

COMMONWEALTH OF PENNSYLVANIA



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September 17, 2012

Rosemary Chiavetta, Secretary
PA Public Utility Commission
Commonwealth Keystone Bldg.
400 North Street
Harrisburg, PA 17120

RE: Petition of PECO Energy Company for Approval of
Its Default Service Program
Docket No. P-2012-2283641

Dear Secretary Chiavetta:

Enclosed please find the Office of Consumer Advocate's Reply Exceptions to the Recommended Decision in the above-captioned proceeding.

Copies have been served upon all parties of record as shown on the attached Certificate of Service.

Sincerely,

Candis A. Tunilo

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Assistant Consumer Advocate
PA Attorney I.D. # 89891

Enclosures

cc: Hon. Dennis J. Buckley, ALJ
Certificate of Service

*154966

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Petition of PECO Energy Company :
For Approval of its Default : Docket No. P-2012-2283641
Service Program :

REPLY EXCEPTIONS
OF THE OFFICE OF CONSUMER ADVOCATE

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Dated: September 17, 2012

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I. INTRODUCTION

On August 29, 2012, the Office of Administrative Law Judge issued the Recommended Decision (R.D.) of Administrative Law Judge (ALJ) Dennis J. Buckley in the Default Service Plan (DSP) proceeding of PECO Energy Company (PECO or the Company). Exceptions were filed on September 10, 2012. The OCA's positions in this proceeding are fully addressed in its Main Brief, Reply Brief, and Exceptions. The OCA files these Reply Exceptions to certain Exceptions filed by the Retail Energy Supply Association (RESA), FirstEnergy Solutions (FES), and Dominion Retail, Inc./Interstate Gas Supply, Inc. (Dominion).

II. REPLY EXCEPTIONS

A. The OCA's Reply As To Default Service Procurement Issues.

OCA Reply to RESA Exception 3: The ALJ Correctly Recommended Adoption of PECO's Planned 2014 Residential Contingent Procurement Process. (RESA Exc. 7-9; R.D. at 26-27; OCA M.B. at 26-28; OCA R.B. at 12-14)

In its Exceptions, RESA recommends that PECO's residential procurement plan be modified so that none of its projected 2014 contract procurements would extend beyond May 31, 2015. The ALJ adopted PECO's procurement proposal and stated that "the Commission should reject RESA's proposal to eliminate PECO's scheduled 2014 procurements." R.D. at 27. The ALJ concluded that:

RESA offers no explanation for why it believes it will be easier to address these risks through a new procurement plan at some future date instead of removing a limited number of previously scheduled solicitations from PECO's plan if and when the need arises.

R.D. at 27.

For the procurement of supply products that extend beyond May 31, 2015, PECO established a contingency plan in the event that there are major changes implemented that would alter default service procurement at the end of the upcoming default service period. PECO

proposed to continue to procure “laddered” contracts that could extend beyond the end of the default period, but PECO witness McCawley explained that the procurements for these products are not scheduled to occur until January 2014 or later, and therefore, there is time to adjust the procurement schedule if changes to default service are adopted. PECO St. 2-R at 7-8. The OCA submits that this is a reasonable approach to the DSP II procurement plan, as it is the best approach to achieve price stability and avoid having to procure a large percentage of a portfolio’s power supply in a single procurement (*i.e.*, for delivery on June 1, 2015).

In its Exceptions, RESA argues that “the least complicated course of action would be to make any adjustments that may be necessary after the Commission issues its guidance.” RESA Exc. at 8. The OCA disagrees that this would be the least complicated approach. OCA witness Hahn and PECO witness McCawley addressed the potential significant issues raised by the elimination of such a contingency plan. OCA witness Hahn explained the importance of laddering:

The concept of layering and laddering of power supply contracts with periodic solicitations throughout the year is an accepted industry practice to achieve price stability, stage solicitations reasonably close to the date of commencement of deliveries, and avoid procuring a large percentage of a portfolio’s power supply in a single procurement. Having all contracts expire on a specific date will undermine that approach.

OCA St. 1-R at 9-10. PECO witness McCawley cited similar reasons as outlined by OCA witness Hahn and stated that “A contract laddering strategy mitigates the rate volatility associated with replacing a large portion of supply in a short period of time.” PECO St. 2-R at 7.

RESA’s Exceptions cites to the Commission’s first Default Service Order as a basis for the elimination of the contracts that extend beyond May 31, 2015. Investigation of Pennsylvania’s Retail Electricity Market: Recommendations Regarding Upcoming Default Service Plans, Docket No. I-2011-2237952 (December 16, 2011) (December 16 Final Order).

Contrary to RESA's Exceptions, the plain language of the December 16 Final Order does not require EDCs to eliminate overhanging contracts but states that EDCs should only **limit** the amount of "short-term energy contracts extending past the end date of the upcoming default service plan period." The Commission went on to state:

Notably, these guidelines are not intended to inhibit EDCs from developing default service plans that include a prudent mix of contracts that achieve the "least cost to customers over time." The Commission reiterates that it will not mandate a prescriptive portfolio of contract lengths and will allow EDCs to retain flexibility in developing plans that meet Act 129 requirements. **For this reason, the Commission declines to accept RESA's and Direct Energy's recommendations that the Commission direct EDCs to develop portfolios that include a more specific mix of contracts.**

December 16 Final Order at 19-20. (Emphasis added). The OCA notes that RESA specifically proposed that the Commission direct that the EDCs eliminate contracts extending beyond the end date of their next default service plans. The Commission clearly gave the EDCs discretion on this issue.

RESA also cites to the Joint Petition of Metropolitan Edison Company, Pennsylvania Electric Company, and West Penn Power Company for Approval of Their Default Service Programs (FirstEnergy DSP II) as a reason for the elimination of the contingency plan for PECO's procurements that extend beyond May 31, 2015. RESA Exc. at 8; FirstEnergy DSP II, Docket Nos. P-2011-2273650 *et al.*, Order at 26-27 (Aug. 16, 2012). There is an important difference between FirstEnergy's DSP Plan and PECO's DSP Plan. FirstEnergy proposed relying upon 24-month full requirements contracts for its Plan. FirstEnergy DSP II, Order at 25-26. Here, PECO has proposed a laddering of contracts in a contingency plan which can be eliminated should changes to default service be adopted. For this reason, the December 16 Final Order provided that the EDCs should have the discretion to decide these issues based upon their individual plans.

The OCA submits that PECO's proposal for the supply plan to be laddered so that default service customers are not fully exposed to changing market conditions at a single point in time should be approved. The OCA submits that there is no justification to leave customers fully exposed to potential dramatic price spikes in the future. OCA St. 1-R at 9-10. As explained above, RESA's proposal should be rejected in favor of a more laddered approach that reduces the risk of an abrupt price spike at the end of the DSP II Plan, and the ALJ's Recommended Decision on this issue should be adopted.

B. The OCA's Reply As To The Creation of A 0.5¢ Per kWh Adder.

OCA Reply to RESA Exception 7: The ALJ Correctly Rejected The Creation of A 0.5¢ Per kWh Adder To The Price of Default Service. (RESA Exc. at 20-23; R.D. at 51-54; OCA M.B. at 47-53; OCA R.B. at 27-33).

1. Introduction.

RESA proposed to add a 0.5¢ per kWh adder¹ to the price of default service for PECO's default service customers that would serve to increase the Price to Compare (PTC). According to RESA, the adder would work as follows: (1) it would be collected from PECO's default service customers; (2) a portion of the collected amounts would be used to pay for the implementation and maintenance of competitive market enhancements; (3) PECO would retain some portion (not more than 10%) if certain unspecified customer migration benchmarks were reached; and (4) the remaining amounts would be refunded to all of PECO's distribution customers. RESA St. 1 at 34. RESA alleged that the 0.5¢ per kWh adder would compensate the Company for currently unrecovered costs of providing default service in addition to paying for the implementation and maintenance of competitive market enhancements. RESA St. 2-SR at 24. OCA witness Hahn, however, concluded that RESA's proposed adder would artificially

¹ RESA named its proposed 0.5¢ per kWh adder the Default Service Cost Recovery Charge (DSCRC) in its Main Brief. See RESA M.B. at 36. Parties in this matter continue to refer to the charge as an "adder." See OCA R.B. at 27-33; PECO R.B. at 25-26.

increase default service rates substantially and increase PECO's annual profits by approximately \$6.6 million. See OCA St. 1-R at 7. It is important to note that despite this increased profit opportunity, PECO itself opposes RESA's proposed adder, and the Company has not expressed any concern that it is not fully recovering its costs as the default service provider. See PECO M.B. at 46.

In the Recommended Decision, the ALJ rejected RESA's 0.5¢ per kWh adder proposal stating that:

I agree with PECO and the OCA that the end-result of the proposed PTC Adder would be the artificial inflation of the PTC with corresponding inaccurate price signals and cross-subsidization of PECO's shopping customers by default service customers. No public benefit would be conveyed by the adoption of a measure for which no need has been shown and which would only serve to distort price signals. The PTC Adder proposal by RESA and supported by Dominion should be rejected by the Commission.

R.D. at 54. The ALJ's recommendation is consistent with the Commission's rejection of a similar adder proposed in FirstEnergy DSP II. FirstEnergy DSP II, Order at 62-63. RESA has submitted Exceptions on this issue. The OCA submits that the ALJ's decision on this issue is consistent with the law and sound public policy, and accordingly should be upheld.

In its Exception on this issue, RESA asserted that ALJ was wrong in recommending rejection of its 0.5¢ per kWh adder because: (1) the 0.5¢ per kWh adder would not artificially inflate the PTC; (2) collecting the 0.5¢ per kWh adder from default service customers and returning remaining amounts to all customers would not amount to cross-subsidization of shopping customers by non-shopping customers; and (3) implementation of the adder would convey a public benefit. RESA Exc. at 20-21. The ALJ properly rejected these arguments.

2. The ALJ Correctly Held That RESA's 0.5¢ Per kWh Adder Would Artificially Inflate the PTC.

As to RESA's first argument that its 0.5¢ per kWh adder would not artificially inflate the PTC, RESA goes on to assert that its adder aligns with the actual costs of providing default service because PECO may incur direct and contingent costs that are inadequately reflected in the Company's default service cost recovery mechanism, the Generation Supply Adjustment charge (GSA). RESA Exc. at 21. The ALJ correctly rejected this argument, stating in relevant part:

[RESA witness] Kallaher identified these costs, but submitted no cost data and did not indicate whether such costs have ever been incurred by PECO or not recovered under the GSA. Rather, Mr. Kallaher simply listed certain hypothetical expenses that may not have been charged to default service customers to date. Such hypothetical expenses cannot form the basis for cost recovery.

* * *

Second, PECO contends, and I agree, that the amount of the PTC adder—\$0.005 per kWh—does not align in any way with the administrative costs of providing default service or PECO's proposed RME [Retail Market Enhancement] programs. ... Accordingly, the revenue generated from RESA's proposed PTC Adder would far exceed the costs it purported to recover. Such a large and artificial increase in the PTC would send inaccurate price signals to customers and could lead to an increase in prices that EGSs offer.

R.D. at 52-53. (Internal citations omitted).

The ALJ correctly found that there is no legal basis for the adder, as the Company is already authorized by the Public Utility Code to recover all costs, on a dollar-for-dollar basis, of providing default service. As to artificially inflating the PTC, OCA witness Hahn testified:

Including an arbitrary adder in the cost of default service will result in higher default service rates, and the DSP would no longer be consistent with a least cost standard. Furthermore, it will increase the PTC, which will allow EGSs offering a percentage discount off the PTC to achieve the minimum savings level at a higher price. This could and likely would increase the costs to customers including those who participate in the Retail Opt-In Auction or Customer Referral Programs. The same theory applies to EGSs selling to customers through normal sales channels and not through any retail market enhancement program. A higher PTC will likely cause higher prices for selling one by one in the retail market.

Thus, the real effect of the RESA proposal is to increase the power supply costs for both default services customers and customers who take advantage of the retail market.

OCA St. 1-R at 7-8. PECO witness Cohn agreed, stating that “[s]uch a large and unjustified increase in the PTC would also send inaccurate price signals to customers.” PECO St. 5-R at 12. As OCA witness Hahn and PECO witness Cohn testified, and the ALJ concluded, the substantial evidence produced in this matter shows that RESA’s 0.5¢ per kWh adder would result in an impermissible artificial increase to PECO’s PTC. R.D. at 52-54.

The OCA further submits that RESA’s adder proposal would permit PECO to recover a profit on the provision of default service because it is pre-tax money that PECO is permitted to retain without any added risk. Pennsylvania law does not permit a profit on the provision of reconcilable default service. The Public Utility Code provides, in relevant part:

The default service provider shall have the right to recover on a full and current basis, pursuant to a reconcilable automatic adjustment clause under section 1307 (relating to sliding scale of rates; adjustments), all reasonable costs incurred under this section and a commission-approved competitive procurement plan.

66 Pa. C.S. § 2807(e)(3.9). See also OCA M.B. at 50-51. A plain reading of the statute indicates that the default service provider has a right to “recover” all reasonable costs “incurred.” ALJ Susan D. Colwell succinctly captured the cost recovery structure of default service in a recent decision, stating: “[a] default service provider is entitled to full recovery of its costs because it is not permitted to make a profit on the cost of the commodity.” Petition of PPL Electric Utilities Corp. for Approval to Implement a Reconciliation Rider for Default Supply Service, Docket No. P-2011-2256365, R.D. at 35 (April 4, 2012). The Courts of Pennsylvania have also plainly addressed the issue of cost recovery by a public utility for “costs” that a utility does not incur.

The Supreme Court of Pennsylvania has held that:

Although the Commission is vested with broad discretion in determining what expenses incurred by a utility may be charged to the ratepayers, the Commission has no authority to permit, in the rate-making process, the inclusion of hypothetical expenses not actually incurred. When it does so, as it did in this case, it is an error of law subject to reversal on appeal.

Barasch v. Pa. PUC, 493 A.2d 653, 655 (Pa. 1985). (Emphasis added). On this same issue of illusory costs, the Commonwealth Court of Pennsylvania has held that:

However, a utility may pass along to its customers only those expenses or costs it actually incurs. Any other approach would permit the utility, by charging higher rates than necessary, to gain a profit from its customers under the guise of recovering operating expenses.

Cohen v. Pa. PUC, 468 A.2d 1143, 1150 (Pa. Commw. Ct. 1983). (Internal citations omitted).

See also Barasch v. Pa. PUC, 532 A.2d 325, 336 (Pa. 1987); Popowsky v. Pa. PUC, 695 A.2d 448, 455 (Pa. Commw. Ct. 1997). Additionally, ALJ Susan D. Colwell recommended that the Commission reject a similar charge in FirstEnergy DSP II, stating:

The MAC [Market Adjustment Charge] is in conflict with the Public Utility Code in several respects, particularly since the Companies receive full recovery of all costs of providing default service on a dollar-for-dollar basis through an automatic adjustment surcharge.

FirstEnergy DSP II, R.D. at 56. The Commission adopted the ALJ's recommendation, stating:

While under the Code, the Companies are entitled to recover all actual costs to provide default service on a dollar-for-dollar basis, the Companies and other Parties failed to provide sufficient empirical support for any actual known and measurable costs that are not being recovered through existing or proposed rates and riders. Accordingly, we adopt the ALJ's recommendation and deny the Exceptions related to the establishment of a MAC.

FirstEnergy DSP II, Order at 62-63. The Public Utility Code, prior Commission decisions and the Courts of Pennsylvania have made clear that the creation of a profit through the recovery of hypothetical costs is impermissible.

The only alleged costs that RESA claims that PECO does not adequately recover through its GSA are: the costs of credit security, overhead and administrative costs.² RESA Exc. at 21. As explained in OCA's Main Brief, RESA's assertions regarding these alleged costs completely lack merit. See OCA M.B. at 52-53. As stated in OCA's Main Brief:

PECO's maintenance of a high credit rating and operation of call centers benefits all distribution customers, not just default service customers. A high credit rating reduces PECO's risk rating and allows it to obtain credit at satisfactory rates, which credit, when used to obtain financing, benefits all distribution customers through base rates. Further, such credit rating is reflected in the Company's return on equity, the opportunity of which to earn is on the distribution portion of PECO's provision of service and therefore, is collected from all distribution customers. Regarding call centers, call centers benefit all distribution customers, since, for example, all distribution customers are directed to call PECO to report an outage.

OCA M.B. at 52-53. Most importantly, PECO itself has not expressed any concern that it is not fully recovering its default service costs. See e.g. PECO M.B. at 46. The OCA submits, further, that the approximately \$6.6 million per year that PECO stands to retain pursuant to RESA's proposal (see OCA M.B. at 49) is significantly more than any unrecovered costs that RESA alleges that PECO incurs as a DSP.

The OCA submits that there is no basis for RESA's proposed 0.5¢ per kWh adder as a cost recovery mechanism. Since it is more correctly classified as a wholly unjustified profit adder to the provision of default service, the ALJ's decision on this issue is in accord with the law and should be upheld.

3. RESA's 0.5¢ Per kWh Adder Proposal Would Result In Improper Subsidization Of Shopping Customers By Default Service Customers.

As discussed above, there is no provision in Pennsylvania law to authorize a profit on the provision of reconcilable default service. In addition, even if all of RESA's 0.5¢ per kWh adder

² RESA witness Kallaher described these as "costs associated with maintaining a high credit rating or operating call centers, which benefit default service customers, but are paid for by distribution customers." RESA St. 2-SR at 24.

were paid back to distribution customers, the adder would result in an improper subsidization of PECO's shopping customers by its default service customers. Mr. Hahn explained the inappropriate subsidy as follows:

I also note that the RESA proposal applies the 5 mils per KWH adder to default service rates, but distributes any amounts remaining, after paying expenses and the PECO incentive, to all customers. Thus, this proposal will cause default service customers to subsidize customers who obtain power supply from an EGS. Default service customers will pay 100% of the costs but receive 75% or less of the remaining funds. This transfer of wealth or economic benefit is unsupported by any cost causation, is extremely inequitable, and discriminatory.

OCA St. 1-R at 8 (The 75% figure applies if 25% of residential customers in PECO's territory are shopping). PECO witness Cohn agreed with OCA witness Hahn's assessment of the impermissible subsidy, noting that it would be inappropriate to collect a charge from one group of customers (default service customers) and refund excess amounts to another group of customers (all distribution customers). See PECO St. 5-R at 12.

In its Exceptions, RESA asserted that its proposed adder would not result in an improper subsidization of shopping customers by default service customers because shopping customers are allegedly subsidizing default service customers by paying the costs of unbundled default service whether they use default service or not. RESA Exc. at 21. RESA's assertions should be rejected. RESA failed to introduce any evidence of what these alleged costs are or any evidence that its proposed collection and refund procedure are in any way related to these alleged costs.

The ALJ correctly found that RESA's assertions completely lack merit. As the ALJ stated:

The OCA contends, and I agree, that if implemented, the adder would create a substantial profit on default service for PECO and require default service customers to unfairly subsidize shopping customers.

R.D. at 53. The OCA submits that as RESA's proposed 0.5¢ per kWh adder unfairly requires default service customers to subsidize shopping customers, the ALJ's decision on this issue is in accord with the law and should be upheld.

4. The Implementation Of RESA's 0.5¢ Per kWh Adder Will Not Convey A Public Benefit.

Although not explicitly stated, it appeared that the public benefit that RESA claimed that its proposed adder would convey is the promotion and encouragement of shopping for electric supply. RESA witness Kallaher testified that by permitting PECO to retain a portion of the adder, the adder would incentivize PECO for its efforts to implement the retail market enhancements and encourage competition. RESA St. 2-SR at 24. Further, RESA asserted in its Exceptions that using some of the proceeds of the adder to pay for retail market enhancements is reasonable and appropriate because a significant number of PECO's customers remaining on default service stay with PECO for their generation supply "even though they would be able to save money or achieve other benefits by shopping." RESA Exc. at 22. The ALJ correctly recommended rejection of RESA's position, stating: "No public benefit would be conveyed by the adoption of a measure for which no need has been shown" R.D. at 54.

As illustrated by OCA witness Hahn, RESA's proposed adder has no actual relationship to the costs that it seeks to recover. As Mr. Hahn testified:

Figure R-2 below provides an estimate of the annual revenue from a 5 mil per KWH adder applied to default service customers. When applied to current default service customers, estimated annual revenue would be approximately \$70 million. As shown above, estimated expenses for the retail market enhancements are about \$3.7 million. Under these assumptions, if PECO were allowed retain 10% of the surcharge revenues less expenses, PECO's incentive would be approximately \$6.6 million per year.

Figure R-2

ESTIMATED ANNUAL SURCHARGE REVENUE					
Customer Class	Est'd Annual MWH Sales ^[1]	% Load served by Alternative Supplier ^[2]	Est'd MWH served by Alternative Supplier	Est'd Default Service MWH	Annual Revenue from 5 mils per KWH charge on Default Service
Residential	13,685,877	25.90%	3,544,642	10,141,235	\$50,706,174
Small C/I	8,331,937	62.00%	5,165,801	3,166,136	\$15,830,680
Large C/I	15,755,017	95.20%	14,998,776	756,241	\$3,781,204
	37,772,831	62.77%	23,709,219	14,063,612	\$70,318,059

^[1] PECO Energy 2011 FERC Form 1 Report
^[2] April 1, 2012 Electric Shopping Statistics

OCA St. 1-R at 7. (Internal footnote omitted). According to Mr. Hahn's Figure R-2 above, under RESA's 0.5¢ per kWh adder proposal, PECO would collect approximately \$70 million from its default service customers, recover the costs of the retail enhancement programs in the amount of approximately \$3.7 million, retain approximately \$6.6 million, and then return the remaining amount of nearly \$59.7 million to all of its distribution customers. Putting aside that the adder amounts to an impermissible profit mechanism for PECO and results in an improper subsidization of shopping customers by default service customers, the OCA submits that the public interest is not served by charging customers artificially inflated default service rates simply as a means to switch to an alternate generation supplier.

The OCA submits that the ALJ correctly recommended that RESA's proposed 0.5¢ per kWh adder be rejected because it would not convey any public benefit, and the ALJ's recommendation should be adopted.

C. The OCA's Reply As To Other Rate Design And Cost Recovery Issues.

OCA Reply to RESA Exception 4: The ALJ Correctly Rejected RESA's And Dominion's Proposals For PECO To Continue Reconciling Its Generation Supply Adjustment Charge Quarterly. The ALJ, However, Should Have Recommended Adoption Of OCA's 12-Month Rolling Average Reconciliation Proposal. (RESA Exc. at 9-11; Dominion Exc. at 2-3; OCA Exc. at 5-7; R.D. at 41-44; OCA M.B. at 37-40; OCA R.B. at 20-22).

The ALJ recommended that the Commission adopt PECO's proposal to move from a quarterly reconciliation of actual costs and billed revenues collected through the Generation Supply Adjustment (GSA) surcharge for the residential class to an annual reconciliation. R.D. at 44. In its Exceptions, the OCA stated that it agreed that a 12-month reconciliation period should be used, but contended that the Commission should adopt OCA's proposal for PECO to reconcile its over- and under-collections (E Factor) on a 12-month rolling average basis. As set forth in its Exceptions, the OCA submits that the use of a 12-month rolling average would achieve better combined performance in terms of lower price variance and a lower level of over- and under-collections. OCA Exc. at 5-7.

In their Exceptions to the Recommended Decision, however, RESA and Dominion have asserted that PECO should continue to reconcile its E Factor on a quarterly basis on the ground that it results in more "market reflective" default service rates."³ RESA Exc. at 9-11; Dominion Exc. at 2-3. RESA and Dominion asserted that there will be a competitive disadvantage to EGSs if the Price to Compare (PTC) does not fully and timely reflect the costs of providing generation service. RESA Exc. at 10; Dominion Exc. at 2. The OCA submits that the ALJ correctly found that due to PECO's billing procedures, the revenue billed and received in a prior month may differ significantly from actual default service expenses incurred in the current month, which

³ RESA and Dominion refer to the standard "market reflective" default service rates throughout their Exceptions. The OCA submits that the legal standard for default service rates is "least cost over time." See 66 Pa. C.S. § 2807(e)(3.4). The Commission has recognized that the least cost over time standard may not always equal current market prices at every given point in time. See e.g. Implementation of Act 129 of October 15, 2008: Default Service and Retail Electric Markets, Docket No. L-2009-2095604, Slip. Op. at 19-20 (Oct. 4, 2011).

“can result in significant fluctuations in the quarterly PTC which are unrelated to the actual costs of default service supply.” R.D. at 44.

As described by PECO witness Cohn:

As Exhibit ABC-1R shows, annual reconciliation is less volatile, resulting in a surcharge of 0.43% whereas the quarterly reconciliation ranges from a surcharge of 6.37% to a credit of 7.74%. A smaller surcharge or credit adjustment more closely aligns with the projected default service supply cost and market price.

PECO St. 5-R at 5.

The ALJ correctly recommended that RESA’s and Dominion’s proposals to retain the quarterly reconciliation of PECO’s E Factor should be rejected. As PECO witness Cohn explained, an annual reconciliation will smooth out the quarterly adjustments reconciling over/under collections and send clearer price signals to customers and EGSs. PECO St. 5-R at 3. An annual reconciliation will even out the billing cycle lag that currently produces significant fluctuations in the PTC, which often display a cyclical effect due to seasonality, that are not directly related to the cost of default service supply. Id.

As stated above, the OCA is generally supportive of PECO’s proposal. See OCA M.B. at 37. OCA witness Hahn, however, recommended a modification to PECO’s proposal. Mr. Hahn explained:

While I agree with a 12-month reconciliation process, I disagree with the proposal to reconcile DSP costs on a one-time annual basis, with the PTC reflecting that annual reconciliation. I believe that a 12-month rolling average reconciliation performed quarterly is a better approach.

OCA St. 1 at 17. The OCA submits that a 12-month reconciliation will smooth out fluctuations in the PTC and result in clearer price signals for both customers and EGSs. The OCA further submits that a 12-month rolling average reconciliation will go a step further and promote a better atmosphere for shopping, as it will create a less volatile PTC. The OCA submits that a 12-month

rolling average reconciliation method should have the effect of smoothing out the PTC, as a longer time frame is used to average out the “E Factor.” Less volatility in the PTC could lead to greater consumer confidence in accepting EGSs’ offers that provide a specified savings over a current PTC. As such, the OCA’s recommendation to implement a 12-month rolling average reconciliation for PECO’s GSA should be adopted. RESA’s and Dominion’s proposals to retain a quarterly reconciliation of PECO’s E Factor should be rejected.

D. The OCA’s Reply As To The Retail Market Enhancement Issues.

OCA Reply to RESA Exception 9: The ALJ Correctly Recommended that Shopping Customers be Eligible for the Opt-In Auction Program. (RESA Exc. at 24-25; R.D. at 59-60; OCA M.B. at 58-60; OCA R.B. at 34-35)

The ALJ correctly declined to adopt RESA’s proposal to exclude shopping customers from the Opt-In Auction Program and Standard Offer Program. R.D. at 59, 69. The ALJ determined that excluding shopping customers would be “unduly restrictive” and recommended that all residential customers be eligible to participate in the Opt-In Auction Program and Standard Offer Program. *Id.* In Exceptions, RESA argues that the main purpose of the programs is to introduce default service customers to the competitive market, and that customers who are currently shopping are already experiencing the benefits of the competitive market. RESA Exc. at 24-25.⁴ RESA states that there are potential negative impacts to those EGSs who are already serving shopping customers and impacts to customers via early cancellation fees. *Id.* at 25.

The OCA submits that RESA’s Exception regarding the participation of shopping customers should be denied. PECO’s proposal would target the marketing for the program to

⁴ The OCA notes that RESA’s Exception is specifically directed towards the Opt-In Auction Program, but states that “[a]llowing existing shopping customers in PECO territory to participate in retail market enhancement programs is not appropriate.” RESA Exc. at 25. The OCA submits that RESA’s Exception is not clear as to whether the Exception is limited to only the Opt-In Auction Program. This issue was addressed in the proceeding for both the Opt-In Auction and the Standard Offer Programs, and the ALJ adopts the same recommendation for the Standard Offer Program. *See* OCA M.B. at 79; R.D. at 69. To the extent that RESA’s Exceptions are also applied to the Standard Offer Program, the OCA submits that the above Reply to Exception should equally apply.

non-shopping customers, but shopping customers would not be precluded from signing up for the program. PECO St. 2-R at 15. PECO's approach is consistent with both the Commission's IWP Order⁵ and the Commission's recent FirstEnergy DSP II Order. IWP Order at 42; FirstEnergy DSP II, Order at 107.

In its Exceptions, RESA argues that the ALJ ignored the record evidence regarding the impacts to EGSs and possible cancellation fees to customers. RESA Exc. at 25. The IWP Order and the FirstEnergy DSP II Order, which the ALJ followed on this issue, specifically addressed these arguments. In the IWP Order, the Commission stated:

The Commission maintains its original position that Retail Opt-In Auctions should be open to both residential default service and residential shopping customers. The Commission agrees with those parties that expressed discomfort in the possibility of EDCs rejecting shopping customer participation. The Commission believes that would cast a shadow over the auctions and appear to be discriminatory against those who have already entered into the retail electric market. Additionally, the Commission believes this will prevent shopping customers from returning to default service in order to participate, which may result in cancelled contracts and the imposition of early termination fees/penalties.

IWP Order at 42. The OCA submits that RESA has failed to provide substantial record evidence to justify a departure from the Commission's prior ruling on this issue.

PECO will not directly solicit shopping customers for participation, but this does not mean that shopping customers who inquire about the offer should not be allowed to participate. OCA witness Alexander testified regarding RESA witness Kallaher's position on this issue as follows:

I cannot agree with his proposal to impose a duty on PECO to implement a program rule to this effect. It is an unfortunate, but inevitable, result that customers already served by an EGS will hear about this publicized enrollment opportunity and may seek to enroll. I agree that PECO's enrollment materials should not be targeted to such customers and I agree that PECO's public statements and customer materials should advise customers already served by an

⁵ Investigation of Pennsylvania's Retail Electricity Market: Intermediate Work Plan, Docket No. I-2011-2237952, Order (March 2, 2012) (IWP Order).

EGS to carefully consider their contract terms and price prior to seeking to enroll in this program. Again, the fact that 25% of PECO's customers are already shopping suggests that these customers are likely to hear about this program and some may seek to enroll. PECO should not be put in a position of monitoring this development or trying to educate individual customers on the implications of enrollment since they have no knowledge of the customer's EGS terms and conditions.

OCA St. 2-R at 7-8.

PECO's approach to direct its marketing efforts towards non-shopping customers, but allowing all customers to participate, carries forward the focus for the program identified in the IWP Order. IWP Order at 42. In its IWP Order, the Commission stated:

[t]o ensure the focus of this competitive enhancement is on those customers who have not shopped, the Commission will also maintain its original position that all marketing, notifications and consumer education efforts for Retail Opt-In Auctions should be targeted to non-shopping, residential, default service customers. As such, although a shopping customer may become aware of the Retail Opt-In Auction and request participation, the auction materials themselves will be directed toward the non-shopping segment of the residential sector.

IWP Order at 42.

Barring customers from participating in a Commission-sponsored program raises the issue of legal, or at the very least, perceived discrimination. The OCA submits that such a situation could damage the public's perception of such programs. Accordingly, the OCA submits that the ALJ's ruling on this issue is in accord with the law and the evidence and should be upheld.

OCA Reply Exception to RESA Exception 12: The ALJ Correctly Recommended That CAP Customers Be Precluded From Participation in the Retail Market Enhancement Programs. (RESA Exc. at 29-31; R.D. at 74-78; OCA M.B. at 85; OCA R.B. at 52)

The ALJ correctly recommended that Customer Assistance Program (CAP) customers be precluded from participating in the Retail Opt-In Auction or the Standard Offer Program. R.D. at 78. In its Exceptions, RESA argues that CAP customers should be permitted to participate in

the retail market enhancement programs and that the CAP benefits that customers receive be made portable. RESA Exc. at 29.

PECO witness Lauren Feldhake and CAUSE-PA witness Philip Bertocci pointed out significant, complex issues that need to be addressed prior to the inclusion of CAP customers in the retail market enhancement programs. PECO M.B. at 66; PECO St. 6-R at 6-8; PECO St. 6-SR at 2-6; CAUSE-PA M.B. at 17; CAUSE-PA St. 1-R at 1-4; CAUSE-PA 1-SR at 3-5. In its Main Brief, PECO also raised a significant number of issues in the record of this case that RESA had not addressed and that need to be addressed before CAP customers should participate in the retail market enhancement programs including:

(1) how to protect CAP customers from commodity volatility; (2) how to seamlessly integrate the Low Income Home Energy Assistance Program and CAP portability; (3) the need to allow PECO's recent CAP tier changes and in-program arrearage forgiveness programs time to mature before making other major changes to its CAP program; (4) integration with PECO's Rate RH phase-out; and (5) how to implement a discount on the customer's bill, especially given that the discount would, in many cases, be larger than the customer's distribution charges. In addition, the risk of higher costs for all customers associated with greater uncollectible expense needs to be considered and addressed.

PECO M.B. at 66. The OCA would add to this list the potential impact on other non-CAP, residential customers who pay for the costs of any CAP shortfalls. The IWP Order recognized these potential problems with enrollment of CAP customers in the retail market enhancement programs and referred the question of whether CAP customers can participate in the retail market enhancement programs to the Commission's Retail Market Investigation (RMI) Universal Service Subgroup. IWP Order at 18.

The OCA supports the positions of PECO and CAUSE-PA and recommends that the issue be considered as part of the RMI Universal Service Subgroup. For the reasons stated

above, the OCA submits that the ALJ correctly decided this issue, consistent with the evidence, and the Commission should uphold that finding.

OCA Reply to RESA Exception Reply Exception 13 : The Commission Should Approve The ALJ's Recommended Decision to Adopt PECO's Proposal In the Standard Offer Program To Offer A 7% Discount Off the Price To Compare At The Time of The Customer's Enrollment For the Entire Term. (RESA Exc. 31-33; R.D. at 69-70; OCA M.B. at 79-80; OCA R.B. 48-49)

In its Exception, RESA argues that the ALJ erroneously recommended that EGSs participating in the Standard Offer Program be required to offer a 7% discount off the Price to Compare (PTC) for the entire service term. RESA Exc. at 31. The ALJ adopted PECO's proposal that the Standard Offer Program "will be required to offer generation service on a month-by-month basis for twelve complete billing cycles at a fixed price of 7% below the PTC at the time of customer enrollment." R.D.at 69. PECO's proposal adopted the model in the Commission's IWP Order. In its Exceptions, RESA argues that:

the Commission should direct that the 7% off PTC price be offered for the first four months of the one-year service term and, after that introductory period, the price offered by the EGS should revert to one that is disclosed to the customer in a mailing from the EGS serving the customer.

RESA Exc. at 31.

The OCA recommended in this proceeding that the Standard Offer Program be for a four-month period, instead of the twelve-month term proposed by PECO, and recommended that the 7% discount be offered for the entire four-month term. OCA R.B. at 48-49. At the end of that four-month period, however, OCA recommended that the customer would return to default service unless the customer affirmatively decided to stay with the EGS or to select another EGS. Id. The ALJ decided to adopt PECO's proposal for the twelve-month term, and the OCA determined to not file Exceptions related to this issue.

The OCA's central objective in recommending the four-month timeframe was to allow customers to have an optimal positive competitive retail market experience with guaranteed savings for the limited term of the program. Under PECO's proposal, customers will experience a 7% discount off the PTC at the time of customer enrollment. OCA M.B. at 79; PECO St. 2-S at Exh. JJM-5S, Article 1.4; OCA St. 2 at 15. With quarterly changes to the PTC, customers would not necessarily be guaranteed savings because during the course of the year, the PTC in effect may decrease below 7% of the PTC at the time of the enrollment. However, under PECO's proposal, customers would never be paying more than 7% off the PTC at the time of the enrollment. Customers would have a fixed price during that period.

RESA's proposal provides no such guarantee of savings beyond the first four months, or even the guarantee of reasonable rates during the remainder of the twelve-month time period. While the OCA does not agree that PECO's proposal is the optimal program design, at least under PECO's proposal, the customer would know how much he or she would be charged per month for electric generation service. Under RESA's proposal, the customer will have enrolled in the program based upon the four-month "introductory" rate, and then the customer will later find out the rate for the remaining eight months. The EGS can charge whatever rate that the EGS wants for the remaining eight months. The OCA submits that this potentially could cause significant customer confusion about the rates and would not provide any limits or protections as to what a customer could be charged. The purpose of the Standard Offer Program is to introduce customers to the retail market without significant risk.

The OCA submits that RESA's proposal has the potential to harm customers. Therefore, the OCA recommends that RESA's Exception should be denied.

OCA Reply to FirstEnergy Solutions Exception 2, Dominion Exceptions 3 and 4: The ALJ Correctly Decided That All of the Costs of the Retail Enhancement Programs Should Be Recovered from EGSs. (FES Exc. at 4-8, Dominion Exc. at 4-6; R.D. at 82-86; OCA M.B. at 87-90; OCA R.B. at 53-56)

The ALJ recommended that the costs of the Opt-In Auction and the Standard Offer Programs be recovered from the EGSs. R.D. at 85, 86. Specifically, the ALJ rejected the arguments of the EGSs and adopted PECO's proposal to recover the costs of both the Opt-In Auction Program and the Standard Offer Program from the EGSs. R.D. at 85-86. This decision is in accord with both the Commission's IWP Order and the recent FirstEnergy decision. IWP Order at 32, 84-85; FirstEnergy DSP II, Order at 136. The OCA agrees that the ALJ correctly decided that all of the costs of the Retail Market Enhancement Programs should be recovered from EGSs and, as such, the Exceptions of FES, RESA and Dominion on this issue should be denied.⁶

1. Opt-In Auction Program.

The ALJ adopted PECO's proposal to recover the costs of the Opt-In Auction Program directly from the winning EGSs in proportion to the number of customers allocated to each EGS. R.D. at 85; PECO M.B. at 72-73; PECO St. 2 at 25. The ALJ also adopted PECO's proposal that in the event that the RFP process does not produce any winning EGSs, the costs of the program would be recovered through a 0.3% discount on payments made to EGSs through the Purchase of Receivables (POR) program until such costs are recovered. Id. PECO has thus proposed a mechanism and an alternative mechanism under which all of the costs of the programs would be recovered from EGSs. The OCA agrees with PECO's proposal as well as this Commission's

⁶ RESA has proposed that the costs of these programs be recovered from default service customers through its 0.5¢ per kWh adder. RESA Exc. at 37-38. The OCA addresses RESA's proposal separately in its Reply Exception to RESA Exception 7 but would note here that recovery of these costs solely from default service customers is particularly unfair since the remaining default service customers are the very individuals who, by definition, are not participating in these programs.

prior Orders that under whatever specific mechanism is implemented, all of the costs of this program should be recovered from EGSs.

The OCA agrees with PECO's statement in its Main Brief that the EGSs have not demonstrated any good cause to deviate from the Commission's IWP Order on this issue. PECO M.B. at 73. The EGSs will be the primary beneficiaries through substantially reduced acquisition and transaction costs, and as such, should be responsible for the costs. PECO's proposal is fully consistent with the IWP Order, which proposed that the costs of the program should be allocated to participating EGSs. The IWP Order stated:

As for the costs of the Retail Opt-In Auctions, we agree with UGIES and OCA that, in general, most, if not all, of these costs should be recovered from participating suppliers. The participating suppliers will be receiving customers via this program in a manner that negate almost all of the usual customer acquisition costs. As such, it is only fair that the suppliers, as the prime beneficiaries of the program, should pick up the associated costs.

IWP Order at 84-85. OCA witness Hahn addressed this issue and stated: "[t]he retail market enhancements are being implemented at the behest of and for the benefit of EGSs. Therefore, the costs should be paid for by the EGSs." OCA St. 1-R at 3. For the reasons stated by PECO, OCA witness Hahn, and in the IWP Order, the OCA disagrees with Dominion and FES and submits that the costs of the Opt-In Auction should be borne by the EGSs.

The OCA supports the ALJ's Recommended Decision, which adopted PECO's proposal and the Commission's recommendation that the costs of the Opt-In Auction be recovered from EGSs, given that EGSs are the entities reaping the possible customer acquisition benefits resulting from the programs. R.D. at 85; IWP Order at 78; PECO M.B. at 72-76.

2. Standard Offer Program.

The ALJ adopted PECO's proposal for cost recovery for the Standard Offer Program. R.D. at 86.⁷ PECO has proposed to recover the initial and on-going costs of the EGS Standard Offer Program through a discount on purchased EGS receivables through the Company's POR program. PECO St. 2 at 28; PECO M.B. at 75-76. As with the Opt-In Auction Program cost recovery proposal, the recovery of the costs of the Standard Offer Program from EGSs is consistent with the IWP Order. IWP Order at 32. In its Exception on this issue, FES argues for an alternative cost recovery mechanism under which a portion of the costs of the Standard Offer Program will be recovered from participating EGSs and any remaining costs would be recovered from customers. FES Exc. at 7. FES argues that the IWP Order does not require that EGSs should bear 100% of the costs of the Standard Offer Program or for the Opt-In Auction program. Id. at 8.

For the same reasons discussed above for the Opt-In Auction Program, the OCA supports the ALJ's Recommended Decision, which adopted PECO's proposal and the Commission's prior recommendation that the costs of the Opt-In Auction be recovered from EGSs, given that EGSs are the entities reaping the possible customer acquisition benefits resulting from the programs. R.D. at 86; IWP Order at 32; PECO M.B. at 75-76. While the OCA would not object to the use of an alternative to the POR discount method proposed by PECO and adopted by the ALJ in this case, the OCA urges the Commission to maintain the position that the costs of these retail market enhancement programs be recovered from the EGSs.

⁷ The OCA notes that Dominion did not provide a specific Exception to the allocation of costs to EGSs regarding the Standard Offer Program. Dominion opposed PECO's proposal to implement a POR discount and recommended that the Standard Offer Program be paid for through a predetermined fee that each EGS would pay for each customer acquired through the Standard Offer Program. Dominion M.B. at 17. The OCA takes no specific position on which form of cost recovery is utilized, as long as the costs are recovered from EGSs as recommended in the IWP Order and in the cost allocation manner to only EGSs as proposed by PECO.

E. OCA Reply As To The Time-of-Use Proposal.

OCA Reply to RESA Exception 14: The ALJ Correctly Recommended Rejection of RESA's Proposal Regarding PECO's Time-Of-Use Offering. (RESA Exc. 33-34, R.D. at 78-79, OCA M.B. at 85-87, OCA R.B. at 52-53).

In its Exceptions, RESA argues that the ALJ erred by rejecting RESA's recommendations regarding PECO's Time-of-Use Offering (TOU). The ALJ concluded that RESA's approach was unnecessary and "would only serve to complicate this matter to no beneficial purpose." R.D. at 79. The OCA agrees with the ALJ's recommendation.

The OCA submits that the ALJ correctly determined that addressing the TOU program in this proceeding is unnecessary as it is being addressed at a separate docket in the Petition of PECO Energy Company for Approval of its Initial Dynamic Pricing and Customer Acceptance Plan, Docket No. M-2009-2123944. Additional proposals at this time may undermine the TOU programs and potentially further delay implementation of the TOU programs. The OCA submits that the ALJ's Recommended Decision should be adopted on this issue.

III. CONCLUSION

For the reasons detailed in these Reply Exceptions, and its Main Briefs and Reply Briefs, the OCA submits that the Exceptions of RESA, FES and Dominion on the issues discussed herein should be denied and the ALJ's recommendations adopted.

Respectfully submitted,

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CERTIFICATE OF SERVICE

Re: Petition of PECO Energy Company for Approval of Its Default Service Program
Docket No. P-2012-2283641

I hereby certify that I have this day served a true copy of the foregoing document, the Office of Consumer Advocate's Reply Exceptions to the Recommended Decision, upon parties of record in this proceeding in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant), in the manner and upon the persons listed below:

Dated this 17th day of September 2012.

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