COMMONWEALTH OF PENNSYLVANIA
PENNSYLVANIA PUBLIC UTILITY COMMISSION
P.O. BOX 3265, HARRISBURG, PA 17105-3265

IN REPLY PLEASE
REFER TO OUR FILE

April 7, 1998

The Honorable Lawrence Roberts
House of Representatives
House Post Office - Main Capitol
Harrisburg, PA 17120

DOCUMENT FOLDER

R-974104

Dear Representative Roberts:

Thank you for your recent letter of March 23, 1998, to Chairman John Quain concerning stranded cost recovery by Allegheny Power which is a matter currently pending before the Public Utility Commission in Allegheny Power's electric restructuring plan filed under the Electric Generation Customer Choice and Competition Act.

Each jurisdictional electric utility company operating in Pennsylvania has filed a restructuring plan with the Pennsylvania Public Utility Commission. The Commission is approaching the issue of stranded cost recovery on a case-by-case basis, and each electric company and other interested parties are litigating a multitude of issues within the context of each restructuring plan filing.

Since this matter is currently pending before the Commission, please know that I have taken the liberty of forwarding your letter to the Secretary of the Commission for inclusion into the official file of the Allegheny Power proceeding. On March 25, 1998, the Office of Administrative Law Judge issued its Recommended Decision in this matter. It will now be placed before the Commission for final consideration. Please find enclosed a copy of the Commission's press release summarizing the Recommended Decisions.

Sincerely,

Rosemary Chiavetta, Esq.
Director of Legislative Affairs

Enclosure

cc: Chairman John Quain
Secretary James McNulty

RECEIVED
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SECRETARY'S OFFICE

14 1995

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House of Representatives
COMMONWEALTH OF PENNSYLVANIA
HARRISBURG

March 23, 1998





Mr. John M. Quain, Chairman
PA Public Utility Commission
P O Box 3265
Harrisburg, PA 17105-3265



Re: ALLEGHENY POWER STRANDED COSTS

Dear Mr. Quain:

I've been very concerned about the possible outcome of this stranded cost issue and how it will affect my district. Allegheny Power has been the lowest cost electric utility in the state of Pennsylvania for decades. This has helped to attract business into this area and keep the businesses we already have. I do not want to lose this advantage.

It is apparent that our current position is due, in large part, to Allegheny's well-managed generating facilities. However, I understand that if Allegheny Power is not permitted to recover its stranded costs, it will have to divest its generation. Whether this divestiture is economic or otherwise, I fear the result will be higher electricity costs for my district.

Loss of local ownership and operation of Western Pennsylvania's generation by Allegheny will have a dramatic negative impact on competition and likely increase our electric bills. For example, the new purchaser of these facilities will have no obligation to sell its power within Western Pennsylvania. It seems to me, they will likely attempt to maximize profits by selling locally generated power first to areas where current rates are double that of ours and second, in our area, at increased market rates. As a result, I suspect that the long-range market rates in our area will tend to increase to some statewide levelized rate. We would, therefore, not be able to take advantage of Allegheny's present low rates.

Higher rates will create a hardship for the current business and be devastating to future economic development for my area. Particularly penalized would be the small business owner and residential customers. I am requesting that in your review of this very complex and important issue that you do not penalize the best managed utility in the state. My view is to allow them to remain an intact company, maintain increased competition, and continue to provide my district with the lowest cost electrical energy.

Sincerely,

Larry Roberts

Lawrence Roberts
State Representative
51st District

LR/dh

SCOTT J. RUBIN
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ORIGINAL

April 9, 1998

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APR 10 1998

PA PUBLIC UTILITY COMMISSION
PROTHONOTARY'S OFFICE

James McNulty, Prothonotary
Pa. Public Utility Commission
P.O. Box 3265
Harrisburg, PA 17105-3265

Re: Duquesne Light Company's Restructuring Plan
Docket No. R-00974104

Dear Mr. McNulty:

Enclosed for filing please find an original and nine (9) copies of the Exceptions of System Council U-10, International Brotherhood of Electrical Workers, in the above-referenced proceeding. A copy of this document has been served on Administrative Law Judge Corbett and all parties of record, as shown on the attached certificate of service.

I am also enclosing an extra copy of the document that I would appreciate having time-stamped and returned to me in the enclosed envelope. Thank you.

Sincerely,

Scott J. Rubin, Esq.

Enclosures

cc: Hon. John Corbett, Jr., ALJ
Office of Special Assistants (with diskette)
All parties of record

DOCUMENT
FOLDER

BEFORE THE
COMMONWEALTH OF PENNSYLVANIA
PUBLIC UTILITY COMMISSION



| | | |
|---|---|---|
| APPLICATION OF DUQUESNE LIGHT COMPANY FOR APPROVAL OF ITS RESTRUCTURING PLAN UNDER SECTION 2806 OF THE PUBLIC UTILITY CODE | : | DOCKET NO. R-00974104 |

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# EXCEPTIONS
# OF SYSTEM COUNCIL U-10,
# INTERNATIONAL BROTHERHOOD OF ELECTRICAL WORKERS

---



SCOTT J. RUBIN
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(717) 743-2233

COUNSEL FOR:
SYSTEM COUNCIL U-10, IBEW

DATED: APRIL 14, 1998

## Table of Contents

## Introduction and Summary of Exceptions

These Exceptions are submitted on behalf of System Council U-10, International Brotherhood of Electrical Workers ("IBEW"). IBEW is the bargaining representative for approximately 2000 employees of Duquesne Light Company ("Duquesne"). IBEW St. 1 at 1. In this proceeding, IBEW is representing the interests of its current members as well as its retirees, both as employees of Duquesne and as consumers of electricity within Duquesne's service territory. *Id.* IBEW presented the testimony of one witness, its business manager Timothy Moran, who prepared IBEW Statement 1.

IBEW takes exception to one aspect of the Recommended Decision issued by Administrative Law Judge Corbett ("the ALJ"). Specifically, the ALJ recommended that, if the merger between Duquesne and Allegheny does not occur, Duquesne should be ordered to sell all of its power plants. RD at 159. The law and the evidentiary record in this case do not support such a sale.

The lack of information concerning the proposed sale of Duquesne's power plants is striking. Neither Duquesne nor any other party has attempted to evaluate the effect of plant sales or closures on the reliability of Duquesne's transmission system, though initial indications are that there would be serious reliability problems caused by closing or selling Duquesne's plants. Neither Duquesne nor any other party has attempted to evaluate the effect of plant sales or closures on Duquesne's employees. Neither Duquesne nor any other party has attempted to evaluate the effect of plant sales or closures on the communities where those plants and employees are located. Moreover, the ALJ and the parties making these proposals, including Duquesne in the later stages of this case, have failed to recognize that the proposed, Commission-ordered sale of these plants is directly contrary to the Public Utility Code.

IBEW fully explored these issues in its Main Brief and the ALJ summarized IBEW's arguments on pages 134-139 of the Recommended Decision. However, the ALJ does not address any of IBEW's legal or factual bases for refusing to order the sale of power plants.

Simply, as IBEW discusses in Exception 1, the Commission does not have the legal authority to order the sale or closure of a power plant. Moreover, even if it did, the evidence of record in this case does not establish the need to do so. In fact, the evidence shows that Duquesne needs these plants in order to provide safe, adequate, and reliable service to its customers. Therefore, the Commission cannot order Duquesne to sell or close any of its power plants.

## Exception

### Exception 1: The ALJ Erred by Recommending that the Commission Order Duquesne to Sell its Power Plants if Duquesne does not Merge with Allegheny Power System, Inc.

In response to proposals made by several other parties, Duquesne has proposed to sell its power plants if the Commission orders it to do so. Tr. 176. Duquesne made it clear, however, that selling its plants was not its preferred method of valuing its stranded costs and that it does not believe that such a sale is the best course of action. Tr. 173, 182. However, Duquesne has offered to "waive our right" and sell its plants if the Commission so orders. Tr. 182.

The ALJ apparently accepted Duquesne's offer, without considering any of the legal or factual reasons why the Commission cannot and should not order Duquesne to sell its power plants. RD at 159.

Perhaps the ALJ relied on Duquesne's Reply Brief. In its Reply Brief, Duquesne stated – for the first time and directly contrary to the testimony of its President – that its proposed plant sale was ***not*** contingent on a Commission order. Duquesne Reply Brief at 2. If the ALJ did rely on this statement, he erred in doing so. The President of the Company testified under oath that

Duquesne was not making a voluntary decision to sell its power plants and that its preferred course of action was to retain those plants. Neither Duquesne's attorneys nor the ALJ can change that into a voluntary action.

This distinction is important. There is no question that the Commission lacks the legal authority to order, or otherwise compel, Duquesne to sell any of its power plants. Section 2804 of the Public Utility Code, 66 Pa. C.S. § 2804(5), specifically prohibits the Commission from ordering a utility to sell any of its facilities, stating: "The commission may permit, ***but shall not require***, an electric utility to divest itself of facilities or to reorganize its corporate structure" (emphasis added).

Moreover, even without the express prohibition in Section 2804, the Commission would not have the right to order a utility to sell or close a power plant (or any other facility). One of the fundamental principles of utility regulation in this Commonwealth is that the Commission does not sit as the "super board of directors" over a utility and neither owns nor controls a utility's property. *Northern Pennsylvania Power Co. v. Pa. PUC*, 333 Pa. 265, 267-68, 5 A.2d 133, 134-35 (1939).

In addition, it is beyond question that the Commission only has such authority as has been delegated to it by the General Assembly. *See, e.g., Pa. PUC v. Philadelphia Electric Co.*, 501 Pa. 153, 460 A.2d 734 (1983); *Western Pa. Water Co. v. Pa. PUC*, 10 Pa. Commonwealth Ct. 533, 31 A.2d 370 (1973). The Commission has certain authority regarding the construction, closure, and sale of power plants, but it does not go so far as to allow the Commission to make the decision for the utility. Specifically, the Commission (1) has the power to order the cancellation or modification of construction of a power plant (66 Pa. C.S. § 520), (2) must approve the retirement of a power plant (66 Pa. C.S. § 521), (3) may prohibit a utility from

closing a power plant if the Commission finds that the plant, or its output, could be sold to another utility (66 Pa. C.S. § 525), and (4) must approve the sale of facilities that are in rate base (66 Pa. C.S. § 1102(a)(3)). But there is absolutely no statutory or other legal authority for the Commission to order a utility to shut down or sell a power plant.

Thus, unless Duquesne makes a voluntary commitment, free of any coercion by the Commission, to sell its power plants, then the Commission cannot order or expect those plants to be sold. As Duquesne's President, Mr. Marshall, made clear, Duquesne has not made such a voluntary commitment. Specifically, Mr. Marshall testified as follows:

> We are not recommending to the Commission that we should sell all of our plants today, nor are we recommending we should shut down any plants today. That is not what you've heard us testify to today.
>
> That is one option that the Commission has, but ***that is not our recommendation to the Commission*** ... (Tr. 173 emphasis added)
>
> * * *
>
> So we're saying, ***if the Commission insists*** that that really is what is necessary to make it a valid option, we will ***waive our right***. We're not suggesting that they have to do it. We're not suggesting that they have to do it for 100 percent either.
> ...
>
> Q. You used the phrase in the answer you just gave "waive our right." Waive your right to what?
>
> A. Under the legislation, ***the Commission is not authorized to order people to divest plants, and we don't want that to be held up*** that somehow we're not trying to provide a meaningful market valuation methodology.
>
> So that's why we -- It's in response to the other parties that we're trying to at least offer this option as an additional option to the Commission.
>
> Q. Please understand I'm not asking you for any kind of a legal conclusion. I just want to understand your proposal.
>
> I think you just said that your belief is that under the statute the Commission does not have the authority to order a utility to divest its generation,

but ***you're willing to waive that protection and somehow give the Commission the authority to do that***?

A. ***That is what our testimony says.***

(Tr. 182-183 emphasis added)

Simply, the Company's President made it clear that the Company was ***not*** voluntarily making a commitment to sell its power plants. Rather, it was willing to waive its protection under the law from having the Commission ***order*** it to sell its power plants. However, the Company cannot waive the protection that the law gives to others, including the utility's employees and the communities where those plants are located. See 66 Pa. C.S. § 2802(18). More importantly, the Company cannot give the Commission authority that the Commission does not have under the law.

Moreover, even if it were lawful for the Commission to order the sale or closure of a power plant, the evidence in this case demonstrates that it would not be in the public interest to do so. Neither Duquesne nor any other party that is proposing the sale or closure of these plants has fully evaluated the transmission constraints that would result. Tr. 950-52. The initial review of transmission issues for the Elrama plant by Duquesne witness Karl, however, shows that serious transmission constraints would be created by the unrestricted sale or closure of that plant. Tr. 945. At this time, neither Duquesne nor any other party has a plan for alleviating those serious reliability concerns. Tr. 952. Further, neither Duquesne nor any other party has studied the reliability impacts of closing the Cheswick station or any other Duquesne facility. Tr. 952.

Furthermore, neither Duquesne nor any other party has evaluated the impact of the sale or closure of any facility on Duquesne's employees or on the communities where those plants and employees are located. Indeed, Duquesne's witnesses Marshall and O'Brien made it clear that

no evaluation had been done of the impact of plant closures or sales on local communities (Tr. 175-78, 569) or on the employees who work at those facilities (Tr. 175-78, 570-73, 578-79).

Yet, in order for the Commission to evaluate a restructuring plan, it must consider the impact of the plan on the utility's employees and on the communities that might be affected. 66 Pa. C.S. § 2802(18). As required by the Public Utility Code, 66 Pa. C.S. § 2806(e), and the Commission's filing guidelines, Duquesne's original filing contained an evaluation of its original restructuring plan on its employees and on the local communities. Duquesne Exh. 1, Sch. N-1 to N-4. However, that evaluation does not consider the possibility that any plants would be sold, nor does it consider the possibility that any plants would be closed before 2005. Duquesne Exh. 1, Sch. L-5; Tr. 345-46. Simply, that original evaluation remains valid for a restructuring plan that does not involve the sale or closure of a power plant. But it has no relevance to a revised restructuring plan that would involve the sale or premature closure of a power plant. As IBEW demonstrated above, there is no other evidence in this case that enables the Commission to consider the impact of such a sale or closure on Duquesne's employees or on communities that might be affected.

IBEW's witness Moran accurately summarized this issue, as follows:

> [T]he power plants make a major contribution to the local economy, in terms of jobs, wages, and taxes. ... [I]t's clear to me that they failed to consider the substantial benefits to other area businesses, and the greater Pittsburgh area as a whole, from having these power plants in operation and owned by a local company. They also failed to consider the substantial costs associated with closing or selling those plants.

IBEW St. 1 at 11.

In summary, it is not in the public interest for Duquesne to sell or close any of its power plants. Even if it were a good idea to have Duquesne sell or close its power plants – which it is not – the Commission lacks the authority to order Duquesne to do so. Therefore, any stranded

cost proposals based on the Commission ordering the sale or closure of a power plant must be rejected.

## Conclusion

For the reasons set forth in these Exceptions and in its other pleadings in this proceeding, System Council U-10, International Brotherhood of Electrical Workers respectfully requests the Pennsylvania Public Utility Commission to issue an order that does not require Duquesne Light Company to sell or close any of its power plants.

Respectfully submitted,

Scott J. Rubin
3 Lost Creek Drive
Selinsgrove, PA 17870
(717) 743-2233

Counsel for:
System Council U-10, IBEW

Dated: April 14, 1998

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

| | | |
|---|---|---|
| In the Matter of Duquesne Light Company's Restructuring Plan | : | Docket No. R-00974104 |

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a true copy of the Exceptions of System Council U-10, International Brotherhood of Electrical Workers, via United States Postal Service Priority Mail upon the participants, listed on the following pages, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant).

Scott J. Rubin, Esq.

Counsel for:
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System Council U-10

Dated: April 9, 1998

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COMMONWEALTH OF PENNSYLVANIA
PENNSYLVANIA PUBLIC UTILITY COMMISSION
P.O. BOX 3265, HARRISBURG, PA 17105-3265

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April 9, 1998

Mr. Robert L. Simpson
Executive Director
Crispus Attucks Association, Inc.
605 South Duke Street
York, PA 17403

R-00974104

98 APR 11 PM 12:32
PROTHONOTARY'S OFFICE

Dear Mr. Simpson:

Thank you for your recent letter of April 1, 1998, to Chairman John Quain of the Pennsylvania Public Utility Commission concerning the proposed merger between MCI and WorldCom. Since this matter is currently pending before the Commission, Chairman Quain referred your letter to me for a response.

Although I cannot comment on the merits of this matter, please know that I have taken the liberty of forwarding your letter to the Secretary of the Commission for inclusion in the official file of this proceeding. However, I can tell you the Communications Workers of America (CWA) have filed two protests to the merger proposal. Those protests are at Docket Numbers A-312025 F. 0002 and A-310236 F. 0004. The Administrative Law Judge (ALJ) who is hearing this matter also has before him a pending Motion to Dismiss those protests. If the ALJ denies the Motion, an evidentiary hearing will probably be scheduled for April to hear the protests. If the ALJ grants the Motion, the protests will be dismissed.

Thank you again for your interest in this matter and for providing the Commission with your viewpoints.

Sincerely,

Rosemary Chiavetta, Esq.
Director of Legislative Affairs

cc: Chairman John Quain
Secretary James McNulty

BTL

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CRISPUS ATTUCKS ASSOCIATION, INC. • 605 South Duke Street • York, PA 17403 • (717) 848-3610





April 1, 1998



Honorable John M. Quain, Chairman
Public Utility Commission
P. O. Box 3265
Harrisburg, PA 17105-3265

Dear Chairman Quain:

At the heart of the Telecommunications Act of 1996 is the axiom that there would be more innovation, greater choices of services, and ultimately, lower prices if telecom markets were more competitive and less regulated. As is often the case with such sweeping national policy, results are what one expects and consequences are what one gets. I am very concerned that the proposed $38 billion merger of MCI and WorldCom will deliver not only unintended, but harmful consequences.

In my view, the proposed combination of the second- and fourth-largest long distance companies must receive very close review from our regulatory agency. Two issues are of greatest concern: protecting the robustly competitive environment of the Internet and ensuring that all Americans have affordable access to all telecommunications services.

The Internet is a place where people and businesses--even those with limited financial resources--can participate in the global marketplace. This highly cooperative, yet highly competitive, structure of providers creates opportunities for commerce of all types. The exponential growth in services, information, and in customers is proof of how well this system works. The WorldCom-MCI merger must not damage this system or threaten its vitality. The companies currently are the two largest Internet "backbone" providers. As I understand, the merged company would control more than half of the Internet's "backbone" network as well as the traffic, giving it the incentive and power to set prices, restrict access, and squeeze out competitors. That is not a recipe that would ensure the continued growth of the Internet.

Also, the merger must not damage the affordable access to telecommunications services that all Americans now enjoy. Analysis shows the merger would increase market concentration in long distance and international calling as well as eliminate a significant competitor in the nascent local calling market. Recent statements by MCI and WorldCom also indicate the companies will target their resources solely to high-value corporate customers. There most rigorous assessment on whether these consequences will harm universal service, isolate residential consumers and small businesses, or discourage telecom investment in rural communities.

I believe the structure that the telecom industry eventually takes should be left largely to the market. Government should, to the fullest extent possible, simply stand aside when it comes to mergers. But this does not mean foregoing a complete analysis of all of the competitive implications of such activity. The competitive implications of a entity that could seize control of the Internet and potentially isolate individual consumers and rural communities would be a giant step away from fulfilling the goals of the Telecom Act.

I trust that our regulators' analysis of WorldCom's and MCI's applications will cover these issues to ensure that their proposed merger produces benefits not merely for the two companies, but also for all Americans

Sincerely,

Robert L. Simpson
Executive Director

RLS:jef

COMMONWEALTH OF PENNSYLVANIA
PENNSYLVANIA PUBLIC UTILITY COMMISSION
P.O. BOX 3265, HARRISBURG, PA 17105-3265

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April 9, 1998

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The Honorable Richard A. Kasunic
Democratic Policy Chairman
Senate of Pennsylvania
Senate Post Office - Main Capitol
Harrisburg, PA

R-00974104

Dear Senator Kasunic:

Thank you for your recent letter of April 7, 1998, to Chairman John Quain concerning stranded cost recovery by Allegheny Power which is a matter currently pending before the Public Utility Commission in Allegheny Power's electric restructuring plan filed under the Electric Generation Customer Choice and Competition Act. Chairman Quain referred your letter to me because he is prohibited from commenting on this matter.

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Since this matter is currently pending before the Commission, please know that I have taken the liberty of forwarding your letter to the Secretary of the Commission for inclusion into the official file of the Allegheny Power proceeding. On March 25, 1998, the Office of Administrative Law Judge issued its Recommended Decision in this matter. It will now receive final consideration on April 30, 1998 at the Commission's Public Meeting. Please find enclosed a copy of the Commission's press release summarizing the Recommended Decisions.

Sincerely,

Rosemary Chiavetta, Esq.
Director of Legislative Affairs

Enclosure

cc: Chairman Quain
Vice Chairman Bloom
Commissioner Hanger
Commissioner Rolka
Commissioner Brownell
Secretary James McNulty

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Democratic Policy Chairman

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TRANSPORTATION

JOINT LEGISLATIVE AIR AND WATER POLLUTION CONTROL AND CONSERVATION COMMITTEE
HARDWOODS DEVELOPMENT COUNCIL

Senate of Pennsylvania

April 7, 1998



John M. Quain, Chairman
Public Utility Commission
North Office Building
PO Box 3265
Harrisburg PA 17105



Dear Chairman Quain:

I am writing this letter to express my concerns regarding the restructuring filing of West Penn Power (Allegheny Power). The decision on this filing will have serious economic impact through potential job loss in southwestern Pennsylvania.

Of great concern to me is the ownership of generation facilities. The Electricity Generation Customer Choice and Competition Act does not require the divestiture of generation facilities to recoup stranded costs. The Act does provide for the recovery of stranded costs through a Competitive Transition Charge (CTC).

The purpose of the Act was to provide lower electricity rates through competition. A company's ability to generate electricity at a low cost will result in higher profits for the company. The company can then use those increased profits for its stranded costs in the future. West Penn should be permitted to recover their stranded costs through their already efficient generation facilities.

I want to reiterate my concern for the potential job loss as a result of selling the generation facilities of West Penn Power. As you are aware, southwestern Pennsylvania is in the throes of economic depression. Any job loss as a result of PUC action will be devastating to this corner of the Commonwealth.

Thank you for your consideration with regard to this issue.



Sincerely yours,

Richard A. Kasunic

Richard A. Kasunic
State Senator
32nd District

RAK/mlg

cc: PUC Commissioners
Rosemary Chiavetta

R-00974104



April 10, 1998

Mr. James McNulty, Secretary
Pennsylvania Public Utility Commission
North Office Building, Room B-20
North Street and Commonwealth Avenue
Harrisburg, PA 17105-3265

RE: Application of Duquesne Electric Company for Approval of Its Restructuring Plan Under Section 2806 of the Public Utility Code
Docket No. ~~R-00974008~~

Dear Mr. McNulty:

Enclosed for filing in the above-captioned proceedings are an original and nine (9) copies of the EXCEPTIONS OF Community Action Association of Pennsylvania, Active Intervenor and Complainant, along with a diskette copy in Microsoft Word 6.0 format.

As indicated on the attached Certificate of Service, I have served copies of the enclosed EXCEPTIONS to the Commission's Office of Special Assistants, along with a diskette copy in Microsoft Word 6.0. format, as well as all active parties in the above proceeding.

If you have any questions regarding this filing, please call.

Sincerely,

John Wilson

Enclosures

cc: Certificate of Service



COMMUNITY ACTION ASSOCIATION OF PENNSYLVANIA

*222 Pine Street ♦ Harrisburg, PA 17101*
*(717) 233-1075 ♦ Fax: (717) 232-1014*

BEFORE THE

PENNSYLVANIA PUBLIC UTILITY COMMISSION



| | |
|---|---|
| **APPLICATION OF DUQUESNE LIGHT COMPANY** FOR APPROVAL OF RESTRUCTURING PLAN UNDER SECTION 2806 OF THE PUBLIC UTILITY CODE | **DOCKET NO. R-00974104** |

# EXCEPTIONS OF

# (CAAP)

The Community Action Association of Pennsylvania
222 Pine Street
Harrisburg, Pennsylvania 17101

**ACTIVE INTERVENOR AND COMPLAINANT**



Dated: April 10, 1997
Date Due: April 14, 1997

# EXCEPTIONS TO ALJ RECOMMENDED DECISION REGARDING UNIVERSAL SERVICE AND ENERGY CONSERVATION PROGRAMS

## I. SUMMARY.

In addition to CAAP, the following parties filed statements of prepared testimony and briefs regarding Universal Service and Energy Conservation Programs with numerous supporting exhibits in response to Duquesne Light Company's Restructuring Plan filing: the OTS, the OCA, the OSBA, DII, Enron, and the Environmentalists. In addition to Duquesne, CAAP, OCA, and the Environmentalists specifically addressed the issues of low income need, and what would constitute "appropriately funded and available" universal service and energy conservation programs in Duquesne's service territory. After hearing this testimony and supporting exhibits, and reviewing the briefs, the Administrative Law Judge made the following specific recommendation to which CAAP takes exception:

> **Based upon the evidence presented in this proceeding, the Company's proposed eligibility and funding levels for its universal service and conservation programs appear to comply with the requirements of the Act and the Commission's Guidelines on Universal Service and Energy Conservation; no further modification appears needed at this time.** (ALJ Dec., p. 776).

This recommendation does not square with the Customer Choice Act, the Commission's Tentative and Final Orders on Universal Service and Energy Conservation Program Guidelines, and the facts as presented by the parties in this case. **Specifically, it endorses the Company's universal service and energy conservation plan despite overwhelming evidence establishing actual low income need far greater than the Company's estimations, and after establishing**

**that Duquesne's plan does meet the Customer Choice Act and Final Order requirement that programs be appropriately funded and available in each utility service territory.**

As CAAP pointed out, "low income customers are not likely to share in the benefits of a restructured industry. In fact, they may be substantially harmed by it unless strong and meaningful programs and policies are put into place to protect them." (CAAP M.B., p. 1). With these concerns in mind, **CAAP, OCA, and the Environmentalists provided expert testimony establishing the actual level of need within Duquesne's service territory.** Further, as detailed in the discussion below, **CAAP, OCA, and the Environmentalists provided expert testimony establishing that an "appropriately funded and available" universal service and energy conservation program for Duquesne's service territory would be one that includes: (1) a Low Income Usage Reduction Program (LIURP) that targets between 2,200 and 3,950 annually, with annual funding between $2,200,000 and $4,500,000, and (2) a Customer Assistance Program (CAP) that targets between 13,251 and 24,000 annually, with annual funding between $5,575,000 and $10,500,000.**

Despite the fact that Duquesne acknowledges it has as many as 115,000 payment troubled low income households, is proposes a plan that: (1) essentially continues LIURP services at the historically low, pre-restructuring levels of 700 households annually, at an annual cost of $700,000, and (2) seeks to limit CAP services to a mere 1,600 households annually, at an annual cost of $500,000. Neither of these program participation and funding recommendations are related to the actual level of need with Duquesne's service territory as required by the Customer Choice Act and the Commission's Final Order.

**CAAP urges the Commission to reject the ALJ's recommended decision and require Duquesne to modify its restructuring plan to include annual LIURP and CAP participation and funding levels within the parameters proposed by the active intervenors as presented herein.**

## II. DISCUSSION.

### A. The Policy Background.

Recognizing the importance of electricity in the lives of citizens in general, and the special circumstances that low income individuals and families face in obtaining such, the Governor and General Assembly included no less than three public policy declarations in the Customer Choice Act in this regard:

- Electric service is essential to the health and well-being of residents, to public safety and to orderly economic development, and *electric service should be available to all customers on reasonable terms and conditions* (emphasis added, § 2802(9));

- The Commonwealth *must, at a minimum, continue the protections, policies and services that now assist customers who are low-income to afford electric service* (emphasis added, § 2802(10); and

- There are certain public purpose costs, including programs for low-income assistance, energy conservation and others, which have been implemented and supported by public utilities' bundled rates. *The public purpose is to be promoted by the continuing universal service and energy conservation policies, protections and services,* and full recovery of such costs is to be permitted through a nonbypassable rate mechanism (emphasis added, § 2802(17)).

In support of these public policy requirements, the Customer Choice Act specified certain concrete programs under the general heading of Universal Service and Energy Conservation that

each utility is to develop and implement to fulfill these declarations. Specifically, the Customer Choice Act states that:

- Universal service and energy conservation is defined as policies, protections and services that help low-income customers to maintain electric service. *The term includes customer assistance programs; termination of service protection and policies and services that help low-income customers to reduce or manage energy consumption in a cost-effective manner, such as the low income usage reduction programs, and applicable renewable resources and consumer education* (emphasis added, § 2803).

Further, the Customer Choice Act charged the Commission with ensuring that:

- *Universal service and energy conservation policies, activities and services are appropriately funded and available in each electric distribution territory.* These policies, activities and services shall be funded in each electric distribution territory by non-bypassable competitively neutral cost recovery mechanisms that fully recover the costs of universal service and energy conservation services. (emphasis added, § 2804 (9));

In its Tentative Order and Final Orders, the Commission recognized the pre-eminent role that Low Income Usage Reduction Program (LIURP) and Customer Assistance Program (CAP) must play in each utility universal service and energy conservation program. The Tentative Order suggested two ways of determining what would constitute an "appropriately funded and available" LIURP and CAP. First, after recognizing that participation levels for similar programs in California were nearly 56% and 58% respectively, the Tentative Order suggested that an "appropriately funded and available" LIURP and CAP in Pennsylvania would be one that targets 40% of the income eligible households for each program. Second, the Tentative Order suggested that an "appropriately funded and available" LIURP word be funded at 0.2% of utility revenues and an "appropriately funded and available" CAP would be one funded at 0.5% of utility revenues.

The Final Order explicitly stated that programs should be meaningful and strong, and that participation and funding should be determined through a process that addresses:

- Identification of existing and proposed efforts;
- Needs assessment of the market for and acceptance of universal service programming in the territory;
- Identification of the greater of the current level of spending or the amounts included in existing rates to support existing efforts; and
- Other statutory mandates and these guidelines. (CAAP M.B., p. 6).

Further, the Commission's Final Order is clear in that expenditures for universal service and energy conservation programs must be examined in conjunction with other requirements of the Act, and EDCs are not to determine universal service and energy conservation funding levels after other funding requirements are met. (CAAP St. 2, p. 7)

**B. The Low Income Need.**

The number of households in Duquesne's service territory that are income eligible for universal service and energy conservation program services is between 104,000 and 117,000. (CAAP M.B., p. 8, OCA M.B., p. 42-3). Duquesne provided two estimates of the number of its payment troubled households, 115,000 (DQE Filing Req. R-9) and 55,538 (CAAP M.B., p. 9), and stated that it had 33,802 of them are "delinquent" payment troubled households. (Id.).

**1. LIURP.**

To date, Duquesne has provided LIURP services to approximately 5,328 low income households (CAAP M.B., p. 13). Based solely on income criteria, the LIURP competitions and low income numbers in Duquesne's service territory suggest that Duquesne has

between 98,000[1] and 112,000[2] low income households still in need of LIURP services. Using the Commission's 40% Tentative Order Methodology which attempts to take into consideration non-income criteria, such as minimum usage requirements, these figures suggest that Duquesne has between 39,000[3] and 44,800[4] low income households still in need of LIURP services. CAAP places this number at 39,492. (Id. at 13). The Environmentalists suggest the number is at least 21,226. (ALJ Dec., p. 764). Despite the established level of need with its service territory, Duquesne proposes to limit LIURP services to 700 households annually. In direct testimony, Duquesne testified that Duquesne has no way of estimating the actual level of remaining LIURP need in its service territory (CAAP M.B. at 10), which is a clear admission that its LIURP participation numbers were not established using a needs assessment as required by the Final Order.

**2. CAP.**

Regarding CAP, Duquesne has yet to implement a CAP program. Based solely on income criteria, the low income numbers in Duquesne's service territory suggest that Duquesne has between 104,000[5] and 117,000[6] low income households still in need of LIURP services. Using the Commission's 40% Tentative Order Methodology which attempts to take

---

[1]Equals OCA Census estimate of 117,000 150% of FPG West Penn households, (OCA sSt. 6, p 42-3), less 5,328 completions. (CAAP M.B., p. 13).

[2]Equals CAAP Census estimate of 104,057 150% of FPG West Penn households, (Id. at 10), less 5,328 completions. (Id. at 13).

[3]Equals 98,000 x 40.0%

[4]Equals 112,000 x 40.0%

[5]Equals CAAP Census estimate of 104,057 150% of FPG West Penn households, (CAAP M.B., p. 10).

[6]Equals OCA Census estimate of 117,000 150% of FPG West Penn households, (ALJ Dec., p. 759-60).

into consideration non-income criteria, Duquesne has between 41,000[7] and 47,000[8] CAP eligible households. Considering the Final Order Requirement that CAP participants also be payment troubled, Duquesne has as many as 115,000[9] CAP program eligible households, depending on which of Duquesne's payment troubled numbers are used.

CAAP argues that a reasonable annual CAP target would be 13,521 (CAAP M.B., p. 12), or an amount equal to 11.6% of Duquesne's low income population, 24.3% of its payment troubled population, and 40% of its identified delinquent payment trouble customers. OCA suggests a reasonable annual CAP target would be 24,000. (OCA M.B., p.83). Based on the Environmentalists position that 50% of the eligible CAP populations should be targeted for service (ALJ, Dec., p.766), this number is as high as 57,000.[10] Duquesne limits CAP participation to 1,600 annually (CAAP M.B., p. 9), or an amount equal to 1.3% of its low income population, 2.9% of its payment troubled population, and 4.7% of its delinquent payment troubled population.

**C. Appropriate and Available Programs.**

The Environmentalists concluded that an "appropriately funded and available" budget should be based on the assumption that 50% of the customers who are eligible for each program will participate, and that such a budget would be $17.49 million. (ALJ Dec., p. 766). CAAP and OCA offered recommendations tailored to specific programs.

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[7]Equals 117,000 x 40.0%.
[8]Equals 119,454 x 40.0%
[9]Equals Duquesne estimated of low income payment troubled customers, DQE Filing Req. R-9.
[10]Equals 115,000 x 50%.

**1. LIURP.**

Based on the identified need in Duquesne's service territory, CAAP recommended that an "appropriately funded and available" LIURP program would target 3,949 annually, with an annual budget of $4,500,845. (CAAP M.B., p. 13, 17). OCA recommended that Duquesne ramp up LIURP funding to 0.2% of its gross operating revenues, or approximately $2.2 million, over four years. (OCA M.B., p. 42). Despite these recommendations and the established level of need within its service territory, Duquesne proposes to limit its annual LIURP budget to $700,000. (CAAP M.B., p. 10). In rebuttal, Duquesne suggested that its historic LIURP funding levels are sufficient to meet the low income need in the new competitive environment, but provided no needs assessment to support this conclusion. (Id.).

**2. CAP.**

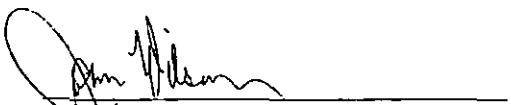
Based on the identified need in Duquesne's service territory, CAAP recommended that an "appropriately funded and available" CAP program would target 13,521 annually, with an annual budget of $10,500,000. (Id. at 12, 18). OCA recommended that Duquesne be required to implement a CAP designed to provide services to 24,000 eligible customers annually by the end of three years, with an annual budget of $5,725,000, an amount equal to approximately 0.5% of gross revenues. (OCA M.B.. p. 83). Despite these recommendations and the established level of need with its service territory, Duquesne proposes to limit its annual CAP budget to $500,000. (CAAP M.B., p. 9). As such, the Company's proposal is severely deficient with respect to the actual needs within its service territory, and contrary to the ALJ's recommended decision, is in violation of the Customer Choice Act and the Commission's Final Order.

C. ***Recommendation.***

CAAP urges the Commission to reject the ALJ's recommended decision and require Duquesne to modify its restructuring plan to include Duquesne's service territory would be one that includes: (1) a Low Income Usage Reduction Program (LIURP) that targets between 2,200 and 4,500 annually, with annual funding between $2,200,000 and $4,500,000, and (2) a Customer Assistance Program (CAP) that targets between 13,251 and 24,000 annually, with annual funding between $5,575,000 and $10,500,000.

**WHEREFORE**, the Community Action Association of Pennsylvania respectfully submits that CAAP's exceptions and recommended modifications to the ALJ's recommended decision in Duquesne's restructuring plan should be accepted and adopted.

Respectfully submitted,



John Wilson
The Community Action Association of Pennsylvania
222 Pine Street
Harrisburg, Pennsylvania 17101

Dated: April 14, 1998

**BEFORE THE**
**PENNSYLVANIA PUBLIC UTILITY COMMISSION**

| | | |
|---|---|---|
| **PENNSYLVANIA PUBLIC UTILITY COMMISSION, et al.** | : | |
| **v.** | : | **DOCKET NO: R-00974104** |
| **DUQUESNE LIGHT COMPANY** | : | |

## CERTIFICATE OF SERVICE

**I hereby certify that I am serving the attached Exception by Priority Mail upon the persons listed on the following pages:**

John Wilson
Community Action Association of Pennsylvania

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April 13, 1998

ORIGINAL



**Via First Class Mail**

James J. McNulty
Secretary
PA Public Utility Commission
P.O. Box 3265
North Office Building
Harrisburg, PA 17105-3265

Re: *Application of Duquesne Light Company for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code, Docket No. R-00974104*

Dear Secretary McNulty:

Enclosed, please find for filing an original and two copies of David Hughes' Brief of Exceptions in the above-referenced matter.

Copies have been served on active parties of record, as indicated in the attached Certificarte of Service.

Thank you for your attention to this matter.

Yours truly,

David Hughes
4037 Ludwick Street
Pittsburgh, PA 15217
(412) 421-4163



Enclosures

99

BEFORE THE PENNSYLVANIA PUBLIC UTILITY COMMISSION

ORIGINAL



| | | |
|---|---|---|
| Application of Duquesne Light Company for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code | } } } | Docket No. R-00974104 |

**BRIEF ON EXCEPTIONS OF DAVID HUGHES**



April 14, 1998

## Introduction

On June 14, 1994, David Hughes, a Duquesne Light Company (Duquesne) ratepayer, filed a Formal Complaint (C-00945953) at the Pennsylvania Public Utility Commission (Commission) claiming that Duquesne's electric rates are unjust and unreasonable. Mr. Hughes based his complaint on the evidence he submitted in his testimony on March 20, 1996 showing that Duquesne's Perry Unit was not used and useful as a result of extended outages. Mr. Hughes asked that he be given relief from paying for an uneconomic investment. On September 19, 1996 the Commission issued a stay in the Complaint proceeding stating that the issues Mr. Hughes raised are more appropriate for hearing during the restructuring proceeding, wherein the Commission would investigate the economics of all of the generating units on the Duquesne system.

Accordingly, Mr. Hughes intervened in this proceeding to present testimony with regard to the used and usefulness of Duquesne units that fail to provide an economic benefit to rate payers. He recommends a refund for unjust and unreasonable rates and a stranded cost sharing/disallowance, based on the Commission's finding in 1988 that the Perry 1 and Beaver Valley 2 (BV2) generating units represent economic excess capacity, and on the 10 year operating performance of the units since then. On March 18, 1998, Administrative Law Judge John H. Corbett, Jr. issued a recommendation to the Commission that Mr. Hughes' complaint and the arguments he raises in the instant proceeding be denied. This document contains Mr. Hughes' Exceptions to the Administrative Law Judge's Recommended Decision.

## Exceptions

I urge the Commission to reject four of Judge Corbett's recommendations:

First, that there be no sharing of the stranded cost burden.

Second, that Mr. Hughes' Formal Complaint and arguments in this proceeding be denied.

Third, that there be no immediate rate reduction, and

Fourth, that Duquesne's proposed mitigation efforts be accepted as submitted.

**Arguments**

VI F (1)(b) Sharing of Stranded Costs

Judge Corbett controverts the intent of the Act by recommending no stranded cost sharing.

In his recommendation (p.432) the presiding officer states: "The record fails to support the assertion of the intervenors that the Company's nuclear units should be considered 'economic excess capacity' if this proceeding were a standard rate case."

Judge Corbett fails to remember that in the last Duquesne rate case (R-870651, March, 1988) the Commission did exactly what the intervenors are seeking in the instant proceeding, i.e. the Commission determined that both the Perry 1 and (BV2) units are economic excess capacity. That was done based on forecasts. As my testimony in this proceeding makes clear, after 10 years of operation of these units, the Commission has been proved correct. These units are uneconomical; they are still economic excess capacity. Indeed, the fact that they represent such a significant part of the Company's stranded cost claim proves this to be the case. It is precisely because these units are uneconomical that the Company's investment in them could not be recovered in a competitive environment. Perry 1 and BV2 are not used and useful. Ratepayers should not be charged for these investments now and they certainly should not be charged for these investments if they choose another power supplier

In addition, Judge Corbett's recommendation that a sharing of stranded costs "can be viewed as a 'taking' of assets, subject to constitutional due process constraints" should also be rejected. Commissioner Hanger's July 3, 1996 statement attached to the Commissions "Investigation into Electric Power Competition" (pp.60-63) presents the legal standards that show that for the Commission to disallow some of the Company's stranded costs would not violate the takings clause of the U.S. Constitution. Specifically, in *Market Street Railway Co. v. Railroad Commission*, the U.S. Supreme Court held that "[t]he due process clause... has not and cannot be applied to insure values or to restore values that have been lost by operation of economic forces."

It is economic forces that have brought about the demand for restructuring of the retail electric industry. If Perry 1 and BV2 were economical, the Company would have no problem recouping its investment.in these assets in a competitive market. Commissioner Hanger goes on to say (p.63):

> Moreover, even if the change from regulated rates to market-based rates could be considered a "taking", the Constitution only protects against takings of property "without just compensation." Every utility has and will continue to receive substantial compensation for its existing investments in a way that cannot reasonably be considered "unjust". Since the utility will continue to be able to charge whatever the market will bear for its generation services, the utility will be fully compensated for future use of the facility. Moreover, the utility has already received both substantial return of and return on uneconomic investments. The utility will continue to receive such compensation that is above market values from those consumers which voluntarily continue to pay regulated rates. Such compensation, plus any CTC recovery permitted, establish that utilities are receiving no less compensation for their investment.
>
> Thus, the foregoing Court decisions suggest that a utility has no constitutional right to any, let alone full recovery of all stranded investment.

Commissioner Hanger is clear: Sharing of the stranded cost burden, or more accurately, disallowing some stranded cost recovery, is not a violation of the takings clause.

The Act gives the Commission the authority to (1) calculate the "appropriate" amount of stranded costs [2802(15)] and (2) determine a "just and reasonable" recovery of that amount [2804(14)]. The Commission has the authority, then, to award anywhere from 0% to 100% recovery of stranded costs. Should the Commission decide to award less than 100% recovery, this would, in effect, be a sharing of the burden. Judge Corbett's position here essentially argues that the Act is unconstitutional.

Judge Corbett goes on to say that "these results [i.e. takings] could not have possibly have been within the contemplation of this legislation", implying, therefore, that a sharing concept is not part of the Act. On the contrary, the concept of sharing of stranded or transition costs is very much a part of the Act. How else could one interpret sections 2802(8) and 2804(14).

> In moving toward greater competition in the electricity generation market, the Commonwealth must resolve certain transitional issues in a manner *that is fair to customers*, electric utilities, investors, the employees of electric utilities, local communities, non utility generators of electricity and other affected parties.2802(8). (emphasis added).

Utilities argue that they were required to make these investments. Even if that were true, the Act recognizes that moving to a competitive market will speed up or condense the payment schedule (return) on these investments, placing a heavy burden on ratepayers. This is like a mortgage lender saying, we are changing your payment schedule from 30 years to 10 years. To ease this new burden, the Act says the implementation plan for dealing with this aspect of restructuring must be "fair to rate payers". That means sharing this burden. Is there another way to guarantee that the intent of the Act in this regard is realized?

There are very persuasive arguments as to why the Company should not recover its investment in Perry 1 and BV2 once competition begins. If we were not heading into retail competition, this Commission would have to adjust this Company's rates. To accept Judge Corbett's recommendation, would be wrong under regulation and it is contrary to the intent of the Act.

Section 2804(14) of the Act says that investors shall have a "fair opportunity to fully recover the amount of transition or stranded costs that the Commission determines to be just and reasonable." Evidence has been submitted (see Schoengold, Environmentalists' St. 1) in this proceeding that shows that there can be a fair sharing of the stranded costs and investors will get a fair return of and on their investment. Other than to make the unsupported claim that proposed stranded cost reductions would "devastate" the Company, Duquesne has not rebutted this evidence. In addition, the Commission must take into consideration the fact that Duquesne ratepayers have paid unfairly high rates for 10 years as a result of the uneconomic investment in Perry 1 and BV2.

Finally, Judge Corbett is wrong to recommend (p.159) acceptance of the Company's demand that there be no sharing of stranded costs if the Company undertakes an auction of its generation assets. An auction, if done right, may be the best way to determine the amount of stranded costs. However, as stated above, the Commission has an additional task, which is to arrive at an "appropriate" amount of stranded costs that is "just and reasonable" for recovery. There is no reason why the Commission should agree to give the Company 100% of its stranded costs simply because the Company agrees to an auction of its generation assets.

The only way for this Commission to fulfill the intent of the Act regarding fairness is to share the costs associated with the transition to an unregulated electric generation market. Judge Corbett's recommendation against sharing stranded costs must be rejected.

VI F 3 Other Arguments Regarding Recovery of Stranded Costs; (c) David Hughes' Position

Judge Corbett claims (p. 453) that "the record amply supports the contentions of the Company that [Mr. Hughes' issues] lack merit." On this basis, he "urges" the Commission to reject the arguments I have presented in this proceeding. Judge Corbett did not support his finding with any reference to the record that he claims exists. I submit that the record does not "amply" support the Company's contentions. In fact, there is no evidence at all in the record to support the Company's contentions because the Company did not submit any evidence to support its contentions. The Company only made its arguments in its main brief, and those arguments had no supporting evidence. Rather, they were inaccurate interpretations of Mr. Biewald's testimony.

There are two matters here. One is my Formal Complaint (C-00945053) and the other is my testimony in the instant proceeding. The Formal Complaint seeks appropriate rate relief as a result of the Perry 1 unit not being used and useful in 1993 and 1994. The arguments in this proceeding have supported my contention that Perry 1 and BV2 are uneconomical and thus have not been used and useful for the duration of their 10 years of operation. The Company never rebutted my testimony in the complaint case.

The only testimony offered by the Company that indirectly relates to my complaint testimony was presented by Mr. Duckworth in this proceeding (Duckworth RT pp.4, 7&8). As I made clear in my surrebuttal (pp.6-8), Mr. Duckworth did not deny my complaint testimony. And he failed to do so in any rejoinder. He simply submitted vague and misleading data to support his claim that the operating performance of the Perry unit was improving. Even if that is true, however, it does not controvert my contention that Perry was not used and useful in 1993 and 1994. There is no basis in the record for Judge Corbett to recommend that my complaint be denied.

In response to the used and useful issues I raised in this proceeding, Duquesne puts forth remarkably weak arguments (p.452) to rebut the testimony of my witness, Mr. Biewald. The

company claims "Mr. Biewald's analysis cannot be relied upon for four reasons": (1) Mr. Biewald did not regard his analysis as "rigorous" and "independent", rather it is "a 'first cut' derived from 'materials at hand, and a number of approximations'.", (2) Mr. Biewald "compared apples to oranges: the sunk costs of Duquesne's nuclear units to the (supposed) incremental cost of purchasing power from the market", (3) "Mr. Biewald's prices for the expected cost of alternatives were 'seriously understated', and (4) "his analysis conflicted with PP&L, where the Commission found it inappropriate to base economic excess capacity adjustment (which is essentially what Mr. Hughes seeks, Hughes St. 1-S) on the estimated cost of 'market purchases'."

With regard to the Company's first argument, the first point to be made is that **the Company did not challenge Mr. Biewald's evidence.** Mr. Biewald's analysis is the only one in the record. The Company may use Mr. Biewald's words to characterize his evidence, but the Company did not refute Mr. Biewald's numbers/evidence. The fact that Mr. Biewald's analysis is a "first cut" does not mean that it is wrong. In fact, the numbers used by Mr. Biewald for this analysis were the Company's own numbers. Mr. Biewald and I stand by these numbers.

The Company's second argument (that Mr. Biewald compares sunk costs to incremental costs) would have merit if Mr. Biewald were doing a prudence analysis; or for planning purposes, attempting to determine whether or not a generating unit should be shut down or not on a going forward basis. In that case, it would be appropriate to leave out sunk or capacity costs from the calculation. However, Mr. Biewald was not doing a "shut down" analysis, rather his testimony is offered in support of my contention that Perry 1 and BV2 fail to meet the useful part of the used and useful standard. In this kind of analysis it is entirely appropriate to compare total costs, i.e. capacity and energy costs to available alternatives. Again, Judge Corbett is in error, the Company never rebutted my evidence. In fact, **the Company did not submit evidence to show that these units are economical**.

The Company's third argument is inaccurate. Duquesne witness Schnitzer (on rejoinder) says that, looking back, actual prices in the mid 1980' were lower than Company projections made at the time, implying that the decision to continue the construction of Perry 1 and BV2 was correct. Mr. Schnitzer claims Mr. Biewald "seriously understated" the "prices for the *expected*

cost of alternatives"(emphasis added). This is inaccurate and irrelevant. Mr. Biewald's evidence did not compare *projected* prices in the mid 1980's to the cost of available alternative capacity. Mr.Biewald compared the *actual* total (capacity & energy) cost of Perry 1 and BV 2 to the *actual* total (capacity and energy) cost of replacement power available at the time in the mid Atlantic region. The analysis clearly shows that both Perry 1 and BV2 are uneconomical or not useful. Again, the Company did not refute Mr. Biewald's actual numbers.

The fourth argument is intertwined with the third. The Company claims that Mr. Biewald's analysis violates PP&L because it is based "on the estimated cost of 'market purchases'." This is simply not true. **When will someone at the Commission understand this fundamental part of my argument?** The part of my request that seeks a refund to customers for unjust and unreasonable current rates, is **not** based on evidence that includes "forecasts" or "projections" of "market prices". The evidence presented on my behalf includes **actual prices** for this region for the period 1987-1997. And compared to the actual prices for the period, Perry 1 and BV2 represent significant losses to ratepayers. Thus, these plants are not useful because they fail to provide an economic benefit to customers. Accordingly, they do not meet the requirements that make them recoverable under traditional rate making and are therefore not recoverable as stranded costs.

VI F 2 (b)(vi) Immediate Rate Reduction

I disagree with Judge Corbett's statement ( p.447) that "the most satisfactory way to achieve rate relief for Duquesne's beleaguered customers is to move as quickly as possible to a fully competitive electric generation market." The best way to get quick relief for Duquesne's "beleaguered" customers is to guarantee a rate reduction at the outset of competition. Any savings a customer can achieve by choosing a cheaper power supplier should come on top of a guaranteed rate cut. Only this combination will bring Duquesne's residential rates closer to the national average price of electricity. Unfortunately, Judge Corbett's position against sharing of the stranded cost burden precludes him from recommending an immediate rate reduction. Sharing the stranded cost burden is the only way to guarantee the promised benefits of competition.

VI F 1(a) Mitigation

Judge Corbett failed to adequately investigate the mitigation efforts presented by Duquesne.

Judge Corbett recommends (p.409) no "adjustment to the mitigation efforts already committed *to be* undertaken by the Company" (emphasis added). The issue here is twofold. First, what is the value of the mitigation efforts the Company has *already* made? And second, what is the basis for the Company's (Duquesne St. 1 at 20; Duquesne St. 2 at 24-26) claims of $1.7 billion in savings from its mitigation efforts. The Company has not supported these claims with detailed evidence.

Judge Corbett has failed to seriously investigate the Company's past mitigation efforts. Section 2808 (C)(5) of the Act states that "The Commission shall consider efforts undertaken over time, *prior to the enactment of this chapter*, to reduce or moderate rate levels..." (emphasis added). Apparently the Company's unsupported claim that it counts $700 million in "avoided rate increases" as mitigation is intended to meet the requirements of this section of the Act. As the testimony and evidence has shown, the Company has made paltry efforts to mitigate the impact of its uneconomic ventures. In fact, the evidence shows that the Company could have mitigated all of its stranded costs by now (see David Hughes' Statement 2). The Company has not rebutted this evidence.

**Summation**

The Commission may be tempted to dismiss my Formal Complaint and arguments in this proceeding, because to do otherwise would require the Commission to make a controversial decisionin this proceeding. However, the evidence I have presented proves that Duquesne ratepayers have unfairly, and for too long, borne the burden of unjust and unreasonable rates. This is the result of Duquesne's decision to make investments that have proven to be uneconomic and the Company's failure to mitigate these costs to the extent possible. Therefore, it is only right, that before we go to a competitive market, current rates be adjusted. That will insure that customers who choose to remain with Duquense as their power supplier, will pay rates that are just and reasonable during the transition. Accordingly, the Commission should "bite the bullet" and reject Judge Corbett's recommendation to deny my formal complaint and the arguments presented in this restructuring proceeding.

## CERTIFICATE OF SERVICE

I hereby certify that I have this day served a true copy of the foregoing document via Federal Express, facsimile or first class mail, postage pre-paid upon the participants, listed below, in accordance with the requirements of 52 Pa. Code § 1.54.

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PA PUBLIC UTILITY COMMISSION
PROTHONOTARY'S OFFICE

**Via Federal Express**
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Prothonotary
Pennsylvania Public Utility Commission
North Office Building, Room B-20
Harrisburg, Pennsylvania 17101

*Re: Application of Duquesne Light Company*
*for Approval of Restructuring Plan*
*Docket No. R-00974104*
*Brief on Exceptions to Recommended Decision*

Dear Mr. McNulty:

Pursuant to Section 5.533 of the Pennsylvania Public Utility Code, enclosed please accept for filing an original and nine (9) copies of Hospital Shared Services ("HSS") and Administrative Resources, Inc. ("ARI") to the Exceptions to the Recommended Decision of Administrative Law Judge John H. Corbett, Jr. in the above-captioned proceeding.

Also, please find an additional copy of the cover of HSS/ARI's Exceptions to the Recommended Decision to be stamped and returned to me in the enclosed self-addressed postage prepaid envelope.

Very truly yours,

DOCUMENT FOLDER

Robert M. Lamkin
Attorney for Hospital Shared Services
and Administrative Resources, Inc.

Enclosures

cc: All Parties
Commission's Office of Special Assistants (hard copy and computer diskette version)

WAS01:50384.1

ORIGINAL

**BEFORE THE**
**PENNSYLVANIA PUBLIC UTILITY COMMISSION**

| | | |
|---|---|---|
| **Application of Duquesne Light Company** | ) | |
| **for Approval of Its Restructuring Plan** | ) | **Docket Nos. R-00974104 and** |
| ***Under Section 2806 of the Public Utility Code*** | ) | **R-00974104C0001-C0004** |

**EXCEPTIONS OF *HOSPITAL SHARED SERVICES***
**AND ADMINISTRATIVE RESOURCES, INC.**
**TO THE RECOMMENDED DECISION OF**
**ADMINISTRATIVE LAW JUDGE JOHN H. CORBETT, JR.**



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**ADMINISTRATIVE RESOURCES, INC.**



**April 14, 1998**

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| **for Approval of Its Restructuring Plan** | ) | **Docket Nos. R-00974104 and** |
| **Under Section 2806 of the Public Utility Code** | ) | **R-00974104C0001-C0004** |

**EXCEPTIONS OF HOSPITAL SHARED SERVICES AND ADMINISTRATIVE RESOURCES, INC. TO THE RECOMMENDED DECISION OF ADMINISTRATIVE LAW JUDGE JOHN H. CORBETT, JR.**

Pursuant to Rule 5.533 of the Rules of the Pennsylvania Public Utility Commission ("Commission"), 66 Pa. C.S. § 5.533 (1997), Hospital Shared Services ("HSS") and Administrative Resources, Inc. ("ARI") hereby file exceptions to the Recommended Decision ("R.D.") of presiding Administrative Law Judge ("ALJ") John H. Corbett, Jr. issued by the Office of the Administrative Law Judge on March 18, 1998.

## I. INTRODUCTION

### A. Background

Duquesne Light Company ("Duquesne" or the "Company") initiated this proceeding on August 1, 1997 by filing its restructuring plan to implement direct access to a competitive market for the generation of electricity in accordance with Section 2806(d) of the Electric Generation, Customer Choice and Competition Act (the "Customer Choice Act"). 66 Pa. C.S. §§ 2801-13 (1997). HSS/ARI principally have focused on the stranded cost element of Duquesne's filing, an element that has proven to be a moving target. HSS/ARI Main Brief ("M.B.") at 2-3 and 18-20. Evidence of the changing nature of Duquesne's position on stranded cost issues is presented by Duquesne's belated offer, first put forth in its rejoinder testimony, to auction its generation facilities

immediately. R.D. at 101. In view of that offer, the ALJ, among other things, recommended that the Commission accept Duquesne's divestiture proposal as the most valid method of establishing the value of Duquesne's generation assets and the stranded costs, if any, associated with those assets. R.D. at 159.

HSS/ARI support that recommendation. *See* HSS/ARI St. No. 1 at 141-49. However, Duquesne's offer to sell its generation assets is not unqualified. Duquesne offers to divest its generation assets only if its proposed merger with Allegheny Power Systems ("APS") is not consummated. R.D. at 102. Thus, as an alternative, in the event that the merger with APS *is* consummated, or that the Commission requires a final administratively determined valuation of Duquesne's assets, the Recommended Decision sets forth numerous recommendations that would serve as the basis to derive an administrative determination of stranded costs. R.D. at 160. Certain of those recommendations affect the level of ratepayers' stranded cost liabilities whether determined through a market valuation or an administrative determination. HSS/ARI submit that those recommendations contain significant errors that result in Duquesne being permitted to recover as stranded costs significant amounts that do not qualify as such.

### B. Summary of Major Errors In The Recommended Decision

A simple formulation of stranded costs can be expressed as follows: stranded costs represent, on a net present value basis, the difference between (a) a utility's projected revenue stream and (b) the combination of its prudently incurred embedded costs and its reasonably projected going-forward costs that are required to keep its generation plants in operation. The Recommended Decision contains three critical errors -- two on the cost side and one on the revenue side of that equation.

Those errors, if not corrected, will result in the imposition of hundreds of millions of dollars in stranded cost liabilities on ratepayers in excess of Duquesne's legitimate stranded costs.

1. The first of those errors relates to Duquesne's projected capital additions. HSS/ARI submitted into evidence the relevant data from each of Duquesne's "Corporate Budget Variance Reports" for the years 1987 through 1996. Those data provide a comparison of Duquesne's budget forecasts for each year with Duquesne's actual expenditures. The data show that Duquesne's budget forecasts just twelve months ahead for generation-related capital additions exceeded actual expenditures on average by 17% during that ten-year time period. Duquesne never challenged the accuracy of the information submitted by HSS/ARI, nor could it given that the variance reports are Duquesne's own internal records. The data submitted by HSS/ARI are exactly the type of data that the Commission relied upon in the *PECO Energy* proceeding as the basis to adjust downward PECO's forecast of future capital expenditures. *Application of PECO Energy Company for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code*, 181 P.U.R.4th 517 (Pa. PUC Dec. 23, 1997) (hereinafter "*PECO Order*") *mimeo* at 82. Notwithstanding that fact and the absence of any Duquesne challenge to the accuracy of the data, the Recommended Decision rejected HSS/ARI's recommendation to adjust downward Duquesne's projected capital expenditures. This is a critical error that inappropriately increases ratepayers' liabilities for stranded costs by assuming Duquesne will spend approximately $352 million for generation-related capital additions through December 31, 2005, notwithstanding Duquesne's ten-year history of over-budgeting which demonstrates that approximately $70 million of that amount represents an excessive forecasted amount that Duquesne likely will not spend. This error impacts the stranded cost quantification only in the event of an administrative determination.

2. The second error on the cost side of the stranded cost equation relates to past capital expenditures. Duquesne has not filed a rate case since 1986, and HSS/ARI introduced evidence that showed that Duquesne's decision not to file a rate case was part of a purposeful corporate strategy, presumably to maximize its profitability. *E.g.*, HSS/ARI M.B. at 10. As a result of not filing a rate case during a ten-year period, Duquesne had an affirmative obligation in this case to prove the reasonableness of its capital expenditures during that time. As the Commission has held:

> [t]here is no presumption of reasonableness which attaches to a utility's claims, at least none which survives the raising of credible issues regarding a utility's claims. A utility's burden is to affirmatively establish the reasonableness of its claim. It is not the burden of the other party to disprove the reasonableness of the utility's claims.

*Pennsylvania Public Util. Comm'n v. Equitable Gas Co.*, 57 Pa. PUC 423, 444 n.37, 54 P.U.R.4th 406 (1983). That ruling is consistent with the Pennsylvania Supreme Court's ruling that "appellants do not have the burden of proving that plant additions were improper, unnecessary or too costly, on the contrary, that burden is, by statute, on the utility to demonstrate the reasonable necessity and cost of the installations . . . ." *Berner v. Pennsylvania Public Util. Comm'n*, 382 Pa. 622, 631, 116 A.2d 738, 744, (Pa. 1955), *relied upon* by the Commission in *Pennsylvania Public Util. Comm'n v. Fawn Lake Forest Water Co.*, 1992 Pa. P.U.C. *LEXIS* 100 at p* 17 (1992).

Based upon Duquesne's failure even to attempt to establish the reasonableness of its past capital expenditures as is required by *Berner, Equitable* and *Fawn Lake*, HSS/ARI conservatively recommended a partial disallowance providing Duquesne the benefit of the doubt that some it its past expenditures were reasonable. However, the ALJ rejected HSS/ARI's recommended disallowance by inappropriately shifting the burden of proof to HSS/ARI to establish a *prima facie*

case that Duquesne's past capital expenditures were *unreasonable*. As he stated: "HSS/ARI fail to identify even a single expenditure as *unreasonable*." R.D. at 176 (emphasis added). Therefore, the Recommended Decision commits a second critical error in imposing upon ratepayers a requirement to pay Duquesne for capital expenditures that never have been shown to be reasonable. This error impacts the level of stranded costs to be determined whether a market valuation or administrative determination of stranded costs is made. It also has a direct impact on Duquesne's unbundled generation and distribution rates that will go into effect January 1, 1999.

3. The third of the critical errors, *i.e.*, the error on the revenue side, arises from the Recommended Decision's determination to select the projected market prices proposed by the Office of Consumer Advocate ("OCA") to determine Duquesne's projected revenues and the value of Duquesne's facilities. Clearly this was done out of some sense of need for consistency with *PECO*. However, this is not the *PECO* proceeding, and as OCA itself stated in its Reply Brief to the ALJ, recognition should be accorded to the evidence of actual market transactions that is in the record in this proceeding. OCA Reply Brief at 10. That evidence shows that generation plants around the country are being sold in excess of utilities' net investments in their existing plants. The one market price projection in this case that best captures that dynamic was sponsored by HSS/ARI, and it happens to be a price projection that HSS/ARI obtained directly from Duquesne itself. It is a market price projection that was performed for Duquesne in November 1996, *i.e.*, just ten months before Duquesne filed its application in this case. It was provided to Duquesne by CS First Boston, Duquesne's financial advisor in its proposed merger with APS. The conclusions to be reached from that price projection also are consistent with the conclusions of other Duquesne internal studies and studies performed for Duquesne by a different consultant -- Metzler and Associates. The CS First

Boston market price projection shows that Duquesne's generation assets have positive market value, *i.e.*, value exceeding Duquesne's net book investment resulting in no stranded costs, a conclusion that is consistent with the evidence of the real market transactions represented by sales around the country of utilities' existing generation facilities. In contrast, OCA's market price projections are inconsistent with those real world transactions -- resulting in stranded cost calculations well in excess of a billion dollars. There is no reason why the Commission should adopt OCA's market price projections that are inconsistent with the evidence in the record of actual market transactions and that improperly impose the risk of a misforecast on Duquesne's ratepayers.

HSS/ARI lodge these, and certain other, exceptions to the Recommended Decision as will be discussed more fully below.

## II. EXCEPTIONS

### A. Issues Concerning Market Value/Stranded Costs Associated With Duquesne's Generation Plants

**Exception No. 1: The ALJ Applied the Incorrect Burden of Proof and Impermissibly Shifted the Burden of Proof to Intervenors with Respect to a Number of Expenditures.**

Duquesne is seeking in this case authority to recover certain past capital expenditures that never have been subject to review by the Commission as part of Duquesne's rates. They never have been subject to review because Duquesne has not filed a rate case since 1986. HSS/ARI St. No. 1 at 54. Further, Duquesne's failure to file a rate case during that time appears to have been part of a purposeful corporate strategy. Exh. RBW-28, p. 0059146. Moreover, specifically because Duquesne has chosen not to file a rate case since 1986, the capital expenditures at issue are of a magnitude significantly higher than would typically be expected.

In HSS/ARI's Direct Testimony, HSS/ARI put Duquesne on notice that HSS/ARI challenged the reasonableness of past capital expenditures. HSS/ARI St. No. 1 at 54-57. HSS/ARI referred Duquesne to the costs HSS/ARI were challenging by reference on a year by year basis to their inclusion in Duquesne's FERC Form 1 reports. HSS/ARI St. No. 1 at 56. As HSS/ARI stated in that testimony, the Commission should not assume the reasonableness of Duquesne's past capital expenditures that had not been subject to review. *Id.* at 57.

Notwithstanding HSS/ARI's challenge, Duquesne produced no evidence to support its past capital expenditures for which it currently is seeking recovery. In fact, Duquesne did not even describe what capital additions it installed since its last rate case, let alone attempt to justify as reasonable its expenditures associated with those additions. Nonetheless, the Recommended Decision approved the Company's recovery of those expenditures, finding that HSS/ARI had failed to overcome an alleged "presumption of reasonableness" with respect to Duquesne's expenditures. R.D. at 57. As set forth below, the ALJ erred because he accorded to Duquesne's expenditures a presumption of reasonableness which conflicts with the law in this jurisdiction, and he inappropriately shifted the burden of proof to HSS/ARI by requiring HSS/ARI to prove the unreasonableness of Duquesne's expenditures.

Pursuant to Section 1301 of the Public Utility Code (the "Code"), the Commission has a statutory mandate to ensure that every rate charged by a utility is found to be just and reasonable. 66 Pa. C.S. § 1301; *Pennsylvania Power Co. v. Pennsylvania Public Util. Comm'n*, 155 Pa. Commw. Ct. 477, 625 A.2d 719, 723 (Pa. Commw. 1993). Section 315(a) of the Code squarely

places the burden of proof[1] with respect to the justness and reasonableness of its rates on the utility which must establish by a preponderance of the evidence that the rates it proposes to charge are just and reasonable. 66 Pa. C.S. § 315(a); *Lower Frederick Township Water Co. v. Pennsylvania Public Util. Comm'n,* 48 Pa. Commw. Ct. 222, 226-27, 409 A.2d 505, 507 (Pa. Commw. 1980). Consistent with Section 315(a), the Commission has ruled that "[i]f and when [a utility] seeks recognition of [capital expenditures], it will then be required to support the prudence of those expenditures." *Pennsylvania Pub. Util. Comm'n v. Philadelphia Electric Co.*, 1990 Pa. P.U.C. LEXIS 155 at p* 54-57 (1990). Further, it is well-established that when an intervenor challenges a rate increase or expenditure, the burden of proof never shifts to the intervenor, but remains at all times with the utility:

> While the burden of going forward may shift, the burden of proof remains on the utility, and this burden of establishing the justness and reasonableness of every component of its rate request is an affirmative one. In contrast, there is no similar burden placed on an intervenor to justify a proposed disallowance.

*Fawn Lake*, 1992 Pa. P.U.C. LEXIS 100 at p* 16-17. Thus, a party challenging a utility's claimed expenditures need establish only the existence of a credible issue regarding the utility's claim to require the utility to affirmatively establish that its claims are just and reasonable.

Moreover, the Pennsylvania courts have made clear that the burden on an intervenor challenging a utility's proposed claims is merely to establish the existence of credible issue. As the Pennsylvania Commonwealth Court has noted, an intervenor challenging a company's claim which is supported only by the utility's bare assertion "was under no obligation to adduce either evidence

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[1] Burden of proof in this context means the duty to establish a fact by a preponderance of the evidence. *Se-Ling Hosiery, Inc. v. Margulies*, 364 Pa. 45, 70 A.2d 854 (Pa. 1950).

or analysis." *University of Pennsylvania v. Pennsylvania Public Util. Comm'n*, 86 Pa. Commw. Ct. 486, 485 A.2d 1228 (Pa. Commw. 1984) (cited with approval in *Fawn Lake*, 1992 Pa. P.U.C. LEXIS 100 at p*17 n.1. The same standard, in fact, has been approved by the Pennsylvania Supreme Court:

> [T]he appellants did not have the burden of proving that the plant additions were improper, unnecessary or too costly; on the contrary, that burden is, by statute, on the utility to demonstrate the reasonable necessity and cost of the installations . . . .

*Berner v. Pennsylvania Public Util. Comm'n*, 382 Pa. 622, 631, 116 A.2d 738, 755 (Pa. 1955).

In ruling on stranded cost issues, and issues related to unbundled generation and distribution rates,[2] the ALJ erred with respect to HSS/ARI's burden in this proceeding. His ruling on burden of proof is in direct conflict with the cases cited above. This error is epitomized in a single sentence in the Recommended Decision, which states; "HSS/ARI fail to identify even a single expenditure as *unreasonable*." R.D. at 176 (emphasis added). Moreover, his error is compounded by his ruling that:

> The HSS/ARI stood the process of traditional ratemaking on its head. According to HSS/ARI, any public utility seeking an adjustment of its rates must prove the reasonableness of each and every claim in its application, even though no party challenged any single item, or risk denial of its request.

R.D. at 176.

HSS/ARI submit that it is the Recommended Decision that stands traditional ratemaking, as well as the traditional reasons for regulating public utilities, on a head. The Recommended Decision would allow a utility, in this instance, Duquesne, to profit by shielding its capital expenditures from scrutiny for ten years, and then getting a "free pass," without explanation, to flow through hundreds

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[2] The ALJ's error in improperly shifting the burden of proof also impacts his determination concerning Duquesne's unbundled generation and distribution rates. *See* Exception 10 *infra*.

of millions of dollars to ratepayers, by placing the burden upon ratepayers to raise with specificity line item challenges to a decade of expenditures for which the utility provided no line item explanations. Such a ruling would disregard the realities that (1) utilities -- not ratepayers -- possess the information about the utilities' expenditures, (2) it is the Commission's mandate to protect ratepayers, and (3) it is not the Commission's duty to ensure a utility's recovery of expenditures absent proof that the expenditures were reasonable. Further, the ALJ's ruling is in direct conflict with the cases cited above, and the Commission's express ruling that "[i]f and when [a utility] seeks recognition of [capital expenditures], it will then be required to support the prudence of those expenditures." *Philadelphia Electric Co.*, 1990 Pa. P.U.C. LEXIS 155 at p*54-57.

Thus, as the case law makes clear, HSS/ARI did not bear the burden of showing that Duquesne's expenditures were unreasonable; rather, Duquesne had the burden of establishing that its expenditures were reasonable. The Recommended Decision thus committed errors in a number of instances by improperly shifting the burden of proof to HSS/ARI. Accordingly, the Recommended Decision must be reversed as is set forth in Exception Nos. 2, 3 and 12 to correct the ALJ's improper shifting of the burden of proof.

**Exception No. 2: Projected Levels of Generation-Related Capital Additions and O&M Expenses (Section VI.B.3.(e) (R.D. at 299-302)).**

**The Recommended Decision Errs By Allowing Duquesne to Base Its Stranded Cost Claims On Projected Costs Far In Excess of Reasonable Amounts.**

As part of its stranded costs claim, Duquesne projected that from 1997 through 2005 it will need to install generation-related capital additions at an expense of $352 million. Exh. DJC-3 at 25. Duquesne also forecast capital additions, in some instances, out to the year 2026 to coincide with

the book retirement dates of its plants. HSS/ARI M.B. at 60; HSS/ARI St. 1 at 57: 21-22. As part of its stranded cost claim, Duquesne also projected O&M expenses, again out to the book retirement date of each plant. *See* Exh. DJC-20. HSS/ARI's Direct Testimony challenged those projections and presented evidence to show why Duquesne's projections should be reduced. HSS/ARI St. 1 at 62-64.

In his Recommended Decision, the ALJ rejected HSS/ARI' position with respect to Duquesne's projected capital additions and O&M expenses. He ruled that rejection was warranted because "insufficient evidence exists in the record to substantiate the proposals of HSS/ARI." R.D. at 302. The ALJ's recommendation is clear error.

First, with respect to Duquesne's projections of capital additions, HSS/ARI produced Duquesne's own "Corporate Budget Variance Reports" which indicate that on average, from 1987 through 1996, Duquesne's actual generation-related capital expenditures were 17% lower than its projected expenditures for the next twelve months. HSS/ARI St. No. 1 at 60; Exh. RBW-21. Thus, the data submitted by HSS/ARI with respect to Duquesne's projected capital expenditures, *i.e.*, data showing a history of over-budgeting, are exactly the type of data the Commission relied upon in *PECO* to order a disallowance. In that case, the Commission ruled:

> Mr. Smith also documents a PECO history of overbudgeting capital expenditures by at least a 5% average amount over the last 10 years. Since the capital expenditures at issue are future expenditures based on budgeting projections, we accept the recommendation of the budgeted capital additions to reflect a more reasonable likely expenditure based on PECO's past history of overbudgeting future capital improvements.

*PECO* Order at 82.

Given that the Corporate Budget Variance Reports submitted here are Duquesne's own records, and Duquesne never challenged HSS/ARI's statements concerning those data, it is implausible that the Commission could determine, in view of its ruling in *PECO*, that the evidence here is insufficient. Accordingly, consistent with the ruling in *PECO*, HSS/ARI submit that Duquesne's forecasted capital additions should be reduced by 20% to reflect its past, documented history of overbudgeting.[3]

The Commission also should reduce Duquesne's forecast of O&M expenses. With respect to those expenses, HSS/ARI showed that Duquesne's production and operation expenses fall short of industry standards in numerous categories and that Duquesne's forecast of O&M expenses is inconsistent with its corporate strategy to reduce costs. HSS/ARI St. No. 1 at 62-64.

HSS/ARI showed that Duquesne's total energy costs were 15% higher than the ECAR average for 1995. Exh. RBW-23 at 6. Its fixed production costs were 40% higher than the ECAR average. *Id.* Its total production costs were 20% above the ECAR average. *Id.* Further, HSS/ARI pointed out that Duquesne claims it is attempting to cut costs to become more competitive. HSS/ARI St. No. 1 at 63. In addition, in a study performed on behalf of Duquesne, its consultants recommended a 45% reduction in plant operations personnel. *Id.* Nonetheless, the Recommended Decision accepts Duquesne's forecast of O&M expenses, a forecast that demonstrates nothing other than a "business as usual" approach to future expenses.

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[3] HSS/ARI note that their recommended 20% reduction is intended to reflect that Duquesne forecasts just 12 months into the future on average are 17% too high. The recommendation for a 20% reduction is intended to capture, conservatively, the likelihood of the greater error that would occur over a longer forecast period.

HSS/ARI submit that Duquesne should be taken at its word, *i.e.*, that it is attempting to streamline its operations to compete in the new competitive environment. Accordingly, HSS/ARI recommended that Duquesne's O&M expense projections be reduced by 15%. HSS/ARI St. No. 1 at 64; HSS/ARI M.B. at 62.

**Exception No. 3:** **Generation-Related Stranded Costs - Net Book Value (Section VI.B.2. (R.D. at 160-75)) and Immediate Rate Reduction (Section VI.F.3(b) (R.D. at 409-32)).**

**The Recommended Decision Errs By Recommending That Duquesne Be Permitted To Include In Net Book Value For Purposes of Calculating Stranded Costs, Expenditures That Duquesne Has Not Shown Are Just and Reasonable; The Recommended Decision Further Errs By Failing To Order An Immediate Rate Reduction To Reflect A Disallowance of Such Expenditures.**

HSS/ARI's Direct Testimony shows that, according to Duquesne's FERC Form 1 reports, between 1987 and 1996, Duquesne made generation-related capital expenditures of approximately $382 million. HSS/ARI St. 1 at 55-56. HSS/ARI objected to Duquesne's proposal to include the entirety of those expenditures in its calculation of net book value because none of those expenditures ever had been reviewed by the Commission, nor had Duquesne, as required, presented any evidence in this case even to attempt to show that those expenditures were reasonable. HSS/ARI M.B. at 24-25. For the same reasons, HSS/ARI objected to Duquesne's request to include the entirety of those expenses in its 1996 cost of service for purposes of determining an unbundled generation rate. *Id.* at 81. Notwithstanding the precedent discussed above that would authorize the Commission to disallow the entirety of Duquesne's expenditures, HSS/ARI recommended that the Commission give Duquesne the benefit of the doubt as to the reasonableness of some of those expenditures. HSS/ARI recommended that, to balance ratepayer and shareholder interests, the Commission disallow 50%

of Duquesne's past expenditures that Duquesne never had shown to be just and reasonable. HSS/ARI St. No. 1 at 55-56.

In the Recommended Decision, the ALJ ruled that HSS/ARI allegedly had failed to introduce a credible issue with respect to the expenditures included in 1996 Test Year cost of service. R.D. at 176. He concluded that HSS/ARI had failed to "identify even a single expenditure as unreasonable," thus improperly shifting the burden of proof to HSS/ARI as discussed above. *See* R.D. at 176. But, again, the Commission has stated emphatically that "[a]n intervenor challenging a company claim supported only by the utility's bare assertion 'was under no obligation to adduce either evidence or analysis.' " *Fawn Lake*, 1992 Pa. PUC LEXIS at p* 17 n.1 quoting *University of Pennsylvania v. Pennsylvania Public Util. Comm'n*, 485 A.2d 1228. Accordingly, the ALJ's Recommended Decision misread the law with respect to the burden on HSS/ARI in challenging the Company's expenditures.

Moreover, the Recommended Decision failed to consider, much less address, evidence in the record which HSS/ARI introduced, and which squarely raised the issue of the reasonableness of the Company's past capital expenditures. For instance, HSS/ARI witness Weisenmiller challenged the reasonableness of Duquesne's expenditures based, in part, on the fact that Duquesne's own potential merger partner recently had found reasons to question Duquesne's expenditures. HSS/ARI St. 1 at 56:23 to 57:15. As Dr. Weisenmiller showed, in a 1996 proceeding before the Commission, a witness sponsored by West Penn testified, referring to Duquesne's costs, "Duquesne is either extremely inefficient or is over-recovering. Because electric service is still bundled, it is difficult to tell if Duquesne's rate is reasonable for any single component of electric service." Exh. RBW-20. Based on that evidence, and noting Duquesne's failure to subject its expenditures since 1986 to

scrutiny, HSS/ARI put Duquesne on notice (*see* R.D. at 833) that the reasonableness of its claimed expenditures were at issue and that it needed to establish that such expenditures were just and reasonable.

Thus, HSS/ARI satisfied their burden of raising a credible issue with respect to the reasonableness of the Company's past expenditures, *i.e.*, it is credible to contend that Duquesne should not be permitted to pass through a decade of capital expenditures, totaling hundreds of millions of dollars, absent at least a minimal showing that the expenditures were just and reasonable. Accordingly, the ALJ's Recommended Decision impermissibly raises the bar for ratepayers. The Recommended Decision therefore should be reversed with respect to this issue.

HSS/ARI submit that, to balance ratepayers and shareholders interests, it would be appropriate, as recommended in HSS/ARI's Main Brief, to disallow 50% of the $382 million in generation-related capital expenditures that Duquesne made between 1986 and the present and to order a concomitant rate reduction. HSS/ARI M.B. at 24-25 and 81. However, HSS/ARI further submit that if the Commission believes that a 50% disallowance is excessive, then the Commission can in its discretion, provide for a lesser disallowance. But, in no event should Duquesne be permitted, with impunity, to shield almost $400 million in expenditures from scrutiny over a ten-year period and then get a "free pass" to foist the entirety of those costs on ratepayers without any proof that the expenditures were reasonable. Failure to grant substantial, meaningful relief with respect to this issue would be error.

**Exception No. 4: Phillips & Brunot Island (Section IV.B.2(c) (R.D. at 168-76)).**

**The Recommended Decision Errs By Including In Duquesne's Net Book Value a Portion of Duquesne's Remaining Net Book Investment In the Cold-Reserved Phillips and Brunot Island Facilities.**

In the Recommended Decision, the ALJ correctly rules that the net book value of Units 1, 2, 3, and 4 of the Phillips Power Station and Units 3 and 4 at the Brunot Island Power Station should be disallowed. R.D. at 175-76. However, the Recommended Decision disallows only $65.58 million associated with those plants. *Id.* The disallowance inadvertently allows Duquesne to recover portions of its book investment in the cold-reserved units.

It is undisputed that Duquesne's net book investment in the cold-reserved units is $106.8 million. Duquesne St. No. 4 at 12-14; *see also* R.D. at 168 n.58. The Recommended Decision apparently reduces that amount to $65.58 million to reflect $40 million in deferred taxes associated with the plants. *Id.* That reduction is unwarranted.

Duquesne's general claim associated with deferred taxes is that ratepayers received the benefit of deferred taxes and, therefore, should not avoid liability for Duquesne's higher tax bill in the future when the "tax benefits" turn around. Duquesne St. 4 at 8:14-9:1. If that argument holds water at all, it does not in the case of the cold-reserved Phillips and Brunot Island units. That is because those units were taken out of rate base in 1986. Therefore, it cannot seriously be disputed that any "tax benefit" associated with the plants since 1986 flowed to Duquesne's shareholders, not its ratepayers. Accordingly, the Recommended Decision should be modified to provide for the disallowance of the full $106.8 million in Duquesne's net book investment in the cold-reserved units.

**Exception No. 5: The ALJ Erred in Accepting the OCA's Estimate of the Market Value of Duquesne's Generating Assets (Section VI.B.2 (R.D. at 251-272)).**

HSS/ARI's Direct Testimony in this proceeding advocated a market valuation approach to provide the best determination of the real market value of Duquesne's assets. HSS/ARI St. No. 1 at 141:10 - 149:4. The ALJ agreed with that approach as is evidenced by his recommendation that the Commission allow an asset divestiture to determine the value of Duquesne's generating facilities. However, as previously indicated, Duquesne has offered to sell its generation assets only in the event that its proposed merger with APS is not consummated. R.D. at 159. Accordingly, there is a real possibility that the preferred valuation method recommended by the ALJ will not be used and that the value of Duquesne's generating assets will be determined administratively.

To account for that contingency, in his Recommended Decision, the ALJ found that, if the proposed Duquesne/APS merger is not consummated, or if the Commission decides that a final administratively-determined methodology for valuation of stranded costs must be found in this proceeding, the Commission should adopt the market value of the Company's generating facilities as determined by the OCA based upon its market price projections performed with the ENPRO model. R.D. at 272-73. HSS/ARI except to that recommendation because the OCA market valuation is inconsistent with the real world evidence in this case, and the OCA stranded cost determination that results from its approach burdens ratepayers with hundreds of millions of dollars in stranded costs that are excessive when evaluated in the context of real market transactions.

The most basic problem with the OCA market price projection is, in fact, that the conclusions to be reached using those market price projections are inconsistent with the evidence in this record of actual market transactions. The evidence shows that existing utility plants around the country are

selling at multiples of net book value, whereas OCA's market price projections conclude that Duquesne's facilities will result in stranded costs. *See, e.g.*, HSS/ARI M.B. at 52-56. Therefore, if the Commission makes an administrative determination of stranded costs, it should base that determination on real market evidence. The record is replete with that evidence, and those real market transactions show that OCA's market valuation does not reflect real world experience.

For example, the evidence shows that in 1995, Duquesne, itself, sold its 50% interest in its Ft. Martin plant to APS at 4.5 times net book value. HSS/ARI M.B. at 55. The evidence also shows that in recent sales of large capacity generation units, the New England Electric System sold facilities at 1.4 times net book value; Pacific Gas & Electric Company sold plants at 1.32 times net book value and Southern California Edison Company sold plants at 2.65 times net book value. HSS/ARI M.B. at 56; HSS/ARI St. No. 1 at 146; HSS/ARI St. No. 1-S at 7.

The results of those sales are consistent with Duquesne's own internal conclusions about the value of its plants, and with the conclusions of Duquesne's consultant and financial advisor. Duquesne itself concluded that its "[s]ale of generating assets can add between $500-$750 million in after-tax cash for investing." Exh. RBW-3 at 12. A consultant retained by Duquesne, Metzler & Associates, performed studies reaching conclusions that are consistent with Duquesne's conclusion. HSS/ARI M.B. at 53-54. In fact, Metzler found that the value of just four of Duquesne's generation plants could exceed net book value by more than $657 million. Exh. RBW-9 at 4. Finally, Duquesne's merger advisor, CS First Boston, found that a sale of just five of Duquesne's generation plants could be made at a premium ranging from $377 million to $734 million. Exh. RBW-10; HSS/ARI St. No. 1 at 21, Table III-1.

Based upon these studies, HSS/ARI submit that CS First Boston's market price projections are the market price projections that the Commission should use in an administrative determination of the value of Duquesne's assets. Exh. RBW-57. Those projections produce results that are consistent with real world transactions, and those results are consistent with Duquesne's and Metzler's studies of the value of Duquesne's assets.

On the other hand, the OCA's market price projection should be rejected. OCA itself recognized that all market price projections (including its own) must be assessed in light of the real market evidence available -- Duquesne's actual sales of portions of its generating assets. OCA R.B. at 10. OCA itself also apparently concedes that any market line adopted in this proceeding must accurately consider Duquesne's generating asset sales. *Id.* And OCA's own market price witness recognized that a critical input assumption he used to determine his market price projections was unrealistically low. OCA St. No. 2 at 9:6-10:16. By relying upon an unreasonably low input assumption, he thus, inappropriately, derived an unreasonably low forecast of future market prices, the effect of which is to inflate Duquesne's stranded costs. Thus, this proceeding differs from *PECO* in that there is superior evidence available in the form of real market data that should supersede OCA's price projections which are less reliable.

Accordingly, HSS/ARI recommend that the Commission reject the ALJ's recommendation to adopt the OCA market price projections because OCA's market price forecast is unreasonably low and imposes substantial stranded costs on ratepayers in excess of the stranded costs market evidence suggests Duquesne will incur. Instead of using the OCA approach, the Commission should adopt the market price projections sponsored by HSS/ARI. Again, those projections were performed for Duquesne; they are consistent with other studies in Duquesne's possession and they produce results

that are consistent with the results of actual sales of existing generation plants that have taken place around the country.

## B. Regulatory Assets

### Overview

Duquesne has claimed that numerous costs qualify as "regulatory assets" and thus, allegedly, are eligible for recovery as part of the Company's stranded cost claim. *See* R.D. at 347-48. As the Commission made clear in *PECO*, only costs that "are not presently included in rates but which the utility is *already entitled* to recover through future rate adjustments are entitled to regulatory asset treatment." *PECO Order* at 66 (emphasis added). As is demonstrated below, in numerous instances, the recommended decision failed to apply this standard.

**Exception No. 6: The ALJ Erred in Approving Duquesne's Claim For Recovery of Any SFAS 109 Deferred Taxes As a Regulatory Asset (Section VI.E.2(a) (R.D. at 348-54)).**

The Recommended Decision reduced Duquesne's claim with respect to SFAS 109 Deferred Taxes by $62.94 million. R.D. at 354. However, the recommended decision erred in its determination that Duquesne is entitled to recover any SFAS 109 Deferred Taxes in the first instance. Duquesne's argument in support of this claim is that ratepayers received the benefit of deferred taxes and, therefore, should not avoid liability for Duquesne's higher tax bill in the future when the "tax benefits" turn around. Duquesne St. 4 at 8:14-9:1. However, HSS/ARI demonstrated that because the Company chose not to file a rate case since 1986, Duquesne retained any tax benefits for its shareholders; it did not pass those benefits back to ratepayers, *i.e.*, to pass through the benefit to ratepayers, Duquesne would have had to file a rate case to make an appropriate adjustment to its rates. HSS/ARI M.B. at 69-70. Moreover, Duquesne is not *already* entitled to

recovery of these deferred taxes. *Id.* Accordingly, Duquesne should not be authorized to recover any deferred taxes as a regulatory asset.

**Exception No. 7: The ALJ Erred in Granting Duquesne's Request for Recovery of $45.77 Million in Unamortized Debt Costs As a Regulatory Asset (Section VI.E.2(b) (R.D. at 354-61)).**

The recommended decision adopted the position of the OCA with respect to the recovery of $45.77 million in unamortized debt costs as regulatory assets. R.D. at 356, 361. HSS/ARI submit that this recommendation is in error.

As HSS/ARI pointed out in their Main Brief, Duquesne failed to demonstrate any nexus between the claimed stranded costs and the electric utility restructuring occasioned by the Customer Choice Act. HSS/ARI M.B. at 71. Additionally, Duquesne Witness O'Brien stated only that "[d]ue to restructuring . . ., the Company will not be able to recover fully the unamortized (sic) remainder of the expense." *Id.* at 10. He did not contend that *none* of the balance will be recoverable though Duquesne has claimed the entire amount as a regulatory asset.

HSS/ARI also pointed out that Duquesne currently amortizes the cost of reacquired debt over the life of the debt, but here is proposing to recover the entire reacquisition premium during the transition period. *See* Exh. RBW-47; *see also* Duquesne Statement No. 4 at 9:19 to 10:15. This proposal is not reasonable. Because the regulatory asset portion of these costs was incurred to finance the construction and/or purchase of generating assets, the reacquisition premium and issuance cost should be amortized consistent with Commission policy, *i.e.*, over the remaining life of the debt. Duquesne's generating assets will not disappear in their entirety at the end of the transition period. Thus, as HSS/ARI indicated, operating units (and Duquesne's shareholders) will continue to benefit from the lower debt costs obtained by refinancing in future years.

Based upon the foregoing, HSS/ARI argued that Duquesne's proposal ignores the tenet of regulatory policy that the cost of a benefit should be matched with the benefit itself. The proposal ignores that tenet by making ratepayers responsible for all of the post-2001 cost of this item while conferring the post-2001 benefit on Duquesne's shareholders. HSS/ARI Statement No. 1 at 109:8-17. However, the recommended decision apparently ignores HSS/ARI's argument, and by doing so, conflicts with a basic principle of regulatory law.

**Exception No. 8: The ALJ Erred In Granting Duquesne's Requested Recovery of $23.5 Million in Deferred Rate Synchronization Costs As a Regulatory Asset (Section VI.E.2(d) (R.D. at 366-70)).**

The Recommended Decision grants Duquesne full recovery of the claimed $23.5 million in deferred rate synchronization costs. R.D. at 370. However, the ALJ erred in his decision because the Company is not *already entitled* to recovery of these costs. HSS/ARI M.B. at 72-73 (citing *PECO* at 66). Further, as set forth in HSS/ARI's main brief, the Commission expressly declined to approve recovery of these costs in the past. HSS/ARI M.B. at 72; Exh. RBW-36. Moreover, in a subsequent proceeding, in wake of OCA opposition, Duquesne was forced to amend its proposal to recognize that such costs were not entitled to recovery from ratepayers. HSS/ARI M.B. at 72; Exh. RBW-38. Thus, the Commission has twice declined Duquesne's attempts to recover these costs. HSS/ARI M.B. at 72. Accordingly, consistent with *PECO*, the costs are not entitled to recovery as a regulatory asset. The recommended decision therefore should be reversed as to the recognition of $23.5 million in deferred rate synchronization costs as a regulatory asset.

**Exception No. 9:** **The ALJ Erred in Approving Recovery As a Regulatory Asset Approximately $8 Million in Compensated Absences and Over $9 Million for Injuries/Damages (Section VI.E.2 (l and m) (R.D. at 397-99).**

The Recommended Decision approved Duquesne's recovery as a regulatory asset approximately $8 million in costs associated with Compensated Absences. R.D. at 398. The Recommended Decision also approved the recovery of over $9 million in costs associated with Injuries/Damages as a regulatory asset. R.D. at 399. In reaching those conclusions, the Recommended Decision summarily rejected HSS/ARI's proposed adjustments with respect to those items. R.D. at 398-399. However, the Recommended Decision provides no reasoning to support the rejection of HSS/ARI's arguments.

With respect to "Compensated Absences", HSS/ARI demonstrated that Duquesne has not adequately justified these costs given the trend toward downsizing that the Company has experienced and likely will experience in the future. HSS/ARI St. 1 at 113. Moreover, Duquesne has not provided any evidence to support the allocation of these costs to its generation function. Perhaps, most significantly, Duquesne chose not to rebut criticisms of its Compensated Absences claims. In fact, there is no discussion of compensated absences in Duquesne's Main Brief. *See* Duquesne M.B. at 47, 50.

With respect to Injuries/Damages, as HSS/ARI demonstrated, although Duquesne concedes that only generation-related costs are recoverable, it has not demonstrated that the claimed $9 million is attributable to the Company's generation functions. HSS/ARI St. 1 at 77. Furthermore, Duquesne has not established the justness and reasonableness of these claims since its last rate case in 1987. *Id.*

The sole basis for the rejection of HSS/ARI's proposed modifications apparently was that the reasoning supplied for approving regulatory asset treatment of other costs -- deferred employee costs -- applied equally to compensated absences. *Id.* Unfortunately, however, the sole reason that the ALJ provided as a basis to approve Duquesne's request to treat deferred employee costs as a regulatory asset was: it "appears justified on this record." R.D. at 374.

Accordingly, there is no basis to uphold the ALJ's approval of the amounts associated with Compensated Absences and Injuries/Damages as regulatory assets. The Commission, therefore, should reject the ALJ's recommendation to allow Duquesne to treat those claims as regulatory assets.

### C. Recovery of Stranded Costs

**Exception No. 10: The ALJ Erred in Approving Duquesne's Proposal to Accelerate Amortization And Denying an Immediate Rate Reduction (Section VI.F.2(a&b) (R.D. at 436-47)).**

The Recommended Decision approves Duquesne's proposal to accelerate amortization of its stranded costs pursuant to Section 2804(4)(v) of the Customer Choice Act. R.D. at 442-43. The Recommended Decision also denies requests for an immediate rate reduction. R.D. at 447-48. Those rulings are intertwined and both are in error.

Duquesne's proposal to accelerate amortization of its stranded costs must be considered in conjunction with the Company's proposal to maintain its current rates. *See* HSS/ARI M.B. at 81-82. Absent approval of Duquesne's request to accelerate amortization and depreciation, Duquesne's cost of service would be reduced by $22 million. O'Brien, Tr. 617:17-20. However, as is explained in HSS/ARI's Main Brief, the net effect of Duquesne's proposal to accelerate amortization and depreciation is to increase its cost of service by $62 million. HSS/ARI M.B. at 81-82. As a result, approval of Duquesne's request to accelerate amortization and depreciation provides Duquesne an

artificial and improper basis to prop up its cost of service to support its current exorbitant rates that are not just and reasonable because they are not cost justified under traditional ratemaking methodologies. HSS/ARI M.B. at 80. Accordingly, the Recommended Decision errs in allowing Duquesne to accelerate amortization and depreciation. The Commission should rectify this error by requiring Duquesne to reduce its generation rates based on a cost of service that reflects the $22 million reduction that would occur absent accelerated amortization and depreciation.

**Exception No. 11: The ALJ Erred in Failing to Address Issues Relating to Class Responsibility For CTC Recovery (Section VII.A.2(b) (R.D. at 509-22, 551-58))**

The Recommended Decision ostensibly adopts the OCA's recommendation with respect to the allocation of stranded cost responsibility to each customer class. R.D. at 556. However, the Recommended Decision is in direct contradiction to the Customer Choice Act with respect to responsibility of stranded cost allocation.

Section 2808(a) of the Customer Choice Act requires stranded costs to be allocated in a manner that does not shift costs within or among classes of customers. 66 Pa. C.S. § 2808(a). The Recommended Decision errs by simply ignoring issues raised by HSS/ARI with respect to the overstatement of particular classes' stranded cost responsibility. R.D. at 521-22.

HSS/ARI showed -- and it is undisputed -- that Duquesne "wrote-up" rates for certain classes of customers in order to obtain an ability to recover revenues that are not the responsibility of those classes. HSS/ARI M.B. at 84-85. As Duquesne's witness Lahtinen testified, in allocating costs to individual rate classes, he was required to reduce the generation component of unbundled rates for certain classes to maintain the rate cap required by the Act. Duquesne Statement No. 5 at 25:3-5. That reduction obviously was required and is appropriate.

However, for certain other rate classes, "where costs are below revenue levels, [Lahtinen] adjusted the generation component to meet, but not exceed, 1996 revenues." *Id.* at 25:5-7. That latter upper adjustment clearly is inappropriate.

In effect, Lahtinen "wrote-up" the rates of these latter classes to recover revenues that are not those classes' responsibility. Similarly, by writing up the latter classes rates, Lahtinen was shifting generation-related revenue responsibility to them for revenues properly chargeable, but not collectible, from other rate classes because of the rate cap provisions of the Act.

Clearly, "writing-up" the rates of the effected classes violates Section 2808(a) of the Act in that generation-related revenue responsibility would be shifted to classes that are not responsible for those costs. HSS/ARI take exception with the ALJ's failure to address this issue. HSS/ARI submit that the Commission should require Duquesne to modify its rate proposal by reducing the revenue responsibility for classes: RS, GS/GM, GL, SH and Traffic Lights. HSS/ARI M.B. at 85.

**D. Transmission and Distribution Rates**

**Exception No. 12: 1996 Test Year Cost of Service. The Recommended Decision Errs by Recommending That Duquesne Be Permitted to Include In Distributions Rates Costs That Duquesne Has Not Shown Are Just and Reasonable. (Section V.B. (R.D. at 46-57)).**

HSS/ARI's direct testimony shows that, according to Duquesne's FERC Form 1 reports, between 1987 and 1996, Duquesne made distribution-related capital expenditures of approximately $473 million. HSS/ARI St. No. 1 at 55-56. Those expenditures are exclusive of amounts related to Duquesne's Beaver Valley 2 nuclear unit and Duquesne's initial capital expenditures for Perry Unit 1. As shown *supra* at 6-10, HSS/ARI raised the issue that Duquesne should be required to demonstrate the reasonableness of its past capital expenditures. Thus, Duquesne was required to

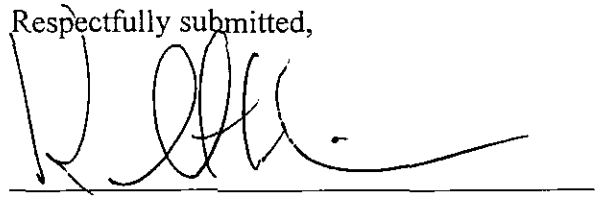
submit evidence that would allow the Commission to find that Duquesne's past capital expenditures were reasonable. However, Duquesne put no evidence in the record at all on this issue. Thus, there is no evidence in the record that will support a finding of reasonableness.

Accordingly, for the reasons discussed above with respect to Duquesne's generation-related capital expenditures, HSS/ARI recommend that the Commission order a disallowance of 50% of Duquesne's $473 million in distribution-related capital expenditures that Duquesne has not shown to be just and reasonable. As a result, the net book value of Duquesne's investment in distribution plant should be reduced by that amount for purposes of determining Duquesne's distribution rates. Again, if the Commission believes a lesser disallowance is more appropriate, then it should order such a lesser amount, but in no event should Duquesne be permitted to include in distribution rates a decade of expenditures totaling $473 million that have not been shown to be just and reasonable. Again, as stated previously with respect to Duquesne's past generation-related capital expenditures, failure to grant substantial, meaningful relief with respect to this issue would be further error.

## III. CONCLUSION

For the reasons set forth herein and in HSS/ARI's Main and Reply Briefs, Hospital Shared Services and Administrative Resources, Inc. hereby respectfully request that the Commission enter an order modifying the recommendation of the ALJ in accordance with these Exceptions.

Respectfully submitted,



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Dated: April 14, 1998

**BEFORE THE**
**PENNSYLVANIA PUBLIC UTILITY COMMISSION**

**CERTIFICATE OF SERVICE**

I hereby certify that I have this day served a true copy of the foregoing document on the appropriate parties in accordance with Section 1.54 of the Commission's regulations.

Dated this 14th day of April, 1998.

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ORIGINAL

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

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|---|---|---|
| PENNSYLVANIA PUBLIC UTILITY COMMISSION, | ) | |
| v. | ) | Docket No. R-00974104 |
| DUQUESNE LIGHT COMPANY Application to Approve Restructuring Plan Pursuant to 66 Pa.C.S. §2806(d) | ) | |



# EXCEPTIONS OF DUQUESNE LIGHT COMPANY

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| **Pennsylvania Public Utility Commission,** | ) | |
| **v.** | ) | **Docket No. R-00974104** |
| **Duquesne Light Company Application to approve restructuring plan pursuant to 66 Pa. C.S. § 2806(d)** | ) | |

## EXCEPTIONS OF DUQUESNE LIGHT COMPANY

Pursuant to the 52 Pa. Code § 5.533 (1997), Duquesne Light Company ("Duquesne") hereby submits its exceptions to the Recommended Decision ("R.D.") in this proceeding.

## INTRODUCTION

The fundamental premise of Duquesne's approach to stranded cost recovery is that the market, not career forecasters, should set the value of Duquesne's generating assets. The stranded costs issues presented in this case are therefore distinctly different from those in PECO Energy. There, the Commission, in determining PECO's stranded costs, was forced to choose between competing "30+ year projections of every important variable in the business, including electricity prices (expressed on an hourly basis), customer consumption and demand, the hourly output of all [PECO's] generating plants, and the O&M and capital costs." Applica-

tion of PECO Energy Company for Approval of its Restructuring Plan, Docket Nos. R-00973953 & P-00971265, Opinion and Order, slip op. at 82 (entered Dec. 23, 1997) ("PECO Energy"). Here, the common thread of all Duquesne's proposals is that such "forecasts" of market prices cannot meaningfully satisfy the "known and measurable" standard; only a market-based approach can. DLC St. 1 at 14; DLC St. 3 at 6. The Judge agreed, finding "an actual marketplace transaction is clearly superior for the purposes of determining the value of an asset to expert predictions of what that value may be." R.D. at 159. The Commission itself recently acknowledged the same, stating "any attempt to determine a future market price is largely speculative." Brief of Respondent, PaPUC at 1, Duquesne Light Co. v. Pennsylvania Public Util. Comm'n, No. 2485 C.D. 1997 (Commw. Ct.) (Apr. 3, 1998).

Against this backdrop, there are essentially two market-based approaches available to the Commission in this case. The first is Duquesne's "final valuation" plan. Under this plan, Duquesne's generation is valued in 2003 (or earlier if market prices rise unexpectedly) using available market evidence. The timing of this valuation is beneficial because electric markets will be far more developed in 2003 than today, providing a broader range of transactions with which to value Duquesne's assets. DLC St. 3 at 18-20; DLC St. 3-R at 16-18. A similar proposal was submitted jointly by DQE, Inc. and Allegheny Energy, Inc. in the merger

proceeding (described there as the "second look" valuation).[1] These final valuation proposals were not, however, adopted by either Judge Corbett or Judge Gesoff; rather, both Judges found that the "delay" associated with these proposals was not appropriate. R.D. at 159 (Duquesne); R.D. at 133 (West Penn).

The other valuation approach is Duquesne's offer to auction all its generating assets today.[2] Duquesne's proposal was not controversial: all parties agreed that an auction is the best valuation method. DLC St. 1-R at 6-11. The Judge accepted the proposal, finding it "irresistible." R.D. at 159. The Judge also adopted Duquesne's proposal that it "be permitted to fully recover (e.g., with no 'sharing' and a compensatory return on equity) its stranded costs as established by the market values produced by the auction." R.D. at 159-60. The Judge also adopted Duquesne's proposal to set an interim CTC (to apply prior to completion of the auction) using "the same rates and credits approved in the pilot program for customers electing direct access during this interim period"; and thereafter to design a

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[1] The key difference was that Duquesne offered to auction all its generating assets as part of its final valuation plan, while in the merger case the companies offered an auction of 5% of their assets.

[2] This offer was not made in the merger proceeding because the merged company intends to maintain its presence in the generation business. We note, however, that in the exceptions filed today in the merger docket, the companies have reserved their right, as a last resort, to auction all their Pennsylvania-jurisdictional generating assets if the Commission fails to approve an adequate Competitive Transition Charge ("CTC") for West Penn.

permanent CTC according to "the general approach used in PECO Energy." R.D. at 159.

Because Duquesne's auction proposal applied only if the merger is not consummated, however, the Judge was forced to consider the "expert predictions" (R.D. at 159) of market prices presented by the Office of Consumer Advocate ("OCA") and Duquesne Industrial Intervenors ("DII"). The Judge adopted the market price forecast of the OCA, relying heavily on PECO Energy. R.D. at 272. (In doing so, he rejected Duquesne's alternative market value calculation that was based on the best available market evidence existing today. DLC Main Br. at 25-34.) A significant portion of the following exceptions thus relate to disputes with the OCA over this issue; the Commission should be aware, however, that these disputes are relevant only if (i) the merger is consummated, and (ii) Duquesne's CTC is set using a one-time administrative determination of stranded costs – i.e., there is no final valuation proceeding or auction of the merging companies' assets (see supra n.2). For convenience, Duquesne has prepared a series of tables that apply Judge Corbett's findings regarding an administrative determination of stranded costs to produce (i) a total stranded amount (both with and without merger synergies), as

recommended by the Judge; and (ii) a system-average CTC designed to recover that amount under several scenarios.[3]

## EXCEPTIONS

### 1. Immediate Auction.

The Judge recommended that, in the absence of a merger with Allegheny Energy, "the Commission accept Duquesne's proposal to offer an immediate divestiture of its generating assets to determine the value of its stranded assets." R.D. at 159. The Judge did not reject any aspect of this proposal and, consequently, Duquesne does not except to that finding. However, Duquesne requests the following clarifications out of an abundance of caution.

#### a. Obligation to Serve.

The Judge agreed with Duquesne that, if all its generation was auctioned, Duquesne should be permitted to submit a plan regarding its continued obligation to serve following such a sale. The Judge was not clear, however, on when that plan would be submitted. Compare R.D. at 159 (plan to be submitted 90

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[3] Appendix B provides the total stranded costs recommended by the Judge (both with and without merger synergies). Appendices C-E develop CTCs under the following three scenarios using the stranded cost amounts contained in Appendix A: (i) a declining CTC that recovers the stranded cost amount over five years on a system-average basis (Appendix C), (ii) a declining CTC that recovers the stranded cost amount over seven years on a system-average basis (Appendix D), and (iii) a levelized CTC that recovers the stranded cost amount over eight and one-half years on a system-average basis (Appendix E).

days following Commission order on restructuring plan) with R.D. at 160 (plan to be submitted after completion of the auction). Duquesne requests clarification that such a plan will be filed following completion of the auction, not 90 days after a final Commission order. See DLC Main Br. at 21. This is appropriate because Duquesne's principal concern – that, after its generating assets are sold, it will not, because of the rate cap, be able to recover the cost of market purchases to serve customers that remain with Duquesne – is affected by the level of the shopping credits produced by the final CTC.[4] This final CTC, in turn, will not be set until the auction is complete. Consequently, Duquesne's concerns regarding its continued obligation to serve at capped rates should be addressed "at the same time that [Duquesne] files a final CTC calculation using market values produced by the auction." DLC Main Br. at 21; R.D. at 160.

**b. Timing of Auction.**

The Judge recommended that "divestiture should occur within 18 months of entry of the Commission's final Order disposing of this application." R.D. at 159. Duquesne requests clarification that while an auction may occur within 18 months, there is no requirement that it be completed by that time. Duquesne cannot control the timing of the necessary regulatory approvals and thus cannot "commit" to

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[4] The higher the shopping credit, the less financial exposure from customers returning due to escalating market prices.

a date on which the sale will be closed. (We note that General Public Utilities predicted that its divestiture will take approximately 21 months to complete from the date of announcement.) The Commission should therefore clarify that there is no "requirement" that an auction be completed within 18 months.

c. **Interim CTC.**

The Judge accepted Duquesne's proposal to "apply the same rates and credits approved in the pilot program for customers electing direct access during [the] interim period" prior to completion of the auction and calculation of the final CTC. R.D. at 159. The Judge did not, however, refer to the companion element of this proposal, which stated that "[a]lso consistent with the pilot program, Duquesne would defer revenue losses associated with the market and customer participation credits for collection in the final CTC." DLC Main Br. at 21 n.9. Duquesne's agreement to use the same rates and credits approved in the pilot program (subject to any modification on appeal[5]) was conditioned on being able to recover the lost revenue associated with the pilot "participation" and "market" credits. Id. While the precise methodology for doing so need not be addressed now (Duquesne will propose such a methodology in its compliance filing 90 days following a final

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[5] See Duquesne Light Co. v. Pennsylvania Pub. Util. Comm'n, No. 2485 C.D. 1997 (Pa. Commw. Ct.).

Commission order[6]), the Commission should clarify that, as proposed by Duquesne, the revenue losses associated with continued application of the pilot credits will be recovered in the final stranded cost amount.[7]

**d. Phillips and Brunot Island.**

Duquesne proposed to auction all its generating assets, including the Phillips and Brunot Island units in cold storage. The Judge, however, denied stranded cost recovery for these units. If that finding is sustained, Duquesne requests clarification that it will have the option to include these facilities in the auction, provided that (i) the facilities are not included in the same "bundle" as the other units, and (ii) and the resulting proceeds from the sale of these units accrues to shareholders, not to ratepayers.

**2. Final Valuation.**

Duquesne will first summarize the key components of its final valuation proposal, including the elements accepted by the Judge, and then provide exceptions to the portions of the proposal rejected by the Judge.

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[6] A general description of the anticipated methodology is provided in Appendix I. This methodology is subject to modification prior to its being filed 90 days following a final Commission order.

[7] To the extent that recovery of these revenue losses requires extension of the transition period for some or all customer classes, Duquesne reserves the right to request such an extension at that time.

### a. Summary of Proposal; Portions Accepted.

Duquesne's final valuation proposal has three principal components. First, the valuation will rely on market evidence, not "expert predictions." R.D. at 159. If the Commission so orders, this valuation will be through an auction of all Duquesne's generating assets. DLC St. 1-R at 11-12. Second, in the interim period prior to the valuation, the CTC will be set as a "residual" from capped rates according to Section 2804(4)(v). Consistent with Section 2804(4)(v), any "excess earnings" during this period will be used to accelerate the amortization of stranded costs. DLC St. 1 at 5. Third, the "shopping credit" applicable during this period will be based on the market prices resulting from an annual firm power sale ("Request for Proposals" or RFP). In addressing this plan, the Judge agreed that a market-based valuation is superior to administrative forecasts (R.D. at 159), and the Commission should "accept the Company's proposal for accelerated amortization under Section 2804(4)(v) with the ROE spillover mechanism set at the level discussed, infra." R.D. at 443. The Judge, however, rejected two key elements of the final valuation plan: (i) the timing of the valuation (R.D. at 159), and (ii) use of the RFP to set an annual shopping credit (R.D. at 554), as discussed below.

**b. Exceptions.**

**i. Timing of Valuation.**

The Judge rejected the final valuation because of the "delay" associated with it (R.D. at 159), but there was no factual basis for doing so. First, a market valuation in 2003 is superior to a valuation conducted today because better market evidence will be available as electric markets mature. DLC St. 3 at 18-20. Second, there is simply no need to conduct a valuation today, as Duquesne will not, even using the Judge's stranded cost determination, recover its stranded costs before 2003. See Appendix B. Third, a final valuation is preferable to a one-time valuation today, given the nature of Duquesne's continuing obligation to serve under the rate cap. DLC St. 1 at 14-18; DLC St. 1-R at 11-17; DLC St. 3 at 12-20; DLC St. 3-R at 15-32, 44-48. Fourth, there is no statutory requirement that a one-time valuation be made today. DLC Reply Br. at 5-6. Fifth, projecting market prices today does not benefit customers by providing "certainty," as some intervenors claimed (DII St. 1 at 25); rather, the only thing "certain" about such projections is that they will be inaccurate. DLC St. 3 at 6-16.

**ii. The RFP.**

The Judge rejected Duquesne's proposal to set the annual shopping credit using an RFP because (i) the market is not sufficiently "mature" to facilitate

such an RFP, and (ii) using an RFP "will stifle any nascent competition." R.D. at 554. We address each objection in turn.

First, the observation that electric markets are not today "mature" misses the point. The purpose of the RFP is to provide an objective basis for measuring actual market prices. These market prices represent Duquesne's ability to mitigate the loss of load associated with direct access. Whether these prices are affected by market "maturity" – or other factors such as severe weather, unexpected outages or new environmental regulations – is simply irrelevant. It is the prevailing price that matters, not the reasons for it. See DLC Main Br. at 68-71.

Second, the suggestion that, if the shopping credit is set at actual market prices under the RFP, it will "stifle any nascent competition" is both telling and an objection to the Act itself. It is telling because the obvious implication is that the shopping credit must be artificially inflated (i.e., above actual market prices) to encourage customer "switching." This has nothing to do with "competition"; it is a subsidy designed to benefit competitors. The Judge's finding also conflicts with Section 2804(4)(v), which states a preference for accelerated amortization of stranded costs and terminating the transition period early, not prolonging the transition period to accommodate "above-market" shopping credits. As the Judge found,

"the most satisfactory way to achieve rate relief . . . is to move as quickly as possible to a fully competitive electric generation market." R.D. at 447.[8]

For the foregoing reasons, Duquesne's final valuation plan should be adopted without modification.

3. **Brunot Island and Phillips.**

The Judge found that the costs of the cold-reserved Brunot Island and Phillips units cannot be recovered because these costs were not stranded by the Act. R.D. at 176.[9] The notion that these cold-reserved units are not stranded by the Act, while perhaps superficially appealing, is incorrect as a matter of fact. The decision to place a unit in "cold reserve" – rather than to retire it – is based on the very expectation that the unit will have value in a future year. Hence the past treatment of these units, even if relevant, supports recovery of their costs. Nor is it dispositive that, based on current projections, the units will continue to be uneconomic in the future; the point is that the Act will render them stranded once and for all.

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[8] Rejecting Duquesne's market-based approach to setting the shopping credit, and substituting the OCA's "expert predictions" of market prices, is contrary to the Judge's finding that "an actual marketplace transaction is clearly superior for the purposes of determining the value of an asset to expert predictions of what that value may be." R.D. at 159.

[9] The OTS recommended this disallowance; the OCA and DII did not oppose stranded cost recovery for these units. DLC Ex. DJC-10.

Given recent history, it would be particularly unfair for the Commission to deny recovery of the BI and Phillips costs. As the Commission is aware, Duquesne has continually sought to reactivate these plants in a manner that would benefit ratepayers (Tr. 109-112), including an agreement with General Public Utilities ("GPU") to reactivate them in support of a 500 MW, 20-year sale. DLC St. 1 at 26. The Commission approved this transaction, finding that it would produce over $300 million in present value benefits to ratepayers. Id.; Tr. 111; see also HSS Ex. RBW-45. While the transaction ultimately fell through (DLC St. 1 at 26), the point is that the Commission determined that ratepayers, not shareholders, should receive the benefits. Id. It is plainly unfair to contend that Duquesne's shareholders, not its ratepayers, should now bear the economic detriment associated with the assets. Id. at 27; DLC St. 2-R at 34-35. The stranded costs associated with these units should therefore be allowed.

**4. Administrative Determination of Market Value.**

**a. Market Price Forecasts.**

The Judge recommended adoption of OCA's market price forecast, finding it "unrebutted" that witness Smith used "the same model in this case as in PECO Energy" and further that in PECO Energy the Commission found his projections to be "the most credible, convincing and reasonable." R.D. at 272-73. The Judge's reliance on PECO Energy was erroneous. There, the Commission found Mr.

Smith's analysis superior to the computer simulations of PECO's witnesses (PECO Energy, slip op. at 83-87); here, however, no similar data was submitted by Duquesne. Rather, Duquesne submitted price projections using market evidence, not computer simulations.[10] Consequently, PECO Energy is inapposite.

It also is untrue that Mr. Smith's analysis was "the same" as in PECO Energy. In that case, the Commission found that Mr. Smith's "overall credibility" was enhanced "by not adjusting PECO's treatment of . . . reserve requirements." PECO Energy, slip op. at 88. Here, however, Mr. Smith departed from this approach and assumed that ECAR will construct new capacity in 2003 to meet an 8% reserve margin. (This produces an arbitrary "spike" in prices in that year. OCA Ex. DCS-4.) But it is undisputed that there is no such reserve margin requirement in ECAR. DLC St. 9-R at 2. Moreover, even apart from whether there is any such "requirement," ECAR predicts that it has ample capacity through at least the year 2005. DLC St. 9 at 9. Thus, his analysis was hardly "the same" in both cases.

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[10] For the years 1997-2005, Duquesne's witness, Mr. Schnitzer, used the results of Duquesne's eight-year RFP. DLC Ex. MMS-4; DLC St. 3 at 32-39; DLC St. 2-R at 12. This is the only market evidence of power prices during that period on the record. For the years beyond 2005, no comparable market evidence was available and therefore Mr. Schnitzer based his forecast (for those years) on the cost of new capacity; the cost of new capacity serves as a "cap" on market prices, although prices may well be below the cap. DLC St. 3 at 25-37. In estimating the cost of new construction (a combined cycle unit), he provided a range ("low" and "high") of prices and, again, relied on actual market data as much as possible. Id. at 26-27 (using market data for gas and gas transportation costs).

**b. Life Extension.**

The Judge found that "some 'life extension' must be attributed to [a generating] asset" because "[i]t is unreasonable to assume the physical life of a stranded asset equates exactly with its book life." R.D. at 281. Based on this finding, the Judge accepted the OCA's life extension projections, which inflate the market value of Duquesne's plants by $170 million. R.D. at 282.

First, the Judge was wrong to conclude that the "physical life" of a generating asset cannot "equate[] exactly with its book life." Id. at 281. The "book life" of an asset is the best estimate of its projected physical life. As the Commission is well aware, these book lives are developed using detailed engineering and economic analysis for the purpose of establishing appropriate depreciation schedules. Notably, in departing from these projections, OCA did not undertake any study of the cost required to life-extend Duquesne's units; rather, the OCA used studies by other utilities (PECO Energy and APS) of their plants. OCA St. 1 at 35, 37. These studies cannot possibly support a "known and measurable" calculation for Duquesne.

Put bluntly, the OCA's life extension forecast is the epitome of "speculative" projections by expert witnesses.[11] The OCA projections assume that current technology will continue to set market prices nearly 40 years from now, an

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[11] Brief of Respondent, PaPUC at 1, Duquesne Light Co. v. Pennsylvania Public Util. Comm'n, No. 2485 C.D. 1997 (Commw. Ct.) (Apr. 3, 1998).

assumption that is "somewhere between silly and reckless." DLC St. 3-R at 22.[12] Indeed, the OCA itself concedes that: "[i]n reality, the Company would defer life extension investment decisions until the years shortly before book retirement date[s] due to the inherent uncertainty of making such decisions this far in advance." OCA St. 1 at 35-36 (emphasis added). In sum, there is no basis in fact for adopting these projections.

**c. Plant Shutdown Study.**

The Judge accepted Duquesne's proposal to file a study prior to January 1, 1999 to "allow the Commission to determine whether any units should be shut down" as uneconomic. R.D. at 287. The Commission should be aware, however, that this proposal applied only to the final valuation; under that proposal, any net operating losses during the transition period would affect the final calculation of stranded costs and hence it was necessary to consider whether a shut down is economic. The same is not true, however, if either (i) an immediate auction is ordered, or (ii) an administrative determination of stranded costs is made. Under either of those two scenarios, a one-time determination of stranded costs is made today, which renders any future analysis of operating revenues/costs (and hence the economics of a shut down) unnecessary.

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[12] Notably, the OCA's Mr. Smith did not defend this assumption and neither did Mr. Kahal on surrebuttal. See OCA St. 1-S; OCA St. 2-S.

d. **Environmental Regulations.**

Duquesne requested a finding that all projections (including the OCA's) failed to address the impacts of two new environmental proposal that, if implemented, would add significantly to Duquesne's operating costs. DLC Main Br. at 39.[13] The Judge, however, held that "no further adjustment" should be made, given that "OCA's market value study . . . adjusts for the impact of the known environmental regulations." R.D. at 303. This finding was in error because Duquesne did not request any such "adjustment" and Duquesne's argument addressed new regulations, not "known" regulations. The Judge's failure to make the requested finding was particularly erroneous, given his acceptance of 40-year projections regarding life extension. R.D. at 281.

5. **Merger Synergies.**

Duquesne excepts to the Judge's findings regarding merger synergies (R.D. at 310-11, 835) for the reasons stated in the exceptions filed in the merger docket jointly by DQE, Inc. and Allegheny Energy, Inc.

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[13] The first is the EPA State Implementation Plan ("SIP call"), which would add over $100 million in capital and O&M expense to Duquesne's fossil units. DLC St. 10-R at 8-9. The second is the recent Kyoto conference, where the participating nations agreed to significantly reduce $CO_2$ emissions. Tr. 937-43.

6. **Decommissioning.**

a. **Nuclear.**

The Judge adopted the OCA's proposal for nuclear decommissioning (R.D. at 335), which used a contingency factor of only 10%. The OCA relied on a "proposed" policy statement by the Commission for this recommendation (OCA St. 3 at 19), yet that policy statement was never adopted by the Commission. DLC St. 13-R at 11-12. By contrast, Duquesne performed a contingency analysis that was site specific (DLC St. 13-R at 11; Tr. 647-49) and its witness, Mr. LaGuardia, testified that his firm's projected contingency factors contingency factors have proven accurate in actual experience. Tr. 649-53.[14]

b. **Fossil.**

The Judge disallowed recovery of fossil decommissioning expense, finding that PECO Energy "controls" this issue. R.D. at 347. In PECO Energy, the Commission held that "[p]rospective fossil decommissioning expenses are not recoverable . . . as a stranded cost, because they are not 'known and measurable' without a specific plan to decommission a particular plant at a particular time and in a particular manner." PECO Energy, slip op. at 92. That finding simply does not apply here, given that Duquesne's witness provided site specific decommissioning

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[14] TLG Services' ability to accurately predict the cost of decommissioning, including contingencies, has been remarkable – falling within approximately 4% for plants already dismantled. DLC St. 13 at 25; Tr. 677-78.

studies for each of Duquesne's plants. As Duquesne's witness testified, these fossil plants will be dismantled to conform to safety codes and the only question is at what cost. DLC St. 13 at 49-51. On that issue, Mr. LaGuardia is the only witness that provided an estimate and, hence, his testimony must be accepted. Finally, as the Judge in the PP&L restructuring case recently held, the Act's definition of "transition or stranded costs" (Section 2803) contemplates recovery of fossil decommissioning expense: it authorizes recovery of "retirement costs attributable to the utility's generating plants other than [nuclear decommissioning costs]." Application of PP&L for Approval of its Restructuring Plan, Docket No. R-00973954, Recommended Decision at 31 (Finding No. 219) (Kashi, ALJ) ("PP&L").

7. **Regulatory Assets.**

a. **Deferred Coal Costs.**

The costs at issue are coal costs that exceeded "caps" in the Company's ECR and were deferred for recovery until fuel costs fell below those caps. DLC St. 4 at 13; DLC St. 2-R at 27-28. The Judge found that "Duquesne has failed to show that these coal costs would be typically recoverable in a regulated environment." R.D. at 379. This finding is based on the argument of DII that the caps were "market" based and that Duquesne's fuel costs will never fall below market levels. DII St. 3-S at 17-18. The caps at issue, however, are cost-based caps (Tr. 190-91)

and Duquesne's fuel costs will decline in 2000 to below these levels. DLC St. 2-R at 27-28; DLC Ex. DJC-3 at 3. The regulatory asset therefore should be allowed.

**b. Deferred Caretaker Costs.**

The costs at issue were incurred in maintaining the Brunot Island and Phillips plants in cold storage. DLC St. 4 at 14-15; DLC St. 2-R at 32-35. The Judge recommended their disallowance, finding that "the assets associated with these caretaker costs . . . will [not] be returned to service within the foreseeable future." R.D. at 385. But the units to service will not be returned to service because they are uneconomic – i.e., stranded assets. The finding thus begs the question of whether such costs should be recovered in a CTC. They should, for all the reasons stated in the foregoing exception regarding BI and Phillips. DLC St. 2-R at 32-35.

**c. SFAS 106.**

The costs at issue are associated with health care benefits and life insurance for retired employees. DLC St. 4 at 13-14. The Judge recommended denial of these costs, finding that "all suppliers in the competitive environment will be subject to SFAS 106." R.D. at 395. This finding proves too much. If that were the standard, Duquesne could not recover any future operating costs (e.g., fuel or capital) because such costs will be borne by "all suppliers." Moreover, these costs

were properly deferred in accordance with prior Commission policy.[15] It also appears that a similar regulatory asset was approved in PECO Energy, slip op. at 72-73.[16] The regulatory asset should be approved.

**d. Warwick Mine Costs.**

The Judge held that the costs associated with the Warwick Mine could not be recovered because they "are not currently in rate base." R.D. at 397. This finding proves too much, as all deferrals since the last rate case are, by definition, not in "rate base." Moreover, this finding ignores the agreement reached with the Commission since the last rate case, under which Duquesne can recover the cost of the Warwick Mine through the ECR. DLC St. 2-R at 31-32; Petition of Duquesne Light Company for Order Establishing a New Coal Cost Standard, No. P-890386, Order at 3 ("Duquesne shall recover and reconcile Warwick Mine costs as part of its Energy Cost Rate procedure"). The regulatory asset should be approved.

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[15] When SFAS 106 took effect, Duquesne, consistent with the Commission's guidelines for implementing SFAS 106, began amortizing this liability over a 20-year period. DLC St. 4 at 13. Under the Act this liability now must be recovered within the transition period. Id. at 13-14. The OCA and OTS did not oppose recovery of these costs. See DLC Ex. DJC-10.

[16] The portion of the SFAS 106 disapproved in that case related to costs associated with an early retirement program (PECO Energy, slip op. at 73), but no such issue is presented in this case.

e. **Deferred Pilot Program Revenue Losses.**

The Judge adopted the OCA's recommendation to "adjust" the pilot program revenue losses for any immediate rate reduction ordered by the Commission in this case. R.D. at 304-05. This finding was in error. Duquesne should be permitted to fully recover any net revenue losses from the pilot program participation and market credits, even if an extension of the transition period is required. The "rates" approved in this case bear no relation to these revenue losses. Nor do the market price projections in this case provide any basis for reconciliation, as they relate to the post-1999 period. The proposed adjustment should be denied.[17]

f. **Miscellaneous Clarifications.**

Three points merit clarification regarding regulatory assets. First, there are several regulatory assets that no party contested and thus were not specifically addressed by the Judge. These assets are included on DLC Ex. DJC-10, as revised in Appendix B, hereto, and their recovery should be allowed as uncontested.

Second, one of these assets, "Deferred Fuel Costs," represents fuel costs incurred during 1996 in excess of Duquesne's ECR. In Docket No. M-00970917, the Commission held that "Duquesne is permitted to create a regulatory asset in an amount equal to its accumulated undercollection of its energy costs

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[17] The Judge also was in error in suggesting that "no party objects" to the OCA proposal (R.D. at 305), as Duquesne vigorously objected to the OCA's rate reduction proposal. See, e.g., DLC St. 2-R at 48.

incurred during the period commencing February 1, 1996 through the conclusion of its restructuring proceeding." Energy Cost Rate Filing for Duquesne Light Company for Fiscal year Beginning April 1, 1997, No. M-00970917, Order at 3 (Mar. 27, 1997) (emphasis added). Consistent with this order, Duquesne will submit an updated deferred fuel amount in its compliance filing at the conclusion of this proceeding.

Third, the Recommended Decision states that Duquesne's SFAS 109 regulatory asset should be "reduced" by $62.94 million. R.D. at 354. This was an adjustment that Duquesne had already made in its rebuttal case (see DLC Ex. DJC-10), thereby eliminating any dispute with OCA over the matter. DLC Main Br. at 45 n.37. Consequently, no "reduction" to Duquesne's claim, as revised on rebuttal, is required. See Appendix B.

**8. CTC Design Applicable To Administrative Determination.**

In this section, Duquesne addresses the question of the CTC design to apply if (i) the merger is consummated, and (ii) an administrate determination of stranded costs (rather than an auction[18] or a final valuation[19]) is adopted.

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[18] Duquesne proposed to apply the general CTC design adopted in PECO Energy if the auction is approved.

[19] Duquesne proposed using Section 2804(4)(v) for setting the CTC if the final valuation is approved.

**a. ROE Spillover; Accelerated Amortization.**

The Judge adopted Duquesne's proposal to use Section 2804(4)(v) to maintain rates at capped levels, but did not approve the remainder of the final valuation upon which that proposal was based. Compare R.D. at 159 with R.D. at 443. Duquesne's proposal to apply Section 2804(4)(v), including a minimum amortization commitment of $1.7 billion and the ROE spillover, applied only to the final valuation plan. It does not apply to an administrative determination of stranded costs. An administrative determination uses on a one-time forecast of market prices and operating costs to calculate a fixed schedule of CTCs. See generally OCA St. 4 at 15; OCA Ex. LS-4. Under this approach, Duquesne bears the risk that market prices may turn out lower, or operating costs higher, than forecast; Duquesne also has the theoretical opportunity, if the converse is true (i.e., market prices turn out higher or operating costs lower than forecast), to earn higher returns. See OCA St. 1 at 43. It thus would be unfair (and one-sided) to combine this approach with an ROE spillover to return "excess" earnings to ratepayers.

**b. CTC Applicable to Administrative Determination.**

The Judge recommended adoption of the following CTC design to implement his administrative determination of stranded costs:

> Under the OCA's approach, the CTC is a residual, which declines each year as the forecasted market prices for the CGC increase each year during the transition. The OCA shows the Company's current

total average rate is 8.930¢/kWh. Subtracting out the OCA's calculations of the appropriate unbundled charges for T&D combined of 2.211¢/kWh as shown on OCA Exhibit LS-7, leaves remaining revenue at current rates of 6.719¢/kWh. The OCA's analysis indicates a market price for 1999, including avoidable generation-related A&G, of 2.529¢/kWh. The remaining balance of 4.19¢/kWh represents the average CTC contribution for 1999.

Adoption of the OCA's methodology for calculating the CTC will mean that the CGC will be sent annually according to the fixed schedule of market prices appearing in *OCA Exhibits LS-7 & LS-7R*. Of course, the Company's collection of the CTC will be subject to annual review by the Commission. 66 Pa. C.S. § 2808(f).

* * *

The Act requires that stranded costs be allocated "in a manner that does not shift interclass or intraclass costs and maintains consistency with the allocation methodology for utility production plant accepted by the commission in the electric utility's most recent base rate proceeding." 66 Pa. C.S. § 2808(a). Consistent with this language and its holding in PECO Energy, Slip op. at 109-113, the Commission should follow the OCA's recommendation to allocate stranded cost responsibility to each customer class on the basis of the production capacity allocator utilized in the Company's last rate case.

The Commission should also adopt the OCA's recommendation to establish a levelized rate reduction. Due to the OCA's estimated increases in market prices, the CTC will decline annually, while allowing for a levelized rate reduction calculated to allow full recovery of stranded costs. *OCA Exh. LS-7 (Revised).*

R.D. at 555-56.

The foregoing passage presents three separate implementation issues: (i) the length of the CTC recovery period, (ii) the appropriate class responsibility for

stranded costs, and (iii) the rates chargeable to non-shopping customers. We address each in turn.

**i. Length of CTC Recovery Period.**

The most natural reading of the foregoing passage is a recommendation that the Commission adopt a "CTC residual" methodology -- i.e., the CTC is the residual after subtracting the OCA's projected CGC and T&D rate from current rates. Under this approach, the transition period would terminate in approximately 2003 (with merger synergies) on a system-average basis. See Appendix C. This interpretation is consistent with (i) the numerical example provided by the Judge, under which the CTC is calculated after deducting the CGC and T&D rate from current rates, (ii) the Judge's adoption of Duquesne's proposal to charge capped rates under Section 2804(4)(v) (R.D. at 443), and (iii) the Judge's rejection of the OCA's proposal for immediate rate reductions, finding that "the most satisfactory way to achieve rate relief . . . is to move as quickly as possible to a fully competitive electric generation market." R.D. at 447.

Duquesne recognizes, however, that the Judge's reference to "levelized rate reductions" could be interpreted as spreading out CTC recovery to effect a "levelized rate reduction" for customers. Under this approach, the CTC would be spread out over the transition period (i.e., through 2005), producing unbundled rates (CTC, T&D and CGC) that are approximately 10% below current

rates (with merger synergies) on a system-average basis. See Appendix D. While Duquesne does not endorse this interpretation – as it directly conflicts with the Judge's specific finding that immediate rate reductions should not be ordered (R.D. at 447) – we note it for completeness.

**ii. Class Responsibility for Stranded Costs.**

The Act states that stranded costs should be allocated "in a manner that does not shift interclass or intraclass costs and maintains consistency with the allocation methodology for utility production plant accepted by the commission in the electric utility's most recent base rate proceeding." 66 Pa. C.S. § 2808(a). In Duquesne's last base rate proceeding, production plant was allocated pursuant to the "average and excess" methodology; however, the required rate increases were applied pursuant to Duquesne's proposal "to spread any revenue increase across the board on a 'zero fuel' basis. This would give each rate class approximately the same percentage increase." Pennsylvania Pub. Util. Comm'n v. Duquesne Light Co., 66 Pa. PUC 518, 1988 Pa. PUC LEXIS 298, *510 (1988). The Commission did so over the objections of the OTS and OCA, which had argued that Duquesne's proposal maintained a "class rate of return difference" and "imposed the highest increases on the customers which were already paying the highest rates of return." Id. *510-511.

Applying these findings to this case requires that any rate changes be applied in a comparable manner to all rate classes. This can be accomplished under

either of the scenarios discussed above. First, under the "residual CTC" methodology – i.e., setting the CTC as a residual after deducting from current rates class-specific CGC[20] and T&D rates – all rate classes are treated comparably, consistent with the approach taken in Duquesne's last base rate case. This method provides a class-adjusted shopping credit that gives each class an equivalent opportunity to access a competitive electric market. It ends the transition period at the same time for all classes (approximately 2003), thereby avoiding a scenario where certain classes complete the payment of a CTC far sooner than other classes. It also maintains the relative differentials in class rates of return that exist today, thereby continuing to apply the rate design methodology adopted in the last base rate case. It therefore should be adopted.

Second, we note that it also is possible to design a CTC that accomplishes a "levelized rate reduction" for each class, if that result is so ordered. However, to ensure consistency with the rate determinations made in Duquesne's last base rate case, the levelized rate reduction must be comparable for all classes. The OCA has suggested (see OCA Ex. LS-6) that certain residential customers should receive large rate reductions, while certain industrial customers should receive no savings at all – and, indeed, that the transition period may have to be extended for

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[20] The OCA-recommended CGC would be adjusted for class load shapes. See Appendix F.

them. OCA St. 2-S at 7.[21] That approach, however, cannot be squared with the rate determinations made in the last rate case: in that case, the Commission did not, as the OCA seems to assume, use the production plant allocator to set rates; rather, the Commission designed rates for each class in a manner that provided "each rate class approximately the same percentage increase." Duquesne, 1988 Pa. PUC LEXIS 298, *510. Hence, the only lawful manner in which to adopt a "levelized rate reduction" in this case is to do so for all classes (thereby terminating the transition period in 2005 for all classes).[22]

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[21] As shown on Appendix H, Rate HVPS and Rate L would have approximately $180 million in combined stranded cost charges remaining unpaid at the end of the transition period (12/31/2005) under the OCA approach. Other classes would have substantial remaining balances as well. Id.

[22] Alternatively, if the OCA's approach is adopted, the Commission must extend the transition period to ensure that Duquesne fully recovers from each rate class the stranded costs allocated to it. Furthermore, any post-2005 CTC must be set without regard to the "rate caps," which do not apply to this period. See 66 Pa. C.S. § 2804(4). The Commission also should be aware that the same issue is presented if the Commission adopts a levelized CTC for 8 ½ years, with the shopping credit as the residual (as in PECO Energy). Under that approach, Duquesne can recover the CTC allocated to each class, but the resulting shopping credit for several classes is below anticipated market prices, thereby causing Duquesne to underrecover its cost of serving these customers if (as expected) they remain with Duquesne (and if the anticipated market prices prove accurate). Consequently, the CTC collection period may have to be extended for these customers beyond 8 ½ years to avoid such undercollections.

### iii. Non-Shopping Customers.

The Commission should clarify that if the unbundled rates (CTC, T&D and CGC) adopted in this case are lower than current rates for any class, only customers that "shop" will receive the associated rate reductions. (Stated another way, customers remaining on the system would continue to pay current rates until the end of the transition (CTC collection) period.) This methodology is consistent with the approach adopted in PECO Energy. It also is consistent with the Judge's rejection of the OCA's recommendation for immediate rate reductions. R.D. at 447.

### 9. ECR Roll-In.

The Judge held that Duquesne could not roll in its ECR at a level higher than "in effect" on the "effective date of the Act." R.D. at 557. This finding is erroneous. Section 2804(4)(v) provides that the ECR cannot be rolled-in at a rate that exceeds the levels "which have been approved by the commission as of the effective date of this chapter." The Commission approved an ECR of up to 14.7 mills/kWh in the Ft. Martin plan prior to the effective date of the Act. DLC St. 2 at 35. The only limitation in the Ft. Martin plan was a requirement that the ECR be cost-justified, but there is no dispute that Duquesne has justified an ECR of 14.7 mills/kWh in this case. DLC St. 1 at 35; DLC Ex. DJC-7; accord OCA Main Br. at 69 (Duquesne is "entitled to [14.7 mills/kWh if] it is justified by higher actual fuel costs"). The ECR roll in, as proposed by Duquesne, should therefore be allowed.

10. **Return on Equity.**

The Judge adopted the OTS' proposed return on equity (10.5%), finding that (i) Duquesne's proposed rate (11.5%) "does not reflect the reduced level of risk inherent in the CTC procedure for collection of stranded costs," and (ii) the OTS recommendation is supported by "substantial evidence." R.D. at 587. Both findings are in error. First, not even the OTS witness contended that a CTC produces "reduced risk" (OTS St. 1); to the contrary, the OTS witness concluded that, because of Duquesne's leveraged capital structure, "a higher than average cost of equity is warranted." OTS St. 1 at 11. (Duquesne's witness, Dr. Makholm, also concluded that there was nothing to suggest a "reduced level of risk" in this case. DLC St. 12 at 35-37.) Second, the OTS recommendation was not supported by "substantial evidence." Dr. Makholm thoroughly critiqued the OTS recommendation (DLC St. 12-R) and the OTS failed to respond. It did not submit surrebuttal testimony to Dr. Makholm or cross-examine him. Dr. Makholm's response is thus unrebutted and his testimony must therefore be accepted.[23]

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[23] One additional point of clarification is appropriate. The Judge accepted the OTS proposed rate of return, which OTS had computed as 9.2% (OTS St. 1, Sch. 1; OTS Main Br. at 75) based on a 10.5% return on equity and the test year 1996 capital structure, including an embedded cost of long-term debt of 8.51% and 7.45% rate on preferred shares. R.D. at 577. The Judge also agreed with OCA's position that Duquesne's claim for unamortized debt costs be valued as of December 31, 1998 at $45.77 million (gross of tax) and be included in the allowed claim for regulatory assets. R.D. at 361. Duquesne interprets these two findings as requiring use of the (continued...)

11. **Rate Redesign.**

The Judge rejected Duquesne's rate redesign because it allegedly "violates the prohibition in the Act against intraclass cost shifting." R.D. at 556. According to the Judge, "two customers having the exact same load in 1999 may pay different CTCs because the applicable CTC will have been imputed based upon the customers' 1996 load." Id. The Judge's "cost-shifting" finding is erroneous and contrary to public policy. The finding is erroneous because, as every witness but one conceded,[24] Duquesne's approach is the only methodology under which there is no cost shifting:

> the Company's approach to unbundling insures that no customer pays more in total (for the sum of his unbundled rate components assuming power is purchased at the CGC rate) than he would have paid under current bundled tariffs at the test or base year level of sales. This is a basic arithmetic identity of the top down approach in general and the Duquesne proposal here. [See DLC Ex. JAL-4.] Moreover, unlike the top down approaches proposed elsewhere (California and New York) which maintain revenue neutrality between bundled and unbundled rates on a class specific basis, Duquesne's approach main-

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[23](...continued)
OTS recommended capital structure and a reduced cost of long-term debt of 7.57% (per the OCA recommendation), resulting in a weighted average cost of capital of 8.73%. See Appendix B. Duquesne does not except to the Judge's finding regarding unamortized debt costs, provided that the OTS, not the OCA, capital structure is used, consistent with the foregoing discussion.

[24] Only MAPSA's Mr. Russell contended there would be cost shifting (MAPSA St. 1-S at 6); all other witnesses, including OCA and DII, either expressly or implicitly acknowledged that there would not. See, e.g., DII St. 1 at 52 ("specific costs have not been explicitly shifted under the Company's proposal").

> tains revenue neutrality on a customer specific basis. Since there is no shifting of revenues at the base year level of sales there can be no cost shifting. This test of cost shifting is a traditional measure used by regulatory jurisdictions since time immemorial to compare the cost shifting implications of alternative rate designs. Rate design alternatives are always assessed on the basis of **test year sales** to insure that each alternative recovers the same overall level of revenues, and to see whether there is cost shifting across classes and finally to determine individual customer impacts within a particular rate class.

DLC St. 5-R at 41 (emphasis in original).

The Judge's recommendation also represents poor public policy. Duquesne's rate redesign will bring rates closer to the marginal cost of production, thereby increasing efficiency in electrical usage. The additional savings to customers are enormous: residential ratepayers will receive a marginal rate reduction of 50%. DLC St. 5 at 34.[25] Moreover, the rate redesign will yield additional mitigation, potentially $15 million annually. DLC St. 1 at 21. In sum, there is no basis in fact or in policy to reject the rate redesign proposal.

**12. Transmission and Distribution Rates.**

**a. Realized Rates of Return.**

The Judge, agreeing with OCA and DII, found that Duquesne should use "realized," rather than required, rates of return for developing T&D rates, reasoning that (i) required rates of return cause "an inappropriate cost-shift and a

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[25] See also PP&L, Recommended Decision at 43 (Findings No. 319-321) (finding reduction in marginal rates to "promote a principal objective of the Act, which is to stimulate growth in the Pennsylvania economy").

violation of the Act's rate cap." R.D. at 68. This finding in error. As indicated supra, there is no possibility of cost-shifting under Duquesne's proposal. DLC St. 5-R at 41. In addition, the suggestion that the rate caps prohibit recovery of a just and reasonable T&D rate would render the Act confiscatory and hence violative of Duquesne's rights, both federal and state, to a fair return on investment. Finally, Duquesne's rates for transmission and ancillary services cannot be "set" by this Commission; they are set by the FERC. Any contrary finding is preempted by federal law. Mississippi Power & Light Co. v. Mississippi ex rel. Moore, 487 U.S. 354 (1988).

**b. Ancillary Services.**

The Judge made two findings regarding ancillary services that are preempted by federal law. First, he found that Duquesne had not "proven" that ECAR rules require that certain ancillary services be provided by the control area. R.D. at 84. These are questions squarely within FERC's jurisdiction (DLC Main Br. at 15-17); if any customer believes that Duquesne is incorrectly applying these rules, the only avenue of redress is through the complaint procedures available under Duquesne's open access tariff or Section 206 of the Federal Power Act. Moreover, the finding was in error, resulting from confusion (actively promoted by MAPSA, MAPSA Reply Br. at 7) regarding two distinct issues. The first is whether ECAR rules prohibit the unbundling of rates (see Tr. 772), which they do not and which is

actually required by FERC Order No. 888. The second is whether ECAR rules prohibit the provision of services by generators located outside the control area, which they do and which is also within FERC's authority because it relates to the provision of jurisdictional services. The finding should therefore be reversed.

The Judge also recommended that the Commission "disallow" Duquesne's proposed energy imbalance charge. R.D. at 84. That charge is FERC jurisdictional and hence the Commission has no authority to "disallow" it.

**13. Special Customer Classes.**

**a. Rule 4 Contracts.**

The Judge, relying on PECO Energy, held that "no contract or tariff may permit a customer to bypass payment of the full CTC" and that, to achieve this result, it may be necessary to "provid[e] a comparable dollar value offset on the regulated transmission, distribution or generation rates." R.D. at 598. First, any such "offset" to regulated T&D rates would be contrary to the Act, confiscatory in violation of federal and state law, and preempted by the Federal Power Act as applied to transmission or ancillary service rates. The only lawful result is to extend the transition period for customer classes that cannot complete payment of their allocated share of stranded costs before 2005. Second, the restriction on offering a discounted CTC to attract new load or retain existing load is poor public policy, as it will harm economic development and reduce stranded cost mitigation opportunities.

DLC Main Br. at 76-77; DLC St. 6 at 19; DLC St. 6-R at 6. The aforementioned findings of the Judge therefore should not be adopted.

**b. Riders 8, 9 and 20.**

The Judge recommended that Duquesne not offer any "special discount contracts to new customers or existing customers with new load." R.D. at 605. The characterization of these contracts as providing "discounts" is erroneous; the contracts apply to load that otherwise would not be served by Duquesne. Thus, the correct characterization is that the contracts provide incremental revenues, not discounted "rates." This increases stranded cost mitigation and benefits the economy of the Commonwealth. DLC Main Br. at 77-78; DLC St. 6 at 17-18. The Judge's finding should not be accepted.

**c. Rider 7.**

Duquesne requests clarification regarding the Judge's finding on Rider 7. R.D. at 611. Duquesne does not object to the finding, provided that the interruptible credit applies only to the load that Duquesne can interrupt (i.e., the portion of the load supplied by Duquesne, not other suppliers).

**14. Service to Returning Customers.**

The Judge found that "[n]o evidence exists in this record to suggest a problem will arise with returning customers engaging in 'gaming' to the detriment of Duquesne"; the Judge therefore rejected Duquesne's proposal to require a returning

customer to remain with Duquesne for 12 months. R.D. at 637. The finding is incorrect. Duquesne's witness testified that customers have an obvious incentive, because of the rate cap, to leave during low-cost periods and return during high-cost periods. DLC St. 5 at 69-70; DLC Main Br. at 80. No party contended this incentive would not exist and there was no credible alternative proposal offered. Id. Consequently, Duquesne's proposal should be adopted.

**15. Fees.**

The Judge recommended that Duquesne not be entitled to charge certain fees "until such time as Duquesne can substantiate the cost-basis" for them. R.D. at 740. Duquesne does not except to this finding, provided that it is interpreted to permit a subsequent filing that specifies the fees and provides the cost basis for them. Duquesne requests this clarification out of an abundance of caution, given that many parties have argued that "all" issues must be resolved in this proceeding.

WHEREFORE, Duquesne's exceptions should be granted for the reasons stated herein.

Respectfully submitted,

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Dated: April 13, 1998

## TABLE OF APPENDICES

# APPENDIX A

## Notes on Tables Implementing Recommended Decision

# Appendix A
## Notes on Tables Implementing Recommended Decision

### Appendix B – Total Stranded Cost Determination

The ALJ Recommended Decision produces an administrative determination of total stranded costs on an after-tax basis of $1,556,150,000 (standalone) and of $1,403,870,000 (net of merger synergy generation benefits). The associated deferred taxes recoverable by DLC on these amounts of stranded costs are $520,240,000 (standalone) and $412,250,000 (net of merger synergy generation benefits). Appendix B contains a Revised Exhibit No. DJC-10 table that shows the ALJ Recommended Total Stranded Cost Determination. This table reproduces the DJC-10 comparison between DLC and the OCA from the DLC Reply Brief, and provides an additional comparison with the ALJ Recommended Decision ("ALJRD"). The notes below refer to the appropriate page of the ALJ Recommended Decision for each line item. Where the treatment of a particular line item is open to multiple interpretations, the note refers to each. Regulatory assets that were not subject to dispute and thus were not briefed by the parties are shown at the DLC value.

**Notes on Appendix B — Revised Exhibit No. DJC-10**

ALJ-1) Net Book Value of Gen. Plant ($1,257.33 MM Gross and $848.55 MM Net of Deferred Tax) reflects the removal of Phillips and Brunot Island (ALJRD at 833) and Warwick mine (ALJRD at 836) from the DLC Net Claim of $917.61 MM, resulting in a total reduction of $113.30 MM Gross and $69.06 MM Net of Deferred Tax.

| | Gross | Def. Tax | Net |
|---|---|---|---|
| Phillips | $78.40 | $29.51 | 48.89 |
| B.I | 28.76 | 12.07 | 16.70 |
| Warwick Mine | 6.04 | 2.56 | 3.48 |
| Reduction from DLC Claim | 113.20 | 44.14 | 69.06 |

ALJ-2) Reflects the OCA recommended Working Capital of $61.53 MM (ALJRD at 834).

ALJ-3) Reflects the DLC recommended M&S and Fuel-Related Sunk Costs of $41.11 MM (ALJRD at 833.)

ALJ-4) Reflects the OCA recommended treatment of sale leaseback premiums (ALJRD at 362 and 835) and the allowance of the DLC claim for the BV2 Lease (ALJRD at 833). The PV of BV2 Lease Expense is shown at the OCA recommended value of $531.36 MM Gross and $300.35 MM Net of Deferred Tax. DLC present valued the BV2 Lease at $475.57 MM Gross and $278.24 MM Net of

Deferred Tax (see ALJRD at 833). The PV of BV2 Lease Expense is stated on a uniform basis in Appendix B by valuing the OCA cash flows at the ALJ recommended 7.43% discount rate.

ALJ-5) Reflects the OCA recommended Nuclear Decommissioning of $44.47 MM and no recommended recovery for fossil decommissioning (ALJRD at 835).

ALJ-6) Reflects the DLC recommended Costs Independent of Operation of $208.23 MM (ALJRD at 834).

ALJ-7) Reflects the OCA recommended Market Value of $299.07 MM (OCA Table 1, at 2; see ALJRD at 833) adjusted to exclude productivity adjustment of $13.04 MM (OCA Ex. MIK-1-Update at 3; see ALJRD at 834).

ALJ-8) Reflects the OCA and DLC recommended SFAS 109 tax regulatory asset of $236.49 MM Gross and $179.00 MM Net of Deferred Taxes. These amounts already reflect the reduction of $62.94 MM for SFAS 109 Plant. (See Note ALJ-16 below; see ALJRD at 350, 354 and 835).

ALJ-9) Reflects the DLC recommended Unamortized Debt Costs valued at 12/31/98 (ALJRD at 835).

ALJ-10) Reflects the DLC recommended 12/31/98 present value. The present value is stated on a uniform basis in Appendix B by valuing the amortization of regulatory assets at the recommended 7.43% discount rate.

ALJ-11) Reflects no recommended recovery for Deferred Coal Costs (ALJRD at 836).

ALJ-12) Reflects no recommended recovery for Deferred Caretaker Costs (ALJRD at 836).

ALJ-13) Reflects the DLC recommended Pre-Accrued Nuclear Outages of $17.60 MM Gross and $10.29 MM Net of Deferred Taxes (ALJRD at 836).

ALJ-14) Reflects the DLC recommended Transition Costs of $18.10 MM Gross and $10.59 MM Net of Deferred Taxes (ALJRD at 836).

ALJ-15) Reflects no recommended recovery for SFAS 106 (ALJRD at 836).

ALJ-16) Reflects no DLC claim and no recommended recovery for SFAS 109 Plant as a regulatory asset. (See ALJRD at 350, 354 and 835).

ALJ-17) Reflects the OCA recommended Merger Savings adjustment of $152.28 MM Net of Deferred Taxes (ALJRD at 835).

The ALJ Recommended Decision accepted the OTS recommendation of a 10.50% return on equity. DLC has calculated pro-forma CTC rates on a company-average based on the recommended level of stranded costs in Appendix B. The pro-forma rates have been calculated using the recommended OTS capital structure and return on equity of 10.50%. However, the cost of debt has been reduced to 7.57% to account for recovery of the unamortized debt premiums as a regulatory asset (see Note ALJ-9 above). The specified rate of return pro-formed (see Note ROE-1 below) has been used to calculate pro-forma CTC rates. An example of monthly amortization of the Total Stranded Cost Determination at the specified rate of return is included in Appendix B.

**Notes on Appendix B –- Specified Rate of Return and Monthly CTC Amortization Example**

ROE-1) The capital structure reflects the recommended ROE of 10.50% and the adjustment to the cost of debt to reflect recovery of unamortized debt premiums as a regulatory asset. The resulting weighted average cost of capital is 8.73% annually (0.70% monthly). Corresponding after-tax WACC is 7.15% and grossed-up for tax WACC is 12.23.

ROE-2) Recommended Deferred Taxes of $520.25 MM are assumed to be amortized on a straight-line basis ($74.32 MM annually) over the seven-year transition period. The present value of these amounts (calculated at the after-tax WACC of 7.15%) equals $398.38 MM. This amount is added to the recommended $1,556.15 MM stranded costs to develop pro-forma CTC rates. The actual amortization of the Deferred Tax balances would depend on the recovery pattern approved by the Commission, and would be recalculated and included in any future DLC compliance filing.

ROE-3) A total of $1,954.53 MM (including recovery of $398.38 MM of Deferred Taxes) is multiplied by the jurisdictional 99.9% to determine the starting balance of Total Recoverable Stranded Costs of $1,952.58 MM.

ROE-4) The starting balance of $1,952.58 MM is amortized monthly based on forecast annual sales volumes divided by twelve. In this recovery pro-forma, the CTC is calculated as a system-average residual after netting out the forecast OCA market price, A&G adder and average T&D rates (see notes CTC-5 to CTC-10 below). On a system-average basis, the stranded costs can be fully recovered by May 2004. Similar monthly amortization schedules are used to develop all other pro-forma CTC rate recovery forecasts.

## Appendix C – "CTC Residual" Method

In Appendix C, the company-average rates have been shown with the CTC plus CGC equal to the rate cap. The CTC is a residual calculated by subtracting the T&D rate and the OCA's market price (plus A&G adder) from the rate cap. The residual CTC declines as the forecast OCA market price rises. On a company-average basis the recommended stranded costs can be recovered through the residual CTC in a little more than five years (on a standalone basis) and a little more than four years (on a merged company basis).

**Notes on Appendix C** (The following notes apply to Appendices D and E as well)

Unbundled average rates are based on 1996 revenues and sales, and do not include Duquesne's proposed roll-in of the ECR at the $14.7/MWH cap.

Transmission rates are based on Duquesne's 1996 cost of service (not including losses or ancillary services) as adjusted for the realized rates of return as of Duquesne's last rate case.

Distribution rates are based on the 1996 cost of service (not including losses) as adjusted for the realized rates of return as of Duquesne's last rate case

The OCA all-hours market price is adjusted upward for Duquesne's customer class load shapes, T&D losses, and GRT. (See Appendix F)

OCA's generation A&G adder has been allocated to customer classes based on A&G allocators in Exhibit JAL-1B, p.16 of 23. The costs associated with generation A&G were taken from OCA Exhibit LS-4 for 1999-2005, and are escalated thereafter at the projected DRI inflation rates per OCA Exhibit MIK-4.

**Appendix D – "Levelized Rate Reduction Method"**

In Appendix D, the company-average rates have been shown with a levelized rate reduction for shopping customers over the seven-year transition period. Again, the residual CTC declines as the forecast OCA market price rises. Accordingly, the sum of the company-average level of the CCG and the residual company-average CTC is the same in each year. This represents an average reduction of approximately 6% (on a standalone basis) and approximately 10% (on a merged company basis) from current rates for shopping customers in each year of the transition period.

**Appendix E – Levelized CTC for 8 ½ years (PECO Energy Method)**

In Appendix E, (for illustrative and comparative purposes) the company-average rates have been shown with the CTC levelized over 8 ½ years. The CGC or "shopping credit" is shown as a residual calculation. The resulting CGC is, by definition, levelized as well. On a company-average basis the CGC is 3.72 cents/kWh (standalone company) and 4.05 cents/kWh (merged company).

**Appendix F – Class CGC Adjustments**

In Appendix F, adjustments to the OCA's all-hours market prices are shown for customer class load shapes, T&D losses and GRT.

**Appendix G – Residual Stranded Cost Obligations of Certain Classes Under OCA Proposal**

If the Commission adopts the OCA's proposal to allocate and reconcile stranded costs by rate class based on production cost allocation factors, the length of the required recovery period will vary greatly between classes. For some classes, recovery of the stranded costs so allocated cannot be completed prior to 2005 using the methods shown in Appendices C and D. The uncollected CTC balance for these classes is shown as of 12/31/2005.

**Appendix H – 8 ½ Year Levelized CTC for Rates L and HVPS**

Appendix H shows the CTC methodology applied in Appendix E for rates L and HVPS. It shows that the residual CGC may be less than the OCA market price (plus the A&G adder) in some or all years.

**Appendix I – Stranded Cost Accounting and Pilot Credit Reconciliation for Asset Auction**

Appendix I describes how Duquesne's generation plant auction will determine the fair market value of the plants for purposes of calculating stranded costs and how the pilot credits and CTCs charged prior to completion of the auction will be reconciled.

# APPENDIX B

## Total Stranded Cost Determination
## (Revised Ex. DJC-10)

**APPENDIX B**
**Revised Exhibit No. DJC-10**
(w/ Gross and Def. Tax)
(All PV Amounts)

**Duquesne Light Company**

**Total Stranded Cost Determination**
**As of December 31, 1998**
($ Millions)

| | DLCo | | | OCA | | | ALJ | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Gross | Def. Tax | Net | Gross | Def. Tax | Net | Gross | Def. Tax | Net | Notes |
| **Generating Plant** | | | | | | | | | | |
| Net Book Value of Gen. Plant | $1,370.53 | $452.92 | $917.61 | $1,365.94 | $452.92 | $913.02 | $1,257.33 | $408.78 | $848.55 | **(ALJ-1)** |
| Working Capital | 0.00 | 0.00 | 0.00 | 61.53 | 0.00 | 61.53 | 61.53 | 0.00 | 61.53 | **(ALJ-2)** |
| M&S and Fuel-Related Sunk Costs | 41.11 | 0.00 | 41.11 | 0.00 | 0.00 | 0.00 | 41.11 | 0.00 | 41.11 | **(ALJ-3)** |
| PV of BV2 Lease Expense (1) | 475.57 | 197.33 | 278.24 | 513.36 | 213.01 | 300.35 | 513.36 | 213.01 | 300.35 | **(ALJ-4)** |
| Net Book Value | 1,887.21 | 650.25 | 1,236.96 | 1,940.83 | 665.93 | 1,274.90 | 1,873.33 | 621.79 | 1,251.54 | |
| P V of Decommissioning | 123.90 | 0.00 | 123.90 | 44.47 | 0 | 44.47 | 44.47 | 0.00 | 44.47 | **(ALJ-5)** |
| PV of Costs Independent of Operation | 208.23 | 0.00 | 208.23 | 0 | 0 | 0.00 | 208.23 | 0.00 | 208.23 | **(ALJ-6)** |
| Estimated Market Value | (46.83) | (19.43) | (27.40) | (511.17) | (212.10) | (299.07) | (488.89) | (202.86) | (286.03) | **(ALJ-7)** |
| Stranded Generating Plant | 2,172.51 | 630.82 | 1,541.69 | 1,474.13 | 453.83 | 1,020.30 | 1,637.14 | 418.93 | 1,218.21 | |
| **Regulatory Assets** | | | | | | | | | | |
| SFAS 109 | $236.48 | $57.48 | $179.00 | $236.48 | $57.48 | $179.00 | $236.48 | $57.48 | $179.00 | **(ALJ-8)** |
| Post-2005 - Unamortized Debt Cost | 29.92 | 10.88 | 19.04 | 29.34 | 10.67 | 18.67 | 29.92 | 10.88 | 19.04 | **(ALJ-9)** |
| Pre-2006 - Unamortized Debt Cost | 16.76 | 6.96 | 9.80 | 16.43 | 6.82 | 9.61 | 16.76 | 6.96 | 9.80 | **(ALJ-9)** |
| Deferred Rate Sync. Costs | 25.37 | 1.87 | 23.50 | 26.52 | 1.95 | 24.57 | 25.37 | 1.87 | 23.50 | **(ALJ-10)** |
| Deferred Employee Costs | 13.83 | 0.00 | 13.83 | 14.24 | 0.00 | 14.24 | 13.83 | 0.00 | 13.83 | **(ALJ-10)** |
| Deferred Nuclear Maintenance | 3.25 | 1.35 | 1.90 | 3.25 | 1.35 | 1.90 | 3.25 | 1.35 | 1.90 | |
| DOE Decom and Decon. | 5.58 | 2.33 | 3.25 | 5.74 | 2.40 | 3.34 | 5.58 | 2.33 | 3.25 | **(ALJ-10)** |
| Deferred Coal Costs | 13.50 | 0.00 | 13.50 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | **(ALJ-11)** |
| Deferred Caretaker Costs | 6.77 | 2.85 | 3.92 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | **(ALJ-12)** |
| BV2 Training Costs | 2.42 | 0.84 | 1.58 | 2.42 | 0.84 | 1.58 | 2.42 | 0.84 | 1.58 | |
| Low Level Rad. Waste | 2.27 | 0.00 | 2.27 | 2.27 | 0.00 | 2.27 | 2.27 | 0.00 | 2.27 | |
| Coal Cost Equalization | 0.12 | 0.00 | 0.12 | 0.12 | 0.00 | 0.12 | 0.12 | 0.00 | 0.12 | |
| Other | 0.53 | 0.00 | 0.53 | 0.53 | 0.00 | 0.53 | 0.53 | 0.00 | 0.53 | |
| Pre-Accrue Nuclear Outages | 17.60 | 7.31 | 10.29 | 0.00 | 0.00 | 0.00 | 17.60 | 7.31 | 10.29 | **(ALJ-13)** |
| Gain on Sale/Leaseback | 55.13 | 0.00 | 55.13 | 55.13 | 0.00 | 55.13 | 55.13 | 0.00 | 55.13 | |
| Deferred Rate Sych. Costs (Tax) | 0.21 | 0.00 | 0.21 | 0.22 | 0.00 | 0.22 | 0.21 | 0.00 | 0.21 | **(ALJ-10)** |
| BV-2 (Tax) | 0.17 | 0.00 | 0.17 | 0.17 | 0.00 | 0.17 | 0.17 | 0.00 | 0.17 | |
| Deferred Fuel Cost | 11.51 | 4.78 | 6.73 | 11.84 | 4.92 | 6.92 | 11.51 | 4.78 | 6.73 | **(ALJ-10)** |
| Transition Costs | 18.10 | 7.51 | 10.59 | 18.20 | 7.61 | 10.59 | 18.10 | 7.51 | 10.59 | **(ALJ-14)** |
| SFAS 106 | 3.28 | 1.36 | 1.92 | 3.37 | 1.40 | 1.97 | 0.00 | 0.00 | 0.00 | **(ALJ-15)** |
| SFAS 109 Plant | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | **(ALJ-16)** |
| Total Regulatory Assets | 462.80 | 105.52 | 357.28 | 426.27 | 95.44 | 330.83 | 439.25 | 101.31 | 337.94 | |
| Total Stranded Cost (Standalone) | $2,635.31 | $736.34 | $1,898.97 | $1,900.40 | $549.27 | $1,351.13 | $2,076.39 | $520.24 | $1,556.15 | |
| Merger Savings | 0.00 | 0.00 | 0.00 | (260.27) | (107.99) | (152.28) | (260.27) | (107.99) | (152.28) | **(ALJ-17)** |
| Total Stranded Cost (w/ Merger Savnigs) | $2,635.31 | $736.34 | $1,898.97 | $1,640.13 | $441.28 | $1,198.85 | $1,816.12 | $412.25 | $1,403.87 | |

DERIVATION OF STRANDED COSTS USED IN RATE RECOVERY ANALYSIS (in $mm)

APPENDIX B
Scenario: Without Merger Savings

| Capital Structure | Proportion | | Rate | Pre-Tax | After-Tax | Grossed-Up Pre-Tax | Notes |
|---|---|---|---|---|---|---|---|
| Equity | 40.08% | | 10.50% | 4.21% | 4.21% | 7.19% | ROE-1 |
| Preferred | 9.69% | | 7.45% | 0.72% | 0.72% | 1.23% | |
| Debt | 50.23% | | 7.57% | 3.80% | 2.22% | 3.80% | |
| Weighted Average Cost of Capital | | | Annual | 8.73% | 7.15% | 12.23% | |
| | | | Monthly | 0.70% | 0.58% | 0.97% | |
| Deferred Taxes per ALJ Decision | | | | $520.25 | | | ROE-2 |
| Amortized Deferred Taxes | | Year 1 | | $74.32 | | | |
| | | Year 2 | | 74.32 | | | |
| | | Year 3 | | 74.32 | | | |
| | | Year 4 | | 74.32 | | | |
| | | Year 5 | | 74.32 | | | |
| | | Year 6 | | 74.32 | | | |
| | | Year 7 | | 74.32 | | | |
| | | Nominal Total | | $520.25 | | | |
| | | PV at 7.15% | | $398.38 | | | |
| Net Stranded Costs per ALJ Decision | | | | $1,556.15 | | | |
| PV of Amortized Deferred Taxes | | | | 398.38 | | | |
| Total | | | | $1,954.53 | | | |
| Jurisdictional % | | | | 99.9% | | | |
| Total Recoverable Stranded Costs | | | | $1,952.58 | | | ROE-3 |

DERIVATION OF MONTHLY STRANDED COST RE[redacted]ERY

APPENDIX B
Scenario: Without Merger Savings

*System Average*

| Month | CTC (c/kWh) | Sales (kWh) | CTC Revenues ($000) | Gross Receipts Taxes ($000) | Beginning Stranded Cost Balance ($000) | Return ($000) | Amortization ($000) | Ending Stranded Cost Balance ($000) | Notes |
|---|---|---|---|---|---|---|---|---|---|
| Jan-99 | 4.019 | 1,098,149 | 44,132 | 2,031 | 1,952,580 | 18,864 | 23,237 | 1,929,343 | ROE-4 |
| Feb-99 | 4.019 | 1,098,149 | 44,132 | 2,031 | 1,929,343 | 18,639 | 23,461 | 1,905,882 | |
| Mar-99 | 4.019 | 1,098,149 | 44,132 | 2,031 | 1,905,882 | 18,413 | 23,688 | 1,882,194 | |
| Apr-99 | 4.019 | 1,098,149 | 44,132 | 2,031 | 1,882,194 | 18,184 | 23,917 | 1,858,277 | |
| May-99 | 4.019 | 1,098,149 | 44,132 | 2,031 | 1,858,277 | 17,953 | 24,148 | 1,834,129 | |
| Jun-99 | 4.019 | 1,098,149 | 44,132 | 2,031 | 1,834,129 | 17,719 | 24,381 | 1,809,748 | |
| Jul-99 | 4.019 | 1,098,149 | 44,132 | 2,031 | 1,809,748 | 17,484 | 24,617 | 1,785,131 | |
| Aug-99 | 4.019 | 1,098,149 | 44,132 | 2,031 | 1,785,131 | 17,246 | 24,855 | 1,760,276 | |
| Sep-99 | 4.019 | 1,098,149 | 44,132 | 2,031 | 1,760,276 | 17,006 | 25,095 | 1,735,181 | |
| Oct-99 | 4.019 | 1,098,149 | 44,132 | 2,031 | 1,735,181 | 16,763 | 25,337 | 1,709,844 | |
| Nov-99 | 4.019 | 1,098,149 | 44,132 | 2,031 | 1,709,844 | 16,519 | 25,582 | 1,684,262 | |
| Dec-99 | 4.019 | 1,098,149 | 44,132 | 2,031 | 1,684,262 | 16,271 | 25,829 | 1,658,433 | |
| Jan-2000 | 3.956 | 1,116,406 | 44,163 | 2,033 | 1,658,433 | 16,022 | 26,109 | 1,632,324 | |
| Feb-2000 | 3.956 | 1,116,406 | 44,163 | 2,033 | 1,632,324 | 15,770 | 26,361 | 1,605,963 | |
| Mar-2000 | 3.956 | 1,116,406 | 44,163 | 2,033 | 1,605,963 | 15,515 | 26,616 | 1,579,348 | |
| Apr-2000 | 3.956 | 1,116,406 | 44,163 | 2,033 | 1,579,348 | 15,258 | 26,873 | 1,552,475 | |
| May-2000 | 3.956 | 1,116,406 | 44,163 | 2,033 | 1,552,475 | 14,998 | 27,132 | 1,525,343 | |
| Jun-2000 | 3.956 | 1,116,406 | 44,163 | 2,033 | 1,525,343 | 14,736 | 27,394 | 1,497,948 | |
| Jul-2000 | 3.956 | 1,116,406 | 44,163 | 2,033 | 1,497,948 | 14,472 | 27,659 | 1,470,289 | |
| Aug-2000 | 3.956 | 1,116,406 | 44,163 | 2,033 | 1,470,289 | 14,204 | 27,926 | 1,442,363 | |
| Sep-2000 | 3.956 | 1,116,406 | 44,163 | 2,033 | 1,442,363 | 13,935 | 28,196 | 1,414,167 | |
| Oct-2000 | 3.956 | 1,116,406 | 44,163 | 2,033 | 1,414,167 | 13,662 | 28,469 | 1,385,698 | |
| Nov-2000 | 3.956 | 1,116,406 | 44,163 | 2,033 | 1,385,698 | 13,387 | 28,744 | 1,356,955 | |
| Dec-2000 | 3.956 | 1,116,406 | 44,163 | 2,033 | 1,356,955 | 13,109 | 29,021 | 1,327,933 | |
| Jan-2001 | 3.934 | 1,134,773 | 44,645 | 2,055 | 1,327,933 | 12,829 | 29,761 | 1,298,173 | |
| Feb-2001 | 3.934 | 1,134,773 | 44,645 | 2,055 | 1,298,173 | 12,542 | 30,048 | 1,268,124 | |
| Mar-2001 | 3.934 | 1,134,773 | 44,645 | 2,055 | 1,268,124 | 12,251 | 30,339 | 1,237,786 | |
| Apr-2001 | 3.934 | 1,134,773 | 44,645 | 2,055 | 1,237,786 | 11,958 | 30,632 | 1,207,154 | |
| May-2001 | 3.934 | 1,134,773 | 44,645 | 2,055 | 1,207,154 | 11,662 | 30,928 | 1,176,226 | |
| Jun-2001 | 3.934 | 1,134,773 | 44,645 | 2,055 | 1,176,226 | 11,363 | 31,226 | 1,145,000 | |
| Jul-2001 | 3.934 | 1,134,773 | 44,645 | 2,055 | 1,145,000 | 11,062 | 31,528 | 1,113,472 | |
| Aug-2001 | 3.934 | 1,134,773 | 44,645 | 2,055 | 1,113,472 | 10,757 | 31,833 | 1,081,639 | |
| Sep-2001 | 3.934 | 1,134,773 | 44,645 | 2,055 | 1,081,639 | 10,450 | 32,140 | 1,049,499 | |
| Oct-2001 | 3.934 | 1,134,773 | 44,645 | 2,055 | 1,049,499 | 10,139 | 32,451 | 1,017,048 | |
| Nov-2001 | 3.934 | 1,134,773 | 44,645 | 2,055 | 1,017,048 | 9,826 | 32,764 | 984,284 | |
| Dec-2001 | 3.934 | 1,134,773 | 44,645 | 2,055 | 984,284 | 9,509 | 33,081 | 951,204 | |
| Jan-2002 | 3.695 | 1,153,788 | 42,630 | 1,962 | 951,204 | 9,189 | 31,478 | 919,725 | |
| Feb-2002 | 3.695 | 1,153,788 | 42,630 | 1,962 | 919,725 | 8,885 | 31,782 | 887,943 | |
| Mar-2002 | 3.695 | 1,153,788 | 42,630 | 1,962 | 887,943 | 8,578 | 32,090 | 855,853 | |
| Apr-2002 | 3.695 | 1,153,788 | 42,630 | 1,962 | 855,853 | 8,268 | 32,400 | 823,454 | |
| May-2002 | 3.695 | 1,153,788 | 42,630 | 1,962 | 823,454 | 7,955 | 32,713 | 790,741 | |
| Jun-2002 | 3.695 | 1,153,788 | 42,630 | 1,962 | 790,741 | 7,639 | 33,029 | 757,713 | |
| Jul-2002 | 3.695 | 1,153,788 | 42,630 | 1,962 | 757,713 | 7,320 | 33,348 | 724,365 | |
| Aug-2002 | 3.695 | 1,153,788 | 42,630 | 1,962 | 724,365 | 6,998 | 33,670 | 690,695 | |
| Sep-2002 | 3.695 | 1,153,788 | 42,630 | 1,962 | 690,695 | 6,673 | 33,995 | 656,700 | |
| Oct-2002 | 3.695 | 1,153,788 | 42,630 | 1,962 | 656,700 | 6,344 | 34,324 | 622,377 | |
| Nov-2002 | 3.695 | 1,153,788 | 42,630 | 1,962 | 622,377 | 6,013 | 34,655 | 587,722 | |
| Dec-2002 | 3.695 | 1,153,788 | 42,630 | 1,962 | 587,722 | 5,678 | 34,990 | 552,732 | |
| Jan-2003 | 3.154 | 1,173,544 | 37,018 | 1,704 | 552,732 | 5,340 | 29,974 | 522,757 | |
| Feb-2003 | 3.154 | 1,173,544 | 37,018 | 1,704 | 522,757 | 5,050 | 30,264 | 492,494 | |
| Mar-2003 | 3.154 | 1,173,544 | 37,018 | 1,704 | 492,494 | 4,758 | 30,556 | 461,937 | |
| Apr-2003 | 3.154 | 1,173,544 | 37,018 | 1,704 | 461,937 | 4,463 | 30,851 | 431,086 | |
| May-2003 | 3.154 | 1,173,544 | 37,018 | 1,704 | 431,086 | 4,165 | 31,149 | 399,937 | |
| Jun-2003 | 3.154 | 1,173,544 | 37,018 | 1,704 | 399,937 | 3,864 | 31,450 | 368,486 | |
| Jul-2003 | 3.154 | 1,173,544 | 37,018 | 1,704 | 368,486 | 3,560 | 31,754 | 336,732 | |
| Aug-2003 | 3.154 | 1,173,544 | 37,018 | 1,704 | 336,732 | 3,253 | 32,061 | 304,671 | |
| Sep-2003 | 3.154 | 1,173,544 | 37,018 | 1,704 | 304,671 | 2,943 | 32,371 | 272,300 | |
| Oct-2003 | 3.154 | 1,173,544 | 37,018 | 1,704 | 272,300 | 2,631 | 32,683 | 239,617 | |
| Nov-2003 | 3.154 | 1,173,544 | 37,018 | 1,704 | 239,617 | 2,315 | 32,999 | 206,618 | |
| Dec-2003 | 3.154 | 1,173,544 | 37,018 | 1,704 | 206,618 | 1,996 | 33,318 | 173,300 | |
| Jan-2004 | 3.039 | 1,194,297 | 36,300 | 1,671 | 173,300 | 1,674 | 32,955 | 140,344 | |
| Feb-2004 | 3.039 | 1,194,297 | 36,300 | 1,671 | 140,344 | 1,356 | 33,274 | 107,071 | |
| Mar-2004 | 3.039 | 1,194,297 | 36,300 | 1,671 | 107,071 | 1,034 | 33,595 | 73,476 | |
| Apr-2004 | 3.039 | 1,194,297 | 36,300 | 1,671 | 73,476 | 710 | 33,920 | 39,556 | |
| May-2004 | 3.039 | 1,194,297 | 36,300 | 1,671 | 39,556 | 382 | 34,247 | 5,309 | |
| Jun-2004 | 3.039 | 184,859 | 5,619 | 259 | 5,309 | 51 | 5,309 | (0) | |

# APPENDIX C

## "CTC Residual" Method

METHOD 1

Scenario: Without Merger Savings

| *System Average* | | | 1<br>1999 | 2<br>2000 | 3<br>2001 | 4<br>2002 | 5<br>2003 | 6<br>2004 |
|---|---|---|---|---|---|---|---|---|
| Sales | | gWh | 13,178 | 13,397 | 13,617 | 13,845 | 14,083 | 14,332 |
| Bundled Rate | | c/kWh | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 |
| Proposed Rates | Transmission | c/kWh | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 |
| | Distribution | c/kWh | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 |
| | CTC | c/kWh | 4.02 | 3.96 | 3.93 | 3.69 | 3.15 | 3.04 |
| Gross Shopping Credit | | c/kWh | 2.49 | 2.55 | 2.57 | 2.81 | 3.35 | 3.47 |
| Market Rates | OCA Mkt Price | c/kWh | 2.12 | 2.18 | 2.19 | 2.43 | 2.97 | 3.07 |
| | A&G | c/kWh | 0.37 | 0.37 | 0.38 | 0.38 | 0.39 | 0.39 |
| Discount | | c/kWh | 0.00 | (0.00) | (0.00) | 0.00 | 0.00 | (0.00) |
| | | % Change | -0.0% | 0.0% | 0.0% | -0.0% | -0.0% | 0.0% |
| CTC Balance | BOY | $000's | 1,952,580 | 1,658,433 | 1,327,933 | 951,204 | 552,732 | 173,300 |
| | EOY | $000's | 1,658,433 | 1,327,933 | 951,204 | 552,732 | 173,300 | 0 |

METHOD 1

Scenario: With Merger Savings

| *System Average* | | | 1<br>1999 | 2<br>2000 | 3<br>2001 | 4<br>2002 | 5<br>2003 |
|---|---|---|---|---|---|---|---|
| Sales | | gWh | 13,178 | 13,397 | 13,617 | 13,845 | 14,083 |
| Bundled Rate | | c/kWh | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 |
| Proposed Rates | Transmission | c/kWh | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 |
| | Distribution | c/kWh | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 |
| | CTC | c/kWh | 4.02 | 3.96 | 3.93 | 3.69 | 3.15 |
| Gross Shopping Credit | | c/kWh | 2.49 | 2.55 | 2.57 | 2.81 | 3.35 |
| Market Rates | OCA Mkt Price | c/kWh | 2.12 | 2.18 | 2.19 | 2.43 | 2.97 |
| | A&G | c/kWh | 0.37 | 0.37 | 0.38 | 0.38 | 0.39 |
| Discount | | c/kWh | 0.00 | (0.00) | (0.00) | 0.00 | 0.00 |
| | | % Change | -0.0% | 0.0% | 0.0% | -0.0% | -0.0% |
| CTC Balance | BOY | $000's | 1,717,841 | 1,394,987 | 1,032,270 | 619,382 | 180,330 |
| | EOY | $000's | 1,394,987 | 1,032,270 | 619,382 | 180,330 | 0 |

# APPENDIX D

## "Levelized Rate Reduction" Method

METHOD 2

Scenario: Without Merger Savings

| *System Average* | | | 1<br>1999 | 2<br>2000 | 3<br>2001 | 4<br>2002 | 5<br>2003 | 6<br>2004 | 7<br>2005 |
|---|---|---|---|---|---|---|---|---|---|
| Sales | | gWh | 13,178 | 13,397 | 13,617 | 13,845 | 14,083 | 14,332 | 14,588 |
| Bundled Rate | | c/kWh | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 |
| Proposed Rates | Transmission | c/kWh | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 |
| | Distribution | c/kWh | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 |
| | CTC | c/kWh | 3.53 | 3.47 | 3.44 | 3.20 | 2.66 | 2.55 | 2.34 |
| Gross Shopping Credit | | c/kWh | 2.98 | 3.04 | 3.06 | 3.30 | 3.84 | 3.96 | 4.17 |
| Market Rates | OCA Mkt Price | c/kWh | 2.12 | 2.18 | 2.19 | 2.43 | 2.97 | 3.07 | 3.28 |
| | A&G | c/kWh | 0.37 | 0.37 | 0.38 | 0.38 | 0.39 | 0.39 | 0.40 |
| Discount | | c/kWh | 0.49 | 0.49 | 0.49 | 0.49 | 0.49 | 0.49 | 0.49 |
| | | % Change | -5.6% | -5.6% | -5.6% | -5.6% | -5.6% | -5.6% | -5.6% |
| CTC Balance | BOY | $000's | 1,952,580 | 1,723,388 | 1,466,867 | 1,174,250 | 871,301 | 600,243 | 305,931 |
| | EOY | $000's | 1,723,388 | 1,466,867 | 1,174,250 | 871,301 | 600,243 | 305,931 | 0 |

METHOD 2

Scenario: With Merger Savings

| *System Average* | | | 1<br>1999 | 2<br>2000 | 3<br>2001 | 4<br>2002 | 5<br>2003 | 6<br>2004 | 7<br>2005 |
|---|---|---|---|---|---|---|---|---|---|
| Sales | | gWh | 13,178 | 13,397 | 13,617 | 13,845 | 14,083 | 14,332 | 14,588 |
| Bundled Rate | | c/kWh | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 |
| Proposed Rates | Transmission | c/kWh | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 |
| | Distribution | c/kWh | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 |
| | CTC | c/kWh | 3.15 | 3.09 | 3.07 | 2.83 | 2.29 | 2.18 | 1.96 |
| Gross Shopping Credit | | c/kWh | 3.35 | 3.42 | 3.44 | 3.68 | 4.22 | 4.33 | 4.54 |
| Market Rates | OCA Mkt Price | c/kWh | 2.12 | 2.18 | 2.19 | 2.43 | 2.97 | 3.07 | 3.28 |
| | A&G | c/kWh | 0.37 | 0.37 | 0.38 | 0.38 | 0.39 | 0.39 | 0.40 |
| Discount | | c/kWh | 0.86 | 0.86 | 0.86 | 0.86 | 0.86 | 0.86 | 0.86 |
| | | % Change | -9.9% | -9.9% | -9.9% | -9.9% | -9.9% | -9.9% | -9.9% |
| CTC Balance | BOY | $000's | 1,717,841 | 1,509,574 | 1,277,363 | 1,012,858 | 742,319 | 508,527 | 256,976 |
| | EOY | $000's | 1,509,574 | 1,277,363 | 1,012,858 | 742,319 | 508,527 | 256,976 | 0 |

# APPENDIX E

## Levelized CTC for 8½ Years
## (PECO Energy Method)

METHOD 3

Scenario: Without Merger Savings

| *System Average* | | | 1<br>1999 | 2<br>2000 | 3<br>2001 | 4<br>2002 | 5<br>2003 | 6<br>2004 | 7<br>2005 | 8<br>2006 | 9<br>2007 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Sales | | gWh | 13,178 | 13,397 | 13,617 | 13,845 | 14,083 | 14,332 | 14,588 | 14,846 | 7,556 |
| Bundled Rate | | c/kWh | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 |
| Proposed | Transmission | c/kWh | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 |
| Rates | Distribution | c/kWh | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 |
| | CTC | c/kWh | 2.79 | 2.79 | 2.79 | 2.79 | 2.79 | 2.79 | 2.79 | 2.79 | 2.79 |
| Gross Shopping Credit | | c/kWh | 3.72 | 3.72 | 3.72 | 3.72 | 3.72 | 3.72 | 3.72 | 3.72 | 3.72 |
| Market | OCA Mkt Price | c/kWh | 2.12 | 2.18 | 2.19 | 2.43 | 2.97 | 3.07 | 3.28 | 3.39 | 3.68 |
| Rates | A&G | c/kWh | 0.37 | 0.37 | 0.38 | 0.38 | 0.39 | 0.39 | 0.40 | 0.41 | 0.41 |
| Discount | | c/kWh | 1.23 | 1.17 | 1.15 | 0.91 | 0.37 | 0.25 | 0.04 | (0.08) | (0.38) |
| | | % Change | -14.1% | -13.4% | -13.1% | -10.4% | -4.2% | -2.9% | -0.5% | 0.9% | 4.3% |
| CTC Balance | BOY | $000's | 1,952,580 | 1,821,675 | 1,668,615 | 1,490,653 | 1,284,526 | 1,046,540 | 772,464 | 457,688 | 97,160 |
| | EOY | $000's | 1,821,675 | 1,668,615 | 1,490,653 | 1,284,526 | 1,046,540 | 772,464 | 457,688 | 97,160 | 0 |

METHOD 3

Scenario: With Merger Savings

| *System Average* | | | 1<br>1999 | 2<br>2000 | 3<br>2001 | 4<br>2002 | 5<br>2003 | 6<br>2004 | 7<br>2005 | 8<br>2006 | 9<br>2007 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Sales | | gWh | 13,178 | 13,397 | 13,617 | 13,845 | 14,083 | 14,332 | 14,588 | 14,846 | 7,556 |
| Bundled Rate | | c/kWh | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 | 8.75 |
| Proposed | Transmission | c/kWh | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 | 0.23 |
| Rates | Distribution | c/kWh | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 | 2.01 |
| | CTC | c/kWh | 2.45 | 2.45 | 2.45 | 2.45 | 2.45 | 2.45 | 2.45 | 2.45 | 2.45 |
| Gross Shopping Credit | | c/kWh | 4.05 | 4.05 | 4.05 | 4.05 | 4.05 | 4.05 | 4.05 | 4.05 | 4.05 |
| Market | OCA Mkt Price | c/kWh | 2.12 | 2.18 | 2.19 | 2.43 | 2.97 | 3.07 | 3.28 | 3.39 | 3.68 |
| Rates | A&G | c/kWh | 0.37 | 0.37 | 0.38 | 0.38 | 0.39 | 0.39 | 0.40 | 0.41 | 0.41 |
| Discount | | c/kWh | 1.57 | 1.50 | 1.48 | 1.24 | 0.70 | 0.59 | 0.38 | 0.26 | (0.04) |
| | | % Change | -17.9% | -17.2% | -16.9% | -14.2% | -8.0% | -6.7% | -4.3% | -2.9% | 0.5% |
| CTC Balance | BOY | $000's | 1,717,841 | 1,602,673 | 1,468,014 | 1,311,447 | 1,130,100 | 920,725 | 679,598 | 402,665 | 85,479 |
| | EOY | $000's | 1,602,673 | 1,468,014 | 1,311,447 | 1,130,100 | 920,725 | 679,598 | 402,665 | 85,479 | 0 |

# APPENDIX F

## Class CGC Adjustments

# ADJUSTMENTS TO OCA's ALL-HOURS MARKET PRICE (cents/kWh)

OCA's All-Hours Market Price (1999) 1.883 [A]

| | Class Load Shape Adj. [B] | T&D Loss Factor Adj. [C] | GRT Adj. [D] | OCA Market Price Adjusted For Load Shapes, Losses, & GRT [E] |
|---|---|---|---|---|
| RA | 1.0033 | 1.105 | 1.046 | 2.18 |
| RS | 1.0079 | 1.105 | 1.046 | 2.19 |
| RH | 1.0011 | 1.105 | 1.046 | 2.18 |
| GSGM | 1.0118 | 1.096 | 1.046 | 2.18 |
| GMH | 1.0071 | 1.090 | 1.046 | 2.16 |
| GL | 1.0057 | 1.051 | 1.046 | 2.08 |
| GLH | 1.0089 | 1.052 | 1.046 | 2.09 |
| L | 1.0030 | 1.036 | 1.046 | 2.05 |
| HVPS | 1.0036 | 1.009 | 1.046 | 1.99 |
| AL | 0.9848 | 1.077 | 1.046 | 2.09 |
| SE | 0.9851 | 1.105 | 1.046 | 2.14 |
| SM | 1.0000 | 1.105 | 1.046 | 2.18 |
| SH | 1.0000 | 1.105 | 1.046 | 2.18 |
| TRAFFIC | 1.0000 | 1.105 | 1.046 | 2.18 |
| System Average | 1.0045 | 1.071 | 1.046 | 2.12 |

Notes:
[A] OCA Exhibit DCS-4.
[B] Exhibit JAL-11 p. 1 of 1.
[C] Exhibit JAL 1D, p. 1 of 6 and JAL-15 p. 1 of 1.
[D] 1/(1-0.044)
[E] = [A] * [B] * [C] * [D]

# APPENDIX G

## Residual Stranded Cost Obligations of Certain Classes Under OCA Proposal

# Uncollected CTC Balances Per OCA Proposal

## (Millions Of Dollars In 2005)

| | Uncollected CTC Balance At the End of 2005 |
|---|---|
| L | 45.0 |
| HVPS | 136.9 |
| RH | 90.8 |
| GMH | 25.8 |
| GLH | 16.0 |
| AL | 0.0 |
| SE | 10.4 |
| Total | **$324.9** |

# APPENDIX H

## 8½ Year Levelized CTC for Rates L and HVPS

METHOD 3

Scenario: Without Merger Savings

| | | | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| *L Customers* | | | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 |
| Sales | | gWh | 1,456 | 1,483 | 1,512 | 1,541 | 1,570 | 1,600 | 1,630 | 1,661 | 846 |
| Bundled Rate | | c/kWh | 5.47 | 5.47 | 5.47 | 5.47 | 5.47 | 5.47 | 5.47 | 5.47 | 5.47 |
| Proposed Rates | Transmission | c/kWh | 0.15 | 0.15 | 0.15 | 0.15 | 0.15 | 0.15 | 0.15 | 0.15 | 0.15 |
| | Distribution | c/kWh | 0.71 | 0.71 | 0.71 | 0.71 | 0.71 | 0.71 | 0.71 | 0.71 | 0.71 |
| | CTC | c/kWh | 1.91 | 1.91 | 1.91 | 1.91 | 1.91 | 1.91 | 1.91 | 1.91 | 1.91 |
| Gross Shopping Credit | | c/kWh | 2.69 | 2.69 | 2.69 | 2.69 | 2.69 | 2.69 | 2.69 | 2.69 | 2.69 |
| Market Rates | OCA Mkt Price | c/kWh | 2.05 | 2.10 | 2.12 | 2.35 | 2.87 | 2.97 | 3.17 | 3.28 | 3.56 |
| | A&G | c/kWh | 0.31 | 0.31 | 0.31 | 0.32 | 0.32 | 0.32 | 0.33 | 0.33 | 0.34 |
| Discount | | c/kWh | 0.34 | 0.28 | 0.26 | 0.03 | (0.49) | (0.60) | (0.80) | (0.92) | (1.21) |
| | | % Change | -6.2% | -5.1% | -4.7% | -0.5% | 9.0% | 11.0% | 14.7% | 16.8% | 22.1% |
| CTC Balance | BOY | $000's | 149,096 | 139,282 | 127,735 | 114,230 | 98,517 | 80,318 | 59,322 | 35,170 | 7,472 |
| | EOY | $000's | 139,282 | 127,735 | 114,230 | 98,517 | 80,318 | 59,322 | 35,170 | 7,472 | 0 |

METHOD 3

Scenario: With Merger Savings

| | | | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| *L Customers* | | | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 |
| Sales | | gWh | 1,456 | 1,483 | 1,512 | 1,541 | 1,570 | 1,600 | 1,630 | 1,661 | 846 |
| Bundled Rate | | c/kWh | 5.47 | 5.47 | 5.47 | 5.47 | 5.47 | 5.47 | 5.47 | 5.47 | 5.47 |
| Proposed Rates | Transmission | c/kWh | 0.15 | 0.15 | 0.15 | 0.15 | 0.15 | 0.15 | 0.15 | 0.15 | 0.15 |
| | Distribution | c/kWh | 0.71 | 0.71 | 0.71 | 0.71 | 0.71 | 0.71 | 0.71 | 0.71 | 0.71 |
| | CTC | c/kWh | 1.68 | 1.68 | 1.68 | 1.68 | 1.68 | 1.68 | 1.68 | 1.68 | 1.68 |
| Gross Shopping Credit | | c/kWh | 2.92 | 2.92 | 2.92 | 2.92 | 2.92 | 2.92 | 2.92 | 2.92 | 2.92 |
| Market Rates | OCA Mkt Price | c/kWh | 2.05 | 2.10 | 2.12 | 2.35 | 2.87 | 2.97 | 3.17 | 3.28 | 3.56 |
| | A&G | c/kWh | 0.31 | 0.31 | 0.31 | 0.32 | 0.32 | 0.32 | 0.33 | 0.33 | 0.34 |
| Discount | | c/kWh | 0.57 | 0.51 | 0.49 | 0.26 | (0.26) | (0.37) | (0.57) | (0.69) | (0.98) |
| | | % Change | -10.4% | -9.3% | -8.9% | -4.7% | 4.8% | 6.8% | 10.5% | 12.6% | 17.9% |
| CTC Balance | BOY | $000's | 131,172 | 122,537 | 112,379 | 100,498 | 86,673 | 70,662 | 52,190 | 30,942 | 6,573 |
| | EOY | $000's | 122,537 | 112,379 | 100,498 | 86,673 | 70,662 | 52,190 | 30,942 | 6,573 | 0 |

METHOD 3

Scenario: Without Merger Savings

| *HVPS Customers* | | | 1<br>1999 | 2<br>2000 | 3<br>2001 | 4<br>2002 | 5<br>2003 | 6<br>2004 | 7<br>2005 | 8<br>2006 | 9<br>2007 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Sales | | gWh | 1,680 | 1,705 | 1,705 | 1,705 | 1,705 | 1,705 | 1,705 | 1,705 | 852 |
| Bundled Rate | | c/kWh | 4.13 | 4.13 | 4.13 | 4.13 | 4.13 | 4.13 | 4.13 | 4.13 | 4.13 |
| Proposed Rates | Transmission | c/kWh | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 |
| | Distribution | c/kWh | 0.48 | 0.48 | 0.48 | 0.48 | 0.48 | 0.48 | 0.48 | 0.48 | 0.48 |
| | CTC | c/kWh | 1.52 | 1.52 | 1.52 | 1.52 | 1.52 | 1.52 | 1.52 | 1.52 | 1.52 |
| Gross Shopping Credit | | c/kWh | 1.99 | 1.99 | 1.99 | 1.99 | 1.99 | 1.99 | 1.99 | 1.99 | 1.99 |
| Market Rates | OCA Mkt Price | c/kWh | 1.99 | 2.05 | 2.07 | 2.29 | 2.79 | 2.89 | 3.09 | 3.19 | 3.47 |
| | A&G | c/kWh | 0.24 | 0.24 | 0.25 | 0.25 | 0.26 | 0.27 | 0.28 | 0.29 | 0.30 |
| Discount | | c/kWh | (0.24) | (0.30) | (0.32) | (0.55) | (1.06) | (1.17) | (1.37) | (1.49) | (1.77) |
| | | % Change | 5.8% | 7.2% | 7.8% | 13.3% | 25.7% | 28.4% | 33.3% | 36.1% | 43.0% |
| CTC Balance | BOY | $000's | 130,756 | 121,003 | 109,683 | 96,979 | 82,721 | 66,719 | 48,760 | 28,605 | 5,986 |
| | EOY | $000's | 121,003 | 109,683 | 96,979 | 82,721 | 66,719 | 48,760 | 28,605 | 5,986 | 0 |

METHOD 3

Scenario: With Merger Savings

| *HVPS Customers* | | | 1<br>1999 | 2<br>2000 | 3<br>2001 | 4<br>2002 | 5<br>2003 | 6<br>2004 | 7<br>2005 | 8<br>2006 | 9<br>2007 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Sales | | gWh | 1,680 | 1,705 | 1,705 | 1,705 | 1,705 | 1,705 | 1,705 | 1,705 | 852 |
| Bundled Rate | | c/kWh | 4.13 | 4.13 | 4.13 | 4.13 | 4.13 | 4.13 | 4.13 | 4.13 | 4.13 |
| Proposed Rates | Transmission | c/kWh | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 |
| | Distribution | c/kWh | 0.48 | 0.48 | 0.48 | 0.48 | 0.48 | 0.48 | 0.48 | 0.48 | 0.48 |
| | CTC | c/kWh | 1.34 | 1.34 | 1.34 | 1.34 | 1.34 | 1.34 | 1.34 | 1.34 | 1.34 |
| Gross Shopping Credit | | c/kWh | 2.18 | 2.18 | 2.18 | 2.18 | 2.18 | 2.18 | 2.18 | 2.18 | 2.18 |
| Market Rates | OCA Mkt Price | c/kWh | 1.99 | 2.05 | 2.07 | 2.29 | 2.79 | 2.89 | 3.09 | 3.19 | 3.47 |
| | A&G | c/kWh | 0.24 | 0.24 | 0.25 | 0.25 | 0.26 | 0.27 | 0.28 | 0.29 | 0.30 |
| Discount | | c/kWh | (0.06) | (0.11) | (0.14) | (0.37) | (0.88) | (0.99) | (1.19) | (1.31) | (1.59) |
| | | % Change | 1.4% | 2.8% | 3.3% | 8.9% | 21.3% | 24.0% | 28.8% | 31.7% | 38.6% |
| CTC Balance | BOY | $000's | 115,036 | 106,456 | 96,497 | 85,320 | 72,776 | 58,698 | 42,898 | 25,167 | 5,266 |
| | EOY | $000's | 106,456 | 96,497 | 85,320 | 72,776 | 58,698 | 42,898 | 25,167 | 5,266 | 0 |

# APPENDIX I

## Stranded Cost Accounting and Pilot Reconciliation for Asset Auction

# APPENDIX I

## Stranded Cost Accounting and Pilot Credit Reconciliation for Asset Auction

Duquesne's generation plant auction will determine the fair market value of the plants as of the date of the sale of such plants in 1999 or 2000 ("Sale Date"). The fair market value of plants not receiving positive bids will be capped at zero as of the Sale Date (with any Costs Independent of Operation being deducted therefrom). Generation stranded costs for these plants will be determined by comparing the net book value of the plant with the fair market value, after properly accounting for all tax consequences of the sale (e.g., capital gains/losses, deferred taxes, etc.). The net book value of the plants sold will be less on the Sale Date than the net book value determined as of 12/31/98 in this proceeding as a result of any depreciation taken in 1999 or 2000.

Duquesne committed in its direct case (as part of its overall $1.7 billion commitment) to an acceleration of generation plant depreciation during the transition period. The annual level of this depreciation commitment was premised on a generation rate cap (including an ECR roll-in) of 8.75 cents/kWh on average, an ROE of 11.50%, and a CTC determined as the residual for each rate class after deducting a market-based CGC. The effect of this rate cap approach was that Duquesne would have earned generation revenues equivalent to those it would have received under traditional cost-of-service regulation. This, in turn, funded the committed level of accelerated plant depreciation.

If the interim CTCs charged to shopping customers prior to the auction are set using the generation credits from the pilot, then Duquesne will receive less revenue for each shopping customer than it would have under the rate cap approach. Similarly, if the roll-in of the ECR is not permitted, and the generation rate cap for non-shopping customers is set at 8.79 cents/kWh on average, Duquesne will receive less revenue for each non-shopping customer than it would have under the rate cap approach. Accordingly, Duquesne cannot commit to the same level of accelerated plant depreciation during this interim period, while earning the specified rate of return on its generation, even if this is calculated at the lower ALJ recommended level of 10.5%.

Duquesne will file as part of its 90 day filing a formula for reconciling the lost revenues for shopping and non-shopping customers with those underlying Duquesne's direct case. The formula will specify the new levels of accelerated plant generation that are consistent with reduced revenue levels and the specified return on equity. The formula will also provide a true-up mechanism for the difference between the expected and realized sales for shopping and non-shopping customers. The resulting depreciation schedule will benchmark the net book values in 1999 and 2000 of the generation plants to be auctioned, and fully account for interim CTC recoveries prior to the Sale Date.

**BEFORE THE**
**PENNSYLVANIA PUBLIC UTILITY COMMISSION**

| | | |
|---|---|---|
| **Pennsylvania Public Utility Commission** | ) | |
| | ) | |
| **v.** | ) | **Docket No. R-00974104** |
| | ) | |
| **Duquesne Light Company Application for Approval of a Restructuring Plan Pursuant to 66 Pa. C.S. § 2806(d)** | ) | |

**CERTIFICATE OF SERVICE**

I hereby certify that I have this day served a copy of the foregoing document, by overnight courier, upon the participants on the attached service list in accordance with Section 1.54 of the Commission's regulations.

Dated this 13th day of April, 1998.

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April 14, 1998

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Re: Application of Duquesne Light Company for Approval of Restructuring Plan Under Section 2806 of the Public Utility Code,
Docket No. R-00974104

Dear Secretary McNulty;

Enclosed please find an original and nine (9) copies of the Office of Consumer Advocate's Exceptions in the above-captioned proceeding.

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

Sincerely,

Marisa A. Sifontes

Marisa A. Sifontes
Assistant Consumer Advocate

Enclosure
cc: All parties of record
Honorable John H. Corbett, Jr. (Via overnight mail)
Office of Special Assistants

DOCUMENT
FOLDER

ORIGINAL

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

| | | |
|---|---|---|
| APPLICATION OF DUQUESNE LIGHT COMPANY FOR APPROVAL OF ITS RESTRUCTURING PLAN UNDER SECTION 2806 OF THE PUBLIC UTILITY CODE | : | Docket No. R-00974104 |

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OFFICE OF CONSUMER ADVOCATE'S
EXCEPTIONS

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Dated: April 14, 1998

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## I. INTRODUCTION AND SUMMARY OF EXCEPTIONS

On March 25, 1998, the Office of Administrative Law Judge issued the Recommended Decision (R.D.) of Administrative Law Judge ("ALJ" or "Judge") John H. Corbett, Jr. in this matter. ALJ Corbett's decision adopts many of the Office of Consumer Advocate's ("OCA") recommendations and OCA submits that, in large part, it represents a thoughtful and well-reasoned decision. However, OCA respectfully submits that there are a few areas where the ALJ's decision is in error and a few areas in which Judge Corbett's decision needs to be clarified. In particular, Judge Corbett's proposed unbundled rates need to be clarified, especially in the absence of schedules summarizing the proposed average rates.

With respect to the ALJ's determination of stranded costs, OCA excepts to Judge Corbett's decision in three respects. Specifically, OCA excepts to the rejection of OCA's generation unit productivity adjustment which was made in its development of stranded costs, as well as Judge Corbett's inclusion in stranded costs of Duquesne's claim of $208.23 million for "Costs Independent of Operation." OCA also specifically excepts to the ALJ's allowance of a return on the unamortized balance of stranded cost recovery on its owned-generation plants over the seven-year CTC recovery period. The OCA submits that Duquesne should not be permitted to recover a return on the unamortized balance of its owned-generation stranded costs, as a means of sharing the burden of stranded costs with the investors who must share responsibility for the Company's uneconomic investments. As noted above, OCA also submits that the ALJ's rate unbundling recommendations need to be clarified; in particular, his recommendation for a levelized rate reduction should be adopted and inconsistent recommendations made elsewhere clairifed or modified. Further, the OCA also excepts to the ALJ's decision to allow Duquesne recovery of the cost of pre-accrued nuclear outage

costs as a regulatory asset, as such recovery will create a double-recovery of these costs.

The OCA submits that, with these corrections, the ALJ's determination of stranded costs is reasonable and should be adopted for the reasons set out in his Recommended Decision and in OCA's Main and Reply Briefs.

Finally, the OCA excepts to Judge Corbett's decision to adopt the Company's proposed universal service plan without modification, and also, to the ALJ's finding that the Company's proposed Universal Service plan complies with the requirements of the Act and Commission's Universal Service Guidelines. The OCA submits that the funding and eligibility levels need to be increased to appropriate levels, and that the modifications to the CAP and LIURP programs, as were made by the OCA, as well as the addition of a renewables pilot, be incorporated into the Company's Universal Service plan in order to form a comprehensive plan that meets the needs of Duquesne's service territory.

II. EXCEPTIONS

EXCEPTION NO. 1: The ALJ's Recommendations On Pages 555-557 With Respect To The Development of the CTC, Shopping Credit, And Rate Reductions Should Be Adopted And The Meaning Of Statements Which Appear Inconsistent With These Recommendations Should Be Clarified Or Modified. (R.D. at 442-43, 447-48)

A. Introduction

On pages 555-57 of his decision, Judge Corbett adopts OCA's recommendations with respect to the development of the CTC, the shopping credit, and rate reductions. These recommendations include (1) that OCA's "proposed market prices will serve as an appropriate proxy for actual market prices during the transition period with sufficient certainty to enable a nascent marketplace to grow"; (2) that the CGC, or "shopping credit" will be set annually "according to the fixed schedule of market prices appearing in OCA Exhibits LS-7 & LS-7R"; (3) "[a]doption of the OCA's methodology for calculating the CTC"; (4) allocation of "stranded cost responsibility to each customer class on the basis of the production capacity allocator utilized in the Company's last rate case"; (5) adoption of "OCA's recommendation to establish a levelized rate reduction" which provides for a declining CTC; (6) rejection of Duquesne's proposal for a two-part CTC; (7) adoption of OCA's proposal "to calculate an avoidable generation credit for administration and general costs, which competitive suppliers incur"; (7) annual reconciliation of stranded costs on a class-specific basis; and (8) roll-in of the Energy Cost Rate ("ECR") at the rate in effect on the effective date of the Act, of 12.8 mills/kWh.

While the ALJ's recommendations on pages 555-57 adopt OCA's recommendations on these issues in their entirety, the ALJ's recommendations on these points appear to be inconsistent with conclusions he reaches elsewhere in his decision. In particular, on pages 442-43 and 447-48,

the ALJ suggests a different result in addressing interpretations of Section 2804(4)(v) of the Act and in addressing proposals for immediate rate reductions. More specifically, the ALJ agrees with Duquesne's position that its proposal to maintain rates at their current level "appears to track" Section 2804(4)(v) of the Act. With respect to OCA's proposal for rate reductions, the ALJ states that "[b]ecause the OCA's proposal for immediate rate reductions entails extension of the transition period, I urge the Commission to reject it." R.D. at 447. He further indicates here that during the transition, "ratepayers will continue to shoulder only the burden of rates capped at their present levels -- no more or no less." Id.

On page 443, the ALJ also appears to adopt, with modification, Duquesne's proposed ROE spillover mechanism, which is premised on a second-look determination of stranded costs in the 2002-2003 time frame. Again, this is inconsistent with the ALJ's statements, on pages 272-73 and 555-57, where the ALJ adopts OCA's approach, which provides for a one-time determination of stranded costs. As discussed below, for the reasons explained in OCA's Briefs, the Commission should reject Duquesne's second-look determination of stranded costs.

The ALJ's statements on pages 442-43 and 447-48 are inconsistent with the more detailed determinations he makes regarding the CTC, shopping credit, and rate reductions on pages 555-57. For reasons explained in OCA's Main and Reply Briefs, OCA submits that the ALJ's determinations on pages 555-57 should be adopted, and the ALJ's conclusions at pages 443 and 447 with respect to Section 2804(4)(v), and the issue of immediate rate reductions found to be in error. Further, the Commission should clarify that, in the absence of a divestiture, there should be a one-time determination of stranded costs in this case, rather than postponing that determination until 2003.

B. The Purpose Of Section 2804(4)(v) Is To Prevent Certain Future Complaints Against Rates Established In This Proceeding, Not To Prevent Rates From Being Reduced To An Appropriate Level In This Proceeding.

Throughout this proceeding, Duquesne has argued that Section 2804(4)(v) of the Act prevents the Commission from establishing rates in this proceeding that are lower than the combined level (ECR plus base rates) of such rates that were in effect on the effective date of the Act if the Commission finds that "excess earnings achieved under the cap are being utilized to mitigate transition or stranded costs for the benefit of ratepayers or to offset other known and measurable cost increases that would be recoverable under traditional ratemaking but are not included in the rate cap." 66 Pa.C.S. § 2804(4)(v). The ALJ appears to have agreed with this interpretation at one point in his Recommended Decision and has apparently found that Duquesne's proposed ROE spillover mechanism will prevent excess earnings. R.D. at 442-43.

As discussed in OCA's Briefs, this interpretation is incorrect and would stand the entire statute on its head. See OCA M.B. at 16; OCA R.B. at 1, 20-21. The purpose of this section of the Electric Competition Act was to prevent complaints against rates being filed subsequent to the establishment of rates in this proceeding, not to prevent the lowering of rates in this proceeding. Contrary to Duquesne's position, the intent of this section, which is part of the rate cap section of the Act, was not to establish a rate floor. See OCA R.B. at 1. Indeed, as discussed in OCA's Main Brief, one of the primary goals of the Act was to provide needed rate relief to Pennsylvania consumers. Such a rate floor would clearly prevent the provision of such rate relief. Moreover, Sections 2807(e)(2) and (e)(3) require electric distribution companies such as Duquesne to provide generation services at prevailing market prices beginning in 2001. If charging of prevailing market prices results in rates below current levels (even when including stranded costs), continuation of the capped rate

level would clearly undermine the objective of charging ratepayers for generation at prevailing market prices. Such an inconsistency should not be read into the statute.

The ALJ appears to rely on Duquesne's reading of the statute, which was elucidated in its Reply Brief. DLC R.B. at 3-4. Duquesne asserts that the section needs no interpretation, and that the only "temporal" dimension of the section is the requirement that capped rates not exceed those approved by the Commission as of the effective date of this chapter. Id. at 4.

Unfortunately, the manner in which the Company discusses this section distorts a plain reading. A plain reading of this section is simply that if the rates established in the restructuring do not exceed the rates in effect on the effective date of the statute, then they may not be reduced post-restructuring based on the complaint of any party if the Commission determines that excess earnings are being used to mitigate stranded costs or to offset other known and measurable cost increases. The purpose is to give some finality to the Commission's determination of rates in the restructuring proceedings, not to prevent it from initially establishing a level of rates that allows the utility to recover an appropriate level of costs, subject only to the rate cap.

In this regard, the use of the phrase "upon complaint of any party" is particularly significant in interpreting this section. Clearly, this restructuring proceeding is a statutorily mandated proceeding and is not a proceeding "upon complaint of any party." This is made plain by Section 2806 which requires the utility to submit its restructuring plan and requires the Commission to review the restructuring plan and issue an order with respect to that restructuring plan within nine months, and makes no reference to complaints. 66 Pa.C.S. §§ 2806(e) and (f). Thus, this is a statutory proceeding, not a proceeding upon complaint of a party and Section 2804(4)(v) was clearly not intended to apply to this proceeding. It is absurd to suggest, as Duquesne does, that the fact that

complaints have been filed by OCA and others in this case creates a new limitation for the Commission in its restructuring order that would not exist if no complaints had been filed.

In light of the above discussion, OCA submits that Section 2804(4)(v) was clearly intended to address future complaints against rates that may be initiated after the establishment of rates in restructuring proceedings. Furthermore, as the Pennsylvania Retailers Association pointed out in its Reply Brief, "it refers to post-restructuring proceeding where electric utilities are achieving significant excess earnings as operating costs decline and as a result of the recovery of stranded costs and general impact of competition." PRA R.B. at 22-23. Clearly, as PRA points out, the section is intended to address circumstances which have not yet occurred but may result from restructuring.

Even if there were any validity in Duquesne's interpretation of Section 2804(4)(v), OCA submits that the ALJ is in error in suggesting that Duquesne's ROE spillover mechanism is an appropriate mechanism to address the Company's excess earnings. As explained in OCA's Briefs and as the ALJ recognizes, the proposed ROE spillover mechanism would require annual reexamination of the Company's earnings. See OCA M.B. at 18-20; OCA R.B. at 21. As the Company recognized, in order to protect parties' due process rights, this would effectively create annual rate proceedings, with discovery, hearings and briefs assessing the Company's earnings. Id. The administrative burden of such a review would be substantial and is inconsistent with the objective of the Act to establish the appropriate rates in this restructuring plan.

C. The Commission Should Adopt The ALJ's Finding On Page 556 Adopting OCA's Recommendation To Establish A Levelized Rate Reduction And Should Clarify, Or Modify, His Apparently Inconsistent Recommendation Earlier In The Decision Rejecting OCA's Rate Reduction Recommendation.

While the ALJ, on page 556 of his Recommended Decision, clearly adopts OCA's

proposed levelized rate reduction, which would reduce Duquesne customer rates by 16.9%, on page 447 he also appears to reject OCA's proposal for rate reductions. This inconsistency needs to be corrected and OCA submits that the Commission should clarify, or modify, the statements on page 447 to make them consistent with the result provided on page 556. In other words, the Commission, for the reasons set forth in OCA's Briefs, should implement OCA's recommended rate reduction. See OCA M.B. at 62-65; OCA R.B. at 21-23. As discussed in OCA's Briefs, a rate reduction is necessary to ensure that ratepayers pay only the amount of stranded costs determined by the Commission: (1) for customers who continue to take generation service from Duquesne, these costs include the Company's T&D rates, the CTC, and the market price of generation; or (2) for customers who take generation service from an alternative electric generation supplier, these costs include T&D rates and the CTC. Id. Customers who are not able to shop, or who choose not to shop, should not be required to pay more than the market prices upon which the estimate of stranded cost is based. This is especially important given that under the ALJ's recommendation it will be a full two years before all customers are able to shop. Additionally, charging a generation rate in excess of "prevailing market prices" is contrary to the clear provisions of the Act, which requires that at the end of the phase-in period, customers who do not choose an alternative generation supplier are to be served at "prevailing market prices" and the utility is to recover the reasonable costs of providing such service. 66 Pa.C.S. § 2807(e)(3).

Finally, the ALJ's reasoning on page 447 is in error because it is based on his understanding that OCA's proposed rate reductions entail extension of the transition period. That is not the case. Under OCA's proposal, stranded costs would be fully collected during the seven-year CTC recovery period.

For all of these reasons, the Commission should clarify, or modify, the statements on page 447 to make them consistent with the recommendations set forth on page 556 of the ALJ's decision.

D. The Commission Should Clarify The ALJ's Decision To Make Clear That It Is Adopting A One-Time Determination Of Stranded Costs In This Proceeding, As Opposed To The Second-Look Determination Of Stranded Costs Proposed By The Company.

While the ALJ adopts OCA's stranded cost valuation and recovery methodology as discussed on pages 272-273 and 555-57 of his Recommended Decision, which provides for a one-time determination of stranded costs and the setting of T&D rates, the CTC, and the market-based generation charge based on projected market prices, the ALJ's apparent adoption of an ROE spillover mechanism on page 443 of his Recommended Decision is inconsistent with these findings. Under the Company's proposal, the ROE spillover mechanism would be used to adjust the CTC rate level in a second-look determination (or final valuation) of stranded costs to occur in 2003. Since the ALJ does not specifically resolve the issue of a one-time versus second-look determination, the Commission needs to clarify the ALJ's decision in this respect. For the reasons discussed in OCA's Briefs, the Commission should adopt a one-time determination of stranded costs and the establishment of rates for the entire CTC recovery period, subject only to change to reflect the annual reconciliation for actual kWh sold. See OCA M.B. at 14-21; OCA R.B. at 7-8. As discussed in OCA's Briefs, the Company's second-look approach to determining stranded costs is inconsistent with the Act's requirement that stranded costs be determined in this proceeding on a net present value basis. Moreover, the second-look approach raises numerous problems, substantially increasing uncertainty in the marketplace for generation services, denying ratepayers of needed rate savings,

weakening Duquesne's incentives to mitigate stranded costs, and, as noted above, creating substantial administrative burdens through annual examination of the Company's earnings for purposes of establishing the ROE spillover effect. Id. Clearly, the limited potential benefit of the second-look approach in providing some additional market information regarding the level of stranded costs is far outweighed by these negative effects. The second-look approach should be plainly rejected and the ALJ's decision adopting the ROE spillover mechanism should be found to be inconsistent with his adoption of OCA's stranded cost valuation and recovery approach.

EXCEPTION NO. 2: The ALJ Erred In Rejecting OCA's Productivity Adjustment. (R.D. at 294)

As the Commission well knows, industry experts and analysts expect that generating plant productivity will increase as a result of the introduction of competition into the generation marketplace. Indeed, this is one of the primary reasons for moving from a system of regulated monopoly to a competitive market. See OCA M.B. at 43. Estimates have been made that fixed O&M costs of generating plants will be reduced from between 15% to 40% on an industry-wide basis, based on estimates made by the Federal Energy Regulatory Commission ("FERC") and the U.S. Department of Energy ("DOE").

While the Company, in its budget figures, has reflected some efficiencies as a result of work force reductions until 2002, OCA witness Kahal testified that there should be some additional efficiency gains after the first few years of retail competition. OCA St. 1 at 33. He conservatively estimated a 1% per year gain in productivity beginning in 2003 and extending for ten years, with the savings capped at 10% and held constant over the remainder of the study period. This productivity gain is applied to the Company's non-fuel O&M and A&G expenses for those plants with positive

plant margins. Id. The result of this adjustment is not a decrease in expenses, but an annual increase in such expenses of 1.0% less than the general inflation rate. Id. The dollar effect of this adjustment is a present value increase of $13.04 million in plant margins (or reduction in stranded costs) at 1/1/99. As discussed in OCA's Briefs, given the much higher estimates of productivity gains made by FERC and the DOE, Mr. Kahal's adjustment is modest and conservative. See OCA M.B. at 44; OCA R.B. at 12.

In his Recommended Decision, ALJ Corbett concluded that there was insufficient evidence in the record to support a productivity adjustment. R.D. at 294. OCA submits that the ALJ erred in this finding and that the productivity adjustment is based on studies of changes in the level of expenses as noted by OCA witness Kahal, and, in Mr. Kahal's expert judgment, can be reasonably relied upon in analyzing stranded costs. Such an adjustment was recommended by ALJ Gesoff in the parallel West Penn proceeding [R-00973981, R.D. at 436] and should likewise be adopted here.

EXCEPTION NO. 3: The ALJ Erred In Allowing The Company Recovery Of "Costs Independent Of Operation" As A Stranded Cost. (R.D. at 298)

In its Rebuttal Testimony, Duquesne presented for the first time a stranded cost claim of $208.23 million for what it termed "Costs Independent of Operation." R.D. at 294-95. These are costs which Duquesne claims will be experienced for plants that generate zero or negative present value margins under the Company's analysis and would thus be shut down, except to the extent that continued operation would offset, on a net basis, some of such costs. Thus, these costs are claimed to be "unavoidable" costs associated with such plants, and as shown on Company witness O'Brien's Exhibit MKO-2, represent primarily overheads allocated to these plants which the Company claims could not be avoided.

As discussed in OCA's Briefs, Duquesne's failure to address these operating losses prior to its Rebuttal case and its failure to study its ability to reduce or avoid these operating losses meant that the parties had no realistic opportunity to analyze and study such data, and evaluate the extent to which such costs could be mitigated. See OCA M.B. at 42. Instead, Duquesne's claim is based on Mr. O'Brien's assertion in his Rebuttal Testimony that only 16% of such overheads could be avoided if the plants were shut down. OCA submits that this assertion is unsupported by any sound analysis and should be rejected. The assumption that there are substantial continuing costs associated with plants that provide no economic benefit is an irrational and inappropriate assumption to make in determining stranded costs. The stranded costs associated with generating plants that have no economic value should be limited to the book value of the plant and should not extend to the general operating costs of the utility. Thus, as OCA witness Kahal testified, stranded costs should not "be set on the basis of negative market values" as Duquesne has proposed, but should be limited to a zero market value (except for nuclear decommissioning) if a plant cannot provide any net operating margins. OCA St. 1-S at 11. Duquesne originally proposed such a zero market valuation for such generating plants and OCA concurs in that treatment. As Mr. Kahal explained in his Direct Testimony:

> A negative net present value result must be treated as zero, since to do otherwise would assume a negative market value for the unit. A negative result, however does not necessarily mean that the plant should be retired. It may be economical to continue to operate the plant if operating expenses can be reduced and/or if the plant can operate at higher output levels than included in Mr. Smith's analysis.

OCA St. 1 at 24.

Finally, OCA submits that a large claim such as the Duquesne's claim for costs

independent of operation should have been accompanied by a detailed study of the ability to mitigate such costs and, in the absence of such an analysis, such a novel claim should be rejected.

In his Recommended Decision, ALJ Corbett found that sufficient evidence for this $208 million claim exists in the record of this proceeding. R.D. at 298. OCA submits that the ALJ erred in making such a finding and the claim should be denied. See OCA M.B. at 45-46; OCA R.B. at 12.

EXCEPTION NO. 4: The ALJ Erred In Placing On Ratepayers The Full Burden, Including A Full Return On Capital, Of The Company's Uneconomic Investments, Especially Its Uneconomic Investment In Nuclear Generating Facilities. (R.D. at 432)

This Commission has, in the past, held that ratepayers should not bear the entire burden of uneconomic expenditures by public utilities, even though such expenditures may have appeared prudent at the time the expenditures were made or committed to be made. The Commission's determinations in this respect have been made in decisions and policy statements affecting both the electric and natural gas utilities, and those decisions have been upheld by the courts. For example, with respect to electric utilities, in Philadelphia Elec. Co. v. Pa. P.U. C., 61 Pa. Commw. 325, 433 A.2d 620 (1980), Commonwealth Court upheld the Commission's decision disallowing recovery of the full return on several existing power plants that had previously been included in rates but were then determined to represent excess capacity. Similarly, in Pennsylvania Elec. Co. v. Pa. P.U.C., 509 Pa. 324, 502 A.2d 130 (1985), appeal dismissed sub nom., Metropolitan Edison Co. v. Pa. P.U.C., 476 U.S. 1137 (1986), the Pennsylvania Supreme Court upheld the Commission's decision to exclude from rates the utilities' investment in Three Mile Island Nuclear Station. In another case, the United States Supreme Court upheld the denial of such cost recovery.

In Duquesne Light Co. v. Barasch, 488 U.S. 299 (1989), the Supreme Court upheld a Commission determination denying any return on or recovery of canceled plant costs, even though the costs were admitted by all parties to be prudently incurred.

The Commission's treatment of uneconomic expenditures in the natural gas industry is also instructive with respect to the balancing of ratepayer and shareholder interests. For example, with respect to natural gas utility take-or-pay costs, the Commission denied recovery of carrying costs (except for the period associated with regulatory lag) and conditioned recovery of the principal amount of such costs through an automatic adjustment clause on the public utility's willingness to absorb a portion of the principal balance of such costs. 52 Pa. Code § 69.181. The Commission's treatment denying recovery of carrying costs was upheld in National Fuel Gas Dist. Corp v. Pa. P.U.C., 677 A.2d 861 (Pa. Commw. 1996), where Commonwealth Court held that the denial of carrying costs was consistent with the Commission's discretion to balance shareholder and ratepayer interests. Similarly, with respect to FERC Order 636 transition costs, the Commission has not allowed the recovery of carrying costs on FERC Order 636 Gas Supply Realignment ("GSR") and Stranded Costs passed through by a natural gas utility's interstate pipeline suppliers. See, e.g., Pa. P.U.C. v. National Fuel Gas Dist. Corp., R-00932548, slip op. at 24, 30 (December 1, 1993). The denial of carrying costs with respect to such expenses is consistent with Commonwealth Court's decision in the case of Butler Twp. Water Co. v. Pa. P.U.C., 81 Pa. Commw. 40, 47-48, 473 A.2d 219, 223 (1984), where Commonwealth Court found that it was within the Commission's discretion to disallow recovery of carrying costs on the unamortized balance of unusual and extraordinary expenses.

In this case, Duquesne has claimed that it is entitled to recover both a full return on,

as well as recovery of, its stranded costs, including its own generating plant. OCA has opposed this weighting of shareholder and ratepayer interests and submits that it is imperative that shareholders bear a portion of stranded costs. The reasons that stranded generating plant costs should be shared are explained in OCA's Briefs. See OCA M.B. at 58-61; OCA R.B. at 16-20. As discussed there, the Company's uneconomic investments in nuclear facilities are almost entirely responsible for the Company's stranded costs. Id. Indeed, while the nuclear plants account for only about one-quarter of Duquesne's installed capacity, they are responsible for almost all of its stranded costs. Id. In this light, OCA submits that balancing of ratepayer and shareholder interests is appropriate with respect to recovery of these costs. OCA witness Kahal proposed a reasonable sharing in that ratepayers would bear the principal amount of such costs and the Company would bear the carrying costs of such investment (the return on the unamortized balance) over the CTC recovery period. Id.

In his Recommended Decision, ALJ Corbett rejected OCA's and other intervenors stranded cost sharing proposals, concluding that "any 'sharing' proposal conceptually can be viewed as a 'taking' of assets, subject to constitutional due process constraints" and "could not possibly have been within the contemplation of the legislation." R.D. at 432.

OCA respectfully submits that the ALJ's view that the proposed denial of a return on these assets may be a "taking" in violation of the United States Constitution is inconsistent with the decisions of the Supreme Court of the United States, which clearly establish that it is the end-result of the Commission's Order which must be considered, not the individual elements of that order. Federal Power Comm'n v. Hope Natural Gas Co., 320 U.S. 591, 603 (1944); Duquesne Light Co. v. Barasch, supra. Furthermore, it has long been recognized that rate orders involve a balancing of the interests of both consumers and investors. As the Pennsylvania Supreme Court stated in a rate

case involving Pennsylvania Gas and Water Company:

> [T]he power to fix "just and reasonable" rates imports a flexibility in the exercise of a complicated regulatory function by a specialized decision-making body and that the term "just and reasonable" was not intended to confine the ambit of regulatory discretion to an absolute or mathematical formulation but rather to confer upon the regulatory body the power to make and apply policy concerning the appropriate balance between prices charged to utility customers and returns on capital to utility investors consonant with constitutional protections applicable to both.

Pa. P.U.C. v. Pennsylvania Gas and Water Co., 492 Pa. 326, 337, 424 A.2d 1213, 1219 (1980), cert. denied, 454 U.S. 824 (1981) (citations omitted). This same general guideline was established by the Supreme Court of the United States in cases both preceding and following the Hope decision. For example, in the Natural Gas Pipeline case, the Court stated:

> But regulation does not insure that the business shall produce net revenues, nor does the Constitution require that the losses of the business in one year shall be restored from future earnings by the device of capitalizing the losses and adding them to the rate base on which a fair return and depreciation allowance is to be earned.

Natural Gas Pipeline, 315 U.S. at 590. Perhaps, of more value for this proceeding, Justices Black, Douglas and Murphy, in a concurring opinion, noted their concern that proper consideration be given to the consumer interest. They stated:

> One *caveat*, however, should be entered. The consumer interest cannot be disregarded in determining what is a "just and reasonable" rate. Conceivably, a return to the company of the cost of the service might not be "just and reasonable" to the public.

Natural Gas Pipeline, 315 U.S. 575, 607 (Black, Douglas, and Murphy, JJ., concurring). Notably, in the Duquesne Light case, supra, the Supreme Court upheld the Commission's entire disallowance of the costs of canceled nuclear plants, not just the return on such investment.

As these decisions indicate, the Constitution does not guarantee a utility a profit; nor does it require that rates be set with reference only to the utility's cost of service. To the contrary, the determination of "just and reasonable" rates clearly involves some balancing of ratepayer and investor interests, including consideration of the economics of the utility's investment.

As the Commission decisions disallowing excess capacity and canceled nuclear plants indicate, the economics of investment decisions and the impact on ratepayers of uneconomic investment decisions have played a continuing role in this Commission's policy. The General Assembly has also forwarded this policy through its legislative mandate. Specifically, Section 1315 of the Public Utility Code codified the long-standing principle that electric utility assets which are not "used and useful" in providing service to the public should not be included in rates. 66 Pa.C.S. § 1315. The Electric Competition Act also forwarded this policy by giving the Commission discretion to determine the "just and reasonable" level of recovery of owned-generation stranded costs. It seems reasonable that the General Assembly gave the Commission this discretion to allow it to determine the appropriate balance between ratepayer and shareholder interests, consistent with its previous determinations.

In light of this history of regulatory policy, OCA respectfully submits that the ALJ erred in rejecting OCA's sharing proposal on constitutional grounds and as being inconsistent with the objectives of the Electric Competition Act. Indeed, the legislative history of the Act makes clear that the legislation was not intended to guarantee 100% recovery of and return on stranded cost. 180 Legislative Journal of the Senate of Pennsylvania 2657-89 (November 25, 1996).

The ALJ also placed substantial emphasis in his decision on the Company's argument that the cases cited by OCA involved plants that were closed (TMI) or "physical excess capacity,"

whereas OCA's sharing proposal was based on "economic excess capacity," determined through a comparison of projected market prices to the cost of service associated with such plants. R.D. at 432. OCA submits that neither case law nor the Commission's decisions have indicated that economic excess capacity is to be treated differently than physical excess capacity. Indeed, Section 1323 of the Public Utility Code, 66 Pa.C.S. § 1323, which requires the disallowance of excess capacity costs for new electric generating capacity, addresses both physical and economic excess capacity.

The ALJ's finding that sharing should be rejected because excess capacity has never been previously determined by comparing market price projections to embedded costs is inappropriate. The Electric Competition Act requires that stranded costs be determined in this way in this proceeding. The use of a different methodology for determining when capacity is excess does not change the fact that the stranded costs identified in this case are uneconomical and that the General Assembly has given the Commission the discretion to authorize less than 100% recovery of and return on the utility's owned generation stranded costs.

The ALJ also asserts that "[t]aken to its logical conclusion, no stranded costs could ever be recovered under the sharing proposals, let alone a 'just and reasonable level,' since nearly all of these costs can theoretically be replaced by purchases in the spot market." R.D. at 432. The ALJ's statement misconstrues the basis of the OCA's sharing proposal. As discussed above, OCA's sharing proposal is designed to balance the interests of ratepayers and investors in the recovery of Duquesne's uneconomic investments. OCA submits that that balance is achieved by allowing Duquesne to recover its stranded costs as an amortized expense over the seven year CTC recovery period, without allowing it a return on the unamortized balance of such expense. OCA submits that

sharing is eminently appropriate in this case and should be adopted.

EXCEPTION NO. 5: The Commission Should Clarify That, Under The CTC Methodology Proposed By OCA And Adopted By The ALJ, No Adjustment To Stranded Costs And The CTC Is Necessary To Reflect Treatment Of Distribution Line Losses And Ancillary Services As Costs Functionalized To Generation. (R.D. at 70)

As discussed in OCA's Briefs, the OCA proposed that the costs associated with distribution line losses and ancillary services should be functionalized as generation costs. OCA witness Lee Smith consequently reversed the Company's adjustment moving the costs associated with providing these services to T&D. See OCA M.B. at 9-12; OCA R.B. at 5-6.[1] Thus, the CTC calculated by Ms. Smith was based on stranded costs which included the net generation plant associated with line losses and ancillary services.

Accordingly, Ms. Smith's exhibits reflect the appropriate functionalization of such costs as generation. As she testified, "[t]he CTC that I have proposed will recover all stranded costs including any associated with line losses, since I have already included line losses in the generation stranded costs and not in T&D. Therefore, the CTC requires no modification." OCA St. 4-S at 4.

In his Recommended Decision, the ALJ states that "[t]o the extent a portion of the embedded costs allocated to distribution losses will become potentially stranded, I also recommend they may be included in the CTC." R.D. at 70. OCA simply wishes to make clear that the OCA's calculation of stranded cost already has been increased to include ancillary services and line losses. The OCA has fully reflected the stranded cost effect of this adjustment. Thus, the CTC calculated

[1]Notably, however, West Penn never reduced net generation plant to reflect removal of such costs and no adjustment therefore had to be made by Mr. Kahal in developing his stranded cost number.

by Ms. Smith includes costs associated with line losses and ancillary services that Mr. Kahal found to be stranded.

While Mr. Kahal's stranded cost determination and Ms. Smith's CTC clearly provide for full recovery of line losses and ancillary services, even if this weren't the case, it should be emphasized that the Company included the capacity costs associated with providing line losses in T&D rates based upon estimated market prices for providing line loss service. Thus, there is no basis to assume that there will be additional stranded costs as a result of moving line losses back to the generation function as the ALJ's Recommended Decision considers may be necessary.[2]

EXCEPTION NO. 6: The ALJ's Determination With Respect To Rule 4 Contracts Should Be Clarified. (R.D. at 557)

While the ALJ's decision adopts OCA's recommendation that stranded costs are to be allocated based on the utility production plant allocator used in the Company's last base rate case (R.D. at 557), the ALJ does not specifically address the situation where such an allocation results in a CTC that violates the generation rate cap for discounted rate customers. See OCA M.B. at 66-67, 70; OCA R.B. at 23-25. As discussed in OCA's Briefs, OCA submits that if such a situation arises, the Company must forgo these revenues "unless for good cause shown, it requests and is granted a longer collection period for these classes." Id. In other words, these stranded costs should not be shifted to other rate classes to make up for the shortfall in collection from the discounted rate

[2]OCA's Main Brief incorrectly suggests that there may be additional stranded costs to be recovered as a result of moving line losses back to the generation function. OCA M.B. at 10. OCA here wishes to correct that error; OCA does not believe that there will be additional stranded costs since stranded costs as calculated by Mr. Kahal reflected the net generation plant associated with line losses and ancillary services, and since these costs were included in T&D rates at estimated market prices.

customers. Id.

EXCEPTION NO. 7: The ALJ's Decision To Allow Recovery of Pre-Accrued Nuclear Outage Costs As A Separate Claim Was In Error. (R.D. at 388-89)

ALJ Corbett recommended that the Commission allow recovery for Duquesne's claim for pre-accrued nuclear outage costs as a regulatory asset. R.D. at 388-389. The OCA submits that this recommendation is in error. Importantly, the ALJ adopted the OCA's stranded cost analysis. R.D. at 272-273. As OCA witness Catlin explained, the costs associated with nuclear outages were included in the stranded cost analysis. He explained:

> In determining the stranded costs associated with Duquesne's company-owned generating units, my associate, Mr. Kahal, has relied on the cash flow analysis provided by Duquesne which compares projected market revenues to generating unit operating costs. **The projected operating costs for the Company's nuclear units include the full cost of the maintenance outages in the years the costs are projected to be incurred.** Therefore, there is no basis for including a regulatory asset for the preaccrual of those same costs under the OCA methodology. To do so would result in double-counting of the costs for which the pre-accrual is made.

OCA St. 3 at 11; OCA M.B. at 56 (emphasis added). Since the amount of Duquesne's claim was included elsewhere in the OCA's analysis, to allow the recovery of this item as a regulatory asset double-counts the cost. Therefore, this item should not be included in the Company's claim for regulatory assets.

It is important to note that the OCA does not object to recovery of these costs. However, as explained in its Main Brief and Reply Brief, it was not necessary to include this amount separately in the OCA's regulatory asset analysis. OCA M.B. at 56; OCA R.B. at 16. Simply put, the OCA did not include these costs as a regulatory asset in its analysis, as the costs were recovered

elsewhere. Thus, by accepting the OCA's stranded cost analysis and then allowing recovery of these costs as a regulatory assets, the ALJ has allowed Duquesne to double recover these costs. In order to correct this error, $10.8 million should be removed from the ALJ's regulatory asset findings.

EXCEPTION NO. 8: The OCA Excepts to the ALJ's Determination that Duquesne's Proposed Eligibility and Funding Levels for its Universal Service Programs Comply With the Requirements of the Act and Commission Guidelines. (R.D. at 776)

A. Introduction

At page 776 of the Recommended Decision, ALJ Corbett found that the Company's proposed Universal Service eligibility and funding levels complied with the requirements of the Act and the Commission's Guidelines, and as such, no modification was necessary. R.D. at 776. The OCA excepts to the ALJ's recommendation in this regard. The OCA submits that the proposed funding levels and eligibility guidelines do not meet the requirements of the Act and are not consistent with the Commission's Universal Service Guidelines or the Commission's Order in PECO Energy. Application of PECO Energy for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code and Joint Petition for Partial Settlement, R-00973953, slip op. (December 23, 1997) [hereinafter "PECO Order"], as modified on reconsideration, slip op. (Jan. 16, 1998) [hereinafter "PECO Reconsideration Order"]. For these reasons, the OCA files this exception to the Recommended Decision and requests that the Company be directed to expand its program and modify its eligibility criteria and funding levels, consistent with the recommendations of OCA witness Brockway.

The OCA acknowledges the innovation that is evident in Duquesne's universal service programs. OCA witness Brockway identified the Company's successes in low income usage

reduction, in particular, as "enviable." OCA St. 6 at 13. However, the OCA also recognizes the limitations contained in the program filed by the Company. As Ms. Brockway explained, there is a risk that the approach that the Company has proposed to take will not be successful. She explains:

> There are three reasons why the Company's approach is risky for the Commission and the low-income customers in the Duquesne Light service area. *First*, the Company does not match its commitment to tailor customer services with an adequate budget commitment. *Second*, the failure to adopt target enrollment and benefit amount leaves too much uncertainty about actual levels of CAP service under the plan. *Third*, some of the concepts for "additional services" proposed in the Plan sound like punitive or counterproductive measures that degrade the quality of service a participant receives. Absent further clarification from Duquesne on these points, it would not be prudent to approve the Company's proposal.

OCA St. 6 at 14 (emphasis in original). To that end, OCA witness Brockway made a number of recommendations designed to address the deficiencies in Duquesne's proposed Universal Service filing.

B. Eligibility

Regarding eligibility, the OCA discussed its concerns with the Company's filing in its briefs. OCA M.B. at 81-83; OCA R.B. at 30-31. First, the Company's definition of eligibility for its universal service programs is extremely narrow, and as it is currently proposed, will not meet the needs of the low-income community. OCA witness Brockway recommended that Duquesne broaden its eligibility criteria to include non-delinquent, high-risk customers. This definition will enable a more complete group of at-risk customers to qualify for CAP assistance. OCA St. 6 at 35; OCA M.B. at 81-82. Ms. Brockway recommended using PP&L's proposed list, with two additions. This would then include households where there is/are:

- Injury or illness of primary wage earner,

- High medical bills,
- Loss of job or other reduction in income,
- Abandoned spouse with young children,
- Very low-income elderly,
- Very low-income households with children under school age, and
- Very low-income households with a permanently disabled person residing in the house and requiring personal care for daily living.

OCA St. 6 at 36; OCA M.B. at 82. Her reasoning for the inclusion of these groups is that these categories represent households where "the adult(s) are unable to take on jobs outside the house to increase the family income sufficiently to afford service, and are locked into their very low-income situation so long as these constraints persist." Id.

Expansion of the Company's eligibility criteria is essential in Duquesne's service territory due to the high burden of low-income customers in meeting their electric bills. OCA M.B. at 82. As Ms. Brockway explained, while the median family in Duquesne's service territory spends 2.8% of its income on electricity (4.3% for electric heating customers), a very low-income family can spend **25% of their income** on electricity (38% for electric heat low-income customers). OCA St. 6 at 26; OCA M.B. at 82.

Second, Duquesne did not set specific targets for customer enrollment even though the Company's own estimates show a need to expand services beyond the current levels. OCA St. 6 at 18; OCA M.B. at 82. OCA witness Brockway recommended that the Company strive for a 50% participation rate of the eligible households.

The OCA submits that it is appropriate that Duquesne broaden its eligibility at this

point, and expand its universal service offerings, and should be directed to do so.

C. Funding/Participation Levels

The OCA also submits that the funding levels proposed by Duquesne and adopted by the ALJ do not provide an appropriate level of funding for Duquesne's service territory. Duquesne has proposed to set its Universal Service budget to its current level of spending. OCA M.B. at 83. As OCA witness Brockway explained, this level of funding does not meet the needs of Duquesne's customers. According to Census data, there are approximately 117,000 households in the Duquesne service area with incomes at or below 150% of the federal poverty level. OCA St. 6 at 31-32. In addition, Duquesne has identified about 53,000 low-income customers that meet the Company's definition of "payment-troubled." Id. Therefore, the OCA submits that the Company's universal service budget must be increased, in order to meet the need of Duquesne's service territory.

In considering the Company's CAP program, this would suggest a budget for direct expenditures associated with the program of $550,000. OCA M.B. at 83. OCA witness Brockway explained that this is not sufficient. Her recommendation is to increase funding for the CAP program to serve the OCA's targeted goal of 24,000 participants. This would require funding of $5,725,000, or 0.5% of the Company's gross operating revenues. OCA St. 6 at 32-33; OCA M.B. at 83. Based on the past average gross cost to the Company of CAP participants, and assuming a similar budget requirement under a full scale program, this would provide sufficient funding to serve the estimated number of low-income customers that are currently delinquent in their bill payment. OCA St. 6 at 33.

Ms. Brockway's recommendation for the LIURP program is to gradually increase the $700,000 that the Company currently has budgeted to approximately $2.2 million, or 0.2% of the

Company's gross operating revenues. OCA M.B. at 83. OCA witness Brockway explained that the expansion of the LIURP program is necessary. She stated that while the program has provided services for 6,000 low-income customers to date, "there are upwards of 117,000 low-income households in the service area, and as many as 25,000 to 35,000 payment troubled low-income households." OCA St. 6 at 43; OCA M.B. at 83. However, it is also important to increase program participation gradually, so as not to jeopardize the successful qualities of the program. OCA St. 6 at 43; OCA M.B. at 83.

The OCA submits that the funding levels and eligibility guidelines that the Company has proposed and the ALJ has adopted, do not comply with the requirements of the Act, nor do they meet the standards of the Commission established in PECO Energy, and thus should be modified.

In the PECO Order, the Commission agreed with PECO that enrollment in PECO's CAP and CAP Rate programs should be increased to 80,000, from a current level of 41,000. PECO Order at 142, 146. This will almost double the level of participation of low-income customers in PECO's service territory. However, the Commission also noted that participation of 80,000 customers may not be sufficient, given the 250,000 households at or below 150% of the poverty level, using the latest census data. Id. at 143, 146. Thus, the OCA submits that the Commission approved a significantly expanded program to serve low income customers, to increase the availability of universal service programs to those in need. The OCA submits that it is reasonable for Duquesne to adopt the level of expansion that the OCA has suggested here, rather than continue its current level of funding as proposed by Duquesne.

As explained in the OCA's Main Brief, the Act states that: "The commission shall ensure that universal service and energy conservation policies, activities and services are appropriately

funded and available in each electric distribution territory." OCA M.B. at 79, quoting 66 Pa. C.S. §2804(9). The OCA submits that as proposed by the Company, and included in the Recommended Decision, Duquesne's Universal Service proposal is neither appropriately funded nor reasonably available to its low income customers. Therefore, for the reasons above and contained in the OCA's Main and Reply Briefs, the OCA respectfully requests that the eligibility and funding levels for Duquesne's Universal Service programs be increased to meet an appropriate level of need in the Company's service territory.

EXCEPTION NO. 9: The OCA Excepts to the ALJ's Determination that Duquesne's Proposal for its CAP Program Is Adequate. (R.D. at 805)

In the Recommended Decision, Judge Corbett accepted the Company's proposal for its CAP program, as filed, and found that the proposal conformed with the Act, the Commission's Universal Service Guidelines, and PECO Energy. R.D. at 805. The Judge then recommended that the proposal be approved without modification. The OCA excepts to this determination.

While the OCA recognizes the overall soundness of Duquesne's CAP program, the OCA explained in its Main Brief that certain modifications need to be made to the Company's program, in order to meet the elements of a successful CAP Program, and to effectively promote the goal of universal service. OCA M.B. at 86; OCA St. 6 at 29-38.

First, the Company proposes a tiered structure for determining the copayment for CAP participants. While the OCA supports a tiered structure for maximum copayment for CAP participants for Duquesne, the Company's proposal places a greater burden on general use customers in the higher tier, as the Company makes no distinction between heating and non-heating customers.

The OCA submits that the Company's proposed structure is appropriate for heating customers. However, the OCA recommends adoption of a lower set of burden guidelines for its general use CAP customers, as is enumerated in OCA witness Brockway's testimony, and the OCA's Main Brief. OCA St. 6 at 29-30; OCA M.B. at 86. Thus, the OCA submits that the following matrix provides the appropriate maximum burden by tier for its general use customers: (1) 0-50% of poverty level -- 4% of income; (2) 51-100% of poverty level -- 6% of income; (3) over 100% of poverty level -- 8% of income. Id.

Second, eligibility and funding for Duquesne's CAP program need to be increased, as discussed above, and a target of a 50% participation rate, or 24,000 customers should be established.

Third, in addition to the concerns explained above, Duquesne's program guidelines contain unnecessary barriers to program participation due to a restrictive payment trouble indicia for screening. Therefore, OCA witness Brockway suggested that the Company rely on a modified arrearage screen to target potential customers. OCA M.B. at 87; OCA St. 6 at 33-35. She explains the trouble with the Company's proposal:

> It does make sense to target CAP benefit dollars to the most at-risk customers. The Company goes too far, however, in screening out customers who are at risk of falling behind on their bills and losing service. The Company uses two indicia of payment-trouble to screen potential CAP participants: past-due balance of at least $500, and housing expenses exceeding 45% of the household income. Apparently, a customer must pass both payment-trouble screens to qualify under Duquesne's CAP. Only one payment-trouble screen is needed to ensure proper targeting of CAP benefits.

OCA St. 6 at 34. Ms. Brockway proposed that passing one payment-trouble screen would be sufficient to ensure proper targeting of CAP benefits. Id.

Fourth, OCA witness Brockway recommends reducing the flat $5/month payment towards customer arrearages to $3/month for customers in the lower tiers of the federal poverty level. OCA M.B. at 87; OCA St. 6 at 37.

Fifth, Ms. Brockway recommends that a detailed evaluation of Duquesne's CAP program be done as the Company ramps-up the program from pilot to full-scale status. OCA M.B. at 87; OCA St. 6 at 38.

Finally, the OCA submits that the low income benefits contained in Duquesne's Universal Service plan be made portable so low income customers are able to enjoy the same choice of suppliers as other customers. OCA M.B. at 88; OCA St. 6 at 36.

The OCA submits that the recommendations contained in OCA witness Brockway's testimony will serve to strengthen the program that Duquesne has proposed to the benefit of not only Duquesne's low-income customers, but all ratepayers. Therefore, the OCA submits that it is reasonable for Duquesne to be directed to incorporate these changes into its Customer Assistance Program.

EXCEPTION NO. 10: The OCA Excepts to the ALJ's Determination that Duquesne's Proposal for its LIURP Program Is Adequate. (R.D. at 805)

In the Recommended Decision, Judge Corbett accepted the Company's proposal for its LIURP program, as filed, and found that the proposal conformed with the Act, the Commission's Universal Service Guidelines, and PECO Energy. R.D. at 805. The Judge then recommended that the proposal be approved without modification. While the OCA recognizes the successes of Duquesne's LIURP Program, the OCA excepts to the ALJ's determination and submits that the

Company be directed to increase funding and eligibility levels for its LIURP Program, as discussed above, and to institute a renewables pilot, as discussed below.

EXCEPTION NO. 11: The OCA Excepts to the ALJ's Determination That Duquesne's Renewables Proposal Is Adequate. (R.D. at 805)

In the Recommended Decision, Judge Corbett found that the Company's renewables proposal conformed with the Act, the Commission's Universal Service Guidelines, and PECO Energy. R.D. at 805. The Judge then recommended that the proposal be approved without modification. The OCA excepts to this determination. The Company did not submit a renewables proposal as part of its restructuring plan or in its testimony in this proceeding. Rather, the Company opposed implementation of a renewables pilot. The OCA submits that Duquesne should be directed to include a renewables pilot as part of its LIURP program, as the Commission ordered in PECO Energy.

OCA witness Nancy Brockway specifically included a renewables pilot as a universal service program in her testimony. OCA St. 6 at 43-47. Ms. Brockway's recommendation was designed to specifically address the General Assembly's inclusion of renewable energy programs in the list of potential universal service measures contained in the Act. See, 66 Pa. C.S. §2803. The OCA submits that such inclusion demonstrates the General Assembly's interest in testing the viability of renewable resources in this context.

Ms. Brockway proposed a renewables pilot that would address, not only environmental concerns, but also would help alleviate the need for costly distribution system upgrades, and require very little maintenance or customer/machine interaction. OCA St. 6 at 46; OCA M.B. at 89. The elements of her pilot are as follows:

- Issuing an RFP to solicit proposals to install 10 units of photovoltaic ("PV") electricity panels at 1 kW in 1999, and 20 units of PV in 2000, on the dwellings of low-income customers.
- Seeking bids in a price range of $5.00 per watt.
- Seeking proposals to install up to $50,000 worth of passive or active solar hot water heating.
- Requiring a diversity of building types, locations, land tenancies, sizes and metering arrangements.
- Conducting a process and impact evaluation of the installations, capturing such features as customer acceptance of the measures, landlord acceptance in the case where the customer is a renter, cost per unit, payback per unit, Total Resource Cost on a present value basis per unit, and the like.
- Involving the Universal Service Advisory Committee during pilot development and evaluation.
- Submitting a report to the PUC in 1999 and 2000 regarding the pilot's status and findings, together with recommendations regarding extending or renewing the pilot.

OCA St. 6 at 43-47; OCA M.B. at 88-89.

In PECO Energy, the Commission recognized the importance of the inclusion of a renewables pilot in PECO's Universal Service program, and ordered that one be implemented. PECO Order at 147. As noted above, however, Duquesne did not include a renewables pilot as part of its filing. Instead, Duquesne argued in brief that the Commission's Guidelines do not require the inclusion of a renewables pilot. DLC M.B. at 90. Duquesne also criticized OCA witness Brockway's renewables pilot proposal, particularly the photovoltaic aspect. The Company argued that photovoltaics would not work due to the "cloudy" weather in Pittsburgh. OCA witness Brockway soundly refuted Duquesne's arguments explaining the precise reasons that photovoltaics are ideal for the conditions in Duquesne's service territory. She explained:

> Mr. Flynn's criticisms of that PV pilot are misplaced. First, photovoltaics operate during cloudy periods. While they do not put

> out as much electricity, they continue to generate electricity under a cloud cover. Second, PV is most useful to the system precisely when the system is peaking from heavy air-conditioning load during hot sunny days. Finally, the objective of the pilot, in addition to exploring cost-effectiveness issues, is to explore questions of infrastructure need and suitablility to low-income housing situations.

OCA St. 6R at 10-11; OCA M.B. at 35.

Based on the above reasoning, the OCA submits that the ALJ's decision to not direct Duquesne to include a renewables pilot as part of its Universal Service program is in error. The Commission should direct Duquesne to include a renewables pilot, such as the one contained in OCA witness Brockway's testimony, as part of its Universal Service program.

## III. CONCLUSION

WHEREFORE, OCA respectfully requests that the Commission adopt these Exceptions and enter an Order approving the ALJ's Recommended Decisions as modified in a manner consistent with the above discussion.

Respectfully submitted,

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Dated: April 14, 1998

CERTIFICATE OF SERVICE

Re: Application of Duquesne Light Company for
Approval of its Restructuring Plan Under
Section 2806 of the Public Utility Code
Docket No. R-00974104

I hereby certify that I have this day served a true copy of the foregoing document, Office of Consumer Advocate's Exceptions, 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:

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April 14, 1998

James McNulty, Secretary/Prothonotary
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RE: Application of Duquesne Light Company for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code; Docket No. R-00974104; Docket No. R-00974104C0001-C0004; **EXCEPTIONS OF THE MID-ATLANTIC POWER SUPPLY ASSOCIATION**

Dear Mr. McNulty:

Enclosed, for filing with the Commission, please find an original and nine (9) copies of the Exceptions of the Mid-Atlantic Power Supply Association in the above-captioned proceeding.

All parties to this proceeding are being served with the foregoing documents, in accordance with the Certificate of Service, attached to MAPSA's Exceptions.

If you have any questions concerning the enclosed documents, please direct to me.

Respectfully submitted,



Todd S. Stewart

Counsel for Mid-Atlantic Power Supply Association

TSS/bes
cc: Honorable John H. Corbett, Jr.

3

ORIGINAL

BEFORE THE PUBLIC UTILITY COMMISSION

| | | |
|---|---|---|
| Application of Duquesne Light Company | : | |
| for Approval of its Restructuring Plan | : | Docket No. R-00974104 |
| Under Section 2806 of the Public Utility Code | : | Docket No. R-00974104C0001-C0004 |

# EXCEPTIONS OF THE MID-ATLANTIC POWER SUPPLY ASSOCIATION ("MAPSA")





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Dated: April 14, 1998

TABLE OF CONTENTS

For the sake of convenience, the Mid-Atlantic Power Supply's Exceptions are superimposed upon the Common Outline of Issues which was used by the parties and the ALJ. That Common Outline is reproduced herein in its entirety; the references to specific sections resolved by the ALJ as being excepted to and the page reference refers to the exceptions' location in this document. For example, MAPSA's first exception, regarding the ALJ's proposed timetable for phase-in of customer choice, is found at page "1" of these Exceptions.

## IV. PHASE-IN OF CUSTOMER CHOICE

B. Timetable For Phase-In

**Exception No. 1**

**MAPSA excepts to the ALJ's recommendation of a three-year phase-in period (R. D. At 42) as being contrary to the law as found by this Commission in the PECO[1] decision; rather, MAPSA supports an accelerated phase-in (MAPSA M. B. at 10) as Ordered by the Commission in PECO.**

On page 42 of the Recommended Decision ("R. D."), Administrative Law Judge ("ALJ") Corbett recommends a three-year phase-in period for Duquesne's customers. Citing the arguments raised by GPU Energy ("GPU") and PECO Energy Company Inc. ("PECO"), in this proceeding, the ALJ found that the Commission's decision in PECO -- which required an accelerated phase-in, allowing for full competition in 2 years, as opposed to 3 -- did not adhere to the requirements of the Statutory Construction Act ("Act") and is not based upon a fair reading of the Competition Act, 66 Pa. C.S. §2801, et seq. The ALJ recommends, contrary to the Commission's decision in PECO, that Duquesne's customers be phased-in in successive one-third increments beginning on January 1, 1999, with the final third being phased-in on January 1, 2001.

In PECO, this Commission expressly found that the public interest required the most rapid phase-in allowed by the Competition Act, the Commission also found that a 3-year phase-in period potentially will cause discrimination and/or competitive advantage/disadvantage between similarly situated customers. (PECO, pp. 46-49). The Commission accordingly

[1] In Application of PECO Energy Company for Approval of its Restructuring Plan Under Section 2806 of the Pennsylvania Public Utility Code, Docket No. R-00973953, et al., (Order entered December 23, 1997) ("PECO").

concluded that the best method for eliminating the potential negative effects of a transition is to accelerate the phase-in to the greatest degree possible under the existing statutory framework.

ALJ Corbett questions the Commission's interpretation of 66 Pa. C.S. §2806(b). (R. D. at 43). ALJ Corbett acknowledges, however, that the term "as of" in the statute is capable of two distinctly different interpretations. (Id.) The ALJ then adopts arguments advanced by GPU and PECO that the Statutory Construction Act, 1 Pa. C.S. §1932, requires that statutes be read *in pari materia* so that they are internally consistent. The ALJ's reasoning, however, ignores a fundamental black letter principle of statutory construction, namely, that an administrative agency's expert interpretation of the statute for which it has enforcement responsibility, is entitled to great deference and will not be reversed unless clearly erroneous. Bell Atlantic - Pennsylvania, Inc. v. Pennsylvania Public Utility Commission, Nos. 101 and 107 M.D., Appeal Docket 1996 (Pa. Supreme 1996), Slip Op. at 14. Deference to a prior interpretation of an agency's enabling statute is even more necessary when the statutory scheme is technically complex, as it is in the present case. Bell Atlantic. The ALJ's acknowledgement that two interpretations of the 66 Pa. C.S. §2806(b) are indeed valid, underscores the fact that this Commission can and should be allowed great deference in its interpretation.

Stated slightly differently, this Commission already has interpreted the statute, specifically 66 Pa. C.S. §2806(b), to permit an accelerated phase-in, as approved in this Commission's decision in PECO. MAPSA's position is that the Commission should adopt the same phase-in procedure for Duquesne's customers.

## VII. THE COMPETITVE TRANSITION CHARGE

D. Recommendation

**Exception No. 2**

**MAPSA excepts to the ALJ's use of the OCA's proposed "market price" as a proxy for an appropriate "shopping credit" (R. D. at 554-557); this wholesale price is insufficient to provide for any competitive market, let alone the robust competitive market required by law. (MAPSA M. B. at 29-37).**

The Competitive Generation Credit ("CGC") is the "bogey" against which suppliers must compete. That is, if a supplier cannot deliver energy and the necessary additional services at a price less than the bogey, there will be no suppliers participating in the competitive market in Duquesne's service territory. The ALJ proposed a competitive generation credit, or "shopping credit," for use in Duquesne's service territory, which is equal to the "market price" proposed by the OCA in this proceeding. (R. D. at 559). The OCA's proposed "market price" will not produce any competition. First, the OCA's proposed "market price" is barely more than a wholesale energy price. As the record indicates, a fully-delivered retail price must allow suppliers to recover: the value of capacity adjusted to load factor of customer classes; the value installed reserves adjusted to load factor of customer classes; the cost of ancillary services; marketers costs; home office overheads; losses; and, profit. (MAPSA St. No. 1, p. 32; MAPSA M. B. 35-36). These costs are in addition to recovering the wholesale price of energy.

The second reason the OCA's proposed "market price" will fail to develop a robust competitive market is that the OCA's rate design methodology was calculated to produce immediate rate decreases for all Duquesne customers, regardless of whether those customers choose to participate in the competitive market. (OCA St. No. 4, at 16). The OCA's proposed

market price obtained discounts for all customers by lowering the level of the CGC. This dynamic was expressly rejected by the Commission in PECO and is contrary to law. In PECO, the Commission found that customer savings, if they are indeed to occur, must be the result of competition and that the Competition Act did not have immediate rate reductions for all customers as one of its goals. (MAPSA Reply Brief at 3).

MAPSA recommends adoption of the methodology for calculating an appropriate CTC/CGC, that was followed by this Commission in PECO. In PECO, the Commission used the following methodology:

- First: Calculate the electric utility's stranded costs in accordance with the record evidence and the methodology set forth in PECO.
- Second: Derive a CTC to collect those reasonable and non-mitigatable costs over an appropriate period (for example, the 9-year period provided for in 66 Pa. C.S. §2808(b)).
- Third: Calculate the appropriate T&D rates.
- Fourth: Mathematically calculate the CGC, by adding the transmission, distribution and CTC charges, and subtracting the total of these three charges from the level of rates in effect on January 1, 1997.
- Fifth: Determine whether the resulting CGC will allow for competition, based upon the record evidence of what a fully-delivered retail price of power is.
- Sixth: Make appropriate adjustments to the CTC/CGC if the CGC (shopping credit) is not large enough to allow for competition.

(MAPSA, M. B. at 33).

The essential step in setting a CTC/CGC is to ensure that the CGC is sufficient to allow for a robust competitive market (Steps 5 and 6, above). Without competition, there are no stranded costs and a CTC is unnecessary. MAPSA has presented sufficient evidence as to the necessary level of a CGC, and measured by that standard, the OCA's proposed "market price" is not sufficient to that purpose and should be rejected.

In order to have competition, the CGC, or "shopping credit," must be in the range of 2.9¢/kWh, for 100% load factor power, to 4.1¢/kWh, for 50% load factor power (i.e., if the residential shopping credit is not at least 4.1¢/kWh, there will be no shopping by residential customers). (MAPSA Exhibit No. 1). For example, in this case, if the Commission were to determine that, as MAPSA believes they should, the appropriate CGC should be somewhere in the range of 2.9¢ to 4.1¢/kWh, as has been proposed by MAPSA, it may be necessary to extend the recovery period for stranded costs, or levelize the recovery mechanism.

## X. COMPETITIVE SAFEGUARDS

### A. Code of Conduct

**Exception No. 3**

**MAPSA excepts to the ALJ's recommendation to modify Duquesne's proposed Code of Conduct in order to bring that Code into compliance with this Commission's decision in PECO (R. D. at 627-628); rather, MAPSA's position is that the entire final Code of Conduct adopted by the Commission in PECO should be adopted as the appropriate Code of Conduct for Duquesne on an interim basis.**

At page 627 of the Recommended Decision, the ALJ recommends that Duquesne modify its proposed Code of Conduct to bring that Code of Conduct into accord with the Commission's Order in PECO. MAPSA submits that, rather than requiring that Duquesne modify its proposed

Code of Conduct, the exact Code required by the Commission in PECO should be implemented here as well. The final language as approved by the Commission, PECO (Order on Revised Compliance Filing; entered February 26, 1998, p. 21), represents the appropriate content of an Interim Code of Conduct which would be applicable until final regulations are adopted.

## XI. DUTY TO SERVE

C. Electric Transmission & Distribution Service

(d) Specific Services

(i) Customer Billing

**Exception No. 4**

**MAPSA excepts to the ALJ's recommendation (R. D. at 718) which refuses to implement, in this proceeding, the "third" bill option which would permit electric generation suppliers to bill for both energy charges and for the EDC's charges; rather, MAPSA asserts (MAPSA M. B. at 40) that the competitive provision of billing service is necessary to promote a truly competitive market.**

In the Recommended Decision, the ALJ refuses to recommend the adoption of a "third" bill option, which would permit customers to receive a single bill from an EGS that includes billing for EDC charges as well as for EGS charges. (R. D. at 718). The ALJ reasoned that the option could not be determined on the basis of this record and should await the results of a generic rulemaking on this subject. This was a similar approach to that adopted by the Commission in PECO. The ALJ, however, fails to acknowledge that the record in this case does contain evidence supporting the adoption of a "third" bill option in Duquesne's service territory. (See, MAPSA St. No. 1 at 42 and Attachment I; Enron Statement 4.0 at 8-9).

Allowing suppliers to provide a single bill will remove Duquesne as a monopoly provider of this service, which is not necessarily a monopoly service. Additionally, it will allow for the further development of competitive alternatives and bring additional value to customers who seek those alternatives. Therefore, this Commission should reconsider its decision to postpone the ultimate resolution of this issue until a generic proceeding and should order Duquesne to unbundle billing services and allow the competitive provision of those services.

(i) Metering

**Exception No. 5**

**MAPSA excepts to the finding of the ALJ which allowed for customers to request the use of a qualified meter (R. D. at 724); rather, MAPSA has argued that all metering services should be capable of competitive provision (MAPSA M. B. at 40) and that the EGS should be able to own, supply and read a customer's meter at the customer's delivery point.**

The ALJ has recommended that the Commission allow the customer, in conjunction with their EGS, to request the use of qualified meter. (R. D. at 724-725). MAPSA has requested in this proceeding that the Commission not only allow the customer to choose an advanced meter, but, also to allow the EGSs to provide metering services, and to unbundle metering service from the regulated rates of customers. (MAPSA M. B. at 40). In a competitive market, those services which are easily susceptible of competitive provision, should be unbundled and should be provided competitively. This allows customers the maximum flexibility in selecting the menu of services which they wish to procure from various suppliers and ultimately will result in the lowest prices to consumers for those services. By allowing Duquesne to maintain metering as a monopoly function when it is not necessarily a monopoly function, the ALJ only precludes

customers from having the choice of the provider of that service. Not allowing competition will not allow competitive forces to maintain the lowest possible price for that service. MAPSA urges this Commission to require Duquesne to unbundle metering services and to allow the competitive provision of those services by EGSs.

## CONCLUSION

Wherefore, MAPSA respectfully requests that this Commission **grant** its foregoing Exceptions to the Recommended Decision of ALJ Corbett in this matter.

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DATED: April 14, 1998

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April 14, 1998

James J. McNulty, Secretary
Pennsylvania Public Utility Commission
Room B-20, North Office Building
Harrisburg, PA 17120

**VIA HAND DELIVERY**

**Re: Application of Duquesne Light Company for approval of Restructuring Plan Under Section 2806 of the Public Utility Code; Docket No. R-00974104**

Dear Secretary McNulty:

Enclosed for filing are the original and nine (9) copies of the Exceptions of the Duquesne Industrial Intervenors ("DII") in the above-referenced proceeding.

As evidenced by the attached Certificate of Service, all parties are being duly served with the exceptions. Please date stamp the extra copy of this letter and return it for our filing purposes.

Very truly yours,

McNEES, WALLACE & NURICK

By Pamela C. Polacek
Pamela C. Polacek

Counsel to the Duquesne Industrial Intervenors

PCP/clc
Enclosures
c: Administrative Law Judge John H. Corbett, Jr. (via Federal Express on 4/13/98)
Cheryl W. Davis, Office of Special Assistants (w/diskette) (via hand delivery)
Certificate of Service

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BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

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| PENNSYLVANIA PUBLIC UTILITY COMMISSION, ET. AL. | : | |
| v. | : | |
| | : | DOCKET NO. R-00974104 |
| DUQUESNE LIGHT COMPANY FOR APPROVAL OF ITS RESTRUCTURING PLAN UNDER SECTION 2806 OF THE PUBLIC UTILITY CODE | : | |

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**EXCEPTIONS OF THE**
**DUQUESNE INDUSTRIAL INTERVENORS – COMPLAINANTS**

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BOC Gases
General Motors Corp.
J&L Specialty Steel, Inc.
LTV Steel Company, Inc.
Nabisco Inc.
Nova Chemicals, Inc.
USX Corporation - US Steel Group





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Counsel to the Duquesne Industrial Intervenors

Dated: April 14, 1998

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## TABLE OF AUTHORITIES

## I. INTRODUCTION

On March 25, 1998, Administrative Law Judge John H. Corbett, Jr., issued the Recommended Decision ("R.D.") in this proceeding. Pursuant to 52 Pa. Code § 5.533 and the established procedural schedule, the Duquesne Industrial Intervenors ("DII"), a party in this proceeding, respectfully submits these Exceptions to the ALJ's well-reasoned R.D. DII submitted both Main and Reply Briefs ("DII M.B." and "DII R.B.", respectively) in this proceeding. DII respectfully urges the Pennsylvania Public Utility Commission ("PUC" or "Commission") to modify the R.D. consistent with the following arguments.

## II. EXCEPTIONS

### 1. The ALJ Inappropriately Rejects The Accelerated Phase-in Proposal Advocated by DII and Accepted by the Commission in the PECO Restructuring Proceeding.

Exception to: R.D. at 30-43 & 829-30; Ordering ¶ 3.

The ALJ adopts the following schedule for the phase-in of direct access in Duquesne's service territory: one-third of the peak load of each customer class will have the opportunity for direct access on January 1, 1999; another one-third of the peak load of each customer class will have the opportunity for direct access on January 1, 2000; and, all of Duquesne's customers will have the opportunity for direct access on January 1, 2001. R.D. at 42-43 & Ordering ¶ 3.

The ALJ rejects the accelerated phase-in schedule that is advocated by DII (and other parties). See DII M.B. at 8-9; DII R.B. at 4-5. Under the DII proposal, one-third of the peak load of each customer class will have the opportunity for direct access on January 1, 1999; another one-third will have the opportunity for direct access on January 2, 1999; and, all of Duquesne's customers will have the opportunity for direct access on January 2, 2000. Id. An identical accelerated phase-in proposal was adopted by the Commission for the phase-in of direct access in

the PECO service territory. Application of PECO Energy Company for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code and Joint Petition for Partial Settlement & Petition of Enron Energy Services Power, Inc. for Approval of an Electric Competition and Choice Plan and for Authority Pursuant to Section 2807(E)(c) of the Public Utility Code to Serve as the Provider of Last Resort in the Service Territory of PECO Energy Company, Docket Nos. R-00973953 & P-00971265, Opinion and Order entered on December 23, 1997, 181 PUR 4th 517, 542 ("PECO Restructuring Order").

DII respectfully excepts to this portion of the R.D. and requests that the Commission's Order in this proceeding incorporate the accelerated phase-in schedule. As DII explains fully in its Main Brief, the language of the Act clearly permits the adoption of an accelerated phase-in schedule. DII M.B. at 8-9. The Act establishes threshold dates by which a maximum participation target must be attained; the Act does not establish a rigid schedule of one-year periods during which only a minimum amount of load can have the opportunity for direct access. Id. In addition, in implementing the Act the Commission must consistently decide a critical issue such as the schedule for the phase-in of direct access.

The parties in this proceeding advance multiple interpretations of the phase-in provision of the Act. If the words of a statute are ambiguous or subject to multiple meanings, the agency or court construing the statute may look to the legislative intent to interpret and implement the statute. 1 Pa. C.S.A. § 1921(c). The ALJ recognizes the reasonableness of DII's interpretation of the Act, which was adopted by the Commission in the PECO proceeding.

> The confusion on this issue arises from the question of how to interpret the words "as of," which appear at the beginning of subparagraphs (b)(1), (2), and (3) of Section 2806 of the Act. 66 Pa. C.S. § 2806(b)(1), (2) & (3). As the record in this case demonstrates, the term "as of" can have two distinctly different meanings. "As of" may mean "at the least," which the Commission apparently attributed to the phase-in schedule in PECO Energy. On the other hand, an equally reasonable interpretation for "as of" may mean "beginning on."

R.D. at 42-43 (emphasis added). DII respectfully submits that a better categorization of the Commission's interpretation of the phrase "as of" in the PECO proceeding is that the phrase means "on" or "by." Regardless of the categorization, by the ALJ's admission, the words of the Act are susceptible to multiple meanings. Id. at 43. Consequently, it is proper for the Commission to interpret this provision of the Act in a manner that furthers the goals of the Act. 1 Pa. C.S.A. § 1921(c).

As the Commission recognized in the PECO decision, the accelerated phase-in schedule maximizes customer access to the competitive market and minimizes possible competitive disputes. PECO Restructuring Order, 181 PUR 4th at 542. Accelerating customer access to the retail generation market facilitates the development of a robust generation market, which is one of the core purposes of enacting Chapter 28. 66 Pa. C.S. §§ 2804 & 2806. Increased participation in retail access encourages competitive forces that promote an efficient generation market and lower electricity prices. In addition, accelerating the phase-in schedule "remedies the mischief" of competitive disadvantages developing during phase-in among similarly situated customers within and outside Duquesne' service territory. Applying the rules of statutory construction leaves no doubt that the General Assembly acknowledged the vast benefits of transitioning to a competitive market, that reasonable acceleration of that transition is in the public interest, and that the Commission has the statutory discretion to implement that accelerated transition.

The accelerated phase-in does not "cut[] one full year (minus one day) out of the phase-in schedule established in Section 2806(b)." See R.D. at 38. Rather, the accelerated phase-in is fully consistent with the letter and spirit of the Act. The public interest clearly supports adoption of the accelerated phase-in schedule for Duquesne's ratepayers.

Furthermore, adoption of a schedule different from the schedule adopted for PECO's customers will be inequitable and unfair. Duquesne's customers deserve the identical opportunity to access the competitive market as PECO customers. See 66 Pa. C.S. § 2802(8). Although the ALJ relies heavily on the PECO precedent in making recommendations on other issues (see e.g., R.D. at 272-73 (citing adoption of the OCA's PJM market price forecast in the PECO proceeding as support for adoption of the OCA's ECAR market price forecast)), the ALJ declines to rely on the PECO precedent for this issue. DII respectfully submits that a core issue such as when the ratepayers will have the opportunity for direct access to the competitive market, must be decided on a uniform basis throughout the state. Although PECO is challenging the accelerated phase-in on appeal (see R.D. at 42), DII submits that the prudent course of action is to uniformly apply the accelerated phase-in schedule. In the event the accelerated schedule is overturned on appeal, then the schedule for PECO and Duquesne can be modified.

The ALJ's rejection of the accelerated phase-in schedule is contrary to established Commission precedent. In addition, the language of the Act can reasonably be read to permit the accelerated schedule. DII respectfully requests the Commission modify the R.D. and institute an accelerated phase-in schedule in the Duquesne service territory.

**2. The ALJ Errs In Not Recognizing the DII Market Price Forecast and Market Value for Duquesne's Generating Units as a Check on the Reasonableness of the OCA Analysis.**

The ALJ's preferred method for establishing Duquesne's asset market value is through an auction. R.D. at 159-60. In the event the auction of Duquesne's generating assets is not completed within 18 months, the R.D. establishes the market value of Duquesne's generating units based on the OCA market price analysis. R.D. at 272-73. In adopting the OCA valuation, the ALJ notes the Commission's acceptance of the OCA's market value analysis in the PECO proceeding. Id.

DII also presents a market price forecast for the ECAR region and a market value of Duquesne's generating units. DII M.B. at 30-39. DII submits that the forecast and valuation performed by Mr. Falkenberg are reasonable. DII urges the Commission to recognize the DII analysis as a favorable check on the reasonableness of the OCA forecast and valuation.

As DII explains fully in its Main Brief, the asset value methodology used by DII calculates the stranded cost related to Duquesne's generating units by comparing the book value of the units to the anticipated profit the units will earn in a competitive market (i.e., the difference between the market price for electricity and the operating costs of the units). DII M.B. at 34-35. This produces the price a hypothetical buyer would offer Duquesne for those units if the Company were to sell the units today. Id. This is the same methodology used to determine the amount of stranded generation costs that PECO will be permitted to recover under the Act. See PECO Restructuring Order, 181 PUR 4th at 555-59.

The DII market price analysis is a reasonable forecast of the future market prices for electricity in the ECAR region. Three elements should be considered in evaluating a market price forecast: (1) the forecasting methodology and model; (2) the inputs to the model; and, (3) the results obtained from the analysis. DII M.B. at 35-39. DII uses a proper forecasting methodology (i.e., a model designed to predict prices in a competitive electricity market). Id. at 35-36. DII uses reasonable and independently derived inputs. Id. at 36-38. Finally, the results obtained from the DII forecast are reasonable. Id. at 38-39. DII submits that its forecast of future market prices is reasonable.

The ALJ notes the acceptance of the OCA market price analysis in the PECO proceeding as supporting adoption of the OCA analysis in this proceeding. R.D. at 272-73. As DII notes regarding many issues, consistency with the PECO precedent is extremely important. Based on comparison to the DII forecast, DII asserts that the OCA's forecast is reasonable for use by the Commission in this proceeding. Specifically, DII recognizes the prudence of using the ENPRO model to forecast market conditions for both regions.

DII submits that Mr. Falkenberg's market price forecast in this proceeding is a balanced and objective analysis of the future market prices in the ECAR region. The Commission in PECO focused on the overall balance of Mr. Smith's analysis of the PJM region, but found "substantial merit" in several of Mr. Falkenberg's recommendations. PECO Restructuring Order, 181 PUR 4th at 559. DII respectfully urges the Commission to also recognize the expertise of Mr. Falkenberg by relying on DII analysis as a check on the reasonableness of the OCA analysis.

### 3. The ALJ Errs in Permitting Duquesne to Recover Purported "Costs Independent of Operation."

Exception to: R.D. at 294-98 & 834.

The ALJ recommends that Duquesne be permitted to recover $208.23 million for "Costs Independent of Operation." R.D. at 298. DII respectfully submits that Duquesne has not fulfilled its burden of proof regarding the existence of these costs; thus, DII respectfully excepts to this recommendation.

As DII explains in its Main Brief, these costs purportedly reflect costs that will be incurred regardless of whether the unit is operated at generating units showing a negative margin under Duquesne's NPV analysis. DII M.B. at 45. Although Duquesne presents a margin analysis in its direct case and fails to claim such costs, the ALJ recommends recovery of the costs based on the Company's claim in its rebuttal testimony. R.D. at 294-98.

These costs could have (and should have) been included in the Company's claim made in its case-in-chief. The Company did not do so. Failure to include a claim for the costs in its direct case prevented the parties from adequately exploring the basis for the purported costs independent of operation. Thus, although the evidence that has been submitted may favor recognition of the claim, DII asserts that the parties have had an inadequate opportunity to introduce additional evidence against recognition because of the Company's belated introduction of the issue. See OCA Statement 1-S at 6-8. DII submits that the Company's failure to fully state its claim for these costs in its case-in-chief prevents the proper recovery of these costs in this proceeding. DII respectfully requests that the R.D. be modified to deny recovery for "Costs Independent of Operation."

**4. The ALJ Errs in Endorsing Duquesne's Proposed Modifications to the Economic Development Rates in Riders 8 and 20.**

Exception to: R.D. at 599-605 & 839; Ordering ¶ 8.

The R.D. endorses Duquesne's proposal to phase-out economic development incentive rates available to existing customers under Riders 8 and 20 in its current tariff. R.D. at 604-05. In support of this recommendation, the R.D. cites the availability of the competitive market to provide the same economic development incentives. Id. DII respectfully excepts to this recommendation and requests the Commission modify the R.D. to continue the availability to existing customers of Riders 8 and 20 during the entire transition period.

As DII explains fully in its Main Brief, the Act requires that Riders 8 and 20 remain available to existing customers throughout the transition period. DII M.B. at 90-92. Elimination of the Riders prior to the end of the transition period will result in existing customers on those riders paying generation charges above the price those customers were paying on January 1, 1997. Id. at 90. This increase to a customer's charges violates the Act's express mandate that the generation component of charges is capped at the January 1, 1997, level for the entirety of the transition period. 66 Pa. C.S. § 2804(4)(i).

The ALJ notes that access to competitive supply will provide customers with benefits equivalent to the economic development incentive rates. R.D. at 604-05. DII submits that the opportunity to gain access to competitively priced electricity is irrelevant to the availability of the rate cap. If the ability to access competitive supply were sufficient to eliminate the protection of

the rate cap, then all customers should logically lose the protection of the cap when they have access to competitive supply. This result is directly contrary to the mandates of the Act and must be rejected. See 66 Pa. C.S. § 2804(4)(i).

In addition, contrary to the ALJ's impression as expressed in the quotation of the PECO decision (R.D. at 604-05), the Commission required PECO to continue offering existing economic development rates such as its Economic Efficiency Rider ("EER") throughout the transition period. PECO Restructuring Order, 181 PUR 4th at 570. In order to fairly and equitably implement restructuring on a state-wide basis, the Commission should mandate that Duquesne continue to offer its customers the equivalent economic incentives in its Riders 8 and 20. See 66 Pa. C.S. § 2802(8).

DII respectfully submits that the R.D. must be modified to require Duquesne to continue the availability of the economic development incentive rates for existing customers in Riders 8 and 20 throughout the transition period. The Duquesne proposal to phase-out economic development incentive rates for existing customers must be rejected.

**5. The ALJ Inappropriately Permits Duquesne to Recover its Claimed Regulatory Asset for Unamortized Debt Costs.**

Exception to: R.D. at 354-361 & 835.

The ALJ permits the Company to recover a stranded regulatory asset for "Unamortized Debt Costs." R.D. at 361. The ALJ recommends that the OCA's calculation of this regulatory asset be accepted. Id. The OCA also makes an adjustment to the Company's claimed cost of debt regarding these costs. OCA M.B. at 52-53. It is unclear whether the ALJ is also recommending acceptance of the OCA cost of debt adjustment. R.D. at 361. In its briefs, DII argues that the

entire claim for unamortized debt costs should be denied because the costs are being recovered elsewhere in Duquesne's quantification of its stranded costs. DII M.B. at 53-55; DII R.B. at 27-28. DII respectfully excepts to the ALJ's recommendation that permits Duquesne to recover this regulatory asset.

As DII explains in its Main Brief, the Company's claim for unamortized debt costs has two components: (1) the unamortized premium on reacquired debt; and, (2) debt issuance expense. Id. at 53. Both components are currently recovered by the Company as costs of debt. Id. The Company's claim for a stranded regulatory asset is improper because the Company fails to remove these costs from its cost of debt. Id. at 53-54. The Company's stranded cost claim is inflated because of the continued inclusion of these costs in its cost of debt. Id. at 54. Thus, the claimed stranded regulatory asset is not a "net electric generation-related" cost pursuant to the Act. See 66 Pa. C.S. § 2803.

Duquesne is compensated for unamortized debt costs in the stranded generation cost portion of its filing; consequently, it is improper double recovery for the Company to also receive a stranded regulatory asset for the costs. DII submits the R.D. should be modified to prevent this double recovery by denying the Company's claim for the unamortized debt cost regulatory asset. In the alternative, the Commission must adopt the OCA's concurrent adjustment that removes these costs from the Company's cost of debt.

**6. The ALJ Errs in Permitting Duquesne to Recover a Stranded Regulatory Asset for Deferred Employee Costs.**

Exception to: R.D. at 370-374.

The R.D. grants the Company's full request for its claimed regulatory asset of "Deferred Employee Costs" because the claim "appears justified on this record." R.D. at 374. DII respectfully excepts to the ALJ's finding and conclusion. The Company's claim for deferred employee expenses is improper because these costs are not "stranded" by the movement to competition and because recovery of these costs is provided for elsewhere in Duquesne's stranded cost calculation.

As DII explains in its briefs, the claimed deferred employee expenses are not stranded by the movement to competition. DII M.B. at 58-60; DII R.B. at 29. The deferrals, which are created by the accounting treatment of these costs, will reverse at some point in the future. Id. When the accounting treatment reverses, Duquesne will be fully compensated for any employee cost it claims is "stranded". Id.

Although all regulatory assets are created by timing differences that will reverse in the future, a regulatory asset must be "stranded" to be recoverable in this proceeding. DII R.B. at 29; 66 Pa. C.S. § 2803. A cost is stranded if it is "typically . . . recoverable under a regulated environment but . . . may not be recoverable in the competitive electric generation market." 66 Pa. C.S. § 2803. The employee costs claimed in this regulatory asset will be recovered by the Company in the competitive environment. DII M.B. at 58-60; DII R.B. at 29. Consequently, the costs are not stranded and recovery is not permissible under the Act. See 66 Pa. C.S. § 2803.

In addition, these deferred employee costs have been inflated each year into the future and included as part of the Company's stranded generation cost quantification. DII M.B. at 59-60. Consequently, if the claimed regulatory asset is permitted, the Company will double recover for these costs. This double recovery is contrary to the Act, which defines "stranded costs" as "net" costs. 66 Pa. C.S. § 2803. The R.D. recognizes that costs recovered in multiple parts of the stranded cost claim are not "net" costs under the Act. R.D. at 347-48. Because, as DII illustrates, deferred employee costs will be recovered in the stranded generation cost part of Duquesne's claim, the regulatory asset should be disallowed.

The Company's claimed stranded regulatory asset for deferred employee expenses is improper under the Act because the costs are not rendered unrecoverable by the transition to the competitive market. In addition, the costs are not net electric costs because Duquesne will be compensated for identical expenses in its stranded generation costs. DII respectfully requests the Commission modify the R.D. to disallow recovery of the deferred employee costs.

### 7. The ALJ Errs in Permitting Duquesne to Recover a Stranded Regulatory Asset for Pre-Accrued Nuclear Outage Costs.

Exception to: R.D. at 385-388 & 836.

The Company requests recovery of a regulatory asset related to a unilateral change by the Company in the accounting treatment of nuclear outage costs. The R.D. recommends recovery of $10.29 million (NPV) by the Company for this regulatory asset. R.D. at 388-89. The ALJ states: "The transition to a competitive market justifies a change in accounting methods for this asset." Id. at 388. DII excepts to this finding.

The costs represented by this regulatory asset are not stranded by the movement to the competitive market. As DII explains, the Company will be made whole for the deferral when the pre-accrual reverses in the last year of the asset life. DII M.B. at 63; DII R.B. at 30-31. Consequently, the costs will be recoverable in the competitive market and do not qualify under the Act's definition of "stranded cost." See 66 Pa. C.S. § 2803. The reasonableness of the accounting change is irrelevant to the issue of whether these costs will be recovered by the Company in the competitive market.

As DII illustrates, the Company will otherwise receive compensation for the pre-accrued nuclear outages in the final year of the asset's life. DII M.B. at 63. Consequently, recovery of pre-accrued nuclear outage costs as a stranded regulatory asset in this proceeding is improper under the Act. DII respectfully requests the Commission modify the R.D. to disallow recovery for the pre-accrued nuclear outage cost regulatory asset.

**8. The ALJ Errs in Rejecting The DII Proposal for Sharing Stranded Costs Between Ratepayers and Shareholders.**

Exception to: R.D. at 409-32 & 837.

DII argues that the Act requires the Commission to use its discretion to determine the amount of stranded costs that are just and reasonable for Duquesne to recover from ratepayers. 66 Pa. C.S. §§ 1301, 2804(13), 2804(14) & 2808(c); DII M.B. at 22, 27-28 & 69-70. This discretion enables the Commission to consider whether any stranded generation costs should be shared between Duquesne's ratepayers and shareholders. The R.D. rejects the DII proposal and other sharing proposals advocated by the OCA and the Environmentalists. R.D. at 432. DII

excepts to this portion of the R.D. and requests the Commission institute the equity return disallowance advanced by DII and other parties in order to arrive at a just and reasonable level of recoverable stranded costs.

The Act clearly establishes that only a "just and reasonable" level of properly claimed and quantified stranded costs is recoverable through the CTC. 66 Pa. C.S. §§ 1301, 2804(13) & (14); DII M.B. at 22, 27-28 & 69-70. The Act states that the Commission "shall allow recovery" of properly claimed and quantified regulatory assets and NUG costs. 66 Pa. C.S. §§ 2808(c)(1) & (2). Regarding stranded generation costs, however, the Commission "shall determine the level of other generation-related transition or stranded costs that may be recovered through the competitive transition charge." Id. § 2808(c)(3). The use of different language to address the Commission's duty regarding stranded generation costs must be construed as authorizing different treatment for stranded generation costs.

The Commission recognized that this difference in statutory language mandates disparate treatment of the types of stranded costs. PECO Restructuring Order, 181 PUR 4th at 563. This statutorily authorized disparate treatment empowers the Commission to employ its "discretion under Sections 2804(13) and (14) to disallow recovery of a portion of accurately quantified 2808(c)(3) stranded costs." Id. This discretion is exercised after the Commission considers the utility's mitigation efforts and the other criteria in Section 2808(c). (See id.: "Although we conclude that PECO's efforts to mitigate stranded costs have been inadequate, we do not exercise our discretion . . . .")

The ALJ notes that none of the cases cited by DII and the OCA to support the sharing proposals directly control the Commission's decision on this issue. R.D. at 432. DII submits that

the lack of solid precedent supporting the proposals is not due to some "fatal flaw" of the DII proposal (id.); rather, the lack of solid precedent supporting the sharing proposal is due to the novelty of the situation at hand. Before adoption of the Act, the Commission had not been faced with a statutory mandate to determine an amount of stranded costs that a utility is entitled to recover because of the transition to a competitive market environment. DII offers the citations to prior Commission and judicial decisions supporting use of an equity return disallowance as one possible source of guidance for the Commission in reaching a decision on this novel issue.

The Act clearly requires the Commission to approve a CTC that recovers only a just and reasonable amount of stranded costs from ratepayers. 66 Pa. C.S. §§ 2804(13), 2804(14), 2808(c) & 1301. If the Commission, in using its regulatory discretion, decides that it is not just and reasonable to recover all of Duquesne's properly claimed and quantified stranded costs from ratepayers, then DII submits that the equity return disallowance applied to stranded generation costs is a reasonable method to arrive at a just and reasonable amount. See DII M.B. at 69-71.

In addition, the ALJ inappropriately considers whether the sharing of stranded costs permitted by the Act is a "taking" under constitutional jurisprudence. R.D. at 432. The Commission must be concerned only with interpreting the words of the Act and adhering to the guidance provided by the General Assembly. Borough of Green Tree v. Board of Property Assessment, 459 Pa. 268, 328 A.2d 819 (1974); Philadelphia Life Ins. Co. v. Commonwealth of Pennsylvania, 410 Pa. 571, 190 A.2d 14 (1963). Although the Commission must consider constitutional principles in implementing the Act, the PUC's primary focus must be on fulfilling the General Assembly's intention as expressed in the Act. The Act clearly contemplates sharing

of stranded costs. The determination of whether the Act is an unconstitutional "taking" because it permits a sharing of stranded generation costs must be addressed by the appellate courts. As the Supreme Court stated in Green Tree:

> [T]he determination of the constitutionality of enabling legislation is not a function of the administrative agencies thus enabled.

459 Pa. at 281, 328 A.2d at 825.

Furthermore, as DII explains in its Reply Brief, employing the equity return disallowance is neither arbitrary nor an "opportunistic switching" in ratemaking standards. DII R.B. at 35. The equity return disallowance uses Duquesne's own debt structure to determine the amount of stranded generation costs to be shared by the shareholders. Certainly, basing the amount of stranded cost to be shared by the shareholders on the Company's debt structure is not arbitrary. Id. In addition, the Commission would not be engaged in "opportunistic switching" from the Commission's treatment of the Fort Martin sale. See R.D. at 411 (citing Duquesne Light Co. v. Barasch, 488 U.S. 299 (1989)). The Commission's actions in the Fort Martin proceeding involved approval of a settlement determining how the proceeds from the Fort Martin sale would be handled. As part of that settlement, the Company agreed to accelerate the amortization and depreciation of assets rather than to increase shareholder returns. Thus, the Fort Martin situation involved a very different procedural and factual situation than exists regarding the Commission's actions implementing this landmark legislation in the context of a fully litigated proceeding.

The United States Supreme Court in Barasch specifically recognized that no single ratemaking methodology rises to constitutional levels. Id. at 316. In other words, the propriety

of a ratemaking methodology is not "cast in stone" simply because of use in one proceeding. Rather, state commissions have latitude to balance the interests of the utility and ratepayers in adopting changes to ratemaking methodologies. Id. The Court stated:

> The adoption of a single theory of ratemaking as a constitutional requirement would unnecessarily foreclose alternatives which could benefit both consumers and investors. The Constitution within broad limits leaves the States free to decide what rate setting methodology best meets their needs in balancing the interests of the utility and the public.

Id. The General Assembly clearly expressed its desire to balance the interests of the utility and the public in the stranded cost determination by empowering the Commission to mandate a sharing of stranded costs. 66 Pa. C.S. §§ 2804(13) & (14). The sharing of stranded costs based on the equity return disallowance is a reasonable balance among the interests of Duquesne, its ratepayers and its customers. DII requests the Commission modify the R.D. on this issue and use the DII recommended equity return disallowance to equitably share stranded costs between ratepayers and shareholders.

**9. The ALJ Errs in Not Endorsing DII's Recommendation that Duquesne Be Urged by the Commission to Pursue Securitization as a Final Mitigation Strategy.**

Exception to: R.D. at 432-36 & 837.

DII recommends that the Company be urged to pursue securitization as a final method to mitigate the stranded costs to be recovered from ratepayers. DII M.B. at 70-71; DII R.B. at 36. The R.D. rejects DII's recommendation. "While posed in the guise of 'encouragement,' the DII's proposal still amounts to coercion proscribed by Section 2812 of the Act." R.D. at 436. DII

respectfully submits that the ALJ is misguided; thus, DII excepts to the ALJ's decision on this issue and requests the Commission urge Duquesne to explore securitization as a final mitigation strategy.

DII acknowledges that the Act places the final decision to pursue securitization solely in the hands of the utility. See 66 Pa. C.S. § 2812; DII R.B. at 36. The Act states, however, that the Commission can consider Duquesne's mitigation efforts, including the use of securitization, in determining a just and reasonable level of stranded costs to be recovered through the CTC. Id. § 2808(c)(4)(vi). The Company's decision to pursue securitization (or to not pursue securitization, in this case) should be considered in the same manner that the Company's decision to pursue (or not pursue) other mitigation strategies is considered. If the Company decides not to pursue securitization or to conduct a detailed study of the possible advantages of securitization, as Duquesne admits it has not done (See Tr. at 242; Exhibit No. DJC-26), the Commission can and should consider this fact in evaluating the utility's stranded cost claim.

Furthermore, DII respectfully submits that the record does not establish that it is impossible for Duquesne to vary the Beaver Valley 2 sale/leaseback agreement in order to permit the Company to securitize all or a portion of its allowed stranded costs. See R.D. at 436. The Company supports this claimed inability with a citation to its rebuttal testimony. See id. at 433 n.131; See also DLC M.B. at 54-55. Interestingly, DII first raises this issue in surrebuttal testimony, submitted to the parties after Duquesne's rebuttal testimony. See R.D. at 433, n. 131; See also DII St. 3-S at 28. The Company did not produce solid evidence that the sale/leaseback agreement cannot be altered to permit securitization in this proceeding. The burden is clearly and solely on the Company to show such evidence.

DII respectfully requests that the Commission modify the R.D. and strongly urge Duquesne to pursue securitization as a final mitigation strategy to reduce the stranded cost burden placed on ratepayers.

### 10. The ALJ's Competitive Transition Charge Recommendation Requires Clarification.

The ALJ makes recommendations regarding the establishment of Duquesne's competitive transition charge ("CTC") that appear to be inconsistent. DII requests the Commission eliminate any apparent inconsistency by specifically adopting the CTC residual methodology advocated by DII. The CTC residual methodology is clearly appropriate and preferable under the Act. See DII M.B. at 75-83 & 85-89; DII R.B. at 38-43.

The ALJ appears to adopt the DII arguments regarding the necessity of using the CTC residual methodology.

> In PECO Energy, the Commission adopted the approach of setting the CGC or "shopping credit" as the residual. Enron proposes that model for this case. However, the CGC residual methodology may result in customers being prohibited from participating in the generation market in some years of the transition period. If the CGC is determined by subtracting distribution, transmission and allocated CTC responsibility from the capped rate, it is possible that the CTC allocation for any year, plus the anticipated market price, will exceed the generation rate cap. If the allocated CTC plus the actual market price, will exceed the rate cap, customers will naturally return to Duquesne's system for service during that year and forego participation in the competitive market place. Conversely, since an EDC can charge no more than "prevailing market prices" after the phase-in period ending January 1, 2001, any customers remaining on the EDC's system will unreasonably subsidize the collection of stranded costs by paying more total costs than are justified by cost-based rates. Thus, the residual CGC approach to setting an appropriate CTC will not foster the creation of a truly competitive marketplace, which the Commission found to be of paramount importance in PECO Energy, and should be rejected.

R.D. at 554-55. To the extent the quotation recommends use of the CTC residual methodology, DII agrees with the ALJ. DII M.B. at 75-78, 80-83, 86-87 & 88-89; DII R.B. at 39-43.

Other statements in the R.D. are inconsistent with the recommended adoption of the CTC residual methodology. Specifically, the ALJ also recommends that the Commission allocate stranded costs to rate classes based on the production demand allocator.

> The Act requires that stranded costs be allocated "in a manner that does not shift interclass or intraclass costs and maintains consistency with the allocation methodology for utility production plant accepted by the commission in the electric utility's most recent base rate proceeding." 66 Pa. C.S. § 2808(a). Consistent with this language and its holding in PECO Energy, Slip Op. at 109-113, the Commission should follow the OCA's recommendation to allocate stranded cost responsibility to each customer class on the basis of the production capacity allocator utilized in the Company's last rate case.

R.D. at 556.

DII submits that recommendation of the CTC residual methodology is inconsistent with recommendation of allocating stranded costs to rate classes. As DII explains fully in its Main Brief, the choice of a CTC residual methodology versus a CGC residual methodology is an overarching issue in this debate. See DII M.B. at 75-76. Use of both an allocation and a CTC residual methodology is unnecessarily complex and may result in drastically different CTC recovery periods for different customer classes. Furthermore, DII illustrates that the OCA proposal will result in some customer classes being economically prohibited from participating in the competitive market. See DII M.B. at 75-78 & 80-83; DII R.B. at 39-41.

As DII further explains, the CTC residual methodology (without an allocation of stranded costs to rate classes) is clearly appropriate and preferable under the Act. Id. The CTC residual methodology avoids problems associated with allocating stranded costs to rate classes. Id. at 80-

83. The CTC residual methodology enables each rate class to have a realistic opportunity to economically participate in the competitive market. Id. at 76-78 & 80-83. The OCA's approach, by comparison, results in cost-shifting and possible rate cap violations, both of which are prohibited under the Act. Id.

DII requests that the Commission clarify the R.D. to specifically adopt the CTC residual methodology advocated by DII.

## III. CONCLUSION

**WHEREFORE**, the Duquesne Industrial Intervenors respectfully request that this Commission modify Administrative Law Judge Corbett's Recommended Decision and grant the DII exceptions on the following issues:

1. Adoption of the DII Accelerated Phase-in Schedule;

2. Recognition of the DII Market Price Forecast and Asset Valuation as a Check on the Reasonableness of the OCA Analysis;

3. Denial of the Company's Claim for "Costs Independent of Operation."

4. Rejection of the Proposed Modifications to the Economic Development Rates in Riders 8 and 20;

5. Rejection of Duquesne's Regulatory Asset Claim for Unamortized Debt Costs;

6. Rejection of Duquesne's Regulatory Asset Claim for Deferred Employee Costs;

7. Rejection of Duquesne's Regulatory Asset Claim for Pre-Accrued Nuclear Outages;

8. Adoption of the DII Equity Return Disallowance;

9. Adoption of the DII Recommendation to Strongly Urge Duquesne to Pursue Securitization; and,

10. Clarification that the CTC Residual Methodology as Advocated By DII will be Used.

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Dated: April 14, 1998

## CERTIFICATE OF SERVICE

I hereby certify that I am this day serving two true copies of the foregoing document upon the participants listed below in accordance with the requirements of Section 1.54 (relating to service by a participant).

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