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November 8, 2010

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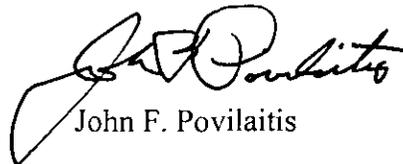
Rosemary Chiavetta, Secretary
Pennsylvania Public Utility Commission
400 North Street – 2nd Floor
Commonwealth Keystone Building
Harrisburg, Pennsylvania 17120

Re: Petition of West Penn Power Company d/b/a Allegheny Power for Expedited
Approval of its Smart Meter Technology and Installation
Plan, Docket No. M-2009-2123951

Dear Secretary Chiavetta:

Attached is an original and three (3) copies of a Reply to Answers in Opposition to Joint Petition for Settlement submitted on behalf of West Penn Power Company d/b/a Allegheny Power in the above-captioned proceeding. In its Secretarial Letter of October 21, 2010 setting the due date for Answers to the Joint Petition for Settlement, the Commission did not address the issue of the Joint Petitioners having the opportunity to respond to the Answers. Allegheny Power therefore requests leave to file the attached Reply to Answers in Opposition to the Joint Petition for Settlement. Copies of this filing have been served on all parties to this case as indicated in the attached Certificate of Service.

Very truly yours,



John F. Povilaitis

JFP/ck
Enclosures

- c. Certificate of Service
The Honorable Mark A. Hoyer
Office of Special Assistants

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**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

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Petition of West Penn Power Company :
d/b/a Allegheny Power for Expedited : Docket No. M-2009-2123951
Approval of its Smart Meter Technology :
Procurement and Installation Plan :

REPLY TO ANSWERS IN OPPOSITION TO JOINT PETITION FOR SETTLEMENT

The Pennsylvania Public Utility Commission ("Commission") Secretarial letter establishing a schedule for Answers and Comments to the Joint Petition for Settlement ("Joint Petition" or "Settlement") filed in this proceeding did not address a responsive filing by either of the Joint Petitioners. West Penn Power Company d/b/a Allegheny Power ("Allegheny Power" or the "Company") therefore respectfully requests leave to file this Reply, limited to certain policy and legal arguments raised in Answers¹ filed by OSBA, WPPII and OTS, expressing opposition to the Joint Petition.²

I. BACKGROUND

The Company and the Office of Consumer Advocate ("OCA") (collectively, the "Joint Petitioners") have agreed to the settlement of the issues in the above-captioned proceeding, and to make all reasonable efforts to obtain this Commission's approval of the Settlement promptly so that the Company's Smart Meter Technology Procurement and Installation Plan ("SMIP"), the last SMIP to come before the Commission for resolution, can be finalized.

The Settlement provides for a further SMIP filing no later than June 2012 (the "Revised SMIP") that will finalize the Company's plans for the full deployment of smart meters to

¹ Answers in Opposition were filed by the Office of Trial Staff ("OTS"), Office of Small Business Advocate ("OSBA") and West Penn Power Industrial Intervenors ("WPII").

² Constellation New Energy, Inc. and Constellation Energy Commodities Group, Inc. (together "Constellation") and the Department of Environmental Protection ("DEP") have indicated they do not oppose the Settlement. Pennsylvania Communities Organizing for Change d/b/a Action United Inc. ("PCOC") has filed a Petition to Intervene and an Answer urging the Commission to approve the Settlement.

Allegheny Power's Pennsylvania customers, consistent with Act 129 and the Commission's Order relating to smart meter implementation. Further details of the SMIP are set forth in the Settlement and Appendices attached thereto. The Statements in Support of the Joint Petition filed by the Company and OCA further address the merits of the proposed settlement, which anticipated to some extent the possible objections to the Settlement by certain parties. Allegheny Power responds to the legal and policy arguments made by OSBA, WPPII and OTS in their Answers as follows.

II. REPLIES TO ANSWERS IN OPPOSITION

A. Reply to the Answer of OSBA

OSBA requests rejection of the Settlement, or in the alternative, imposition of several proposed modifications in the form of conditions. Allegheny Power agrees to certain of those conditions and opposes others.

OSBA requests that the Commission insert an express statement in any order approving the Settlement, to the effect that the approval will not be a mitigating factor in any proceeding considering penalties against the Company for failure to achieve the reductions in electricity consumption mandated by Act 129. The Joint Petitioners have not requested that the Settlement be considered a mitigating factor in some hypothetical future penalty proceeding. The Company opposes this condition because it would constitute a factual determination in a future hypothetical proceeding. To grant OSBA's request would be unlawful from a due process perspective, since any future penalty proceeding should be decided on the basis of the record of that case. It also would be poor policy to start establishing mitigating or non-mitigating factors ahead of a future proceeding, since to do so would ignore the as yet unknown context of such a

proceeding and hamstringing the administrative flexibility the Commission should have in such a case.

OSBA requests that the Commission, in this SMIP proceeding, reject a claimed \$6 million in costs shifted to Small C&I customers in the Amended EE&C/Dr Plan filed by the Company on September 10, 2010 (in a different, separately docketed proceeding) because of a "delay" in smart meter deployment. The Company opposes this condition. The Commission has not yet acted on Allegheny Power's SMIP, therefore there is no "delay" that is being requested. More importantly, it would be unlawful and prejudicial to the Company for the Commission to essentially decide in this SMIP case, the issue of customer class cost responsibility in a different, separately docketed proceeding.

OSBA requests an express statement that the Company's recoverability of \$40 million in SMIP costs be rejected for now or allowed on a tentative basis, subject to refund after an ultimate Commission decision in a future proceeding that occurs presumably after the proposed FirstEnergy Corp and Allegheny Energy, Inc. merger has been approved and implemented. In support of this condition OSBA argues that a further reasonableness and prudence review should occur and recognizes that "the Company could not have anticipated the merger at the time it filed its original EE&C Plan and at the time it filed its original SMIP."³ OSBA is requesting that the prudence of the \$40 million expenditure be evaluated in hindsight after it is clear if a merger has occurred, the Company has upgraded its CIS and other infrastructure, and begun deploying smart meters on a widespread basis.

³ OSBA Answer, p. 12.

The Settlement recognizes that the Company made expenditures between 2009 and 2010 in support of the development of a smart meter deployment plan. These costs are related to activities defined as Phase 1 and Phase 2 activities in the Appendix A accompanying the Settlement. To date, the Company actually has expended approximately \$45.1 million. The Settlement permits only \$40 million to be recovered in the smart meter surcharge, via a levelized surcharge over a 10-year period beginning with the smart meter surcharge start date, with interest (at the statutory rate, currently 6%, on any deferred amounts) to more closely match cost recovery of these up front expenditures to the deployment of the smart meters. Whether the additional \$5.1 million incurred by the Company should be recovered through the smart meter surcharge remains in dispute. The Settlement permits the Company to file for recovery of these disputed amounts in its next distribution base rate case and/or as part of the smart meter surcharge in connection with its Revised SMIP filing. All rights are preserved under the Settlement to continue to dispute the reasonableness of recovery of the \$5.1 million in disputed charges and to oppose any recovery of these costs.

Fundamental Pennsylvania regulatory law provides for the recovery of reasonable and prudent costs of rendering service. The Company's \$40 million of expenditures so qualify. The accuracy of the expenditures is not seriously in dispute. The OSBA position to either delay recovery or subject it to a retrospective examination for reasonableness based on events occurring in the future is inconsistent with the law governing such recovery. Hindsight is always 20/20. But the relevant time for determination of the reasonableness of a utility's expenditures is at the time of the expenditures. Joint Application for Approval of the Merger of GPU, Inc. with FirstEnergy Corp. Docket Nos. A-110300F0095 et al., 2001 Pa. PUC LEXIS 22, 153-154 (Pa. PUC 2001), (The Commission must assess the reasonableness of a utility's decision-making

based upon the state of information available when decisions had to be made and without reliance on hindsight. See Pennsylvania Public Utility Commission v. Philadelphia Electric Company, 71 Pa. PUC 42, 1989, Pa. PUC LEXIS 188 (December 7, 1989).

In a Commission prudence review, utility actions must be based upon facts known or information available at the time a decision is made. "Prudence" is that standard of care which a reasonable person would be expected to exercise under the same circumstances encountered by utility management at the time a decision has to be made. OSBA's request that the prudence of the \$40 million pre-merger expenditure be judged in light of the facts available post merger is inconsistent with the law governing prudence reviews. In determining whether a judgment was prudently made, only those facts available at the time the judgment was exercised can be considered. Hindsight review is impermissible. See Re: Salem Nuclear Generating Station, 60 Pa. PUC 249, 70 PUR 4th 568, 574 (1985)). See also Petitions of West Penn Power Company; Allegheny Ludlum Corporation v. West Penn Power Company, Docket Nos. P-910511; P-910512; P-910512C001, 1992 Pa. PUC LEXIS 14, citing Pennsylvania Public Utility Commission v. Pennsylvania Power Co., 64 Pa. P.U.C. 308, 319. As facts change in the future, or, more facts become known, hindsight may prove the decision to be prudent or imprudent. But such facts may not be used to reconsider the prudence of West Penn's decision at the time that decision was made. To do so would be to engage in hindsight review, which is impermissible. Pennsylvania Public Utility Commission v. Pennsylvania Power Company, R-870732; 1988 Pa. PUC LEXIS 407; 67 Pa. PUC 91; 93 P.U.R.4th 189. OSBA's requested condition should not be adopted.

OSBA requests that the Commission require an *ex post* review of the allocation of the \$40 million among the rate classes to determine the accuracy of the Joint Petitioners calculations and consistency with the Settlement's cost allocation methodology. Allegheny Power does not object to this requirement being added to the Commission's approval of the Settlement since it provides assurances to the parties that their surcharge is accurate.

Finally, OSBA requests Commission acknowledgement that a decision on the costs associated with its Phase 3 deployment of 25,000 smart meters will be made in a future proceeding or that the recovery will be on a tentative basis, subject to refund after a final decision on recoverability is made in a future proceeding.⁴ OCA in its Statement in Support correctly noted that these costs are subject to further review. Allegheny Power does not object to the Commission clarifying in its Order approving the Settlement that the reasonableness of the costs associated with the deployment of the 25,000 smart meters will finally be determined in a subsequent proceeding where those costs are being recovered through the smart meter surcharge.

B. Reply to the Answer of WPPII

WPPII formulates two basic objections to the proposed Settlement. First, WPPII argues that it is speculative whether the proposed deceleration of smart meter deployment will achieve cost savings. The WPPII Answer states that "[t]he Settlement provides no substantive or confirmable evidence that such a significant scale-back in the deployment of smart meters will serve the Commonwealth's objectives and benefit West Penn customers."⁵ The Commission has already approved with respect to the FirstEnergy companies the Settlement's core concept that the grace period will be utilized to develop a final SMIP proposal, so there is no question that the Settlement is consistent with the Commonwealth's objectives. Furthermore, WPPII's argument

⁴OSBA Answer, p. 13-14.

⁵ WPPII Answer, p. 6.

that savings from the decelerated deployment of smart meters are speculative is contradicted by the clearly lower initial monthly smart meter surcharges that are provided by the Settlement – 96 cents instead of \$11.16 for residential, \$1.02 instead of \$12.37 for small commercial customers, and \$1.22 instead of \$14.90 for large commercial and industrial customers.⁶ Also, the Settlement provides a schedule that allows any long term savings that may arise from the proposed merger to be evaluated and injected into the next SMIP filing.

Second, WPPII argues that if the Commission approves the Settlement, it should expressly disallow \$8.1 million in costs from the Commercial and Industrial rate schedules in the Company's pending Amended EE&C/DR filing. The Joint Petitioners have stressed that the Settlement does not dictate any outcome in the pending Amended EE&C/DR filing, nor should it. That case is a separate docket with its own record and WPPII invites the Commission to violate parties rights in that case by making a finding on that case in the SMIP docket. WPPII treats the currently effective Allegheny Power EE&C/DR Plan as inviolate, which is a complete contradiction of the extensive process the Commission has established for the monitoring those plans and the filing and evaluation of proposed amendments to those plans when appropriate.

WPPII's arguments in opposition to the Settlement should be rejected.

C. Reply to the Answer of OTS

Preliminarily, OTS suggests that the Settlement does not comply with the Commission's order establishing a negotiation period in this proceeding because the Joint Petition is not supported by all parties. The reality is that a majority of the parties in this case either support or do not oppose the Settlement. In fact, PCOC has recently filed a Petition to Intervene in this docket and an Answer in support of the settlement. OTS finds the Settlement's resolution of

⁶ See Allegheny Power Supplemental Main Brief, p. 24 for residential rates under the 375,000 smart meter alternative deployment recommended by ALJ Hoyer and attachment REV-1 for the surcharge rates applicable to all customers' rate schedules under the same 375,000 meter alternative.

many issues relating to deployment schedule and costs to be of little weight or value, but that is only because OTS did not address in litigation the core issues of the reasonableness of the Company's smart meter deployment plan or the cost of the Company's proposed SMIP.⁷ Rather, OTS has focused on a narrow set of concerns that have not been recognized by the Commission as valid concerns in the other SMIP proceedings.

OTS argues that the Settlement's assertion that it provides an opportunity to avoid certain near term expenditures and time to analyze whether a less costly smart meter deployment can be designed is not supported by the record.⁸ OTS is incorrect. Using the grace period to develop a final SMIP and take advantage of additional information and future opportunities that may present themselves was precisely the position argued by OCA in litigation, and that position was supported by expert testimony.⁹

OTS argues that the Settlement alters the Company's EE&C/DR Plan by providing for the deployment of only 25,000 smart meters without record support. In fact, the Settlement provides for approximately 90,000 smart meter in phases and the Settlement is careful to make no determinations with respect to the Amended EE&C/DR Plan that is pending before the Commission.

The levelization of cost recovery in the surcharge and consequent delay in the Company's recovery of costs was remedied in the Settlement by the provision of interest. OTS objects to the recovery of interest.¹⁰ However such recovery is permitted by the Commission and is warranted

⁷ See Main Brief of the Office of Trial Staff. OTS limited its litigation of issues in this proceeding to proposing quarterly revenue rate adjustments, the reconciliation procedural schedule, interest on over and under collections, rate of return and capital structure.

⁸ OTS Answer, p. 5.

⁹ OCA Statement No. 1, the Direct Testimony of J. Richard Hornby; OCA Statement No. 2, the Direct Testimony of Nancy Brockway.

¹⁰ OTS Answer, p. 6.

by its acquiescence in the delay of recovering reasonable expenses.¹¹ No hearings are required to establish that provision of interest is within the Commission's legal authority.

OTS asserts that Appendix A to the Settlement lacks sufficient detail.¹² However the work performed in Phases 1 and 2 has largely been completed and was extensively addressed in the record.¹³ Phases 3 through 5 are to be completed in the future. Until the filing of this Answer, OTS did not exhibit any interest in what occurred in any particular phase of the proposed SMIP.

OTS proposals to set return on equity and capital structure on a rolling quarterly basis for smart meter cost recovery has not to date been accepted by the Commission in other SMIP proceedings. The Commission has given no indication it is receptive to such a standard and such standards should not be solely applied to Allegheny Power's SMIP.

The OTS call for hearings on the Settlement and its complaints regarding the expedited Answer period set for the Joint Petition apparently do not echo with any other party to the case. Delaying finalization of the SMIP proceeding for a further extended period of time due to additional hearings is unnecessary and does not recognize the importance of the Commission finishing its important work in this proceeding, which was filed in August of 2009. No hearings are necessary, and the Commission should promptly complete its review of the Joint Petition and approve the Settlement without further formal proceedings.

¹¹ *Investigation Into Demand Side Management by Electric Utilities: Uniform Cost Recovery Mechanism*, 1991 Pa. PUC LEXIS 207, 127 P.U.R. 4th 516

¹² OTS Answer, p. 7.

¹³ See Allegheny Power Statement No. 2, the Direct Testimony of John C. Ahr; Allegheny Power Statement No. 3, the Direct Testimony of Richard C. Arthur, Jr.

WHEREFORE, the Company, by its counsel, respectfully requests that the Commission consider this Reply as part of its disposition and approval of the Settlement, accept OSBA's proposed conditions with respect to reviewing the accuracy of the surcharge's collection of amounts approved for recovery by the Settlement among rate classes and further final review of the costs associated with the deployment of 25,000 smart meters in Phase 3, and otherwise reject the conditions and requirements proposed by the parties objecting to the Settlement.

Dated: November 8, 2010

Respectfully submitted,



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On behalf of West Penn Power Company
d/b/a Allegheny Power

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Petition of West Penn Power Company :
d/b/a Allegheny Power for Expedited : Docket No. M-2009-2123951
Approval of its Smart Meter Technology :
And Installation Plan :

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of the foregoing documents in accordance with the requirements of 52 Pa. Code § 1.54 et seq. (relating to service by a participant).

VIA FIRST CLASS AND
ELECTRONIC MAIL

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