

**BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

**Docket No. R-2010-2161694**

**PPL Electric Utilities Corporation**

**Statement No. 6**

**Direct Testimony of Douglas A. Krall**

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

2 A. My name is Douglas A. Krall. My business address is Two North Ninth Street,  
3 Allentown, Pennsylvania, 18101.

4

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

6 A. I am employed by PPL Electric Utilities Corporation (“PPL Electric” or the  
7 “Company”), a subsidiary of PPL Corporation, as Manager – Regulatory  
8 Strategy.

9

10 **Q. Please describe your primary responsibilities in that position.**

11 A. As Manager – Regulatory Strategy, I am responsible for assisting in the  
12 development of long-term strategy, goals and objectives; providing regulatory  
13 insights into the development and implementation of business strategies; and  
14 leading the development of responses to legislative, regulatory, and political  
15 issues.

16

17 **Q. What is your educational background?**

18 A. I graduated from Stevens Institute of Technology in Hoboken, New Jersey in  
19 1973 with a Bachelor of Engineering degree in Mechanical Engineering. I have  
20 completed courses in Business Administration at Muhlenberg College in  
21 Allentown, Pennsylvania.

22

23

1 **Q. Are you a registered Professional Engineer?**

2 A. Yes. I have been a registered Professional Engineer in the Commonwealth of  
3 Pennsylvania since 1977. My registration number is PE-026733-E.

4

5 **Q. Please describe your professional experience.**

6 A. I joined the Mechanical Engineering Department of PPL Electric's predecessor,  
7 Pennsylvania Power and Light ("PP&L"), in 1973 as an Engineer-Level I working  
8 on studies related to PP&L's generating plants. In 1974, the engineering  
9 functions were restructured and I became a member of the Power Plant  
10 Engineering Department. In 1975, I was promoted to the position of Engineer-  
11 Level II and, in 1978, to the position of Project Engineer within that department.  
12 Later in 1978, I transferred to the System Planning Department and, in 1981, I  
13 was promoted to the position of Senior Project Engineer. In both of those  
14 positions I was responsible for the development of plans related to maintaining  
15 and upgrading PP&L's existing fossil and hydro generating plants. In 1984, I was  
16 promoted to the position of Manager-Generation Development Planning within  
17 the System Planning Department with responsibility for the portion of PP&L's  
18 capital budget related to existing fossil and hydro generating plants as well as  
19 overall administrative responsibility for PP&L's capital budget. I also was, in that  
20 position, PP&L's coordinator for activities related to compliance with the 1990  
21 Federal Clean Air Act Amendments. In December 1994, my title changed to  
22 Manager-Integrated Resource Planning, but the duties remained relatively the  
23 same. In April 1996, I became the Manager-Resource Planning and Pricing. In

1 that capacity, I supervised the development of integrated resource plans, the  
2 administration of PP&L's responsibilities regarding non-utility generation, the  
3 development of PP&L's capital budget, and the development and administration  
4 of PP&L's tariff for electric service. When the Competition Act was passed in  
5 Pennsylvania in late 1996 and the pace of industry restructuring accelerated, my  
6 duties in this position changed rapidly. The generation and capital budgeting  
7 functions were moved to other organizations and, ultimately, to different affiliates.  
8 In their place, I took on new duties related to load analysis and coordination of  
9 activities within the regulated distribution entity to implement customer choice.  
10 In August 2001, I assumed my current position.

11  
12 **Q. Have you previously testified as a witness before the Pennsylvania Public**  
13 **Utility Commission ("PUC") or the Federal Energy Regulatory Commission**  
14 **("FERC")?**

15 A. Yes. I have testified before the PUC on numerous occasions, including the  
16 Company's restructuring proceeding (Docket No. R-00973954), three base rate  
17 proceedings (Docket Nos. R-00943271, R-00049255, and R-00072155), the  
18 Company's Competitive Bridge Plan for the procurement of default generation  
19 service (Docket No. P-00062227), Rate Stabilization Plan (Docket No. R-2008-  
20 2021776), Default Service Plan (Docket No. P-2008-2060309), Rate Mitigation  
21 Plan (Docket No. P-2009-2091280), Energy Efficiency and Conservation Plan  
22 (Docket No. M-2009-2093216), Smart Metering Plan (Docket No. M-2009-  
23 2123945), Time of Use filing (Docket No. R-2009-2122718), Purchase of

1 Receivables filing (P-2009-2129502), proceedings regarding non-utility  
2 generators, including the buy-out of a power purchase agreement with a non-  
3 utility generator and the impacts on the Company and its customers of existing  
4 power purchase agreements, and proceedings arising from customer complaints.

5 At the FERC, I have testified in regard to the Company's compliance plans  
6 under the 1990 Clean Air Act Amendments (Docket No. ER95-1267), and in  
7 regard to its investment in generating plants to serve its wholesale customers  
8 (Docket No. SC97-1-000).

9  
10 **Q. What is the purpose of your testimony in this proceeding?**

11 A. My testimony addresses the following:

- 12 1. The status of the Company's program to purchase receivables from  
13 competitive Electric Generation Suppliers ("EGSs") serving PPL Electric  
14 customers.
- 15 2. The allocation of the proposed revenue increase and rate design  
16 considerations.
- 17 3. The Company's consumer education and consumer programs that are  
18 reflected in this request.

1 **Purchase of Receivables (“POR”) from EGSs**

2 **Q. Please summarize your testimony with regard to the purchase of**  
3 **receivables from EGSs.**

4 A. The Company has maintained a form of POR program since the Commission’s  
5 approval of the Company’s restructuring settlement on August 27, 1998. In  
6 2009, as part of the settlement of the Company’s Petition for Approval of a  
7 Default Service Program and Procurement Plan for the Period January 1, 2011  
8 through May 31, 2014 (“Default Service Plan”), the Company agreed to file a  
9 revised POR plan as part of its next distribution rate case. In the absence of a  
10 rate case filing with an effective date of January 1, 2011, PPL Electric agreed to  
11 file a stand-alone POR plan to become effective on January 1, 2011. On May  
12 15, 2009, the Commission issued a Tentative Order identifying specific actions  
13 PPL Electric should take to reduce potential barriers to retail competition in the  
14 Company’s service territory. Among those actions was the filing of a POR  
15 program to be effective on January 1, 2010; a full year earlier than had been  
16 ordered in the context of PPL Electric’s Default Service Plan. In its Final Order  
17 regarding Retail Markets, the Commission stated that it would not be inconsistent  
18 for PPL Electric to file a POR plan to be effective January 1, 2010, and to still  
19 have the opportunity to revise that plan in a subsequent base rate case or stand-  
20 alone filing. The purpose of my testimony regarding POR is, first, to  
21 acknowledge PPL Electric’s obligation under its Default Service Plan to file a  
22 POR plan in this base rate proceeding to be effective January 1, 2011 and,  
23 second, to propose that the program filed by the Company on September 10,

1 2009 for the period January 1, 2010 through December 31, 2010, pursuant to the  
2 Retail Markets Order and approved by Commission order entered November 19,  
3 2009, be extended to operate beyond December 31, 2010. In his direct  
4 testimony, Statement No. 7, Mr. Kleha describes the calculation of the  
5 appropriate discount rates for purchasing EGS' accounts receivables and the  
6 Company's Merchant Function Charge for recovery of its generation supply-  
7 related uncollectible accounts expense from the residential and small commercial  
8 and industrial customer classes.

9  
10 **Q. Please provide an overview of the Company's original POR program.**

11 A. Pursuant to the Company's Restructuring Settlement, the Company administered  
12 a de facto POR program for EGSs offering retail supply in PPL Electric's service  
13 territory and using the consolidated billing option offered by PPL Electric.  
14 *Application of Pennsylvania Power & Light Company for approval of its*  
15 *Restructuring Plan under Section 2806 of the Public Utility Code, Docket No. R-*  
16 *00973954, Order entered August 27, 1998.* Under that program, PPL Electric  
17 paid an EGS the entire amount for undisputed EGS charges, regardless of  
18 whether or not the customer had paid the Company for up to a three-month  
19 period. Under that program, PPL Electric could not terminate service to a  
20 customer for the customer's failure to pay the EGS portion of its bill. In addition,  
21 PPL Electric could not terminate EDC consolidated billing, i.e., cause the  
22 customer to pay the EGS directly, unless the customer was in arrears for 90 days  
23 or three billing cycles, whichever was shorter. At that point, the EGS, after

1 having received three months of payments at a zero discount, became  
2 responsible for billing its own charges. The EGS was free to terminate its service  
3 to the customer if the customer failed to pay its bills. If the EGS chose to  
4 terminate its generation service, the customer would be returned to default  
5 generation service and PPL Electric would become responsible for the billing and  
6 collection of generation service charges.

7  
8 **Q. Please describe how this approach was revised pursuant to the Company's**  
9 **September 10, 2009 POR petition and subsequent Commission order.**

10 A. Under the POR program that became effective on January 1, 2010, the Company  
11 purchases EGS receivables for customers in its Residential and Small  
12 Commercial & Industrial ("Small C&I") Rate Classes at a discount from standard  
13 supply charges. The discounts are different for Residential and Small C&I  
14 customers. Each of the discount rates is composed of two components: (1) an  
15 uncollectible accounts expense percentage factor, and (2) a POR development,  
16 implementation, and administration percentage factor. In parallel, the Company  
17 instituted a Merchant Function Charge ("MFC") which "unbundles" from its  
18 distribution base rates the uncollectible accounts expense associated with  
19 generation supply. Under this construct, the Company continues to recover  
20 uncollectible accounts expense associated with non-generation supply-related  
21 delivery service from Residential and Small C&I customers through distribution  
22 rates. Uncollectible accounts expense associated with generation supply for  
23 Residential and Small C&I default service customers is separated from the

1 Company's distribution rates and is recovered through the MFC which, in turn, is  
2 included in the Generation Supply Charge. The MFC also is included in the Price  
3 To Compare ("PTC") that is reported by PPL Electric. Residential and Small C&I  
4 customers who sign-up with an EGS for generation supply do not pay the MFC.  
5 Large Commercial & Industrial ("Large C&I") customers continue to operate  
6 under the original POR construct.

7  
8 **Q. Please describe how PPL Electric administers the existing POR program.**

9 A. PPL Electric administers the existing POR program through a set of Electronic  
10 Data Interchange ("EDI") transactions that are defined and maintained by the  
11 PUC's Electronic Data Exchange Working Group ("EDEWG"). These  
12 transactions enable PPL Electric's customer information system to communicate  
13 directly with the information systems of EGSs for the purpose of assuring that  
14 customers are properly and timely enrolled with the generation supplier of their  
15 choice, timely and correctly billed for generation service, and customer payments  
16 are timely and accurately posted and remitted to the appropriate generation  
17 service provider. These transactions, and the processes they support, recognize  
18 that, in order to be successful, retail competition requires more than simply  
19 billing, but also maintaining accurate customer records and assuring the correct  
20 scheduling and settlement of energy through PJM.

1 **Q. Please describe how the EDI transactions support the existing POR**  
2 **program.**

3 A. When a customer elects to receive generation service from an EGS, the  
4 customer notifies the EGS of his election. The EGS then sends an EDI  
5 enrollment transaction to the Company. That transaction includes an identifier  
6 that tells the Company's customer information and billing system whether the  
7 customer will be billed for generation service directly by the EGS or whether the  
8 EGS will send its charges to the Company to be consolidated into a single bill to  
9 be rendered by the Company. The existing POR program relates only to the  
10 option wherein the Company consolidates its charges and an EGS' charges onto  
11 a single bill. In response to the EGS' enrollment transaction, the Company's  
12 customer information and billing system will mark the enrollment, the billing  
13 option, and other information on the customer's account, and create and transmit  
14 two communications. The first is an EDI transaction back to the EGS confirming  
15 the enrollment, the billing option, and other information. The second is a letter to  
16 the customer confirming his election of the EGS and billing option, the date when  
17 EGS service will commence, and offering the customer the opportunity to  
18 rescind. Assuming that the customer does not rescind his EGS election, the  
19 customer's account would, at this point, become part of the existing POR  
20 program.

21

22

23

1 **Q. Please describe the next steps in the existing process.**

2 A. On the next meter read after enrollment, the customer's bill will include default  
3 generation service charges from PPL Electric for the last time. Also, following  
4 that meter read, the EGS would begin to schedule energy on behalf of the  
5 customer. At the next meter read, the Company's customer information and  
6 billing system will create another EDI transaction and transmit it to the EGS.  
7 That transaction will provide the EGS the customer's usage for the billing period  
8 so that the EGS can calculate charges for its service. Upon calculation of its  
9 charges, the EGS creates an EDI transaction which it transmits back to PPL  
10 Electric. This transaction tells the Company's customer information and billing  
11 system the generation charge to be printed on behalf of the EGS on the  
12 consolidated bill that PPL Electric will prepare and render to the customer. PPL  
13 Electric is required to keep the billing window open for up to three days to allow  
14 for these steps to be completed. When PPL Electric renders a bill with EGS  
15 charges, the Company takes on the obligation to remit the total amount for  
16 generation charges less the appropriate discount to the EGS within 25 days for  
17 residential customers and 20 days for non-residential customers, regardless of  
18 whether the customer pays the Company or not. On the date payment is due to  
19 the EGS, i.e., either 25 or 20 days from the date the bill is sent to the customer,  
20 the Company's customer information and billing system will initiate payment of  
21 the appropriate amount to the EGS and an EDI transaction to confirm that  
22 payment.

23

1 **Q. Does the Company's POR program accommodate budget billing?**

2 A. Yes, it does. In the event that the EGS offers budget billing for its charges, the  
3 EGS will send to the Company an amount to be printed on the bill that reflects  
4 the EGS' budget amount, however, the EDI transaction will still indicate the total  
5 amount less the discount. That is the amount that PPL Electric is obligated to  
6 remit to the EGS.

7

8 **Q. Was this a difficult change to implement?**

9 A. Yes. The Company undertook a significant number of programming and business  
10 process changes in order to implement this POR program. The first change was  
11 to reprogram the Company's customer information and billing system so that it  
12 can recognize two different POR programs – the previous program for Large C&I  
13 customers and the revised program for all other customers. For those accounts  
14 that are eligible to be part of the revised program (i.e., Residential and Small C&I  
15 accounts), the Company needed to program the Merchant Function Charge,  
16 include it in the generation service portion of the bill, assure that it can be  
17 isolated and tracked separately from the reconcilable portions of the Generation  
18 Supply Charge, and assure that it is not charged to customers who are taking  
19 service from an EGS. The processing of EDI transactions was modified to  
20 identify that the EDC consolidated billing option indicator triggers different POR  
21 programs for different customer classes. The EDI transactions themselves were  
22 modified to add new fields necessary to accommodate budget billing and the  
23 Company modified its programming for the tracking and management of

1 individual account balances to remove the logic that causes a customer who is  
2 90-days in arrears to be converted to dual bill, to properly reflect purchased  
3 generation supply-related receivables in the Company's collections systems, and  
4 to accommodate the possibility of an EGS budget amount. Finally, the Company  
5 implemented programming to track, separately, the billings, remittances, and  
6 balances by age of participants in the proposed program in order to track and  
7 manage the program and assure that the proper discount rate is being used  
8 going forward.

9  
10 **Q. How large was the programming effort?**

11 A. This was a very significant effort in terms of the amount of resources invested,  
12 the short time frame, the criticality of the systems modified, and the timing of the  
13 work. In terms of resources, the Company expended about 1,500 man-hours of  
14 effort and \$150,000. The Company began efforts to develop the scope of the  
15 work at the time it filed the petition in early September 2009 and continued to  
16 make final modifications through March, 2010. In terms of criticality, the systems  
17 impacted are among the most critical in the Company's customer information and  
18 billing system, because they involve the collections process at the individual  
19 customer level and revenue reporting. If the systems do not work correctly,  
20 individual customers may be negatively impacted and the Company's ability to  
21 comply with accounting rules, including Sarbanes-Oxley requirements, may be  
22 jeopardized.

23

1 **Q. Did EGSs participate in the implementation?**

2 A. Yes, they did. The EGSs participated actively in the litigation of the Company's  
3 proposal and they, along with other parties, entered into a settlement that  
4 resolved all but two issues. As part of the Settlement, the Company agreed to  
5 hold bi-weekly conference calls up to December 31, 2009 with the parties to  
6 report on the status of its implementation of the POR program. Those calls  
7 actually continued into 2010 as programming complexities were encountered and  
8 the EGSs participated actively in helping to resolve some of the issues  
9 encountered.

10

11 **Q. Please describe why the Company believes that no further changes are**  
12 **required to its POR program.**

13 A. The Company believes that, as a result of its extensive interactions with EGSs in  
14 the implementation of this program, the program currently in place is well  
15 understood by the EGSs and is able to meet most of their needs. The Company  
16 also believes that, because of the complexity of customer information and billing  
17 systems, any revision to the existing program is likely to involve as much effort  
18 and place the original modifications at risk. The Company already has identified  
19 the need to modify these same systems to accommodate rate changes that have  
20 been committed to and which must be implemented on January 1, 2011, as well  
21 as rate-ready billing, EGS Consolidated Billing, certain parts of its Act 129 Smart  
22 Meter Plan, and modifications to allow the calculation of a single budget amount  
23 that reflects the sum of delivery charges and EGS charges. The Company

1 remains concerned that all of this work being done in a relatively short timeframe  
2 creates a situation in which programmers working on one functionality may be  
3 relying on programming that they are unaware is being changed by a  
4 programmer working on another functionality. As noted above, if these critical  
5 systems do not work correctly, individual customers may be negatively impacted  
6 and the Company's ability to comply with accounting rules, including Sarbanes-  
7 Oxley requirements, may be jeopardized.

8  
9 **Allocation of the Revenue Increase and Rate Design Principles**

10 **Q. Please summarize your testimony with regard to the allocation of the rate**  
11 **increase and rate design principles.**

12 A. My testimony in this regard covers two areas. These are:

- 13 1. The principles that guided the allocation of the increase include the  
14 Company's adherence to the Commonwealth Court decision in the matter of  
15 Lloyd vs. PA. Public Utility Commission 904 A.2d 1010 (Pa. Commonwealth  
16 2006) that remanded to the Commission its order, at Docket No. R-00049255,  
17 regarding PPL Electric's 2004 request for a base rate increase; the  
18 Commission's Order, entered on July 25, 2007, regarding the issues that had  
19 been remanded to the Commission by the Court at Docket No. R-00049255;  
20 and, the Commission's Order, entered December 6, 2007, regarding PPL  
21 Electric's 2007 request for a base rate increase at Docket No. R-00072155.

1           2. The Company's efforts to create rate designs that recover fixed costs through  
2           fixed charges and those costs that vary as a function of usage through usage  
3           charges.

4  
5   **Q.    Please summarize the series of cases and orders that bear on the revenue**  
6   **allocations that the Company proposes in this proceeding.**

7   A.    PPL Electric historically has allocated revenue increases based on the results of  
8    a class cost-of-service study, with a goal of moving the return of each rate  
9    schedule toward the system average return on a relative rate of return basis.  
10   These allocations always were subject to the principle of gradualism in order to  
11   avoid disparate increases to particular rate schedules. In its 2004 request for a  
12   base rate increase (Docket No. R-00049255), PPL Electric allocated the  
13   proposed revenue increase in a way that moved each rate schedule toward  
14   the system average return, with the constraint that no rate schedule receive an  
15   increase of more than 10% on a total bill basis, i.e., generation, transmission,  
16   CTC, ITC and distribution rates. The Commission approved this approach  
17   (Order entered December 22, 2004 at Docket No. R-00049255), but it was  
18   rejected by the Commonwealth Court. Specifically, the Court held, in its August  
19   4, 2006 decision, that it was not appropriate to consider the total bill impact in  
20   allocating a distribution rate increase, and that the Company had incorrectly  
21   allowed the principle of gradualism to "trump" all other considerations, particularly  
22   the cost of providing service, which the Court described as the "polestar" for rate  
23   design issues.

1           On February 8, 2007, the Commission entered an order which remanded  
2 the matter to the Office of Administrative Law Judge for the conduct of  
3 proceedings to resolve the issues raised by the Lloyd decision. Those  
4 proceedings resulted in the development among the parties of a Joint Petition for  
5 Settlement, which subsequently was approved by Commission Order entered on  
6 July 25, 2007. The Joint Petition for Settlement provided the following with  
7 regard to the allocation of the increase in distribution revenues:

- 8           • The allocations previously approved in 2004 were revised to significantly  
9           accelerate movement of the rate classes to the full cost of providing  
10           service.
- 11           • A rider was established to refund and recoup the differences between the  
12           distribution charges approved by the Commission in its December 22,  
13           2004 Order and those established in the Settlement.
- 14           • The Company committed, subject to certain caveats, to a plan to move its  
15           distribution rates to “at or near” the full cost of providing service over a  
16           series of three rate cases with the 2004 case, as adjusted by the  
17           Settlement, as the first case in that series. The Company’s 2007 request  
18           for a base rate increase was to be the second case in the series, and this  
19           case represents the third case.

1 **Q. Please describe how the Company proposes to allocate the distribution**  
2 **rate increase in this proceeding.**

3 A. Consistent with its prior commitment in the Settlement, PPL Electric has sought  
4 to allocate the increase in a way that is consistent with regulatory practice and  
5 precedent, including the Lloyd decision and the Commission's order on remand  
6 approving settlement of that case, and which reasonably balances the interests  
7 of the various rate classes and does not result in undue rate discrimination.

8  
9 **Q. Please elaborate on what is meant by "at or near full cost of service".**

10 A. Paragraph 20 of the Settlement states, "PPL Electric also proposed to move its  
11 distribution rates for all major rate classes to at or near full cost of service over  
12 the course of three rate cases including the 2004 rate case." The Commission  
13 order entered July 25, 2007 that approved the Settlement also admitted into  
14 evidence specific pieces of testimony, including PPL Electric Statement No.  
15 Remand – 1, the Remand Direct Testimony of Douglas A. Krall. Pages 11 and  
16 12 of Statement No. Remand – 1 include the following:

17 "The Company proposes to move its distribution rates for all major rate  
18 classes to at or near full cost of service in three rate cases, including the  
19 2004 rate case. Specifically, the Company proposes to maintain the  
20 distribution rates approved in this case (with an adjustment to remove  
21 storm damage costs) which, in fact, resulted in meaningful movement  
22 toward cost of service on a relative rate of return basis for major rate  
23 classes; move one-half of the remaining difference in its recently filed  
24 2007 rate case; and move to full cost of service in its next case after that.  
25 There are three caveats. First, for certain rate classes, most notably Rate  
26 Schedule RTS (Residential Thermal Storage) and street lighting rates, one  
27 or two more rate cases may be required because these rates currently are  
28 so far below cost of service that it would take very disproportionate  
29 increases to move them to full cost of service in three rate cases. Second,  
30 as explained by Mr. Kleha, cost of service is an art, not a science, and

1 while the Company will attempt to move rates reasonably close to full cost  
2 of service, some modest differences may remain. Finally, the Company  
3 would reserve the right to apply principles of gradualism to  
4 ameliorate individual customer rate impacts to the extent necessary in  
5 future proceedings.”  
6

7 **Q. Please describe the process used to allocate the revenue requirement**  
8 **among rate classes.**

9 A. Mr. Kasper initially allocated the revenue requirement among rate classes in  
10 strict accordance with Mr. Kleha’s cost-of-service study. The resultant  
11 requirements were then reviewed, consistent with the Remand Settlement, for  
12 the purpose of identifying disproportionate increases and disparate results. That  
13 review identified the following conditions:

- 14 - This initial allocation process would have resulted in the residential class  
15 receiving a rate increase well in excess of the total increase requested in  
16 this case and all other rate classes would have received substantial rate  
17 decreases.
- 18 - This initial allocation process resulted in customers on Rate Schedule  
19 RTS experiencing an increase in their distribution rate of about 200%.

20  
21 **Q. How did PPL Electric address these disparate and disproportionate**  
22 **results?**

23 A. As described in his testimony (Statement No. 8), Mr. Kasper reallocated the  
24 revenue requirements in a manner that allocated the entire proposed rate  
25 increase to residential customers and allocated no rate increase or decrease to  
26 all other customer groups. Then, working within the residential class, Mr. Kasper

1 limited the allocation of revenues to customers on Rate Schedule RTS to the  
2 amount necessary to bring them from a position of minus 54% of system average  
3 return at present rates to a position of approximately 0% of average system  
4 return at proposed rates. This resulted in reducing the increase in distribution  
5 rates for Rate Schedule RTS customers from about 200% to about 60%. The  
6 revenue requirements not recovered from Rate Schedule RTS customers were  
7 reallocated to customers on Rate Schedule RS.

8  
9 **Q. Is this proposed allocation consistent with the results of Mr. Kleha's cost of**  
10 **service study?**

11 A. Yes, it is. As shown in Appendix C to Mr. Kasper's testimony (Statement No. 8),  
12 while this allocation does not perfectly match the results that would be achieved  
13 by strict adherence to the cost-of-service study, it does result in substantial  
14 movement of all rate classes towards system average rate of return.

15  
16 **Q. Aren't these results still somewhat disparate and disproportionate?**

17 A. One might argue that the increase in rates should be more evenly spread among  
18 customer classes, however, the Company believes that this approach is  
19 consistent with the requirement in the Remand Settlement that, in this third step,  
20 the Company propose rates that move the classes reasonably close to full cost of  
21 service, while not introducing disparity and disproportionate impacts among the  
22 classes.

23

1 **Q. Might it be argued that the resultant rates are not reasonably close to full**  
2 **cost of service?**

3 A. That is also true; however, the Settlement agreed to by all parties did not set  
4 numerical limits on the resultant rates, but, instead, specifically recognized that,  
5 at the end of the third step, rates might still only be “near” the point that would  
6 otherwise result from strict adherence to cost of service results. In addition,  
7 several other points need to be considered in determining whether the proposed  
8 allocation of the increase is consistent with cost-of-service principles.

9 First, as noted above and reiterated in the direct testimony of Mr. Kleha  
10 (Statement No. 7), cost-of-service is an art, not a science, and there is clearly no  
11 universally accepted methodology for conducting such studies. There are many  
12 different methods of conducting cost allocation studies, and these methods can  
13 produce markedly different results. Mr. Kleha describes in his testimony an  
14 analysis he performed of three hypothetical cost allocation studies, each of which  
15 employed a different approach to the classification of distribution system costs.  
16 The results of this analysis are set forth in Exhibit JMK 5. The first of these  
17 classifies distribution costs as 50% customer-related and 50% demand-related  
18 and produces results that are very close to those achieved using the Company’s  
19 methodology. The second approach classifies distribution costs as 50%  
20 demand-related and 50% energy-related and results in a significant shift of costs  
21 away from residential customers and toward commercial and industrial  
22 customers. The third approach classifies distribution system costs as one-third  
23 customer-related, one-third demand-related and one-third energy-related. As

1 expected, the results of this approach, which also shifts costs away from  
2 residential customers and toward commercial and industrial customers, are  
3 between the other two. Looking at the range of results produced by these three  
4 studies, each of which begins with assumptions that, while different, are not  
5 unreasonable, I believe it is reasonable to conclude that the allocation proposed  
6 by the Company reasonably reflects cost-of-service and fully complies with the  
7 Lloyd decision and the settlement of the case on remand.

8           Second, at the time of the Settlement, the parties did not know the  
9 outcome of the second step of the process (the 2007 request for an increase in  
10 base rates). As it turned out, that request was settled in a “black box” process  
11 that produced agreement on certain specific rate results, but did not specify a  
12 system rate of return, the use of any particular cost allocations, or establish the  
13 contribution of any customer class to a system rate of return.

14           Third, at the time of the Settlement, the parties could not have known with  
15 certainty the conditions that would be faced in the allocation of costs in a future  
16 base rate proceeding whose filing date was unknown. Among the significant  
17 uncertainties were the amount of new costs that would be incurred, on behalf of  
18 which customer groups those costs would be incurred, and the numbers of  
19 customers, the sales, and the demands that would exist at the time of that future  
20 proceeding.

1 **Q. In the allocation of costs in this proceeding, did the Company allow cost-**  
2 **of-service principles to be overshadowed by other considerations?**

3 A. No, it did not. In the opinion of Commonwealth Court, the Company did allow  
4 cost-of-service principles to be “trumped” by other considerations in 2004;  
5 specifically, the objective of holding the increase for all customer groups on a  
6 total bill basis to less than 10%. In its decision, the Court acknowledged that  
7 other factors can and should be considered, but cost-of-service principles must  
8 be the “polestar” in the rate-making process. In this case, the Company sought,  
9 in the first instance, to employ only cost-of-service principles. Other factors were  
10 brought into play only to the extent necessary to avoid disparate and  
11 disproportionate results among rate classes.

12  
13 **Q. Please describe the adjustment made in allocating costs to Rate Schedule**  
14 **RTS.**

15 A. The situation with Rate Schedule RTS is actually identified in the record  
16 supporting the Settlement language, so this result is not unexpected. Rate  
17 Schedule RTS was established in the early 1980s and was designed to provide a  
18 rate incentive to customers who chose to install electric space and water heating  
19 with thermal storage capability. Residential thermal storage systems enable  
20 customers to charge their heating systems during a self-selected off-peak period.  
21 Off-peak time period options were 5 PM to 7 AM, 6 PM to 8 AM, and 7 PM to 9  
22 AM; although virtually all participants selected the 5 PM to 7 AM option. As  
23 initially designed, the rate schedule reflected a bundled rate that consisted of a

1 monthly charge, a \$/kW demand charge for on-peak demands in excess of 2 kW,  
2 and a cent/kWh charge for all kWh. When rates were unbundled pursuant to the  
3 Company's Restructuring Settlement at Docket No. R-00973954, the distribution  
4 component included the monthly charge and a portion of the demand charge, the  
5 generation component included both a demand charge and a usage charge, and  
6 the transmission and stranded cost recovery (both the Competitive Transition  
7 Charge and the Intangible Transition Charge) components were simply usage  
8 charges. Rate Schedule RTS was closed to new participants as of December  
9 31, 1995 in anticipation that deregulation of electricity markets would alter the  
10 economics underlying the rate schedule and necessitate changes. In its 2004  
11 base rate case, the Company continued the basic structure of the Rate Schedule  
12 RTS distribution charge, but sought to increase revenue recovery in order to  
13 achieve a rate of return closer to the system average rate of return. In its 2007  
14 base rate case, the Company again sought to increase the revenue recovery to  
15 move closer to system average rate of return, consistent with the second-step of  
16 movement dictated by the Lloyd decision and, also, in anticipation that the  
17 installation of smart meters for all customers and the expiration of the generation  
18 rate caps would blur the distinctions between service under Rate Schedule RS  
19 and Rate Schedule RTS, proposed changing the structure of the distribution rate  
20 to more closely model the monthly charge and three-usage-block structure of  
21 Rate Schedule RS. In this case, the Company has sought to make the Rate  
22 Schedule RS and Rate Schedule RTS distribution charges identical. However,  
23 because the cost allocation reflects demand and because these customers have

1 a very significant coincident demand at 5 PM when most of the systems begin  
2 charging, the allocation of revenue requirements actually should result in higher  
3 distribution charges than those for customers on Rate Schedule RS. While that  
4 result may be analytically correct, it makes no logical sense as these customers  
5 gradually move toward being provided the same service as any other residential  
6 customer. This is consistent with the fact that, with the expiration of the  
7 generation rate caps on January 1, 2010, Rate Schedule RTS customers now  
8 have flat generation rates that do not vary with time and the Company has  
9 advised these customers that they no longer need to be concerned about their  
10 demand during a specific on-peak period. Accordingly, the revenue allocation for  
11 these customers is limited by the rate design which reflects the same monthly  
12 charge as is proposed for Rate Schedule RS and flat cent per kWh pricing of  
13 usage designed to recover sufficient revenues to achieve a 0% contribution to  
14 system average return.

15

16 **Q. Are there other cost allocation assumptions that are worthy of note?**

17 A. Yes, there are. Again, with the expiration of the generation rate caps and the  
18 movement of previously regulated products to the competitive market, the  
19 Company is proposing to combine the revenue allocations for its Large Power –  
20 Primary customers (Rate Schedules LP-4 and IS-P) and to combine the revenue  
21 allocations for its Large Power – Transmission customers (Rate Schedules LP-5,  
22 LP-6 and IS-T). Rate Schedules IS-P and IS-T date back to the middle 1980's  
23 and provided customers the option of interruptible service. In its Restructuring

1 Settlement, the Company closed both rate schedules to new customers and  
2 unbundled the rates of then-existing customers within the distribution and  
3 generation rate caps. The Company no longer offers an interruptible default  
4 service. Most of the customers have left the rate schedules with only six being  
5 served under Rate Schedule IS-P and one being served under Rate Schedule  
6 IS-T. There is no logical basis to allocate revenues differently for these  
7 customers than any other customer served at the same voltage level. In the  
8 case of Rate Schedule LP-6, it currently serves only two customers and, again,  
9 there is no logical basis to allocate revenues differently for these customers than  
10 any other customer served at the same voltage level.

11

12 **Q. Please describe the principles that have guided the Company's**  
13 **development of the rate designs it proposes in this proceeding.**

14 A. The fundamental principle employed to guide the design of rates was, consistent  
15 with the nature of distribution service, to move from revenue collection through  
16 usage-based charges to revenue collection through fixed charges. There are  
17 very few, if any, distribution system-related costs that are a function of usage.  
18 PPL Electric's minimum system study indicates, for example, that residential  
19 customers ought to be paying a monthly customer charge in excess of \$30 as  
20 compared to the current monthly charge of \$8.44. As a matter of correct  
21 economics, it is appropriate, from the perspective of customers, utilities, and the  
22 Commonwealth, to collect fixed costs on a fixed-charge basis. In addition, the  
23 usage blocks in the Company's present distribution rates are priced in a manner

1 that declines as usage increases. In the proposed rate designs, the Company  
2 has priced usage blocks that remain in the proposed rate designs at a flat cent  
3 per kWh rate. Such an approach removes an incentive to increase use and is  
4 consistent with the Commission's directive to remove declining block designs  
5 from the PTC (Default Service and Retail Electric Markets, Final Policy  
6 Statement entered May 10, 2007 at Docket No. M-00072009 adding Section  
7 69.1810 to Title 52 of the Pa. Code).

8  
9 **Q. Please describe why this is important from the perspective of customers.**

10 A. This becomes particularly important when a customer considers different options  
11 for the generation portion of his/her bill and also when a customer considers  
12 investments in conservation and energy efficiency. Both a customer's buying  
13 decision with regard to generation and the decision to invest in conservation and  
14 energy efficiency are fundamentally functions of usage. Both of those decisions  
15 can be distorted when non-usage-related components are being collected on a  
16 usage basis. Moving the collection of distribution costs from a usage basis to a  
17 fixed basis will make the savings available from EGS options more clear to  
18 customers and promote competition. Similarly, moving the collection of  
19 distribution costs from a usage basis to a fixed basis will make the savings  
20 available from investments in conservation and energy efficiency clearer to  
21 customers. Additionally, the "flattening" of the usage charges that remain will  
22 encourage customers to engage in conservation and energy efficiency. But  
23 even beyond the selection of an alternative supplier or investment in

1 conservation and energy efficiency, one of the broad goals of restructuring  
2 always has been to make customers aware, through rates, of the consequences  
3 of their generation buying preferences. These include not just price, but also the  
4 amount of consumption, the use of different energy sources, and the burden  
5 those choices place on the environment. Moving the collection of distribution  
6 costs from a usage basis to a fixed basis will help to clarify these issues for  
7 customers as well.

8  
9 **Q. Doesn't a customer have more incentive to undertake conservation and**  
10 **energy efficiency measures if the usage charges are greater?**

11 A. It is true that the greater the usage charges the more incentive customers have  
12 to make investments to avoid them. However, to the extent that demand charges  
13 remain, there is still an incentive to undertake conservation and energy efficiency  
14 and, in the Company's proposed rates for residential customers, the kWh  
15 charges that remain should actually incent additional conservation and energy  
16 efficiency measures, as compared to the present rates. Finally, the continued  
17 collection of a significant portion of distribution costs through inappropriate usage  
18 charges means that customers who undertake conservation and energy  
19 efficiency and, thereby, avoid contributing to the recovery of distribution costs are  
20 simply shifting those costs from themselves to others. In the process, they are  
21 harming utility investors because the utility's rate of return will be reduced until  
22 rates can be reset in a future base rate proceeding.

23

1 **Q. What issue does this create for the Commonwealth?**

2 A. Section 410(a) of the American Recovery and Reinvestment Act of 2009  
3 (“ARRA”) authorizes grants to States which meet certain criteria including having  
4 in place “...a general policy that ensures that utility financial incentives are  
5 aligned with helping their customers use energy more efficiently and that provide  
6 timely cost recovery and a timely earnings opportunity for utilities...”. The  
7 practice of collecting fixed costs through usage-based charges with true-up  
8 occurring only on the occasion of a base rate proceeding actually penalizes the  
9 investors of utilities that promote conservation and energy efficiency programs to  
10 their customers. Such a practice is not consistent with Federal policy, as  
11 articulated in the ARRA, and could put the receipt of current or future Federal  
12 funds at risk.

13  
14 **Q. How has PPL Electric addressed this issue in this filing?**

15 A. PPL Electric has, where appropriate, designed distribution rates that increase the  
16 proportion of revenues that are collected through either customer charges or  
17 demand charges, and has reduced the proportion that are collected through kWh  
18 charges. Mindful that such a re-design can introduce significant changes among  
19 usage levels within rate schedules, PPL Electric proposes, consistent with the  
20 principle of gradualism, modest changes in this regard. For example, although  
21 PPL Electric is proposing an increase in the customer charge in residential Rate  
22 Schedule RS from \$8.44 per month to \$15.38 per month, it is well short of the  
23 \$30 per month or more that can be justified based on the minimum system study.

1 The \$15.38 per month customer charge is the amount that results from keeping  
2 revenue collection through the per kWh charges at the current level. In this way,  
3 the proposed rate design is able to satisfy the objective of moving toward fixed  
4 collections while not reducing the incentive for customers to undertake  
5 conservation and energy efficiency improvements. The flattening of the usage  
6 charges will actually increase the conservation and energy efficiency incentive for  
7 residential customers who use more than 200 kWh per month.

### 8 9 **Consumer Education and Consumer Programs**

10 **Q. Does the Company's filing include funding to provide consumers with**  
11 **programs and education to help them use electricity more wisely?**

12 A. Yes, it does. By Final Order entered July 18, 2008 at Docket No. M-2008-  
13 2032279, the Commission approved PPL Electric's Consumer Education Plan for  
14 2008-2012 submitted in compliance with the Commission's Final Order at Docket  
15 No. M-00061957 entered May 17, 2007. As noted in the Order, the Company  
16 was approved to spend slightly more than \$5 million per year in each year of the  
17 plan on consumer education and programs under the following headings:

- 18 - Customer choice education;
- 19 - Energy efficiency education and demand side response;
- 20 - Education efforts regarding Meter Data Management, Energy Analyzer,  
21 customer rate options, and customer choice; and
- 22 - Energy efficiency programs.

1 As further noted in the Final Order, the Company had identified these efforts in its  
2 2007 Distribution Rate Case and they were approved as part of the Settlement of  
3 that case. In this case, the Company reaffirms its commitment to these efforts  
4 and has included the amounts called out in the Consumer Education Plan in its  
5 future test year O&M requirement.

6 **Q. How do these efforts relate to the Company's efforts under Act 129 of**  
7 **2008?**

8 A. These programs predate Act 129 and are separate from the Company's Energy  
9 Efficiency and Conservation Plan (Docket No, M-2009-2093216) and the  
10 Company's Smart Meter Plan (Docket No. M-2009-2123945).

11

12 **Q. Does this conclude your direct testimony?**

13 A. Yes, it does.