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November 9, 2011

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: William R. Lloyd, Jr., Small Business Advocate v. PPL Electric Utilities Corporation
Docket No. C-2011-2245906

PPL Electric Utilities Corporation Proposed Generation Supply Charge-1 for the period June 1, 2011 through August 31, 2011
Docket No. M-2011-2243137

Dear Secretary Chiavetta:

Enclosed please find the Reply Brief of PPL Electric Utilities Corporation in the above-referenced proceeding. Copies will be provided as indicated on the certificate of service.

Respectfully Submitted,

Anthony D. Kanagy

ADK/skr
Enclosure
cc: Honorable Susan D. Colwell
Certificate of Service

CERTIFICATE OF SERVICE

I hereby certify that true and correct copies of the foregoing have been served upon the following persons, in the manner indicated, in accordance with the requirements of § 1.54 (relating to service by a participant).

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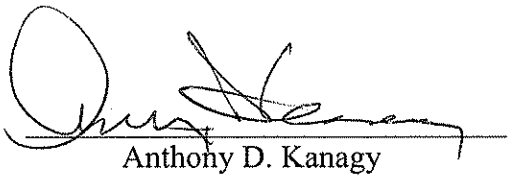

Anthony D. Kanagy

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

William R. Lloyd, Jr. Small Business Advocate, Complainant	: : :	
v.	:	Docket No. C-2011-2245906 M-2011-2243137
PPL Electric Utilities Corporation, Respondent	: :	

REPLY BRIEF OF PPL ELECTRIC UTILITIES CORPORATION

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Dated: November 9, 2011

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I. INTRODUCTION

Pursuant to the procedural schedule adopted in this proceeding, PPL Electric Utilities Corporation ("PPL Electric" or the "Company") and the Office of Small Business Advocate ("OSBA") filed Main Briefs on October 26, 2011. PPL Electric hereby files its Reply Brief in response to the arguments raised in the OSBA's Main Brief. As explained below, the OSBA, standing alone, asks the Administrative Law Judge ("ALJ") and the Pennsylvania Public Utility Commission ("Commission") to reject PPL Electric's reconciliation mechanism, overrule 30 years of precedent, include unbilled revenue in reconciling the GSC-1 rate in violation of Section1307(e) of the Public Utility Code, deny PPL Electric full and current recovery of its default service costs in violation of Act 129, and disrupt competitive retail electric markets, all in order to address a problem that no longer exists and that was caused in the first instance, not by PPL Electric's reconciliation mechanism, but by the Commission's requirement that PPL Electric reconcile its default service rates on a quarterly, instead of an annual, basis. The relief requested by the OSBA is unnecessary, unlawful, would affirmatively harm the retail electric markets and, therefore, should be rejected.

The OSBA filed its Complaint in this proceeding against PPL Electric's June 1, 2011 Generation Supply Cost-1 ("GSC-1 Rate"). The central focus of the OSBA complaint was the large undercollection experienced by the Company during 2010 due to the initial proration of the GSC rate and the resulting large E factor component reflected in the June 1, 2011 GSC-1 Rate. Initially, it must be emphasized that the Company has recovered almost all of the 2010 undercollection from small C&I customers and, as a result, the E factor rate has declined significantly. See PPL Electric Hearing Exh. No. 1. Any problems or concerns resulting from the initial proration of the GSC rate, the resulting 2010 undercollection, and its impact on 2011 GSC-1 rates have been resolved through the normal operation of the GSC-1, and are not

expected to recur in the future. The OSBA's Complaint, therefore, is largely moot. Moreover, the remedy advanced by the OSBA would itself create a new problem, as it would require a substantial refund to small C&I customers which, in turn, would create a large negative E factor that would reduce default service rates significantly and severely disrupt retail competitive markets.

Further, as explained in the Company's Main Brief and herein, the "problem" identified by the OSBA, i.e., the large increase in the June 1 GSC-1 rate, was not due primarily to the amount of the undercollection, but was due to the fact that PPL Electric was required by the Commission, over PPL Electric's objection, to reconcile the GSC-1 quarterly as opposed to annually. If PPL Electric had been permitted to reconcile costs annually, its GSC-1 rate for small C&I customers would have been much lower and much more stable. As PPL Electric explained in its Main Brief, if E factor rates are averaged over the January 2011 through November 2011 period, the resulting E factor rate would be 2.154¢ per kWh and the table below shows the impact on the total rate if the average E factor rate is applied.

Application Period	Total Rate	C Factor Rate	Average E Factor Rate[1]
January 1, 2010 – December 31, 2010	10.125 ¢ per kWh	10.125 ¢ per kWh	0
January 1, 2011 – May 31, 2011	10.447 ¢ per kWh	8.293 ¢ per kWh	2.154 ¢ per kWh
June 1, 2011 – August 31, 2011	10.171 ¢ per kWh	8.017 ¢ per kWh	2.154 ¢ per kWh
September 1, 2011 – November 30, 2011	9.366 ¢ per kWh	7.212 ¢ per kWh	2.154 ¢ per kWh

This table demonstrates that PPL Electric's reconciliation methodology did not cause any rate problems – the problem, if any, is quarterly reconciliation.

[1] PPL Electric recognizes that the average E factor rate above may not be the exact rate that would have been applied if PPL Electric had been permitted to reconcile costs on an annual basis. However, it is a reasonable proxy which demonstrates that rates could have been much more stable.

In its Main Brief, the OSBA has advanced numerous criticisms of PPL Electric's reconciliation methodology, but fails to provide any lawful or reasonable alternative. Any reconciliation methodology must comply with Section 1307(e) of the Public Utility Code, the cost recovery provisions of Act 129, and the rate cap provisions of the Competition Act. As explained herein, PPL Electric's methodology complies with all three statutory provisions. The OSBA's methodology clearly violates the first two statutory provisions cited above and, at least as described by the OSBA in its Main Brief, appears to violate the third.

It is undisputed that PPL Electric's reconciliation methodology is consistent with over 30 years of Commission practice and precedent. Despite all of OSBA's arguments to the contrary, there is good reason to follow, and not abandon, over 30 years of Commission practice and precedent. First, the Company's reconciliation methodology is consistent with the statutory provisions of Section 1307(e). Second, the reconciliation methodology works. PPL Electric recognizes that the undercollection caused a significant rate increase for small C&I customers on June 1, 2011. However, this rate increase was not due to the reconciliation methodology itself, but, instead, due to the fact that PPL Electric was required to implement quarterly, as opposed to annual, reconciliation. If PPL Electric had been permitted to adopt annual reconciliation, the rate increase experienced by customers would have been much lower. Moreover, the overall amount of the undercollection for small C&I customers has been significantly reduced, from approximately $22.35 million as of November 30, 2010 to approximately $1.4 million as of August 31, 2011. See PPL Electric Hearing Exh. No. 1.

For the reasons explained herein, PPL Electric does not believe that any changes to its reconciliation methodology are necessary or reasonable. However, it is clear that any changes must comply with the three statutory provisions cited above and must only be adopted prospectively. The OSBA's proposal to include unbilled revenues in the reconciliation

mechanism cannot be accepted because it would violate Section 1307(e). Moreover, any change must allow PPL Electric to recover its cash working capital costs because, otherwise, the Company will be denied full recovery of its costs to provide default service.

There are several changes that the Company could adopt to provide additional rate stability for customers. First, the Commission could allow PPL Electric to implement an annual, as opposed to quarterly, reconciliation mechanism. This would smooth the rate impacts associated with recovering or refunding over or under collections. The Commission also could approve the Company's proposed Reconciliation Rider and Competitive Transition Rider at Docket No. P-2011-2256365. These proposals would help to stabilize the rate impacts due to reconciliation.

Finally, it is important to note that both the Commission's Bureau of Investigation and Enforcement ("I&E") and the Office of Consumer Advocate ("OCA") participated in this proceeding. Neither of these parties has filed a Main Brief opposing the Company's reconciliation methodology.

For the reasons explained herein and in the Company's Main Brief, the OSBA's Complaint should be denied and dismissed.

II. ARGUMENT

A. BURDEN OF PROOF

In its Main Brief, the OSBA argues that PPL Electric bears the burden of proof because OSBA's complaint was filed against a "proposed rate" as opposed to an "existing rate." See OSBA MB, p. 9. OSBA misstates the issues in this proceeding in an attempt to shift the burden of proof to PPL Electric.

It is clear from OSBA's Main Brief that the gravamen of its complaint is against PPL Electric's reconciliation methodology under the Company's Commission-approved tariff. This is evident by simply reviewing the headings in the Table of Contents for OSBA's Brief. The primary OSBA argument is that "PPL's Reconciliation Accounting Method is Flawed." The case law is clear that complainants bear the burden of proof in challenging Commission-approved tariffs. *Paul Kossman t/a Kossman Dev. Co. v. Pa. P.U.C.*, 694 A.2d 1147 (Pa. Cmwlth. 1997); *Shenango Township Board of Supervisors v. Pa. P.U.C.*, 686 A.2d 910, 914 (Pa. Cmwlth. 1996). In addition, the OSBA even admits in its Brief that the Commission already has approved the Company's reconciliation procedures. On page 11, the OSBA states as follows:

> The OSBA does not dispute that the Commission has approved the reconciliation *procedures* in PPL's tariff.

OSBA MB, p. 11. Because the OSBA is challenging the Company's Commission-approved reconciliation procedures under the Company's Commission-approved tariff, the OSBA bears the burden of proof.

Moreover, to the extent the OSBA is not challenging PPL Electric's reconciliation methodology, the OSBA is challenging the amount of the Company's 2010 undercollection. OSBA MB, p. 25. As the Company explained in its Main Brief, the Commission already has conducted a hearing on the amount of the 2010 undercollection, and PPL Electric bore the burden of proof at that hearing. PPL Electric should not be required to bear the burden of proof

again as to the amount of the 2010 undercollection. The amount of the 2010 undercollection is not a proposed part of the rate, but an existing part of the rate that was approved by the Commission.

On page 10 of its Main Brief, the OSBA argues that the proposed GSC-1 has never been adjudicated and approved by the Commission. This is irrelevant. The OSBA is not challenging PPL Electric's mathematical calculation of the June 1 GSC-1 rate or the reasonableness of the underlying costs. The OSBA is challenging the 2010 undercollection amount which has been adjudicated and approved by the Commission several months before the OSBA filed its Complaint. Because the OSBA's Complaint is against the 2010 undercollection amount and this amount has been approved by the Commission, OSBA bears the burden of proving the 2010 undercollection amount is unreasonable. See 66 P. C.S. § 315(a).

B. REFUNDS

On page 12 of its Main Brief, the OSBA argues that PPL Electric's June 1 GSC-1 rate is subject to refund because it is not a "Commission-made rate." PPL Electric does not agree with the OSBA's "Commission-made rate" analysis. The OSBA is requesting a refund based on a change to PPL Electric's Commission-approved reconciliation procedures. PPL Electric does not agree that a refund can be made because the Company's reconciliation procedures have been approved by the Commission. Therefore, any change to the Company's reconciliation procedures can only be done on a prospective basis. *See Brockway Glass v. Pa. P.U.C.*, 63 Pa. Cmwlth. 238, 437 A.2d 1067 (1981). However, the OSBA is also challenging the Company's actual revenues for 2010 in this proceeding. The Company does not dispute the contention that the amount of its 2010 undercollection, as related to actual costs and revenues, can be subject to refund.

Nevertheless, as explained herein and in PPL Electric's Main Brief, no refund is necessary. PPL Electric's reconciliation methodology has been followed by PPL Electric and the Commission for over 30 years. In addition, PPL Electric has accurately reflected all appropriate costs and revenues in its GSC and GSC-1.

Moreover, as a point of clarification, the fact that the GSC-1 rates may be subject to refund does not mean that PPL Electric bears the burden of proof in this proceeding. As explained above, the gravamen of the OSBA's complaint is against PPL Electric's Commission-approved reconciliation procedures under the Company's Commission-approved tariff. A complainant bears the burden of proving Commission-approved procedures are unreasonable. *Paul Kossman t/a Kossman Dev. Co. v. Pa. P.U.C.*, 694 A.2d 1147 (Pa. Cmwlth. 1997); *Shenango Township Board of Supervisors v. Pa. P.U.C.*, 686 A.2d 910, 914 (Pa. Cmwlth. 1996). Moreover, while the OSBA is legally entitled to file a complaint against the Commission-approved 2010 reconciliation amount, because the amount has been approved by the Commission, the OSBA bears the burden of proving it is unreasonable. 66 Pa. C.S. § 315(a).

C. OSBA FAILS TO PRESENT A LAWFUL AND REASONABLE ALTERNATIVE TO THE COMPANY'S RECONCILIATION METHODOLOGY

In its Main Brief, the OSBA has presented a number of criticisms against the Company's reconciliation methodology. The OSBA argues that the Company's methodology reflects bad accounting principles, that it mismatches revenues and expenses and that it produces unstable default service rates. OSBA MB, pp. 14, 17. Despite these criticisms, with which the Company does not agree, the OSBA has failed to present any lawful and reasonable alternative. Any reconciliation methodology must comply with three statutory mandates:

1. It must comply with the requirements of Section 1307(e). 66 Pa. C.S. § 1307(e).

2. It must provide for full cost recovery under Act 129. 66 Pa. C.S. § 2807(e)(3.9).

3. It must adhere to the generation rate caps established in the Competition Act and PPL Electric's Restructuring Settlement. 66 Pa. C.S. § 2804(4)(ii).

As explained in more detail below, PPL Electric's reconciliation methodology meets all three statutory requirements. PPL Electric's reconciliation methodology fully complies with Section 1307(e) of the Public Utility Code, which requires utilities to reconcile "revenues received" with "expenses incurred" for each period. 66 Pa. C.S. § 1307(e)(1). The Commission's long-standing precedent considers billed revenues as revenues received under Section 1307(e). PPL Electric's practice of reconciling billed revenues for each period against expenses that are incurred fully complies with Section 1307(e).

PPL Electric's reconciliation methodology also provides for full cost recovery under Act 129. The Company's reconciliation methodology provides for a form of cash working capital, which both the Commission and OSBA recognize is a legitimate cost of providing default service. See 52 Pa. Code § 69.1808(a)(4); OSBA MB, p. 23.

PPL Electric's methodology also meets the generation rate cap requirement because PPL Electric prorated revenues received in January 2010 for service rendered before January 1, 2010 and for service rendered after January 1, 2010. If PPL Electric did not prorate revenues, customers would have been charged rates that would have been higher than the capped rates for service rendered in December 2009.

The OSBA's proposed methodology clearly does not meet the first two statutory requirements, and it is unclear whether it meets the third statutory requirement described above. First, OSBA's proposed methodology of including "earned" or in other words unbilled revenues

in the reconciliation calculation violates Section 1307(e). Unbilled revenues are clearly not "revenues received." See 66 Pa. C.S. § 1307(e)(7). Revenues cannot be considered to be received if they have not yet been billed.

OSBA's proposed methodology also does not allow for full cost recovery. OSBA's proposed methodology would deny PPL Electric a cash working capital allowance for providing default service.

In addition, it is unclear whether the OSBA's proposed methodology would have caused PPL Electric to violate the generation rate caps. In its Main Brief, the OSBA argues that "there is no reasonable justification for proration" and that PPL Electric is "not required to use proration." It is unclear what the OSBA means by these statements. However, it is clear that if PPL Electric did not prorate bills sent in January 2010 and charged new uncapped generation rates for all service provided under the bill, customers would have been charged rates that were higher than the capped rates for service rendered in December 2009. Therefore, it appears that OSBA's methodology would violate the generation rate caps.

The following table shows how both PPL Electric's reconciliation methodology and the OSBA's proposed methodology stack up against the three statutory requirements:

Statutory Requirement	PPL Electric's Reconciliation Methodology	OSBA's Proposed Methodology
Section 1307(e) (revenues received and expenses incurred)	Yes	No
Act 129 (full cost recovery)	Yes	No
Competition Act (generation rate caps)	Yes	Unclear

If the Commission modifies PPL Electric's reconciliation methodology, it must adopt a methodology that meets all three of the statutory requirements described above. The Commission cannot simply require PPL Electric to include unbilled revenue or exclude actual expenses from the reconciliation because this would violate Section 1307(e). The Commission cannot deny the Company a cash working capital allowance because this would deny full cost recovery. In addition, the Commission cannot disallow the January 2010 proration because this would violate the generation rate caps and also not allow PPL Electric to fully recover its costs for providing service after the rate caps expire.

D. OSBA'S "MATCHING PRINCIPLE" PROPOSAL IS UNLAWFUL AND INCONSISTENT WITH COMMISSION PRACTICE

1. OSBA's "Matching Principle" Proposal Violates Section 1307(e) And Proration.

In its Main Brief, the OSBA argues that "It is a fundamental principle of accounting to match revenues and costs." OSBA MB, p. 14. Therefore, OSBA argues that PPL Electric must reconcile 12 months of costs with 12 months of "earned" revenue based on those costs in the first application period. OSBA MB, p. 14. This argument is a central component of the OSBA's case. PPL Electric agrees that costs and revenues must match under a Section 1307(e) cost recovery mechanism. However, where proration is adopted for a new Section 1307(e) rate, costs and revenues are matched over two years – not one year. OSBA's matching of 12 months of costs with 12 months of earned revenue, by including unbilled revenue, violates Section 1307(e)(1) and the requirement that PPL Electric prorate revenues in the first month of a new Section 1307(e) cost recovery mechanism.

Section 1307(e)(1) provides for reconciliation of "revenues received" with incurred costs. "Earned" or "unbilled" revenues are not revenues that have been received by the Company. It is clear based upon reading the OSBA's Main Brief and testimony that OSBA's definition of

"earned" revenues includes revenues that have not been billed by the Company. OSBA MB, p. 13. Unbilled revenues have not been received by the Company. Therefore, OSBA's proposal to include "earned" or "unbilled" revenues in the reconciliation formula violates Section 1307(e) and cannot be accepted.

Reconciling billed revenues with actual incurred costs makes sense because it allows Commission auditors to verify the Company's actual costs with actual revenues. Tr. 49. If OSBA's proposal to include unbilled revenues in the reconciliation mechanism were adopted, PPL Electric would be reconciling actual costs with estimated revenues in an Application Period. As explained by Mr. Kleha, who has over 30 years experience on this subject:

> You can't have a true reconciliation of costs that are actual to revenues that are an estimate. That is not a reconciliation.

Tr. 49.

Moreover, PPL Electric is required to prorate revenues received in the first month of a new Section 1307(e) cost recovery mechanism. As explained by Mr. Kleha, PPL Electric and other utilities have prorated customers' bills in the initial implementation month of a new Section 1307(e) cost recovery mechanism for more than 30 years. PPL Electric St. No. 1-R, p. 5. Under proration, PPL Electric was required to reduce billed revenues for January 2010 to eliminate revenues received for service rendered in December 2009, the period prior to the implementation of the Section 1307(e) cost recovery mechanism.

However, it is important to emphasize that the proration effects are included in the E-Factor for the next reconciliation period. As explained by Mr. Kleha in this proceeding:

> Mr. Knecht's analysis is incomplete because he only looks at the first year of application of a new Section 1307(e) cost recovery mechanism. Mr. Knecht fails to consider the effect of the "E factor" component in the second application period of a Section 1307(e) cost recovery mechanism. If the second application period reflects a full 12-month period, it will, by design, include a full 12 months of actual billed revenue and 12 months of actual incurred

> costs in its calculation. It also will include the "E factor" resulting from the first application year's reconciliation, which, by design, accounts for the so-called "missing" 1/2 month of revenue (caused by proration) from the first application year. As a result, at the end of the second application period, the reconciliation of the Section 1307(e) cost recovery mechanism will have matched 24 months of actual incurred costs with 24 months of actual billed revenue.

PPL Electric is properly matching costs and revenues under its GSC and GSC-1.

2. OSBA's "Matching Principle" Is Inconsistent With Over 30 Years Of Commission Precedent.

It is undisputed in this proceeding that the Commission's long-standing practice is to reconcile actual costs with billed revenues. See PPL Electric St. No. 1-R, p. 5; Tr. 49. OSBA's "Matching Principle" proposal would violate over 30 years of Commission precedent because it would include unbilled revenues in the reconciliation calculation. As PPL Electric explained in its Main Brief, OSBA is confusing accounting principles with ratemaking principles. Unbilled revenues are not considered for ratemaking purposes. PPL Electric MB, pp. 24-26.

Moreover, PPL Electric matches costs and revenues under its GSC and GSC-1. As explained above and in PPL Electric's Main Brief, over a two-year period there is a matching of 24 months of costs and 24 months of revenues.

E. PPL ELECTRIC RECONCILIATION METHODOLOGY IS NOT FLAWED

1. PPL Electric Reconciles Costs And Revenues Pursuant To The Statutory Mandates Set Forth In 66 Pa. C.S. § 1307(e).

OSBA argues PPL Electric's reconciliation methodology is unjust and unreasonable because it results in an undercollection "that is not really an undercollection at all...." OSBA MB p. 14. PPL Electric's reconciliation methodology cannot result in rates that are statutorily unjust and unreasonable because PPL Electric reconciles costs and revenues pursuant to the specific language set forth in Section 1307(e) of the Public Utility Code. 66 Pa. C.S. § 1307(e). Section 1307(e)(1) provides that utilities must reconcile "total revenues received" with total

expenses "incurred." PPL Electric reconciles billed revenues with total expenses incurred.[2] PPL Electric St. No. 1-R, p. 8. Unbilled revenues have not been received by the Company.

Moreover, OSBA's notion that the undercollection is not real or did not exist is simply incorrect. Under Section 1307(e), revenues received in an application period are reconciled with total expenses that are incurred in the same period.[3] 66 Pa. C.S. § 1307(e). Under Section 1307(e)(1)(iii), the difference between these two amounts is the amount of the over or undercollection for the application period. OSBA's argument that PPL Electric reported a false undercollection is contrary to the plain language of Section 1307(e)(1). 66 Pa. C.S. § 1307(e)(1).

2. PPL Electric Reconciles Costs And Recoveries Pursuant To Over 30 Years Of Commission Practices And Precedent.

It is undisputed and unrebutted in this proceeding that PPL Electric's reconciliation methodology is consistent with over 30 years of Commission practice and precedent. Despite this, the OSBA argues that PPL Electric's reconciliation methodology is flawed and creates a false undercollection. OSBA MB, p. 14. In effect, the OSBA is arguing that the Commission's long-standing reconciliation methodology, which complies with the statutory provisions of Section 1307(e), is flawed.

The OSBA's argument is without merit. The Commission should not abandon over 30 years of practice to address a problem that no longer exists. As shown on PPL Electric Hearing Exh. No. 1, the undercollection for Small C&I customers, as of August 31, 2011, is approximately $1.4 million. The reconciliation methodology is working as it should.

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[2] In the first month of a new Section 1307(e) cost recovery mechanism, billed revenues historically have been prorated to split revenues for service rendered prior to the new Section 1307(e) cost recovery mechanism and service rendered after the new Section 1307(e) cost recovery mechanism is effective. PPL Electric St. No. 1-R, p. 5.

[3] As explained above and in PPL Electric's Main Brief, the Company was required to prorate revenues received in January 2010. This reduced revenues for the 2010 application period so that only revenues for service rendered on and after January 1, 2010 were included in the reconciliation.

3. Cost Recovery Under A Section 1307(e) Mechanism Is Properly Reviewed Over A Two-Year Period.

In its Main Brief, OSBA focuses on the fact that the reconciliation for 2010 included 12 months of costs and 11 ½ months of billed revenues. OSBA MB, p. 14. As PPL Electric explained above and in its Main Brief, it is not appropriate to focus on a single application period under a Section 1307(e) cost recovery mechanism. The proration of revenues reduces billed revenues in the first month of a new Section 1307(e) cost recovery mechanism. These revenues are reflected in the E-Factor in the next application period. Therefore, cost recovery should be reviewed over a 24-month period or over two application periods. The "missing" ½ month of revenue is factored into the E factor of the second application period so that over a 24-month period there is a matching of 24 months of actual costs incurred and 24 months of actual billed revenue. PPL Electric St. No. 1-RJ, p. 8.

4. Quarterly Reconciliation Caused The Substantial June 1, 2011 E Factor.

There are two questions in this proceeding related to the 2010 undercollection. The first concerns the amount of the 2010 undercollection, and the second concerns the level of the June 1, 2010 E Factor rate. The two questions are related, but it is clear that the OSBA is quite concerned about the level of the June 1, 2010 E Factor rate.

The Company has explained that the real cause of the substantial June 1, 2011 E Factor rate was quarterly reconciliation. If PPL Electric had been permitted to adopt annual reconciliation, the June 1, 2011 E Factor rate for small C&I customers would have been much lower. See PPL Electric MB, pp. 21-23.

F. THE RECONCILIATION METHODOLOGY PROVIDES AN APPROPRIATE FORM OF CASH WORKING CAPITAL.

In its Main Brief, the OSBA agrees that PPL Electric should be permitted to recover a working capital allowance for providing default service. OSBA MB, p. 23. However, OSBA

argues that PPL Electric should not be able to recover working capital costs through the GSC-1 reconciliation because PPL Electric did not make a specific claim for working capital in its default service proceeding. OSBA MB, p. 23. OSBA states as follows:

> If PPL anticipated using its proration accounting method to create an "undercollection" as a source of funds for working capital, the Company shall have sought authorization from the Commission to do so.

OSBA's conclusions are incorrect because the OSBA fails to consider all of the facts. As the Company has explained on many occasions in the proceeding, its reconciliation methodology is consistent with the methodology that it has used and that has been approved by the Commission for over 30 years. PPL Electric was not required to make a specific claim for recovery of cash working capital costs because it deemed the recovery of such costs to be sufficient through the Commission's long-established reconciliation procedures.

PPL Electric did not seek to abandon over 30 years of Commission precedent with regard to its reconciliation methodology in the default service proceeding. PPL Electric did realize that its Commission-approved reconciliation methodology produced a form of cash working capital allowance and, therefore, did not make a separate request to recover cash working capital because this could have constituted a double-recovery of costs.

G. PPL ELECTRIC WAS LEGALLY REQUIRED TO PRORATE REVENUES FOR BILLS SENT IN JANUARY 2010.

At various points in its Main Brief, the OSBA argues that PPL Electric has offered no reasonable justification for proration and that PPL Electric is not required to prorate. OSBA MB, pp. 17, 20. These statements clearly are contrary to law, violate sound ratemaking principles and further would constitute a true violation of OSBA's matching principle.

January 1, 2010 marked a significant change in the default service structure for PPL Electric. Before January 1, 2010, PPL Electric was required to provide default service at capped

rates with no Section 1307(e) cost recovery mechanism to recover its costs. As of January 1, 2010, PPL Electric's rate caps expired and PPL Electric was authorized to fully recover its costs under a Section 1307(e) cost recovery mechanism.

Billed revenues in January 2010 included revenues for service provided in December 2009. PPL Electric was required and authorized by law to prorate revenues or split revenues for service rendered before January 1, 2010 and service rendered on and after January 1, 2010. If PPL Electric did not prorate revenues, this would have caused PPL Electric to include revenues associated with service provided under capped rates in its Section 1307(e) cost recovery mechanism, which recovers costs for providing default service after rate caps expire. This is clearly contrary to law because it would have included revenues that were unrelated to service provided after January 1, 2010 in the Section 1307(e) cost recovery mechanism. This would artificially inflate PPL Electric's revenues and not allow it to recover its full costs for providing service after January 1, 2010.

Moreover, PPL Electric's tariff clearly provides that its GSC is for service rendered on and after January 1, 2010. See OSBA Exhibit D. Therefore, PPL Electric must prorate revenues between service rendered before January 1, 2010 and service rendered on and after January 1, 2010.

Finally, if PPL Electric did not prorate revenues, this would have caused customers to pay higher than capped rates for service rendered in December 2009 when the rate caps were still in effect. This would have violated the Competition Act and PPL Electric's restructuring settlement. See 66 Pa. C.S. § 2804(4).

OSBA's arguments that PPL Electric is not required to use proration, and that PPL Electric has not justified proration, are incorrect.

H. PPL ELECTRIC DID NOT UNDERREPORT REVENUES.

In its Main Brief, the OSBA claims that PPL Electric has underreported revenues for 2010. OSBA MB, p. 25. According to OSBA, PPL Electric's reported year-end undercollection for small C&I customers was $29.2 million while December 2010 unbilled revenues were $14.8 million. According to OSBA, the difference between these two numbers, $14.4 million, resulted from causes other than the accounting method. OSBA MB, p. 25.

The Company's witness, Mr. Woodruff, explained why there could be discrepancies. First, Mr. Woodruff explains that there was no revenue associated with Company use consumption in 2010, but that the practice was changed after the Company's 2010 distribution rate case. PPL Electric St. No. 2-R, pp. 7-8. Mr. Woodruff also explained that there were a number of estimates used in determining default service revenues for the 2010 reconciliation filing. PPL Electric St. No. 2-R, p. 8. Further, Mr. Woodruff explained that differences in rate structure can affect the proration calculation for each customer class. PPL Electric St. No. 2-R, p. 9. However, Mr. Woodruff further explained that on an overall basis, monthly costs and revenues balance out over time. PPL Electric St. No. 2-R, p. 17. Moreover, Mr. Woodruff explained that the Company includes all billed default service revenue and costs in its GSC and GSC-1 charges and all costs and charges are regularly audited by Commission staff. PPL Electric St. No. 2-RJ, p. 2.

In its Main Brief, the OSBA requests that the Commission direct the Bureau of Audits to conduct a detailed audit to evaluate the issues identified by Mr. Knecht. OSBA MB, p. 28. As the Company explained in its Main Brief, this request is unnecessary because the Commission's Bureau of Audits is already auditing PPL Electric's GSC and GSC-1.

I. THE MARCH 8, 2010 LETTER

In its Main Brief, the OSBA argues that a March 8, 2010 cover letter from PPL Electric supports the OSBA's position in this proceeding. OSBA MB, p. 15. PPL Electric disagrees with the OSBA for several reasons.

OSBA states that the letter claims that the undercollection is "not representative of a true over/undercollection." OSBA MB, p. 15. OSBA's reference is correct, but it takes this sentence fragment out of context and, thereby, distorts its plain meaning. As explained above, PPL Electric explained that it was experiencing billing issues with the transition to a competitive market. See Letter, p. 2. In addition, the Company explained that the reported undercollection also was due to proration. Therefore, the comment that it was not representative of a true over/under collection reflected the fact that the primary cause of the undercollection was not due to a difference between actual and estimated costs, but rather was caused by one-time billing issues as part of the transition to a competitive market and by proration which was required by law and PPL Electric's Commission-approved tariff.

The letter also states that "a full year's reconciliation of revenue and costs will generally balance out, because the proration effects are reflected in the first and last months of each annual reconciliation." As Mr. Kleha explained in this proceeding, the proration effect is reflected in the E-factor in the subsequent application period. Tr. 44. The "full year's" reconciliation of revenue and costs referenced in the letter refers to the application of the E-factor in the second year of the GSC-1 rate. This is consistent with the explanation above that costs and revenues balance out over a 24-month period.

J. THE OSBA HAS NOT PRESENTED ANY REASONABLE JUSTIFICATION TO ABANDON OVER 30 YEARS OF COMMISSION PRECEDENT.

According to the OSBA, Commission precedent of reconciling actual costs with billed revenues in Section 1307(e) cost recovery mechanisms is distinguishable based on the facts of this case. OSBA MB, p. 19. As explained herein, PPL Electric's reconciliation practice is not only consistent with Commission practice, but also consistent with Section 1307(e). While the Commission can overturn its precedent in certain situations, it cannot violate the Public Utility Code. Therefore, OSBA's argument regarding Commission precedent is superfluous. Nevertheless, PPL Electric will explain why the OSBA is incorrect that Commission precedent is distinguishable.

First, OSBA argues that an integral aspect of PPL Electric's default service plans is to provide stable rates, and it is not clear "that previous reconciliation mechanisms applied to circumstances in which stable rates were crucial." OSBA MB, p. 19. As PPL Electric explained in its Main Brief, OSBA is clearly overstating the significance of rate stability under Act 129. See PPL Electric MB, p. 27. In addition, the competitive market may provide an opportunity for customers to choose an option which provides additional rate stability.

Second, OSBA argues that it is not clear that earlier reconciliation mechanisms involved costs that represented such a large share of a customer's bill. As explained by Mr. Kleha, this reconciliation methodology has been used for all reconciliation mechanisms, including the Energy Cost Rate ("ECR"), which represented a large part of customers' bills. In addition, this argument from OSBA relates back to its rate stability argument. See OSBA MB, p. 19. In many other proceedings, competitive suppliers have argued against rate stability for default service rates. In addition, in the Commission's recent Tentative Order on retail competition, the Commission recommended that EDCs contemplate expanding hourly priced default service to

medium sized commercial and industrial customers. *Investigation of Pennsylvania's Retail Electricity Market: Recommended Directives on Upcoming Default Service Plans,* Docket No. I-2011-2237952, Order entered October 14, 2011, p. 8. Hourly priced rates are not stable rates. This also demonstrates that the OSBA's rate stability concerns are overstated.

Third, OSBA states that it is not clear that earlier reconciliation mechanisms were intended to be part of a price-to-compare for retail competition and that the Company's reconciliation mechanism results in large reconciliation charges. OSBA MB, p. 20. As PPL Electric explained in its Main Brief, the large reconciliation effect that occurred in the first year was due to the initial effects of proration. PPL Electric MB, p. 23. Moreover, PPL Electric has largely recovered its undercollection. If the OSBA were to prevail, PPL Electric would be required to refund a false overcollection that could significantly reduce the PTC and distort the competitive market. Therefore, the OSBA's proposed "remedy" would create the very problems it claims to be trying to fix.

Fourth, OSBA states that it is not clear that earlier rate mechanisms "were implemented at a time when customers were already facing a substantial rate increase, as was the case for the GSC." OSBA MB, p. 20. According to the OSBA, this makes rate stability a more important rate design attribute. This argument again relates to rate stability. As explained above, the OSBA is touting rate stability as the most important aspect of default service programs, despite the fact that rate stability is only one component of Act 129. In addition, the OSBA's point regarding rate stability when the GSC was implemented is moot because that occurred approximately two years ago, and PPL Electric cannot go back in time and change rates that were charged to customers.

The OSBA has not presented any substantial justification for abandoning over 30 years of Commission precedent in this proceeding. Moreover, as explained above, Commission

precedent cannot be abandoned because Commission precedent complies with the statutory requirements of Section 1307(e). 66 Pa. C.S. Section 1307(e).

K. OSBA'S ARGUMENT THAT SHOPPING DOES NOT INCREASE THE UNDERCOLLECTION AMOUNT MISINTERPRETS MR. KLEHA'S TESTIMONY.

In its Main Brief, OSBA cites PPL Electric St. No. 1-R at page 9 and argues that "Mr. Kleha attempted to explain the magnitude of the 2010 reported undercollection as being a function of increased customer shopping." OSBA MB, p. 22. The OSBA has misinterpreted Mr. Kleha's Rebuttal Testimony. In his Rebuttal Testimony, Mr. Kleha was explaining how the increase in the number of shopping customers increased the GSC-1 rate for customers because there were fewer customers to pay the undercollection that was incurred in 2010. As a result of the increased level of customer shopping, the E-factor rate charged to remaining default service customers in the GSC-1 was increased.

In addition, at the hearing, Mr. Kleha explained how Settlement B PJM costs for each application period are not received until two months after the period has ended, after customers who created those costs had left default service to shop with alternative generation suppliers. Tr. 36. As more customers shop, they are not available to pay for the default service undercollection, even though the Settlement B true up costs may have been related to service provided to these customers.

L. OSBA'S REQUESTS FOR RELIEF SHOULD BE DENIED.

On page 30 of its Brief, the OSBA makes three requests for relief. These requests should be denied. First, the OSBA requests that the ALJ and the Commission find that PPL Electric's accounting methodology resulted in rates that were not just and reasonable. As explained herein and in the Company's Main Brief, PPL Electric reconciles actual received (billed) revenues and

actual incurred costs pursuant to the methodology set forth in Section 1307(e) of the Public Utility Code and long-standing Commission precedent.

Second, the OSBA requests that the ALJ and the Commission direct the Bureau of Audits to conduct a detailed audit of the Company's default service revenues and costs for 2010. As the Company has explained in this proceeding, the Bureau of Audits already is conducting an audit of the Company's 2010 GSC and 2011 GSC-1, which includes default service costs and revenues for 2010. Therefore, this request is unnecessary.

Third, the OSBA requests that the ALJ and the Commission direct PPL Electric to make refunds as appropriate to default service customers. For all of the reasons that PPL Electric has explained in this proceeding, the Company has properly reconciled its revenues and costs pursuant to Section 1307(e) and over 30 years of Commission practice and precedent. There are no grounds for refunds.

Moreover, it is important to note that one of the OSBA's primary arguments in this proceeding concerns unbilled revenues for December 2010. It must be emphasized that unbilled revenues in December 2010 became billed revenues in January 2011. These revenues were included in the reconciliation for the January 1, 2011 through May 31, 2011 application period, which was included in the June 1, 2011 GSC-1 rates. Therefore, the June 1 GSC-1 rate included all December 2010 revenues in the calculation. PPL Electric should not be required to add unbilled revenues for December 2010 into its prior reconciliation because they already have been included as billed revenues in January 2011.

M. ALTERNATIVES TO INCREASE RATE STABILITY.

One of OSBA's primary arguments in this proceeding is that the Company's reconciliation methodology does not produce stable rates. The Company explained in its Main Brief that it does not anticipate that customers will experience significant rate fluctuations due to

proration in the future. PPL Electric MB, p. 23. However, in the event that rate stability is a concern, there are several alternatives that the Commission could consider.

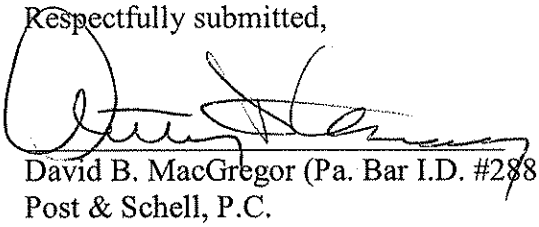
First and foremost, the Commission could allow PPL Electric to reconcile on an annual, as opposed to quarterly, basis. This would smooth rate impacts for customers. See PPL Electric MB, pp. 21-23. Second, the Commission also could approve the Company's Reconciliation Rider ("RR") and Competitive Transmission Rider ("CTR") filing at Docket No. P-2011-2256365. As Mr. Kleha explained, the RR and CTR will help promote rate stability for customers. PPL Electric St. No. 1-R, pp. 13-14.

Moreover, even Mr. Knecht admits that the RR will reduce rate variability. In the RR and CTR proceeding, Mr. Knecht submitted testimony on November 2, 2011. On pages 6-7 of that testimony, Mr. Knecht stated that the RR will have the benefit of smoothing rate variances.

III. CONCLUSION

PPL Electric Utilities Corporation has clearly and unequivocally demonstrated in this proceeding that its reconciliation methodology is consistent with Section 1307(e) of the Public Utility Code and over 30 years of Commission practice and precedent. The Office of Small Business Advocate has presented many criticisms of the Company's reconciliation methodology. However, the Office of Small Business Advocate has not presented any proposal that would comply with Section 1307(e) or allow the Company to fully recover its costs. For the reasons explained herein and in PPL Electric Utilities Corporation's Main Brief, the Office of Small Business Advocate's Complaint should be denied and dismissed.

Respectfully submitted,



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