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October 19, 2012

VIA eFILING

Rosemary Chiavetta, Secretary
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400 North Street
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**Re: Petition of PECO Energy Company for an Evidentiary Hearing
 on the Energy Efficiency Benchmarks Established for the Period
 June 1, 2013 through May 31, 2016
 Docket No. P-2012-2320334**

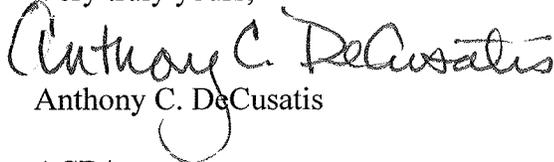
Dear Secretary Chiavetta:

Enclosed for filing is the **Initial Brief of PECO Energy Company** ("Initial Brief") in the above-referenced matter.

As evidenced by the attached Certificate of Service, a copy of the Initial Brief has been served electronically and via first class mail upon Administrative Law Judge Elizabeth H. Barnes and all parties.

Should you have any questions, please contact me directly at 215.963.5034. Thank you.

Very truly yours,


Anthony C. DeCusatis

ACD/tp
Enclosures

c: Certificate of Service (w/encls.)

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

**PETITION OF PECO ENERGY FOR AN :
EVIDENTIARY HEARING ON THE :
ENERGY EFFICIENCY BENCHMARKS : DOCKET NO. P-2012-2320334
ESTABLISHED FOR THE PERIOD :
JUNE 1, 2013 THROUGH MAY 31, 2016 :**

CERTIFICATE OF SERVICE

I hereby certify that I have this date served true and correct copies of the **Initial Brief of PECO Energy Company** upon the individuals listed below, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant):

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**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

**PETITION OF PECO ENERGY :
COMPANY FOR AN EVIDENTIARY :
HEARING ON THE ENERGY : DOCKET NO. P-2012-2320334
EFFICIENCY BENCHMARKS :
ESTABLISHED FOR THE PERIOD :
JUNE 1, 2013 THROUGH MAY 31, 2016 :**

**INITIAL BRIEF OF
PECO ENERGY COMPANY**

**Before Administrative Law Judge
Elizabeth H. Barnes**

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I. INTRODUCTION AND PROCEDURAL HISTORY

On October 15, 2008, Governor Edward G. Rendell signed into law House Bill No. 2200 (“Act 129”), which added Section 2806.1 to the Pennsylvania Public Utility Code (“Code”). Act 129 required certain Pennsylvania electric distribution companies (“EDCs”), including PECO Energy Company (“PECO” or the “Company”), to file energy efficiency and conservation (“EE&C”) plans by July 1, 2009 containing the plan elements specified in Section 2806.1(b) of the Code (“Phase I EE&C Program”).¹ 66 Pa.C.S. § 2806.1(b). Additionally, Sections 2806.1(c) and (d) required that EDCs’ Phase I EE&C plans be designed: (1) to reduce retail energy consumption by a minimum of 1% by May 31, 2011 and a minimum of 3% by May 31, 2013; and (2) to reduce peak demand, measured by reference to the 100 highest hours of demand, by a minimum of 4.5% no later than May 31, 2013. 66 Pa.C.S. §§ 2806.1(c) and (d).

In compliance with Section 2806.1 and the Pennsylvania Public Utility Commission’s (“Commission”) Order entered January 16, 2009 at Docket No. M-2008-2069887 (“*Phase I Implementation Order*”), which implemented the terms of that section, PECO prepared and submitted its EE&C plan for the Phase I EE&C Program on July 1, 2009. The Commission approved PECO’s Phase I Plan, with modifications, on October 28, 2009, and further revisions were adopted in various subsequent orders.²

¹ 66 Pa.C.S. § 2806.1(l) exempts EDCs with fewer than 100,000 customers from this requirement.

² See, e.g., *Petition of PECO Energy Company for Approval of its Act 129 Energy Efficiency and Conservation Plan and Expedited Approval of its Compact Fluorescent Lamp Program*, Docket No. M-2009-2093215 (Order entered Feb. 17, 2010); *Petition of PECO Energy Company for Approval of its Act 129 Energy Efficiency and Conservation Plan and Expedited Approval of its Compact Fluorescent Lamp Program*, Docket No. M-2009-2093215 (Order entered Jan. 27, 2011).

Act 129 requires the Commission to impose penalties of not less than \$1 million and not more than \$20 million on any EDC that fails to achieve the consumption and/or peak demand reduction targets established under Sections 2806.1(c) and (d) of the Code. 66 Pa.C.S. § 2806.1(f)(2)(i). Act 129 also requires the Commission, by November 30, 2013, to evaluate the costs and benefits of the Phase I EE&C Program and, if the benefits of the Program are found to exceed their costs, to adopt “additional required incremental reductions in consumption” and “additional incremental requirements for reduction in peak demand.” 66 Pa.C.S. §§ 2806.1(c)(3) and (d)(2). Additionally, Section 2806.1(d)(2) provides that, if the Commission imposes additional requirements for an incremental reduction in peak demand, the reduction “shall be accomplished no later than May 31, 2017.”

In accordance with Act 129, the Commission launched its evaluation of the cost-effectiveness of the Phase I EE&C Program. To that end, on March 1, 2012, the Commission issued a Secretarial Letter seeking comments on the design and implementation of any future phase of the EE&C Program. In addition, the Commission retained a Statewide Evaluator (“SWE”) to conduct baseline and market potential studies, which were publicly released on May 8 and 10, 2012, respectively. Based on those studies and the Commission’s interpretation of the program cost cap imposed by Section 2806.1(g),³ the SWE concluded that “continuing electric energy efficiency programs in a Phase 2 of Act 129 will continue to be very cost effective for Pennsylvania ratepayers.”⁴

³ 66 Pa.C.S. § 2806.1(g) provides that “[t]he total cost of any plan required under this section shall not exceed 2% of the [EDC’s] total annual revenue as of December 31, 2006.”

⁴ *Electric Energy Efficiency Potential for Pennsylvania Final Report* (dated May 10, 2012) (“Market Potential Study”), p. 2.

On May 11, 2012, the Commission issued a Tentative Implementation Order at Docket Nos. M-2012-2289411 and M-2008-2069887 outlining its proposed standards for a Phase II EE&C Program. Based on the SWE's recommendations in its Market Potential Study, the Commission proposed to adopt additional required incremental reductions in consumption that vary by EDC. Numerous parties, including PECO, filed comments and reply comments in response to the Tentative Implementation Order.

On August 3, 2012, the Commission adopted EDC-specific targets for reducing energy consumption.⁵ In the *Phase II Implementation Order*, however, the Commission acknowledged that PECO had raised a legitimate due process issue with respect to the Phase II EDC targets because EDCs had not been afforded the opportunity for an evidentiary hearing on the facts used by the Commission to impose those targets. As a consequence, the *Phase II Implementation Order* provided that the consumption reduction targets “will become final for any EDC that does not petition the Commission for an evidentiary hearing by August 20, 2012.” *Id.* at 31. The *Phase II Implementation Order* further provided that, upon receipt of a timely petition for evidentiary hearing, the matter would be assigned to the Office of Administrative Law Judge for expedited hearings and that the record would have to be certified to the Commission no later than November 2, 2012. *Id.* at 31 and 120. The Commission permitted interested parties to file petitions to intervene in EDC-initiated evidentiary hearings no later than August 30, 2012. *Id.*

This proceeding was initiated on August 20, 2012, when PECO, pursuant to Ordering Paragraph No. 3 of the *Phase II Implementation Order*, filed its Petition for An Evidentiary Hearing (“Petition”) on its tentative, Company-specific consumption reduction target for the

⁵ *Energy Efficiency and Conservation Program*, Docket Nos. M-2012-2289411 and M-2008-2069887, at 24 (Order entered Aug. 3, 2012) (“*Phase II Implementation Order*”).

period June 1, 2013 to May 31, 2016 (“Phase II”). As described in the Petition, PECO proposes adjustments to its Phase II consumption reduction target based on allocating an appropriate level of funding to demand reduction (“DR”) programs and using a baseline to establish a spending limitation for PECO that is representative of current and reasonably projected revenue levels.

PECO served copies of its Petition on all parties who filed comments at Docket No. M-2012-2289411. On August 29, 2012, Administrative Law Judge (“ALJ”) Elizabeth H. Barnes issued a Prehearing Conference Order that scheduled a Prehearing Conference in this matter for September 10, 2012. On September 5, 2012, PECO submitted its direct testimony in support of the Petition. Thereafter, the following entities were afforded intervenor status in this case:

Coalition for Affordable Utility Service and Energy Efficiency in Pennsylvania	(“CAUSE-PA”)
Citizen’s For Pennsylvania’s Future	(“PennFuture”)
Clean Air Council and Sierra Club	(“CAC/Sierra”)
Community Action Association of PA	(“CAPP”)
Comverge, Inc.	(“Comverge”)
Duquesne Light Company	(“Duquense”)
Independent Statewide Evaluator	(“SWE”)
Office of Consumer Advocate	(“OCA”)
Philadelphia Area Industrial Energy Users Group	(“PAIEUG”)

At the Prehearing Conference, a schedule was established for submitting written testimony, holding an evidentiary hearing and filing briefs. *See* Scheduling Order (September 13, 2012). Written direct testimony was submitted by Duquesne and PennFuture and rebuttal testimony was submitted by PECO on the dates established for each submission. In addition, PECO responded to interrogatories issued by PennFuture.

An evidentiary hearing was held at the Commonwealth Keystone Building in Harrisburg on October 3, 2012. At the hearing, PECO witness Frank J. Jiruska was cross-examined and the testimony and exhibits of all parties were admitted into evidence. PECO submits this Initial Brief in support of its proposed adjustments to its Phase II consumption reduction target.

II. PECO'S PROPOSED ADJUSTMENTS TO ITS PHASE II EE&C BENCHMARK

In the *Phase II Implementation Order*, the Commission declined to establish an independently-determined statewide Phase II energy efficiency target applicable to all EDCs, as was done for Phase I. *See* 66 Pa.C.S. §§ 2806.1(c) and (d). Instead, using data from the SWE's Market Potential Study and Baseline Studies, the Commission developed Phase II consumption reduction targets that varied from EDC to EDC based on maximum permitted funding levels and projected acquisition costs. *Phase II Implementation Order*, pp. 14-23. Under this approach, the Commission set a Phase II consumption reduction target for PECO of 2.9%. *Id.*, p. 24; *see also* PECO St. No. 1, p. 8. As described below, PECO proposes adjustments to that 2.9% target to reflect an appropriate level of funding for DR as well as a total funding cap that is consistent with revenue levels achievable under current market and economic conditions.

A. PECO's Phase II Consumption Reduction Target Should Be Reduced Based On Allocating An Appropriate Level Of Funding For DR Programs

Section 2806.1(d)(2) of the Code authorizes the Commission to impose peak DR targets beyond those set by statute for Phase I only if it finds that the existing statewide DR program is cost-effective. The SWE's final report on the cost-effectiveness of existing DR programs and its recommendations for further DR reductions will not be completed and available for the Commission's consideration until the first quarter of 2013. Accordingly, the Commission concluded that it did not have authority at this time to establish a further peak DR target and, therefore, declined to do so. *Phase II Implementation Order*, p. 33. However, the Commission reserved the right to impose further peak DR targets which, when established, would have to be achieved by the statutory deadline of May 31, 2017 to avoid the imposition of penalties. *See* 66 Pa.C.S. § 2806.1(d)(2).

Because it decided not to include a peak DR target in the Phase II EE&C Program at this time, the Commission directed that the entire amount of each EDC's allowable spending under the funding cap should be dedicated solely to energy consumption reductions. *Phase II Implementation Order*, p. 41. As explained below, the Commission's decision was erroneous for several reasons and is also inconsistent with findings it made in the *Phase II Implementation Order* itself.

1. PECO's Existing Direct Load Control ("DLC") Measures

Although the Commission deferred a decision on the cost-effectiveness of the statewide peak DR program, it strongly encouraged EDCs to maintain specific, cost-effective DR measures as part of their EE&C programs even after the expiration of Phase I:

The Commission, however, does recognize that the EDCs and residential electric customers in particular have made significant strides in the implementation of residential curtailment measures, such as direct load control programs. Therefore, to minimize customer confusion or adverse customer reaction, EDCs may continue, *under the Act 129 EE&C Program*, residential demand response curtailment measures, such as direct load control programs, that will be cost effective if continued. Such specific measures, if continued, could be viewed as providing the interim demand response program suggested by some parties until the Commission determines whether or not there is a cost-effective Act 129 peak demand reduction program design. The Commission will not, however, set any reduction goals for an EDC choosing to voluntarily continue any DR programs.

Phase II Implementation Order at 42 (emphasis added).

Significantly, the Commission found that there would be material adverse effects from terminating cost-effective DR measures at the conclusion of Phase I. Indeed, the Commission recognized that such a premature termination of cost-effective measures would produce "stranded costs" during Phase II and would create "the potential for customer confusion,

specifically in the residential sector.” *Phase II Implementation Order*, pp. 38 and 40.

Additionally, the Commission assumed that, if and when it establishes a DR target in the future, “the infrastructure currently deployed would still be available to the EDCs in attaining any potential Phase III peak demand reductions targets.” *Id.* at 39. Notwithstanding those findings, the Commission did not provide any funding for the continuation of existing DR measures or for the implementation of new ones. Instead, in tentatively adopting the Phase II consumption reduction target for PECO, the Commission assumed that all of the funding resources available under Act 129’s spending cap would be used exclusively for the energy efficiency program. *See Phase II Implementation Order*, p. 41.

In contrast to the Commission’s approach, PECO is proposing to allocate approximately \$36 million of its total allowable Phase II EE&C plan spending to sustain its existing DLC measures for residential and small commercial customers (collectively, the “Mass Market DLC Program”) during Phase II. PECO’s proposed adjustment would reduce its allowable spending figure by \$36 million and result in an adjusted energy savings target of 2.5%. *See* PECO Exhibit FJJ-7.

The Mass Market DLC Program provides customers incentive payments for allowing PECO to control their central air conditioning equipment. As PECO witness Jiruska testified, applying the Total Resource Cost (“TRC”) test to PECO’s Mass Market DLC Program yields a score of 2.38, which clearly demonstrates that the total avoided-cost benefits of the program are substantially greater than the total costs of the program’s DLC measures. PECO St. 1, p. 10; PECO Exhibit FJJ-1. In addition, continuing the cost-effective Mass Market DLC Program will avoid possible customer confusion, prevent curtailment service providers (“CSPs”) from losing confidence in the sustainability of the program and mitigate administrative cost increases due to

the multiple program ramp-ups that would result from a lapse of continuity between Phase I and a potential third phase of Act 129 (“Phase III”). PECO St. No. 1, pp. 10-13. As shown on PECO Exhibit FJJ-4, the beneficial effects of maintaining the Mass Market DLC Program during Phase II can be accomplished for an estimated annual cost of \$12 million, or \$36 million over the three-year duration of Phase II.

PennFuture was the only party that presented testimony in opposition to PECO’s proposed funding allocation. PennFuture’s witness, Glenn Reed, contended that allocating any Phase II funding to DLC or DR measures was unnecessary and unwarranted for three reasons. First, Mr. Reed asserted that the Mass Market DLC Program can be continued during Phase II without Act 129 funding because PECO can sustain those measures and still meet its Phase II EE&C benchmark. As alleged support for this averment, Mr. Reed cited the Commission’s authorization for EDCs to apply excess Phase I energy savings toward their Phase II targets, which Mr. Reed believes would furnish sufficient funds to allow PECO to sustain its DLC measures. PennFuture St. (Reed), Question and Answer Nos. 31-34, 42.⁶ Second, Mr. Reed asserted that continuing the Mass Market DLC Program is not “mandatory” and, in any event, the cost of that program is overstated because it includes small commercial customers. As to the latter point, Mr. Reed argued that the Commission’s support for maintaining cost-effective DR measures encompassed only those measures that target residential customers and not small *commercial* customers’ DLC measures. *Id.*, Question and Answer Nos. 28-29, 42. Third, Mr. Reed alleged that further funding for the Mass Market DLC Program should not be significant because “existing DLC equipment has already been paid for.” *Id.*, Question and Answer No. 30. None of Mr. Reed’s arguments stand scrutiny, as explained below.

⁶ Mr. Reed’s statement does not contain page or line numbers. Hence, citations to his statement must be identified by Question and Answer numbers.

Mr. Reed's Contention That PECO Can Sustain DR Measures Throughout Phase II Without Allocating Any Phase II Funding To Those Measures. Mr. Reed's first contention simply misses the point. Projections of PECO ability to meet the tentative consumption reduction target identified by the Commission have no bearing on the funding necessary for the Mass Market DLC Program or other DR measures. What Mr. Reed fails to recognize is that the Commission has directed EDCs to spend the *full* amount of the funding resources available under the Act 129 spending cap on *energy efficiency* measures in each program year of Phase II, even after they achieve their savings target. *Phase II Implementation Order*, pp. 26, 29. As a result, even if PECO's Phase II consumption reduction target were satisfied, in part, by energy savings achieved during Phase I, any unused Phase II budget may not simply be redirected to PECO's Mass Market DLC Program – or any other DR measure – as PennFuture's witness recommends. As things now stand, given the directives set forth in the *Phase II Implementation Order*, those resources may only be spent on energy consumption reductions and not re-directed, as Mr. Reed and PennFuture assume.

Mr. Reed also asserts that because EDCs are permitted to credit accumulated excess savings toward their Phase II targets there is no need to furnish Act 129 funding for the Mass Market DLC Program or for the preparatory steps essential to meeting subsequently established Phase III DR targets. That assertion is also wrong. Specifically, even if the accumulated excess could be used as Mr. Reed assumes, the monetary effect is not enough to sustain PECO's Mass Market DLC Program let alone fund the preparation necessary for meeting a subsequently determined DR target. The arithmetic that demonstrates Mr. Reed's error is straight-forward. PECO currently anticipates banking approximately 83,000 megawatt-hours ("MWh") of excess

energy savings from Phase I that may be used toward its Phase II target.⁷ This amount translates to approximately \$18.9 million in unused budget, as Mr. Jiruska explained. Tr. 66 (discussing PECO's Response to PennFuture Interrogatory PF-I-1). That funding amount is well below the projected \$36 million needed just to sustain PECO's Mass Market DLC Program. Accordingly, the total amount of funding available by virtue of accumulated excess Phase I energy savings, even if it could be used for DR measures, does not cover the cost of maintaining PECO's Mass Market DLC Program for the Phase II period.

Mr. Reed's Contention That The Commission Supports, But Does Not Require, Continuation Of Cost Effective Residential DR Measures. At the outset, Mr. Reed's contention that the Commission did not "require" EDCs to "continue" cost-effective residential DR programs amounts to little more than an exercise in semantics. As previously explained, the Commission found that continuing cost-effective residential DR programs would benefit customers and that discontinuing those measures for the duration of Phase II would have significant deleterious effects. *Phase II Implementation Order*, pp. 38-40. Moreover, the Commission assumed that, if and when DR targets are established in the future, "the [DR] infrastructure currently deployed would still be available to the EDCs" to furnish the means for achieving those targets. *Id.* at 39. In short, while not using the words "require" or "requirement," what the Commission actually said with respect to the continuation of cost-effective residential DR programs is hardly different, as a practical matter, from imposing such a requirement.

⁷ Estimates of banked MWh savings change from month to month. The final actual savings figure will not be known until Phase I ends on May 31, 2013, although even that figure must be verified by the Commission in February 2014.

Mr. Reed's contention that the Company's Mass Market DLC Program costs are overstated because they include costs related to DLC measures for small commercial customers is similarly without merit. As the Commission recognized, EDCs have made significant strides in implementing curtailment measures, such as residential DLC programs. *Phase II Implementation Order*, p. 42. And, although the Commission did not specifically target small commercial demand curtailment programs for continuation in the *Phase II Implementation Order*, it is undeniable that PECO's ability to meet a subsequently determined peak DR target by the statutory deadline would be severely jeopardized if PECO could not capture peak demand reductions from this customer sector. Furthermore, and unmentioned by Mr. Reed, the cost of the small commercial component of the Mass Market DLC Program constitutes only about \$5.9 million of the estimated \$36 million cost of that program. PECO Exhibit FJJ-3.

Mr. Reed's Contention That Further Funding Of The Mass Market DLC Program Should Be Minimal Because "Existing DLC Equipment Has Already Been Paid For." The equipment in question consists primarily of the DLC switches used to control customers' air conditioning equipment. The fact that DLC equipment was, in large part, recovered during Phase I does not mean that PECO's Mass Market DLC Program can be sustained for another three years without funding.⁸ Mr. Reed totally ignored the program's largest cost elements, which consist of administrative costs and customer incentive payments and are not in any way related to DLC infrastructure. Notably, but unmentioned by Mr. Reed, the DLC equipment that PECO installed during Phase I is a perfect example of a substantial asset that would be "stranded" if DLC measures were discontinued at the conclusion of Phase I – precisely the

⁸ Mr. Reed also ignored the fact that not all of the installed DLC equipment will perform flawlessly over its entire estimated service life and, therefore, some portion of DLC equipment needs to be replaced each year. The associated replacement and repair costs are part of the total cost of maintaining operable DCL measures. Tr. 49-50.

outcome the Commission stated, in the *Phase II Implementation Order* (p. 41), EDCs should strive to avoid.

2. Designation Of Phase II Funding For DR In Anticipation That EDCs Will Be Required To Achieve An Additional Incremental Reduction In Peak Demand

PECO also proposes to allocate approximately \$17.4 million of its total Phase II allowable funding to achieve a subsequently established peak DR target by May 31, 2017. As Mr. Jiruska explained, \$17.4 million is a conservative estimate of the costs PECO will have to incur during Phase II to prepare for DR programs that must be in place before the summer of 2016 to meet a DR target by the statutory deadline. That estimate reflects PECO's Phase I experience, a modest projected increase in the acquisition cost to achieve peak demand reductions in subsequent phases of Act 129 and the uncertainty surrounding the amount of resultant DR that energy efficiency programs will produce after they become operable. PECO St. No. 1, pp. 15-16. Notably, no party submitted testimony contesting PECO's projected start-up costs, which include costs incurred for program design, developing a request for proposals to solicit CSPs, administering the competitive bidding process, preparing TRC calculations, marketing, and customer enrollment.

As previously noted, if the Commission hereafter determines that further DR measures will be cost effective and, therefore, establishes peak DR targets, PECO would have to reduce its peak demand by the targeted levels during the summer of 2016. PECO St. No. 1, p. 14; PECO Exhibit FJJ-5. This timeframe is dictated by the Commission's directive that targeted savings must be measured by reference to a period of peak demand occurring during the months of June through September – a period the Commission also directed should be the focus of EDCs' peak demand reduction measures. *Phase I Implementation Order*, p. 21 (“[T]he 100 hours of highest

demand for the annual system peak demand determination should be limited to the months of June, July, August and September.”) Consequently, to achieve peak demand reductions during the summer of 2016, all of the DR measures and associated infrastructure must be in place well before then (i.e., during the Phase II period). *Id.* For example, as shown on PECO Exhibit FJJ-5, PECO must initiate information technology system upgrades in the summer of 2013 – the beginning of the Phase II period. In addition, the program design process must commence two years prior to the June 1, 2016 implementation date. And, if those programs and associated infrastructure must be in place, they need to be funded with money that PECO is authorized to spend below the Act 129 statutory cap.⁹

PennFuture opposes any allocation of Phase II funds to DR, asserting that PECO may spend **Phase III** funds during Phase II to “lay the foundation” for additional incremental peak demand reduction requirements. PennFuture St. (Reed), Question and Answer Nos. 36-42. Mr. Reed’s contention is fundamentally flawed. In concluding that PECO need not designate a portion of its Phase II allowable spending for additional incremental DR requirements, Mr. Reed assumes that the Commission has already authorized EDCs to begin performing administrative duties (e.g., planning, marketing, contracting with CSPs, etc.) related to potential Phase III EE&C plans and to defer such costs until Phase III cost recovery rates are in effect. However,

⁹ PECO’s legitimate concerns are not addressed by the suggestion that the cost of DR measures incurred during Phase II might be claimed for recovery by petitioning the Commission for authority to establish a separate automatic adjustment clause under Section 1319 of the Code (66 Pa.C.S. § 1319). If the DR measures at issue are to be considered part of Act 129 for purposes of meeting an Act 129 DR target, then those costs must be earmarked as such and recovered under the preexisting Act 129 cost recovery mechanism. To do otherwise is to create a separately funded DR program that operates in parallel with, but separate from, the Act 129 measures that count toward any subsequently established DR target. Moreover, the lawfulness of such a separate funding scheme is subject to serious questions because, if permitted, it would be an end-run around the spending limitation the legislature imposed under Act 129.

the Commission has not yet authorized EDCs to incur any costs related to future energy efficiency measures, let alone DR programs that will be implemented beyond the Phase II period. Indeed, the Commission is still conducting its Act 129 evaluation of Phase I DR programs. In short, the Commission has provided EDCs no assurance that costs incurred to prepare for subsequent DR mandates during the Phase II period will ultimately be recoverable. Therefore, the foundational premise of PennFuture's recommendation to deny any Phase II funding for DR is incorrect.

The Commission should adopt PECO's proposed adjustment to its Phase II allowable spending to allocate an appropriate level of funding to prepare to meet targeted peak DR savings by May 31, 2017. The associated three-year cost estimate of \$17.4 million cost would reduce the consumption reduction target by approximately 0.1%. This adjustment, in combination with the reduction resulting from allocating approximately \$36 million to maintaining the Mass Market DLC Program, would reduce the consumption reduction target from the 2.9% to 2.3%. *See* PECO Exhibit FJJ-7.

B. PECO's Phase II Consumption Reduction Target Should Be Reduced Based On The Commission's Overstatement Of Allowable Spending

As previously explained, the Commission assumed an allowable spending level of 2% of PECO's 2006 annual revenues – approximately \$256.2 million – in determining PECO's Phase II consumption reduction target.¹⁰ In its Petition, PECO identified two adjustments that must be made to establish a reasonable, allowable spending level. First, the Commission should use 2011 data rather than 2006 data as a revenue baseline to establish PECO's Phase II EE&C plan

¹⁰ The Commission developed each EDC-specific consumption reduction target based on a formula that makes those targets a function of the available funding level divided by the EDC's acquisition cost (expressed in dollars per MWh). *See* PECO St. No. 1, p. 7.

funding limit. Second, electric generation supplier (“EGS”) revenues collected by PECO pursuant to Commission-mandated consolidated billing should be excluded from the 2011 revenue figure. These adjustments, collectively, reduce the consumption reduction target by 1.0%, from 2.9% to 1.9%. *See* PECO Ex. FJJ-8.

1. Revenue Baseline

Section 2806.1(g) of the Code provides a hard “cap” on the amount that the Commission is authorized to permit EDCs to spend to achieve consumption and demand reduction targets established under Act 129. Specifically, Section 2806.1(g) states in pertinent part as follows:

Limitation on costs. – The total cost of any plan required under this section shall not exceed 2% of the electric distribution company’s total annual revenue as of December 31, 2006.

Although Section 2806.1(g) sets the outer limit of EDC spending that is permitted under Act 129, it does **not** mandate that the Commission direct EDCs to spend every dollar up to that “cap.” To the contrary, nothing in Section 2806.1(g) or any other provision of Act 129 limits the Commission’s authority and discretion to employ a funding amount below the “cap” to establish reasonable consumption reduction target. Indeed, if the Commission believed otherwise, then its entire approach to setting consumption reduction targets for Phase II proceeded on a false premise, and the Commission failed to exercise the discretion it is clearly afforded under Section 2806.1(g).

Simply stated, the Commission should not merely assume that the outer limit of maximum EDC spending demarcated by Section 2806.1(g) should be used to set consumption reduction targets. Instead, the Commission should – as it must – acknowledge and exercise its discretion to set a funding level that is not only below the “cap” but is reasonable based on the

revenue levels an EDC is likely to achieve during the period that a consumption reduction target must be met. As explained by Mr. Jiruska, PECO's revenue for the twelve months ended December 31, 2011 is a far more reasonable baseline than 2006 revenues, which were billed during a pre-recession period when electric generation prices were much different from what they are today. PECO St. No. 1, pp. 17-18. In fact, the decline in energy prices since 2006 – and, in particular, since 2008, when Act 129 became law – has resulted in EE&C surcharges becoming a significantly higher proportion of customers' total electric bill revenue. *Id.* These important factors, which were not considered and not recognized by the Commission in establishing the consumption reduction targets, require that that the Commission re-examine its approach.

PennFuture opposes the use of 2011 revenue baseline but does so without engaging the substance of PECO's evidence and arguments on this issue. In fact, PennFuture does not contest – because it cannot – the fundamental facts supporting PECO's position. Both revenue levels and energy prices are considerably lower today than in either 2006 or 2008, and EE&C surcharges are a higher proportion of customers' total bills. Instead of addressing the point PECO actually made, PennFuture, in effect, changes the subject, arguing that PECO's proposed adjustments, by reducing allowable spending, would result in “lost benefits” for customers. PennFuture (Reed), Question and Answer Nos. 20-23. As might be expected, Mr. Reed discusses only the alleged “lost benefits” that a subset of PECO's customers might realize from increased spending while ignoring – and hoping the Commission will ignore – the other side of the coin, namely, the reduced costs that **all** customers would be asked to bear under PECO's proposal. Contrary to Mr. Reed's assertions, using a revenue baseline that is properly reflective

of current market and economic conditions will benefit all customers by lowering their overall electric bills.

As previously explained, the substantial decline in energy prices since Act 129's enactment has caused EE&C surcharges to become a significantly higher proportion of customers' total electric bills. PECO St. No. 1, p. 18. Moreover, in light of the current difficult economic conditions, a reduction in PECO's Phase II budget that properly reflects reasonably expected revenue levels for the Phase II period would produce a more reasonable spending level, yield a more realistic consumption reduction target, and reduce the burden on all customers that are subject to the EE&C surcharge.

2. Treatment Of EGS Revenue

As previously explained, Section 2806.1(g) of the Code imposes an outer limit on the amount the Commission can require EDCs to spend on Act 129 consumption and peak demand reduction measures. Specifically, the operative portion of that section sets the maximum spending limit at "2% of the electric distribution company's *total annual revenue* as of December 31, 2006" (emphasis added). Section 2806.1(m) defines significant terms used in Act 129. That section provides that "[e]lectric distribution company total annual revenue" shall mean: "Amounts *paid to* the electric distribution company *for* generation, transmission, distribution and surcharges by retail customers" (emphasis added).

The plain language of Section 2806.1(m) makes it clear that the amounts "paid to" an EDC "for generation" encompass only those payments that customers make to the EDC for generation service the EDC furnishes, i.e., default service. Just as clearly, amounts that EDCs collect as agents on behalf of EGSs under Commission approved consolidated billing do not

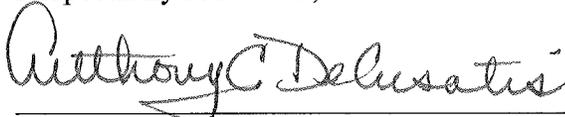
constitute revenues “paid to” an EDC “for generation.” Rather they are amounts paid to EGSs for generation service furnished by such EGSs. The EDC, as to such amounts, is just the “middle man” – fulfilling the ministerial role of an agent collecting sums they have no right to keep. As such, amounts that EDCs collect on behalf of EGSs should be excluded from the “total annual revenue” used to establish allowable spending levels. Indeed, the Commission has no authority to include such amounts in setting the funding limit.

As explained in the direct testimony of its witness, Mr. David Defide, Duquesne supports excluding EGS revenue from PECO’s Phase II allowable spending as long as the Commission adopts a uniform approach for all EDCs. Duquesne St. No. 1, pp. 6-7. Duquesne also expressed concerns about its ability to meet its EDC-specific Phase II consumption reduction target of 2.0% if the Commission adheres to the statutory definition imposed by Section 2806.1(m). Those concerns are not warranted. As explained by Mr. Jiruska, a reduction in allowable spending for Phase II would not impair an EDC’s ability to meet its target because, as calculated by the Commission, an EDC’s Phase II target will automatically decline in proportion to any reduction in allowable spending (*see* footnote 9, *supra*). Therefore, following the statutory prescription and applying the Commission’s approach to setting consumption reduction targets, Duquesne’s 2.0% target will consequently decline without the need for an additional filing.

III. CONCLUSION

For the reasons set forth above, the Commission should enter an order adopting PECO Energy Company's proposed adjustments to its energy consumption reduction target for the period June 1, 2013 to May 31, 2016.

Respectfully submitted,



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