pre-payments, those amounts
4 will accrue interest at the statutory rate of 6%, which will be compounded
5 monthly.

6 **10. Q. How has PECO calculated the pre-payments for 2009 and 2010?**

7 A. In order to calculate appropriate pre-payment levels, PECO had to estimate the
8 increases in generation supply rates for each eligible customer class that will
9 occur on January 1, 2011, when generation supply will reflect market prices.
10 As the basis for those estimates, PECO used the prices established by the
11 successful bids in PPL Electric Utilities Corporation's ("PPL") March 2008
12 request for proposals ("RFP") for full requirements default supply service for
13 the year 2010. However, PECO had to adjust the RFP results to recognize
14 differences between PECO and PPL. Once the adjustments were made and a
15 2011 estimated increase developed, the proposed pre-payment schedule was
16 established.

17 **11. Q. Please explain the adjustments PECO made to the PPL RFP prices.**

18 A. PECO made four adjustments. The first is a basis adjustment to recognize the
19 historic difference between the PJM Interconnection, LLC's ("PJM")
20 locational marginal prices ("LMP") at the PECO and PPL zones. A basis
21 difference arises because not all zones within PJM have the same underlying

1 LMP. The differences are due to congestion or other factors. PECO analyzed
2 data for 2006 and 2007 that compared the LMPs at the PECO and PPL zones,
3 respectively, to the LMP at PJM's Western Hub (the delivery point for
4 exchange-traded futures). This analysis shows that, historically, PECO's LMP
5 has been approximately 2% higher than PPL's. The results of the PPL RFP
6 were adjusted accordingly.

7 A second adjustment was made to have the capacity cost reflect PECO's load
8 factor. This adjustment is necessary because PPL has a higher load factor than
9 PECO. A higher load factor affects the cost to acquire generation supply.
10 With that in mind, PECO calculated its load factors based on its peak load
11 contribution (as defined by PJM) and compared it to similarly calculated load
12 factors that PPL provided to potential bidders in its RFP. The comparison
13 shows significantly better load factors for PPL:

	PPL	PECO
Residential	61%	46%
Small Commercial and Industrial	66%	44%

14 The calculated load factor differences were translated into price differences
15 and used to adjust the RFP results. The adjustment was made by converting
16 the capacity cost derived from PJM's Reliability Pricing Model ("RPM")
17 auction to a dollar-per-MWh value. To do so, the RPM price, which is
18 expressed in dollars per MW-day, was divided by 24 hours, and the quotient

1 of that calculation was divided by the respective load factors. The results of
2 these calculations for PPL and PECO were compared to derive the adjustment.

3 The third adjustment was made to reflect the difference between a 2010 cost
4 basis and a 2011 cost basis. This adjustment is necessary because PPL's RFP
5 solicited bids for default service generation supply for 2010, while PECO
6 needs to estimate its costs for 2011. The difference between 2010 and 2011
7 prices was derived from energy futures trading in April shortly after the PPL
8 RFP was made public. The comparison was done by combining the on and
9 off-peak futures prices at the PJM Western Hub for 2010 and 2011,
10 respectively, to obtain the all-hours price for both 2010 and 2011. The
11 difference between these calculated values is the basis for the adjustment.

12 The fourth adjustment reflects differences in cost caused by differences in load
13 shape. Customers use more energy in the higher priced hours. Therefore, a
14 load shaping premium needs to be added to the all-hours price to account for
15 this fact. Comparing PECO to PPL, PECO's customers use proportionately
16 more energy in the higher-priced hours than PPL's customers. The load
17 shaping premiums supplied by PPL to bidders in its RFP were compared to
18 PECO's estimated load shaping premiums. The PECO premiums are about
19 1% higher, and the PPL RFP prices were adjusted accordingly.

20 **12. Q. What was the overall effect of the adjustments you described above?**

21 **A.** The net effect of the foregoing four adjustments is to increase the PPL RFP
22 prices (excluding line losses and gross receipts tax) from \$96.88 per MWh to

1 \$100.25 per MWh for the residential procurement group and from \$96.84 per
2 MWh to \$101.73 per MWh for the small commercial and industrial
3 procurement group. For purposes of its RFP, PPL did not have a procurement
4 group that corresponds to PECO's medium commercial and industrial
5 procurement group. Therefore, PECO started with the PPL RFP price for its
6 small commercial and industrial procurement group and made all of the
7 adjustments described above except the load shaping adjustment. This
8 produced a price of \$96.04/MWh.

9 **13. Q. How were the adjusted prices from the PPL RFP used to determine the**
10 **appropriate level of pre-payments?**

11 A. Using the adjusted prices, PECO estimated the rate increase that each eligible
12 rate class would experience as of January 1, 2011. The rate increases for each
13 class were used to develop the equal increases that would have to occur on
14 July 1, 2009 and January 1, 2010, 2011 and 2012 to move customers' current,
15 capped default service rates to the estimated rate levels over a period of three
16 and one-half years. (The July 1, 2009 increase will only be in effect for six
17 months.) This calculation is shown in Exhibit ABC-3 accompanying my
18 testimony.

19 **14. Q. Please explain the calculation described above for one of the eligible rate**
20 **classes.**

1 A. As shown on Exhibit ABC-3, PECO estimated that Rate R customers will
2 experience an increase of 17% in 2011.³ Under the Market Rate Transition
3 Phase-In Program (the “Phase-In Program”), a Rate R customer would pay an
4 additional \$0.0053 per kWh starting in July 2009. This additional charge
5 would increase to \$0.0107 per kWh in 2010. Because pre-payment charges
6 will be applied on a per-kWh basis, the higher a customer’s usage, the more
7 the customer pre-pays. Making pre-payments a function of usage will scale
8 the resulting credits to the post-2011 increase in generation supply costs a
9 customer is likely to experience, which will also be a function of usage. The
10 amounts pre-paid by the customer in 2009 and 2010 would be credited to the
11 customer in 2011 and 2012. The 2011 monthly credit will be 5.822% of the
12 accumulated pre-payment plus interest at the end of 2010. The 2012 monthly
13 credit will be 2.911% of the accumulated prepayments plus interest at the end
14 of 2010. The pre-payments and credits produce a series of increases equal to
15 3.4% of an average customer’s total bill that will occur as of July 2009,
16 January 2010 and January 2011, and 0.4% increases as of January 2012 and
17 January 2013. The 2012 and 2013 increases are lower due to the effect of the
18 phase-out of the residential rate design that I previously described. Similar
19 calculations were done for each of the eligible rate classes, and the results are
20 shown in Exhibit ABC-3. Exhibit ABC-3 also shows how the increases

³ If all other things remain equal, an **average** Rate R customer will experience decreases of 2% in 2012 and 2013 that result from phasing-out the existing rate design for this rate class, which PECO proposes in its DSP filing. However, the class as a whole will not experience a decrease. Instead, intra-class differences in usage characteristics will result in some customers experiencing somewhat larger decreases and others experiencing increases as a result of the rate design changes.

1 calculated for 2009 and 2010 were converted to a rate, expressed in cents per
2 kWh, to be applied to customers' bills for pre-payments in those years. The
3 pre-payment charges calculated for each eligible tariff rate class are shown in
4 Exhibit ABC-3 and in the proposed Phase-In Rider.

5 **15. Q. How will the credits be applied to customers' bills?**

6 A. The pre-paid funds, plus accrued interest, will be credited to customers' bills
7 over two years. (Three years for Rates RH and OP.) For customers on
8 eligible rate schedules other than Rate RH and OP, the first year's credit will
9 be double the credit in the second year. The monthly credit will be a fixed
10 dollar amount determined after the customer's last bill has been issued in
11 2010. Exhibit ABC-4 shows an illustrative calculation of the monthly credit.
12 The factors that will be applied to the year-end 2010 balance to derive the
13 credit amounts for 2011 and 2012 assume that customers are repaid at the
14 beginning of each billing month because the credits are reflected as soon as
15 the customer is billed.

16 **16. Q. Will there need to be a reconciliation of pre-payments and credits?**

17 A. No, a reconciliation process is not required. The credits are calculated, and
18 are designed to operate, like a loan amortization schedule. By the end of the
19 phase-in period, the exact amount of pre-payments plus accrued interest will
20 have been returned to customers as billing credits. To assure complete

1 payment, the remaining balance in a customer's account will be distributed in
2 the last month of the credit period.

3 **17. Q. Under this program, PECO will pay customers interest on their pre-**
4 **payments, which will be reflected as future bill credits. Will that interest**
5 **be taxable for state and federal income tax purposes?**

6 A. Yes, the interest will be taxable for state and federal income tax purposes.
7 Accordingly, each year that credits are applied to a customer's bill, PECO will
8 issue to the customer an Internal Revenue Service Form 1099 showing the
9 interest income paid that year, just as PECO does with interest paid on
10 customer deposits.

11 **18. Q. Is the proposed Phase-In Rider available to customers that purchase**
12 **generation supply from an electric generation supplier ("EGS")?**

13 A. Yes, the Phase-In Rider is designed to be competitively neutral from an
14 electric "choice" perspective and, therefore, applies to all customers, whether
15 they purchase default generation supply service from PECO or obtain
16 generation service from an EGS.

17 **19. Q. Will customers "opt in" or have to "opt out" of the proposed Phase-In**
18 **Program?**

19 A. The Phase-In Program is a voluntary program. In order to participate, a
20 customer will have to affirmatively opt into the program.

1 20. Q. How will customers enroll in the Phase-In Program and how will PECO
2 notify them that the program is available?

3 A. After the Commission enters an order approving the Phase-In Program, the
4 Company will educate customers about the program and open a 60-day
5 enrollment period. Customers will be able to enroll through the Internet by a
6 conspicuous tab on PECO's website, through PECO's Interactive Voice
7 Response ("IVR") system, by calling customer service, or by completing and
8 returning a pre-addressed and postage pre-paid enrollment form. PECO will
9 promote the Phase-In Program through bill inserts, media advertisements, e-
10 mails to its electronically billed customers, and notices on the PECO website.
11 These promotional activities will start after the Commission approves the
12 program.

13 21. Q. Will any customers be ineligible for this program?

14 A. Yes. Customers who are on PECO's Rate CAP ("Customer Assistance
15 Program") and customers whose accounts are in arrears will not be eligible for
16 the Market Rate Phase-In Program. Also, Large Commercial and Industrial
17 customers (i.e., those with peak load of 500 kW or higher) are not eligible for
18 the Phase-In Program.

19 22. Q. Why are these customers excluded from the program?

20 A. The Phase-In Program allows participating customers to pay more than their
21 current bill to defray a future increase. CAP customers' payments are

1 generally based upon their ability to pay and, therefore, they would not be in a
2 position to pay more than their current bill. As explained in PECO's DSP
3 filing, the Company proposes enhancements to its CAP rate to help CAP
4 customers deal with the transition to market prices for generation. Customers
5 whose accounts are in arrears are not able to pay their current bills and,
6 therefore, would not be in a position to make the additional payments called
7 for under the Phase-In Program. In the case of Large Commercial and
8 Industrial customers, the Company's outreach indicates that they have other
9 options and are better able to handle the transition to market pricing.

10 **23. Q. Can a customer leave the Phase-In Program once he or she has enrolled?**

11 A. Yes. Customers can leave the program at any time by notifying the Company
12 that they would like to withdraw from the program. The Company will then
13 remove the customer from the Phase-In Program starting with the first billing
14 cycle after notice is given, provided there are at least 15 days between PECO's
15 receipt of the notice and the billing date. Otherwise, the customer will be
16 removed as of the start of the next billing cycle. Additionally, customers
17 leaving the Company's service territory will automatically be removed from
18 the program and issued a credit on their final bill for any prepaid amounts.
19 Finally, if a customer closes his or her account and does not concurrently
20 transfer it to another account in the Company's service territory, he or she will
21 be removed from the program. On the other hand, a customer moving from
22 one location to another within PECO's service territory would be able to

1 remain in the program as long as the new account was established at the same
2 time the previous account was closed.

3 **24. Q. Can a customer who has enrolled in the Phase-In Program be removed**
4 **from the program by PECO?**

5 A. Yes. There are two instances in which a customer will be removed from the
6 program by PECO. First, if the customer, after enrolling, is put on a CAP rate,
7 he or she will automatically be removed from the program. Second, if a
8 customer misses two consecutive payments of PECO electric bills, he or she
9 will be removed from the program.

10 **25. Q. If a customer leaves the Phase-In Program either voluntarily or**
11 **involuntarily, what happens to any balance of pre-paid funds?**

12 A. If a customer leaves the program for any reason, any balance of pre-paid
13 funds, plus accrued interest, will be credited to the customer's account. If the
14 customer has an arrearage, the credit will be applied first to the outstanding
15 arrearage. Customers with no outstanding balance owed to the Company may
16 request a refund check. There is no penalty or cost imposed on a customer for
17 leaving the program.

18 **26. Q. Are customers currently on PECO's budget plan eligible for the Phase-in**
19 **Program?**

1 A. Yes. Customers on PECO's monthly budget plan are eligible for the Phase-In
2 Program. The monthly pre-payment or credit would be added to, or subtracted
3 from, budget payments of budget plan customers who enroll in the program.

4 **III. COST RECOVERY FOR THE MARKET RATE TRANSITION**
5 **PHASE-IN PROGRAM AND THE CUSTOMER EDUCATION**
6 **PLAN**

7 **27. Q. What are the costs of the Phase-In Program that PECO seeks to recover?**

8 A. The Company seeks to recover the cost of implementing and administering the
9 Phase-In Program, which includes costs for information and billing system
10 enhancements, customer notification and enrollment. Exhibit ABC-5
11 accompanying my testimony shows the Company's current estimates by cost
12 category and year. PECO will also seek to recover enrollment costs.
13 However, because enrollment costs can vary substantially based on the level
14 of enrollment, they were not included in Exhibit ABC-5.

15 **28. Q. How does the Company propose to recover the costs you identified**
16 **above?**

17 A. The Phase-In Program will provide benefits to all eligible customers, whether
18 they will purchase their generation supply from PECO or an EGS. Therefore,
19 PECO proposes to recover these costs from all eligible customers through a
20 fully reconcilable, non-bypassable charge established under Section 1307 of
21 the Public Utility Code. The resulting charge will be included in PECO's

1 distribution rates, not shown as a separate line item on customers' bills, and
2 will not be included in PECO's "Price to Compare."

3 **29. Q. What are the costs of the Customer Education Program that PECO seeks**
4 **to recover and how does the Company propose to recover those costs?**

5 A. In its Order approving PECO's Customer Education Program, the
6 Commission established approved expenditure levels for that program over
7 four phases spanning 2008 through 2012. PECO seeks to recover the costs of
8 the Customer Education Program, in accordance with the four-phase budget
9 set forth in the Commission's Order, up to the level of expenditures approved
10 by the Commission. In the same Order, the Commission tentatively approved
11 PECO's request to establish a reconcilable cost recovery mechanism for
12 Customer Education Program costs as part of its DSP filing. Consistent with
13 that directive, the Company proposes to recover the approved Customer
14 Education Program costs through the same rate mechanism it is asking the
15 Commission to approve for recovery of Phase-In Plan costs, which will
16 impose a non-bypassable charge and be fully reconcilable. In establishing the
17 charge under this rate recovery mechanism, the cost of the Customer
18 Education Program will be allocated among procurement classes targeted by
19 the education material proportion to the number of customers in each class. In
20 its Order, the Commission also asked that "an April through March billing
21 period be used for annual [changes in the charge] . . . with a filing date of
22 February 1 and an April 1 effective date." The Company has incorporated the

1 Commission's recommended filing dates in the proposed tariff supplement
2 that will establish the charge. As also noted in the Commission's Order,
3 PECO will reduce the costs it seeks to recover for the Customer Education
4 Program by any unexpended funds budgeted to educate customers about retail
5 competition under Paragraph 37 of the Joint Petition for Settlement of its
6 Restructuring Plan at Docket Nos. R-0097953 and P-00971265.

7 **30. Q. Please explain how the proposed surcharge mechanism will work.**

8 A. Exhibit ABC-2 is the Company's proposed tariff supplement that contains the
9 terms of the surcharge mechanism as "Original Page 34E." As indicated by
10 the tariff language, the surcharge will be recalculated once per year. As
11 previously noted, the proposed surcharge will be filed with the Commission
12 on February 1 of each year to become effective on April 1 of the following
13 year. The surcharge will be based upon an estimate of expenditures for the
14 year in which it will apply. Capital costs, if any, will be amortized over the
15 useful live of the underlying assets with interest at 6% on the unrecovered
16 balance until those costs are included in PECO's rate base in a subsequent
17 base rate case and reflected base rates. There will be an annual reconciliation
18 of actual costs and revenues each year. Any over or under-collection, plus
19 interest thereon at 6%, will be reflected in the surcharge filed each February.
20 The reconciliation will be for 12-month periods ending December 31. The
21 first charge shall be filed on the first day of the month after Commission
22 approval, with an effective date 60 days later. As discussed earlier, if the

1 Company incurs recoverable costs before April 1, 2009, those costs will be
2 deferred and will accrue interest at 6% until recovered.

3 **31. Q. How will the costs be allocated or assigned to each eligible customer**
4 **class?**

5 A. The Phase-In Program's costs will be allocated based upon customer count to
6 all eligible customer classes. As previously explained, Consumer Education
7 Program costs will be allocated among procurement groups targeted by the
8 program based on the number of customers in those groups.

9 **IV. CONCLUSION**

10 **32. Q. Does this complete your testimony?**

11 A. Yes.