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September 2, 2010

BY E-FILE

Rosemary Chiavetta
Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street, 2nd Floor North
P.O. Box 3265
Harrisburg, PA 17105-3265

RE: Pennsylvania Public Utility Commission v. PPL Electric Utilities Corporation
Docket No. R-2010-2161694

Dear Secretary Chiavetta:

Enclosed please find the original Initial Brief of PPL Electric Utilities Corporation in the above-referenced proceeding.

Copies have been provided to the persons in the manner indicated by the certificate of service.

Respectfully Submitted,

John H. Isom

JHI/jl
Enclosures
cc: Honorable Susan D. Colwell
Certificate of Service

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the **Initial Brief of PPL Electric Utilities Corporation** has been served upon the following persons, in the manner indicated, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant).

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John H. Isom

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:	
	:	
v.	:	Docket Nos. R-2010-2161694, *et al.*
	:	
PPL Electric Utilities Corporation	:	
	:	

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MISCELLANEOUS

I. INTRODUCTION

PPL Electric Utilities Corporation ("PPL Electric" or the "Company") provides electric distribution services to approximately 1.4 million customers in a certificated service territory that spans approximately 10,000 square miles in all or portions of 29 counties in eastern and central Pennsylvania. PPL Electric Ex. 1, Exhibit Regs. § 53.53, I-B-1. PPL Electric is a "public utility" and an "electric distribution company" as those terms are defined under the Public Utility Code, 66 Pa.C.S. §§ 102 and 2803.

In this proceeding, PPL Electric requests Pennsylvania Public Utility Commission ("Commission") approval of a distribution rate increase, with an anticipated effective date of January 1, 2011. The distribution rate increase reflects PPL Electric's status as a distribution only electric utility and is based on financial and operating data for that single business line. The requested rate increase reflects the business environment the Company currently faces, particularly its need to make significant capital investments to ensure that it is able to continue to provide safe and reliable service to its customers. PPL Electric St. 1, p. 10.

Based on the results of a class cost allocation study and the requirements of the Commonwealth Court's decision in *Lloyd v. Pa. P.U.C.*, 904 A.2d 1010, 1020 (Pa. Cmwlth. 2006) *appeal denied*, 591 Pa. 676, 916 A.2d 1104 (2007) (*"Lloyd"*), the Company proposes to allocate the entire increase to the residential class with no proposed rate increase for commercial and industrial customers. The proposed rates are designed to reflect cost of service for each rate class and to reduce cross subsidization of rate classes. PPL Electric St. 1, pp. 4-5.

As set forth in the Joint Petition for Partial Settlement ("Settlement") filed on August 26, 2010, and in the various statements in support thereof, the parties have achieved settlement on all revenue requirement, universal service, and residential rate design issues. Revenue allocation, non-residential rate design, and certain tariff and competitive issues as specified in the proposed

Settlement have been reserved for resolution by Administrative Law Judge Susan D. Colwell (the "ALJ") and the Commission. PPL Electric will address herein each of the issues reserved for litigation.

A. STATEMENT OF THE CASE

On March 31, 2010, PPL Electric filed with the Commission Supplement No. 83 to its Tariff-Electric Pa. P.U.C. No. 201 ("Supplement No. 83"), to become effective on June 1, 2010, together with supporting data, written testimony and exhibits. In Supplement No. 83, PPL Electric proposed a general increase in distribution base rates designed to produce approximately $114.7 million in additional annual base rate operating revenues based upon a future test year ending December 31, 2010, as adjusted for ratemaking purposes.

Supplement No. 83 was suspended by operation of law pursuant to Section 1308(d) of the Public Utility Code, 66 Pa.C.S. § 1308(d), for up to seven months, or until January 1, 2011, unless permitted by Commission Order to become effective at an earlier date. By Order entered May 20, 2010, the Commission initiated an investigation of PPL Electric's proposed general rate increase. In the Order, the Commission also noted several issues of concern and asked the parties to address these issues. The matter was assigned to the Office of Administrative Law Judge, and ALJ Colwell was assigned to preside over the proceeding.

The Office of Trial Staff ("OTS") filed a Notice of Appearance. Complaints against the proposed rate increase were filed by the Office of Consumer Advocate ("OCA"), the Office of Small Business Advocate ("OSBA"), PP&L Industrial Customer Alliance ("PPLICA"), Eric Epstein, Dr. Elaine F. Wasilawski, Elaine and Clayton Andrews, Jr., Ashley Buck, Elaine B. Santarelli, Gerard Martin, Peter Grieger, Linda M. Johnson, Stephen F. Goldstein, Eugene R.

Ruoff, Shannon Stiffler, and the Township of Whitehall.[1] Petitions to Intervene were filed by Richards Energy Group, Inc. ("REG"), Sustainable Energy Fund of Central Eastern Pennsylvania ("SEF"), Commission on Economic Opportunity ("CEO"), Dominion Retail, Inc., Washington Gas Energy Services, Inc., Citizens for Pennsylvania's Future, International Brotherhood of Electric Workers, Local 1600 and Retail Energy Supply Association ("RESA"). In addition, various customers filed Protests to the requested distribution rate increase.

An initial Prehearing Conference was held on May 26, 2010. Parties participating in the Prehearing Conference filed Prehearing Memoranda identifying potential issues and their expected witnesses. At the Prehearing Conference, the parties proposed a procedural schedule, which was adopted by the ALJ. In addition, the parties agreed to, and the ALJ approved, modified discovery rules for the above-captioned proceeding, which included shorter response times than those provided for in the Commission's regulations at 52 Pa. Code §§ 5.321 *et seq.*

In the Second Prehearing Order, dated May 27, 2010, the ALJ set forth the litigation schedule for the proceeding and the revised periods for responding to discovery requests. In addition, the ALJ listed the parties who had filed notices of intervention, petitions to intervene and complaints. The ALJ also granted the Petitions to Intervene of RESA, REG, IBEW, CEO, Dominion, SEF, and PennFuture. Further, the ALJ indicated that the parties had agreed that there should be five public input hearings, which were held on June 14, 2010, in Scranton and Wilkes-Barre, on June 21, 2010, in Bethlehem and Allentown, and on June 23, 2010, in Harrisburg.

The parties engaged in substantial formal and informal discovery in support of their respective positions. PPL Electric responded to more than 630 discovery requests, many of

[1] A complaint was also filed by Donald L. Foreman, which was withdrawn on June 28, 2010.

which had multiple subparts. In addition, substantial discovery requests were propounded to other parties.

On June 29, 2010, parties other than PPL Electric served their direct evidence, including testimony and exhibits. In addition, PPL Electric served supplemental testimony addressing the issues in which the Commission had expressed concern in its Order entered on May 20, 2010. On July 27, 2010, PPL Electric, OTS, OCA, OSBA, and PPLICA served rebuttal testimony and exhibits. The OTS, OCA, OSBA, PPLICA, SEF, and RESA served surrebuttal testimony and exhibits on August 5, 2010. On August 9, 2010, PPL Electric served rejoinder testimony and exhibits.

The parties held multiple settlement conferences to attempt to resolve amicably the issues in the case. These conferences resulted in a settlement of certain but not all of the issues in this proceeding.

An evidentiary hearing was held before the ALJ on August 11, 2010. At the hearing, the parties' respective testimony and exhibits were admitted into the evidentiary record to provide context and support for the Settlement and to provide an evidentiary basis for the ALJ and the Commission to decide the issues reserved for litigation. In addition, at the hearing on August 11, 2010, customer-complainant Elaine Andrews gave oral testimony. The evidentiary record was closed on August 23, 2010.

On August 26, 2010, the parties filed a Joint Petition for Partial Settlement and various statements in support thereof. As a result of the Settlement, the only issues reserved for litigation involve revenue allocation, non-residential rate design, and certain tariff and competitive issues. A briefing schedule has been established by the ALJ. PPL Electric's Supplement No. 83, requesting a distribution base rate increase, is ripe for disposition.

B. LEGAL STANDARDS AND BURDEN OF PROOF

Under the Public Utility Code, a public utilities' rate must be just and reasonable and cannot result in unreasonable rate discrimination. 66 Pa.C.S. §§ 1301 and 1304.

A public utility seeking a general rate increase has the burden of proof to establish the justness and reasonableness of every element of the rate increase request. 66 Pa.C.S. § 315(a); *Pa. P.U.C. v. Aqua Pennsylvania, Inc.*, Docket No. R-00038805, 236 PUR 4th 218, 2004 Pa. PUC LEXIS 39 (August 5, 2004). However, a public utility, in proving that its proposed rates are just and reasonable, does not have the burden to affirmatively defend claims made in its filing that no other party has questioned. As the Commonwealth Court has explained:

> While it is axiomatic that a utility has the burden of proving the justness and reasonableness of its proposed rates, it cannot be called upon to account for every action absent prior notice that such action is to be challenged.

Allegheny Center Assocs. v. Pa. P.U.C., 570 A.2d 149, 153 (Pa. Cmwlth. 1990).

Although the ultimate burden of proof does not shift from the utility seeking a rate increase, a party proposing an adjustment to a ratemaking claim of a utility bears the burden of presenting some evidence or analysis tending to demonstrate the reasonableness of the adjustment. *See, e.g., Pa. P.U.C. v. PECO*, Docket No. R-891364, *et al.*, 1990 Pa. PUC LEXIS 155 (May 16, 1990); *Pa. P.U.C. v. Breezewood Telephone Company*, Docket No. R-901666, 1991 Pa. PUC LEXIS 45 (January 31, 1991). In addition, tariff provisions previously approved by the Commission are deemed just and reasonable and, therefore, a party challenging a previously-approved tariff provision bears the burden to demonstrate that the Commission's prior approval is no longer justified. *See, e.g., Pa. P.U.C. v. Philadelphia Gas Works*, Docket Nos. R-00061931, *et al.*, 2007 Pa. PUC LEXIS 45 at *165-68 (September 28, 2007) (adopting the ALJ's discussion on burden of proof).

Further, a party that raises an issue that is not included in a public utility's general rate case filing bears the burden of proof. For example, in *Pa. P.U.C. v. Metropolitan Edison Company, et al.*, Docket Nos. R-00061366, *et al.*, 2007 Pa. PUC LEXIS 5 (January 11, 2007), a party offered proposals to have the companies incur expenses not included in their filings. The ALJ held that, as the proponent of a Commission order with respect to its proposals, the party bears the burden of proof as to proposals that are not included in the companies' filings. The Commission agreed and adopted the ALJ's conclusion that Section 315(a) of the Public Utility Code cannot reasonably be read to place the burden of proof on the utility with respect to an issue the utility did not include in its general rate case filing and which, frequently, the utility would oppose. *Id.* at *111-12.

II. SUMMARY OF ARGUMENT

The issues presented in a typical electric distribution rate case generally fall within four broad categories: (1) revenue requirement; (2) revenue allocation and rate design; (3) universal service; and (4) tariff and competitive issues. The parties have achieved settlement on all revenue requirement and universal service issues, as well residential rate design issues. This leaves revenue allocation, non-residential rate design and certain tariff and competitive issues for resolution by the ALJ and the Commission. A summary of PPL Electric's position on the remaining issues is set forth below.

Revenue Allocation. Revenue allocation is almost always one of the most hotly contested issues in a base rate case. Many parties have an obvious (and appropriate) interest in allocating less of the revenue increase to their own rate class and more of the increase to other rate classes. The Company has no inherent interest in allocating the increase to one rate class versus another and has sought to allocate the increase in a fair and impartial manner. Notably, the OTS, the only other major party without a particular rate class constituency, has not opposed the Company's proposed revenue allocation.

The Company's proposed revenue allocation was substantially driven by the Company's 2004 distribution rate case and in particular, the Commonwealth Court decision in that case, *Lloyd*, which held that cost of service should be the "polestar" for revenue allocation, and that while other factors, such as gradualism, can be considered, these factors should not be allowed to "trump" cost of service. In addition, as part of the remand proceeding in that case, the Company agreed to and the Commission approved a process by which the Company would seek to move rates to cost of service in three rate cases, subject to several important caveats which are addressed in more detail below.

This proceeding is the third proceeding referenced in the Commission's *Lloyd* remand order, and accordingly, the starting point for the Company's analysis was to allocate the increase so as to move all rate classes to full cost of service. However, to achieve this result, residential rates would have to be increased by far more than the full requested increase and several rate classes would have to receive substantial rate decreases. Given the amount of the increase requested and the discretion reserved to the Company and the Commission under *Lloyd* and the settlement of that case on remand, the Company developed an alternative revenue allocation that in essence assigned the entire increase to residential customers and proposed no increase to other customer classes. This allocation provides for a very substantial movement toward full cost of service and in the Company's view is just and reasonable and fully complies with the *Lloyd* decision and the remand settlement.

The revenue allocation issue was complicated to some degree by the fact that the Company proposed certain changes to its cost of service study in this proceeding, principally the decision to classify the primary distribution system into both customer and demand components (prior studies classified this system as solely demand related). The Company believes that this proposed change is fully justified and that the Commission should adopt this cost of service study and the Company's associated revenue allocation in this proceeding. However, the Company recognizes that the ALJ and the Commission may wish to review the revenue allocation issue on a strictly consistent basis, particularly given the three rate case plan developed in the *Lloyd* remand proceeding. The Company therefore also presented a cost of service study that was identical in methodology to that presented in its last two base rate proceedings. For the most part, the results of the two studies are not materially different; however, there are two significant differences. First, under the prior cost of service study

allocating the full rate increase to the residential class would produce a class rate of return somewhat above the system average return. Second, Rate LP-4 moves from well above cost of service under the proposed cost of service study to well below cost of service under the prior cost of service study.

If the Commission wishes to rely on the prior cost of service study, then some modification to the Company's proposed revenue allocation should be adopted. First, the residential class should receive most but not all of the revenue increase. Second, there should be some increase to Rates LP-4, LP-5, and LP-6. A more specific alternative proposal is presented in the revenue allocation section of this brief.

Non-Residential Rate Design. The major contested rate design issue is Donsco Incorporated's ("Donsco") request for a special rate. This issue is addressed in detail below, but several overarching points should be emphasized. First, Donsco has not challenged any aspect of the Company's proposed rates in this proceeding; rather, its complaint relates entirely to PPL Electric's existing rates and tariff structure. As a result, under well-established precedent, Donsco bears the burden of proof as to whether it is entitled to a special rate, and as explained below, Donsco has utterly failed to meet that burden of proof.

Second, Donsco relies heavily on a provision in the Competition Act which permits the Commission to approve special rates for individual customers. This provision, however, clearly does not require PPL Electric to offer such a special rate, and PPL Electric, for the many reasons set forth below, is not willing to do so, including but not limited to, the fact that such a special rate would harm other customers and would create an unfair competitive advantage for Donsco to the detriment of other similarly situated PPL Electric customers.

Third, Donsco goes to great lengths to present a case that it is "unique" as compared to other LP-4 customers and LP-5 customers who have opted to take service at 69 kV and paid for the cost of conversion. As explained, the facts demonstrate otherwise and do not support a separate rate for Donsco. The Commission, for good reason, has consistently rejected claims for special rates for individual customers, and these decisions have been uniformly affirmed by the appellate courts.

Fourth, Donsco repeatedly emphasizes the large percentage increase in distribution rates it experienced on January 1, 2010, as a result of the Commission-approved expiration of certain legacy promotional and business development generation-related rates developed many years ago. However, the expiration of these rates coincided with the end of generation rate caps and the beginning of large scale shopping for competitive generation supply. Donsco is now able to obtain, and in fact has obtained, its electricity from the competitive market, and generation represents about 80% of Donsco's electric bill under present rates. Donsco, in essence, wants to have it both ways: It wants all of the benefits of the competitive market but wants to retain all of the benefits of legacy generation-related rates developed under cost of service rate regulation of generation. Donsco's proposal is unfair to other LP-4 customers, is unfair to Donsco's competitors, would be extremely poor public policy and therefore should be rejected.

Tariff Issues. SEF proposes certain changes to PPL Electric's net metering tariff. As explained below, these changes are inconsistent with PPL Electric's current Commission-approved tariff, are inconsistent with the Commission regulations on net metering, and are wholly inconsistent with well-established cost of service principles.

Purchase of Receivables Program. RESA proposes several major changes which would fundamentally alter PPL Electric's POR program. The details of each proposal are addressed

below, but three points should be emphasized. First, the Commission has expressly held that POR programs are voluntary, *i.e.*, the Commission does not have the statutory authority to require utilities to offer such programs. PPL Electric voluntarily proposed a POR plan for 2010, this plan has been approved by the Commission, and PPL Electric has voluntarily proposed to extend that plan beyond 2010 in this proceeding. The changes proposed by RESA would fundamentally change PPL Electric's POR program and would impose unacceptable risks on PPL Electric and its non-shopping customers. PPL Electric is not willing to offer a POR program as proposed by RESA. RESA's proposals should be rejected for that reason alone.

Second, it should be emphasized that PPL Electric's POR program was only recently approved by the Commission (November 19, 2009) and has only been in effect for approximately eight months. PPL Electric made major and costly changes in its billing and IT systems to implement this voluntary POR program and is still modifying its systems to deal with issues that have arisen with this program. It is too soon to be adopting wholesale changes to a program that is still in the process of being implemented. RESA fully participated in the proceeding which established PPL Electric's POR program, and now seeks to make fundamental changes to the POR program, most of which were previously raised by RESA and not adopted by PPL Electric or the Commission. PPL Electric urges the Commission to provide some time for PPL Electric to fully implement its current program before considering fundamental changes that have already been proposed and not adopted.

Third, RESA's proposal to rebundle uncollectible accounts expense is particularly troublesome. RESA has argued for years in favor of unbundling generation costs from distribution rates so these costs will not have to paid by shopping customers. Uncollectible accounts expense has been the "classic" example cited repeatedly by RESA as a cost that must

be unbundled. RESA's own witness in this case has previously testified that there is "no rational basis" for not unbundling uncollectible accounts expense, yet proposes just such a result in this case. Under RESA's proposal the Merchant Function Charge would be non-bypassable, *i.e.*, it would be paid by both shopping and non-shopping customers. This proposed rebundling of uncollectible accounts expense clearly should be rejected. Moreover, if, for some reason, RESA's proposal were adopted, there would be absolutely no need and no possible justification for having a POR program. If RESA's proposal were adopted, PPL Electric's POR program should immediately be terminated.

III. RATE STRUCTURE

A. COST OF SERVICE

1. Introduction

Fully allocated cost of service studies, such as those presented by PPL Electric in this proceeding, take the Company's overall total cost of service and allocate it to the various rate classes and then calculate the rate of return provided by that class. The studies then compare the rate of return provided by each rate class to the system average rate of return to determine if each rate class is paying above or below its allocated cost of service. That conclusion provides important guidance in base rate proceedings as to whether a rate class should receive a rate increase, and if so, the amount of the increase.

Although cost of service studies may appear to have great precision, the Commission has repeatedly recognized that the cost of service study is only a guide to designing rates and is only one factor, albeit an important one, to be considered in the rate setting process. *See, e.g., Pa. P.U.C. v. Pennsylvania Power & Light Co.*, 55 PUR 4th 185, 249 (1983); *Pa. P.U.C. v. Aqua Pennsylvania, Inc.*, R-00072711, 2008 Pa, PUC LEXIS 50 (July 31, 2008); *Pa. P.U.C. v. West Penn Power Co.*, R-00973981, 1998 Pa. PUC LEXIS (May 29, 1998). The Commission has concluded further that there is no one single absolutely correct method for preparing cost of service studies. In fact, the Commission has referred to cost of service studies as more of an art form than science. *Application of Metropolitan Edison Co.*, R-00974008 (June 30, 1998); *Pa. P.U.C. v. Pennsylvania Power & Light Co.*, 55 PUR 4th 185 (1983). Significantly, all of the witnesses in this proceeding agree that a cost of service study is a guide and that no one cost of service study is absolutely correct. PPL Electric St. 7, pp. 24-25; OSBA St. 1, p. 22; OCA St. 3, p. 4; PPLICA St. 2-R, p. 7. Recently, the Commonwealth Court of Pennsylvania has concluded that cost is the "polestar" of utility ratemaking. *Lloyd v. Pa. P.U.C.*, 904 A.2d 1010 (Pa.

Cmwlth. 2006), *appeal denied*, 591 Pa. 676, 916 A.2d 1104 (2007) ("*Lloyd*"). As a result of the *Lloyd* decision, cost of service studies have assumed a greater degree of importance in utility ratemaking, but it still must be recognized that cost allocation is not an exact science, that there is no single "correct" cost allocation methodology and that the Court did not hold that all other considerations are to be disregarded.

2. PPL Electric's Cost of Service Study Confirmed in PPL Electric Ex. JMK-2A Should Be Accepted For Use In This Proceeding

Pursuant to the Commission's regulations at 52 Pa. Code §§ 53.53, *et seq.*, PPL Electric presented fully-allocated cost of service studies showing the allocation of its distribution costs among the various rate classes at both present and proposed rates for the historic (PPL Electric Ex. JMK-1) and future (PPL Electric Ex. JMK-2 Rev.) test years. PPL Electric's witness, Mr. Joseph M. Kleha, who has over 30 years experience in preparing cost allocation studies, applied well-established and appropriate cost allocation principles in preparing these studies. *See generally* PPL Electric St. 7, pp. 19-26.

In total, PPL Electric produced six cost of service studies. The first two, PPL Exhibit JMK-1 and JMK-2 were submitted as part of the original filing and were for the historic and future test years, respectively. Because PPL Electric determined that PPL Exhibit JMK-2 contained certain errors, it was not moved into evidence. It was replaced by PPL Electric Exhibit JMK-2 (Rev.), which eliminated the errors and which was admitted into evidence. Tr. 386. PPL Electric also presented PPL Electric Exhibit JMK-2A which is the same as PPL Electric Exhibit JMK-2(Rev.) except that Exhibit JMK-2A classifies substations as entirely demand-related and has been updated to reflect PPL Electric's final accounting exhibit, PPL Electric Ex. Future 1 (Revised). PPL Electric St. 7-R, p. 7. PPL Electric also presented Exhibit JMK-2B, which

follows precisely the methodology used in prior cases in which all primary voltage facilities are classified as demand related. PPL Electric St. 7-R, pp 9-10.

As explained in more detail below, PPL Electric proposes that the ALJ and the Commission rely on the cost of service study presented in Exhibit JMK-2A in this proceeding. This cost of service study reflects certain improvements/refinements to studies presented by PPL Electric in prior rate cases and therefore is more precise and accurate, in the Company's view, than the methodology used in prior rate cases and contained in Exhibit JMK-2B. Exhibit JMK-2A is very similar to Exhibit JMK-2 (Rev.). The only difference is that Exhibit JMK-2A, responding to criticisms lodged by OSBA, classifies substations as 100 percent demand related, whereas Exhibit JMK-2 (Rev.) classifies substations as having both a customer and demand component. PPL Electric believes, as a matter of cost allocation theory and practice, that substations do have both a customer and demand component, but recognizes that this may be a controversial issue and is an issue that need not be finally decided in this proceeding. The results in Exhibit JMK-2A also lie somewhere in between Exhibit JMK-2 (Rev.) and Exhibit JMK-2B and provide an appropriate compromise study for use in this proceeding.

Two other parties in this proceeding produced cost of service studies – OSBA and OCA. PPLICA produced evidence generally supportive of PPL Electric's cost of service study. PPLICA St. 2-R, pp. 1-5. In addition, PPLICA criticized the peak and average cost of service study produced by OCA, PPLICA St. 2-R, pp. 5-7, and also criticized OSBA's reliance on multiple studies. PPLICA St. 2-R, pp. 8-9. The OSBA submitted its own cost of service study, but its disagreements with PPL Electric's cost of service study were not substantial. In fact, to a very large extent, OSBA and PPL Electric agree upon the cost of service study methods that the

Commission should consider in evaluating revenue allocation and rate design in this proceeding. OSBA St. 3, p. 2.

As in past proceedings, however, OCA has proposed substantial revisions to PPL Electric's cost of service study. Predictably, most of the revisions proposed by the OCA would, if adopted, place the residential rate classes in a more advantageous position. PPL Electric St. 7-R, p. 3. PPL Electric, as a party without incentives to favor one rate class or another, has taken a reasonable, moderate position in allocating costs to various customer classes. It also should be noted that the OTS, which represents the public interest in general and not any particular rate class, has not opposed the Company's cost of service study.

Cost of service studies generally include three fundamental steps: First, costs of service are functionalized into their appropriate function: generation,[2] transmission or distribution. Second, costs are classified as demand, customer or energy related. Third, costs are allocated among the rate classes.

PPL Electric also eliminated from the cost of service studies revenues and expenses that are recovered through specific cost recovery mechanisms under Section 1307 of the Public Utility Code, *e.g*, the Generation Supply Charge, the Competitive Transition Charge, the Universal Service Rider and the State Tax Adjustment Surcharge. The remaining transmission and distribution investments and expenses were then separated into the transmission function, which is not addressed in this proceeding, and the distribution function, which is the subject of this proceeding. PPL Electric St. 7, pp. 20-21.

[2] There is no longer a generation function for PPL Electric because its generation facilities and operations were divested following PPL Electric's restructuring proceeding under the Electricity Generation Customer Choice and Competition Act, 66 Pa.C.S. Ch. 28.

Next, PPL Electric sub-functionalized distribution costs between the primary and secondary distribution systems. The primary system is a three phase system that operates at 12 or 23 kV. The secondary system includes single phase facilities that operate at or below 12 kV. PPL Electric Ex. JMK-3(Rev.), p. 1.

After all distribution costs of service have been functionalized, the next step is to classify costs as customer, demand or energy related. It is generally agreed that distribution system costs are either demand or customer related, but not energy related. A portion of distribution plant costs is incurred to meet peak demand because each component of the distribution system must be sized to meet the peak demand placed on it. Similarly, a portion of distribution plant costs is incurred in proportion to the number of customers served, *i.e.*, it varies with the number of customers served. Such costs, which include for example billing costs, meters and services, are classified as customer related. OSBA St. 1, pp. 5-6.

The third classification, energy costs, are those costs that vary in proportion to the amount of electricity delivered. In general, however, no electric distribution costs are caused by average or annual amounts of energy delivered by PPL Electric. PPL Electric's approach of not classifying any electric distribution costs as energy related is consistent with the National Association of Regulatory Utility Commissioners' ("NARUC") Electric Utility Cost Allocation Manual ("Manual"). PPL Electric St. 7-R, pp. 11-12, PPLICA St. 2-R, pp. 6-7; PPLICA Ex. RAB-1R and long-standing Commission practice for electric utilities.

In its cost of service studies, PPL Electric classified certain plant, such as meters, as 100 percent customer-related. Most plant, however, was classified as partly customer related and partly demand related. In order to quantify the portions of plant that is customer related and the portion that is demand related, PPL Electric used the minimum size system methodology. This

methodology is consistent with prior PPL Electric rate cases and is one of two methods recommended in the NARUC Manual.[3] PPL Electric St. 7, p. 26; PPLICA Ex. RAB-1.

A minimum system study seeks to identify and quantify the costs that would be incurred to serve a customer with minimal or no load. The cost of serving a customer with minimal or no load is based on the smallest size equipment currently being installed on the system. PPL Electric St. 7-R, p. 13. This portion of the distribution system is classified as customer related. The remainder of the system is classified as demand related. PPL Electric St. 7, p. 26.

The cost allocation methodology used by PPL Electric in this proceeding generally followed the methodology used in many prior base rate cases over the past 30 years. The Company, however, did implement two refinements in this proceeding, each of which was designed to address criticisms of PPL Electric's cost of service studies in prior proceedings.

First, in prior proceedings, certain parties contended that the "minimum size" system study used by PPL Electric was flawed because the smallest equipment that is currently being installed on the system had significant load-carrying capacity and therefore was partly demand related. PPL Electric 7, p. 23. To address these criticisms, PPL Electric undertook a rigorous engineering analysis of the minimum size overhead (10 kVa ("kilovolt ampere")) and underground (25 kVa) transformers which are currently the smallest size transformers being installed on its system. The analysis performed by PPL Electric was based upon the Capitalized Cost Method. The analysis identified the total cost of the transformers, the cost of no load losses and the cost of load losses. The purpose of this analysis was to identify the "no load" portion of

[3] The other method is the zero-intercept method. The shortcomings of this method as applied to PPL Electric are explained in more detail below.

PPL Electric's overhead and underground transformers so that only the "no load" portion could be classified as customer-related. PPL St. 7, pp. 23-24.

Second, in prior proceedings, certain parties contended that PPL Electric should apply the minimum system method to the primary distribution system instead of simply assuming that this system was 100% demand related. In response, PPL Electric for the first time, in PPL Exhibit JMK-2(Rev.), applied the minimum system study to both the primary and secondary distribution systems and developed specific customer and demand components for each sub-system. PPL Electric St. 7, p. 24. As explained above, PPL Electric also submitted Exhibits JMK-2A, which treats substations as all demand related and JMK-2B which applied PPL Electric's traditional methodology. In this proceeding, PPL Electric prefers Exhibit JMK-2A as an appropriate transition from treating the entire primary voltage system as demand related to treating the entire primary voltage system as partly customer related and partly demand related.

The next step in preparation of the cost of service study was to allocate the cost of service among the rate classes. In this step, classified costs are either directly assigned to the specific rate classes or are arithmetically distributed among rate classes using an allocation factor that is consistent with the underlying cost classification. For some costs, the allocators relate directly to the underlying customer/demand classification. For example, demand-related costs are allocated based on an appropriate measure of peak demand, such as non-coincident peak demand.[4] Similarly, customer related costs, in general, are allocated based upon the number of customers. For other costs, allocators must be selected based on factors that most closely relate to the incurrence of the cost. For example, general plant and related operation and maintenance

[4] The non-coincident peak demand is based on the highest demand imposed by each rate class on the distribution system at any time during the test year, regardless of the demand placed on the system by other classes at that time. PPL Electric St. 7, p. 21.

expenses, as well as most administrative and general expenses, are classified and allocated in proportion to allocated direct labor costs. Materials and supplies are classified and allocated in proportion to distribution plant, and cash working capital costs are classified and allocated in proportion to allocated operation and maintenance costs. Taxes other than income taxes are generally classified and allocated in proportion to allocated plant costs. Deferred income taxes are classified and allocated in proportion to a combination of allocated labor costs and allocated plant costs. Income taxes are allocated based upon the income produced by each rate class. OSBA St. 1, pp. 9-10.

As explained previously, PPL Electric's preferred cost of service study in this case, PPL Electric JMK-2A, is consistent with the cost of service studies presented by PPL Electric and accepted by the Commission in prior cases, but does adopt some refinements/improvements in response to other parties' criticisms in those cases. PPL Electric fully supports Exhibit JMK-2A as it is more precise than PPL Electric's historical approach and reflects certain improvements recommended by other parties in prior proceedings without departing substantially from prior practices. For example, PPL Electric acknowledged, in prior cases, that its minimum system had some load carrying capacity, and that its primary distribution system had both a customer and demand component. However, the analyses necessary to implement these changes had not been undertaken at that time. Those analyses were completed for this proceeding, however, and PPL Electric's cost of service studies have been revised accordingly. PPL Electric St. 7-R, p. 9.

PPL Electric recognizes, however, that the ALJ and the Commission may wish to evaluate the movement of PPL Electric's rates toward the system average rate of return based on a strict uniform methodology from rate case to rate case, particularly given the fact that this is the third rate proceeding as defined in the *Lloyd* remand settlement and discussed in more detail

below. For this reason, PPL Electric also provided an alternative cost of service study that follows exactly the same approach that has been used by PPL Electric and accepted by the Commission in prior base rate cases. This alternative cost of service study is provided in PPL Electric Ex. JMK-2B. It must be emphasized, however, that the cost of service study provided as PPL Electric JMK-2B does not contain the refinements to the determination of the customer component of distribution plant that are explained above. Therefore, in PPL Electric's view, PPL Exhibit JMK-2B is not as accurate as PPL Electric Exhibit JMK-2A and therefore should not be used as the primary tool in allocating revenue requirement among the rate classes.

3. OCA's Criticism of PPL Electric's Cost of Service Study Should Be Rejected

The only party to this proceeding who offered any substantial criticism of PPL Electric's cost of service studies was OCA. Specifically, the OCA contends that 100% of PPL Electric's distribution system is demand related, criticized the use of the minimum system methodology to determine any customer component of the distribution system, and criticized of the data used by PPL Electric in its minimum system study. For the reasons explained below, OCA's criticisms of PPL Electric's cost of service study are without merit and should be rejected.

a. The OCA's Argument That PPL Electric's Distribution System Is 100% Demand Related And Has No Customer Component Should Be Rejected

The central contention presented by OCA witness Watkins is the extreme and unprecedented conclusion that all of PPL Electric's distribution system should be classified as demand related, and none of it should be classified as customer related. OCA St. 3, pp. 10-12. Contrary to OCA's assertions, however, it is clear that two factors cause electric distribution companies to invest in plant: (1) to meet the peak demands of individual customers and (2) to interconnect all customers on the distribution system with the transmission system. OSBA St. 2,

pp. 2-3; PPL Electric St. 7-R, pp. 11-12; PPLICA St. 2-R, pp. 2-3; NARUC Manual, p. 90; PPLICA Ex. RAB-1R. The NARUC Manual specifically states that: "As previously indicated, distribution plant is a fixed investment in facilities which does not vary with the consumption of energy and which is closest to the point of use. Therefore, distribution plant is classified as demand and customer-related cost." PPL Electric St. 7-R, p. 12, fn. 1. It is clear that distribution plant is required to connect customers to the system and that, in general, the more customers serviced by an electric distribution company, the greater its investment in distribution plant will be. Under the OCA's view of the world, the number of customers is simply irrelevant to the design and structure of a distribution system and distribution system costs are only incurred to meet peak demand. Under this view, two utilities with identical peak demands would have the same distribution system, both as to design and cost, even if one utility had one customer and the other had a million customers. Such a conclusion makes no sense and demonstrates the lack of merit in the OCA position.

OCA also criticizes the inclusion of a customer component of the distribution system on the grounds that, in its opinion, the customer component does not recognize how distribution systems are designed and constructed. OCA St. 3, pp. 13-14; OCA St. 3-S, pp. 2-3. In support of the contention, OCA argues that, for various reasons, some equipment on electric distribution systems is oversized and that costs can vary depending upon whether facilities are installed in urban or rural areas and depending on economies of scale. From these premises, OCA argues that there is no correlation between the number of customers served by an electric distribution company and costs incurred to provide service, and therefore, electric distribution systems have no customer component. OCA St. 3, pp. 10-12.

OCA's contention, while factually accurate, does not support its position that no portion of distribution system costs should be allocated on a customer basis. It is PPL Electric's position, based on long-standing practice and precedent, that the distribution system should be classified as part customer related and part demand related. The purpose of the minimum size system methodology is to identify the customer component by determining what portion of the distribution system is required to simply connect the customer to the system. Obviously, the minimum size system allocation methodology makes no attempt to address the sizing of those portions of the system needed to meet peak load requirements or the possible over-sizing of portions of the system. Those portions of the system should be and are classified as demand related. Indeed, the most the OCA argument proves is that the distribution system has both a customer component and a demand component. On this point, PPL Electric agrees.

In further support of its contention that there is no customer component of the distribution system, OCA relies on a study it conducted of the distribution of customers, by rate class, throughout PPL Electric's service territory, as determined by zip codes. OCA explains its zip code analysis as follows:

> Unlike the CCOSS study conducted for its last rate case, PPL has made an *a priori* assumption that it is appropriate to allocate a portion of its distribution plant based on customer counts and a portion based on demand levels. As indicated earlier, the only reason why it may be appropriate to allocate a portion of distribution plant expenses based on number of customers, rather than utilization, is due to the possibility that the mix of customer classes varies significantly across the urban and rural portions of a service territory. In this regard, I conducted an analysis of the distribution, or mix, of PPL's customer classes across its service area. . . . .
>
> PPL's customers are dispersed in a reasonably proportional manner throughout its service area. In other words, there is no distinct difference in the mix of customers (by class) across the rural and urban portions of PPL's service area. The relationship of Residential customers relative to non-Residential customers is

> relatively constant throughout PPL's service area. . . . As such, PPL's distribution plant and expenses are properly assigned to classes based only on utilization and any consideration of customer counts is improper for the allocation of distribution plant, as such, these PPL distribution plant should be classified as 100% demand-related.

OCA St. 3, pp. 10-12. OCA's approach is erroneous for numerous reasons.

First, OCA begins with an incorrect assumption. Mr. Watkins opens his discussion of this issue with the following statement: "Unlike the CCOSS study conducted for its last rate case, PPL has made an *a priori* assumption that it is appropriate to allocate a portion of its distribution plant based on customer counts and a portion based on demand levels." This statement is simply not true. PPL Electric has at least for the last 30 years classified a portion of its distribution system as demand related and a portion as customer related and has at least for the last 30 years used a minimum system study to determine these two components. PPL Electric St. 7, p. 22. Indeed, in PPL Electric's 2004 base rate case, ALJ Turner, in her Recommended Decision specifically noted that PPL Electric's cost of service studies both were performed using the "minimum size" method and recommended that the Commission rely primarily on PPL Electric's cost of service studies for guidance in allocation of revenue requirement. *Pa. P.U.C. v. PPL Electric Utilities Corp.*, Docket No. R-00049255, p. 142, 2004 Pa. PUC LEXIS 41 (Oct. 21, 2004).[5]

Second, Mr. Watkins further states that the "only reason" to have customer component for the distribution system is if the mix of customer classes (residential vs. business) is significantly different across the rural and urban parts of a utility's service territory. OCA St. 3, p. 10. This statement also is incorrect and simply ignores the explanations provided by PPL

[5] In its Order, the Commission did not address issues related to the cost of service studies.

Electric, OSBA and PPLICA. Specifically, it is appropriate to have a customer component of distribution plant because the number of customers affects distribution system investment. Costs should be allocated based on the factors that cause a cost to be incurred or cause a cost to vary. PPL Electric's distribution costs are incurred and vary based on the number of customers connected to the system and the demand imposed by those customers on the system. A utility distribution system with one customer will look quite different from one with one million customers. As all witnesses other than Mr. Watkins agree, the number of customer is clearly a relevant factor in classifying and allocating distribution system costs.

Third, Mr. Watkins' study is flawed because it focuses only on the relative proportion of residential vs. business customers in rural and urban areas and ignores the obvious and indisputable fact that on an absolute basis, there are many more residential customers than business customers connected to PPL Electric's distribution system. Even if the cost of connecting business customers to the system were the same as the cost of connecting residential customers, a greater proportion of distribution system plant cost should be allocated to residential customers because there are so many more of them, and therefore, a much greater amount of plant investment is needed to connect residential customers to the system. Although the relative percentage of residential and business customers may be the same throughout PPL Electric's system in both urban and rural areas, the fact remains that there are many more residential customers than business customers. OCA's study simply confirms this obvious fact and the corresponding conclusion that the number of customers served is an important and valid factor for classifying distribution system costs.

b. PPL Electric's Use Of A Minimum System Methodology To Determine The Customer Component Of Plant Is Reasonable And Appropriate

i. OCA's Zero Intercept Method Should Be Rejected

OCA contends that, if it is determined that the distribution system has a customer component, it should be calculated using the zero intercept method and not the minimum system method. OCA St. 3, pp. 12-13. OCA's assertion is incorrect at least as to PPL Electric's distribution system. PPL Electric has specifically investigated using the zero intercept method and has determined that this method is impractical for PPL Electric. PPL Electric's most recent review of the zero intercept method produced negative zero intercept costs for wood poles, copper conductors and aluminum conductors. Clearly, the zero intercept method is not accurate or reasonable at least for PPL Electric. More generally, the zero intercept method is highly complex and in the end, inherently arbitrary. PPL Electric St. 7-R, p. 14. And, in any event, neither the OCA nor any other party has conducted a zero intercept study in this case, and it therefore is not an available option.

ii. PPL Electric's Application Of the Minimum System Study To Substations Is Reasonable

It is noted that both OSBA and OCA criticized PPL Electric's primary cost of service study set forth in PPL Electric Exhibit JMK-2 (Rev.) because PPL Electric allocated a portion of its investment in substations on a customer basis. OCA St. 3, pp. 17-18, OSBA St. 1, p. 17. PPL Electric believes it is appropriate to allocate substation partly based on the number of customers served because voltage transformation is necessary to connect distribution customers to the transmission system. Therefore, the "no load" portion of the investment in substations is appropriately classified as customer-related. Nevertheless, for the purposes of this proceeding only, PPL Electric recommends that the ALJ and the Commission rely primarily on PPL Electric

Ex. JMK-2A for guidance in revenue requirement allocations. That cost of service study classifies substations as 100% demand-related. Such treatment is appropriate in this proceeding in order to avoid a substantial change in cost of service methodologies in a single rate case.[6]

iii. PPL Electric's Minimum Size System Study Produces Reasonable Results And Are Based On Appropriate Data

OCA next argues that the results of PPL Electric's minimum system study are unreasonable because the customer component percentage of the primary sub-system is greater than the customer component percentage of the secondary sub-system. OCA St. 3, p. 15. This argument is without merit. In fact, it is reasonable and appropriate that the primary distribution system would have a higher customer component due to the relatively rural nature of its service territory. The primary distribution systems of rural electric distribution utilities generally have a higher proportion of customer costs because it is more efficient to move electric energy over long distances at higher voltages. PPL Electric St. 7-R, pp. 20-21. OSBA concurred that it is not necessarily true that primary distribution systems would have a lower customer component than secondary distribution systems. OSBA St. 2, pp. 5-6.

OCA, in an attempt to generally discredit PPL Electric's cost of service studies, next embarks on a series of criticisms of the data relied upon by PPL Electric in its cost of service study. First, OCA criticizes PPL Electric's record keeping as being "less than detailed." OCA St. 3, p. 15. OCA's criticism is unwarranted. PPL Electric's continuing property records comply fully with FERC's Uniform System of Accounts at 18 C.F.R. Part 101. PPL Electric St. 7-R, p. 21. OCA also criticizes PPL Electric's cost of service study because it relies on conductor length

[6] If the ALJ and the Commission would prefer to rely on the more accurate study which classifies all primary voltage plant including substations as demand and customer related, then they should rely on PPL Electric Ex. JMK-2(Revised).

instead of circuit length. Contrary to implication in OCA's testimony, the Uniform System of Accounts does not require or prescribe that conductors be accounted for on a circuit foot basis. PPL Electric has recorded on its books costs based on linear feet of conductors, not circuits, for at least fifty years, and neither FERC nor the Commission have criticized that practice in the numerous audits that have taken place of PPL Electric's books and records during those decades.[7] PPL Electric St. 7-R, p. 21. Further, as explained by Mr. Kleha, any imprecision in PPL Electric's books and records on this issue would benefit residential customers. PPL Electric St. 7-R, p. 21.

OCA next complains that PPL Electric has included the cost of fiber optic communication cables in its cost of service study. OCA St. 3, p. 16. Again, OCA's criticisms are meritless. It is completely proper to include costs of fiber optic communication cable because such cable is used to transfer data to PPL Electric's System Control and Data Acquisition ("SCADA") devices from circuit breakers and sectionalizing devices, which are part of PPL Electric's primary voltage distribution facilities. The SCADA devices are used to determine whether the system is operating properly and to control remote circuit breakers and sectionalizing devices to restore service. PPL Electric St. 7-R, p. 22. Such data are transferred to operations centers where they used to address and resolve quickly any service issues. Therefore, fiber optic communication cables enable PPL Electric to continue to provide adequate and reliable service, and are appropriately included in the cost of service study.

OCA's next criticizes PPL Electric's cost of service study because there are 59 million linear feet of wire whose size and material are not recorded on PPL Electric's continuing plant

[7] Circuit length and conductor length differ because some circuits require more than one conductor. For example, three phase service requires three conductors. Therefore, for every foot of three phase circuit there are three feet of conductors.

records. OCA St. 3, p. 16. OCA claims that PPL Electric's cost of service study is flawed because PPL Electric cannot determine whether such conductor is attributable to the primary system or to the secondary system. OCA is wrong. These conductors are fully examined in the field and verified before they are included in PPL Electric's electric facility database. Based on such examinations and verifications, PPL Electric has determined that all of the conductor in question is part of the primary system, and not the secondary system. As to OCA's contention that the size and materials of the conductors are unknown, in fact such conductor is predominately 2 ACSR[8] and 6 guage copper. PPL Electric St. 7-R, p. 22.

OCA also contends that PPL Electric has misclassified multiplex cables as part of the secondary system. OCA claims that such cable is instead primarily used for customer services, *i.e.*, the line from the street to the customer's home or business, with some limited use in street lighting and signal systems. OCA St. 3, p. 16. This criticism is based on the OCA's assumption that "the vast majority of overhead capital is secondary distribution systems are constructed with un-insulated single wire conductors." OCA St. 3, p. 16. OCA's assumption is wrong. Starting in the 1960s, PPL Electric began replacing single-wire secondary voltage conductors with multiplex secondary voltage level conductors.[9] Since then, PPL Electric has replaced the vast majority of its uninsulated, single-wire secondary voltage conductors with multiplexed secondary voltage conductors. PPL Electric St. 7-R, p. 22.

OCA next claims that PPL Electric's cost of service study misstates the price of for 10 kVa transformers as $468 per unit. OCA St. 3, p. 17. Contrary to OCA's conclusions, however, $468 was not the price used by PPL Electric for a 10 kVa transformer in the cost of service

[8] Aluminum conductor steel reinforced.

[9] PPL Electric's multiplex conductors have three or four conductors. One wire is neutral and uninsulated. The remaining conductors are insulated.

study. The Company's "no load" book value of $298.64[10] is set forth on page 13 of Exhibit JMK-3-Revised. Clearly, PPL Electric did use the correct book value of a 10 kVa transformer installed on the secondary voltage level portion of its distribution system. PPL Electric St. 7-R, p. 24.

4. OCA's Cost of Service Study Should Be Rejected

a. OCA's Peak and Average Allocation Of Demand Costs Should Be Rejected

OCA presented cost of service studies based on the peak and average method of allocating demand-related costs. OCA St. 1, pp. 22, 25. Under the peak and average method, 50 percent of demand-related costs are allocated based on each rate class's non-coincident peak demand and 50 percent of demand related costs are allocated based on the average level of daily use of energy by each rate class. The peak and average method assumes that 50 percent of demand costs are incurred due to rate class average use of energy. This assumption, as explained below, is simply without basis. PPL Electric allocated demand-related costs based entirely on each rate class's non-coincident peak. This method assumes, correctly, that demand-related costs are incurred to meet peak demands. The non-coincident peak method is correct for allocating demand-related costs because facilities are sized, and costs are incurred, to meet peak demands.

OCA's position regarding its cost of service study which used the peak and average method for allocating demand-related costs is somewhat puzzling. It clearly presented the results of peak and average studies. OCA St. 3, pp. 22, 25. As expected, in general, the study shows higher returns for the residential classes because it benefits rate classes with poor load factors

[10] $340.61 (book value) x "no load" factor of 87.7 percent.

and is disadvantageous to rate classes with high load factors. OCA specifically relied on its peak and average study to set the outer extreme of the "range" of reasonable results that it relied on for guidance in its allocation of revenue requirement. OCA St. 3, pp. 26-27. Indeed, the Peak and Average Study provides the only support for OCA's proposed $16 million increase to Rate Schedule GS-3. Nevertheless, OCA emphatically, and at some length, denied that it recommended any cost of service study that utilized a peak and average allocation method. OCA St. 3-S, pp. 1-2. Because OCA denies that it recommended any peak and average cost of service study in this proceeding, its flaws will be addressed only briefly here.

The main flaw of the peak and average cost of service study for an electric distribution system is that it is not based upon principles of costs causation. Contrary to the implicit assumption inherit in every peak and average cost of service study for an electric distribution system, the size and cost of distribution facilities do not vary based upon the average or annual amount of energy consumed by customers. Instead, distribution facilities are sized to meet peak load requirements and to physically connect customers to the system. NARUC Manual, Section IX-8; PPLICA Ex. RAB-1; PPL Electric St. 7-R, pp. 11-12; OSBA St. 2, pp. 2-3; PPLICA St. 2-R, pp. 4-7. Indeed, the NARUC manual does not even recognize or refer to the peak and average method. PPLICA St. 2-R, pp. 5-6.

The adoption of a peak and average method for cost allocation for an electric distribution system would be unprecedented. The Commission has previously rejected use of the peak and average method for electric utilities with regard to their distribution systems. *Pa. P.U.C. v. Pennsylvania Power Co.*, 85 PUR 4th 323 (1987).[11]

[11] In electric public utility cases, on occasion the Commission expressed interest in the peak and average method for an electric company. Such interest, however, has been limited to generation and transmission facilities. *See, e.g., Pa. P.U.C. v. Philadelphia Electric Co.*, R-850152 (June 27, 1986).

b. Other Allocators Proposed By OCA Should Be Rejected

In its preferred cost of service study, OCA slants the results more favorably for the rate classes it represents by substituting allocators of certain costs for allocators used by PPL Electric in its cost of service studies. The allocators selected by OCA, however, are not appropriate, and their use should be rejected.

OCA recommends use of different allocators for costs recorded in several accounts. The most significant of the cost allocation changes recommended by OCA is the recommendation, in terms of its effect on the results of the cost of service study, pertain to administrative and general ("A&G") expenses. PPL Electric allocated A&G expenses based on labor. This allocation is consistent with prior cost of service studies filed by PPL Electric with and approved by the Commission. It also follows the cost allocation principles set forth in the NARUC Manual. In contrast, OCA would allocate certain A&G expenses on non-labor factors. For example, OCA would allocate Account 923 – Outside Services Employed, Account 925 – Injuries and Damages, Account 930 – Miscellaneous General Expense and Account 935 – Maintenance of General Plant on the basis of its plant investment allocators.

OCA's approach, however, is not only contrary to the recommendations in the NARUC manual but also are inappropriate based upon the definitions of these accounts and the Uniform System of Accounts. Specifically, Outside Services Employed includes fees and expenses of professional consultants and others for general services that are not applicable to any particular operating function or to other accounts. In contrast, plant investment, which OCA would use to allocate amounts recorded in this account, is all allocated to specific operating functions — productions, transmission or distribution. PPL Electric St. 7-R, pp. 25-26.

Injuries and Damages expense includes cost of insurance and reserve accruals to recognize the costs of injuries and damages claims. Expenses include payment of claims by

employees and others and the costs of labor and supplies incurred as a result of injury and damages claims including medical and hospital service and expenses for employees resulting from work related injuries and benefits paid for incapacitated employees. Again, there is no relationship between Injuries and Damages expense and plant. PPL Electric St. 7-R, p. 26.

Miscellaneous General expense includes the costs of labor and expenses regarding general management of utility property not recorded elsewhere. Such expenses include miscellaneous labor, industry association dues, stockholder expenses, directors' fees and expenses. Again, there is no relationship between miscellaneous general expenses and plant. PPL Electric St. 7-R, p. 26.

Maintenance of General Plant expense includes labor, materials used and expenses incurred to maintain general property. General plant, itself, has been and continues to be allocated on the basis of labor. There is no reason to allocate expenses for maintenance of general plant differently from general plant. PPL Electric St. 7-R, pp. 26-27.

None of the allocators recommended by OCA are appropriate, and the allocators used by PPL Electric in its cost of service study are appropriate and should be used by the ALJ and the Commission.

In its recommended cost of service study, OCA also misallocated costs associated with PPL Electric's universal service programs. OCA improperly allocated such costs to the residential class. Such allocation was incorrect because such costs are recovered through the Universal Service Rider, and therefore are excluded from PPL Electric's revenue requirement in this distribution rate proceeding. PPL St. 7-R, p. 27.

5. Conclusion as to Cost of Service Studies

The ALJ and the Commission should accept PPL Electric's recommended cost of service study that is found in PPL Electric Ex. JMK-2A as its primary guide in allocating revenue requirement among the rate classes.

B. REVENUE ALLOCATION

1. Background

PPL Electric's proposed allocation of revenue requirement among the rate classes in this proceeding is driven largely by the Commonwealth Court's decision in *Lloyd* which involved, *inter alia*, an appeal of the revenue allocation in PPL Electric's 2004 base rate proceeding. In that case, the Court concluded that, although other factors can be given some consideration, cost of service is the "polestar" of utility rates. The Court concluded further that other considerations, such as gradualism, should not be permitted to "trump" cost of service as the primary basis for allocating the revenue increase. The Court remanded the proceeding to the Commission for further consideration of the revenue allocation in light of the principles set forth in the Court's decision.

In the remand proceeding before the Commission, PPL Electric and the other parties entered into a settlement, which was approved by the Commission in an Order entered on July 25, 2007. As part of the settlement, PPL Electric agreed to move distribution rates to or "near" cost of service over a series of three distribution rate cases with the 2004 case, as adjusted by the Settlement, being the first case in that series. PPL Electric's 2007 distribution base rate case at Docket No. R-00072155 was the second case in the series, and this proceeding is the third case subject to the settlement of the 2004 distribution rate proceeding. PPL Electric St. 6, pp. 15-17.

It has been clear from the beginning, however, that the settlement of the remand of the 2004 rate proceeding did not require that rates had to be set in lockstep with cost of service in

this proceeding. In the remand of the 2004 rate case before the Commission, PPL Electric provided the following explanation of the revenue requirement allocation provisions of the settlement of the 2004 distribution rate proceeding:

> The Company proposes to move its distribution rates for all major rate classes to at or near full cost of service in three rate cases, including the 2004 rate case. Specifically, the Company proposes to maintain the distribution rates approved in this case (with an adjustment to remove storm damage costs) which, in fact, resulted in meaningful movement toward cost of service on a relative rate of return basis for major rate classes; move one-half of the remaining difference in its recently filed 2007 rate case; and move to full cost of service in its next case after that. There are three caveats. First, for certain rate classes, most notably Rate Schedule RTS (Residential Thermal Storage) and street lighting, one or two more rate cases may be required because these rates currently are so far below cost of service that it would take very disproportionate increases to move them to full cost of service in three rate cases. Second, as explained by Mr. Kleha, cost of service is an art, not a science, and while the Company will attempt to move rates reasonably close to full cost of service, some modest differences may remain. Finally, the Company would reserve the right to apply principles of gradualism to ameliorate individual customer rate impacts to the extent necessary in future proceedings.

PPL Electric St. 6, pp. 18-19. There is no requirement that PPL Electric's rates in this proceeding be set in a manner that all rate classes produce exactly the system average rate of return.

2. PPL Electric's Proposed Allocation

As an initial step in allocating the proposed distribution rate increase, PPL Electric first developed a revenue allocation that strictly followed cost of service and moved all rate classes to the proposed system average rate of return. Upon review, however, PPL Electric determined that this approach did not produce a just and reasonable result. Specifically, the increase to the residential rate classes would have been far in excess of the total increase requested in this case, and all of the other rate classes would have received very substantial rate decreases. Further, this

initial cost-based allocation produced a distribution rate increase to customers served under Rate Schedule RTS of about 200 percent. PPL Electric St. 6, p. 19. Such increases for an entire rate class are to be mitigated where it is practical to do so and where mitigation can be accomplished without unfair effects on other customers.

In order to avoid these unreasonable results, PPL Electric developed an alternative allocation. Specifically, PPL Electric allocated the entire proposed rate increase to residential customers and allocated no rate increase or decrease to other customer classes. Within the residential class, PPL Electric limited the increase to Rate RTS to the amount necessary to move it from a negative 54 percent of the system average return to approximately zero percent of system average return. This reduced the increase to Rate RTS from about 200 percent to about 60 percent. The difference between revenue requirements of Rate Schedule RTS at the system average rate of return and the amount allocated by PPL Electric was allocated to Rate RS, under which most residential customers are served. PPL Electric St. 6, pp. 19-20.

In this context, it should be noted that, unlike most other parties to this proceeding, PPL Electric has no "axe to grind" regarding the allocation of revenue to any particular rate classes. Instead, PPL Electric again in this proceeding has proposed allocations that are fair, reasonable, even-handed and consistent with sound rate-making principles. It must be noted also that OTS, the other party with no "axe to grind" on revenue allocation issues, has voiced no objection or opposition to PPL Electric's proposals.

PPL Electric's proposed allocation follows the results of PPL Electric's cost of service study, PPL Electric Ex. JMK-2A, and moves all rate classes significantly toward the system average rate of return, as shown by the chart below, which is taken from PPL Electric Ex. JMK-2A, pp. 8-11.

Rate Classes	Relative Return at Present Rates	Relative Return at Proposed Rates
PA Jurisdiction Distribution	100.00%	100.00%
RS	53.10%	78.61%
RTS	-59.94%	-2.65%
GS-1	163.91%	113.17%
GS-3	360.73%	250.06%
LP-4	212.88%	145.20%
ISP	140.06%	135.83%
LP-5	-372.02%	-237.33%
LP-6	-1064.39%	-831.53%
LPEP	237.36%	163.51%
GH	217.81%	150.94%
SL/AL	145.47%	100.77%

Clearly, PPL Electric's proposed allocation of revenue requirement among the rate classes is reasonable and achieves substantial progress in moving rate classes toward the system average rate of return. PPL Electric's proposed allocation should be adopted.

3. OSBA's Proposed Allocation

The OSBA proposed a different allocation of revenue requirement. The chart below compares the allocation proposed by PPL Electric with the allocation proposed by OSBA at originally proposed rates, expressed in dollars of increased revenues:

Rate Class	PPL Electric Proposed Allocation ($000)	OSBA Proposed Allocation[12] ($000)
RS	112,398	109,235
RTS	2,240	2,240
GS-1		
GS-3		
LP-4, ISP	2	2,000
LP-5, LP-6	35	1,200
LPEP		
GH		
SL/AL		
TOTAL	114,675	114,675

Under the OSBA's proposal, Rate Schedules LP-4, IS-P, LP-5 and LP-6 would receive rate increases, and the revenue from these rate increases would be used to reduce the rate increase allocated to customers under Rate Schedule RS. PPL Electric St. 6-R, p. 22.

The foregoing chart sets forth OSBA's proposal at originally proposed rates. OSBA also recommended that approximately the first $18 million of any reductions in revenue requirement be assigned as rate decreases to customers under Rate Schedule GS-1 ($6 million), Rate Schedule GS-3 ($12 million) and Rate Schedule LPEP ($135,000). OSBA St. 1, p. 29. OSBA refers to this approach as First Dollar Reduction.

[12] See OSBA St. 1, p. 27.

OSBA's proposed revenue requirement allocation is influenced by its reliance on PPL Electric's cost of service study which uses the same methodologies that PPL Electric has used in prior proceedings (Ex. JMK-2B). As explained in the previous section of this Initial Brief, PPL Electric's preferred cost of service study in this proceeding includes certain refinements/improvements that make it more precise and more accurate than the studies used in prior proceedings. For this reason, this study should be used as the primary tool in allocating revenue requirement among the rate classes, because it is more accurate than PPL Electric's prior methodology while avoiding abrupt changes in methodologies.[13]

In any event, the ALJ and the Commission should reject the rate decreases proposed by OSBA in its First Dollar Relief scaleback proposal. As OSBA has acknowledged, the allocation proposed by PPL Electric at proposed rates is directionally reasonable and that it would not be reasonable to move all rate classes to the system average rate of return in this proceeding. OSBA St. 1, p. 25. OSBA acknowledges further that it is not necessary to move all rate classes to the system average return in order to comply with the *Lloyd* decision. Moreover, simple fairness dictates that, if the residential customers are to receive the entire or almost the entire increase, they should be the primary beneficiary of any scaleback. OSBA's proposal to assign the entire

[13] If the Commission decides that it is appropriate to rely primarily on the cost of service study presented in Exhibit JMK-2B, then the revenue allocation should be revised in two respects: (1) the entire amount of the increase should not be allocated to the residential class; and (2) some portion of the increase should be allocated to Rate Schedules LP-4/ISP, LP-5 and LP-6. One means to achieve this result would be to start with the OSBA proposed allocation at the full requested revenue increase and proportionally scale back this proposal to reflect the settlement rate increase of $77.5 million, *i.e.*, multiply the OSBA increases by 67.6% ($77.5 million/$114.675 million). To reflect the settlement regarding Rate Schedule RTS, the Commission would cap the increase to Rate RTS at 150 percent of the scaled back RS percentage increase. The difference between this capped RTS increase and the proportional scale back increase to RTS would be allocated to Rate RS. In addition, the OSBA proposed increase to Rates LP-5 and LP-6 would be fairly substantial on a percentage basis ($1.2 million ÷ $1.57 million (PPL Electric Ex. JMK-2B, p. 9) = 76%) . To avoid this result, some additional increase could be allocated to Rate Schedule LP-4/ISP. Total revenue for this class at present rates is approximately $36.521 million (PPL Electric Ex. JMK-2B, p. 8) and a 10% increase, for example, would be $3.651 million as compared to the $2 million proposal of OSBA at the full requested increase.

benefit of the first $18.1 million of any rate reduction to customers under Rate Schedules GS-1, GS-3 and LPEP is inappropriate because those customers would receive no increase under either PPL Electric's or OSBA's proposed allocations of the initially proposed rate increase. Further, the concept of giving these rate classes the entire benefit of the first $18.1 million of any reduction in revenue requirement, regardless of the total amount of the reduction, is arbitrary and should be rejected. Other principles such as gradualism and value of service are still entitled to some weight. OSBA St. 1, p. 23. PPL Electric's proposed allocation is reasonable, and no decrease in rates is necessary to move rate classes substantially closer to the system average rate of return.

4. OCA's Proposed Allocation

The OCA also proposed a different allocation of revenue requirement:

Rate Class	OCA ($000)	PPL Electric ($000)
RS/RTS[14]	89,800	114,638
GS-1	0	0
GS-3	16,166	0
LP-4/ISP	7,036	2
LPEP	0	0
LP-5, LP-6	1,382	35
Lighting	0	0

[14] OCA's allocation of $89.8 million is for both Rate Schedules RS and RTS. The OCA did not separately allocate revenue requirement to Rate Schedule RTS. Instead, it proposed to limit the percentage increase to the RTS rate classes to 150 percent of the percentage increase to the RS Rate Class. OCA St. 3, pp. 37-38.

OCA's proposed allocation of PPL Electric distribution revenue requirement is clearly strongly influenced by its two cost of service studies, both of which should be disregarded for the reasons explained more fully above. In summary, OCA's Demand Non-coincident peak study, under which all distribution plant is classified as demand-related should be rejected because it is based on the assumption that there is no customer component of distribution plant, contrary to the NARUC Manual, general industry practices and decisions of this Commission in prior PPL Electric rate proceedings.

Similarly, OCA's Peak and Average Study should be disregarded because there is no credible argument that investment in plant is made to meet average or annual customers loads, *i.e.*, the peak and average study is not based on cost causation. Although OCA states that it does not recommend the peak and average study (OCA St. 3-S, pp. 1-2), it clearly relied on the study. This conclusion is most clearly demonstrated by OCA's proposed $16 million rate increase to the GS-3 Rate Class. The OCA presents four cost of service studies: (1) PPL 67% Customer NCP (Non-coincident Peak), (2) PPL Prior Method Primary at 100% Demand NCP, (3) OCA 100% Demand Peak and Average and (4) OCA 100% Demand NCP. All of these studies except the peak and average study show the GS-3 Rate Class producing a rate of return that is substantially above the system average rate of return at present rates. Only the OCA's peak and average study shows Rate GS-3 producing a return below the system average. Yet, the OCA proposes a substantial $16 million, 13.71 percent increase for the GS-3 Rate Class. This increase can only be justified if Rate GS-3 is currently producing a return that is below the system average and only the OCA's peak and average method shows such a result. OCA, despite it protests to the contrary, has placed substantial reliance on its flawed peak and average study. OCA St. 3, p. 29. Since there is no basis for adopting a peak and average cost of service study on the facts of this

case, OCA's proposed allocation of PPL Electric's revenue requirement also is entirely without credible record support and should be rejected.

5. Scaleback of Rates

As indicated above, PPL Electric and certain other parties filed with the Commission on August 26, 2010, a Joint Petition for Partial Settlement of Rate Investigation. There, PPL Electric agreed to an increase in annual distribution operating revenues of $77.5 million in lieu of the original proposed increase of $114.7 million. Obviously, PPL Electric's original allocation of its proposed increase in distribution annual operating revenues must be scaled back to reflect the reduced rate increase provided for in the Settlement.

As explained above, PPL Electric's proposed allocation of the original annual distribution operating revenue increase of $114.7 million was to allocate the entire increase to the residential class. In PPL Electric's view, because the residential rate classes would have received the entire rate increase under PPL Electric's filing, the residential rate classes should benefit from the entire scaleback of the original proposed increase in annual distribution operating revenues. Under PPL Electric's preferred costs of service study, PPL Electric Ex. JMK-2A, all rate classes at proposed rates show substantial movement toward the system average rate of return. PPL Electric St. 8-RJ, p. 9.

C. TARIFF STRUCTURE

1. No Special Rate Should Be Implemented For Donsco

Donsco claims that it is entitled to a special rate. This claim should be rejected for the many reasons set forth below. Two points, however, should be emphasized at the outset. First, Donsco is not complaining about any rate *proposed* by PPL Electric in this proceeding. Instead, it seeks relief from the expiration of the time-of-day option under Rate Schedule LP-4 and similar generation-related discounts in distribution rates, all of which expired on December 31,

2009, with the generation rate caps. The expiration of these generation-related discounts in distribution rates became effective pursuant to tariff provisions approved by the Commission as part of the settlement of PPL Electric's restructuring proceeding in *Application of Pennsylvania Power & Light Company for approval of Restructuring Plan under Section 2806 of the Public Utility Code*, Docket No. R-00973954 (August 27, 1998). Because Donsco is not challenging any rate proposal of PPL Electric in this proceeding and instead is seeking relief from existing rates by advancing its own rate proposal, Donsco bears the burden of proving that it is entitled to a special rate. See Section I.B., *supra.* As explained in detail later in this section of the Initial Brief, Donsco has failed to meet its burden of proof, and its request for a special rate should be rejected.

Second, Donsco's claim that it is unique and deserves a special rate is not an issue of first impression. Other customers have presented such claims in the past, the standards for recovering such requests are well established, and such requests have been rejected repeatedly. The fact that Donsco is a relatively large LP-4 customer, allegedly has certain unique circumstances, and may have a low cost of service (produces a high rate of return), even if proven (which they have not been in this case) would not support a separate rate for Donco. As the Commonwealth Court stated in *Southeastern Pennsylvania Transportation Authority v. Pa. P.U.C.*, 470 A.2d 1092, 1094-95 (Pa. Cmwlth. 1984), in affirming the Commission's rejection of a special rate for SEPTA:

> In support of its argument for a separate mass transportation rate, SEPTA points to its unique service characteristics. The Commission, in adopting the ALJ's decision, rejected SEPTA's claim for a separate rate. The ALJ noted that SEPTA attempted to show its uniqueness without examining other High Tension (HT) customers. The ALJ further noted that the mere fact SEPTA may contribute a rate of return greater than the system average dos not mean it deserves a special rate. We agree. We rejected a similar

> argument in *United States Steel Corp. v. Pennsylvanian Public Utility Commission*, 390 A.2d 849 (Pa. Cmwlth. 1978). There, U.S. Steel requested a separate rate, presenting two substantial factors demonstrating its uniqueness: (1) its average gas usage was more than eighty-seven times higher and thirty times higher than the average usage of the two rate classes with which it was to be combined, and (2) it received gas service directly from the gas transmission pipeline. What we stated in U.S. Steel is equally applicable to the case before us. A large volume of use does not entitle a customer to a preferred rate. Questions concerning the reasonableness of rates and the differences between rates are factual questions for the Commission whose findings must be upheld if supported by competent evidence. *U.S. Steel* at 211, 290 A.2d at 859. Moreover, the mere fact that SEPTA may contribute a rate of return greater than the class average does not mean that it deserves a special rate. *See, e.g., Part Towne v. Pennsylvania Public Utility Commission*, 433 A.2d 610, 614 (Pa. Cmwlth. 1981).

Donsco's claim for a separate rate should be similarly rejected.

Donsco is a customer of PPL Electric under Rate Schedule LP-4 which applies to large customers receiving service at 12 kV. Donsco's principal plant, in terms of consumption of electricity, is in Wrightsville, Pennsylvania. Donsco also owns and operates a smaller plant in Mount Joy, Pennsylvania, which is also a customer of PPL Electric under Rate Schedule LP-4. PPL Electric St. 8-R, p. 3.

Donsco seeks relief from changes in rates that occurred on January 1, 2010, prior to the date of the filing of this rate case, with the expiration of the generation rate caps that had been established pursuant to the Electricity Generation Customer Choice and Competition Act, 66 Pa.C.S. Ch. 28, in PPL Electric's restructuring proceeding. The Donsco Wrightsville plant was affected most importantly by the expiration of the Time-of-Day rate ("TOD") option and to a lesser degree by the expiration of the Economic Development Incentive ("EDI") rider. The Mount Joy plant was affected by the expiration of the expiration of Price Response Service. PPLICA St. 1, pp. 2-3.

These tariff provisions, although they were contained in PPL Electric's distribution rates, clearly pertained to generation. The TOD option recognized that generation costs are lower during off-peak hours, and the EDI rider was intended to promote economic development which would make greater use of generation assets. PPL Electric Ex. OGK-1A, pp. 19, 27A. These rates were legacy rates that made sense when PPL Electric was a vertically integrated electric public utility that owned and operated substantial generation facilities. Pursuant to PPL Electric's Commission-approved tariff, these generation related discounts in distribution rates expired on December 31, 2009. Since restructuring of the electric industry and since PPL Electric divested its generation facilities, it no longer makes sense for PPL Electric, an electric distribution company, to make rates offerings related to generation costs. PPL Electric St. 8-R, p. 7. Any savings related to costs of generation now should be attained through prices offered by electric generation suppliers.

Indeed, this logic underlies the unbundling of electric rates into separate distribution, transmission and generation components under Section 2804(3) of the Electricity Generation Customer Choice and Competition Act, 66 Pa.C.S. § 2804(3). The essence of unbundling is that charges for generation services, charges for distribution services and charges for transmission services should each stand on their own and not subsidize each other. For these reasons, discounts in PPL Electric's distribution rates related to generation costs pursuant to PPL Electric's Commission-approved tariff, expired with the generation rate caps on December 31, 2009.

In addition, both plants were affected by the expiration of the Remand Riders that implemented the settlement of the remand of the 2004 base rate case to the Commission pursuant

to the Commonwealth Court decision in *Lloyd.* The Remand Riders reduced rates under rate schedules for large customers and increased rates for residential customers.

In this proceeding, Donsco has proposed that a special rate be established particularly for its Wrightsville plant, although Donsco also requests that this special rate be designed such that the Mount Joy plant could qualify for it in the future. PPLICA St. 2, p. 8. An explanation of the background of the service to Donsco and the physical location of the Donsco Wrightsville plant is useful for an understanding the issues presented by Donsco's proposals in this proceeding.

Donsco's Wrightsville plant is located on the west side of the Susquehanna River in York County, across from Columbia, Pennsylvania, which is located in Lancaster County. Donsco's Wrightsville plant is located in a small piece of PPL Electric's service territory on the west side of the Susquehanna River that is supplied by 12 kV distribution lines that run from the North Columbia substation on the east side of the Susquehanna River. These 12 kV lines are attached to the U.S. Route 30 Bridge that crosses the Susquehanna River between Columbia and Wrightsville. PPL Electric St. 8-R, pp. 2-3.

In 2000, in order to meet environmental requirements, Donsco converted its process for melting iron at Wrightsville from a coke fuel and limestone flux cupola to an electric process, which substantially increased Donsco's electric load at the Wrightsville facility. PPLICA St. 1, p. 4. At about that time, representatives of Donsco and PPL Electric met to discuss the manner in which PPL Electric would serve Donsco's increased load at its Wrightsville facility. The parties discussed the possibility of 69kV service under Rate Schedule LP-5, but Donsco and PPL Electric concluded that such service would be impractical due to environmental concerns and costs.

From time to time, Donsco has approached PPL Electric with regard to the possibility of receiving 69 kV service in order to qualify for lower cost service under Rate Schedule LP-5. In order to qualify for service under Rate Schedule LP-5, the customer must receive service at 69 kV or higher voltage, and the customer must furnish and maintain all equipment needed to transform the energy from the line voltage down to the voltage at which the customer can use the electric energy in its operations. PPL Electric St. 8-R, p. 4.

PPL Electric was willing to construct the required transmission facilities, but Donsco would be required to pay the cost of the facilities needed to provide service at transmission voltage levels. Connections to PPL Electric's 69 kV transmission system are subject to the Open Access Transmission Tariff of the PJM Interconnection, Inc. ("OATT"). Under the OATT, customers connecting to the transmission system are required to pay the costs of all facilities needed for the service. PPL Electric St. 8-R, pp. 4-5; PPL Electric St. 8-RJ, p. 4.

In considering the possibility of serving Donsco at 69 kV or greater, PPL Electric considered alternatives from the North Columbia substation on the east side of the Susquehanna River and 115 kV service from a transmission line of the Metropolitan Edison Company on the west side of the river near the proposed Red Front substation. The option of serving Donsco's Wrightsville facility at 69 kV from the North Columbia substation has proven to be impractical. The crossing would require approximately two miles of new 69 kV transmission line (Tr. 416) across the Susquehanna River. This option has not proved practical due to the environmental and siting difficulties in crossing the Susquehanna River, the cost of two miles of new 69 kV transmission line and the additional cost that Donsco would incur to transform the electric energy at 69 kV to the voltage level at which Donsco can use it. Constructing a 69 kV transmission line across the Susquehanna River has proven to be impractical. PennDOT would not allow the line

to be installed on the existing bridge so it would have to be a stand-alone project. An overhead would be the least cost option, but an overhead line could adversely affect wildlife habitat and impair the scenic panorama of the river in this area. For these reasons, an overhead line is not a viable option. Nor is tunneling under the Susquehanna River a feasible option. PPL Electric estimated that the cost would exceed $10 million and that the project would take 5 to 6 years to complete. Although a submersible cable was evaluated, it turned out to be not practical from an engineering or an economic prospective. PPLICA St. 1, pp. 10-11. Similarly, the option of providing service from a Metropolitan Edison transmission line near the proposed Red Front substation was considered but was rejected due to its cost. The cost of the alternative from Metropolitan Edison would be approximately $11 million. PPLICA Cross-Examination Ex. 6. As explained above, under either option, Donsco would be responsible also for installing its own transformer to convert the electric supplies at transmission voltages to voltage levels at which Donsco could use the electric supplies for its operations.

Because 69 kV service to Donsco has proven to be impractical, Donsco and PPL Electric decided that 12 kV service would be provided pursuant to Rate Schedule LP-4. PPLICA St. 1, p. 9. In order to provide 12 kV service to Donsco, it was necessary for PPL Electric to construct two new 12 kV conductors from the North Columbia 69-12 kV substation to Donsco's Wrightsville plant. New conductors were needed because, without them, PPL Electric would not have sufficient capacity to serve both Donsco's increased load and the loads of other customers on the west side of the Susquehanna River. PPL Electric St. 8-R, p. 3. It is important to note that Donsco has not contended that 12 kV service furnished by PPL Electric has been inadequate or unreliable. Donsco here is seeking only lower rates for service and not any improvement in service.

PPL Electric was able in 2000 to serve Donsco's additional load at a minimal cost for new facilities. The nearest source of supply to meet Donsco's increased load was PPL Electric's North Columbia 69-12 kV Substation. In order to provide increased 12 kV service to Donsco, it would be necessary to transform 69 kV electricity to 12 kV. PPL Electric, however, was able to avoid the necessity for the acquisition and installation of a new, additional 69-12 kV transformer at the North Columbia substation to serve Donsco by reconfiguring the substation to free up one transformer that could be dedicated to serving Donsco. To accomplish this result, PPL Electric rearranged all the existing 12 kV lines so that they could be supplied from other existing transformers at the substation. The remaining transformer was then configured to serve Donsco exclusively. PPLICA Cross Examination Exhibit 6.

In order to provide PPL Electric with a reasonable cash flow from the new facilities for serving Donsco, pursuant to PPL Electric's tariff, Donsco was required to enter into a five-year line extension guarantee. PPL Electric Ex. OGK 1, pp. 7B-8A, Rule 4. After three years, however, Donsco and PPL Electric terminated the line extension agreement in exchange for an agreement that service to Donsco could be interrupted when necessary to continue service to other customers in the area. After that time, Donsco paid PPL Electric only about $40,000 annually in distribution rates under Rate Schedule LP-4 (Tr. 419-420), which is far less than the revenue requirement associated with the new facilities that were constructed to provide 12 kV service to Donsco, which cost in excess of $1 million. PPLICA Cross Examination Exhibit 5.

PPLICA has cited Section 2806(h) of the Electricity Generation Customer Choice and Competition Act for the proposition that the Commission may approve flexible prices, including contract based tariffs with negotiated rates designed to meet the specific needs of a customer and address competitive issues. PPLICA St. 2-S, p. 2. PPLICA, however, has not cited, and cannot

cite, any authority for the proposition the PPL Electric can be required to agree to such a rate, especially where is would be inappropriate to do so.

No special rate is appropriate for Donsco. Such rate would be unfair to other customers in at least three different respects. First, rates for other customers being served on Rate Schedule LP-4 would have to increased to offset a rate reduction for Donsco and other similarly-situated customers who could qualify for any rate beneficial to Donsco. In fact, under Donsco's proposal, other LP-4 customers would be required to pay higher rates even though they would not receive any additional benefits. PPL Electric St. 8-R, p. 6. Second, such a rate would not be fair to other former LP-4 customers who paid the costs, often significant,[15] of installing 69 kV facilities in order to be eligible for service on Rate Schedule LP-5, which has significantly lower rates because none of the costs of the 12 kV secondary distribution system are allocated to service at 69 kV or greater voltages under Rate Schedule LP-5. PPL Electric St. 8-R, p. 6. Third, even Section 2806(h), which PPLICA cites in favor of its contentions, recognizes the competitive effect of rate reductions. A rate reduction for Donsco would be unfair to its competitors, *i.e.*, other forges, unless similar rate reductions were made available to the other forges, which would have the effect of increasing the burden to be shifted to other customers of PPL Electric under Rate Schedule LP-4, which are not forges.

Donsco argues that it is entitled to a special rate because present rates have caused it to experience hardships and because special circumstances apply to it. Donsco's claim is legally and factually flawed. Donsco's proposal for a special rate is in essence a claim that present rates are unreasonably discriminatory as to Donsco. As a legal matter, in order to prove unreasonable

[15] Such payments have at times in exceeded $10 million. PPL Electric, St. 8-R, p. 5.

rate discrimination, a customer must show that its rates are unreasonably high and that rates of other customers are unreasonably low. As the Commission has stated:

> The Commonwealth Court has repeatedly held that the proponent of a charge of unlawful rate discrimination must demonstrate that certain customers are paying an unreasonably high rate in order to make up a deficiency created by unreasonably low rates charged to other customers. *Building Owners and Managers Assoc. v. Pa. P.U.C.*, 470 A.2d 1092, 1096 (Pa. Cmwlth. 1984); *Manufacturers Assoc. of Erie v. Pa. P.U.C.*, 407 A.2d 114, 116 (Pa. Cmwlth. 1979); *Phila. Suburban Trans. Co. v. Pa. P.U.C.*, 281 A.2d 179, 186 (Pa. Cmwlth. 1971).

Pa. P.U.C. v. Pennsylvania-American Water Co., Docket Nos. R-00943231, *et al.*, 172 Pa. PUC 160, 1996 Pa. PUC LEXIS 141 at *17 (June 6, 1996). *See also Building Owners and Managers Association v. Pa. P.U.C.*, 470 A.2d 1092, 1096 (Pa. Cmwlth. 1984). Donsco has presented no cost basis for any conclusion that existing rates are unreasonable as to it or that any other customers are paying unreasonably low rates. Even if Donsco's claims of hardships and special circumstances were valid, which they are not as explained next, Donsco has failed even to address matters that are required to sustain a claim of rate discrimination. For this reason alone, Donsco's claim should be rejected.

As a factual matter, Donsco's claim of unfair treatment also is without merit. Prior to January 1, 2010, Donsco took advantage of the TOD option under Rate Schedule LP-4 by shifting its operations to off-peak periods. In addition, Donsco benefited from the EDI rider. Both the TOD option and the EDI rider expired on December 31, 2009. Tr. 456. In addition, Donsco had benefited from "Remand Riders 1 and 2" which reduced distribution costs through December 31, 2009 under the settlement of the remand at PPL Electric's 2004 distribution rate case after the Commonwealth Court decision in *Lloyd*. PPLICA St. 1, p. 6.

It is true that the simultaneous expiration of these three tariff provisions resulted in a significant increase in distribution charges applicable to Donsco. The elimination of the TOD

option, EDI rider and Remand Riders caused increases in distribution charges from approximately $2,500 per month to approximately $27,500 per month. The effects of the expiration of the TOD option and the EDI rider alone, without regard to the expiration of the Remand Riders, was an increase in monthly distribution charges from approximately $5,500 per month to approximately $27,500 per month. PPLICA St. 1, p. 7.

It is important to note that the principal tariff provision that reduced Donsco's distribution rates prior to January 1, 2010, was the TOD option. This provision, however, reflects benefits that are primarily generation-related. The TOD option was appropriate and reasonable when PPL Electric was a vertically integrated utility and that owned generation facilities and provided generation services using those facilities.

After the restructuring of the electric utility industry in Pennsylvania, however, PPL Electric, with Commission approval, sold its generation facilities. To the extent that a customer's operations reduce costs to generators, such as operations that use electricity during off-peak periods, the customers should receive prices reflecting those cost reductions from the generators – the electric generation suppliers – and not from a distribution company such as PPL Electric. For these reasons, it is no longer appropriate for such generation-related discounts to be included in PPL Electric's distribution rates. PPL Electric St. 8-R, p. 7.

Discounts in distribution rates were practical and workable when all electric services were provided by vertically integrated and subject to a cost of service regulatory regime. With the Electricity Generation Customer Choice and Competition Act, however, Pennsylvania adopted a competitive regime for generation services and, as part of that transition, required unbundling of rates for generation services. Under a competitive generation pricing regime, it is

appropriate for Donsco to enter the competitive market for electric generation supplies and obtain such supplies under the terms and conditions most favorable to it, as it has done.

Although Donsco has claimed economic hardship from the increases in distribution rates effective January 1, 2010, there is no record evidence as to its specific cost of generation services. Clearly, the "hardship" claimed by Donsco is not as great as Donsco would have the ALJ and the Commission believe for at least two reasons. First, even after all the distribution rate increases about which Donsco complains, distribution rates are only about 20 percent of Donsco's total cost of electricity. PPL Electric St. 8-RJ, p. 7. Prior to January 1, 2010, and the 900 percent distribution rate increases about which Donsco complains, it was paying closer to 2 percent of its total electric bill for distribution services.

Second, although the record does not reflect the level of Donsco's generation charges, it is clearly purchasing generation at a favorable price. Although the TOD option utilized by Donsco prior to January 1, 2010 has expired, PPL Electric does currently offer a "Real Time Price" option for generation supply charges for large commercial and industrial customers such as Donsco. See, PPL Electric Ex. OGK 1A, p. 19Z.3C. – 19Z.3D. Under this option, customers pay actual costs of electric generation when they utilize generation supplies. Therefore, a customer, such as Donsco, that can shift its operations to off peak periods, when cost of generation supplies are lower, will benefit through lower charges for generation services from PPL Electric. Despite the availability of such services from PPL Electric, Donsco chose instead to purchase its electric generation supplies from an Electric Generation Supplier. PPL Electric St. 8-R, p. 7. Clearly, Donsco anticipates that the prices for generation supplies from its electric generation supplier will be more favorable to it than even PPL Electric's Real Time Price option.

Donsco should not be allowed to have it "both ways." In essence, it want to return to distribution rate levels that were set when electric rates were fully regulated and distribution rates contained discounts related to generation costs and at the same time have all of the benefits of a competitive generation market. Limiting Donsco to generation prices as the source of discounts for generation services will cause no hardship. It merely prevents Donsco from "double dipping" for generation savings in both regulated distribution services and competitive generation services.

Nor is Donsco's claim of "special circumstances" valid. The "special circumstances" that Donsco claims apply to it are summarized at, *inter alia*, PPLICA St. 2, p. 7. The first circumstance is that its demand, 4MW (megawatts), is reasonably consistent with the demands of customers served under Rate Schedule LP-5. PPL Electric, however, serves approximately 20 customers under Rate Schedule LP-4 with demands of 4 MW or greater. Tr. 415. The second circumstance cited by Donsco is that lower distribution rates would enhance prospects for economic development, load retention and employment. Lower distribution rates for every business customer, however, would make additional resources available to the customer for other purposes, including economic development, load retention and employment. Donsco's second factor does not distinguish it from any other business customer of PPL Electric. The third special circumstance cited by Donsco is that its conversion to 69 kV service is not economically or environmentally feasible. Again, this circumstance does not distinguish Donsco from other large LP-4 customers of PPL Electric because all larger LP-4 customers would benefit from switching to LP-5 service if there were no economic or environmental impediments. Tr. 415. The fourth factor cited by Donsco is the proximity of its Wrightsville plant to 69 kV facilities. As indicated previously, however, the Donsco Wrightsville plant is approximately 2 miles from

the closest 69 kV facility, and it is not unusual for LP-4 customers to be within 2 miles of 69 kV facilities. Tr. 415-16. The fifth factor cited by Donsco is the fact that it entered into a line extension guarantee agreement in approximately 1999 regarding the extension of 12 kV service to Donsco. This circumstance does not justify special treatment of Donsco for three separate reasons. First, even a line extension guarantee does not cover the cost of the facility. The guarantee calls for payment only of a portion of the total cost of providing service which includes the facilities that are specifically constructed to serve the customer as well as all other shared facilities and costs of service including, for example, billing systems, customer service representatives, maintenance, transformers, *etc.* It is simply not correct that a customer who enters into a line extension guarantee agreement and fulfills his obligations under that agreement has paid for the facilities constructed to serve it. PPL Electric St. 8-RJ, p. 6. Second, Donsco did not fulfill its obligations under the extension guarantee. Instead, Donsco requested relief from the last two years of the line guarantee agreement, thereby saving itself approximately $280,000, in total. PPL Electric St. 8-RJ, p. 2. Donsco has not demonstrated any special circumstance that would justify a special distribution rate for it. Third, Donsco paid nothing for the 69-12 kV transformer that has been dedicated to its service since 2000. PPLICA Cross Examination Ex. 5.

Another shortcoming of Donsco's proposal is that it has provided no cost justification for any rate discount or special rate. Donsco has provided no insight into the level of costs that should be recovered through a rate charged to it. Such information would be critical it determining a rate that could be charged to Donsco. Although PPL Electric has not conducted a study of the costs of serving Donsco at its Wrightsville plant, there is every reason to believe that no discount could be justified on the basis of cost. As explained previously, PPL Electric

invested more than $1 million in 12 kV distribution facilities to extend 12 kV service to Donsco in 2000. The investment to serve Donsco, however, was much greater. The cost of the extension did not include the cost of the 69-12 kV transformer at the North Columbia substation that has been dedicated exclusively to its service. PPLICA Cross-Examination Ex. 5. It would also be necessary for PPL Electric to recover through rates charged to Donsco the appropriate portion of shared costs that PPL Electric incurs to serve all customers, including Donsco.

Nor has Donsco proposed any specific rate. Therefore, the ALJ, the Commission and PPL Electric have no basis to determine revenue from the unknown discounted rate to use in its proof of revenues to develop rates for other customers. Donsco did in its testimony mention a specific monthly bill for distribution charges of $4,562. Donsco St. 2-S, p. 5. This amount, however, was simply Donsco's average monthly bill for distribution services during 2009 and was provided for illustration only. Donsco stated that it was not Donsco's calculation of the correct amount under criteria described by OSBA. Donsco St. 2-S, p. 5, fn. 2. Donsco merely used this amount to calculate the rate increase to other LP-4 customers that would be necessary to offset the loss of revenue that would result from reinstituting Donsco rates that were in effect prior to January 1, 2010. Donsco's calculation is meaningless and certainly would not justify any special rate for Donsco.

These shortcomings in Donsco's evidence are important particularly in light of the fact that Donsco, as explained above, bears the burdens of proof and persuasion that its proposal for a special rate is just and reasonable. Donsco has failed to meet its burden of proof, and its request for a special rate should be denied.

2. Rate Design

a. Rate Schedule GS-3

REG raises concern with PPL Electric's proposed rate design for Rate Schedule GS-3. REG contends that the proposed rate design will produce a rate increase for most GS-3 customers and a rate decrease for only the largest customers in the class. REG St. 1, pp. 3-4. REG therefore recommends that PPL Electric adjust the demand charge so that all GS-3 customers will have no increase in rates. REG St. 1, p. 4. As explained below, PPL Electric's proposed rate design follows the cost of service study and REG's proposal makes no sense.

Under PPL Electric's current Rate Schedule GS-3, all of the distribution revenue requirement is recovered through demand charges. PPL Electric St. 8, pp. 13-14. In this proceeding, PPL Electric proposes to redesign the rate to include both customer and demand charges. PPL Electric St. 8, p. 13. Under the proposed rate design for Rate Schedule GS-3, the customer charge will be $50 and the demand charge will be reduced from $4.677/kWh to $4.266/kWh. PPL Electric Ex. OGK-2, p. 6. Since PPL Electric has not proposed any increase in total revenue for Rate Schedule GS-3 as a whole, PPL Electric St. 8-R, p. 33; PPL Electric St. 8-R, Appendix C, these charges remain the same at the agreed to $77.5 million distribution rate increase. If the Commission decides to allocate some portion of the increase to Rate GS-3, then these charges would be proportionately increased in the Company's compliance filing.

PPL Electric is purely a transmission and distribution entity that delivers electricity to retail customers. At a given voltage level, the costs of providing transmission and distribution delivery service does not vary with the amount of energy consumed or the pattern of that consumption. PPL Electric 8-R, p. 8. The goal of PPL Electric's proposed rate design was to move toward rate designs that recover fixed costs through fixed charges and those costs that vary as a function of usage through usage charges. PPL Electric St. 6-R, p. 21. It is appropriate, from

the perspective of customers, utilities, and the Commonwealth, to collect fixed costs on a fixed-charge basis. PPL Electric St. 6, p. 26.

In this proceeding, PPL Electric is proposing to continue to move towards distribution rates that are more demand and customer dependent and less usage-based. PPL Electric St. 8, p. 11. The customer charge proposed for Rate Schedule GS-3 recovers the full customer component (customer related cost) of the rate class, and the demand charge recovers the demand related components. PPL Electric St. 8-R, p. 32. Increased reliance on customer and demand charges for Rate Schedule GS-3 customers is appropriate because it reflects cost causation more accurately than the present rate design. PPL Electric St. 8-R, pp. 32-33.[16] PPL Electric's proposal to implement customer charges and reduce the demand charge for Rate Schedule GS-3 also is consistent with *Lloyd*, which held that rate structures should be adjusted to reflect the cost of service to each rate class and to eliminate cross-subsidization of rate classes.

REG does not appear to oppose the addition of a customer charge to Rate GS-3. As Mr. Richards candidly states:

> I do not dispute the fact that the revenue provided to the company by both the GS-1 and GS-3 classes as a whole has remained the same. I also accept the fact that in any intra-class rate realignment there will be individual winners and losers.

REG St. 1, p. 3. However, with respect to Rate Schedule GS-3, REG is concerned that the Company's proposed rate design will produce small rate increases for most customers and will produce rate decreases for only the largest customers in the class. REG St. 1, pp. 3-4. To address this concern, REG requests that PPL Electric, to the extent possible, be required to adjust

[16] Indeed, REG does not disagree with PPL Electric's attempt to more accurately reflect its operations by moving toward customer and demand charges. REG St. 1, p. 2.

the demand charge in Rate GS-3 to reflect a zero increase for all GS-3 customers. REG St. p. 4. REG's proposal should be rejected for the following reasons.

First, as explained above, PPL Electric's proposed rate design follows cost of service. REG does not dispute that PPL Electric's rate design follows the cost of service and has presented no evidence that the proposed increases and decreases within Rate GS-3 are unreasonable or violate principles of gradualism in rate design.

Second, REG's proposal makes no sense. The only way to achieve REG's goal of no increase to any individual GS-3 customer would be revert to the current demand charge only rate structure. The addition of a customer charge to the rate will, as Mr. Richards acknowledged in the above-quoted passage, produce increases for some customers and decreases for others even with total class revenue held constant. The only "possible" way to implement REG's proposal is to completely reject PPL Electric's proposal and revert to a demand charge only rate that does not accurately reflect cost of service.

Based on the foregoing, PPL Electric's proposal with respect to Rate Schedule GS-3 is just and reasonable and, therefore, should be approved

b. Rate Schedule(s) GH-1 and GH-2

As explained below, PPL Electric and OSBA have resolved most of the issues related to Rate Schedules GH-1 and GH-2. OSBA's remaining proposal regarding the GH rate classes should not be adopted. The GH-1 Rate Schedule is for commercial space heating service available only to customers who use electricity for all of their energy requirements, including space heating. Rate Schedule GH-2 is for customers with separately method heating loads who take the remainder of their electric service under Rate Schedule GS-1 or GS-3. Rate Schedules GH-1 and GH-2 have been closed to new customers since August, 1972. Presently, about 827 customers are served under Rate Schedule GH-1. OSBA St. 1, p. 32.

PPL Electric proposed in this proceeding to adopt a rate design for Rate Schedule GH-1 that is similar to the proposed rates for service under Rate Schedule GS-3. That is, rates under Rate Schedule GH-1 would be changed to include a $50 customer charge and eliminate the minimum billing demand. PPL Electric further proposed to set the demand charge for GH-1 service slightly above the demand charge under Rate Schedule GS-3.

OSBA, in contrast, proposes to eliminate Rate Schedule GH-1 and require all current customers to move to Rate Schedule GS-3. Because the billing demand rate under Rate Schedule GH-1, at proposed rates, is slightly higher than the billing demand under Rate Schedule GS-3, under OSBA's proposal, PPL Electric would experience some reduction in revenue if OSBA's proposal were adopted. OSBA proposes that any revenue shortfall be recovered through rate increases to customers served under Rate Schedule GH-2. OSBA St. 1, pp. 36-37.

PPL Electric opposed OSBA's proposal to eliminate Rate Schedule GH-1 for several reasons. PPL Electric St. 8-R, pp. 21-24. Upon review, OSBA agreed that Rate Schedule GH-1 can remain in effect. OSBA St. 3, p. 9.

In order to resolve any rate issues related to the potential migration of customers served under Rate Schedule GH-1 to GS-3, PPL Electric proposed to make the rates in Rate Schedule GH-1 equal to rates in Rate Schedule GS-3 and increase the demand charges of Rate Schedule GS-2 to compensate for the Rate Schedule GH-1 rate reduction. In this way, potential revenue effects of migration of customers from Rate Schedule GH-1 to GS-3 would be mitigated, and customers would not be required to move from Rate Schedule GH-1 to Rate Schedule GS-3 which could adversely affect price offers from EGSs. PPL Electric St. 8-R, p. 24. OSBA accepted also this proposal of PPL Electric. OSBA St. 3, p. 9. This issues also appears to be resolved.

OSBA, however, continues to argue that all GH-1 customers should be allowed to migrate to Rate Schedule GS-3. As OSBA acknowledges, however, certain customers under Rate Schedule GS-3 receive single phase service. Such customers were grandfathered under Rate Schedule GS-3 and have not been required to move to Rate Schedule GS-1 which was designed to serve single phase customers. OSBA St. 1, p. 36. PPL Electric opposes any proposal which would permit additional single phase customers to be served under Rate Schedule GS-3. Rate Schedule GS-3 was specifically designed for serving three phase customers, and Rate Schedule GS-1 was designed for serving single phase customers. The fact that a few grandfathered single phase customers are served under Rate Schedule GS-3 is an historical anachronism that, if anything, should be eliminated and not enlarged. There is no cost basis for permitting additional single phase customers to be served under Rate Schedule GS-3. PPL Electric St. 8-R, pp. 22-23.

3. Billing Demand

a. The Definition of Billing Demand

REG raises concerns regarding the definition of billing demand or billing kW in Rate Schedules GS-1 and GS-3. REG St. 1, p. 5. PPL Electric agrees with the concerns raised by REG and agrees to correct the definition of "Billing kW" in Rate Schedules GS-1 and GS-3 as explained below.

PPL Electric's Supplement No. 83 defines "Billing kW" for Rate Schedules GS-1 and GS-3.

> The Billing KW for the Competitive Transition Charge and Transmission components are the average number of kilowatts supplied during the 15-minute period of maximum use during the current billing period.

PPL Electric Ex. OGK-1, pp. 24A, 25. However, as explained in rejoinder, the word "Transmission" will be changed to "Distribution." PPL Electric 8-RJ, p. 9. As a result, the definition of "Billing kW" for Rate Schedules GS-1 and GS-3 will provide as follows:

> The Billing KW for the Competitive Transition Charge and Distribution components are the average number of kilowatts supplied during the 15-minute period of maximum use during the current billing period.

In all other respects, the definitions of demand or billing kW in Supplement No. 83 are correct.

b. The Determination of Billing Demand under Rate Schedules GS-1 and GS-3

REG suggests that demand charges to all customers under Rate Schedules GS-1 and GS-3 be based on the hour of highest use instead of the 15 minutes of highest use during a billing month. REG contends that a switch to hourly demand would conform to pricing signals and other components of certain bills. REG St. 1, p. 5. For the reasons that follow, REG's recommendation is impractical and should be rejected.

PPL Electric currently bills GS-1 and GS-3 customers on 15-minute increment demands. PPL Electric St. 8-R, p. 30. For billing purposes, PPL Electric uses data from the meter's demand register. The demand register saves that greatest usage during any 15-minute interval. When a new level of highest use in an interval occurs, the register replaces the prior level of usage, which information is not retained in the register. That process is repeated until the register is reset at the next meter reading. PPL Electric St. 8-R, p. 31.

Although the electronic memory in the meters presently installed at Rate Schedule GS-1 and GS-3 customers' premises do save information regarding hourly usage, the saved data is not sufficiently reliable to be used for billing purposes. PPL Electric St. 8-R, p. 31. Unlike the demand register, the meter's electronic memory saves hourly data for three eight hour periods. If the data is not successfully transmitted to PPL Electric's Automated Meter Reading ("AMR")

billing system within the three eight-hour periods, the meter begins to save data from the next eight-hour period and erases the data from the first eight hour period. PPL Electric St. 8-R, p. 31. However, it is not uncommon for data from the electronic memory, as distinguished from the demand register, to be lost due to delays in transmitting the data. Transmissions can be interrupted due to delays caused by even brief outages. Therefore, hourly usage information from the electronic memory often is incomplete. In addition, the data saved in the electronic memory is rounded. Between transmission delays and rounding, the data from the electronic memory is simply not sufficiently reliable to be used for billing purposes. PPL Electric St. 8-R, p. 31.

REG's proposal to switch to hourly demand for GS-1 and GS-3 customers is impractical because it would require expensive new metering at all premises of all customers who pay demand charges.[17] PPL Electric St. 8-R, p. 30. In order to implement REG's proposal, it would be necessary for PPL Electric to replace meters at premises of all customers who pay demand rates. Presently, that would involve replacing more than 200,000 meters. The cost of such meters is approximately $130 each, including the installation cost. Further, REG's proposal would require substantial reprogramming of PPL Electric's billing system and reprogramming of the automated meter reading system. PPL Electric St. 8-R, p. 32. Finally, it would not be practical to implement hourly interval billing in this proceeding because PPL Electric does not know what the number of demand billing units would be, and therefore, sufficient information is not available to design rates. PPL Electric St. 8-R, p. 32.

[17] The only exceptions would be at the premises of a few very large customers where more sophisticated and expensive meters and related equipment have already been installed. PPL Electric St. 8-R, pp. 30-31.

Based on the foregoing, REG's proposal to implement demand charges based on the hour of highest use instead of the 15 minutes of highest use during a billing month for all customers under Rate Schedules GS-1 and GS-3 is impractical and should be rejected.

4. Net Metering

In this proceeding, PPL Electric is proposing to make several changes to its Net Metering Renewable Customer-Generators Rider ("Net Metering Rider") to coordinate that provision with the Alternative Energy Portfolio Standards Act, Act of November 30, 2004, P.L. 1672, *as amended*, 73 P.S. §§ 1648.1-1648.8, and the Commission's regulations implementing the Act, 52 Pa. Code §§ 75.61-75.70. First, the billing provision will be revised to provide for annual payments for excess generation at PPL Electric's Price to Compare. Second, a section has been added to the Rider to set forth the conditions under which shopping customers can qualify and participate in the Company's net metering program. PPL Electric St. 8, p. 18; PPL Electric Ex. OGK-1, p. 19L.3.

As set forth in Paragraph 30 of the Settlement, SEF reserved for litigation issues related to PPL Electric's proposed Net Metering Rider. Specifically, SEF takes issue with the method for calculating compensation for generation in excess of use, as well as with the net-metering tariff language. SEF's issues are without merit and, for the reasons that follow, should be rejected.

SEF first contends that the calculation of compensation for kWh generation in excess of kWh use under PPL Electric's proposed Net Metering Rider fails to properly credit Net Metering customer's for distribution charges. SEF St. 1-S, p. 16. SEF argues that the Commission's regulations require PPL Electric to credit customer-generators for both generation and distribution charges and that the credit for distribution charges should apply to all distribution charges, including customer and demand charges. SEF St. 1-S, 13. PPL Electric disagrees. For

the reasons explained below, the credit for distribution charges should only apply to energy charges and not to customer or demand charges.

Section 75.13 of the Commission's regulations provide, in pertinent part, as follows:

> (c) The EDC shall credit a customer-generator at the full retail rate, which shall include generation, transmission and distribution charges, for *each kilowatt-hour* produced by a Tier I or Tier II resource installed on the customer-generator's side of the electric revenue meter, up to the total amount of electricity used by that customer during the billing period. If a customer generator supplies more electricity to the electric distribution system than the EDC delivers to the customer-generator in a given billing period, *the excess kilowatt hours shall be carried forward and credited against the customer-generator's* usage in subsequent billing periods at the full retail rate. Any excess kilowatt hours shall continue to accumulate until the end of the year....
>
> (d) At the end of the year, the EDC shall compensate the customer generator *for any excess kilowatt hours generated* by the customer-generator over the amount of kilowatt hours delivered by the EDC during the same year at the EDC's price to compare.

52 Pa. Code § 75.13(c), (d) (emphasis added). The plain language of Section 75.13 provides that an EDC is obligated to credit or compensate customer generators only for the excess energy or kilowatt-hour of electric usage, not the customer or demand component of a customer's bill.

Under the Net Metering Rider, the kilowatt-hours generated by the customer is automatically credited against the kilowatt-hours of usage by the two-way net metering equipment which nets customer usage and customer generation. The customer is given full retail value for the kilowatt-hours generated for distribution (if kilowatt-hour charges exist in the rate schedule), Act 129 charges, transmission, energy & capacity, and competitive transition charge. Pursuant to PPL Electric's currently effective and approved tariff, customers are responsible for the customer charge, the minimum bill, and any demand that may have been registered on the meter, even if customer generation was equal to or exceeded customer usage. PPL Electric St. 8-RJ, p. 8; PPL Electric Ex. OGK-1, p. 19L.3. As explained in the rebuttal testimony of Mr.

Kasper, over 90% of the charges on the average customer's bill are comprised of kWh charges. PPL Electric St. 8-R, p. 9. Therefore, PPL Electric is crediting over 90 percent of the distribution charges for residential customers.

These requirements have not changed in the proposed tariff. This is a reasonable and appropriate result. Net Metering customers continue to be connected to the Company's distribution system and continue to use that system both as a consumer of electricity and as a generator of electricity. The customer charge is designed to recover costs associated with connecting a customer to the system regardless of the customer usage (either as a buyer or as a seller). The demand charge is designed to recover the costs associated with the maximum demand a customer places on the system (again either as a buyer or as a seller). There is therefore no rational basis for eliminating the customer charge or demand charge as part of the Net Metering Rider. PPL Electric St. 8-RJ, p. 8. As explained above, clearly it is inconsistent with the Commission's regulations on this point, and is unnecessary given over 90% of charges are energy based.

SEF next contends that the Net Metering Rider should be revised to replace the terms "PJM" or "PJM Planning period" with the term "within 15 days of May 31 of each year." SEF St. 1, p. 11. PPL Electric believes this proposed revision is unnecessary. First, the suggested addition of the term "within 15 days of May 31 of each year" is not included in the Commission's regulation. PPL Electric St. 8-R, p. 20. Second, the term "PJM Planning period" is included in the Commission's regulations at 52 Pa. Code § 75.12. Third, the tariff language complies with the Commission regulation and the term "PJM planning period ending May 31 of each year" is already included in the Billing Provisions Section 1 of the proposed Net Metering Rider. PPL Electric Ex. OGK-1, p. 19L.3.

Finally, SEF contends that the Net Metering Rider language should be written in "plain English" so that the average utility customer is able to understand. SEF St. 1, p. 11. PPL Electric strives to make all tariff provisions clear and understandable. Moreover, the language of concern to SEF has been specifically approved by the Commission. Indeed, the Net Metering Rider was revised pursuant to the Commission's July 26, 2007 Secretarial Letter. It should also be noted that PPL Electric has not received any customer complaints or expressions of concern regarding the tariff language that is the subject of SEF's contentions. Thus, customers seem to understand the net metering provisions of the tariff and interpret them in a manner that is consistent with PPL Electric's intent. PPL Electric St. 8-R, pp. 19-20.

D. THE AVAILABILITY OF CERTAIN DATA TO CUSTOMERS AND ELECTRIC GENERATION SUPPLIERS

REG contends that PPL Electric should be required to make certain data available to GS-1 and GS-3 customers and to EGSs. Specifically, REG recommends that PPL Electric be required to make annual Peak Load Contributions and annual Transmission Obligations available online. REG St. 1, pp. 5-6. However, PPL Electric is not required to present any customer billing history on the web other than the Eligible Customer List. PPL Electric St. 8-R, p. 33.

The Eligible Customer List is available online to suppliers and aggregators, such as REG. Although it is not required to do so, PPL Electric also provides the customer billing history to customers through the customer web interface as a service to its distribution customers. PPL Electric St. 8-R, pp. 33-34. The PPL Electric customer web interface is a customer information system that maintains two years of data online. Historic data over two years old is archived and not available online for presentation, hence such data is not available to the customer web interface. Any data older than two years, up to 4 years, is only available by special request. PPL Electric St. 8-R, pp. 33-34.

The Peak Load Contribution and Transmission Obligation values are available in the Eligible Customer List, which, as explained above, REG has access to as a supplier or aggregator. PPL Electric only uses these values to bill Transmission Obligation and Capacity Obligation if a large C&I customer is taking POLR service from the Company at real-time rates. However, the Peak Load Contribution and Transmission Obligation values are not stored in the customer records in the PPL Electric customer information system, and therefore, would not be available to customers through the customer web interface. PPL Electric St. 8-R, p. 34.

For these reasons, REG's proposal that PPL Electric should be required to make certain data available to GS-1 and GS-3 customers and to EGSs should be rejected.

IV. MISCELLANEOUS ISSUES

A. AREAS OF CONCERN FROM THE COMMISSION'S MAY 20, 2010 ORDER

In Appendix A to its May 20, 2010 Order initiating an investigation into the Company's proposed rate increase, the Commission identified 16 areas of concern that the Parties to this proceeding should address. PPL Electric agrees with the Commission that the proposed increase in distribution base rates should be carefully examined to determine whether the request is lawful, just, and reasonable. To that end, the Parties to this proceeding have engaged in extensive discovery to thoroughly examine all the issues raised in this proceeding, including the areas of concern identified by the Commission. PPL Electric. St. 7-S, p. 2. PPL Electric herein explains its position on each of the areas of concern identified by the Commission.

1. Test Year Revenue and Expense Claims

In issue number 1, the Commission states that PPL Electric's test year revenue and expense claims must be closely examined to determine their accuracy and the extent to which they support the requested revenue increase. The Company's historic test year revenues and expenses are set forth in PPL Electric Exhibit Historic 1 and PPL Electric Statement No. 3. The Company's future test year revenues and expenses are set forth in PPL Electric Exhibit Future 1 (Revised) and PPL Electric Statement No. 2. The parties to this proceeding have engaged in extensive discovery on these materials, and all of the Company's claims have clearly been closely examined. After extensive investigation and negotiation, the parties have achieved settlement on all revenue requirement issues.

2. Capital Investment

In issue number 2, the Commission states that the level of capital investment appearing in PPL Electric's rate base claim must be closely reviewed to ensure that it was prudently made,

and that any utility plant acquired is necessary, used and useful to the provision of electric distribution service. PPL Electric's capital budgeting process was reviewed by the Commission in 2008 when it conducted a Focused Management and Operations Audit of PPL Electric Utilities Corporation at Docket No. D-2009-2102172. The Commission made no specific findings or recommendations for changes to PPL Electric's capital budgeting process. PPL Electric St. 7-S, p. 4.

PPL Electric's determination of the jurisdictional capital investments and operating expenses is set forth in PPL Electric St. No. 7 and PPL Exhibits JMK 1, JMK 2-Revised, JMK 3 and JMK 3-Revised. PPL Electric's capital budgeting process and capital spending needs are explained in PPL Electric Statement No. 2 and PPL Electric Exs. MAV 1 through MAV 5. The parties to this proceeding have engaged in extensive discovery on these materials, and all of the Company's claims have clearly been closely examined. After extensive investigation and negotiation, the parties have achieved settlement on all revenue requirement issues, including PPL Electric's capital investments and operating expenses, capital budgeting process, and capital spending needs.

3. Revenue Allocation

In issues numbered 3 and 4, the Commission states that PPL Electric's proposed revenue allocation, including the methodology for allocating revenue between Rate Schedules RTS and RS, must be carefully examined to determine whether or not it is just and reasonable. The allocation of PPL Electric's proposed increase among rate classes is explained in PPL Electric St. 6 and PPL Electric St. 8. The parties have engaged in extensive discovery on this issue. Additionally, PPL Electric's proposed revenue allocation was thoroughly examined and addressed in OSBA St. 1, OSBA St. 3, OCA St. 3, and OCA St. 3-S. PPL Electric's revenue allocation, and issues related thereto as explained above. Further, the allocation of revenue

requirement between Rate Schedules RS and RTS was resolved by the Settlement. *See* Section III.B, *supra*.

4. Rate Design

Issues numbered 5 through 8 provide that PPL Electric's proposed rate designs must be carefully examined to determine whether they are just and reasonable. PPL Electric's proposed rate design is explained in PPL Electric St. 6 and PPL Electric St. 8. As explained therein, in this proceeding, PPL Electric proposes increased recovery of revenues through customer and demand charges, and the elimination of declining usage blocks, the elimination of minimum billing kW for applicable rate schedules, and the combination of revenue requirements for certain interruptible service rate schedules.

PPL Electric provides distribution services to retail customers. At a given voltage level, the costs of providing distribution delivery service do not vary with the amount of energy consumed or the pattern of that consumption. PPL Electric 8-R, p. 8. The rate structures and prices proposed by PPL Electric are designed to recover the costs to maintain and improve the delivery system. These costs are not tied to the amount of electricity purchased, but are customer and demand related, and are incurred regardless of customer kWh or energy consumption. PPL Electric St. 8-R. p. 9. How rapidly a customer uses the energy (demand) and the basic infrastructure (customer charge) must be supported by all customers, not just the high kWh usage customers. PPL Electric St. 8-R, p. 11.

The parties have engaged in extensive discovery on PPL Electric's proposed rate designs. Additionally, the proposed rate designs have been carefully examined and addressed in OTS St. 3, OCA St. 3, OSBA St. 1, OSBA St. 3, PPLICA St. 1, PPLICA St. 2, PPLICA St. 1-S, PPLICA St. 2-S, SEF St. 1, SEF St. 1-S and REG St. 1. Importantly, the Parties have achieved a

settlement on all residential rate design issues. Remaining issues related to non-residential rate design are explained and addressed above. *See* Section III, *supra*.

5. Cost Allocation and Cost-of Service Study

In issues numbered 9 and 10, the Commission indicates that the Parties should scrutinize the cost allocation methodologies utilized in PPL Electric's class cost-of-service study and determine whether they support the Company's proposed revenue allocation and rate design. The Company's cost allocation studies are explained in PPL Electric St. 7 and PPL Electric Exs. JMK 1 and JMK 2-Revised, as well as JMK-2A and JMK-2B, which provide specific details regarding the assignment and allocation of PPL Electric's transmission and distribution costs, and the determination of the Pennsylvania jurisdictional distribution service revenue requirements on a system and rate class basis.

The Parties engaged in extensive discovery on issues related to revenue allocation and cost of service. Additionally, the Company's cost allocation and cost-of-service study was thoroughly examined and addressed in OTS St. 3, OCA St. 3, OCA St. 3-S, OSBA St. 1, and OSBA St. 3. Although the parties were able to achieve settlement on all revenue requirement issues, certain issues related to revenue allocation were reserved for litigation. Issues related to PPL Electric's cost-of-service study and revenue allocation are explained and addressed above. *See* Sections III.A and III.B, *supra*.

6. Net Metering

In issue number 11, the Commission states that PPL Electric's proposal to modify the language of its Net Metering for Renewable Customer-Generators Rider to reflect changes in the AEPS Act and to clarify the net metering provisions for shopping customers must be reviewed to determine whether such changes are just and reasonable. In this proceeding, PPL Electric is proposing to make several changes to its Net Metering Renewable Customer-Generators Rider

("Net Metering Rider") to coordinate that provision with the Alternative Energy Portfolio Standards Act, Act of November 30, 2004, P.L. 1672, *as amended*, 73 P.S. §§ 1648.1-1648.8, and the Commission's regulations implementing the Act, 52 Pa. Code §§ 75.61-75.70. First, the billing provision will be revised to provide for annual payments for excess generation at PPL Electric's Price to Compare. Second, a section has been added to the Rider to set forth the conditions under which shopping customers can qualify and participate in the Company's net metering program. PPL Electric St. 8, p. 18; PPL Electric Ex. OGK-1, p. 19L.3.

PPL Electric's Net Metering proposal was the subject of substantial discovery. The Company's Net Metering program was addressed at the public input hearings, Tr. 211-12, as well as in SEF St. 1 and SEF St. 1-S. As set forth in Paragraph 30 of the Settlement, SEF reserved for litigation issues related to PPL Electric's proposed Net Metering Rider. These issues related to Net Metering are explained and addressed above. *See* Section III.C, *supra*.

7. Purchase of Receivables

In issue number 12, the Commission states that PPL Electric's proposed continuation of its Purchase of Receivables ("POR") program and its proposed changes in the discount rates and Merchant Function Charge ("MFC") must be closely examined. In this proceeding, PPL Electric is proposing that the purchase of receivables ("POR") program approved by Commission for the period January 1, 2010 through December 31, 2010 be extended to operate beyond December 31, 2010. PPL Electric St. 6, pp. 6-7. PPL Electric's proposal to extend its current POR program to operate beyond December 31, 2010, was the subject of extensive discovery. In addition, RESA thoroughly addressed PPL Electric's POR program in RESA St. 1 and RESA St. 1-SR. RESA opposes PPL Electric's proposal to extend the current Commission-approved POR program to operate beyond December 31, 2010, and recommends several modification to the existing POR program. Each of RESA's issues are explained and addressed below. *See* Section IV.B, *infra*.

8. Customer Education and Energy Efficiency Programs

In issue number 13, the Commission states that PPL Electric's proposed customer education and energy efficiency programs must be carefully examined to ensure they are not already included in the Company's Act 129 energy efficiency and conservation plan budget, and are not already being recovered through the Company's Act 129 Compliance Rider. The Commission approved PPL Electric's Consumer Education Plan on July 18, 2008, at Docket No. M-2008-2032279, which was submitted in compliance with the Commission's Final Order at Docket No. M-00061957, entered May 17, 2007. PPL Electric's Consumer Education Plan provided for the Company to spend approximately $5 million on specific consumer education programs for each year of the plan. In this proceeding, the Company proposes to continue its efforts to fund these valuable customer education programs and, therefore, included the amounts associated with these programs in its future test year O&M requirement. PPL Electric St. 6, p. 30. However, these programs predate Act 129 and are separate and apart from PPL Electric's Energy Efficiency and Conservation Plan ("EE&C Plan") at Docket No. M-2009-2093216, as well as the Company's Smart Meter Plan at Docket No. M-2009-2123945. PPL Electric St. 6, p. 31. Consequently, the costs associated with the proposed customer education and energy efficiency programs are not already included in the Company's EE&C Plan budget, and are not already being recovered through the Company's Act 129 Compliance Rider.

The Company's expenses, including the costs associated with the customer education and energy efficiency programs, were the subject of extensive discovery. Further, this issue was addressed in OTS St. 2, OTS St. 2-SR, OCA St. 1, OCA St. 1-S, SEF St. 1, and SEF St. 1-S. After extensive investigation and negotiations, the parties were able to resolve this issue. As set forth in the Settlement, the settlement rates include $5.09 million of customer education costs for PPL Electric's Consumer Education Plan and do not reflect the $39,000 of education and

marketing for the Company's time-of-use rates identified in SEF's testimony. Further, all education and marketing expenses for PPL Electric's time-of-use rates will be recovered through PPL Electric's Generation Service Charge ("GSC") pursuant to the Commission's Order in PPL Electric Time-of-Use proceeding at Docket No. R-2009-2122718, entered March 9, 2010.

9. Updates to Tariff Provisions

In issue number 14, the Commission states that PPL Electric's proposed updates to its tariff to clarify certain provisions and eliminate other provisions must be reviewed to determine whether such changes are appropriate. The proposed tariff is explained in PPL Electric St. 8 and PPL Electric Ex. OGK-1. The parties engaged in extensive discovery on the proposed changes to PPL Electric's tariff provisions. The parties also submitted testimony in support of their respective positions on PPL Electric's proposed changes to its tariff provisions. Although the parties were able to resolve some of the issues, other issues related to the tariff provisions were reserved for litigation. The litigated tariff issues are explained and addressed above. *See* Section III.C, *supra*.

10. Ring Fencing and Credit Ratings

In issues number 15 and 16, the Commission indicates PPL Electric's ring fencing efforts and techniques to obtain a better credit rating should be carefully examined. In 2001, PPL Electric completed a strategic initiative to insure its legal separation ("ring fencing") from PPL Corporation and its other affiliated companies. This initiative was designed to enable PPL Electric to substantially reduce its exposure to volatility in energy prices and fuel supply risks through 2009 and to reduce its business and financial risk profile by limiting its business activities to the transmission and distribution of electricity, and businesses related to or arising from electric transmission and distribution businesses. PPL Electric St. 4-S, pp. 1-3. These enhancements to PPL Electric's legal separation from PPL Corporation and its other subsidiaries

are intended to minimize the risk that a court would order PPL Electric's assets and liabilities to be substantially consolidated with those of PPL Corporation or its other subsidiaries in the event that PPL Corporation, or another PPL Corporation subsidiary, were to become a debtor in bankruptcy court. *Id.* at p. 3.

The credit ratings for both PPL Corporation and PPL Electric are set forth in PPL Electric St. 4-S, p. 4. The factors the rating agencies consider important in determining PPL Electric's credit ratings are set forth in PPL Electric St. 4-S, pp. 4-5. PPL Electric does not take any steps specifically designed to obtain a better credit rating than PPL Corporation. However, PPL Corporation does make every effort to obtain appropriate ratings for both corporations. Some of the steps that PPL Corporation takes include managing each corporation in an efficient and cost-effective manner, as well as maintaining a reasonable capital structure for each. Further, PPL Electric's ratings reflect its status as a fully regulated utility. PPL Corporation's ratings reflect the financial metrics of all of its subsidiaries, including several companies that are engaged only in competitive electricity markets. To the extent that regulated businesses are viewed as less risky than competitive businesses, PPL Electric's ratings will tend to be somewhat higher than PPL Corporation's ratings. PPL Electric St. 4-S, pp. 5-6.

Importantly, as set forth in the Settlement, the Parties were able to achieve settlement as to all revenue requirement issues, including the appropriate capital structure to be used by PPL Electric.

B. PURCHASE OF RECEIVABLES PROGRAM

1. Background of PPL Electric's Current and Proposed Purchase of Receivables Program

In this proceeding, PPL Electric is proposing that the purchase of receivables ("POR") program approved by Commission for the period January 1, 2010 through December 31, 2010 be

extended to operate beyond December 31, 2010. PPL Electric St. 6, pp. 6-7. Based on the Company's extensive interactions with electric generation suppliers ("EGSs") in the implementation of this program and the fact that the current POR program has not impeded development of a competitive retail market, the Company believes that the POR program currently in place is well understood by the EGSs and is able to meet most of their needs, as well as the needs of their customers. PPL Electric St. 6, p. 14; PPL Electric St. 6-R, p. 5.

The purchase and sale of accounts receivable is a financial instrument employed by commercial entities to avoid credit and collection activities and to take advantage of the time-value of money. In its most basic sense, accounts receivable are moneys owed for specific services rendered. Tr. 442. In the absence of a POR program, the entity rendering the service is responsible for the costs and efforts associated with the billing and collection of the amounts owed by its customer and bears the risk that the customer will not timely remit payment and/or not pay the outstanding amount in full. Under a POR program, the entity rendering the service sells its accounts receivable to a third party and receives immediate payment for the receivables less an agreed upon discount to reflect collection risk and the time value of money. Tr. 443. A POR program therefore allows the seller of the receivable to receive payment sooner and avoid the costs and risks associated with collecting any delinquent amounts owed by the customer. Tr. 443.

PPL Electric has administered a *de facto* POR program since the Commission's approval of the Company's restructuring settlement in 1998. *Application of Pennsylvania Power & Light Company for Approval of its Restructuring Plan under Section 2806 of the Public Utility Code*, Docket No. R-00973954, 1998 Pa. PUC LEXIS 197 (August 27, 1998). Under its original POR program, PPL Electric paid an EGS the entire amount for undisputed EGS charges, regardless of

whether the customer had paid the Company for up to a three-month period. PPL Electric could not terminate service to a customer for the customer's failure to pay the EGS portion of its bill. PPL Electric also could not terminate consolidated billing unless the customer was in arrears for 90 days or three billing cycles, whichever was shorter. At that point, the EGS, after having received three months of payments at a zero discount, became responsible for billing its own charges. The EGS was free to terminate its service to the customer if the customer failed to pay its bills. If the EGS chose to terminate its generation service, the customer would be returned to default generation service and PPL Electric would become responsible for the billing and collection of generation service charges. Tr. 443-44.

In 2009, as part of the settlement of the Company's Default Service Plan for the Period January 1, 2011 through May 31, 2013, PPL Electric agreed to file a revised POR plan as either part of its next distribution rate case or a stand-alone POR plan to become effective on January 1, 2011.[18] Thereafter, the Commission issued an order on August 11, 2009, directing PPL Electric to file a POR program to be effective on January 1, 2010.[19] Pursuant thereto, PPL Electric filed a voluntary POR program, together with a Merchant Function Charge ("MFC"), which was approved by the Commission for the period January 1, 2010 through December 31, 2010. *Petition of PPL Utilities Corporation Requesting Approval of a Voluntary Purchase of Accounts Receivables Program and Merchant Function Charge*, Docket No. P-2009-2129502, 279 PUR4th 539, 2009 Pa. PUC LEXIS 266 at *9 (November 19, 2009) (*PPL Electric POR Program"*). The current POR program was the result of a partial settlement and the Commission's resolution of two issues reserved for litigation. In approving the current POR

[18] *Petition of PPL Electric Utilities Corporation for Approval of a Default Service Program and Procurement Plan for the Period January 1, 2011 Through May 31, 2013*, Docket No. P-2008-2060309 (June 30, 2009).

[19] *PPL Electric Utilities Corporation Retail Markets*, Docket No. M-2009-2104271 (August 11, 2009).

program, the Commission specifically held that POR programs are voluntary and the Commission is without authority to require electric distribution companies ("EDCs") to offer POR programs. *Id.* at *12-13.

In this proceeding, PPL Electric is proposing to extend its voluntary Commission-approved POR program beyond its expiration date of December 31, 2010. PPL Electric's POR program applies to residential and small commercial and industrial customers ("c&i"); it does not apply to large c&i customers. PPL Electric St. 6, p. 8. The accounts receivable purchased by PPL Electric are the moneys owed by shopping customers to the EGS for generation services. PPL Electric purchases these accounts receivable at a discount from the standard supply charges to offset the risks and expenses associated with accounts that may ultimately be uncollectible. PPL Electric St. 6-R, p. 4.

The discount rate is composed of two components: (1) an uncollectible accounts expense percentage factor; and (2) a POR development, implementation, and administration percentage factor. PPL Electric St. 6, p. 8. The uncollectible accounts expense percentage factor primarily is based on an average of the Company's actual bad debt write-offs for the most recent five calendar years. PPL Electric St. 7, p. 33; PPL Electric Ex. JKM-7. The POR administrative percentage factor is based on: (a) PPL Electric's POR administrative costs; (b) shopping levels; (c) POR program participation levels; and (d) average competitive supply rates. PPL Electric St. 7, p. 33.

Given the different energy requirements, collection mechanisms available, and uncollectible accounts expense percentages, the discounts rates for the residential and small c&i customers are different. PPL Electric St. 6, p. 8. The proposed discount rate for the residential customers is 1.855%, which reflects an uncollectible accounts expense percentage factor of

1.805% and an administrative cost factor of 0.05%. The proposed discount rate for the small c&i customers is 0.06%, which reflects an uncollectible accounts expense percentage factor of 0.01% and an administrative cost factor of 0.05%. PPL Electric St. 7, p. 32. Because the Company has very limited experience regarding the operation of its current POR program, which only began January 1, 2010, PPL Electric is proposing to continue using its current POR administrative percentage factor of 0.05% to recover its POR administrative costs until such time as it obtains more actual experience with the implementation of the program. PPL Electric St. 7, pp. 33-34.

In conjunction with its POR program, PPL Electric also implemented a Merchant Function Charge ("MFC"), which unbundles from its distribution base rates the uncollectible accounts expense associated with generation supply. As a result, the uncollectible accounts expense related to distribution service is recovered from all ratepayers through distribution charges. In turn, the uncollectible accounts expense related to generation service is separated from PPL Electric's distribution rates and recovered as follows: (1) by the Company from default service customers through the MFC; or (2) by individual EGSs from shopping customers taking competitive supply as a component of their generation price. PPL Electric St. 6-R, p. 2. Thus, residential and small c&i customers who contract for generation supply with an EGS do not pay the MFC. However, the MFC is added to the Price to Compare so that EGSs are able to reflect generation uncollectible costs in their competitive supply offers.[20] PPL Electric St. 7, p. 30.

PPL Electric's POR program is entirely voluntary, *i.e.*, EGSs can elect to participate or not participate in the program. PPL Electric St. 7, p. 30. Under the residential customers

[20] For both the residential and small c&i rate classes, the MFC is equal to the uncollectible accounts expense percentage included in the discount percentage under the current and proposed POR program. PPL Electric St. No. 7, p. 35.

program, an EGS must sell all of its accounts receivable for that rate class and use PPL Electric's consolidated billing to participate in the POR program. PPL Electric St. 6-R, p. 12. For the small c&i customers, an EGS may elect to participate in the POR program for some or all of its small c&i customers, but must use EDC consolidated billing for those customers in the POR program. PPL Electric St. 6-R, p. 12.

Under the current and proposed POR program, the EGS calculates customer charges for its generation service and transmits those charges to PPL Electric.[21] PPL Electric includes the generation charge on behalf of the EGS on the consolidated bill that the Company prepares and sends to the customer. Importantly, when PPL Electric renders a bill with EGS charges, the Company takes on the obligation to remit the total amount of generation charges, less the appropriate discount, to the EGS within 25 days for residential customers and 20 days for small c&i customers, regardless of whether the customer has actually paid the Company. PPL Electric St. 6, p. 11.

When the Company purchases the EGSs' receivables, it obtains the right to pursue collection activities against the customer, including termination, to recover unpaid amounts for generation service owed by the customer. However, PPL Electric has no recourse to seek recovery of any unpaid amounts from the EGS. PPL Electric St. 6-R, pp. 6-7.

To implement the current POR program, it was necessary for PPL Electric to make a significant number of programming and business changes. The implementation of the current POR program required very significant effort in terms of the amount of resources invested, the short time frame, the criticality of the systems modified, and the timing of the work. PPL

[21] The current and proposed POR program accommodates EGS budget billing. In the event that the EGS offers budget billing for its charges, the EGS will send the Company an amount to be included on the consolidated bill that reflects the EGS' budget amount. PPL Electric St. No. 6, p. 12.

Electric St. 6, pp. 12-13. Importantly, the current POR program has only been in effect since January 1, 2010, and PPL Electric is still in the process of fully implementing the program.

Notably, EGSs and RESA actively participated in the establishment of the Company's current POR program, and they, along with other parties, entered into a settlement that resolved all but two issues. PPL Electric St. 6, p. 14. The Company believes that, as a result of the extensive interactions with the EGSs in the implementation of the current POR program, the current and proposed POR program is well understood by the EGSs and is adequate to meet most of their needs, as well as the needs of their customers. PPL Electric St. 6, p. 14. Indeed, PPL Electric's current POR program does not appear to have been an impediment to the development of the competitive market as demonstrated by the fact that, as of July 3, 2010, in PPL Electric's service territory, 386,473 residential customers (or 31.5% of the total number of residential customers) and 69,312 small c&i customers (or 39.5% of the total number of small c&i customers) were either taking service from an EGS or signed up to begin supply pending the issuance of their next bill. PPL Electric St. 6-R, p. 5. In fact, the information used to develop the Company's most recent quarterly report on shopping filed with the Commission reveals that 24 different EGSs were actively supplying residential customers and 30 different EGSs were actively supplying small c&i customers in PPL Electric's service territory. PPL Electric St. 6-R, pp. 5-6.

2. RESA's Modifications to PPL Electric's Proposed Purchase of Receivables Program Should be Rejected

RESA is the only party to oppose PPL Electric's proposal to extend the current Commission-approved POR program to operate beyond December 31, 2010. RESA recommends the following modifications to PPL Electric's POR program: (a) the Company should eliminate the uncollectible accounts expense percentage factor from the discount rate and

recover the costs associated with all generation-related uncollectible accounts expense through the application of a non-bypassable MFC to both shopping and non-shopping customers; (b) the Company should eliminate the "all-in/all-out" requirement for residential customers; (c) the Company should eliminate the current tracking mechanism to monitor individual EGS uncollectible percentages for small c&i customers; and (d) the Company should expand the POR program to apply to large c&i customers.[22] PPL Electric will address each of RESA's proposed modifications below.

PPL Electric's current POR program was the result of a partial settlement and the Commission's resolution of two issues reserved for litigation: (1) the termination/reconnection of residential customers for non-payment of EGS charges; and (2) the definition of "basic supply services." *See PPL Electric POR Petition,* at *2. Importantly, as explained above, PPL Electric is not proposing a new POR program, it is proposing to continue the current POR program. Neither RESA or any other party has presented any evidence of change in circumstances, facts, or law that would justify or otherwise necessitate a departure from PPL Electric's current Commission-approved POR program.

Notably, the current POR program has only been in effect since January 1, 2010, and PPL Electric is still in the process of fully implementing the program. Before any changes are made, sufficient time should be given to fully implement the current POR program and evaluate its effectiveness. The Company further notes that any changes to the proposed POR program,

[22] RESA also recommends that the Company should provide annual reports with the Commission detailing its then-current and projected future administrative costs to provide the POR program. RESA St. 1, p. 6. Although PPL Electric does not believe that such a reporting requirement is necessary because it will continue to incur ongoing costs related to the administration of its POR program, PPL Electric is willing to implement an annual reporting requirement on a prospective basis. Accordingly, upon approval of the proposed POR program, without any other modification, the Company agrees to file an annual report for its 2011 POR program that provides the actual costs for that program year, and the following year's expected costs, associated with the overall administration of its POR program. PPL Electric St. 7-R, p. 41.

including changes necessary to implement any of the modifications proposed by RESA, could require the incurrence of additional costs that would be recovered through the administrative percentage factor. PPL Electric St. 7-R, p. 41.

Further, and most importantly, PPL Electric's POR program is a voluntary program, meaning that PPL is not required to offer it. Despite RESA's contention to the contrary (RESA St. No. 1-SR, pp. 2-4), the Commission has concluded that it does not have authority to require EDCs to offer POR programs. Indeed, in approving PPL Electric's current POR program the Commission held as follows:

> Specifically, PPL contends that it voluntarily filed its POR Program with the Commission in response to the Retail Markets Order, and does not believe that the Commission has the authority to require it to purchase an EGS' receivables. We agree. In *PECO Energy Co. v. Pa. PUC*, 568 Pa. 39, 791 A.2d 1155 (2002), the Supreme Court of Pennsylvania stated as follows:
>
> > The power of the Commission is statutory, arising either from words contained in the enabling statutes or by a strong and necessary implication from those words, and the legislative grant of power in any particular case must be clear.
>
> No provision of the Code either expressly or by "strong and necessary implication" provides the Commission with the authority to require EDCs to purchase accounts receivable from EGSs.

PPL Electric POR Petition, at *12 (emphasis added). RESA has proposed several significant changes to the PPL Electric POR plan. They are not acceptable to PPL Electric for the reasons explained below and, for that reason alone, should be rejected.[23]

[23] RESA disregards the Commission's holding and states that surely the Commission can make minor changes to the POR program. RESA St. 1-SR, pp. 3-4. RESA's position is in error and, in any event, irrelevant as RESA's proposed changes clearly are not minor but, rather, are major, substantial and burdensome.

a. RESA's Proposal to Eliminate the Uncollectible Accounts Expense Percentage Factor Should be Rejected

RESA recommends that the Company should eliminate the uncollectible accounts expense percentage factor from the discount rate and recover the costs associated with all generation-related uncollectible accounts expense through a non-bypassable MFC assessed on all distribution customers. RESA St. 1, p. 11. As explained below, RESA's proposal is without merit and, moreover, it is fundamentally inconsistent with Commission's policy of unbundling generation-related costs from distribution rates.

As explained above, PPL Electric, with express Commission approval, has unbundled the generation supply-related uncollectible accounts expense from its distribution base rates and recovers this expense through the MFC. PPL Electric St. 6-R, p. 4. The MFC is paid by all POLR customers, and PPL Electric includes the MFC in its Price to Compare. PPL Electric St. 7, p. 35. The MFC, however, is a bypassable charge, *i.e.*, shopping customers do not pay the MFC. This construct provides EGSs with two options for dealing with the risk of collection. One option is to not participate in the POR program and reflect the risk of uncollectibles in the price they charge shopping customers. The second option is to sell the account receivable to PPL Electric at a discount and have the Company assume the costs of collection and the risk of non-collection. Accordingly, under the voluntary POR program, EGSs are provided with the competitive advantage of determining the extent of the generation-related uncollectible accounts expense that they are willing to bear.

RESA in essence now seeks a third option. RESA proposes to eliminate the uncollectible accounts expense from the discount percentage factor, thereby increasing the amount that PPL Electric pays EGSs for their accounts receivable, eliminating all EGS collection risk, and shifting the risk of non-payment for competitive supply to all customers through a non-bypassable MFC,

which would be paid by all distribution customers whether or not they shop for their energy supply. RESA St. 1, p. 11. Stated otherwise, RESA's proposal attempts to shift the risk of non-payment for competitive supply from EGSs, and their shopping customers, to all customers. PPL Electric, in contrast, believes that EGSs should bear the collection risk for their own customers, either by including it in the charges to those customers or by selling their receivables to PPL Electric at a discount. In no event, however, should this risk and cost be borne by non-shopping POLR customers. PPL Electric St. 6-R, pp. 10-11.

Notably, both OTS and OSBA agree that the collection risk for shopping customers should remain with the EGSs and, therefore, recommend that the Commission reject RESA's proposal for a non-bypassable MFC. Ms. Wilson, on behalf of OTS, recommended that the Commission reject RESA's proposal, stating as follows:

> I disagree with Mr. Hudson's proposal to eliminate the uncollectible accounts expense percentage factor from the discount rate and recover the costs associated with all generation-related uncollectible accounts expense through the non-bypassable assessment of the Merchant Function Charge on all distribution customers.
>
> ***
>
> A collection risk from sales is a typical cost of conducting business. The EGSs take on collection risks when they sell electricity to a wholesaler, retailer, or the end user. When an EGS enters the retail market and participates in a public utility's POR program, their collection risk should remain part of their profit-oriented business. In a POR program, the public utility is able to inform an EGS in advance what the collection risk is based on the historic experience with their customer base. (This is known as the utility's uncollectible or bad debt expense ratio). The collection risk associated with electricity commodity sales (the business being conducted) should remain with the entity that is recognizing the commodity sales revenue. In other words, the collection risk associated with the residential and small commercial and industrial customers electing to purchase electricity form an EGS, rather than the public utility, should remain with the EGS. Therefore, the bad debt rate should remain a component of a POR discount to

> appropriately move the business risk to the business carrying on the sales.

OTS St. 2-R, pp. 9-10. Similarly, Mr. Knecht, on behalf of OSBA, opposed RESA's proposal, stating as follows:

> My disagreement with Mr. Hudson is based on the fact that the EGSs who service customers outside the PoR program are responsible for collecting the bills from those customers and are therefore responsible for uncollectibles costs related to those customers.
>
> By requiring customers outside the PoR program to pay the MFC, Mr. Hudson's proposal will put the EGSs who wish to provide service outside the PoR program at a competitive disadvantage. Customers who are outside the PoR program will pay the non-bypassable MFC, and will implicitly absorb their own EGS's uncollectibles costs in the rates paid to the EGS.
>
> ***
>
> In reality, EGSs incorporate the risk of incurring uncollectibles into their pricing margins, and those margins are passed on to their customers. Therefore, competition cannot shield the shopping customers who are outside the PoR program from double-paying for generation-related uncollectible costs.
>
> ***
>
> In PPL Electric's proposal, non-shopping customers pay for uncollectibles through the PPL Electric MFC, which applies only to non-shopping customers. Shopping customers in the PoR program implicitly pay for the uncollectibles cost in the discount applied by PPL Electric to its purchase price for receivables. Shopping customers outside the PoR program implicitly pay for the uncollectible costs in the rates charge by their EGS.

OSBA St. 2, pp. 22-23.

In addition to improperly reassigning risk, RESA's proposal also should be rejected because it, in essence, rebundles generation-related and distribution-related uncollectible accounts expense charges through a non-bypassable MFC. Although PPL Electric acknowledges that the charges would not be rebundled as a single distribution charge as they were prior to the

establishment of the current POR program and the MFC, the creation of a non-bypassable MFC that applies to shoppers and non-shoppers is, in essence, a return to the prior bundled state.

Such a result is inconsistent with the goals of the Competition Act and clear Commission policy. Section 2804(3) of the Competition Act provides as follows:

> The commission shall require the unbundling of electric utility services, tariffs and customer bills to separate the charges for generation, transmission and distribution....

66 Pa.C.S. § 2804(3). *See also Lloyd* (holding that Section 2804(3) mandates rates for services as unbundled charges for transmission, distribution and generation). Further, the Commission has encouraged EDCs to unbundle generation-related costs from distribution rates.

> While utility rates were unbundled into transmission, distribution and generation components as part of the restructuring process, there is significant concern on the part of the Commission and others that some generation costs have been improperly allocated, or "embedded," in EDC distribution rates. The Commission has not undertaken a full-fledged review of distribution rates with the goal of resolving this issue. This was in part due to the existence of rate caps and the agreements reached in the restructuring settlements. With the coming expiration of the remaining rate caps, there is now no obstacle to taking this issue up for consideration.
>
> Our preference is that this issue will be addressed in the next distribution rate case for each EDC. For those EDCs who have not initiated cases by the end of 2007, the Commission reserves the right to initiate a cost allocation proceeding to resolve this issue.

Default Service and Retail Electric Markets, Final Policy Statement, Docket No. M-00072009, 256 PUR 4th 341, 2007 Pa. PUC LEXIS 3 at *12-13 (May 10, 2007).

Under its current POR program, PPL Electric has unbundled the generation-related uncollectible accounts expense, which currently is recovered through either the discount percentage factor percentage (shopping customers) or through the MFC (default service customers), from the distribution-related uncollectible accounts expense, which currently is

recovered through distribution rates. PPL Electric St. 6, p. 8. Now that PPL Electric has unbundled generation-related uncollectible accounts expense from distribution base rates, RESA proposes that they be rebundled through a non-bypassable charge to all customers. RESA's rebundling proposal is directly contrary to the position RESA maintained in PPL Electric's most recent Default Service Plan proceeding. RESA took the following position with respect to unbundling in that proceeding:

> A company's bad debt expense is directly related to the level of revenues it bills. If PPL only provided distribution service its number of non-paying customers would likely be approximately the same, but the absolute amount of unpaid bills would be much less. Thus, a portion of bad debt expense allowance in its distribution rates is associated with PPL's generation or default service revenues. ***There is no rational argument that could justify not allocating this portion to the default service portion of the rate and collecting it there.***

See Docket No. P-2008-2060309, RESA St. No. 1, p. 33; PPL Electric St. 6-RJ, p. 9.

In support of its position that uncollectible accounts expense should be eliminated from the discount percentage factor, RESA asserts that the current POR program is complicated and impedes competitive market development. RESA St. 1, p. 12. However, as explained above the structure of PPL Electric's current POR program does not appear to have been an impediment to the development of the competitive market. PPL Electric St. 6-R, pp. 5-6.

RESA further contends that the current POR program is inconsistent with the requirements of the settlement in the default service proceeding wherein the parties agreed to establish a POR program RESA St. 1, p. 8. However, RESA disregards the language of the Commission's order in the default service proceeding, which provides, in pertinent part, as follows:

> [D]iscounts to POR payments to suppliers to reflect incremental uncollectible expenses not included in distribution rates, which may include the unbundled uncollectible accounts percentage;

> provided, however, that customers will not be responsible for any reconciliation of the discount against actual results.

Petition of PPL Electric Utilities Corporation for Approval of a Default Service Program and Procurement Plan for the Period January 1, 2011 Through May 31, 2013, Docket No. P-2008-2060309 (June 30, 2009). The Commission's order clearly provides that the discount "may include the unbundled uncollectible accounts percentage." Consistent therewith, the discount applied in PPL Electric's POR program does reflect the full, unbundled generation-related uncollectible accounts percentage, as well as a component to recover administrative costs. PPL Electric St. 6-R, p. 8.

RESA finally argues that the current POR program is inconsistent with recent actions by the Commission regarding POR programs in the service territories of other electric distribution companies ("EDCs"). RESA St. 1, p. 12. However, the POR programs of other EDCs do not establish a statewide standard.[24] PPL Electric St. 6-R, p. 8. Rather, each POR program adopted by an EDC reflects the unique circumstances of the individual EDC, including the ability of its customer information and billing systems to accommodate specific program structures.[25] PPL Electric St. 6-R, p. 9. Indeed, RESA relies on the POR program adopted by PECO; however, RESA disregards that, unlike PPL Electric, PECO has not unbundled its uncollectible accounts expense. Further, the Company believes that its POR program is consistent with the POR

[24] To the extent that there is sufficient justification for a statewide standard POR program, such standard should be developed through a rulemaking proceeding where all affected EDCs, EGSs, and customers are afforded the opportunity to participate and comment on any proposed standard POR program. PPL Electric St. No. 6-R, p. 8. In the alternative, the Commission should convene a working group to comprehensively address all issues related to the design and administration of uniform standards for POR programs. In fact, PPL Electric notes that the Retail Markets Working Group, under the oversight of the Commission's Law Bureau, is tasked with the responsibility to develop policy recommendations on matters including "consideration of an EGS receivables purchase program in each service territory." *See* Commission's Secretarial Letter, Docket No. M-0007209 (April 15, 2008).

[25] *See, e.g., Establishment of Interim Guidelines for Purchase of Receivables (POR) Programs*, Docket No. M-2008-2068982, I-00040103F0002, Slip Op. at 9 (December 19, 2008) (wherein the Commission held that it will review and approve POR programs for natural gas distribution companies on a case-by-case basis).

program administered by Duquesne Light. *See Pa. P.U.C. v. Duquesne Light Company*, Docket No. R-00061346 (December 1, 2006). Importantly, because POR programs are voluntary as explained above, the fact that another EDC's POR program has conditions that are different from those proposed by PPL Electric has no bearing on PPL Electric's voluntarily offered POR program. PPL Electric St. 6-R, pp. 9-10.

Finally, if RESA's proposal were adopted and the uncollectible accounts expense was recovered through a non-bypassable charge to all customers, the discount factor would be eliminated from the POR program, at which point there would be no reason for a POR program. The whole purpose of a POR program is to sell accounts receivables to a third party to take advantage of the time value of money and to receive immediate payment for the receivables less an agreed upon discount to reflect collection risk. Tr. 442-43. If the discount to reflect the collection risk is removed, there simply would be no point in purchasing the accounts receivable. Accordingly, RESA's proposal should be rejected.

b. RESA's Proposal to Eliminate the "All-in/All-out" Requirement for Residential Customers Should be Rejected

RESA also proposes that the Company should eliminate the "all-in/all-out" requirement for residential customers. RESA St. 1, p. 13. RESA contends that this restriction, which does not exist for small c&i customers, prohibits an EGS from serving residential customers on a simple, fixed-price rate with the convenience of a single EDC consolidated bill while, at the same time, providing another set of residential customers a more complex, customized product via dual billing. RESA St. 1, p. 14. Although PPL Electric agrees with RESA's characterization of the "all-in/all-out" requirement, RESA's proposal to eliminate this requirement disregards the purpose of the requirement and the success of the current POR program. RESA's proposal therefore should be rejected.

As explained above, PPL Electric's POR program is entirely voluntary, and EGSs can elect to participate or not participate in the program. PPL Electric St. 7, p. 30. However, for residential customers, an EGS must sell all of its accounts receivable for that rate class and use PPL Electric's consolidated billing to participate in the POR program. PPL Electric St. 6-R, p. 12. Thus, an EGS serving residential customers is unable to place certain residential accounts on POR/consolidated billing while billing other residential accounts through dual billing without POR. RESA St. 1, p. 13.

RESA concedes that there is a risk that the Company could under recover its generation uncollectible accounts expense if EGSs were permitted to selectively enroll poor paying customers. Indeed, in his direct testimony Mr. Hudson stated on behalf of RESA as follows:

> [F]rom a theoretical perspective I do agree that under PPL's current POR program (with the MFC unbundling mechanism) there is a risk that PPL could under recover its generation related uncollectible accounts expense if EGSs were permitted to selectively enroll only poor paying customers onto POR.

RESA St. 1, p. 10. This risk is greater for residential customers as compared to other classes for several reasons: The residential class includes low-income customers; the uncollectible accounts expense is much higher for the residential class; the limitations on the ability to terminate service under Chapter 56, including the moratorium on winter shutoffs; and the Company's ability to pursue collections is subject to Chapter 56. PPL Electric St. 6-R, p. 13.

In the absence of the "all-in/all-out" requirement, an EGS could potentially maintain the billing and collection responsibilities for low risk, good-paying residential customers, while shifting the risk of residential customers with poor credit or payment histories to PPL Electric through use of its consolidated billing. As a result, the Company's actual uncollectible accounts expense would likely be higher than the average for all residential customers, and it might be significantly higher due to the moratorium on residential winter terminations under chapter 56.

The "all in/all out" requirement was a protection, under the Company's current POR program, as an appropriate mechanism to address this concern. PPL Electric St. 6-R, p. 13. RESA has failed to introduce evidence of any conditions that have changed since the settlement that established the current POR that would alter the risk acknowledged by RESA.

Further, as explained above, the large number of residential customers currently taking competitive supply within the PPL Electric service territory and the large number of EGSs serving residential customers does not suggest that the "all-in/all-out" requirement has been any impediment to EGS participation in the development of a robust competitive market. PPL Electric St. 6-R, pp. 5-6, 13.

c. RESA's Proposal to Eliminate the Current Tracking Mechanism for the Small C&I Customer POR Program Should be Rejected

In opposition to PPL Electric's proposal to continue its current POR program, RESA recommends that the Company should eliminate the current tracking mechanism to monitor individual EGS uncollectible percentages for small c&i customers. RESA contends that the tracking of EGS uncollectible accounts expense under the POR program is complicated and can impede development of the competitive market. RESA St. 1, p. 9. RESA proposal is without merit and should be rejected.

As explained above, unlike the Residential Rate Classes, an EGS may selectively enroll small c&i customers in the POR program through consolidated billing, while serving other customers through dual billing. PPL Electric St. 6-R, p. 12; RESA St. 1, p. 16. Stated otherwise, an EGS participating in the POR program is not required to use consolidating billing for all of its small c&i customers. As a result, an EGS can maintain the billing and collection responsibilities for low risk, good-paying small c&i customers, while shifting the risk of small c&i customers with poor credit or payment histories to PPL Electric through use of its consolidated billing. To

discourage such "cherry-picking" activities, the parties to the settlement mutually agreed to a tracking mechanism to monitor individual EGS uncollectible accounts expense for small c&i customers when the EGS does not enroll all accounts in the POR program. RESA St. 1, p. 16.

PPL Electric currently is capturing the data necessary to report on EGS uncollectibles by individual EGS. PPL Electric St. 6-R, pp. 16-18. Although PPL Electric has not yet produced a report on EGS uncollectibles due to limited data and implementation issues, PPL Electric St. 6-R, pp. 16-18, the large number of small c&i customers currently taking competitive supply within the PPL Electric service territory and the large number of EGSs serving small c&i customers does not suggest that there are significant impediments to EGS participation. PPL Electric St. 6-R, pp. 5-6, 14.

Further, PPL Electric notes that the obligation to track is a burden on the Company, not EGSs. The tracking requires no action by EGSs and does not alter the normal flow of enrollments, the processing of billing information, the rendering of bills, or the processing of remittances to EGSs. PPL Electric St. 6-R, p. 14. Further, it is important to note that the Company is proposing to decrease the uncollectible accounts percentage factor for small c&i customers (as well as the MFC for that class) from 0.12% to 0.010%. PPL Electric St. 7-R, p. 32; PPL Electric Ex. JMK-7. Thus, it is difficult to see how EGSs serving this class are harmed either by the existence of the tracking provision or by PPL Electric's decision to delay reporting on the results of the tracking. PPL Electric St. 6-R, pp. 17-18.

d. RESA's Proposal to Expand the POR Program to Apply to Large C&I Customers Should be Rejected

RESA also recommends that the Company should expand the current POR program to apply to large c&i customers. RESA's rationale is that by "not offering POR to large c&i customers, PPL's default service for this customer class is at a competitive advantage as

compared to EGS offers because EGS offers for this class must reflect the cost of expected uncollectible accounts expense whereas PPL's default service does not reflect any generation related uncollectible account expense." RESA St. 1, p. 19. However, RESA disregards the fact that PPL Electric maintains a POR program for large c&i customers, and that such program has not been an impediment to competition.

Despite RESA assertion to the contrary, PPL Electric does in fact offer a POR program for large c&i customers. PPL Electric's large c&i POR program is not part of, and is separate in design from the current POR program for the residential and small c&i customers described above. PPL Electric St. 6-R, p. 19. Under PPL Electric's large c&i POR program, the Company pays the EGS in full, without a discount, for a period of three months. After the three month-period, if the customer has a 60-day arrearage, the Company initiates a change to move the customer from consolidated billing to dual billing, meaning that the EGS then will become responsible for the billing of its own charges. Once dual billing is selected, there is no receivable being transferred from the EGS to the Company. Similar to residential and small c&i customers, the Company has no recourse to seek from the EGS recovery of any amounts not paid by the large c&i customers. PPL Electric St. 6-R, pp. 7, 19.

RESA's contention that EGSs are at a competitive disadvantage because they must reflect the uncollectible accounts expense in their offers to large c&i customers is overstated. The uncollectible accounts expense percentage factor for the large c&i customers is only 0.010%. PPL Electric St. 7-R, p. 32; PPL Electric Ex. JMK-7. Consequently, any competitive disadvantage that may exist after the first three months is not significant. PPL Electric St. 6-R, p. 19.

RESA's proposal to expand the POR program to large c&i customers would create a significant risk for the Company, as well as other customers, in the event that a large c&i customer declares bankruptcy because the low uncollectible accounts expense percentage factor for the large c&i customers does not reflect the risk of bankruptcy. *See* RESA St. 1-SR, p. 19 (acknowledging that if large c&i customer's generation-related charges are uncollectible, the amount would be substantial). In order to adequately offset such risk, PPL Electric would either have to substantially upwardly adjust the uncollectible accounts percentage or require a substantial deposit to reflect this bankruptcy risk.

The risk faced by PPL Electric and its customers in the event a large c&i customer declares bankruptcy is exacerbated because, under the current tariff, it is not clear that the Company may obtain deposits for costs associated with generation service. Under Rule 10.C of PPL Electric's tariff, the Company can obtain a deposit or guarantee of payment only for service provided by the Company. PPL Electric Ex. OGK-1, p. 14A. Although it could be argued that once PPL Electric purchases the account receivable for generation service it is included as a service provided by the Company, it is not clear whether shopping customer's generation service can be included in the deposit or guarantee of payment. Thus, to avoid the significant risk created by the bankruptcy of a large c&i customer, PPL Electric's tariff would need to be amended to clearly grant PPL Electric the ability to obtain a deposit for generation service when a large c&i customer is enrolled in the POR program.

Further, a significant number of the shopping customers in this class receive a separate bill from their EGS and, therefore, would not be affected by a POR program. Indeed, currently, two thirds of the large c&i customers who are taking competitive supply are being billed separately by their EGS. Many of these customers are enrolled in complex, customized

products. PPL Electric St. 6-R, pp. 19-20. As conceded by RESA, the EDC consolidated billing format is simply not compatible for such complex, customized products offered by EGSs. RESA St. 1, p. 14. Changing the structure of the large c&i POR program would involve significant programming and put efforts to install other functionality intended to encourage a competitive market at risk of not being completed in a timely manner. PPL Electric St. 6-R, p. 20.

Finally, PPL Electric notes that the large c&i POR program currently in place appears not to have been a significant impediment to the development of the competitive market. As of July 3, 2010, 993 large c&i customers (or 78.7% of the total number of large c&i customers) were either taking service from an EGS or were signed up to begin supply pending the issuance of their next bill. Further, information used to develop the Company's most recent quarterly report on shopping filed with the Commission indicates that 24 different EGSs were actively supplying large c&i customers. PPL Electric St. 6-R, p. 20.

C. CEO'S PROPOSAL TO INCREASE FUNDING OF THE WRAP AND HELP PROGRAMS SHOULD BE REJECTED

In this proceeding, the Commission on Economic Opportunity ("CEO") has proposed that PPL Electric be required to increase annual funding for the WRAP program from $8.0 million to $9.5 million (CEO St. 1, p. 6) and increase the funding of the Operation HELP program from $1.3 million to $1.6 million. For the reasons explained below, both of CEO's recommendations should be rejected.

WRAP is PPL Electric's Low-income Usage Reduction Program which the Commission mandated by regulations codified at 52 Pa. Code Ch. 58. PPL Electric St. 9, p. 3. PPL Electric's budget for the WRAP program for 2010 is $8 million, and PPL Electric plans to maintain its current annual funding level for WRAP through 2013. PPL Electric St. 9, p. 12.

CEO's recommended increase in WRAP funding is inappropriate for several reasons. First, the amount of the increase is completely arbitrary. CEO provides absolutely no basis for its proposal. This shortcoming of CEO's contention is particularly significant because it is proposing an adjustment that PPL Electric incur an additional expense, CEO bears the burden of proof. *Pa. P.U.C. v. Metropolitan Edison Co.*, Docket No. R-00061366, 2007 Pa. PUC LEXIS 5 (January 11, 2007) (holding that a party proposing that a utility incurs additional expenses not in its filing bears the burden of proof). CEO's failure to meet its burden of proof, alone, provides a sound basis for rejecting its recommendation.

Second, CEO views the Company's level of WRAP funding in isolation, and not in conjunction with other sources of funding of low-income weatherization projects for PPL Electric's low-income customers. CEO ignores the fact that, with the implementation of Act 129, PPL Electric has already nearly doubled its annual budget for low-income weatherization. Over the next 4 years, PPL Electric will expend an **additional $29 million** for low-income weatherization over and above projects from traditional WRAP. This funding will go to existing weatherization community based organizations ("CBOs") and contractors, including CEO, who currently administer WRAP. In 2010, for example, PPL Electric's weatherization budget for low-income customers is $16 million, which includes $8.0 million from the traditional WRAP and $8.0 million under Act 129.

An additional source of funding for low-income weatherization projects is the federal stimulus package under the American Recovery and Reinvestment Act ("ARRA"). This package has provided an unprecedented level of funding for such programs. So far, the Pennsylvania Department of Community and Economic Development has received about $252 million in ARRA funding for low-income weatherization programs to be spent over the next 3 years.

Expending this significant additional amount of weatherization funding will be challenging because it will require expanding training capabilities and increasing the production capacity of the Pennsylvania Department of Community and Economic Development's contractors.

In addition to the ARRA funding, the Department of Community and Economic Development will continue to receive traditional funding from the United States Department of Energy and the transfer of weatherization funding from LIHEAP. The Department of Public Welfare ("DPW") transfers up to 15% of its total federal LIHEAP allocation to the Department of Community and Economic Development's weatherization program. For the 2009-2010 LIHEAP program year, DPW transferred $15.5 million to the Department of Community and Economic Development.

Thus, there are currently five funding streams for low-income weatherization programs – (1) utility LIHEAP program such as WRAP, (2) funds under Act 129, (3) Department of Energy funding, (4) transfer of LIHEAP funding to the Department of Community and Economic Development, and (5) funding under the ARRA. Given the above factors and numerous sources of substantial funds, PPL Electric believes that its funding of its traditional WRAP at $8.0 million annually is appropriate. The needs for funding of low-income weatherization programs should be balanced against the costs borne by other residential customers who pay for them.

CEO's recommendation regarding PPL Electric's Operation Help also should be rejected. PPL Electric's Operation HELP pays for any type of home heating bill for low-income customers. The fund is supported by donations from customers, employees, and PPL Corporation. PPL Electric Ex. TRD-1. No portion of the funding for Operation HELP is raised through rates.

CEO's proposal, to require PPL Electric to guarantee a minimum funding level of $1.6 million should be rejected for numerous reasons. First, although PPL Electric will continue to promote donations to Operation HELP, it is inappropriate for PPL Electric to be required to guarantee any set amount. Total donations to the program have increased over the past 5 years from approximately $912,000 in 2005 to just over $1.4 million in 2009. PPL Corporation's donation of $1 million annually to Operation HELP is the largest such donation of any electric or gas utility in Pennsylvania. PPL Electric St. 9-R, p. 6. PPL Corporation has demonstrated generosity despite the absence of any legal requirement to do so.

Second, substantial additional funds are not needed for Operation HELP because it is not designed to serve a large number of low-income customers or any customer over an extended period of time. Instead, Operation HELP supplements larger programs such as LIHEAP by providing assistance to customers who are just over the LIHEAP program income levels or cannot receive assistance because the program is closed. PPL Electric St. 9-R, p. 7.

Third, as a legal matter, because no portion of Operation HELP's funding is included in rates, the Commission cannot order an increase in contributions by PPL Electric or PPL Corporation or their employees or customers. The program is voluntary for all participants. In *Re. Pennsylvania-American Water Co.*, 231 PUR 4th 277, 315 (2004), this Commission stated that: [q]uite simply, the Commission is without authority to require PAWC or any public utility, to either make or increase contributions derived solely from shareholder funds." See also *Pa. P.U.C. v. PPL Electric Utilities Corp.*, Docket No. R-00049255, p. 95 (Dec. 22, 2004), where the Commission stated as follows:

> Operation HELP is wholly funded by contributions from the Company's shareholders, customers and employees. As such, we agree with the ALJ's determination that the Commission lacks jurisdiction to direct further contributions to Operation HELP or

> mandate the manner in which the Company chooses to distribute these contributions. The Exceptions filed by the CEO and OCA are denied.

Operation HELP is beyond the Commission's jurisdiction, and there is no legal basis to require PPL Electric to file a plan with the Commission or for a program over which the Commission has no control or jurisdiction.

For the foregoing reasons, CEO's proposed increases in funding of Operation HELP and the WRAP should be denied.

D. ISSUES FROM PUBLIC INPUT HEARINGS

1. Net Metering and EGSs

At one of the public input hearings, a customer inquired about who provides the compensation for excess electricity produced by customer-generators that purchase their electric generation supplies from an EGS. Tr. 211-12. The Commission's regulations provide, in pertinent part: "The credit or compensation terms for excess electricity produced by customer-generators who are customers of EGSs shall be stated in the service agreement between the customer-generator and the EGS." 52 Pa. Code § 75.13(e). This regulation is appropriate because customer generation reduces the amount of energy purchased by the customer from the EGS and allows the EGS to reduce the amount of generation supplies that it obtains for sale to end-user customers. PPL Electric, as the provider of distribution services, has no role in the provision of generation supplies by an EGS and is properly not responsible for compensation to customer-generators who obtain electric generation supplies from an EGS. PPL Electric St. 8-R, p. 21.

2. Copper versus Aluminum Conductors

At the public input hearings, it was suggested that PPL Electric should be using copper for its conductors rather than aluminum. Tr. 101, 108-110, 131-132, 134-139. This was

primarily based on the belief that the National Electric Code ("NEC") applied to electric utility companies. However, the NEC is not applicable to electric utility installations. *See* Section 90.2(B) of the 2005 National Electric Code Handbook.[26] Rather, it is the National Electric Safety Code that is applicable to public electric utilities. *See* Section 1.011 of the 2007 National Electric Safety Code. PPL Electric St. 8-R, p. 26. Further, due to its advantageous physical characteristics, technological advances, and favorable price as compared to copper, there has been continuous significant growth in the volume, sizes, and varieties of aluminum conductors. Aluminum is now used for virtually all overhead primary (12 kV) and secondary voltage distribution lines and service wires. PPL Electric's predominant use of aluminum conductors is reasonable and appropriate. PPL Electric St. 8-R, pp. 27-29.

3. Service Interruptions and Demand Charges

At the public input hearings, comments were made regarding momentary service interruptions and increases in customers' 15 minute demand charges. Tr. 103-104, 126-129. Momentary interruptions occur periodically on a distribution system for many reasons. Relays and other devices are incorporated into the system in order to isolate malfunctioning equipment and protect the Company and customer equipment as well as Company personnel. Momentary interruptions last only a few seconds at most; whereas, the demand charge is measured in 15 minute intervals. Even if a momentary interruption were to somehow activate electrical equipment, the interruption should activate the equipment only for a very short period of time. Therefore, a momentary interruption would not cause any significant increase in the customer's usage over a 15-minute period. As such, momentary interruptions will not significantly impact a

[26] Note: Section 90.2(B) of the National Electric Code Handbook is identical in the 2002, 2005 and 2008 NEC Code books. The 2008 NEC Book will become effective in 2011.

customer's demand charge. PPL Electric St. 8-R, pp. 24-25. Notwithstanding, PPL Electric is having a Key Account Manager contact the customer who raised the concern at the public input hearing and offer to provide an evaluation of the situation to determine more specifically what is happening and what may be needed to address the customer's concerns. PPL Electric St. 8-R, p. 25.

4. Distribution Rate Increase

During the public input hearings, several customers testified regarding the amount of the distribution rate increase proposed by PPL Electric in this proceeding. It should be noted that PPL Electric undertook all reasonable efforts to keep this increase to the minimum necessary to provide safe and reliable service to its customers. The amount of the originally proposed increase is $7.41 per month for the average residential customer, which translates to about a 5% increase on a total bill basis. PPL Electric St. 6-R, p. 57.

Further, the Company has now procured approximately 80% of its generation supply for customers who will take default generation service during the first five months of 2011. Based on the results of these solicitations, the Company estimates that its generation service charge for an average residential customer will decrease by approximately 9% to 12% from its current rate. On a total bill basis, the net effect of the distribution increase, if granted in full, and the generation rate decrease, if solicitations to date are an accurate indicator, should be a rate decrease for the average residential customer taking default generation service of between 1% and 3%. PPL Electric St. 6-R, p. 58.

To further mitigate the effects of the rate increase as detailed in PPL Electric St. 9, the Company has an extensive set of programs available for low income and payment troubled customers. Finally, under the terms of the Settlement, the Parties have agree to a reduction in the distribution rate increase from approximately $114.7 million to $77.5 million.

5. Energy Efficiency and Conservation

In this proceeding, PPL Electric proposes an increase in the fixed customer charge and the elimination of declining usage blocks. At the public input hearings, several customers raised issues with PPL Electric's rate design and whether it promotes conservation. Tr. 205-207, 209-210, 215-216, 222, 225-226, 258-259, 271-272, 282, 320-321, 328-329. PPL Electric presented extensive evidence that its rate design will promote conservation and energy efficiency. PPL Electric St. 8-R, pp. 8-13. After extensive investigation and negotiations, the parties achieved a Settlement on all residential rate design issues. Under the terms of the Settlement, the fixed customer charge for rate class RS will be increased from $8.44 per month (including USR) to $8.75 per month (excluding USR), the present RTS customer charge of $18.06 will remain in effect. Also, there will be a flat energy rate for residential customers. The lower than filed customer charge and the elimination of declining usage blocks agreed to in the Settlement will encourage conservation. Therefore, the Settlement specifically addresses the concerns raised at the public input hearings.

V. CONCLUSION

WHEREFORE, for all the foregoing reasons, PPL Electric Utilities Corporation respectfully requests that its proposed increase in rates and other proposals set forth in Supplement No. 83 to Tariff – Electric Pa. P.U.C. No. 201, as modified by the Joint Petition for Partial Settlement of Rate Investigation, be approved.

Respectfully submitted,

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