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PENNSYLVANIA



PUBLIC UTILITY COMMISSION

06



ANNUAL REPORT

MISSION OF THE PUBLIC UTILITY COMMISSION

The Pennsylvania Public Utility Commission balances the needs of consumers and utilities to ensure safe and reliable utility service at reasonable rates; protect the public interest; educate consumers to make independent and informed utility choices; further economic development; and foster new technologies and competitive markets in an environmentally sound manner.



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CHAIRMAN'S LETTER



THE HONORABLE EDWARD G. RENDELL
GOVERNOR OF PENNSYLVANIA

THE HONORABLE CATHERINE BAKER KNOLL
LIEUTENANT GOVERNOR

MEMBERS OF THE GENERAL ASSEMBLY,

I am proud to share with you the many successes, challenges and changes that defined this fiscal year as we submit to you the 2005-06 Annual Report for the Pennsylvania Public Utility Commission. Our spotlight continues on rates, reliability and choice so we can protect the public interest, promote economic development and preserve the environment.

As an agency, we are very concerned about costs – both internally and externally. While no one likes rate increases, we have been determined to balance fairly the needs of consumers with the financial stability for the utilities as we consider rate requests. According to a March 2006 report by a New York City-based investment firm, the Pennsylvania PUC is the most consumer friendly state utility commission in the Mid-Atlantic states. Rate caps currently shield most electric consumers from increases. Significantly, the Commission began a process to study potential policy actions that could mitigate any possible price spikes for consumers as the rate caps on electricity prices expire. As an independent agency funded by utility ratepayer dollars, it is important to note that we have saved utilities money. We released an annual report on management audits and management efficiency investigations, noting that, since 2000, we have helped utilities to save up to \$102 million through voluntary improvements to operations, service reliability and safety by regulated utilities.

And we want to save consumers money, too, wherever possible. Last winter demonstrated again that global energy markets impact Pennsylvania consumers who coped with significant increases in natural gas prices. We worked aggressively to educate consumers about critical utility issues, including the high winter heating costs, through our "Prepare Now" campaign. We conducted a statewide consumer-education campaign and supported the Governor's Stay Warm PA campaign. We stand ready to continue this important responsibility.



We are determined to improve reliability in the energy systems that serve Pennsylvanians and will continue to monitor and evaluate the performance of our jurisdictional utilities. Moreover, we found that effective natural gas competition did not exist. Hence, the Commission established a working group of stakeholders to explore avenues for removing competition hurdles.

Mergers and acquisitions also set this year apart from others; the Commission considered six major mergers/acquisitions of multi-industry utilities. Throughout the process, the Commission, in a timely manner, worked to protect the public interest – which includes preserving jobs and maintaining reliability.



We continued to move toward full implementation of three comprehensive laws that represented sweeping changes to the way energy and water utilities terminate consumers; the way electric utilities include the use of alternative energy sources for generation; and the way telephone companies are regulated.

The Commission took action to continue, consolidate and/or eliminate general filing and reporting requirements imposed on local telephone exchange carriers. Also, Lifeline and Link-Up programs for low-income consumers were expanded as we implement the General Assembly's law creating a new Chapter 30.

Water is our most precious natural resource and we remained committed to affordable, quality water as well as ensuring the viability of water companies. We took the first step in clarifying our regulations to define a "service interruption" for water utilities. We also kick-started the process of revising certain policies designed to improve the way jurisdictional water utilities communicate with consumers during emergencies. The Commission commemorated National Drinking Water Week, asking consumers to "Be Water Wise" and to focus on the value of drinking water and how responsible water usage conserves this resource while saving consumers' money.

Technology was the driving force behind changes that improved transportation and safety. Better use of technology is allowing the Commission to communicate more effectively, electronically accept insurance forms and process insurance violations. To this end, we are overhauling the existing case management system to improve electronic workflow capability and provide efficient access for all consumers, utilities and practitioners through the implementation of electronic filing. The Information Management Access Project – InfoMAP – will ensure a "21st Century PUC."

We stand ready to face the challenges and changes in the coming years. We continue to uphold our mission to ensure safe, reliable and reasonably priced utility service for the people of Pennsylvania.

A handwritten signature in black ink that reads "Wendell F. Holland".

Wendell F. Holland
Chairman

2005-06 COMMISSIONERS

FRONT ROW, LEFT TO RIGHT: CHAIRMAN WENDELL F. HOLLAND,
VICE CHAIRMAN JAMES H. CAWLEY, COMMISSIONER KIM PIZZINGRILLI,
BACK ROW, LEFT TO RIGHT: COMMISSIONER TERRANCE J. FITZPATRICK,
COMMISSIONER BILL SHANE



INTRODUCTION

Utility service is a critical element to the health and safety of Pennsylvania's residential and business customers. The Pennsylvania Public Utility Commission (PUC) ensures that electric, natural gas, water and local telephone service is available upon request at a reasonable rate and provided safely with a reasonable, reliable level of service. Similarly, customers using taxis, moving trucks or motor coaches also expect fair rates and adequate service.



With the restructuring of Pennsylvania's electric, natural gas and telecommunications industries, the Commission's role also is to educate customers so they may take advantage of the benefits of competition.

Under the law, utilities are entitled to fair rates of return when seeking increases. The PUC recognizes that it is in the long-term public interest to permit a strong financial climate for investment in public utilities. By allowing a fair return to investors, companies can attract capital to provide and improve services for all customers.

The PUC's challenge is to balance the interests of both consumers and the utility industry. To achieve this, the Commission strives to be prudent, fair and forward looking.

ORGANIZATION

The Commission is comprised of five full-time members nominated by the Governor for staggered five-year terms. The appointments must be approved by a majority of the Senate. The Commissioners set policy on matters affecting utility rates and services, as well as on personnel, budget, fiscal and administrative matters. Commissioners take official action on cases during regularly scheduled public meetings.

The Commission has its headquarters in Harrisburg with regional offices in Altoona, Philadelphia, Pittsburgh and Scranton.

The PUC regulates approximately 6,200 public utilities furnishing the following in-state services for compensation: electricity; natural gas; telephone; water and wastewater collection and disposal; steam heat; transportation of passengers and property by motor coach; truck and taxicab; pipeline transmission of natural gas and oil; and public highway-railroad crossings. Municipal utility service is exempt from PUC regulation, with the exception of services furnished beyond a municipality's corporate boundaries. Rural electric cooperatives, cable television and cellular telephones also are exempt from PUC regulation.

The Commission is funded by assessments of the regulated public utilities. The PUC may assess utilities up to three-tenths of 1 percent of gross intrastate revenue to cover the cost of regulation. Assessments are paid into the state Treasury's General Fund for use solely by the Commission.

The Public Utility Commission was created by the Pennsylvania Legislative Act of March 31, 1937, which abolished the Public Service Commission.

BROAD POWERS



The PUC exercises broad powers in meeting its regulatory obligations. In today's rapidly changing business environment, utilities must consider all of their options. The number of utility mergers, acquisitions and affiliated interest agreements has increased significantly during the last several years. With limited exceptions, utilities are required to obtain Commission approval for these transactions, as well as to operate, extend or abandon service. The PUC's responsibility is to ensure these actions are in the public interest.



Top: The Commissioners preside over regularly scheduled public meetings in Harrisburg.

Bottom: The Commission's meetings are open to anyone who wishes to be present and are attended by Commission staff, consumer advocates, industry representatives and residents.

In Fiscal Year 2005-06, the Commission revised its rules of practice and procedure, to reflect significant changes in the PUC's jurisdiction and responsibilities, which had not been modified since 1996. State and federal laws and Commission regulations have changed the landscape for our utilities and consumers when it comes to utility competition, consumer protections, alternative energy and telecommunications technology. The revisions ensured the state has a 21st century PUC ready to protect the public interest and balance the needs of all parties. The Commission's final rules of practice and procedure strike a balance among utilities, consumers and the public without imposing unnecessary delays, burdens or costs. The rules also strike a balance between proceedings where the parties are represented by attorneys and proceedings where the parties represent themselves.

The PUC also has worked diligently to ensure an effective transition to competitive markets in the electric, natural gas and telecommunications industries. The goal of competition and access to market prices for electricity would improve customer services and prompt the development of new technologies.

Although parts of the natural gas and electric markets are competitive, customers still receive transmission and distribution service from their local utilities. The local utilities also continue to maintain the electric lines or natural gas pipelines to ensure that safe, reliable utility service is delivered to customers. Likewise, phone customers who do not select a different provider for local service will continue to receive reliable service from their existing company. In every case,

customers who do not or cannot choose a different company continue to receive quality utility service that is reliable and rates that are fair and set appropriately.

In the interest of rail and motor safety and service, the PUC examines the structural strength of railroad bridges and underpasses. In addition to a team of railroad safety inspectors, the PUC has a staff of motor carrier investigators who check on the safety insurance, cargo and certified routes of truck, taxi and motor coach operators.

If customers have complaints about a utility, they may seek help through the PUC's Bureau of Consumer Services. Trained customer service representatives help to resolve billing disputes, help with quality of service issues, establish payment plans or restore service. An additional toll-free number provides consumers with assistance on competition-related issues.

RATES

In order to provide economical and efficient service to a community, the state grants electric distribution, natural gas distribution, steam heat, water and wastewater companies the right to provide their service within a specified geographic area. History shows and economics dictate that the construction of distribution facilities by multiple utilities in the same location would be extremely costly and disruptive to communities. The utility is regulated by the PUC to assure fair rates for safe and adequate service.

Competition is permitted in the supply of electricity and natural gas. Charges for the supply of electricity and natural gas by licensed competitors are not regulated and are based on market prices. Many electric utilities are operating under negotiated generation rate caps for supply services. The prices for the delivery through the distribution system of electric and natural gas continue to be regulated by the PUC.

Competition also is permitted for long-distance and local telephone service. Most local telephone companies operate under a price stability formula that limits their ability to seek rate increases based on the rate of inflation and other factors. The rates for competitive local exchange carriers that are competing against the incumbent local telephone companies also do not require PUC approval.

FILING FOR RATE INCREASE

When a regulated utility seeks a rate increase, it must file a request with the PUC that shows the proposed new rates and effective date, and must prove that the increase is needed. The utility also must notify customers at least 60 days in advance. The notice must include the amount of the proposed rate increase, the proposed effective date, and how much more the ratepayer can expect to pay.

HOW ARE RATES SET

The ratemaking process ensures the lowest reasonable rate for consumers while maintaining the financial stability of utilities. Under the law, the utility is entitled to recovery of its reasonably incurred expenses and a fair return on its investment. The PUC evaluates each utility's request for a rate increase based on those criteria.

HOW LONG DOES IT TAKE

By operation of law, the rate request is suspended for up to seven months if the PUC does not act before the proposed effective date for the rate increase for electric, natural gas, steam heat, water and wastewater companies. The PUC uses that time to investigate and determine what if any of the requested increase is justified.

During the investigation, hearings are held before an Administrative Law Judge (ALJ) at which the evidence in support of the rate increase is examined and expert witnesses testify. In addition, consumers are offered an opportunity to voice their opinions and give testimony. Briefs may be submitted by the formal parties. A recommendation to the PUC is made by the ALJ. Finally, the matter is brought before the Commissioners for a vote and final decision.

Together with the 60-day notice period, the rate increase process takes about nine months.

HEARINGS AND RECOMMENDATIONS

When the PUC investigates a rate increase, it is assigned to an ALJ, who is an attorney with experience in administrative law. The ALJ presides at formal hearings, which are open to the public and conducted like a formal court proceeding.

At the formal hearing, the company, the PUC's Office of Trial Staff (OTS) and other parties such as the state's Office of Consumer Advocate and the state's Office of Small Business Advocate present their cases and are subject to cross-examination. OTS reviews the company's records and requests, and presents its view on what is in the public interest.



Individual ratepayers may become formal parties by applying in writing to do so. Ratepayers may speak for themselves, or an attorney may represent individual ratepayers or groups of ratepayers. Consumers also can have their say informally by writing or calling the PUC or by testifying at a public input hearing. By providing testimony, consumers

The PUC's Administrative Law Judges – such as Judge Charles E. Rainey Jr. – are attorneys with experience in administrative law.

place their views in the official file on the case. Public input hearings are conducted by the ALJ in the utility's service territory. Consumer testimony becomes part of the record on which the PUC will base its decision.

After weighing the evidence and hearing the arguments, the ALJ writes a recommended decision addressing each issue in the case within the limits set by law. The recommended decision may approve, disapprove or modify the original request. Parties may file exceptions to the judge's decision and subsequently reply exceptions may be filed. Sometimes, rate cases are resolved after all of the parties reach a settlement on the issues. The entire matter is then sent to the Commissioners for a vote at a public meeting.

FINAL ORDER

The Commissioners make the final decision, authorizing rates that: (1) permit revenues that allow the company to meet its reasonable expenses, pay interest on its debt and provide a fair return to stockholders so it will continue to attract investment; and (2) assign the proper rate for residential, commercial and industrial customers that reflects the cost of service. The Order has the weight of law unless the PUC changes it in response to a petition for reconsideration, or it is successfully challenged in court.

RATEPAYER ROLE

Ratepayers must pay for the service they use, which includes a share of the reasonable cost of utility company expenses such as operating and maintenance expenses, administrative expenses, depreciation and taxes. While the ratemaking process is complex, consumers have the right to be informed about the process, receive an explanation of their utility bills, have their complaints addressed in a prompt and fair manner, and receive continuous utility service if payment responsibilities are met.

Consumers have a right to participate in the ratemaking process and can do so by filing an informal complaint, which can include attending a public input hearing. They also can file a formal complaint.



The Office of Administrative Law Judge provides fair and prompt resolution to contested proceedings before the Commission.

COMMISSION BUDGET

EXECUTIVE GOVERNMENT OPERATIONS		
GENERAL GOVERNMENT	GENERAL FUND	GENERAL FUND
	ACTUAL 2005-06	REVENUE ALLOCATED 2006-07
STATE FUNDS :		
PERSONNEL	\$35,854,000	\$40,689,000
OPERATING	8,286,000	10,717,000
FIXED ASSETS	273,000	225,000
TOTAL STATE FUNDS	\$44,413,000	\$51,631,000
FEDERAL FUNDS :	\$1,407,000	\$1,324,000
PERSONNEL	121,000	297,000
OPERATING		
TOTAL FEDERAL FUNDS	\$1,528,000	\$1,621,000
TOTAL COMMISSION BUDGET :	\$45,941,000	\$53,252,000

OTHER REVENUE SOURCES

TYPE	2004-05 RECEIPTS	2005-06 RECEIPTS
FILING & COPYING FEES	\$235,688	\$274,587
ELECTRIC GENERATION APPLICATION FEES	4,900	11,200
FINES	928,555	339,422
FEDERAL - GAS PIPELINE SAFETY	395,000	350,000
FEDERAL - MOTOR CARRIER(MCSAP)	1,046,148	1,147,298
TOTAL	\$2,610,291	\$2,122,507

2005-06 APPLICATION & FILING FEES, FINES & PENALTIES

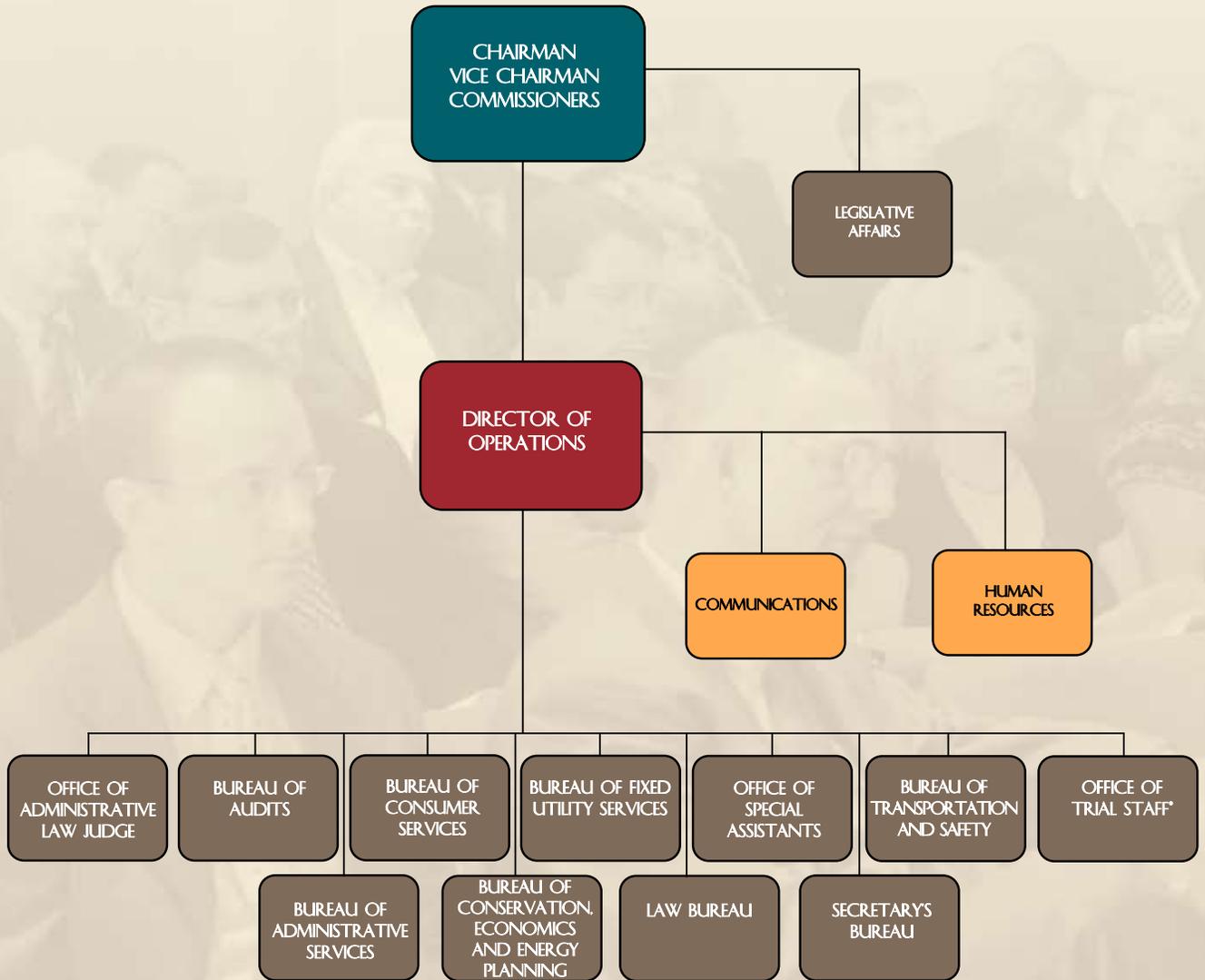
	ELECTRIC GENERATION APPLICATION FEES	FINES	FILING & COPY FEES	TOTAL
1ST QUARTER	\$3,150	\$111,517	\$59,923	\$174,590
2ND QUARTER	3,500	32,260	62,912	98,672
3RD QUARTER	1,750	54,916	69,345	126,011
4TH QUARTER	2,800	140,729	82,407	225,937
TOTAL	\$11,200	\$339,422	\$274,587	\$625,209

2005-06 FISCAL OPERATIONS AND ASSESSMENTS

2005-06 FISCAL OPERATIONS AND ASSESSMENTS	AMOUNT
1ST QUARTER	\$46,129,019
2ND QUARTER	776,812
3RD QUARTER	1,614,147
4TH QUARTER	1,263
TOTAL	\$48,521,241

The Fiscal Office received \$48,521,241 from assessment billings within the 2005-06 Fiscal Year.

ORGANIZATIONAL CHART



*The Director of Operations has responsibility for the Office of Trial Staff only with regard to administrative matters.



From Left to Right: Commissioner Kim Pizzigrilli, Vice Chairman James M. Cawley, Chairman Wendell F. Holland, Commissioner Bill Shane, Commissioner Terrance J. Fitzpatrick

2005-06 BUREAU DIRECTORS

DIRECTOR OF OPERATIONS



Karen Moury
Director of Operations

The Director of Operations is responsible for the day-to-day administration and operation of the bureaus and offices within the Commission, including: goals and objectives; organizational structures; staff selection and training; performance standards; assignments to bureaus; and coordination of multi-bureau projects. The Director's Office is also comprised of administrative support staff, the Office of Communications and the Office of Human Resources. The Office of Communications handles media relations, public outreach and employee communications. The Human Resources Office handles all personnel issues and provides administrative and advisory services to all PUC management.



Tom Charles
Manager of Communications



Carol McLeod
Director of Human Resources

BUREAU OF ADMINISTRATIVE SERVICES



Peter B. Dalina
Director of Administrative Services

The Bureau of Administrative Services is responsible for the preparation of the Commission's budget, collection of assessments, various fiscal operations, processing of contracts, information and technology functions and office services. The Bureau also provides support to the Director of Operations for administrative matters in the Commission's daily operation. Mail distribution, inventory control, automotive and travel-related services also are handled through this department. The Bureau is comprised of assessment, fiscal, management information and office services.

OFFICE OF ADMINISTRATIVE LAW JUDGE



Veronica A. Smith
Chief Administrative Law Judge

The Office of Administrative Law Judge fulfills a judicial role within the Commission by hearing cases, mediating cases through the alternative dispute resolution process and issuing decisions. Headed by a Chief Administrative Law Judge, the Office's primary duty is to provide fair and prompt resolution to contested proceedings before the Commission. The Administrative Law Judges (ALJs) are attorneys with experience in administrative law. They are independent judges who preside over the hearings in cases, which can include consumer complaints, rate filings, investigations, ability to pay/billing disputes and applications. ALJ decisions are based upon a record of evidence, legal precedent and policy.

BUREAU OF AUDITS



Tom Sheets
Director of Audits

The Bureau of Audits performs financial, management and specialized audits on electric, natural gas, water and telecommunications utilities. The Bureau also reviews certain adjustment clause rate filings. The audits may result in recommendations to improve accounting or operational procedures that, if adopted, may mean a significant one-time savings or become annual savings for the utility. The Bureau also is responsible for auditing the annual reconciliation statements associated with stranded costs of electric distribution companies and certain water companies that are authorized to use the Distribution System Improvement Charge.

BUREAU OF CONSERVATION, ECONOMICS AND ENERGY PLANNING



Wayne Williams
Director of Conservation,
Economics & Energy
Planning

As the research arm of the PUC, the Bureau of Conservation Economics and Energy Planning gathers data on energy market issues, serves market monitoring functions, and focuses on development in the energy market related to prices and supply. The Bureau studies and researches energy matters and advises the Commission of results to assist in making policy decisions. The Bureau monitors developments in energy markets such as pricing trends, demand forecasts and the availability of supply to meet demand. The Bureau also makes certain electric utilities are meeting the required benchmarks and standards for reliability to ensure the continued safety, adequacy and reliability of generation, transmission and distribution of electricity in the Commonwealth.

BUREAU OF CONSUMER SERVICES



Mitch Miller
Director of Consumer
Services

The Bureau of Consumer Services responds to and investigates informal complaints by residential and small commercial consumers. The Bureau also serves as a mediator between utilities and consumers, working to resolve complaints or develop payment arrangements. The Bureau provides consumers with utility-related information and monitors compliance with PUC regulations regarding consumers. The Bureau provides an analysis of utility performance when handling consumer complaints and issues.

BUREAU OF FIXED UTILITY SERVICES



Robert A. Rosenthal
Director of Fixed Utility
Services

The Bureau of Fixed Utility Services serves as an adviser to the PUC on technical issues for electric, natural gas, water and wastewater, and telecommunications utilities. The Bureau offers policy recommendations on rates, tariffs and regulatory matters, processes fixed utility applications and coordinates emergency operations of utilities. The Bureau processes filings such as securities certificates and affiliated interest agreements. The Bureau also reviews and maintains county 911 system plans; telecommunications relay service reports; annual financial reports; and utility tariffs. The Director of the Bureau is vested with the authority to act for the Commission during emergencies and represents it on the Pennsylvania Emergency Management Council.

LAW BUREAU

The Law Bureau acts as the Commission's in-house legal counsel, providing legal advice to the Commission. The Bureau's director serves as Chief Counsel to the Commission. Three main categories of legal services are provided by the Bureau: advisory, representational and prosecutory/enforcement. The Law Bureau initiates both in-house prosecutions and enforcement proceedings against public utilities. During in-house prosecutions, the Bureau investigates and files complaints against utilities that fail to file annual reports, pay annual assessments or maintain adequate service or reliability. During enforcement proceedings, the Bureau will file lawsuits in Commonwealth Court against utilities that fail to obey final PUC Orders or court orders. The Law Bureau represents the Commission before state and federal courts when the Commission's decisions are challenged. The Bureau also represents the Commission before federal agencies such as the Federal Communications Commission or the Federal Energy Regulatory Commission on issues that impact Pennsylvania.



Bohdan R. Pankiw
Chief Counsel

OFFICE OF LEGISLATIVE AFFAIRS

The Office of Legislative Affairs acts as the liaison between the PUC and the Governor's Office, General Assembly and the Pennsylvania Congressional Delegation. The Office identifies legislation that may affect the Commission or public utilities and obtains staff analysis; provides bill analysis and relevant information to the legislature; and promotes the Commission's position on legislation and issues with the General Assembly. The Office also handles requests for information from the Governor, legislators and constituents.



June Perry
Director of Legislative
Affairs

SECRETARY'S BUREAU

The Secretary's Bureau is the PUC's official point of contact with the public. The Bureau receives all official documents and filings, serving as the prothonotary of the Commission. All official Commission actions are issued over the Secretary's signature. All correspondence and filings must be addressed to the Secretary to be considered filed before the Commission. The Bureau docket all filings, assigns formal proceedings to appropriate bureaus and maintains the PUC's case management system. The Secretary's Bureau also is responsible for coordinating and monitoring all public meeting agendas and meeting minutes, and issuing all Commission Orders and Secretarial Letters.



James J. McNulty
Secretary

OFFICE OF SPECIAL ASSISTANTS

As the Commission's advisory support bureau, the Office of Special Assistants is comprised of attorneys, rate case review specialists and administrative support staff. The Office drafts opinions and orders for the Commission to vote on at public meetings. The Office reviews and offers recommendations on the exceptions to Administrative Law Judge decisions, petitions for reconsideration and requests for extensions of filing deadlines. The Office prepares Opinions and Orders to be consistent with Commissioner motions adopted at public meetings.



Cheryl Walker Davis
Director of Special Assistants

BUREAU OF TRANSPORTATION AND SAFETY



Mike Hoffman
Director of
Transportation & Safety

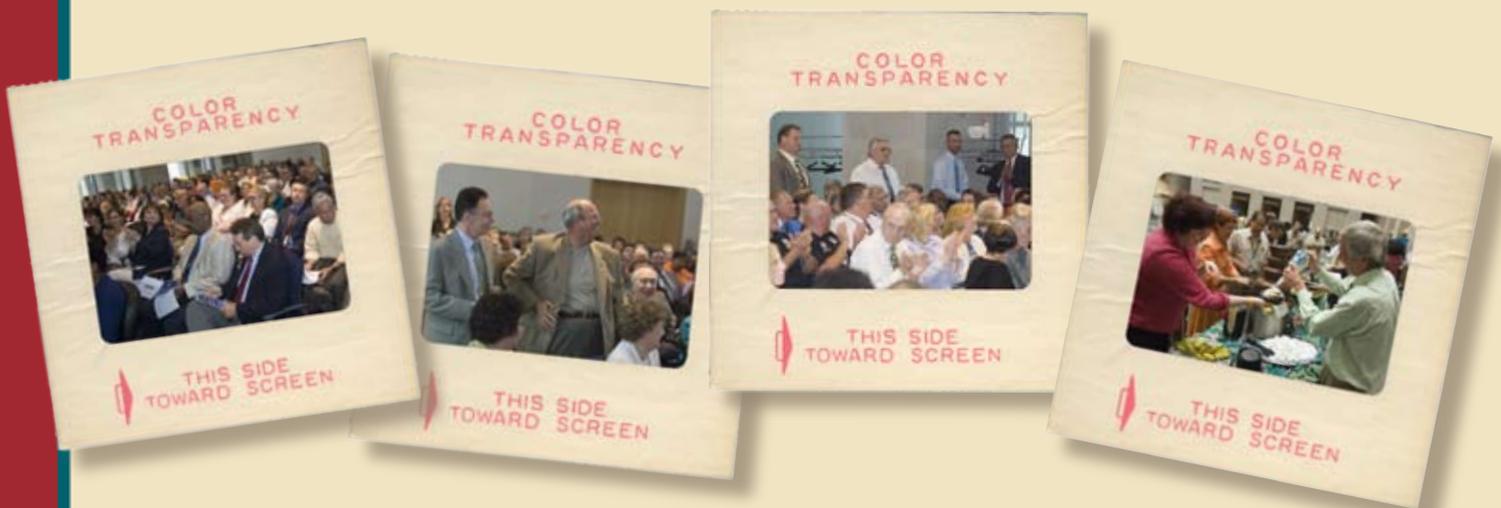
Comprised of the Motor Carrier Services and Enforcement Division, the Rail Safety Division and the Gas Safety Division, the Bureau of Transportation and Safety seeks to ensure safe and reliable natural gas, rail and motor carrier service throughout the state. The Bureau handles applications and rate filings of motor carriers; ensures compliance with PUC regulations; performs rail crossing and bridge safety inspections; and inspects natural gas facilities and records to ensure compliance with state and federal requirements.

OFFICE OF TRIAL STAFF



Johnnie Simms
Director of Trial Staff

The Office of Trial Staff represents the public interest in all matters having an impact on rates before the PUC. The Director is designated as the Commission's chief prosecutor, and the office is made up of the administrative, legal and technical divisions. The Office of Trial Staff is responsible for reviewing Commission filings made by utilities involving rate-related matters. The Office has an obligation to ensure that utilities charge rates that are reasonable, non-discriminatory and at a level that allows the utility to provide safe and reliable service that is affordable. Due to its prosecutory role, the Office of Trial Staff works independently of the other bureaus within the Commission.



Bureau Directors and employees celebrate during the Commission's Employee Appreciation Ceremony on June 8, 2006. Employees were recognized for their years of service with the Commonwealth and their accomplishments at the Commission during the year.

CONSUMER ISSUES

During Fiscal Year 2005-06, the Commission remained committed to monitoring and evaluating utility performance, as well as working aggressively to educate consumers about critical utility issues. The Commission conducted a statewide consumer-education campaign that included radio ads, educational workshops and community events. The campaign encouraged consumers to "Prepare Now" for high winter heating costs. The PUC also commemorated serving its 2 millionth customer and continued with the implementation of the changes to the utility termination rules while working to educate consumers about the changes and their rights.

NOW SERVING...2 MILLION PLUS



Jimithy Hawkins from the Commission's Call Center in Harrisburg handles consumer inquiries and complaints.

The Commission's Bureau of Consumer Services (BCS) has been handling consumer complaints since 1977. On Oct. 25, 2005, BCS received its 2-millionth utility-related complaint from a consumer. The PUC receives numerous consumer complaints and inquiries annually regarding utility service and quality. In fact, the National Association of Regulatory Utility Commissioners has rated BCS as one of the best consumer-oriented operations in the country.

The 2-millionth complaint presented a challenging case that involved jurisdictional issues, as well as water quality issues, and was representative of the work that is the daily routine at BCS. Although consumers present complex and often challenging issues for the BCS investigative staff, each investigator stands ready to assist customers in whatever way is possible.



THE RESPONSIBLE UTILITY CUSTOMER PROTECTION ACT (CHAPTER 14)

During Fiscal Year 2005-06, the Commission continued with the implementation of the Responsible Utility Customer Protection Act (Chapter 14). The law changed the guidelines relating to termination of service in the winter, cash deposits, reconnection of service and determinations of liability. The changes apply to electric distribution companies, water distribution companies and large natural gas distribution companies (those having an annual operating income in excess of \$6 million). Steam, telephone and wastewater utilities are not covered by Chapter 14.

The Commission engaged all of the stakeholders in the implementation process, including utilities and consumer advocates. The PUC held an initial Roundtable Forum and issued its first Implementation Order, which set specific guidelines for utilities and consumers on how the law would be put into practice. It was followed by a second Roundtable Forum and a separate forum specific to Philadelphia Gas Works (PGW) at which interested parties were again encouraged to file written comments on a variety of issues. After a review of the comments, on Sept. 9, 2005, the Commission issued a second Chapter 14 Implementation Order, which addressed a wider variety of issues, including winter termination rules, termination notice content requirements, reconnection requirements, medical certificate procedures, liability and liens.



The PUC developed handouts to educate consumers about the changes to termination guidelines under Chapter 14.

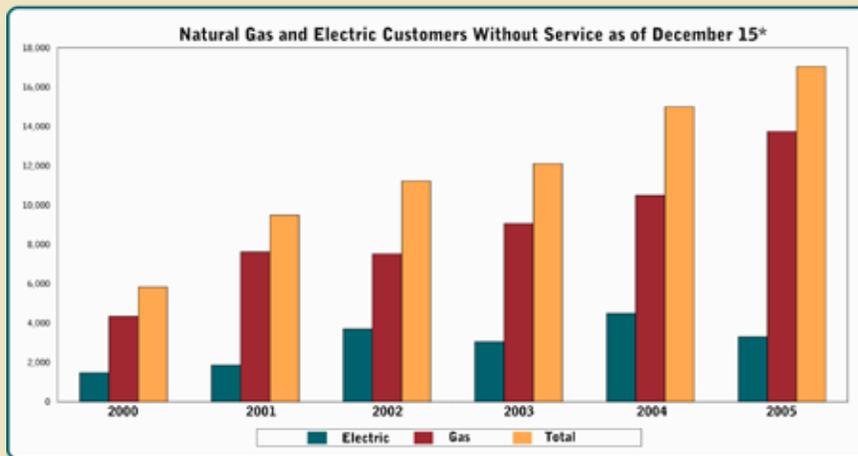
The Commission also revisited one of the issues addressed in its first Implementation Order, specifically the prohibition on a Commission ordered payment arrangement if the customer had a previous arrangement negotiated directly with the utility. On Oct. 27, 2005, after reviewing comments from interested parties, the Commission ruled that the existence of a previous company negotiated agreement did not bar the Commission from issuing a payment agreement. The Commission also prepared and implemented a statewide consumer-education program, the goal of which was to inform utility consumers of the changes in utility collection practices as a result of Chapter 14 and to urge consumers with payment problems to seek assistance as soon as possible.

The Commission continues to work to implement the law to fulfill its purpose and policy. In doing so, the PUC's main concern is the health and safety of Pennsylvanians. As required by the Act, the Commission will seek to amend Chapter 56 to bring it into alignment with Chapter 14. Also as required by the Act, the Commission will be issuing its first biennial report to the General Assembly and Governor on the impact and effectiveness of the new law.

COLD WEATHER SURVEY RESULTS

Each year prior to the winter-heating season, the PUC requires electric and natural gas utilities to check residential properties where service has been shut off. The goal of the annual Cold Weather Survey is for the company to try to reach payment agreements with the occupants so service can be restored. The Commission requests that utilities make four attempts to contact the consumer or a responsible adult occupant at the property where service has been terminated. These contacts include a combination of telephone calls and letters to establish contact, with the fourth attempt being a personal visit to the property.

In December 2005, the survey found that about 17,400 occupied households were without heat-related utility service. An additional 4,000 homes were using unsafe heating sources, bringing the total homes not using a central heating system to more than 21,400; this is up from 17,659 in 2004.



*Does not include households using alternative heating sources.

Residential electric households not using a central heating system totaled 3,518 while 17,545 natural gas households had no service. About 9,495 households -- 56 percent of the total accounts without service -- were in the Philadelphia area. The results also show an additional 17,560 residences where services were terminated appear to be vacant.

The companies resurveyed the households without utility service in February 2006. At that time, the total number of homes not using a central heating system decreased by 29 percent to 14,533.

Terminations of electric and natural gas service have increased from 2004 to 2005. Statewide electric and natural gas terminations went from 171,091 in 2004, to 255,399 in 2005 -- a 49 percent increase. Likewise, reconnections of electric and natural gas service increased during the same time period going from 98,104 in 2004 to 161,058 in 2005 -- a 64 percent increase.

At this time, water utilities are not required to report termination and reconnection data to the Commission. Aqua Pennsylvania and Pennsylvania American have voluntarily provided termination data. Terminations for those companies have increased from 10,604 in 2004 to 28,149 in 2005 -- a 165 percent increase. The Commission does not currently have reconnections data. Since Chapter 14 included water utilities, the Commission will have better statistical data from these utilities in coming years.

PREPARE NOW CAMPAIGN

The PUC launched the third year of its successful "Prepare Now" campaign. The partnership between the PUC, utilities and consumer advocates carries a simple message: "Prepare Now" for winter's higher energy costs. This educational program is keeping with the Commission's focus on rates, reliability and choice, so it can protect the public interest, increase economic development and protect the environment.



The campaign urged consumers to learn about changes in the law related to utility shut-offs and know their rights. It also encouraged consumers to prepare by weatherizing their homes, conserving energy and learning about private and public programs to help them cope with colder weather and pay their bills.

On Sept. 9, 2005, the PUC directed electric, natural gas and water utilities to coordinate with the PUC, consumer advocates and community-based organizations to educate Pennsylvanians about changes in the law dealing with utility shut-offs.

In February 2006, the Commission used \$340,000 in voluntary contributions from regulated electric and natural gas companies to launch a statewide radio campaign highlighting the availability of Universal Service Programs and changes in the law governing utility terminations. The PUC partnered with the participating utilities and the Council for Utility Choice to produce the new radio spots. The Council, a non-profit corporation working in conjunction with the PUC, directed the campaign. Input was provided by Energy Association of Pennsylvania, PUC Consumer Advisory Council, Community Action Association, Pennsylvania Telephone Association, Office of Consumer Advocate and professional educators.



PUC Chairman Wendell F. Holland urges consumers to apply for the Low Income Home Energy Assistance Program.

Utilities providing voluntary contributions to the campaign included: Allegheny Power, Columbia Gas Co.; Duquesne Light Co.; Equitable Gas; Metropolitan Edison; PECO; Pennsylvania Electric; Pennsylvania Power; PG Energy; PPL; and UGI.

The Commission continued to deliver the "Prepare Now" message across the state to help Pennsylvanians – particularly seniors and low-income consumers – deal with the winter. The messages delivered were:

- Consumers should contact their electric or natural gas company to learn about local programs to help;
- Each major natural gas company in Pennsylvania has established a Customer Assistance Program and a Low-Income Usage Reduction Program (LIURP). LIURP, for example, helps reduce gas usage by providing consumers with energy efficient equipment and insulation;
- The Weatherization Program is the country's longest-running, and most successful, energy efficiency program. The federally funded program helps low-income families to permanently reduce their energy bills by making their homes more energy efficient; and
- The Low Income Home Energy Assistance Program or LIHEAP is a federally funded program that helps low-income senior and families with their energy costs. For more information on the LIHEAP program, contact local County Assistance Offices or the Pennsylvania LIHEAP Hotline at 1-866-857-7095.



STAY WARM PA CAMPAIGN

During the winter of 2005-06, the Commission supported the Governor's Stay Warm PA campaign, which partnered consumer advocates, utilities and businesses in an outreach effort. Gov. Ed Rendell also met with CEOs of the state's major utilities and challenged them to meet their required participation rates under the Consumer Assistance Program (CAP) by doubling their enrollment. CAPs allow qualifying low-income consumers to pay discounted bills. In response to this initiative, electric and gas utilities came to the PUC for approval of measures such as increasing spending on CAPs, and exercising discretion in applying collection tools.



The Commission also permitted seven electric and natural gas companies to transfer nearly \$15 million in unspent utility consumer-education funds to help low-income families in their service territories this winter using Universal Service Programs. The Commissioners cited energy costs were as much as 40 percent higher as the reason why these funds needed to be moved to low-income programs for the upcoming 2005-06 winter heating season. The companies – Allegheny Power, Metropolitan Edison, Pennsylvania Electric Co., PG Energy, PPL Electric Utilities Corp., PPL Gas Utilities Corp., and T.W. Phillips Gas and Oil Co. – transferred most of the funding to their Universal Service Programs such as CAPs or LIURPs.

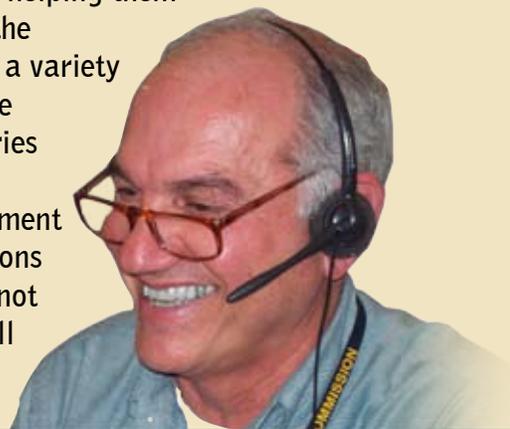


KEYSTONE CONNECTION

The Commission continued its publication of the "Keystone Connection," a newsletter that is released quarterly to about 700 subscribers, including news media and industry stakeholders. "Keystone Connection" provides a snapshot of activities in Pennsylvania's competitive marketplace. The goal is to provide beneficial information to the public about important developments in the electric, natural gas, transportation, telecommunications and water industries.

UTILITY CONSUMER ACTIVITIES REPORT AND EVALUATION

Educating Pennsylvania consumers on utility issues and helping them to resolve utility problems remain a major concern for the Commission. Full-time investigators within BCS handle a variety of consumer contacts related to billing problems, service delivery and repairs. The PUC received 108,298 inquiries in 2005, a 17 percent increase from the previous year. Inquiries include information requests, requests for payment arrangements that BCS cannot accommodate and opinions from consumers. For the most part, these contacts did not require investigation by BCS. These inquiries include all contacts to BCS, including those received through the



Competition/Choice Hotline, contacts through other telephone numbers, U.S. mail service and e-mail communication.

While final data is not yet available, preliminary numbers show that the PUC investigated 22,628 consumer complaints in 2005, with 20,512 of those complaints coming from residential consumers and 2,116 from commercial consumers. That represents a decrease of about 14 percent in total consumer complaints from 2004, with residential consumer complaints decreasing by about 11 percent.

Preliminary statistics show that the PUC also handled 61,393 requests for payment arrangements from residential customers in 2005, a 35 percent decrease from 2004. The majority of requests for payment arrangements in 2005 involved electric or natural gas companies. About 53,725 residents requested payment arrangements for their electric or natural gas bills – a 38 percent decrease from 2004. About 2,670 residential telephone consumers requested payment arrangements, which is a 34 percent decrease from 2004.

The PUC also surveys consumers who have contacted BCS with a utility-related problem or payment arrangement request in order to monitor its own customer service. In 2006, the PUC began compiling this data by the calendar year and any data for 2006 is not yet available. However, for the first half of the 2005-06 fiscal year (July 1 to Dec. 31, 2005), 74 percent of consumers said they would contact the PUC again if they were unable to resolve their problem by talking with the utility with more than 70 percent of consumers rating the service they received from the PUC as “good” or “excellent.”

UTILITY CUSTOMER SERVICE PERFORMANCE REPORT

According to the 2004 Customer Service Performance Report, the majority of electric and natural gas customers contacted said they were satisfied with the way company customer service representatives handled their calls in 2004. This annual report provides information on the customer service performance of the major electric and natural gas companies. The companies include: Allegheny Power; Duquesne Light Co.; Metropolitan Edison; Pennsylvania Electric Co.; PECO Energy Co.; Pennsylvania Power Co.; PPL Electric Utilities; UGI-Electric; Columbia Gas; Dominion Peoples; Equitable Gas Co.; National Fuel Gas; PG Energy Corp.; Philadelphia Gas Works; and UGI-Gas.

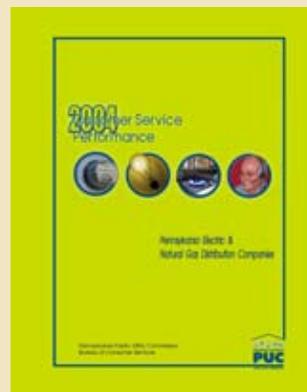
Based on customer surveys, an average of 90 percent of electric and 84 percent of natural gas customers said they were satisfied with the ease of reaching their company. A greater percentage of customers said they were satisfied with the way company representatives handled their calls. A majority of the customers were satisfied with both the courtesy and level of knowledge demonstrated by customer service representatives.

The annual report also includes data provided by the utilities on the performance of the company’s customer service operations. Two electric companies – PECO and UGI Electric – reported that their call abandonment rate more than doubled. Abandoned calls represent the number of customers who hang up while on hold to speak to a representative. The other electric companies’

call abandonment rates either fell slightly or remained the same as the previous year.

The average call abandonment rate for the natural gas companies of 8 percent is twice that of the electric companies. Equitable Gas reported the highest call abandonment rate.

The full report for 2004 is available on the PUC's Web site at www.puc.state.pa.us under "Publications and Reports." In addition, the telephone access charts covering performance in 2005 are available on the Web site in the "Announcements" section. This year, customer service performance charts, which are included in the annual Customer Service Performance Report, will be posted to the PUC Web site.



2004 Customer Service Performance report cover

SETTLEMENTS WITH UTILITY COMPANIES

In Fiscal Year 2005-06, the PUC approved four settlements with utility companies that totaled more than \$715,000 in settlement monies to help consumers. The settlement agreements, reached between the PUC's independent prosecutory staff and the utilities, followed informal investigations into alleged violations of the Public Utility Code and the Responsible Utility Customer Protection Act (Chapter 14). In each case, the company denied the prosecutory staff's assertions. All of the agreements required the companies to improve their communication with consumers. In many of the agreements, the PUC stipulated that the settlement monies should be deposited into programs to help low-income families. The money in these settlements cannot be recovered from ratepayers.

The settlements included:

- Pennsylvania Electric Corp. (Penelec) contributing \$250,000 to the company's Consumer Assistance Program (CAP) and \$100,000 to the Dollar Energy Fund. The informal investigations centered on improper terminations of electric service on May 11, 2005, in Hastings, Cambria County, and June 27, 2005, in Erie. Following the Hastings termination, four fatalities resulted from a May 14, 2005, fire, which according to media reports was caused by an unattended candle. Following the Erie termination, a July 3, 2005, fire injured two children. According to police reports, the fire was caused by an overloaded extension cord running from another apartment.
- Philadelphia Gas Works (PGW) contributing \$100,000 to the company's CAP. The informal investigation focused on two deaths, which occurred due to hypothermia after termination. A December 2002 death occurred after PGW repeatedly failed to contact a residential customer, failed to leave a 24-hour notice as required and then terminated service. The investigation alleged six violations of the company's tariff and the Public Utility Code. In a separate investigation, the prosecutory staff alleged that a January 2003 death occurred after PGW failed to bill an account and then subsequently terminated the service with no wrongdoing by the consumer. The investigation alleged eight violations of the company's tariff and the Public Utility Code.

- PPL Electric Utilities contributing \$175,000 to the company’s Hardship Fund. According to PUC’s prosecutory staff, PPL violated provisions of Chapter 14 of the Public Utility Code by terminating service to customers in March of 2005. Some of these customers were low-income customers whose service should not have been terminated in the winter. In addition, PPL failed to follow the proper notice procedure in some instances, and in some cases failed to restore service within the required timeframes. The company also inappropriately required payment of reconnection fees on accounts that were improperly terminated.
- PECO Energy: \$90,015 to provide a \$15 credit on the bills of customers who received erroneous termination notices from the company. A PECO computer error resulted in 6,001 termination notices to be mailed in February 2005 to non-delinquent, low-income consumers. PECO acted immediately to prevent any further incorrect mailings; however, the company waited 17 days before notifying affected customers of the error.

PUBLIC OUTREACH



The PUC’s public outreach specialists, from top, Shari Williams, Christina Chase-Pettis and James Rowland, provide utility education to thousands of consumers annually with a focus on helping seniors and low-income residents.

The PUC’s public outreach specialists provided utility education to thousands of consumers with a focus on working with seniors and low-income residents. The team conducted a grassroots effort to reach out to consumers by regularly traveling throughout the state conducting or participating in workshop events, seminars, roundtable discussions and community fairs. During those events, plain language materials were provided in order to educate consumers about complex utility issues including changes in the law. Public outreach specialists also assisted consumers in addressing their specific concerns with a utility or utility-related issue.

In 2005, the team focused on educating Pennsylvanians and non-profit, community-based organizations about three primary issues through its “Prepare Now” and “Be Utility Wise” campaigns.

Messages encouraged consumers to:

- Use electricity, natural gas and water wisely to potentially save money. Consumers were provided with informational materials and tips on how to become more responsible in their utility usage;
- Know their rights as a responsible utility consumer and be aware of important changes in the law related to utility shut offs (Chapter 14); and
- Consider budget billing as a way to make heating bills more predictable and affordable throughout the year. Consumers were encouraged to enroll in budget billing as an effective way to deal with high natural gas prices during the winter months. Budget billing spreads monthly payments over the year, avoiding the potential price spikes of winter months.

PA RELAY

In 2005, the Public Utility Commission, the Pennsylvania Relay Service Advisory Board and PA Relay service provider AT&T continued their statewide campaign to educate Pennsylvanians about PA Relay – the service that enables the hearing public to communicate by telephone with individuals who are deaf, hard of hearing or speech disabled.

www.PARELAY.net

The focus of the campaign is to educate the hearing public about relay technology to enhance the opportunities of people with hearing loss and speech disabilities for communicating with the hearing public in their daily lives.

Highlighting the 2005 campaign activities was the recognition of July 11, 2005, as “7-1-1/PA Relay Day” in Pennsylvania by Lt. Gov. Catherine Baker Knoll. In addition, Lt. Gov. Knoll joined Chairman Wendell F. Holland and Commissioners Bill Shane and Kim Pizzigrilli in a statewide report highlighting the importance of PA Relay. Additionally, the campaign included a traveling exhibit, “PA Relay on the Road,” which crisscrossed Pennsylvania during the summer, visiting county fairs, legislative outreach events, festivals and other venues with large audiences. The display included interactive demonstrations of relay technology and was staffed by a trained representative who distributed informational literature.



From left: Commissioner Bill Shane, Commissioner Kim Pizzigrilli, Lt. Gov. Catherine Baker Knoll, Christy Smith from TV’s “Survivor,” who is deaf, and PUC Chairman Wendell F. Holland promote the PA Relay service.

INFOMAP

The PUC partnered with Pennsylvania-based Unisys, a worldwide technology services and solutions company, to develop the PUC’s Information Management and Access Project (InfoMAP).



InfoMAP will overhaul the PUC’s case management system, improving the Commission’s docketing, tracking and sharing of information. It will also provide a single-entry point to submit and access information, initiate transactions and conduct business, thereby permitting electronic filings and giving the public electronic access to information filed with and produced by the PUC. The Commission’s current system was developed in 1978 and includes a number of mainframe-based applications that are very difficult to support due to the declining number of technicians who are familiar with such applications.

Once completed, InfoMAP will be state-of-the-art and will provide easier access to the Commission through systems such as electronic filing, as well as electronic payment systems. The estimated completion date is the first quarter of 2008.

IDENTITY THEFT INVESTIGATION

On July 14, 2005, the Commission concluded its nine-month investigation into whether the PUC's rules, regulations and policies adequately protected consumers and utilities from the effects of identity theft.

The Commission encouraged utilities to enhance their protection of personal information; develop or re-evaluate their notification of database security breach procedures and their internal policies on identity theft; and continuously review their policies on the storage of confidential customer information. The PUC also will continue to monitor federal and state statistics, reports and legislation addressing identity theft and related issues.

Identity theft takes place when one person uses another's personal information such as name, Social Security number, credit card number or other identifying information to commit fraud or other crimes. As noted in the Order initiating the investigation, "Identity theft results in losses for both the customer and the utility company. For the victims of identity theft, the recovery from damage and the tainting of one's financial reputation may be a slow, arduous and time-consuming process.

Often, repair to a victim's credit reputation and financial condition takes years. For the utility company, identity theft frequently results in uncollected charges for service as well as increased expenditures of company resources to collect unpaid bills."

ENERGY

The focus remained steadfast on both electric service and natural gas distribution system reliability in Fiscal Year 2005-06. The PUC saw a significant rise in the number of rate cases before the Commission. A number of mergers and acquisitions also were considered. Issues surrounding competition within both the electric and natural gas markets, including rates, emerged as a focal point. The Commission began a process to study possible policy actions that could mitigate any possible price spikes for consumers as the rate caps on electricity prices expire. The Commission also continued to improve its homeland security and emergency preparedness.

HOMELAND SECURITY & EMERGENCY PREPAREDNESS

The Commission has in place a self-certification regulation that requires each regulated utility to certify in an annual filing that it has reviewed its physical security, cyber-security, emergency and business continuity plans, and conducted tests or drills of these plans. This regulation followed a recommendation from the PUC's House Resolution 361 investigative report.



The Commission also is spearheading an organizational structure of utility support to the Commonwealth's nine regional counter-terrorism task forces. A utility representative from both mobile and fixed utilities will be placed on a local task force.

The emergency preparedness of the utilities in the Commonwealth was severely tested by floods in June 2006. Flooding affected electric, natural gas, water and telephone service in many parts of the Commonwealth, especially in the eastern part of the state. The Commission also supported the Disaster Recovery Centers set up to help with the recovery effort.

During emergencies, a Commission team mobilizes at the Pennsylvania Emergency Operations Center in Harrisburg. The PUC Emergency Management Response Team provides assistance to utilities responding during an emergency, and coordinates with other state agencies to ensure that all available resources are being used. Its primary goal is to meet the needs of those responding to an emergency quickly and effectively. The team also makes sure a clear line of communications is available from the utilities to the PUC, Pennsylvania Emergency Management Agency and Governor.

The Commission team has undergone Homeland Security sponsored training and is certified in the National Incident Management System and the National Response Plan.



Dave Newcomer, the PUC's Emergency Management Coordinator, addresses participants at a Regional Terrorism Task Force Meeting.

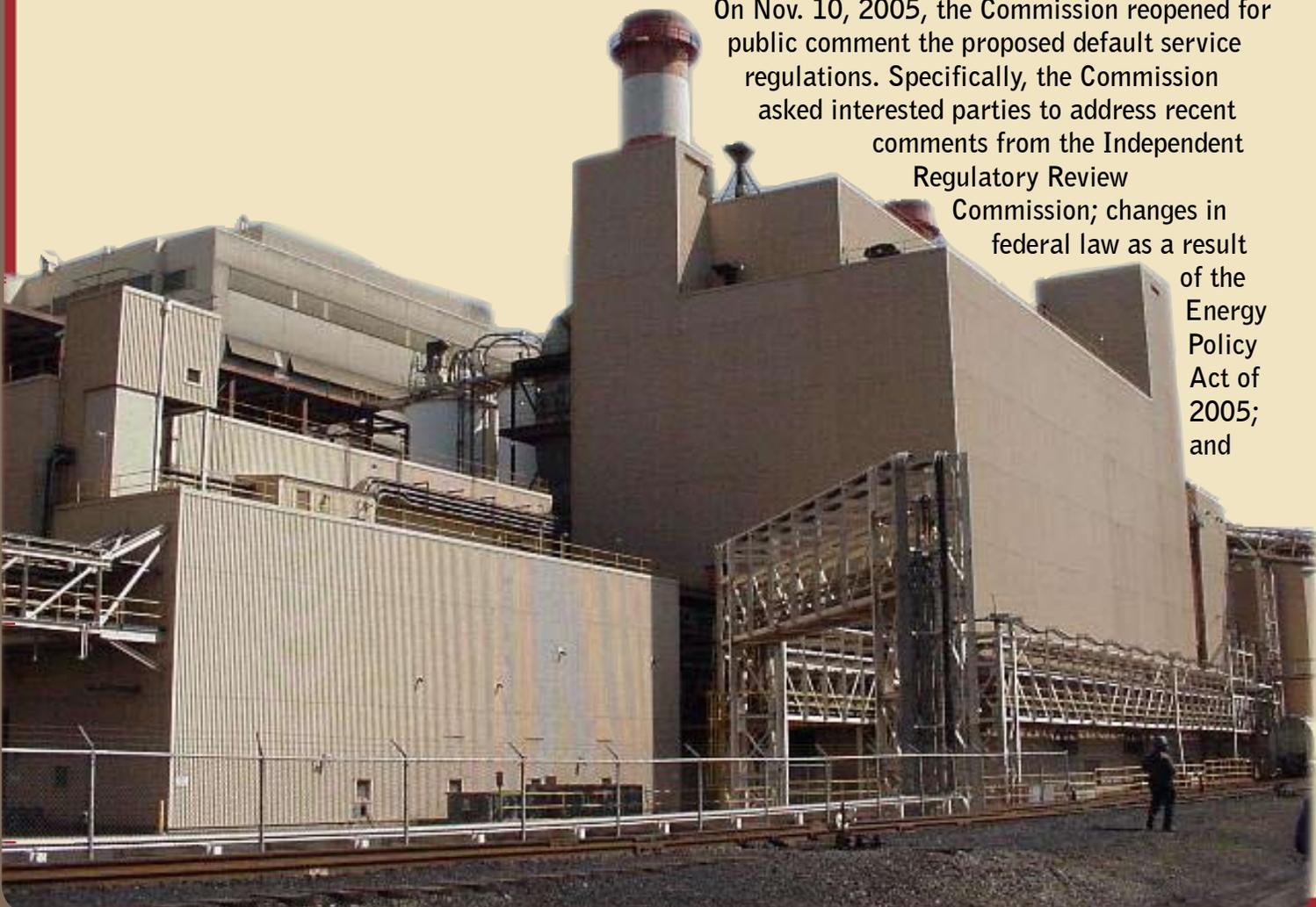
ELECTRIC OVERVIEW

The state is nearing the end of the transition period for the restructuring of the electric utilities. Recognizing the ongoing need to provide guidance to the industry, the Commission reopened for comment proposed default service regulations in November 2005. The PUC also held a hearing as part of its study into policy options that could mitigate any possible price spikes for consumers as the rate caps on electricity prices expire. The 1996 electric competition law requires electric companies to provide service to customers who have not selected an alternative generation supplier.

ELECTRIC RESTRUCTURING, DEFAULT SERVICE

While the law identifies certain underlying requirements that must be followed by the PUC in determining the electric distribution companies' obligations, it also provides significant flexibility in developing default service regulations. Those regulations will establish criteria for generation service provided to customers who do not receive or choose not to receive the service from an alternate supplier. It is one of the most important rulemakings for the Commission since the restructuring of the electric industry. The rulemaking is the mechanism for establishing pricing for electricity after the rate caps, created during the restructuring of the electric industry, expire.

On Nov. 10, 2005, the Commission reopened for public comment the proposed default service regulations. Specifically, the Commission asked interested parties to address recent comments from the Independent Regulatory Review Commission; changes in federal law as a result of the Energy Policy Act of 2005; and



cost-recovery issues related to the state's Alternative Energy Portfolio Standards Act. The comments have been received; and Commission staff continues to evaluate them as final rules are developed.

The Commission acted on three temporary default service plans for companies whose rate caps expire prior to the development of the statewide regulations. The Commission approved a settlement that established the second round of default service rates for UGI Utilities Inc. The generation rate cap for Pike County Light & Power also expired during this fiscal year. The Commission modified and approved the default service proposal for Pennsylvania Power Co. that will go into effect when its rate caps expire on Dec. 31, 2006.

Currently, 16 electric distribution companies and 42 licensed electric generation suppliers operate in Pennsylvania.

OPTIONS TO MITIGATE POTENTIAL SIGNIFICANT INCREASES

On June 22, 2006, the Commission held an en banc hearing to begin a process to develop policies to mitigate higher electricity prices.

Most Pennsylvania electricity consumers are paying capped generation rates and will continue to do so until the end of 2009 or 2010. Recent events in Pennsylvania, Maryland and Delaware have shown that electricity consumers can be exposed to sudden dramatic price increases when long-term generation rate caps expire. The long-term caps were agreed upon during state restructuring proceedings for the electric utilities.

The Commission heard testimony from consumer advocates and industry experts on the issues and possible policy actions that could mitigate potential future significant electricity price increases. More than 30 parties filed comments with the Commission prior to the hearing regarding ideas to assist in addressing potential significant price increases.

PIKE COUNTY LIGHT & POWER

The Commission took steps to help consumers in the Pike County Light & Power (PCLP) territory where consumers experienced a significant rate increase with the expiration of its rate caps. The results of implementation of its default service plan for the territory resulted in about a 73 percent increase in consumer bills.

On April 20, 2006, the Commission approved a retail aggregation program for PCLP consumers that resulted in a modest reduction in those rates. The action stemmed from unique circumstances that resulted in PCLP consumers experiencing unprecedented increases in rates. The initial wholesale auction process for purchasing power for those consumers was affected by many factors, including: the timing of the auction, which occurred during peak natural gas prices; minimal auction participants; and no competitive retail activity in the area. As part of a fact-finding investigation, Vice Chairman James Cawley and Commissioner Bill Shane presided over a public hearing in Milford. The results of the investigation were released in June 2006; and the

Commission continues to look for long-term solutions of improving wholesale market access to PCLP customers.

RATE INCREASE REQUESTS

In Fiscal Year 2005-06, the Commission received rate increase requests from electric utilities totaling more than \$535.7 million. Final decisions on those rate increase requests must be reached by the second quarter of Fiscal Year 2006-07.

On April 7, 2006, Duquesne Light Co. filed its first distribution base rate case since 1986 requesting an increase of \$162.7 million. The proposed increase would affect about 600,000 residential, commercial and industrial customers in two counties.

FirstEnergy submitted a request on April 10, 2006, to increase its rates for the company's Metropolitan Edison Co. (Met-Ed) and Pennsylvania Electric Co. (Penelec) customers. The companies proposed a "Rate Transition Plan," which would increase customer rates in 2007, 2008 and 2009 to recover certain generation, transmission and distribution expenses. The Met-Ed increase of \$216 million would impact 535,000 customers throughout the state. The Penelec increase of \$157 million would impact 588,000 customers throughout Pennsylvania.

ALTERNATIVE ENERGY PORTFOLIO STANDARDS ACT OF 2004

On Nov. 30, 2004, the Alternative Energy Portfolio Standards Act was signed into law. Generally, the Act requires that electric distribution companies and electric generation suppliers include a specific percentage of electricity from alternative resources in the generation that they sell to Pennsylvania customers.



Photo courtesy of West Penn Power Sustainable Energy Fund.

The Act took effect on Feb. 28, 2005, and the first reporting year began on June 1, 2006. The Commission opened an implementation proceeding and convened a staff-led working group in March 2005. The Commission subsequently issued two Implementation Orders at this docket that established a timetable for compliance and resolved certain other issues.

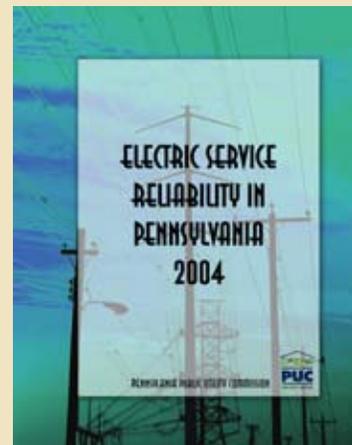
The Commission issued a Final Order on Sept. 29, 2005, establishing rules for the participation of demand side management resources in this market. The Commission also designated an alternative energy credits registry, issued a request for proposal for the program administrator and qualified many generators for alternative energy system status. After the conclusion of the fiscal year, the Commission issued final Orders establishing regulation for net metering and interconnection of distributed generation resources. Those regulations received approval from the state's Independent Regulatory Review Commission.

RELIABILITY

Under the Electric Generation Customer Choice and Competition Act, each electric distribution utility is obligated to ensure that its service does not deteriorate below the level of service reliability that existed prior to the Jan. 1, 1997, effective date of the Act.

During the 2005-06 fiscal year, the Bureau of Conservation Energy & Economic Planning (CEEP) was designated as the lead bureau with primary responsibility for ongoing, continuous monitoring and follow-up concerning electric distribution system reliability. Prior to this action, electric reliability responsibilities were handled by an ad hoc working group comprised of several Commission bureaus. Within CEEP, the Commission established a supervisor of electric reliability who monitors the reliability of the Commonwealth's electric power grid, primarily as it relates to the distribution grid.

CEEP's monitoring effort was focused on reviewing annual and quarterly reports filed by the electric distribution companies. Large electric companies have to stay within 10 percent of a PUC-established benchmark for a rolling three-year period and within 20 percent of the benchmark during a rolling 12-month period. Four smaller electric companies – UGI, Citizens, Pike County and Wellsboro – also must stay within 10 percent of their benchmark for a rolling three-year period, but will be allowed to go up to 35 percent of the benchmark for the rolling 12-month period. Benchmarks are the Commission's goals for each utility on the number and duration of outages.



An annual reliability report – Electric Service Reliability in Pennsylvania – was issued by the Commission in December 2005. The public report trends reliability performance from 1994 to 2004 and includes the causes of outages, by percentage, and information on all major events. The annual reliability report reviewing 2005 performance is to be released in the first quarter of Fiscal Year 2006-07.

On April 21, 2006, the Commission issued a proposed rulemaking for the purpose of establishing inspection and maintenance standards for Electricity Distribution Companies (EDCs). The proposed regulation requires an EDC to have a plan for: periodic inspection and maintenance of poles; overhead conductors and cables; wires; transformers; switching devices; protective devices; regulators; capacitors; substations; and other facilities critical to maintaining an acceptable level

of reliability. The proposed regulation also sets forth minimum inspection and maintenance intervals for vegetation management, poles, overhead lines and substations. Comments on the proposed rulemaking have been received and are under review by the Commission in advance of the final rulemaking.

MERGERS AND ACQUISITIONS

On Jan. 27, 2006, the Commission approved the merger of Exelon Corp., the parent company of PECO, and New Jersey's Public Service Enterprise Group Inc. (PSEG). The terms of the merger resulted from a settlement reached between the company and consumer, business, environmental and low-income advocates.

As part of its merger approval, the Commission gave the approval for a fact-finding investigation into the issues related to the possibility of consolidating Philadelphia Gas Works (PGW) into the natural gas business Exelon. The fact-finding investigation is to begin 30 days following the consummation of the merger. While Commission approval of the merger is a major step in the process, approvals by other jurisdictions were still required. After the close of the fiscal year, the merger was terminated by the companies, and as a result, all related dockets were closed.



ORGANIZATION OF PJM STATES/ORGANIZATION OF MISO STATES

In May 2005, the PUC and 13 other regulatory commissions within the PJM Interconnection territory formed a non-profit organization known as the Organization of PJM States Inc. (OPSI). PJM operates the competitive wholesale electricity market in our region and manages a regional planning process for generation and transmission expansion to ensure future electric reliability.

Chairman Wendell F. Holland serves as the first President of OPSI. The purpose of OPSI is to provide coordination of state participation in the PJM stakeholder process by consultation on upcoming issues and assist the sharing of information among member agencies. OPSI facilitates the submission of joint comments to PJM and the Federal Energy Regulatory Commission (FERC). Since its inception, OPSI has provided comments to FERC in two dockets.

The Organization of MISO States Inc. (OMS) is OPSI's counterpart in the Midwest Independent System Operator's (MISO) service territory. The Commission is a member of OMS; and Commissioner Kim Pizzingrilli serves as the Treasurer of OMS. The PUC continues to monitor and participate in OMS workgroups and send comments to FERC.

OPEN ACCESS TO INTERSTATE TRANSMISSION

Open and non-discriminatory access to interstate transmission systems by all electric generators remains essential for a properly functioning wholesale market for electricity. To support this objective, the Commission participated on various rules committees with PJM Interconnection and the MISO.

Changes to the existing FERC Open Access Transmission Tariff rules were proposed on May 19, 2006. FERC has indicated that it wishes to update and strengthen its transmission and market tariff rules in accordance with the Energy Policy Act of 2005 (EPACT 2005) to forestall the exercise of market power in wholesale electric markets.

In addition, the PUC is actively monitoring and participating in the application by PJM to replace its existing capacity mechanism with a "Reliability Pricing Model" designed to increase generator investment in the PJM territory. FERC issued an Interim Order on April 20, 2006, largely approving PJM's application even though it is opposed by nearly all buyers of electricity in the PJM wholesale market. After the conclusion of the fiscal year, a settlement was reached and is being considered by FERC.

The PUC is monitoring FERC's implementation of provisions of EPACT 2005. A number of policy statements and proposed or final regulations have been issued. On June 15, 2006, FERC issued rules intended to carry out its EPACT Section 1221 responsibilities to receive siting applications from transmission project owners that wish to take advantage of the "federal backstop" provisions, where state authorities have either failed to act within one year of a state application or are unable to do so under state law. Such projects must be located within National Interest Electric Transmission Corridors designated by the federal Department of Energy under rules yet to be issued.

The PUC also is monitoring PJM's changes to its market monitoring plan, purportedly in response to a general FERC policy statement regarding the relationship of Regional Transmission Organization market monitors to FERC's enforcement function. A number of parties, including the PUC, filed comments or protests in response to the filing.

RENEWABLE AND SUSTAINABLE ENERGY

This year, the PUC led the effort to update the Pennsylvania Sustainable Energy Board (PASEB) bylaws, to reflect the passage of Act 213 of 2004, the Alternative Energy Portfolio Standards Act, as well as best practices for the regional funds.

The Annual Meeting was held on Sept. 15, 2005. Presentations were made by each of the funds on their activities during 2004. Presentations were also made by staff of the Commission and Department of Environmental Protection, on the topics of alternative energy and Act 213 of 2004.



Various restructuring and merger settlements from electric competition allocated nearly \$80 million of ratepayer funds, over about a 10-year period beginning in 1998, for regional projects to develop renewable and clean energy technologies. The Commission is responsible for approving nominations to each fund's board of directors and changes to their governing bylaws. Examples of projects for which the regional boards have approved funding include wind farms, photovoltaic applications and renewable energy education.

In 2005, the funds provided slightly less than \$12 million in loans and more than \$2 million in grants for investments in renewable and clean energy, and energy efficiency projects. Commission staff continues its liaison role with the regional sustainable energy funds.

ELECTRIC COMPANY AUDITS

The Commission's Bureau of Audits periodically performs management and operations audits (MAs) or management efficiency investigations (MEIs) of its jurisdictional energy distribution companies. Among the MAs and MEIs completed within the 2005-06 fiscal year were:

- Duquesne Light Co. – The MA of Duquesne found that the company has the opportunity to achieve annual and one-time benefits or savings of up to \$6 million and \$32.1 million, respectively, by implementing recommendations to reduce its customer arrearages and accounts receivable write-offs, collecting the authorized interest on its loans to affiliates, and by writing off obsolete inventory.
- PPL Electric Utilities, North Penn Gas Company and PFG Inc. – The MEI of the combined PPL energy companies found that the companies had achieved \$20.8 million in annual savings and \$1.3 million in one-time savings by implementing past management audit recommendations to improve allocation of costs among affiliates, adjust affiliate service costs to market rates, and reduce inventory levels. Also, the MEI found that the companies have the opportunity to achieve approximately \$1.6 million in annual savings and \$10.9 million in one-time savings by further reducing its inventories.

In addition to the periodic MAs and MEIs, the Bureau of Audits conducts a variety of other electric company audits annually. During the fiscal year, bureau staff completed 14 competitive transition cost, purchased power or consumer-education audits of jurisdictional electric companies with recommended adjustments of \$1.1 million.

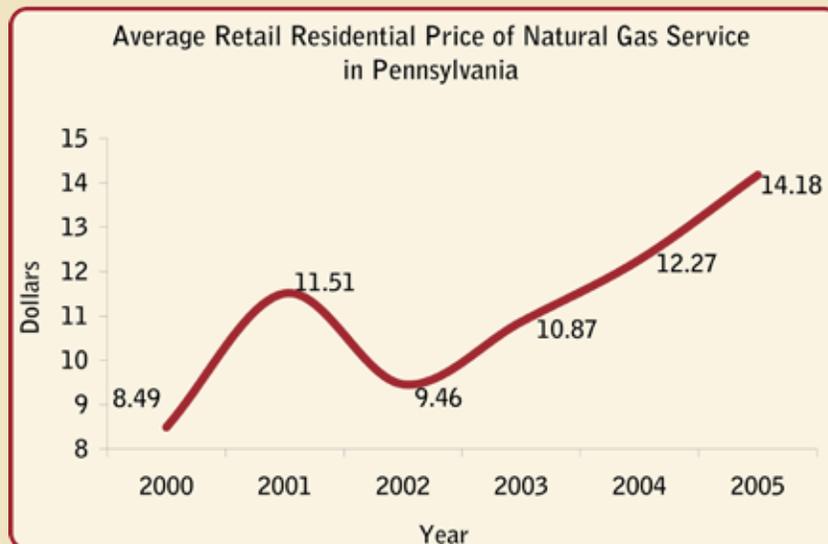
NATURAL GAS OVERVIEW

WHOLESALE NATURAL GAS PRICES

Market conditions and the extraordinary destruction of Hurricanes Katrina and Rita pushed wholesale prices for natural gas up in the fall of 2005. These increases placed a significant burden on customers. The primary natural gas wholesale trading center for the continental United States is the Henry Hub in Louisiana, where much of the hurricane destruction was centered. Daily gas wholesale spot prices and gas futures also are centered at the Henry Hub.

Hurricanes Katrina and Rita damaged, set adrift or sank 192 oil and natural gas drilling rigs and producing platforms. More than 30 percent of Gulf of Mexico daily gas production was lost; and more than 50 percent of on-shore natural gas production in Louisiana was lost.

Before the hurricanes, prices were \$8 to \$9 per thousand cubic feet (Mcf) at the Henry Hub. After the hurricane damage, prices were in excess of \$12/Mcf, and for several days were above \$15/Mcf. Warm weather in the first three months of 2006 pushed wholesale prices down below \$8/Mcf (January was 30 percent warmer than normal).



Retail gas prices have not increased as much as wholesale spot prices. Natural gas utilities maintain a portfolio of supplies: contract supplies (delivered by pipeline) with varying terms and conditions; gas from storage; local production; and spot gas purchases.

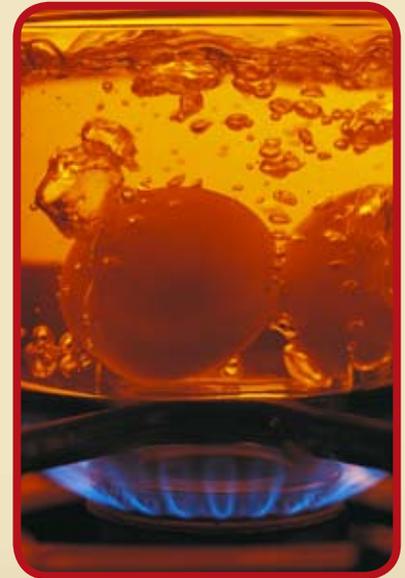
Currently, 33 regulated gas distribution companies and 85 licensed natural gas suppliers operate in Pennsylvania.

INVESTIGATION INTO NATURAL GAS COMPETITION

On Oct. 6, 2005, the Commission released its Report to the General Assembly on Competition in Pennsylvania's Retail Natural Gas Supply Market. The report followed an investigation into the level of competition in the state's natural gas market. It comes five years after the 1999 Natural Gas Choice and Competition Act permitted customers to purchase gas from independent natural gas suppliers (NGSs), while still having their gas delivered by regulated natural gas distribution companies (NGDCs). The Act directed the Commission to investigate the level of competition after five years and to report its findings to the General Assembly.

The Commission opened its investigation in May 2004, and asked NGDCs, NGSs, the state office of Consumer Advocate and all other interested parties to evaluate the level of competition in the retail natural gas market in Pennsylvania. After review of the investigation's evidence, including comments from the NGDCs, NGSs and other interested parties, as well as an en banc hearing, the Commission determined that effective competition in the retail natural gas supply services market statewide did not exist at the time. The report may be accessed on the PUC Web site at www.puc.state.pa.us.

With that conclusion reached by the Commission, the Act required the Commission to convene an industry-wide stakeholder group to explore avenues, including legislative, for encouraging increased participation in Pennsylvania's retail natural gas supply market. The Commission established the Stakeholders Exploring Avenues for Removing Competition Hurdles (SEARCH) group.



SEARCH

The stakeholders include: NGDCs; NGSs; the Office of Consumer Advocate; the Office of Small Business Advocate; advocates for large industrial customers; the Energy Association of Pennsylvania; and representatives from transportation pipelines.

The initial meeting of the SEARCH was held on March 30, 2006. The barriers identified during the PUC's investigation were divided among four subgroups for evaluation: Inter-Company Activity; Customer Interface; Cost of Service; and Competition Monitoring. It is anticipated that SEARCH will complete its meetings and submit a report to the PUC identifying ways to increase competition in Pennsylvania's natural gas supply services market by early 2007.

BASE RATE INCREASE REQUESTS

In Fiscal Year 2005-06, the Commission received base rate increase requests from four of the state's major natural gas utilities totaling more than \$90.1 million. Final decision on those rate increase requests must be reached by the first half of 2006-07. The base rate increase requests include:

- T.W. Phillips – \$21.67 million filed on Feb. 13, 2006. The proposed increase would affect about 59,500 consumers in nine western Pennsylvania counties.
- PG Energy – \$29.8 million filed on April 13, 2006. The proposed increase would affect about 160,880 customers in northeast and central Pennsylvania.
- PPL Gas Utilities – \$12.8 million filed on April 27, 2006. The proposed increase would affect about 75,000 consumers in 27 counties.
- National Fuel Gas Corp. – \$25.9 million filed on June 2, 2006. The proposed increase would affect about 214,000 customers in 14 northwestern Pennsylvania counties.

MERGERS AND ACQUISITIONS

On Feb. 16, 2006, UGI Corp. filed to acquire PG Energy from Southern Union Co. PG Energy, based in Wilkes-Barre, serves about 158,000 customers in 13 counties in northeastern and central Pennsylvania, including Scranton and Williamsport. UGI serves 307,000 natural gas customers in 14 Pennsylvania counties, including areas such as Harrisburg, Lancaster, Reading, the Lehigh Valley and their surrounding suburbs. After the close of the fiscal year, the merger was approved.

On March 31, 2006, Equitable Energy filed to acquire Dominion Peoples Natural Gas Co. Both companies are based primarily in the Pittsburgh region, but with operations in West Virginia, Kentucky and Ohio. The merger would create the largest natural gas company in Pennsylvania with more than 700,000 customers. An ALJ is expected to issue a recommended decision in late 2006 for the Commission's consideration.

RELIABILITY

The Commission has also launched an examination of the reliability of natural gas distribution systems. This inter-bureau team has been meeting with the various distribution companies and gathering extensive information on the practices of the companies.

GAS SAFETY DIVISION

In Fiscal Year 2005-06, the Bureau of Transportation and Safety's Gas Safety Division commenced Transmission Pipeline Integrity Management inspections. These federally mandated inspections consist of a review of pipeline systems by more advanced methods, such as pigging, direct assessment and statistical analysis to ensure the pipelines are safe and reliable. The division has three inspectors certified to conduct these inspections.

From June 27 to 29, 2006, the Gas Safety Division hosted the National Association of Pipeline Safety Representatives (NAPSR) Eastern Region Meeting in Hershey. The meeting was attended by 40 gas safety program managers and federal inspectors from across the country. Discussion centered on new federal inspection programs and causes of pipeline incidents in the United States. The PUC's Gas Safety Division Chief, Paul Metro, is the Chairman of the NAPSR Eastern Region for 2006.

This year, the Gas Safety Division filed formal complaints against several natural gas distribution companies. Facility inspections and investigations of incidents involving these companies revealed serious safety violations. The division



PUC Gas Safety Inspectors works with representatives from a natural gas utility to make certain of the safety of the natural gas in our communities.

also investigated 12 reportable incidents. A reportable incident includes events that result in the death or injury of a person and/or property damage, including lost gas, of \$50,000 or more.

Additional Gas Safety Division activities include:

- 917 inspections (represents compliance, regulator and relief station, discontinued service, corrosion control, transmission line and compressor station inspections);
- 12 investigations of reportable incidents;
- 44 non-compliance letters; and
- 77 gas safety violations.

GAS COMPANY AUDITS

As with the electric companies, the Commission's Bureau of Audits performs periodic management and operations audits and management efficiency investigations (MEIs) of natural gas companies. Among those audits completed during the 2005-06 fiscal year were:

- PG Energy – The MEI was limited to a review and evaluation of the company's efforts to implement eight recommendations from the bureau's October 2001 focused management and operations report. During the MEI, the auditors found that PG Energy had realized annual and one-time benefits or savings of just under \$1.5 million and \$311,000, respectively, by implementing the past management audit recommendations to reduce management's spans of control and inventory. The MEI also resulted in 10 additional recommendations for improvement that, if fully implemented, could result in additional annual and one-time savings of approximately \$1.5 million and \$515,000, respectively, by reducing meter reading costs and further improving inventory turnover.

- T.W. Phillips – This MEI was limited to a review and evaluation of the company's efforts to implement 12 recommendations from the bureau's December 2001 focused management and operations report.



During the MEI, the auditors found that T.W. Phillips had realized annual and one-time benefits or savings of just under \$539,000 and \$225,600, respectively, by implementing prior management audit recommendations to reduce interest expense, increase recovery of finaled accounts, and eliminate one day of its billing lag. The MEI also resulted in 10 additional recommendations for improvement that, if fully implemented, could result in additional annual and one-time savings of approximately \$1.1 million and \$496,000, respectively.

In addition to the periodic MEIs, the Bureau of Audits conducts annual gas cost rate and purchased gas cost rate audits of the small and large gas companies. Bureau staff completed 32 of these audits during the year, with recommended adjustments of over \$2.75 million.

PUC FILES FERC COMPLAINT OVER PRICES

On April 7, 2006, the PUC, the Office of Consumer Advocate and the Public Service Commission of New York filed a complaint with FERC against National Fuel Gas Supply Corp. The agencies asked FERC to find that the company's existing rates are unjust and unreasonable under the Natural Gas Act. The company is an interstate natural gas pipeline and affiliate of National Fuel Gas Distribution Corp., which serves retail customers in Pennsylvania and New York. The agencies alleged the company was obtaining earnings above its FERC-authorized rate of return and, as a consequence, overcharging its customers in Pennsylvania and New York. FERC has set the case for hearing. After the conclusion of the fiscal year, the PUC entered into a settlement agreement which is being reviewed by FERC.

STEAM HEAT OVERVIEW

Four steam heat utilities currently operate in Pennsylvania. Community Central Energy Corp. (CCEC) in the Scranton area is in the process of discontinuing service to its customers.

COMMUNITY CENTRAL ENERGY CORP.

CCEC provides heat for about 27 industrial, commercial, institutional and residential entities in the Scranton area. The company uses natural gas to generate steam for its heating customers.

On Feb. 9, 2006, the Commission launched an investigation into the viability of the company after the loss of a contracted natural gas supplier affected the company's ability to ensure reliable service. The report, released in June 2006, concluded that the company experienced net losses during the calendar years 2003 through 2005. For 2003 and 2004, the Commission also found a disturbingly low ratio between the company's current assets and current liabilities.

A PUC survey of the company's customers revealed that most customers are in the process of converting to another heating source as a result of the high cost of steam heat. The survey results indicated that the company would not be able to survive much beyond the 2005-06 heating season due to the loss of its customer base.

On May 17, 2006, the company filed its application for abandonment, which the Commission approved after the conclusion of the fiscal year.

TRIGEN PHILADELPHIA

TRIGEN Philadelphia inaugurated a new chilled water service to provide cooling to its customers in Philadelphia. Chillers were located at its Edison station, and service will be rolled out to its customers over the next few years, depending upon their distance from the facility.

RATE INCREASE REQUEST

On June 29, 2006, NRG Thermal (Pittsburgh operations) filed a base rate increase of about \$1.14 million (21.3 percent). NRG Pittsburgh provides steam and hot and chilled water service to 18 commercial customers on the north side of the city of Pittsburgh. The major drivers for the increase are the company's construction program and increased expenses such as labor and benefits.

TELECOMMUNICATIONS

During this fiscal year, the Commission licensed 40 new local exchange carriers while taking action on three mergers for large telecommunications providers and protecting jobs when the Commission determined that these mergers were in the public interest. The Commission also moved forward with its implementation of key provisions of Act 183 of 2004 (Chapter 30), which encourages accelerated deployment of broadband services in exchange for alternative regulation and included the elimination of reporting requirements for local telephone companies. The PUC continued efforts to ensure that no customer is left without local telephone service by improving the availability of local service provider abandonment programs and expanding the Lifeline and Link-Up programs for low-income consumers. The Commission also maintained the PA Telecommunications Relay Service and other services that allow consumers who are deaf, hard of hearing and speech disabled to communicate by telephone with the hearing public.

LICENSED TELEPHONE COMPANIES

More than 40 new competitive local exchange carriers (CLECs) were added during the fiscal year. The three largest incumbent local exchange carriers (ILEC) are Verizon Pennsylvania Inc., Verizon North Inc., and United Telephone of Pennsylvania (Embarq). Currently, the number of telecommunications carriers certified by the Commission is as follows:

Classification	Quantity
Incumbent Local Exchange Carriers	37
Competitive Local Exchange Carriers	157
Interexchange Carriers, Toll Resellers	342
Interexchange Carriers, Toll Facilities-Based	65
Competitive Access Providers	83
Total	684

MERGERS AND ACQUISITIONS

During the fiscal year, the Commission approved a number of large mergers. These included the merger of:

- SBC Communications Inc. and AT&T Corp. to create AT&T Inc., which was approved in an Order entered on Oct. 6, 2005;
- Verizon Communications Inc. and MCI Inc., which was approved by the Commission in an Order entered on Jan. 11, 2006; and



- AT&T Inc. and BellSouth Corp., which was approved by the Commission on June 1, 2006.

All of these mergers were done at the holding company level and did not change the operation or certifications of the companies' jurisdictional entities.

On March 16, 2006, the PUC opened an investigation following an AT&T announcement that it intended to reduce its workforce by more than 200 employees in western Pennsylvania. The workforce reduction announcement came six months after PUC approval of the company's merger with SBC and was going to substantially reduce the workforce of its only remaining Pennsylvania-based Telecommunications Relay Service (TRS) call center. The call center handles calls between people who are deaf, hard of hearing and speech disabled and the hearing public.

In its merger application, AT&T made assurances that the merger would not adversely affect the continuity of Pennsylvania TRS and it would be able to meet its regulatory obligations and commitments as the TRS provider. The investigation was suspended after AT&T announced on March 31, 2006, it would not be continuing with the planned layoffs.

Two wireless mergers of note – Sprint-Nextel and Alltel-Western Wireless – were completed in 2005. While Commission approval of these mergers was not required, both Alltel and Sprint have decided to divest their local telephone companies. Commission approval of these spin-offs was required.

On April 7, 2006, the PUC approved a settlement that transferred control of United PA and LTD Long Distance from the newly merged Sprint/Nextel into a new independent parent company known as Embarq.

On June 12, 2006, the PUC also approved a plan that allowed Alltel to spin off its local phone business and merge it with Valor Communications Group Inc. The transaction was designed to create a voice, broadband and entertainment services company focused on the rural market in the United States. Similar to the Sprint/Nextel control transfer of its local landline business, the transaction will reposition Alltel Corporation as a wireless only service provider.

CHAPTER 30 IMPLEMENTATION

The Commission continues to implement key provisions of Act 183 of 2004, which seeks to encourage earlier completion of existing network modernization plans (NMPs) by incumbent local exchange carriers (ILECs) with more economic incentives and less Commission regulation. The continued Commission-approved alternative regulation encourages companies to accelerate broadband development.

About 33 ILECs have filed amended network NMPs under the options provided in Chapter 30. Companies had three options under the plan. Twenty-nine chose the first option, which provides for 100 percent broadband deployment by 2008 with a productivity offset of zero. Two companies chose the second option which requires a rural ILEC to commit to 80 percent broadband availability by 2010 and 100 percent by 2013 or 2015 plus a bona fide request program or business attraction or

retention program. Verizon and Verizon North have elected Option 3, which provides for a non-rural ILEC to commit to 100 percent broadband availability by 2013 or 2015 plus a business attraction or retention program.

PUC APPROVES PRICE CAP FILINGS

Most of the ILECs adopted price caps using the Gross Domestic Product – Price Index outlined in Act 183 of 2004 as the inflation factor under the alternative regulation portion of their Chapter 30 Plan. As a result, the carriers file their annual price stability index either accompanied by tariffed rate increases or banked revenue to be implemented within four years. During the fiscal year, companies with price caps collectively increased local service rates almost \$36 million with accumulated banked revenues of \$3 million.

UPDATED REPORTING AND FILING REQUIREMENTS

In reviewing the new Chapter 30, the Commission took action to continue, consolidate and/or eliminate general filing and reporting requirements imposed on location exchange carriers. In an Oct. 5, 2005, Final Implementation Order, the PUC eliminated or modified nine reporting requirements. Also, the Commission determined that residential account information filed by the companies must be provided on an annual basis rather than quarterly.

The Commission eliminated nine reports in accordance with Chapter 30. Also, the Commission adopted a new format for the annual financial report. The revised annual financial report appreciably abridged the information to be filed thereby reducing this reporting requirement for telecommunications carriers. The annual financial report for Calendar Year 2005 was due March 31, 2006.

On Oct. 27, 2005, the Commission approved investigative audits for the purpose of verifying reported progress by ILECs toward their Chapter 30 NMP obligations and to require ILECs to pay for the audits. The Commission also directed that the balance of Verizon's unencumbered escrow fund monies be used to pay for its NMP audit(s), and determined that it was appropriate to wait until Verizon's next biennial report, due in 2007, to conduct the initial NMP audit.

BONA FIDE RETAIL REQUEST PROGRAM

Chapter 30 created the Bona Fide Retail Request Program, which triggers the carriers' duty to expedite provision of broadband service where the requests for service meet a certain threshold. Under the program, customers within a "community" – as defined by Chapter 30 – may submit



a written request for broadband service. In most cases, if 50 retail customers or 25 percent of the retail access lines in a "community," whichever is less, request broadband service and commit to at least one year of service from the participating provider, then service must be provided within one year. Carriers are obligated to implement the program if they opted for later deployment in 2013 or 2015. Those carriers include Verizon, Verizon North, Windstream and Embarq.

The Pennsylvania Department of Community and Economic Development (DCED) is charged with administering this program. Several "communities" have met the requirements and deployment to their areas has begun. The Director of Operations is creating a staff team to work with DCED and the utilities on issues that arise with this program.

LOCAL SERVICE PROVIDER ABANDONMENT PROCESS FOR JURISDICTIONAL TELECOMMUNICATIONS COMPANIES

In its continuing efforts to ensure that no customer will be left without local telephone service, the PUC added important information to the Web site that pertains to the Commission's regulations regarding the local service provider (LSP) abandonment process. The regulation, as well as the application for abandonment, is available on the Web site to any LSP who may be considering leaving the Pennsylvania market.

The Commission also began posting the names of any LSPs that have begun the abandonment process with the Commission. In addition, Commission staff closely monitored a number of competitive local exchange carriers (CLECs) that received notice from a major incumbent local exchange carrier that it was threatening to terminate the wholesale service to the CLECs. The Commission staff also worked to ensure that all CLECs properly followed the abandonment procedures if they chose to leave the local service market in Pennsylvania as a result of the threatened termination.

During 2005-06, three LSPs ceased providing local service to their customers in Pennsylvania. However, due to the recently enacted regulations and the continuing monitoring by the Commission, no customers were stranded without local service when the companies exited the market.

CHANGING LOCAL SERVICE PROVIDERS RULEMAKING

The Commission's regulations for changing LSPs became effective Aug. 13, 2005. The regulations represent the culmination of a collaborative process that involved representatives of the industry, consumer advocates and a number of bureaus within the Commission. The purpose is to establish rules, procedures and standards so telephone customers can change telephone service providers without confusion, delay or interruption to their basic service. Each LSP operating in Pennsylvania must make available on its Web site the names and contact information of company representatives who are available to resolve problems experienced by other companies associated with migrating a customer's service from one company LSP to another. The companies are to supply the Web site addresses to the Commission. The Commission obtained this information from the companies and posted contact information for more than 70 LSPs on the PUC Web site.

The Commission also designated two Commission staff members through which LSPs and network service providers may request expedited resolution for any alleged problems between service providers or compliance with these regulations. The Commission sent this information to the LSPs and also posted the contact information on its Web site. As a result, any LSP facing problems migrating a consumer's local telephone service will have the tools available to resolve the problems.

PA UNIVERSAL SERVICE FUND

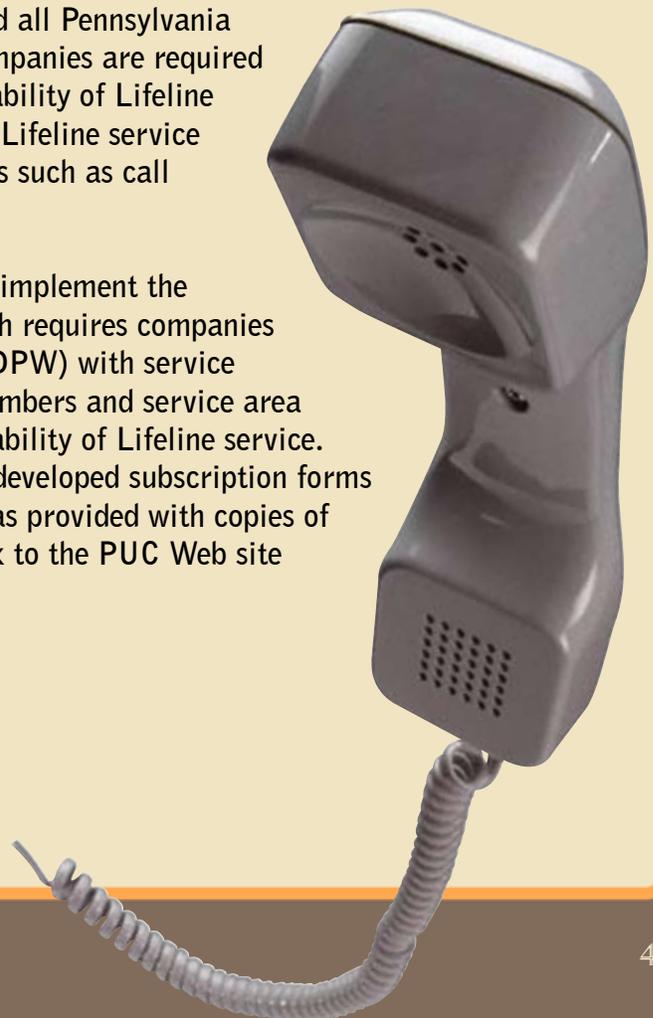
The PA Universal Service Fund ensures a gradual and smooth transition for the removal of subsidies in local rates by lowering access charges paid by long-distance toll providers in the rural ILEC territories. On July 1, 2006, auditor Withum, Smith & Brown submitted an auditor's report on the financials of the fund's activities during 2005. This report is on the PUC's Web site at www.puc.state.pa.us.

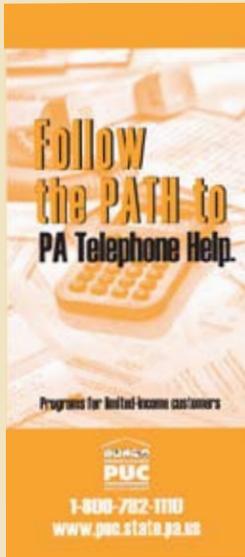
LIFELINE AND LINK-UP PROGRAMS

The Commission expanded the Lifeline and Link-Up programs to be consistent with the Federal Communications Commission's default Lifeline/Link-Up programs. On May 23, 2005, the Commission adopted new criteria for Pennsylvania's Lifeline/Link-Up program eligibility. Consumers participating in the National School Free Lunch Program with incomes at or below 135 percent of the Federal Poverty Guidelines are now eligible for the program.

In addition, the Commission directed three CLECs and all Pennsylvania ILECs to implement the Lifeline provisions. These companies are required to inform new and existing customers about the availability of Lifeline and Link-Up services. They must also permit eligible Lifeline service customers to purchase any number of optional services such as call waiting at the tariffed rates for these services.

Commission staff worked with a stakeholder group to implement the Lifeline service automatic notification provision, which requires companies to provide the state's Department of Public Welfare (DPW) with service descriptions, subscription forms, contact telephone numbers and service area information so it can notify its clients about the availability of Lifeline service. With the input of the stakeholders, Commission staff developed subscription forms and a listing of company contacts by county. DPW was provided with copies of the informational brochures for distribution and a link to the PUC Web site containing additional information on the programs.





PA TELEPHONE RELAY SERVICE (TRS), THE TELECOMMUNICATIONS DEVICES FOR THE DEAF PROGRAM (TDDP), AND NEWSLINE (SEE ALSO CONSUMERS).

During the fiscal year, the Bureau of Audits began the second audit of the underlying costs associated with the Telecommunications Devices for the Deaf Program. The first audit of the underlying TRS costs covering two fiscal years – ending June 30, 2005 – is continuing. Technological advances have established captioned telephone voice-carry-over relay service (CTVRS) as an alternative to regular TRS for the speaking segment of the deaf and hard-of-hearing community. The “CapTel ®” pilot program, begun in 2003 to test CTVRS in PA, has been converted to interim service and opened to new users while the search for a regular CTVRS provider continues. The General Assembly added funding responsibility for “Newsline” to the TRS surcharge. “Newsline” is an on-demand, newspaper reading service for the blind and others who cannot physically read a newspaper, accessible via toll-free telephone lines. The combined monthly line-item surcharge on customer bills for the TRS, TDDP and “Newsline” programs for 2005-06 remained the same for residential customers and decreased for business customers.

VERIZON'S PERFORMANCE ISSUES

The PA Carrier Working Group (CWG), comprised of Commission staff, Verizon PA, competitive local exchange carriers, the Office of Consumer Advocate, Office of Small Business Advocate and other interested parties, focuses on metrics and remedies. It continues to work with a footprint-wide CWG group to resolve outstanding issues raised in recent third-party reviews of the various states' Carrier-to-Carrier Guidelines and Performance Assurance Plans (PAPs). Additionally, work continues in the PA CWG on PA-specific operations and problems as well as incorporating foot-print changes into the PA Guidelines and PAP. A PA CWG subgroup is working on migration guidelines to facilitate customer migrations, especially between CLECs.

OP-12

In Ordering Paragraph No. 12 (OP-12) of its “Functional/Structural Separation Order” relating to Verizon Pennsylvania Inc., the Commission agreed to host meetings to aid in the resolution of operational and performance issues arising between Verizon and its wholesale customers. Issues that have been addressed include billing errors, invalid queries and difficulties with claims processing. This forum provides an opportunity for improved communications between Verizon and its wholesale customers, and is facilitated by Commission staff. Considerable time has been spent delving into complex technical issues and factual details to identify root causes of problems and resolve operational and performance issues without the time, expense and acrimony of litigation.

WATER/WASTEWATER

The Commission regulates the rates and service of more than 200 water and wastewater companies, including a number of municipal water and wastewater systems. In Fiscal Year 2005-06, the Commission acted on 13 water and wastewater rate increase requests. The Commission also processed 56 applications for Certificates of Public Convenience, including requests for additional territory, abandonments, formation of new companies, mergers and acquisitions.

The focus on water consumer educational activities continued, with the highpoint being the public exhibits and media event that marked National Drinking Water Week and raised awareness of the value of drinking water.

As part of its ongoing efforts to enhance small water system viability, the Commission moved forward with an acquisition incentive policy statement and continued its ongoing interagency cooperation activities. The Commission also issued an investigative report following a fluoride spill at a water utility which led to opportunities for all regulated utilities to enhance public notification during emergencies. The Commission also began revising certain related policies intended to improve both the substance and timeliness of utility communications with customers during emergencies.

OPPORTUNITIES FOR ENHANCED EMERGENCY COMMUNICATIONS

The PUC directed staff to investigate a Dec. 10, 2005, Pennsylvania American Water Co. (PAWC) high fluoride concentration incident that affected about 34,000 customers in Cumberland and York counties. According to the investigation report released March 10, 2006, the elevated level of fluoride concentration was the result of operator error at PAWC's Yellow Breeches Water Treatment Plant in Fairview Township, Cumberland County. Corrective measures have since been implemented. Other areas reviewed relating to customer communications and emergency preparedness and response revealed the need for further corrective measures across the industry.

Accordingly, the Commission sought to further clarify its regulation with a proposed policy statement regarding public notice guidelines during unscheduled water service interruptions. The goal is to ensure that actual, timely notice to customers is provided by water utilities whenever



an event potentially endangers the customer's water supply. It also addresses the importance of assuring adequate alternative sources of water are available in pre-determined, conspicuous and sufficient locations in the affected area.

The proposed policy statement enhances customer notification in situations that impact health and safety of water consumers such as "boil water" or "do not consume" orders. It includes a series of acceptable methods for improving the timeliness and effectiveness of notice to water customers and state and local officials when the quality or quantity of the potable water supply has been affected. It also encourages improvement in the use of technology, media and direct customer contacts.

In a related action, the Commission issued a proposed rulemaking to clarify its regulations defining water service interruptions. PUC regulations direct utilities to notify the Commission by telephone within one hour of an unscheduled service interruption affecting 2,500 or 5 percent of their total customers, whichever is less, for six or more consecutive hours. During the PAWC investigation, the company asserted that "service interruption" was not clearly defined in the regulation. The Commission did not agree but has taken steps to more clearly define that term.

The proposed change to the regulations defines "service interruption" as "any interruption of service affecting the quantity or quality of water delivered to the customers." The Commission is considering comments made on the proposed regulation before issuing a final decision on the issue.

AUDITING EMERGENCY RESPONSE PLANNING

The Commission requires that companies certify that their physical and cyber, emergency response and business continuity plans are current. During Fiscal Year 2005-06, the PUC found that deficiencies in the plans that the companies previously had certified were in accordance with Commission requirements. In some cases, the plans were outdated and phone numbers for Commission contacts were obsolete. To correct the deficiencies, the PUC initiated a new audit program to ensure that all water utilities' emergency response plans are current and in compliance with all applicable laws and regulations, including cyber and physical security along with business continuity.

WATER SYSTEM VIABILITY

Pennsylvania has more than 2,200 community drinking water systems, many of which are small water systems serving less than 3,300 consumers. The PUC regulates the rates and service of about 125 of those water companies. Many were built decades ago, and a number now face operational, technical and financial challenges that could affect customer service.

Many small water systems have varying degrees of operational constraints that impact their viability. Operational constraints inherent to small systems typically include: compliance problems; limited technical and managerial expertise; lack of capital for improvements, with a limited ability to borrow at reasonable rates; deferred maintenance; deteriorated and undersized infrastructure; and minimal sources of supply or storage.

A viable water system is one that is self-sustaining and has the financial, managerial and technical capabilities to reliably meet both PUC and Department of Environmental Protection requirements on a long-term basis. The Commission remains committed to enhancing water system viability to ensure ratepayers of small water systems receive the same quality of service provided by larger, viable water companies.

REGIONALIZATION

Many of the water/wastewater mergers and acquisition applications the Commission acts on are a form of regionalization. In general, regionalization is the consideration of water resources in terms beyond artificial boundaries (townships, boroughs, city limits, municipalities, service territories, etc.). Some water systems in Pennsylvania lack the management and funding to stand alone as viable systems. Regionalization typically results in a cost-effective solution or alternative that works to ensure system reliability and water quality.

The benefits of regionalization include increased economies of scale and service efficiencies; and improved operations, management and technology. Approaches to regionalization can include mergers, acquisitions, physical interconnections, satellite management agreements and cooperative purchasing/operational pools. Regionalization is not limited to large jurisdictional companies buying or taking over smaller companies. In some cases, nearby non-jurisdictional water companies such as municipalities or authorities also have participated in regionalization efforts.

ACQUISITION INCENTIVES POLICY STATEMENT

Progress on a new acquisition incentive policy statement continued during this fiscal year. A final decision is expected in the first quarter of Fiscal Year 2006-07. The policy statement builds on earlier Commission actions to alleviate barriers to acquisitions, enabling ratepayers of the smaller, more troubled systems to experience improved service after being acquired by a larger, more viable water system. The policy statement will provide further guidance on when and how utilities interested in making an acquisition should submit original cost documentation that determines the appropriate value of the assets of an acquired system. It also addresses the opportunity for acquiring utilities to earn an acquisition premium for the purchases of companies that may not be as severely troubled, but the purchase will still improve the overall long-term viability of the water and wastewater industry.

REVIEW OF EQUITY INVESTORS' PURCHASE OF WATER/WASTEWATER UTILITIES

On March 16, 2006, the PUC reopened the record of an application proceeding involving the sale of a group of water and wastewater utilities to an equity investor. The Commission raised questions about the degree of utility managerial experience the purchaser may have and what impact, if any, it could have upon the quality of service for ratepayers.

The sale involves a stock transfer of Nuon Global Solutions USA Inc. to Hydro Star, LLC. Nuon Global owns Penn Estates Utilities Inc., Utilities Inc. of Pennsylvania and Utilities Inc. – Westgate,

which provide water and wastewater utility service in the state. Hydro Star is a subsidiary of the American International Group (AIG) Highstar Capitol II, LP, which is a member of the AIG Global Investment Group, an affiliate of AIG. After the conclusion of the fiscal year, the review was completed and no additional conditions were placed on the transaction.

RATE INCREASE REQUESTS

During the fiscal year, the Commission took the following actions related to approximately \$41.9 million in rate increase requests:

Aqua Pennsylvania

Customers Served: 400,000 in 24 counties
Requested Rate Increase: \$38.8 million (14%)
Approved Rate Increase: \$24.9 million (9%)
Primary Reasons: Capital improvements, upgrades to treatment facilities and a new radio frequency metering system.

CAN DO Sewer

Customers Served: 50 in Luzerne County
Requested Rate Increase: \$93,000 (17.8%)
Approved Rate Increase: \$93,000 (17.8%)
Primary Reason: Recovery of increased operating expenses in new service area.

City of Bethlehem Water

Customers Served: 12,888 in Bethlehem and surrounding areas
Requested Rate Increase: \$885,000 (14%)
Approved Rate Increase: \$599,000 (9.5%)
Primary Reason: Increased operating costs.

City of Lancaster Water

Customers Served: 27,740 in Lancaster County
Requested Rate Increase: \$999,995 (14%)
Approved Rate Increase: \$950,000 (13%)
Primary Reason: Recovery of system improvement costs.

CMV Sewer

Customers Served: 378 in York County
Requested Rate Increase: \$82,000 (65%)
Approved Rate Increase: \$82,000 (65%)
Primary Reason: Recovery of sewer plant investment costs since 1991.

Glendale YearRound Sewer

Customers Served: 1,364 in Cambria County
Requested Rate Increase: \$90,000 (39%)
Approved Rate Increase: \$50,000 (22%)
Primary Reason: Recovery of sewer plant investment costs since 1997.

Marietta Gravity Water

Customers Served: 1,042 in Lancaster and York counties
Requested Rate Increase: \$114,000 (15%)

Approved Rate Increase: \$88,000 (12%)
Primary Reason: Recovery of increased operating expenses since 1991.

Meadows Sewer

Customers Served: 252 in Cumberland County
Requested Rate Increase: \$55,000 (29%)
Approved Rate Increase: \$24,000 (12%)
Primary Reason: Recovery of sewer plant investments since 1989.

MESCO Sewer

Customers Served: 175 in York County
Requested Rate Increase: \$48,000 (77%)
Approved Rate Increase: \$15,000 (23%)
Primary Reason: Recovery of increased operating expenses since 1991.

Newtown Artesian Water

Customers Served: 9,659 in Bucks County
Requested Rate Increase: \$662,000 (16%)
Approved Rate Increase: \$180,000 (4.2%)
Primary Reason: Recovery of increased operating costs.

Pocono Waterworks Co.

Customers Served: 170 in Wayne County
Requested Rate Increase: \$18,000 (29%)
Approved Rate Increase: \$18,000 (29%)
Primary Reason: Recovery of increased operating expenses since 1995 to comply with state Department of Environmental Protection and PUC regulations.

Wilcox Water

Customers Served: 212 in Elk County
Requested Rate Increase: \$20,000 (43%)
Approved Rate Increase: \$11,000 (24%)
Primary Reason: Recovery of new well and increased operating expenses since 1995.

Wonderview Water

Customers Served: 150 in Columbia County
Requested Rate Increase: \$13,000 (23%)
Approved Rate Increase: \$9,000 (13%)
Primary Reason: Recovery on increased operating expenses since 1993.

At the end of Fiscal Year 2005-06, rate increase requests still pending before the Commission included: Columbia Water Co. (\$519,000); Emporium Water Co. (\$316,144); United Water Co. (\$7.54 million); and York Water Co. (\$4.5 million).

DISTRIBUTION SYSTEM IMPROVEMENT CHARGE

The Distribution System Improvement Charge (DSIC) allows water companies to use a surcharge to fund more upgrades of aging infrastructure than would otherwise be feasible at a reasonable rate for customers. Pennsylvania was the first state in the nation to use the DSIC. Because of the DSIC, water customers experience improved water quality, greater rate stability and increased water pressure. Further benefits result due to fewer main breaks and service interruptions, along with lower levels of unaccounted for water.



Implemented in 1997, DSIC is an automatic adjustment charge that enables companies to recover certain infrastructure improvement costs between base rate cases through a quarterly surcharge on customers' bills. The cost is small when compared to the noticeable benefits, with approximate average monthly costs to ratepayers ranging from a few cents a month to about \$1.50. The DSIC has had substantial impact on accelerating infrastructure remediation in Pennsylvania. Prior to the DSIC, water utilities' progress in upgrading infrastructure relative to actual service lives was a major challenge. For example, one large company would have taken 900 years to complete its entire system and another would have taken 225 years. This problem is due in part to the fact that the original cost of the distribution systems has increased substantially over the past century. Today, with DSIC, projected timeframes for upgrades of entire distribution systems range from 117 to 160 years, more closely matching that of actual service lives.



The value of accelerated infrastructure remediation is substantial, benefiting customers not only today but well into the future due to noticeable improvements in water quality, pressure, fire protection, service reliability and rate stability. Numerous customer protections are included as well, such as a 5 percent cap on the total bill for an annual reconciliation audit and the requirement for customer notice.



Due to the DSIC and other innovative regulatory mechanisms, Standard & Poor's has recognized the PUC for effectively encouraging water company investment.

COLLECTION SYSTEM IMPROVEMENT CHARGE

On March 14, 2005, the Pennsylvania Commonwealth Court reversed a PUC Order that had approved a petition by PAWC to implement a Collection System Improvement Charge (CSIC). The Court concluded that the PUC did not have the authority to approve a rate mechanism such as CSIC to recover the fixed costs of a wastewater utility plant placed into service between base rate cases. The case revolved around the September 2003 decision of the PUC to allow PAWC to recoup approximately \$3 million to replace collection mains in three wastewater systems it purchased between 1995 and 2002.

Both the PUC and PAWC filed petitions for allowance of appeal in the Pennsylvania Supreme Court. On March 7, 2006, the Pennsylvania Supreme Court issued an Order denying both petitions. In the meantime, the state's Office of Consumer Advocate (OCA) filed a complaint against the company's initial CSIC charges. The case was assigned to a PUC Administrative Law Judge. In light of the Pennsylvania Supreme Court's March 7, 2006, decision, PAWC and OCA filed a joint petition for settlement of the complaint. Under the proposed settlement, PAWC would refund all of the CSIC charges it had obtained from its customers. The proposed settlement is pending before the ALJ.

MANAGEMENT AUDITS AND EFFICIENCY INVESTIGATIONS

The Commission's Bureau of Audits periodically performs management and operations audits or management efficiency investigations of its jurisdictional water companies. Among the audits completed within the 2005-06 fiscal year were:

- The York Water Co. – The management efficiency investigation of York Water found that the company had taken some action on or fully implemented all nine of the past management audit recommendations reviewed. The audit also found that approximately \$54,000 in annual savings and \$363,000 in one-time savings could be achieved by increasing its inventory turnover.

Other water company audits completed by the bureau during the fiscal year were three DSIC audits and three CSIC audits. Adjustments of about \$800,000 were recommended as a result of these audits.

LAND USE PLANNING ACTIVITIES

For the past three years, the Commission has worked jointly with 22 state agencies and programs that play a role in land use, development and conservation to craft the principles and recommended best practices for land use planning.

The Governor's Economic Development Cabinet issued its guide to state agencies in November 2005 titled "Keystone Principles for Growth, Investment and Resource Conservation." The agencies will gradually begin implementing the principles and criteria by applying them to significant programs over the coming months and eventually expanding their application to all relevant programs.

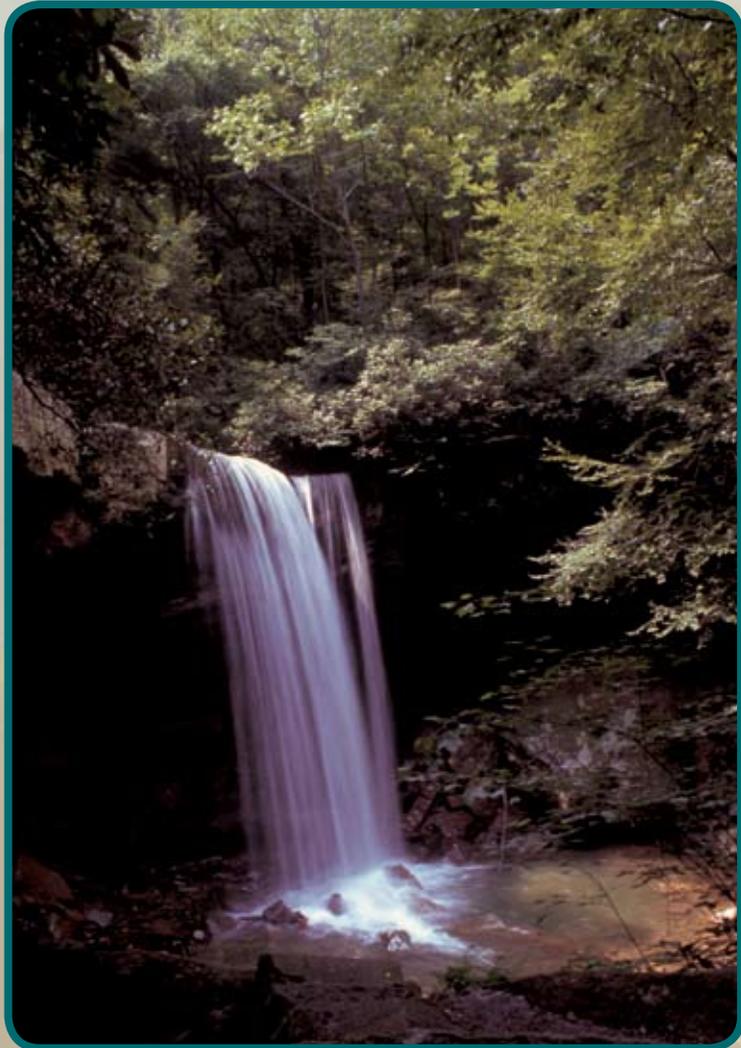
The Commission and other agencies will develop plans for how they will work with local governments when there are issues of consistency related to county and local or multi-municipal plans and ordinances. The land-use agreement creates a process to ensure that consistent county and local planning and zoning are considered in state agency permitting and funding decisions, which is a long-term concern of county and local governments. The goal of the principles and criteria is to strengthen the ability of agencies to consider and choose projects that are generally consistent with local plans and ordinances.

This inter-agency coordination builds on the Commission's 2001 Policy Statement on Land Use Planning, which provides that the Commission will consider the impact of its decisions upon local comprehensive plans and zoning ordinances. Further specification of land use planning considerations were also provided when the Commission updated its regulations pertaining to filing requirements for certificates of public convenience (completed in May of 2006). Specifically, newly formed utilities requesting an initial certificate of public convenience must include proof of compliance with any officially adopted county comprehensive plans, municipal comprehensive plans and applicable zoning designations.

STATEWIDE WATER RESOURCES

The PUC participates on the Statewide Water Resources Committee charged with carrying out Act 220 of 2002. This law requires the development of a statewide plan to manage the Commonwealth's water resources more effectively. Act 220 calls for the 25-year-old state Water Plan to be updated within five years, with regular updates every five years thereafter. The updated plan is to address the quantity of water available in the Commonwealth, the amount used, and the amount needed.

The Committee, which has adopted draft regulations and bylaws, held eight regional meetings and public hearings to receive input and comment about the direction of the plan. The Committee is in the process of collecting sound scientific data on a watershed basis, which will allow the Committee and all other concerned parties to assess the cumulative impact of our activities in order to preserve and protect water resources for future generations of Pennsylvanians.



WATER CONSUMER EDUCATION



With the backdrop of 162 one-gallon jugs of water representing the amount of water one person can use in a day, the PUC marked National Drinking Water Week from May 8-12, 2006, with the help of more than 100 elementary school children. More than 20 exhibits were on display in the Atrium of the Commonwealth Keystone Building. Participants in this educational event included various state agencies, regulated water companies, consumer and environmental groups, river basin commissions, conservation groups and others involved in water-related issues. The exhibits presented information about the hydrologic cycle, how drinking water is treated and delivered to the home, and the irreplaceable value of water service when compared to other commodities.



The Commission reminded consumers to "Prepare Now: Be Water Wise," highlighting the importance of using water wisely to save a valuable resource and money by lowering bills and avoiding shut-offs. Water consumers were encouraged to learn more about the changes in the law related to utility shut-offs and how these changes impact water consumers. The Commission also provided information about customer assistance programs designed to help low-income consumers with their bills.



An actor portraying Ben Franklin joined the Commission to deliver the messages found in two famous Franklin quotes of "A penny saved is a penny earned" and "When the well is dry, we know the worth of water." Both of his famous quotes underline the importance of using water wisely to potentially save money by lowering utility bills and avoiding shut-offs. State Rep. Carole Rubley presented a proclamation from the General Assembly commemorating National Drinking Water Week. Water company representatives also participated in the outreach event, providing further educational materials about the value of water service.

TRANSPORTATION & SAFETY

During Fiscal Year 2005-06, technology was the driving force behind changes in the Bureau of Transportation and Safety. Better use of technology is allowing the bureau's Motor Carrier Division to accept insurance forms and generate insurance violations electronically as they monitor the safety standards for more than 6500 motor carriers throughout the state. During the year, the division conducted about 19,500 enforcement activities. The enforcement staff also began using wireless Internet connections to conduct their enforcement activities more efficiently. The Rail Safety Division – a participant in the national Operation Lifesaver rail education program – conducted more than 30,880 inspections of locomotives, rail cars, tracks and rail operations. The division also participated in the enforcement of a Federal Rail Administration order that requires railroads to make changes to ensure that switches are restored to their normal position after use.



MOTOR CARRIER SERVICES AND ENFORCEMENT DIVISION

ELECTRONIC FILING OF INSURANCE FORMS

On April 3, 2006, the Commission's Bureau of Transportation and Safety Motor Carrier Division began a pilot program to permit the electronic filing of proof of insurance for its regulated motor carriers.

Under the pilot program, insurers are required to provide proof of insurance by filing paper documents through the mail. Under electronic filing, insurance companies file proof of insurance on behalf of PUC-certificated carriers. The insurers use a Web site established by National Online Registries, a company which acts as a conduit between states and insurance companies. It is believed that electronic filing will provide more timely filings and save money for both the insurers and the Commission. A significant, additional cost savings should be realized when the division transitions to direct receipt of electronic insurance filings from insurance companies. Since the pilot program began, the division has processed more than 900 electronic filings.

The Commission will re-evaluate the one-year pilot program prior to its termination and make a decision if the pilot program should be extended. A proposed rulemaking may then be initiated to revise the Commission's regulations to provide for electronic filing of insurance documents.

INSURANCE COMPLAINTS

During Fiscal Year 2005-06, the division worked with the PUC's Management Information System Office to automatically generate its insurance complaints through the existing case management system. Insurance complaints are generated against motor carriers who fail to maintain evidence of insurance with the PUC. Previously, staff drafted each complaint.

The case management system now automatically prints a complaint on the date the motor carrier's insurance is no longer effective. Staff simply verifies the information in the complaint prior to mailing it to the motor carrier. This operational change has helped the Compliance Office staff become more timely and efficient in managing its large volume of tasks.

MOTOR CARRIER SAFETY ASSISTANCE PROGRAM



Effective Oct. 1, 2005, the Pennsylvania State Police (PSP) became the lead agency for the administration of Motor Carrier Safety Assistance Program (MCSAP). From 1985 to 2005, the state Department of Transportation was the lead agency for the MCSAP. With the PSP designation, the PUC entered into a Memorandum of Understanding with the PSP in order to continue participation in the federal grant program.



The Commission's motor carrier enforcement staff and management team has received exceptional cooperation and support from the PSP. Under the PSP, the PUC enforcement staff has become a partner in the New Entrant Audit Program, and will become the auditing group for the bus carriers residing in Pennsylvania. The Motor Carrier Division continues to remain very active in the roadside truck inspection program, conducting more than 10,000 inspections this fiscal year.

WIRELESS INTERNET CARDS

In Fiscal Year 2005-06, the Commission purchased wireless cards for Motor Carrier Services and Enforcement Division enforcement staff. As a participant in the MCSAP, the Federal Motor Carrier Safety Administration has required mobile electronic access to its motor carrier data bases for personnel conducting roadside truck inspections.

The wireless cards enable enforcement officers to connect with their laptops to the federal administration Web sites to access federal driver and vehicle information during roadside inspections. The information allows officers to verify the status of the operator's commercial driver's license, vehicle registration information and a safety history of the motor carrier. The wireless cards also allow the officers to connect with their PUC e-mail and employee self-service accounts from remote locations allowing for better use of their time on the road.



REGULATED MOTOR CARRIERS

- 5,145 property
- 538 taxis
- 412 limousines
- 283 paratransit
- 71 airport transfer
- 312 group and party
- 61 scheduled route
- 303 household goods movers



2005-06 ENFORCEMENT ACTIVITIES

- 14,565 truck, bus, small passenger vehicle inspections
- 531 informal complaint investigations
- 1,173 safety fitness reviews
- 1,970 cases reviewed
- 1,252 prosecutory actions



RAIL SAFETY DIVISION

U.S. DEPARTMENT OF ENERGY TRANSPORTATION EXTERNAL COORDINATION WORKING GROUP

During the fiscal year, the Rail Safety Division attended meetings of the U.S. Department of Energy's Transportation External Coordination Working Group. The division representative is a member of the Rail/Routing Topic Group, which is responsible for determining appropriate routing for high-level radioactive waste shipments. This year's meetings focused on the development of route selection criteria and the analysis process to determine appropriate routing for High Level Spent Nuclear Fuel. The discussions included routing shipments from various parts of the county to Yucca Mountain, Nevada, for permanent storage, as well as temporary storage facilities.

FEDERAL RAIL ADMINISTRATION EMERGENCY ORDER NO. 24

The Rail Safety Division's safety inspectors are participating in the enforcement of the Federal Railroad Administration's Emergency Order No. 24. On Oct. 19, 2005, the Federal Railroad Administration (FRA) issued an Emergency Order that requires railroads to modify their operating rules and take specific actions to ensure that switches are restored to their normal position after use.





In 2004 and 2005, the frequency and severity of collisions resulting from improperly aligned main track switches increased. Accidents caused by switching errors also increased with the most serious accident in January 2005 in Graniteville, South Carolina, when nine people died, 630 were injured and 5,400 residents were evacuated. The accidents have occurred when railroad employees were working in areas that were not equipped with remote electronic signal monitors (i.e. train dispatchers are unable to monitor switch positions) and failed to follow track-switching procedures.

The FRA's October 2005 Emergency Order mandates that railroads retrain and periodically test employees on switch operating procedures and ensure that the position of the switches is communicated between crewmembers. The Commission is actively enforcing this Emergency Order, providing a safer and more efficient rail system for railroad employees and Pennsylvania citizens.

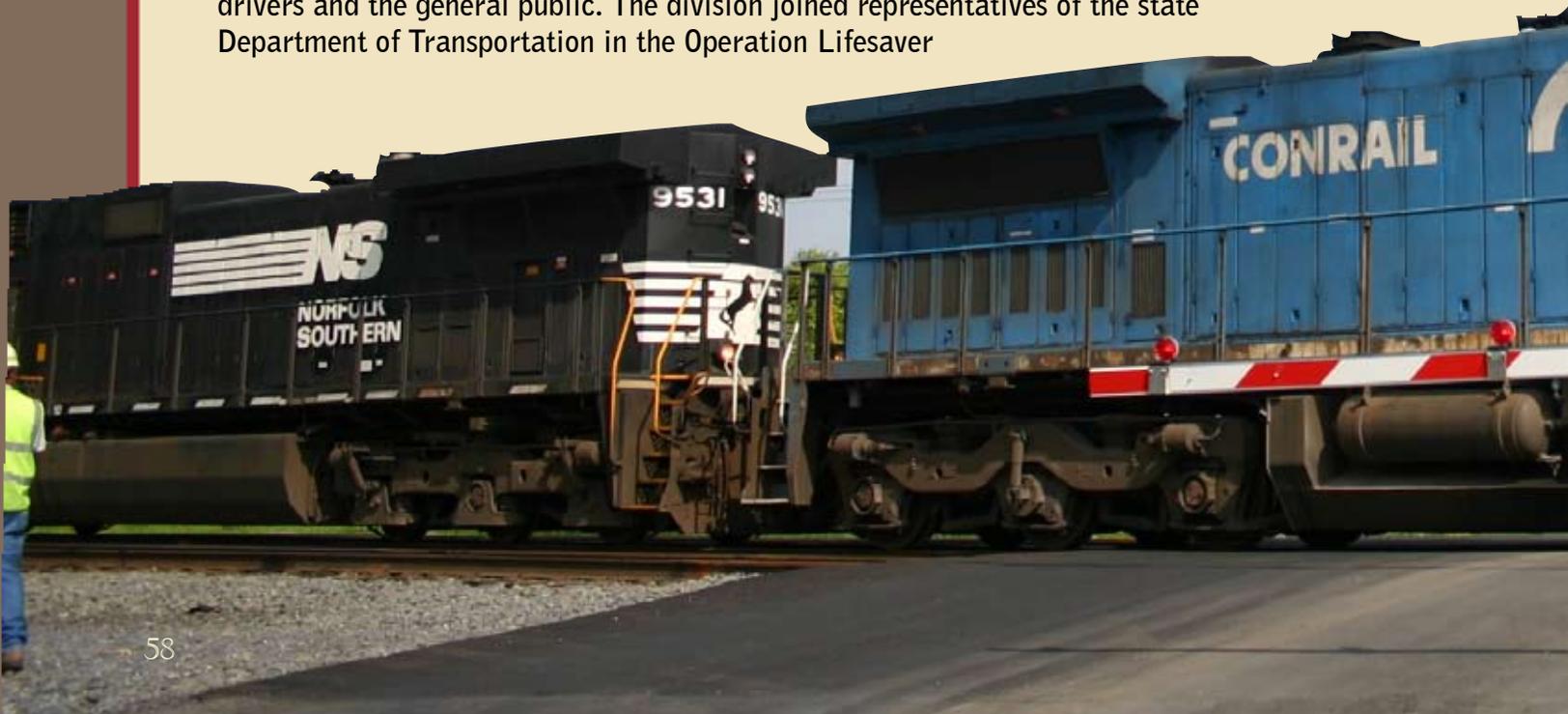
OPERATION LIFESAVER

The Rail Safety Division also is an active participant in the national Operation Lifesaver Program. Operation Lifesaver is a national non-profit public education program dedicated to eliminating collisions, deaths and injuries at highway-rail intersections and on railroad rights-of-way. In Fiscal Year 2005-06, the division conducted 17 presentations to various groups, including school students, school bus drivers and the general public. The division joined representatives of the state Department of Transportation in the Operation Lifesaver



**OPERATION
LIFESAVER®**

Pennsylvania



booth at the Pennsylvania State Farm Show, distributing informational brochures and discussing the dangers at highway-rail crossings and on railroad rights of way.

2005-06 INSPECTIONS

- 24,171 railroad car inspections
- 455 locomotive inspections
- 5,843 miles of railroad track inspected
- 414 operating practice inspections



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