

COMMONWEALTH OF PENNSYLVANIA



OFFICE OF SMALL BUSINESS ADVOCATE

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September 2, 2010

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**HAND DELIVERED**

Rosemary Chiavetta, Secretary  
Pa. Public Utility Commission  
Commonwealth Keystone Building  
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 for filing are the original and nine (9) copies of the Main Brief, on behalf of the Office of Small Business Advocate, in the above-docketed proceeding. As evidenced by the enclosed certificate of service, two copies have been served on all active parties in this case.

If you have any questions, please contact me.

Sincerely,

A handwritten signature in black ink, appearing to read "Steven C. Gray".

Steven C. Gray  
Assistant Small Business Advocate  
Attorney ID #77538

Enclosures

cc: Parties of Record

Robert D. Knecht

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**BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

**Pennsylvania Public Utility Commission :  
v. : DOCKET NO. R-2010-2161694  
PPL Electric Utilities Corporation :**

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**MAIN BRIEF  
ON BEHALF OF THE  
OFFICE OF SMALL BUSINESS ADVOCATE**

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**Dated: September 2, 2010**

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REVENUE ALLOCATION ANALYSIS

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**I. Introduction**

On March 31, 2010, PPL Electric Utilities Corporation (“PPL” or the “Company”) filed with the Pennsylvania Public Utility Commission (“Commission”) a request for additional annual distribution revenues of \$114.675 million.

On May 20, 2010, the Commission suspended the proposed effective date of PPL’s filing and instituted an investigation into the justness and reasonableness of the issues raised in the PPL filing.

On April 29, 2010, the Office of Small Business Advocate (“OSBA”) filed a complaint against the PPL filing.

On May 26, 2010, a prehearing conference was held before Administrative Law Judge (“ALJ”) Susan D. Colwell.

On May 27, 2010, ALJ Colwell issued her Scheduling Order.

On June 29, 2010, the OSBA submitted the direct testimony of Robert D. Knecht. On July 27, 2010, the OSBA submitted the rebuttal testimony of Mr. Knecht. On August 5, 2010, the OSBA submitted the surrebuttal testimony of Mr. Knecht.

On August 26, 2010, the parties filed a partial settlement, which established \$77.5 million as the revenue requirement. The OSBA did not sign the partial settlement but also did not oppose it. Under the partial settlement, numerous issues, *e.g.*, cost of service and revenue allocation, were reserved for litigation.

Evidentiary hearings were held in Harrisburg on August 11, 2010.

The OSBA submits this main brief pursuant to the procedural schedule set forth in ALJ Colwell’s May 27, 2010, Scheduling Order.

## **II. Summary of Argument**

- The cost of service study presented by PPL in this case, with the corrections advocated by the OSBA and adopted by the Company, provides a rational and reasonable basis for revenue allocation and rate design decisions. The cost of service study presented by PPL in its previous base rates cases also provides a rational and reasonable basis for those decisions. Both cost of service studies are reasonably consistent with the underlying methodologies used by PPL in recent base rates cases, and both generally follow the practices set forth in the National Association of Regulatory Utility Commissioners Manual. The range of results produced by these two cost of service studies provides the ALJ and the Commission with the flexibility to adjust the revenue allocation without having to resort to the use of an alternative cost of service study.

- The revenue allocation proposed by the Company should be modified, as proposed by the OSBA, so that certain underpaying classes contribute more towards their cost of service.

- There are three rate classes with above-system average rates of return at proposed rates. In order to move those classes closer to their cost of service in this proceeding, those classes should be granted first dollar relief through the use of rate cuts.

- The GS-3 rate class should be assigned a customer charge of \$30 and a billing demand charge of \$4.5106 per kW, scaled back for any reduction in the class revenue approved by the Commission.

### III. Rate Structure

#### A. Cost of Service

##### 1. The PPL Cost of Service Studies

PPL ultimately submitted two future test year distribution class cost of service studies in this proceeding.

The first cost of service study (“COSS”) employed a new methodology for classifying the Company’s primary system distribution plant (“PPL New”).<sup>1</sup>

The second COSS (“PPL Classic”) was identical to PPL New, except that it used a methodology for classifying the Company’s distribution plant that was the same as that found in the COSSs used by PPL in the Company’s prior base rate proceedings. *See* PPL Statement No. 7-R, at 9-10.<sup>2</sup>

PPL relies primarily on PPL New for its revenue allocation and rate design proposals in this proceeding, although it recognizes that “parties to this proceeding and the presiding ALJ, as well as the Commission, may wish to consider the results of a cost allocation study using exactly the same cost allocation methodology as it used in its two prior base rate proceedings [*i.e.*, PPL Classic].” PPL Statement No. 7-R, at 9-10.

The PPL cost of service studies analyzed the total distribution costs of the Company, then functionalized, classified, and allocated those costs among the various customer classes.<sup>3</sup> As OSBA witness Mr. Knecht observed:

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<sup>1</sup> PPL submitted its new COSS in Exhibit JMK-2 in its original filing. PPL submitted Exhibit JMK-2 Revised on June 17, 2010, in order to correct an error uncovered by the OSBA in discovery. PPL submitted its final version of its new COSS in Exhibit JMK-2A in the rebuttal testimony of Joseph A Kleha. This COSS corrected Exhibit JMK-2 Revised for an error identified by OSBA witness Mr. Knecht, and incorporated PPL’s revised test year accounting claims and revenue allocations. *See* PPL Statement No. 7-R, at 2 and 7.

<sup>2</sup> PPL Classic was also presented in Mr. Kleha’s rebuttal testimony, and is set forth in Exhibit JMK-2B.

<sup>3</sup> *See* OSBA Statement No. 1, at 3-8, for a detailed discussion of cost of service studies.

The underlying principle of a COSS is that costs are assigned to the rate classes that *cause* the utility to incur those costs.

OSBA Statement No. 1, at 4 (emphasis in original).

The Company asserted that the “methodologies” employed by PPL to create its COSSs “generally follow the same principles used by the Company for over thirty years, including its restructuring filing at Docket No. R-00973954 and its most recent base rate case at Docket No. R-00072155.” PPL Statement 7-S, at 6.

However, PPL made one substantive methodological change to its COSS in this proceeding. Specifically, the Company’s “methodology for classifying distribution plant investment and expense into customer and demand-related costs was modified to address some of the criticism raised by the parties in PPL Electric’s recent base rate cases.” *Id.* PPL witness Joseph Kleha explained the change, as follows:

Historically, PPL Electric’s cost allocation studies have not reflected a classification of primary voltage level distribution facilities into their applicable customer-related and demand-related cost components. As a result, in prior base rate proceedings, PPL Electric’s cost allocation studies were criticized regarding the load-carrying capability of the primary voltage level equipment used in its minimum size system studies. In response to this criticism, as I indicated in Statement No. 7, in this proceeding, for the first time, PPL Electric proposed to classify its primary voltage level facilities into their applicable demand-related and ‘minimum or no load’ customer-related cost components.

PPL Statement No. 7-R, at 7-8.

As explained by OSBA witness Mr. Knecht, PPL New differs in “the distribution plant classification methodology used by PPL Electric in its last three base rates proceedings extending back to 1995” because there was no customer component of the primary voltage distribution facilities’ costs in those prior proceedings. OSBA Statement No. 1, at 19.

## 2. The OSBA's Cost of Service Studies

Mr. Knecht replicated PPL's originally filed COSS when the Company declined to provide a fully functional, electronic version of its COSS because of confidentiality concerns. OSBA Statement No. 1, at 11-13.

In his direct testimony, Mr. Knecht concluded that PPL's originally filed COSS methodology would be within the range of industry practice, if two specific corrections were made. *See* OSBA Statement No. 1 at 17. First, Mr. Knecht observed that PPL's classification of services plant needed to be corrected for the error identified in discovery.<sup>4</sup> Second, Mr. Knecht indicated that substation plant should be classified as 100 percent demand-related, rather than classified into both demand-related and customer-related components.<sup>5</sup> Mr. Knecht corrected both of these errors and developed the "IEc Update COSS." *See* OSBA Statement No. 3 at 2.

The OSBA also simulated PPL's originally filed COSS under the distribution plant classification methodology that the Company used in its recent base rates cases. More specifically, Mr. Knecht modified the distribution plant classification methodology to classify all *primary system* distribution plant costs as 100 percent demand-related. Mr. Knecht referred to this COSS as the "PPL Prior Method COSS." *See* OSBA Statement No. 3 at 2.

Mr. Knecht summarized the OSBA's two, differing, cost of service methodologies, as follows:

For the purposes of this proceeding, I have relied both upon the Update COSS [the Company's June revision] and the PPL Prior Method COSS. Based on the information currently available to me, I believe that the results of these two COSS methodologies represent a reasonable range within which revenue allocation and rate design decisions can be made. Both of these methods rely on reasonable cost allocation methodologies, and are reasonably

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<sup>4</sup> PPL subsequently corrected this error in its June revision.

<sup>5</sup> PPL subsequently corrected this error in Exhibit JMK-2A.

consistent with both PPL Electric past practice and the procedures detailed in the NARUC [National Association of Regulatory Utility Commissioners] Manual.

OSBA Statement No. 1, at 21.

Ultimately, PPL generally accepted the adjustments recommended by Mr. Knecht. As a result, there is no material difference between PPL and the OSBA with respect to the COSSs upon which the ALJ and the Commission should rely for revenue allocation and rate design purposes. In that regard, Mr. Knecht concluded:

Therefore, the Company and I generally agree upon the COSS methods that the Commission should consider in evaluating revenue allocation and rate design in this proceeding.

OSBA Statement No. 3, at 2.

In sum, PPL New is consistent with Mr. Knecht's "IEc Update COSS." PPL Classic is consistent with Mr. Knecht's "PPL Prior Method COSS."

### **3. The OCA Cost of Service Studies**

The Office of Consumer Advocate ("OCA") submitted two COSSs in this proceeding. In both OCA COSSs, all joint-use electric distribution plant costs were classified as 100 percent demand-related, and no joint-use distribution plant costs were classified as customer-related.<sup>6</sup>

One OCA COSS allocated demand-related costs using the "Peak & Average" methodology. The other OCA COSS allocated demand-related costs using non-coincident peak ("NCP") demands. *See, e.g.*, OCA Statement No. 1, at 25-26, Tables 6 and 7.

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<sup>6</sup> Joint-use distribution plant is plant that may be used by more than one customer and includes substations, poles, overhead lines, underground lines, transformers, and related equipment. The OCA did not contest the Company's classification of plant dedicated to individual customers, *i.e.*, services, meters and related on-site equipment. *See* OCA Statement No. 3, Schedule GAW-3, page 2 of 15.

Although the OCA performed a COSS using the Peak & Average methodology, the OCA did not appear to be advocating the adoption of that methodology by the Commission. In that regard, OCA witness Glenn A. Watkins identified his recommended COSS as follows:

However, on balance, it is my opinion that my CCOSS [class cost of service study] results utilizing a classification of distribution plant as 100% demand-related, an allocation of demand-related costs based on class NCPs, and my recommended specific account allocation adjustments presents a fair and unbiased estimate of relative contributions to PPL's profitability.

OCA Statement No. 3, at 25.

PPL presented extensive criticism of the OCA's COSSs. *See* PPL Statement No. 7-R, at 10-15. The OSBA did so as well. *See* OSBA Statement No. 2, at 2-10. PPLICA also criticized the OCA's cost of service studies. *See* PPLICA Statement No. 2-R, at 1-7. In essence, the fundamental disagreement that the OCA has with PPL, OSBA, and PPLICA with respect to cost of service methodology can be summarized as follows: Mr. Watkins does not believe that *any* distribution plant costs should be allocated based upon the number of customers. OCA Statement No. 1, at 14; OSBA Statement No. 2, at 2.

The ALJ and the Commission will ultimately decide whether the OCA's COSSs can withstand the detailed criticisms leveled by the Company, the OSBA, and PPLICA. Nevertheless, two observations are uncontested.

First, the NARUC Electric Utility Cost Allocation Manual specifies that joint-use electric distribution plant costs be classified into both demand-related and customer-related components (with the exception of substation costs, which should be classified as 100 percent demand-related). However, neither of the OCA COSSs classifies any joint-use distribution plant costs as customer-related. *See* OSBA Statement No. 2, at 3. *See also* PPLICA Statement No. 2-R, at 4.

Second, the simple fact of the matter is that the primary concept advocated by the OCA in this proceeding – that joint-use distribution plant costs should not have a customer component – has not been adopted by the Commission in any previous PPL base rate case.

## B. Revenue Allocation

### 1. The PPL and OSBA Full Requirement Revenue Allocation Proposals

As set forth above, there are three COSSs that could potentially be used to determine how PPL's distribution revenue increase should be allocated among the Company's customer classes. First, there is the COSS employed by PPL in its last three base rates cases, PPL Classic. Second, there is PPL New, which was presented for the first time in this proceeding. Finally, there is the OCA 100% Demand NCP COSS recommended by OCA witness Mr. Watkins. OCA Statement No. 1, at 25.

The following table sets forth class rates of return under these three COSSs at PPL's present rates:<sup>7</sup>

	<i>PPL New</i>	<i>PPL Classic</i>	<i>OCA COSS</i>
RS	3.3%	5.2%	6.1%
RTS	-3.2%	-4.2%	-4.7%
GS-1	10.3%	12.3%	12.9%
GS-3	22.8%	10.6%	7.0%
LP-4	14.3%	2.2%	2.1%
ISP	9.7%	0.1%	-0.0%
LP-5	-8.6%	-8.7%	-12.1%
LP-6	-6.0%	-6.1%	-11.0%
LPEP	16.3%	16.6%	16.6%
GH	13.8%	6.2%	3.6%
SL/AL	9.3%	8.7%	11.1%
<b>Total</b>	<b>6.3%</b>	<b>6.3%</b>	<b>6.3%</b>

<sup>7</sup> This table reflects the analysis set forth in OSBA Statement No. 2, at 14, Table IEC-R3. Note that the rates of return presented in this table are based on Mr. Knecht's analysis in his direct testimony. Therefore, they differ modestly from the COSS results eventually presented by Mr. Kleha in Exhibits JMK-2A and JMK-2B. The only substantive differences between Exhibits JMK-2A and JMK-2B and Mr. Knecht's analysis are the class rates of return for the LP-5 and LP-6 rate classes. Due to a correction in the allocation of uncollectibles costs to those classes made by Mr. Kleha in his rebuttal testimony, those classes have far lower rates of return than shown in the table.

The following points are readily apparent from this table:

- The RS class is *underpaying* its cost of service under all three COSSs.
- The RTS class is significantly *underpaying* its cost of service under all three COSSs.
- The GS-1 class is significantly *overpaying* its cost of service under all three COSSs.
- The GS-3 class is *overpaying* (sometimes significantly) its cost of service under all three COSSs.
- Rate classes LP-5 and LP-6 are significantly *underpaying* their cost of service under all three COSSs.
- The LPEP class is significantly *overpaying* its cost of service under all three COSSs.
- The street lighting classes (SL/AL) are *overpaying* their cost of service under all three COSSs.

In contrast, for three of the customer classes, the choice of COSS makes a difference in whether the class is overpaying, paying, or underpaying its cost of service. Those classes are LP-4, ISP, and GH.

The Company proposed the following revenue allocation based upon PPL New, using the originally requested revenue increase of \$114.675 million:<sup>8</sup>

<b>PPL Electric Proposed Revenue Allocation</b>				
<b>\$000</b>				
	<i>Current Revenues</i>	<i>Proposed Revenues</i>	<i>Increase</i>	<i>%</i>
RS	\$410,279	\$522,677	\$112,398	27.4%
RTS	3,955	7,007	2,240	56.6%
GS-1	74,155	74,155	--	0.0%
GS-3	117,909	117,909	--	0.0%
LP-4	31,235	30,990	(245)	-0.8%
ISP	1,221	1,468	247	20.2%
LP-5	1,079	1,125	46	4.3%
LP-6	51	40	(11)	-21.6%
LPEP	445	445	--	0.0%
GH	6,377	6,377	--	0.0%
SL/AL	22,407	22,407	--	0.0%
<b>Total</b>	<b>\$669,113</b>	<b>\$783,788</b>	<b>\$114,675</b>	<b>17.1%</b>

To evaluate the reasonableness of the Company's proposed revenue allocation, OSBA witness Mr. Knecht simulated the impact of the Company's proposal on class rates of return using the PPL New and PPL Classic COSSs. He then averaged the class rates of return under those two COSSs. Mr. Knecht explained his reasoning for relying on the simple average of the results of both COSS methodologies, as follows:

[T]he Company and I generally agree upon the COSS methods that the Commission should consider in evaluating revenue allocation and rate design in this proceeding. We disagree only as to the relative weight to give these two alternative COSSs. Mr. Kleha

<sup>8</sup> OSBA Statement No. 1, at 24, Table IEc-4.

would primarily rely on the results of the Exhibit JMK-2A ('IEc Update') COSS [PPL New], because he believes that it is most consistent with the dictates of the NARUC Electric Utility Cost Allocation Manual and because he concludes that the costs for the primary distribution system contain both a customer and a demand component. While I generally agree with Mr. Kleha's arguments, I rely on both COSSs equally. I do so because I believe that the Exhibit JMK-2A ('IEc Update') COSS [PPL New] method will overstate the customer-related component of distribution costs, due to the load carrying capability of the minimum system. I also rely in part on the Exhibit JMK-2B ('PPL Prior Method') COSS [PPL Classic] because it is consistent with a long-established Company practice.

OSBA Statement No. 3, at 2 (footnote omitted).

Mr. Knecht concluded:

As long as the methodologies used in those COSSs are reasonably consistent with cost causation and industry practice, I find that the range of results can be useful to the regulator. Moreover, in light of the well-established concern regarding the load carrying capability of the minimum system, averaging two generally reasonable COSS methodologies in this particular proceeding can provide the Commission with some reasonable assurance that the revenue allocation and rate design are not based on extreme results.

OSBA Statement No. 3, at 3.

The following table sets forth the results of the revenue allocation of the Company's originally filed revenue request based upon the two PPL COSSs, as well as upon Mr. Knecht's average of those two studies:<sup>9</sup>

<b>Comparison of COSS Study Results</b>			
<b>Class Rates of Return at PPL Electric Proposed Rates</b>			
	<i>PPL New</i>	<i>PPL Classic</i>	<i>OSBA Simple Average of these two COSSs</i>
RS	7.1%	9.7%	8.4%
RTS	0.4%	-1.6%	-0.6%
GS-1	10.3%	12.3%	11.3%
GS-3	22.8%	10.6%	16.7%
LP-4	14.1%	2.2%	8.1%
ISP	13.3%	1.6%	7.4%
LP-5	-8.0%	-8.1%	-8.0%
LP-6	-10.6%	-10.7%	-10.6%
LPEP	16.2%	16.6%	16.4%
GH	13.8%	6.2%	10.0%
SL/AL	9.3%	8.7%	9.0%
<b>Total</b>	<b>9.1%</b>	<b>9.1%</b>	<b>9.1%</b>

Based upon the results of this examination, Mr. Knecht observed and recommended the following:

The basic RS residential class exhibits an average rate of return that remains modestly below the system average, after an average distribution-only rate increase of 27.4 percent (compared to a system average increase of 17.1%).

The RTS rate class unfortunately remains well below allocated costs. However, PPL Electric proposes to assign a distribution rate increase of over 50 percent to that class (about 42 percent including the purchase of receivables adjustment, remand riders,

<sup>9</sup> This table reflects the analysis set forth in OSBA Statement No. 1, at 26, Table IEc-5.

Universal Service Rider, and Act 129 Rider charges), which significantly strains the principle of gradualism. While a lower increase for the RTS class may be justified on the grounds of rate shock, I note that the Company's proposed rates for the RTS class will still result in average RTS distribution rates that, on a per-kWh basis, are less than one-half that of the regular residential distribution rates.

The average class rates of return for GS-1, GS-3, GH, LPEP, and SL/AL remain above system average, but by smaller margins.

However, the LP-4 and ISP classes exhibit an average rate of return that is somewhat below system average, at 8.1 percent versus system average of 9.1 percent. In effect, based on my COSS analysis, the Company's proposal overshoots the mark, by moving these classes from an above-average rate of return to a below-average rate of return.

OSBA Statement No. 1, at 26-27.

In order to address the resulting below-average rate of return for LP-4 and ISP, Mr. Knecht recommended that PPL's proposal be modified by assigning a \$1.85 million increase to rate class LP-4, and a \$0.15 million increase to rate class ISP at the full revenue requirement. These rate increases would reduce the share of the \$114.675 million increase allocated to the residential RS rate class. OSBA Statement No. 1, at 27.

Furthermore, because rate classes LP-5 and LP-6 show rates of return far below the system average, Mr. Knecht recommended assigning a total increase of \$1.2 million to the LP-5 and LP-6 rate classes at the full revenue requirement. These rate increases would also reduce the share of the \$114.675 million increase allocated to the residential RS rate class.<sup>10</sup> *Id.*

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<sup>10</sup> As noted in Mr. Knecht's surrebuttal, the adjustment to the LP-5 and LP-6 rate classes will still leave the class rate of return for those classes below zero, after recognizing the correction made by Mr. Kleha in his rebuttal testimony. OSBA Statement No. 3, at 5.

A table showing the OSBA's proposed revenue allocation at the Company's full revenue requirement is set forth below:<sup>11</sup>

<b>OSBA Revenue Allocation Proposal Full PPL Electric Revenue Requirement</b>	
	<i>OSBA</i>
RS	\$109,162
RTS	2,240
GS-1	--
GS-3	--
LP-4	1,605
ISP	397
LP-5	1,241
LP-6	30
LPEP	--
GH	--
SL/AL	--
<b>Total</b>	<b>\$114,675</b>

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<sup>11</sup> This table reflects the analysis set forth in OSBA Statement No. 1, at 11, Table IEC-R1.

The following table compares the class rates of return under the two PPL COSSs and under the OSBA's proposed revenue allocation at the Company's full revenue request of \$114.675 million:<sup>12</sup>

<b>Comparison of COSS Study Results</b>			
<b>Class Rates of Return with the OSBA Revenue Allocation</b>			
	<i>PPL New</i>	<i>PPL Classic</i>	<i>OSBA Simple Average of these two COSSs</i>
RS	6.9%	9.6%	8.2%
RTS	0.4%	-1.6%	-0.6%
GS-1	10.3%	12.3%	11.3%
GS-3	22.8%	10.6%	16.7%
LP-4	15.4%	2.7%	9.1%
ISP	15.4%	2.6%	9.0%
LP-5	9.1%	9.0%	9.1%
LP-6	9.1%	9.0%	9.1%
LPEP	16.2%	16.6%	16.4%
GH	13.8%	6.2%	10.0%
SL/AL	9.3%	8.7%	9.0%
<b>Total</b>	<b>9.1%</b>	<b>9.1%</b>	<b>9.1%</b>

The revenue allocation adjustments recommended by Mr. Knecht to the LP-4, LP-5, LP-6, and ISP rate classes bring those classes to a 9.0% or 9.1% rate of return at the Company's proposed revenue request of \$114.675 million.

## **2. The OCA Full Requirement Revenue Allocation Proposal**

Based upon the 100% Demand NCP COSS, the OCA proposed a revenue allocation in this proceeding. OCA Statement No. 1, at 29. Mr. Knecht summarized the PPL, OSBA, and

<sup>12</sup> This table reflects the analysis set forth in OSBA Statement No. 1, at 28, Table IEC-6.

OCA revenue allocation proposals as follows:<sup>13</sup>

<b>Comparison of Revenue Allocation Proposals Full PPL Electric Revenue Requirement</b>			
	<i>PPL Electric</i>	<i>OSBA</i>	<i>OCA</i>
RS	\$112,398	\$109,162	\$89,800
RTS	2,240	2,240	
GS-1	--	--	--
GS-3	--	--	16,166
LP-4	(245)	1,605	7,036
ISP	247	397	
LP-5	46	1,241	290
LP-6	(11)	30	
LPEP	--	--	--
GH	--	--	1,382
SL/AL	--	--	--
<b>Total</b>	<b>\$114,675</b>	<b>\$114,675</b>	<b>\$114,675</b>

Mr. Knecht explained the difference between the OCA revenue allocation proposal and that advocated by the OSBA, as follows:

Mr. Watkins and I agree that, at the Company's full revenue requirement proposal, the GS-1, LPEP and street lighting classes should be assigned no rate increase. We also agree that the LP-4, LP-5 and LP-6 rate classes should be assigned rate increases, although we differ in the magnitude of those increases. We disagree about the rate increases for the GS-3 and GH rate classes; specifically, Mr. Watkins proposes rate increases for those classes, but I do not.

*Id.*, at 10. Mr. Knecht concluded:

*The overwhelming factor contributing to the different revenue allocation proposals is the cost allocation analyses upon which we rely. PPL Electric relies on its filed COSS, and has presumably concluded that the PPL Update COSS did not necessitate any*

<sup>13</sup> OSBA Statement No. 1, at 11, Table IEC-R1.

change in revenue allocation. I rely on the IEC Update COSS, as well as the PPL Electric Prior Method COSS. Mr. Watkins relies primarily on his two COSS methods, although he appears to consider the results of the PPL Update COSS and the PPL Electric Prior Method COSS with respect to assignment of revenues to the LP-4 and GH rate classes.

OSBA Statement No. 2, at 11 (emphasis added).

Essentially, it is not a surprise that the revenue allocation among PPL's customer classes will change based upon the different COSS methodologies.

As set forth above, the OCA recommended COSS requires a significant methodological change from both PPL New, proposed in this proceeding, and PPL Classic, employed in recent Company base rate proceedings. That change will require that there be no customer component to the classification of the Company's distribution plant costs. That change will also result in a significantly different allocation of the revenue increase, as illustrated above.

Because the OCA COSS is not a reliable indicator of class cost of service, the OCA's revenue allocation should be rejected.

### 3. Allocating the Reduced Revenue Requirement

As filed, the Company requested an overall revenue increase of \$114,675,000. A settlement was reached among the parties to allow PPL to increase its distribution revenue by \$77.5 million. The revenue allocations set forth above were all based upon the allocation of the Company's full revenue request of \$114.675 million.

To address the revenue allocation of the \$77.5 million, the OSBA recommends that first dollar relief ("FDR") be provided to the GS-1, GS-3, and LPEP rate classes. Mr. Knecht explained the OSBA proposal, as follows:

[T]he only rate classes that exhibit above system average rate increases under both COSS methodologies [upon which I rely] are the GS-1, GS-3, and LPEP rate classes.

OSBA Statement No. 1, at 29. *See also Id.*, at 28, Table IEc-6.

Mr. Knecht continued:

To improve progress toward cost-based rates, I recommend that the first \$18.1 million in any reduction to the Company's proposed rate increase be assigned to these three classes (\$6 million to GS-1, \$12 million to GS-3 and \$135,000 to LPEP). I base these dollar values on the objective of providing rate relief to these classes, but retaining the requirement that the class rate of return after FDR remains at or above the system average under both COSS methodologies [upon which I rely].

*Id.*, at 29.

The FDR proposed by the OSBA for the GS-1, GS-3, and LPEP classes is similar to the FDR approved by the Commission in *Pennsylvania Public Utility Commission v. PPL Gas Utilities Corporation*, Docket No. R-00061398 (Order entered February 9, 2007). In that case, FDR was provided for the only class with an above-system average rate of return at proposed rates. Applying that precedent in this proceeding would mean FDR for the only three classes with above-system average rates of return at proposed rates.

The \$77.5 million settlement revenue increase is more than \$18.135 million below the Company's filed revenue request of \$114.675 million. Therefore, the full \$18.135 million FDR proposed by Mr. Knecht can be achieved within the context of the settlement. Furthermore, an additional reduction in proposed revenues of about \$19.1 million ( $\$114.675 \text{ million} - \$18.135 \text{ million} - \$77.5 \text{ million}$ ) is necessary. Mr. Knecht addressed this further rate reduction as follows:

A traditional proportional scaleback is not feasible under the circumstances of this case, because zero increases and rate reductions are being assigned at the full revenue requirement. A proportional scaleback would therefore share none of the reduced revenue requirement with the classes assigned a rate decrease, and would have the perverse effect of actually increasing the revenue from those classes assigned a rate decrease.

I therefore recommend that any further reduction be applied to all rate classes, in proportion to class distribution revenues after the increase and after the FDR. Thus, for example, an additional reduction of \$20 million after FDR would represent about 2.4 percent of distribution revenues. Every class' distribution revenues after FDR would therefore be reduced by 2.4 percent.

OSBA Statement No. 1, at 31.

Finally, Mr. Knecht observed:

Thus, simply because the Company's proposal for a zero rate increase for the GS-1 class may have been reasonable at the full revenue requirement, it cannot be concluded that a zero increase is reasonable under a reduced revenue requirement.

My scaleback proposal addresses this specific issue. By scaling back revenues from all rate classes (including rate reductions for the overpaying classes), my proposal will retain the progress toward cost-based rates that is built into my revenue allocation proposal at the full revenue requirement.

OSBA Statement No. 3, at 8.

A table showing the OSBA's proposed revenue allocation at the \$77.5 settled revenue requirement is set forth below:

<b>OSBA Revenue Allocation Proposal \$77.5 Million Settled Revenue Requirement</b>	
	<i><b>OSBA</b></i>
RS	\$96,245
RTS	2,086
GS-1	(7,695)
GS-3	(14,634)
LP-4	788
ISP	357
LP-5	1,183
LP-6	28
LPEP	(143)
GH	(159)
SL/AL	(557)
<b>Total</b>	<b>\$77,500</b>

A spreadsheet setting forth the arithmetic of the OSBA's revenue allocation proposal is attached to this brief at Appendix A.

The OSBA respectfully submits that rate cuts are appropriate in this proceeding for the GS-1, GS-3, and LPEP classes. As PPL witness Joseph Kleha acknowledged:

[T]he Company has committed to move all rate classes toward the system average rate of return and cost-based rates over three base rate cases.

PPL Statement No. 7-R, at 5. Mr. Knecht explained that this is the third case contemplated by that commitment. Specifically, Mr. Knecht testified as follows:

In the Company's 2004 base rates remand proceeding, PPL Electric ' . . . proposed to move its distribution rates for all major rate classes to at or near full cost of service over the course of three

rate cases including the 2004 rate case.’ In the settlement of the Company’s 2007 base rates case, the parties agreed to assign a rate decrease to the GS-1 rate class, as well as certain other rate classes. Because the current proceeding represents the third case, rates should be modified such that class revenues are at or near allocated costs.

OSBA Statement No. 3, at 7

However, without the rate cut proposed by the OSBA, a straight scaleback of PPL’s original revenue allocation will dilute the move of GS-1, GS-3, and LPEP to cost of service because the settled revenue requirement is about \$37 million less than the Company’s original request. Mr. Knecht detailed this problem, as follows:

Despite PPL Electric’s commitment in its 2004 base rates remand proceeding, the Company determined that the principle of rate gradualism precluded it from immediately moving all rates to cost of service at the Company’s full revenue requirement in this proceeding. *I generally agreed with the Company’s conclusion at the full revenue requirement.*

However, it is critical to recognize that, as the Company’s revenue requirement is reduced, the GS-1 class revenues will move even farther away from allocated costs unless they are also reduced. For example, under the Exhibit JMK-2B (‘PPL Prior Method’) COSS [*i.e.*, PPL Classic], the GS-1 class rate of return is 12.4 percent, or 3.3 percentage points above the system average return of 9.1 percent. However, if the approved revenue requirement is based on an 8.1 percent system average return on rate base, and no decrease is assigned to the GS-1 class, the excess return (*i.e.*, the amount above the system average) from the GS-1 class will increase from 3.3 to 4.3 percentage points. That will be a substantial increase in the magnitude of the cross-subsidy provided by GS-1.

Thus, simply because the Company’s proposal for a zero rate increase for the GS-1 class may have been reasonable at the full revenue requirement, it cannot be concluded that a zero increase is reasonable under a reduced revenue requirement.

OSBA Statement No. 3, at 7-8 (footnote omitted).

The OSBA FDR proposal will retain the progress towards cost-based rates that was built into the revenue allocation proposal at the Company's full revenue request.

**C. Tariff Structure**

Mr. Knecht described the Company's rate design proposal for the GS-3 customer class as follows:

The current GS-3 distribution tariff consists only of a demand charge, with a minimum billing demand of 25 kW. PPL Electric proposes to modify the GS-3 tariff to include a \$50 per month customer charge, and to eliminate the minimum billing demand. In order to keep the overall class rate increase at zero, PPL Electric proposes to reduce the demand charge.

OSBA Statement No. 2, at 18-19.

In his direct testimony, Mr. Knecht supported the Company's proposal to add a customer charge of \$50.00 per month for the GS-3 customer class. OSBA Statement No. 1, at 35.

However, in light of the direct testimony of Frank Richards on behalf of Richards Energy Group ("REG") regarding the bill impact of the Company's proposal, Mr. Knecht stated as follows:

I believe Mr. Richards' direct testimony raises a valid concern that the bill impact on smaller GS-3 customers may be unreasonable. For a 25 kW GS-3 customer, the impact of the PPL Electric proposal would be a monthly bill increase from \$116.93 to \$156.65, an increase of some 34 percent. This increase is about twice the system average distribution increase, and may result in customer dissatisfaction within a rate class that faces a zero overall increase.

OSBA Statement No. 2, at 19.

As an alternative, Mr. Knecht proposed the following:

Therefore, to mitigate the effect on smaller GS-3 customers, I recommend that the GS-3 customer charge in this proceeding be limited to \$30 . . . Based on the figures in Attachment IV-C [Exhibit Regs. §53.53 Part IV -- Rate Structure and Cost Allocation Attachment IV-C (O.G. Kasper)] (page 9 of 27), I calculate that setting the GS-3 demand charge at \$4.5106 per kW of billing demand would produce the same revenues as PPL

Electric's proposal. This change would reduce the bill impact on a 25 kW GS-3 customer from 34 percent to 22 percent.

OSBA Statement No. 2, at 19-20.

The OSBA's proposal will add a customer charge as requested by the Company, albeit at a lesser dollar charge, *i.e.*, \$30 per month versus \$50. The OSBA's proposal will also reduce the GS-3 billing demand charge from the current amount of \$4.677 per kW to \$4.5106 per kW. In other words, to be revenue neutral within the GS-3 class in comparison to the Company's original proposal, the OSBA's proposal will require a higher billing demand charge than the \$4.266 per kW originally proposed by PPL. Thus, raising the billing demand charge will allow the GS-3 customer charge to be reduced from \$50 to \$30 per month.

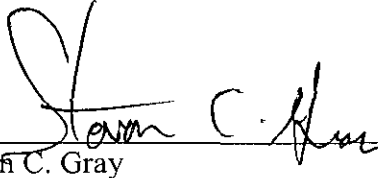
Although the smaller GS-3 customers will experience a rate increase (at the full revenue requirement) because of the Company's rate design proposals, the OSBA's proposal will mitigate the impact upon those customers. That impact will be further mitigated if the ALJ and the Commission approve the OSBA's proposal to give FDR to the GS-3 class, which will require a scaleback of the tariff charges proposed above.

#### IV. Conclusion

Wherefore, the OSBA requests that the ALJ and the Commission:

1. Adopt the PPL New and PPL Classic cost of service studies as the basis for the revenue allocation and rate design decisions in this proceeding;
2. Allocate the \$77.5 million revenue requirement among the rate classes by
  - a. assigning each class a revenue requirement based on an average of the two PPL cost of service studies at the full revenue requirement of \$114.675 million;
  - b. scaling back the full revenue requirement via the OSBA's proposal for \$18.135 million in first dollar relief for the GS-1, GS-3, and LPEP rate classes; and
  - c. allocating the remainder of the reduction in the full revenue requirement to the RS, RTS, LP-4, ISP, LP-5, and LP-6 rate classes on a proportional basis; and
3. Assign the GS-3 rate class a customer charge of \$30 per month and a billing demand charge of \$4.5106 per kW, scaled back for any reduction in the class revenue approved by the Commission.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Steven C. Gray", written over a horizontal line.

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Dated: September 2, 2010

## **APPENDIX**

PPL Electric 2010 Base Rates Case: Docket No. R-2010-2161694										
Revenue Allocation Analysis (\$000): OSBA Scaleback Proposal to Settlement Increase										
	Current Revenue	PPL Proposed Increase	OSBA Adjustments	OSBA Full Requirements Increase	OSBA First Dollar Relief	Revenues After FDR	Scaleback to Settlement Increase	Scaleback Pct of Revenues after FDR	OSBA Proposed Revenues	OSBA Proposed Increase
	(a)	(b)	(c)	(d)	(e)	(f)	(g)	(h)	(i)	(j)
RS	410,279	112,398	(3,236)	109,162		519,441	(12,917)	-2.49%	506,524	96,245
RTS	3,955	2,240		2,240		6,195	(154)	-2.49%	6,041	2,086
GS-1	74,155	-		-	(6,000)	68,155	(1,695)	-2.49%	66,460	(7,695)
GS-3	117,909	-		-	(12,000)	105,909	(2,634)	-2.49%	103,275	(14,634)
LP-4	31,235	(245)	1,850	1,605		32,840	(817)	-2.49%	32,023	788
ISP	1,221	247	150	397		1,618	(40)	-2.49%	1,578	357
LP-5	1,079	46	1,195	1,241		2,320	(58)	-2.49%	2,262	1,183
LP-6	51	(11)	41	30		81	(2)	-2.49%	79	28
LPEP	445	-		-	(135)	310	(8)	-2.49%	302	(143)
GH	6,377	-		-		6,377	(159)	-2.49%	6,218	(159)
Lighting	22,407	-		-		22,407	(557)	-2.49%	21,850	(557)
<b>Total</b>	<b>669,113</b>	<b>114,675</b>	<b>(0)</b>	<b>114,675</b>	<b>(18,135)</b>	<b>765,653</b>	<b>(19,040)</b>	<b>-2.49%</b>	<b>746,613</b>	<b>77,500</b>
<b>Sources:</b>										
(a)	Exhibit IEC-3, page 2, "Total Sale of Electricity" (Also Table IEC-4)									
(b)	Exhibit IEC-3, page 1, "Full Req. Rate Increase" (Also Table IEC-4)									
(c)	OSBA Statement No. 1, page 27									
(d)	(b) + (c)									
(e)	OSBA Statement No. 1, page 29									
(f)	(a) + (d) + (e)									
(g)	Total = (a) + \$77,500 - (g)									
Class = Class Revenues After FDR/System Revenues After FDR * Total Scaleback										
This method is described at OSBA Statement No. 1, page 31.										
(h)	(g)/(f)									
(i)	(f) + (g)									
(j)	(h) - (a)									

**BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

**Pennsylvania Public Utility Commission** :  
v. : **DOCKET NO. R-2010-2161694**  
**PPL Electric Utilities Corporation** :

**CERTIFICATE OF SERVICE**

I certify that I am serving two copies of the Main Brief, on behalf of the Office of Small Business Advocate, by e-mail and first-class mail (unless otherwise noted) upon the persons addressed below:

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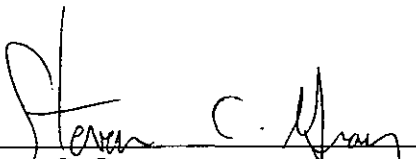
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