



COMMONWEALTH OF PENNSYLVANIA  
OFFICE OF SMALL BUSINESS ADVOCATE

October 5, 2012

**E-FILED**

Rosemary Chiavetta, Secretary  
Pa. Public Utility Commission  
Commonwealth Keystone Building  
P.O. Box 3265  
Harrisburg, PA 17105-3265

**Re: Petition of PPL Electric Utilities Corporation for Approval of a Default Service Program and Procurement Plan for the Period June 1, 2013 through May 31, 2015  
Docket No. P-2012-2302074**

Dear Secretary Chiavetta:

Enclosed for filing is the Initial Brief, on behalf of the Office of Small Business Advocate, in the above-docketed proceeding. As evidenced by the enclosed certificate of service, two copies have been served on all active parties in this case.

If you have any questions, please contact me.

Sincerely,

A handwritten signature in blue ink that reads "Steven C. Gray" with a stylized flourish at the end.

Steven C. Gray  
Acting Small Business Advocate  
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Enclosures

cc: Parties of Record  
Robert D. Knecht

**BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

**Petition of PPL Electric Utilities Corporation :  
for Approval of a Default Service Program and : Docket No. P-2012-2302074  
Procurement Plan for the Period June 1, 2013 :  
through May 31, 2015 :**

**CERTIFICATE OF SERVICE**

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

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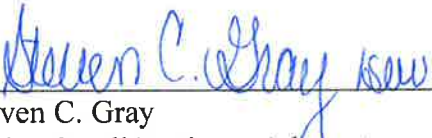
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Procurement Plan for the Period June 1, 2013 :  
through May 31, 2015 :**

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

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**Dated: October 5, 2012**

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## **I. Introduction**

### **A. Statement of Position**

The OSBA supports the procurement of supplies for small commercial and industrial customers through the use of a portfolio of laddered, fixed-price, full requirements, load-following products.

The OSBA supports the procurement of supplies for small commercial and industrial customers through auctions conducted every six months, with the resulting contracts having a duration of one year.

The OSBA does not support the use of a retail opt-in auction for small commercial and industrial customers.

### **B. Procedural History**

On May 1, 2012, PPL Electric Utilities Corporation (“PPL” or the “Company”) filed with the Pennsylvania Public Utility Commission (“Commission”) a Petition for Approval of a Default Service Program and Procurement Plan for the Period June 1, 2013 through May 13, 2015 (“Petition”).

On June 4, 2012, the Office of Small Business Advocate (“OSBA”) filed an Answer and Notice of Intervention against the Petition.

On June 6, 2012, a prehearing conference was held before Administrative Law Judge (“ALJ”) Susan D. Colwell.

On June 7, 2012, ALJ Colwell issued her Scheduling Order.

On July 20, 2012, the OSBA served the direct testimony of Robert D. Knecht. On August 17, 2012, the OSBA served the rebuttal testimony of Mr. Knecht. On August 31, 2012, the OSBA served the surrebuttal testimony of Mr. Knecht.

An Evidentiary hearing was held telephonically on September 7, 2012. Evidentiary hearings were also held in Harrisburg on September 10 and 11, 2012.

The OSBA submits this initial brief pursuant to the procedural schedule set forth in ALJ Colwell's June 7, 2012, Scheduling Order.

## **II. Summary of Argument**

The OSBA supports PPL's proposed procurement product mixture for the Company's small commercial and industrial customers.

The OSBA supports PPL's proposed procurement schedule for the Company's Small C&I customers. The Company's approach is consistent with the Commission's guidelines, and it represents a reasonable balance between making the price to compare ("PTC") consistent with wholesale market conditions and providing some reasonable stability to the PTC. The OSBA does not support the use of three and six month contracts in order to terminate all supplier contracts by the May 2015 end date. The use of short-term contracts and a "dead stop" end date could result in unreasonable rate instability.

The OSBA supports PPL's proposed supplier load cap for the Company's small commercial and industrial ("Small C&I") customers. Because the default service load for Small C&I customers is relatively small, there is little risk associated with supplier default, and lowering the supplier load cap may very well result in higher prices for Small C&I customers.

The OSBA recommends the issue of including Cash Working Capital ("CWC") costs in the default service rates be deferred to the Commission's proceeding on reconciliation of default service costs. There is no pressing need to address this issue in this proceeding, and PPL has not offered a credible method for how a CWC claim should be developed in the present circumstances.

The OSBA supports PPL's proposed reconciliation mechanism for the Company's small commercial and industrial customers for the purposes of this proceeding. While PPL's proposal will not cure the defects in the Company's approach that have resulted in wild fluctuations in the PTC for Small C&I customers, these issues are best addressed in the generic proceeding

regarding default service reconciliation. PPL's proposal does have the advantage that it will at least smooth out the fluctuations in the PTC. Moreover, as the Company's approach has failed at having the PTC reflect the actual current cost of procured electricity supplies, the Company's current proposal is likely no worse than the existing mechanism.

The OSBA recommends that PPL pass transmission costs currently recovered in the Company's Transmission Service Charge along to the default service wholesale suppliers in order to level the playing field in the competitive marketplace.

The OSBA does not object to PPL's proposal to include Time of Use service in the default service procurement for the Company's small commercial and industrial customers. In light of past performance, OSBA expects that Small C&I customers will have little interest in taking TOU service from the Company.

The OSBA does not support the use of a retail opt-in auction for the Company's small commercial and industrial customers. The Commission's guidelines for retail market enhancements indicate that Small C&I customers should not be included in such an auction, and the rationale used by the Commission to reverse those guidelines in the recent First Energy default service proceedings does not apply to PPL.

### **III. Argument**

#### **A. Burden of Proof**

PPL has the burden of proof in this proceeding to establish that the Company is entitled to the relief that it is seeking. 66 Pa. C.S. § 332(a). PPL must establish the Company's case by a preponderance of the evidence. *Samuel J. Lansberry, Inc. v. Pa. PUC*, 578 A.2d 600 (Pa. Cmwlth. 1990), *alloc. denied*, 529 Pa. 654, 602 A.2d 863 (1992). To meet the Company's burden of proof, PPL's evidence must be more convincing, by even the smallest amount, than that presented by any opposing party. *Se-Ling Hosiery, Inc. v. Margulies*, 364 Pa. 45, 70 A.2d 854 (1950). The Commission's decision must be supported by substantial evidence in the record. More is required than the mere trace of evidence or a suspicion of the existence of a fact sought to be established. *Norfolk & Western Ry. Co. v. Pa. PUC*, 489 Pa. 109, 413 A.2d 1037 (1980).

The OSBA observes that this proceeding is an unusual regulatory proceeding. As the default service supplier, PPL Electric is generally entitled to recover its prudently incurred costs. However, PPL is generally not entitled to earn any profit on these costs, since little or no rate base is involved. In contrast, a number of participants in this proceeding do have a profit interest in the outcome. While the OSBA fully supports a competitive marketplace, the OSBA's focus in this proceeding to make certain that all proposals are based on sound regulatory and legal principles so that the profit motivation of certain parties does not have the Small C&I customers of PPL.

**B. The Proposed Default Service Program**

**1. Class Procurements**

**b. Small C&I – Fixed Rate**

**i. Product Mixture**

The OSBA is in agreement with PPL's proposed product mixture for the Company's proposed procurement for the Small C&I customers. PPL witness A. Joseph Cavicchi described the Company's proposed Small C&I procurement in his direct testimony. *See* PPL Statement No. 2, at 14-22. Mr. Cavicchi summarized PPL's procurement proposal for the Company's Small C&I customers, as follows:

For its ... small commercial and industrial default service customers, PPL Electric's DSP II envisions obtaining a portfolio of laddered fixed-price full requirements load-following supplies while reducing real-time wholesale electricity spot market supplies and block supplies.

*Id.*, at 14.

OSBA witness Robert D. Knecht assessed the Company's procurement proposal, as follows:

I do [agree with the with the Company's proposal for Small C&I procurement]. . . . I agree with the proposal to eliminate spot market purchases from the mix. In light of the wild swings associated with reconciliation charges, including a relatively small amount of spot market purchases in the supply mix is not going to help make PPL Electric's GSC [Generation Supply Charge] any more reflective of actual market conditions. Moreover, the spot market purchases serve to exacerbate the problems associated with the reconciliation mechanism.

OSBA Statement No. 1, at 9.

In addition, the OSBA submits that the Company's proposal is consistent with the Commission's policy statement with respect to default service procurement. For non-residential

customers with maximum demand between 25 and 500 kW, 52 Pa. Code § 69.1805(2) states that “Fixed term contracts may be laddered to minimize risk, with a minimum of two competitive bid solicitations a year to further reduce the risk of acquisition at a time of peak prices.”

Therefore, the OSBA supports the Company’s proposed procurement product mixture for the Small C&I customer classes.

**ii. Procurement Schedule**

The OSBA generally agrees with the Company’s proposed procurement schedule for the Small C&I customer classes. Mr. Knecht explained the support for PPL’s proposed procurement schedule, as follows:

I agree with the Company’s proposal to transition toward a procurement approach in which approximately half the default service load is procured every six months, with a contract duration of one year. The essence of the Company’s proposal in this proceeding is to provide a transition to such a steady-state approach. Consistent with Commission default service procurement guidelines, the Company’s approach will include at least two procurements per year, and will retain laddering of contracts (at least through May 2015).

OSBA Statement No. 1, at 9 (footnote omitted).

However, in conformance to the Commission’s guidelines, the Company included shorter duration procurements in order to obey the May 2015 end date. As addressed more fully below, the OSBA recommends that these “stub” procurements be modified.

Therefore, in general, the OSBA supports the Company’s proposed procurement schedule for the Small C&I customer classes. The OSBA does, however, recommend that the “stub” procurements be eliminated, as discussed below.

### iii. Wholesale Supplier Load Cap

The OSBA supports the Company's proposal "that the maximum amount of Small C&I default service load be no more than 85 percent of the load retained in any particular default service procurement." OSBA Statement No. 2, at 17. *See also*, PPL Statement No. 1, at 19-20.

The Office of Consumer Advocate ("OCA"), however, proposed an additional restriction upon the Company's load cap. Mr. Knecht explained the OCA proposal, as follows:

[OCA witness] Mr. Hahn does not object to that restriction [the Company's proposed 85% load cap], but he proposes to add the additional restriction that there be an aggregate load cap for all default service supply for Small C&I customers of 50 percent. Mr. Hahn bases this recommendation on his conclusion that an 85 percent limit would result in the risk of supplier bankruptcy being too high.

OSBA Statement No. 2, at 17.

Mr. Knecht stated three reasons why the OCA proposal is not reasonable and appropriate for the Company's Small C&I customers. First, Mr. Knecht explained that the OCA proposal may cost the Small C&I customers money:

Mr. Hahn does not, at least explicitly, recognize that setting supplier caps has a potential cost to ratepayers. If the overall cap is binding, a lower-cost bidder is necessarily being displaced by a higher-cost bidder. For example, if one supplier puts in a bid that will result in it having 60 percent of the overall Small C&I load at 6.0 cents per kWh, and the next lowest bid price is 6.2 cents per kWh, Mr. Hahn's proposal will require that some of the 6.2 cent per kWh load displace the 6.0 cent per kWh that would exceed the cap, resulting in higher default service prices. Thus, the risk of supplier default must be weighed against the higher cost to ratepayers.

*Id.*, at 18.

Second, Mr. Knecht testified that a load cap for the Residential customer class should differ from a load cap on the Small C&I customer classes:

Mr. Hahn does not distinguish between Residential and Small C&I customers for his proposed cap. However, Residential default service load is substantially larger than Small C&I default service load. Over the past year, Residential 'Fixed' default service load has been more than four times larger than Small C&I 'Fixed' default service load. It would therefore be much easier for PPL Electric to replace 85 percent of Small C&I load in the event of supplier default than it would to replace 85 percent of Residential load. Or, put another way, replacing 85 percent of Small C&I default service load would be approximately the same as replacing 20 percent of Residential default service load.

*Id.* (footnotes omitted).

Third, Mr. Knecht explained that the OCA load cap proposal will interfere with supplier participation:

[I]n practice, the 85 percent restriction for each procurement will likely result in a lower overall limit on maximum supplier participation in the Small C&I class. Small C&I default service load is unlikely to be more than 400 to 500 MW. Therefore, each of PPL Electric's procurements for Small C&I default service load will involve somewhere between 2 and 4 tranches, based on PPL Electric's target tranche size of 100 MW. Thus, even if there is a dominant bidder, the 85 percent limit for each individual procurement will generally require that one tranche be sold to an alternative supplier, with a market share of roughly 25 to 50 percent. In effect, the 85 percent cap will implicitly restrict any supplier's participation to considerably less than 85 percent. If 500 MW is the default service load targeted, I estimate maximum market share based on the 85 percent limit at approximately 63 percent.

OSBA Statement No. 2, at 18-19 (footnotes omitted).

In his surrebuttal testimony, Mr. Hahn offered no specific response to any of Mr. Knecht's analysis, other than to reiterate his initial position. *See* OCA Statement No. 1-S, at 1-2.

Therefore, the OSBA respectfully submits that the OCA's load cap proposal, with its added complexity, the possible reduction in supplier participation, and the possible price increases to the Small C&I consumer, is not justified for the limited protection the proposal

provides.<sup>1</sup> The OSBA supports the Company's load cap proposal for the Small C&I customer classes.

**d. Contract Terms Beyond May 2015**

As set forth above, the Company included shorter duration procurements in order to conform to the Commission's directive to have all contracts terminate at the end of May 2015.

Mr. Knecht explained the problem:

Unfortunately, to be consistent with the Commission's recent guidance regarding retail market enhancement, PPL Electric included 'stub' procurements with terms of only three and six months, in order that no contracts extend beyond May 2015. This approach will result in a 'hard stop' for all default service contracts at May 31, 2015, which may result in a substantial rate discontinuity.

OSBA Statement No. 1, at 9-10.

The OSBA recommends that the Commission allow PPL the flexibility forego the "stub" procurements and allow certain Small C&I contracts to extend beyond May 2015. Mr. Knecht argued for this solution, as follows:

I encourage the Commission to consider allowing PPL Electric to extend its last two Small C&I procurements to 9-month and 12-month terms, to retain the rate stability advantages of contract laddering. Retaining the laddered approach may be particularly appropriate for PPL Electric, in that shopping levels are already relatively high, and it is therefore less likely that additional retail market enhancements will be needed three years from now.

*Id.*, at 10.

Therefore, as set forth above, the OSBA supports the Company's proposed procurement schedule for the Small C&I customer classes. The OSBA does, however, recommend that the "stub" procurements be eliminated and extended to 9 or 12 months in duration.

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<sup>1</sup> The OSBA takes no position on the OCA's load cap proposal for the Residential class.

**f. Administrative Costs and Cash Working Capital**

In this proceeding, PPL initially proposed to include Cash Working Capital (“CWC”) costs in the Company’s default service rates if the Commission were to overturn the Company’s reconciliation accounting method, which was at issue in a separate proceeding. *See* PPL Statement No. 5, at 9-10. *See also, William R. Lloyd, Jr. v. PPL Electric Utilities Corporation*, Docket No. C-2011-2245906 (Order entered July 19, 2012), and *PPL Electric Utilities Corporation Proposed Generation Supply Charge-1 for the Period June 1, 2011 through August 31, 2011*, Docket No. M-2011-2243137 (Order entered July 19, 2012).

However, in those separate proceedings, the Commission upheld PPL’s reconciliation accounting methodology. *See Lloyd v. PPL*, at 26-27. Nevertheless, after the Commission entered Orders in the other dockets, the Company declined to withdraw its proposed methodology for developing a CWC claim in this proceeding.

Mr. Knecht summarized PPL’s latest update regarding the Company’s original CWC proposal:

[PPL] has not [withdrawn its claim for CWC as a result of the Commission’s decision in that proceeding which accepted PPL Electric’s traditional methodology]. Mr. Kleha retains the claim for CWC because (a) the Commission may yet require EDCs to modify their default service reconciliation accounting to properly match revenues and costs, and/or (b) the Commission may adopt Constellation witness Mr. Bennett’s proposal regarding payment terms for wholesale suppliers.

OSBA Statement No. 3, at 6.

In regard to Mr. Kleha’s two scenarios, Mr. Knecht testified, as follows:

Regarding Mr. Bennett’s proposal, Mr. Kleha would need to modify his calculation to (a) reflect the new payment terms (which Mr. Kleha does in Exhibit JMK-7), and (b) credit the CWC working capital claim for the CWC that the Company has already

obtained from default service ratepayers through the accounting mismatch (which Mr. Kleha does not do in Exhibit JMK-7).

Regarding the eventual outcome of the Commission's generic investigation of default service reconciliation issues, it is impossible to evaluate all of the possible results of that investigation. Any CWC claim arising from that proceeding would need to reflect the specifics of the Commission's decision. The methodology for calculating CWC should therefore be deferred at least to the Commission's generic proceeding regarding reconciliation at Docket No. M-2012-2314313.

OSBA Statement No. 3, at 7.

The current status of the Company's CWC proposal is less than clear. Nevertheless, in regard to the Company's original CWC proposal, Mr. Knecht observed:

I agree that CWC costs are a legitimate cost incurred by PPL Electric in providing default service, and I agree that PPL Electric should be permitted a reasonable opportunity to recover any working capital costs that it incurs. In theory, these costs should have been unbundled in PPL Electric's restructuring proceeding. Thus, at a conceptual level, I agree with the Company. Moreover, I have not undertaken a detailed analysis as to whether PPL Electric's specific proposed calculations for working capital costs are just and reasonable.

OSBA Statement No. 1, at 13 (footnotes omitted).

However, Mr. Knecht noted four general problems with the Company's CWC proposal. First, Mr. Knecht noted that the Company failed to recognize the dissimilar characteristics of the customer classes:

PPL Electric fails to recognize the differences between rate classes with respect to CWC costs. CWC costs are related to the lag between the time the Company needs to pay its bills and the time it receives payment from its customers. The Company calculates that, for default service, that lag *averages* 27.0 days, based on an average bill payment lag of 66.7 days and an average cost payment lag of 39.7 days. However, the bill payment lag varies considerably by rate class. The Small C&I class consists primarily of customers with 15 day bill payment terms, and includes a relatively small set of customers with 30 day payment terms. As

shown at Exhibit JMK-4, the bill payment lag for those two sets of customers is 27 days and 39 days respectively. Thus, the bill payment lag for all Small C&I customers is actually *shorter* than the cost payment lag. In effect, Small C&I customers do not contribute to CWC costs at all, and in fact are providing a CWC credit to the Company (in addition to the CWC funding effect of the accounting mismatch). Thus, Small C&I default customers should be assigned a CWC credit rather than a CWC cost.

OSBA Statement No. 1, at 13-14 (emphasis in original).

Second, Mr. Knecht observed that PPL failed to provide any details on a reconciliation mechanism:

[T]he Company does not indicate how it intends to recover or reconcile CWC costs and credits. Because default service CWC will generally vary based on overall revenues which fluctuate with load, power purchase prices and shopping levels, it would be appropriate to recover these costs as a percentage of revenues. A reasonable approach for doing so would be to include the CWC charge/credit in the merchant function charge ('MFC'). In order to encourage the Company to collect bills in a timely way, variances in the CWC percentage rate should not be reconciled.

OSBA Statement No. 1, at 14 (footnote omitted).

Third, Mr. Knecht testified that the Company's purchase of receivables program has not been addressed in PPL's CWC proposal:

[T]he Company has not addressed the issue of CWC costs associated with its purchase of receivables ('PoR') program for EGSs. Unless PPL Electric pays EGSs exactly when it receives payment from ratepayers, there will necessarily be either a net lag or net lead between the time when the Company pays the EGS and when the Company receives payment from ratepayers. This lag or lead should be reflected in a CWC charge or credit to the EGS. Implementing such a CWC charge or credit would most logically be implemented by factoring it into the PoR discount.

*Id.*, at 14.

Fourth, Mr. Knecht recommended that the Company take a different approach in regards to late payment fees:

[T]he Company imposes late payment fees on some customers associated with payments beyond the due date for the bills. My understanding from PPL Electric's tariff is that these charges apply to the entire bill, including default service charges, charges related to EGS supply covered by the PoR program, and distribution charges. The portion of these charges that is related to generation service, either default service or billing for EGSs, should serve as an offset to CWC costs.

*Id.*, at 14.

Given the fatal flaws and lack of clarity in the Company's proposed methodology, combined with the fact that PPL is being permitted to keep the CWC that it has already raised from its default service customers through the flawed reconciliation accounting methodology, the OSBA respectfully requests that the Company's proposal be rejected for the purposes of this proceeding. Ultimately, the OSBA recommends that the issue of the inclusion of CWC costs in default service rates be deferred to the Commission proceeding at *Default Service Reconciliation Interim Guidelines*, Docket No. M-2012-2314313.

## **2. Rate Design**

### **b. Residential and Small C&I – Reconciliation**

In the Company's direct testimony, PPL proposed a reconciliation mechanism for the generation component of the PTC for Small C&I customers. *See* PPL Statement No. 5, at 4-10. In general, PPL Electric proposed to continue the existing methodology, except that the generation charge ("GSC-1") will be updated every six months (rather than quarterly), and the reconciliation amount will be recovered on a "rolling" 12-month basis.

As the Commission is well aware, PPL Electric's reconciliation mechanism has been a debacle for the past year, especially for Small C&I customers. The enormous fluctuations in PPL's PTC resulting from the flawed reconciliation have rendered the PTC virtually useless as a

signal of market prices for electricity and has contributed to customer gamesmanship. Mr.

Knecht testified:

Overall, during the Company's DSP I period, the default service generation charge for Small C&I customers has been wildly unstable, with the total GSC-1 ranging from a low of 5.52 cents per kWh to a high of 12.17 cents per kWh. This price gyrations, caused substantially by the reconciliation component bouncing up and down from a huge charge to a huge credit, has distorted price signals to customers who are evaluating shopping options, and has caused customers to switch in and out of default service in order to take advantage of the reconciliation mechanism.

OSBA Statement No. 1, at 5.

Nevertheless, the OSBA observes that the Commission has thus far declined to take any specific action to address the underlying causes of this problem. Therefore, for the purposes of this proceeding, the OSBA supports the Company's reconciliation proposal. As explained by

Mr. Knecht

[R]ather than debate this issue in this proceeding for a single EDC, I observe that, as a result of its decision at Docket Nos. M-2011-2243137 and C-2011-2245906, the Commission is undertaking a generic proceeding regarding default service reconciliation.

I also observe that many of the issues regarding reconciliation are dependent upon the resolution of other issues involved in default service procurement. For example, if default service procurement plans include purchases of a substantial amount of short term and spot market supplies, it is more important to update default service balances promptly than if default service plans rely solely on medium term fixed price contracts.

Therefore, resolving certain basic issues regarding default service procurement methods and retail market enhancement programs will simplify the discussion of what reconciliation mechanism is appropriate. I therefore recommend that PPL Electric's default service reconciliation mechanism be deferred to the generic proceeding.

In the interim, I recommend that the Company's proposal be adopted, as it represents a reasonable compromise between the position advocated by RESA and the proposals put forward by the

Company in its RR/CTR proceedings at Docket No. P-2011-2256365.

OSBA Statement No. 2, at 4 (formatting added).

Therefore, the OSBA supports the Company's reconciliation proposal for the Small C&I customer classes. The OSBA will investigate other reconciliation proposals and methodologies in the Commission's generic proceeding addressing this issue.

**h. Recovery of Transmission and Other Related Charges**

Mr. Knecht summarized the Company's proposal for its Transmission Service Charge ("TSC"), as follows:

In its filing, PPL Electric proposed to continue to recover transmission costs for default service customers through a reconcilable TSC (as part of the price to compare ('PTC')), while requiring electric generation suppliers ('EGSs') to pay for transmission service to their customers.

OSBA Statement No. 3, at 2.

Mr. Knecht identified four major problems with the Company's TSC proposal. First, Mr. Knecht observed that PPL's TSC proposal negatively impacts EGSs:

PPL Electric's treatment of transmission costs in the PTC mechanism tilts the playing field in favor of default service and wholesale suppliers and to the detriment of retail EGSs. Under PPL Electric's approach, wholesale suppliers are not obligated to provide basic transmission service, and they therefore face no risks associated with transmission costs. PPL Electric implicitly recovers these costs for the wholesale supplier through the TSC. And because the TSC is reconcilable, PPL Electric itself faces little or no risk associated with these costs. In contrast, EGSs are obligated to pay these transmission costs, and then recover them from their customers in their retail rates.

OSBA Statement No. 1, at 6.

Second, Mr. Knecht testified that the PPL TSC proposal does not properly follow cost causation:

PPL Electric's reconciliation of the TSC does not reasonably reflect actual costs incurred by class. For demand-related costs (which represent most of the TSC costs), PPL Electric's reconciliation mechanism relies on *forecasted* class contributions to peak demands, rather than *actual* contributions to peak demands. For example, for setting the 2010 TSC, PPL Electric forecasted that Small C&I customers would represent 27.2 percent of default service peak demand and 30.2 percent of default service energy. (The energy share is a little higher than the demand share, because Small C&I customers have a higher load factor than average for default service.) However, shopping levels for Small C&I customers proved to be proportionally higher than forecast, which caused the actual Small C&I energy share to be 24.1 percent rather than the 30.2 percent forecast. Despite this large reduction in energy share, however, the Company retained the forecast 27.2 percent share of demand costs in its reconciliation calculation, despite the fact that the demand costs associated with the shopping customers were shifted over to their EGSs. The net effect of this inconsistency was to provide a large reconciliation credit to the Residential class, and to impose a large reconciliation charge on the Small C&I class.

This method continued to apply to the TSC during DSP I with similar results, generally to the detriment of Small C&I customers. In effect, PPL Electric's TSC reconciliation approach has created undue encouragement for Small C&I customers to shop by overstating the TSC, while reducing the economic incentive for Residential customers to shop by understating the TSC.

OSBA Statement No. 1, at 6-7 (emphasis in original) (footnotes omitted).

Third, Mr. Knecht pointed out that PPL's math is questionable:

PPL Electric's recent calculation of the TSC charge is suspect. In setting the TSC for 2010, for the first five months of 2011, and for the 12-months ending May 2012, PPL Electric forecast that the Small C&I share of energy consumption was higher than its share of peak demand. In effect, PPL Electric forecasted that the load factor for Small C&I customers would be higher than that for Residential customers. This pattern is consistent with the load data for Residential and Small C&I customers on the Company's website. However, in its May 14, 2012, submission at Docket No. M-2012-2302811, PPL Electric forecasts that the Small C&I class will be responsible for 15.3 percent of default service energy and 24.1 percent of default service demand. In concert with a disproportionate reconciliation charge, PPL Electric's arithmetic

results in a TSC for Residential customers of 0.69 cents per kWh compared to a TSC for Small C&I customers of 1.29 cents per kWh, despite the fact that Small C&I customers are generally less costly to serve.

PPL Electric's energy and peak demand forecasts imply that the Small C&I load factor will be approximately 0.57 times the Residential class load factor. Thus, for example, if PPL Electric forecasts that the Residential load factor is, say, 50 percent, the Small C&I load factor will be 28.5 percent. While it is certainly possible that the Small C&I customers who remain on default service have relatively low load factors, this is an unlikely and extreme result. Moreover, under PPL Electric's reconciliation mechanism, the unlikely high demand share of 24.1 percent for Small C&I customers will be perpetuated in the reconciliation mechanism, regardless of whether actual Small C&I demand levels are much lower.

OSBA Statement No. 1, at 7-8 (footnotes omitted).

Fourth, Mr. Knecht observed:

[T]he differing eligibility rules for Small C&I customers between the GSC-1 and the TSC involve needless complexity and confusion.

*Id.*, at 8 (footnote omitted).

With regard to the first of these problems, Mr. Knecht proposed two alternative solutions to help alleviate the problems with the Company's TSC proposal. Mr. Knecht summarized those proposals, as follows:

In my direct testimony, I argued that this approach was anti-competitive, and that it could be resolved by either (a) recovering non-market-based ('NMB') transmission costs for both shopping and default service customers in a non-bypassable charge, or (b) assigning transmission costs to default service suppliers to level the playing field.

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

Mr. Knecht's first proposal to recover NMB transmission costs in a non-bypassable default service rider has been rejected by the Commission in *Joint Petition of Metropolitan*

*Edison Company, et al., for Approval of Their Default Service Program*, at Docket No. P-2011-2273650, *et al.* (Order entered August 16, 2012) (“*FirstEnergy Order*”). See OSBA Statement No. 3, at 3.

Mr. Knecht explained his second proposal, as follows:

If PPL Electric assigns transmission costs to wholesale suppliers, it should adopt a policy that transmission costs are assigned to both wholesale and retail suppliers on the same basis, primarily based on actual PLC levels by rate class group. In this approach, the TSC is eliminated and no reconciliation is necessary, because the variances are absorbed by wholesale suppliers. Transmission costs would implicitly be recovered by wholesale suppliers in their bid prices, and by retail suppliers in their prices to customers.

OSBA Statement No. 1, at 8-9.

Therefore, the OSBA recommends that Mr. Knecht’s second solution “to pass transmission costs currently recovered in [PPL’s] TSC onto the default service wholesale suppliers” be adopted. *Id.*, at 8. The OSBA submits that this change would level the playing field between retail and wholesale suppliers.

Regarding Mr. Knecht’s second and third concerns with PPL Electric’s TSC mechanism, the OSBA notes that the problems are mitigated simply by assigning transmission costs to the default service wholesale suppliers.

Resolving the next two problems depends on which of these approaches is adopted. . . .

If PPL Electric assigns transmission costs to wholesale suppliers, it should adopt a policy that transmission costs are assigned to both wholesale and retail suppliers on the same basis, primarily based on actual PLC levels by rate class group. In this approach, the TSC would be eliminated and no reconciliation would be necessary, because the variances would be absorbed by both wholesale and retail suppliers. Transmission costs would implicitly be recovered by wholesale suppliers in their bid prices, and by retail suppliers in their prices to customers.

*Id.*, at 8-9.

Finally, regarding Mr. Knecht's fourth issue with the Company's TSC proposal, Mr. Knecht suggested that some simplification take place in regard to the definition of a Small C&I customer:

PPL Electric's default service plan should be modified such that the eligibility criteria for Small C&I is the same for all components of the PTC. Having two different definitions of 'Small C&I' for two different aspects of the PTC is bound to cause confusion, no matter how hard the Company tries to make it clear. The start of a new default service plan represents a good opportunity to bring a little more consistency to default service pricing.

*Id.*, at 9.

In rebuttal, PPL responded by vaguely asserting that this proposal may have "adverse effects on certain customers" and could lead to "cost shifting among customer classes." PPL Statement No. 5-R, at 11-12. Unfortunately, Mr. Knecht was unable to evaluate this response, given its lack of specificity. In surrebuttal, Mr. Knecht testified:

I can neither agree nor disagree. Mr. Kleha does not explain who the 'certain customers' are who 'may' be affected, or how the 'cost shifting' among customer classes 'may' occur. I certainly had no intention of creating a cost shifting problem with my recommendation. It was my goal to eliminate a confusing tariff inconsistency between the two components of the price to compare ('PTC'), and to simplify the Company's recordkeeping.

Thus, based on the evidence available to me, I retain the recommendation in my direct testimony. However, if PPL Electric presents credible evidence that a material amount of cost shifting would occur under my proposal in its rejoinder testimony, I will recommend to the OSBA that it not argue in support of this recommendation in its briefs in this proceeding.

OSBA Statement No. 3 at 4.

In the absence of hard evidence, the OSBA can only conclude that PPL is resisting a change because it is a change, and not for any credible regulatory reasons. The OSBA therefore

recommends that Mr. Knecht's proposed change in eligibility rules for the Small C&I rate class group be adopted.

### **3. Time of Use Rate Option**

In general, the OSBA does not object to PPL's proposal to incorporate Time of Use ("TOU") service into the default service procurement for Small C&I customers. *See* PPL Statement No. 3, at 3-10.

Mr. Knecht did identify some problems with the Company's TOU proposal. First, the Company's proposal sets forth different on-peak and off-peak periods for the Residential and Small C&I customer classes. OSBA Statement No. 1, at 10. Mr. Knecht pointed out that "[h]ourly market prices are the same for Residential and Small C&I customers, and any benefits of shifting a kWh of electricity from a high-priced hour to a lower-priced hour is the same for both classes." OSBA Statement No. 1, at 10. Consequently, there is no economic basis for the Company's proposal.

Second, Mr. Knecht explained the impact upon wholesale suppliers:

[I]ntegrating TOU service with basic 'fixed rate' default service will increase the risk faced by wholesale suppliers. This increased risk will likely result in higher wholesale bid prices for default supplies than would exist if TOU service were separately procured. In effect, default service fixed rate customers will be asked to absorb the risks associated with customers who take TOU service. This can be perceived as inequitable to fixed rate default service customers.

*Id.*, at 10-11.

Nevertheless, Mr. Knecht found no "practical" reason to object to the Company's TOU proposal:

I support the Company's TOU proposal for Small C&I customers on practical grounds. When first implemented in January of 2011, Small C&I customers interested in TOU rates were lured into

taking service by the fact that both on-peak and off-peak rates were below the corresponding fixed default service rate. However, for the past ten months, both the on-peak and off-peak TOU rates for Small C&I customers have been higher than the basic default service rate. As such, all TOU customers necessarily pay more for power under the TOU rates than under fixed default service rates, regardless of when they consume power. ***Not surprisingly, this pricing situation has likely soured customer interest and has resulted in only a very few customers remaining on the Company's TOU default service.***

Thus, I expect that there is little interest in Company-sponsored TOU rates.

I therefore see no need to tinker with the unattractive aspects of the Company's proposed rate design. I also believe that wholesale suppliers will perceive very little risk associated with TOU service, given the low level of interest in the product. And finally, I see no need to have a separate and costly procurement, from either wholesale or retail suppliers, to provide service to the very few customers who would be interested.

OSBA Statement No. 1, at 11 (footnote omitted) (formatting added) (emphasis added).

Simply put, the TOU product offered by the Company is not a popular, nor viable, rate offering. Thus, the OSBA does not object to its inclusion in the Small C&I procurement as it should have little impact on either supplier or customer.

### **C. Retail Market Enhancements and Customer Referral Programs**

#### **3. Opt-In Auction**

On March 2, 2012, the Commission entered an Order at Docket No. I-2011-2237952, wherein the Commission concluded that Small C&I customers would not be included in retail opt-in auctions. *See Investigation of Pennsylvania's Retail Electricity Market: Intermediate Work Plan*, Docket No. I-2011-2237952 (Order entered March 2, 2012) ("IWPf Order"), at 42.

On August 16, 2012, the Commission entered an Order in the FirstEnergy Companies' default services proceedings. In the *FirstEnergy Order*, the Commission reversed its March

decision and decided that Small C&I customers should be eligible to participate in retail opt-in auctions. The Commission stated, as follows:

While we recognize that this decision deviates from our conclusions within our recent *IWPF Order*, we find that RESA's position with regard to the *relatively* low levels of current shopping in the Companies' service territories is compelling. In particular, the record indicates that over half of the small commercial customers in the Companies' service territories are not participating in the competitive market and the reasons for these customers not shopping are similar to those for residential customers.

*FirstEnergy Order*, at 103-104 (emphasis added).

The Commission's departure from the *IWPF Order* appears to be based upon two prongs. The first prong is that there was "relatively low levels of current shopping" in the FirstEnergy service territory. The second prong is that "over half of the small commercial customers in the Companies' service territories are not participating in the competitive market." Thus, the Commission appears to have adopted a rule that if the percentage of commercial customers who shop is less than 50 percent, then commercial class should be included in the retail opt-in auction.

Given that formulation of the Commission's rule, PPL's Small C&I customers should not be included in any retail opt-in auction. The shopping level of the Company's Small C&I customers exceeds the threshold set forth in the *FirstEnergy Order*. Mr. Knecht explained the OSBA position, as follows:

In contrast to the FirstEnergy Companies, PPL Electric has the highest level of Small C&I shopping of any EDC in Pennsylvania. Moreover, it is in fact the only large EDC in Pennsylvania with a commercial customer shopping rate in excess of 50 percent. (See attached Exhibit IEc-S1, which is the most recent shopping statistics from the OCA's website.) Thus, the Commission's

rationale for reversing its original finding in the IWPF Order in the FirstEnergy Decision should not apply to PPL Electric.

OSBA Statement No. 3, at 5-6 (footnote omitted).

Consequently, the OSBA respectfully submits that there is no basis for including the Company's Small C&I customers in any retail opt-in auction.

#### IV. Conclusion

Wherefore, the OSBA respectfully requests that the Commission:

- 1) Adopt PPL's proposed procurement product mixture for the Company's Small C&I customers;
- 2) Adopt PPL's proposed procurement schedule for the Company's Small C&I customers but eliminate the use of "stub" contracts;
- 3) Adopt PPL's proposed supplier load cap for the Company's Small C&I customers;
- 4) Defer the PPL issue of including Cash Working Capital costs in the default service rates to the Commission's proceeding on reconciliation of default service costs;
- 5) Adopt PPL's proposed reconciliation mechanism for the Company's Small C&I customers for the purposes of this proceeding;
- 6) Order PPL to pass transmission costs currently recovered in the Company's Transmission Service Charge along to the default service wholesale suppliers;
- 7) Adopt PPL's proposal to include Time of Use service in the default service procurement for the Company's Small C&I customers; and
- 8) Reject the use of a retail opt-in auction for the Company's Small C&I customers.

Respectfully submitted,



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