which can be recovered at market prices, and those costs which are stranded, i.e., are in excess of market prices, which are designed to be recovered through the CTC. OCA M.B. at 64.

In the Company's view of the world, it should be permitted to recover the full 6.719¢/kWh from customers who remain with the utility because even if it recovers this full amount, it will still have stranded costs at the end of the CTC recovery period. Further, for customers who opt to take generation service from an alternative supplier, the Company would subtract out the market price of generation, and the residual would be the CTC. Under the Company's analysis, the CGC would be the one-year auction price of 1.81¢/kWh, which is separately stated by customer class on Mr. Lahtinen's Schedule JAL-11. In contrast, OCA's analysis indicates a market price for 1999, including avoidable generation-related A&G of 2.529¢/kWh, based on Mr. Smith's analysis of market prices and Ms. Smith's analysis of generation-related A&G during 1999. Id. at 64-65.

The problem with the Company's approach is that the CTC would be set at a level (4.19¢/kWh) significantly higher than is necessary to recover stranded costs. The consequence of this proposal would be that, in OCA's view, the Company would significantly overrecover its stranded costs during this period. Id. at 65.

In place of this proposal, OCA has proposed that the CTC be designed to recover the amount of stranded cost that the OCA has found to be appropriate for recovery from ratepayers. The CTC could be designed in several different ways. For example, it could be designed to provide levelized collection of stranded costs, declining CTC, levelized rate reduction, or a levelized charge. OCA has proposed a levelized rate reduction which utilizes a declining CTC. As Ms. Smith testified, a levelized rate reduction produces a smaller financial

impact on the Company than a levelized CTC because it results in smaller rate reductions in the earlier years. OCA St. 4-S at 9; OCA M.B. at 65.

Other parties have proposed setting the CGC, or "shopping credit" as the residual, and the PECO Order adopts this approach. However, OCA submits that this approach to CTC rate design should not be adopted for a number of reasons. In particular, OCA submits that it is inappropriate to establish generation rates, which allow Duquesne to charge excessive generation rates to customers who either (1) do not have the choice of an alternative supplier, or (2) choose to remain with the utility during the transition period due to the absence of real competition. OCA M.B. at 65.

(i) The OCA's Response to Duquesne

The OCA notes Duquesne argues that its proposal will shorten the CTC collection period because any excess earnings will be used to accelerate stranded cost amortization. Duquesne M.B. at 60. OCA sees no benefit in this proposal. Under this approach, rather than benefitting from an immediate rate savings, customers will be required to pay current high rates until the "final valuation" and then will realize a rate reduction, only if the Company admits to overearning or other parties are able to demonstrate overearning to the Commission. Furthermore, under the Company's approach, it has little incentive to lower costs and realize greater returns, since the cost of higher returns will be flowed through to ratepayers. OCA submits the better approach is to provide an immediate rate reduction to reflect the benefits of the competitive market to all customers. OCA R.B. at 22.

The Company also argues that under OCA's approach, there is no guarantee that the shopping credit will accurately reflect market prices and will, therefore, send the wrong price signal to customers. Duquesne M.B. at 61-62. OCA submits that while the pre-determined shopping credit, under OCA's proposal, may not precisely track market prices, it will provide a reasonable initial proxy of such prices and sufficient certainty to enable an infant marketplace to grow. After the phase-in period, the Company will be permitted to charge "prevailing market prices" for generation and such prevailing market prices will, in effect, be the CGC. 66 Pa. C.S. §2807(e)(3); OCA R.B. at 22.

(ii) <u>The OCA's Response to Enron</u>

The OCA also notes Enron proposes to treat the CGC, or "shopping credit," as the residual rather than providing for rate reductions, relying on the Commission's Order in PECO Energy. Enron M.B. at 24-31. The OCA submits this approach should be rejected. OCA M.B. at 62-65. In particular, all customers should see their rates reduced as a result of restructuring, not just those customers who "shop." Id. at 65. Second, if the residual is the "shopping credit," then remaining customers will unreasonably subsidize the collection of stranded costs by paying more total costs than are justified by cost-based rates. Id. Third, and perhaps most importantly, the Act is clear that after the phase-in period ending January 1, 2001, utilities may charge no more than "prevailing market prices," subject to the Act's rate caps, as discussed in more detail below in connection with Provider of Last Resort issues. Id. Clearly, Enron's approach would require the Company to charge more than this amount and would

effectively cause remaining utility customers to subsidize shopping customers. This proposal should be plainly rejected. OCA R.B. at 23.

(c) **DII's Position**

DII suggests the Commission's determination of a CTC design methodology for the recovery of Duquesne's stranded costs encompasses many sub-issues. The fundamental issue is the "overall approach" of the CTC design. DII defines "overall approach" to mean whether the methodology uses a CTC residual approach or a competitive generation credit ("CGC") residual approach.

- Under the CTC residual methodology, transmission and distribution costs and the projected market price during each year of the transition period are subtracted from the total capped rate as of January 1, 1997, to determine the customers' CTC responsibility. DII St. 1 at 33-35; Duquesne St. 5 at 63.

- Under the CGC residual methodology total stranded costs are allocated to rate classes for each year of the transition period. OCA St. 4 at 14-15. That allocation of CTC and transmission and distribution costs are subtracted from the total generation component of the rates to produce the CGC. Id. The allocation can be based on a levelized recovery or some other type of recovery.

The choice of methodology is an overarching issue, because use of one methodology or the other may dictate whether customers are economically able to participate in the competitive market during the transition period. DII St. 1 at 34. The development of the competitive market may be irreparably harmed by use of a CTC methodology that prohibits some classes of customers from accessing competitive supply. DII M.B. at 75-76.

DII submits adoption of the CTC residual methodology by the Commission is clearly appropriate under the Act. First, the CTC residual methodology will provide for a more

orderly transition to a competitive market. See, 66 Pa. C.S. §2804(14). Because the target market price and the anticipated market prices are related (and the calculation of the CTC is in effect subordinate to and dependent on projected market price) more customers will have the opportunity to economically participate in the competitive market. See, DII St. 1-S at 18.

> Under this approach, the market rate component of Duquesne's unbundled rate schedules would reflect expectations for market rates in each year of the transition period. As a result, if customers could obtain market rates at levels below the market generation rate component of Duquesne's unbundled rates in any given year, they would have an incentive to purchase power from an alternative supplier. This approach would result in an orderly development of a competitive market and provide opportunities for both customers and alternative generation suppliers to transact purchases and sales.
>
> Utilizing this approach to rate unbundling would give Duquesne's customers an opportunity to actually participate in the market.

DII St. 1 at 34; DII M.B. at 76-77.

Conversely, the CGC residual methodology may result in customers being economically prohibited from participating in some years of the transition period. As explained above, the CGC is determined by subtracting distribution, transmission and allocated CTC responsibility from capped rates. It is possible that the CTC allocation for any year plus the anticipated market price will exceed the generation rate cap. See, DII St. 1-R at 17.

> Although conceptually, Ms. Smith's approach of utilizing an expected market generation rate and an allocated CTC revenue requirement (using a production demand allocation factor) could be utilized, in the case of Duquesne Light Company, the OCA's proposal will violate the generation rate cap provisions of the Competition Act for a number or rate schedules including rate HVPS.
>
> Based on my preliminary review, one of the reasons for the violation of the rate cap under the OCA proposal for Rate

> Schedule HVPS is that the production revenue requirement proposed to be utilized in the analysis does not reflect: 1) the presence of interruptible sales on Rate Schedule HVPS, 2) the nature of limited availability "avoidance generation energy" among Rate Schedule HVPS customers and other supplemental energy purchases, all of which are reflected at full cost responsibility in the production demand revenue requirement but are not reflected at full rate levels in the bundled rates that are used in the unbundling process. As a result, these customers, when assigned fully loaded transmission and distribution charges, expected market generation cost and fully allocated CTC revenues, are assigned costs under the OCA proposal in excess of actual current rates. As proposed, this is not feasible for rate unbundling on the Duquesne system and would lead to a violation of the generation rate cap for a number of rate classes.

Id. If the allocated CTC plus the actual market price exceeds the rate cap, customers will naturally return to bundled Duquesne service in that year, and forego participation in the competitive market place. DII M.B. at 77.

Furthermore, under the CTC residual methodology proposed by DII, because the projected market price increases each year, the correlating CTC decreases. DII St. 1 at 46-47, Exhs. SJB-7, SJB-8 & SJB-9. This decreasing CTC, over the years, will transition customers to the time when the CTC is no longer being recovered and supply decisions can be made without considering stranded cost liability. This is an appropriate process to segue customers to the fully competitive market where decisions are based only on the price of electricity. DII M.B. at 77-78.

The CGC residual methodology is inappropriate for use in this proceeding. As applied by the OCA, the methodology results in violations of the rate cap for certain customer classes. Certainly, a CTC methodology that, on its face, will conflict with other components of the Act cannot be endorsed by the Commission. The DII analysis based on the CTC residual

methodology will advance the development of a competitive market and result in an orderly transition to full competition. For these reasons, DII respectfully requests that the Commission use the CTC residual methodology in determining the CTC for the various Duquesne rate classes. Id. at 78.

DII notes the Company claims that Section 2804(4)(v) of the Act requires that both the CTC residual methodology and the Company's variable CTC charge be adopted by the Commission. Duquesne M.B. at 60-62. Although DII agrees with the Company's use of the CTC residual methodology (the Company refers to this as the "top down" approach), DII submits that Section 2804(4)(v) does not mandate acceptance of the Company's variable CTC methodology. DII R.B. at 38.

Section 2804(4)(v) states:

> If an electric distribution utility rolls its energy cost rate into base rates at a combined level that does not exceed its combined level of such rates which have been approved by the Commission as of the effective date of this chapter, the utility shall not be required to reduce its capped rates below the capped level upon the complaint of any party if the Commission determines that any 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 within the capped rates.

66 Pa. C.S. §2808(4)(v). This Section does not require, as Duquesne suggests, that the Company be guaranteed recovery of its full capped rate level throughout the transition period. Instead, the provision simply requires that once Duquesne's rates are set in this proceeding, a complaint cannot be successfully sustained against the capped rates, unless certain circumstances occur. Specifically, the complainant must show that any excess earnings achieved under the cap

are not being utilized to mitigate transition or stranded cost or to offset other known and measurable cost increases. The Company misconstrues this Section of the Act. DII R.B. at 38.

(d) <u>HSS/ARI's Position</u>

HSS/ARI submit that there are no grounds for Duquesne to recover a CTC because Duquesne has no stranded costs and thus has no entitlement to charge a CTC. Nonetheless, if the Commission grants any portion of Duquesne's stranded cost claim, HSS/ARI submit that Duquesne's proposal for calculating CGCs and CTCs should be rejected. HSS/ARI M.B. at 83.

Duquesne proposes to calculate CGCs and CTCs based upon an annual solicitation for block power sales. Duquesne St. 5 at 29:1-2. As described by Duquesne's witness Lahtinen, Duquesne would design the CGC based upon the results of the annual solicitation. Id. at 56-57. In simple terms, Duquesne would make certain adjustments to the results of the annual solicitation ostensibly to try to take the solicitation results from a wholesale to a retail level. N.T. 728-729; <u>See</u>, also, Duquesne St. 5 - Rejoinder at 2. The CGC, along with unbundled charges for transmission, distribution and ancillary services, would be subtracted from Duquesne's current rates to develop CTCs. Duquesne St. 5 at 29. To understand the shortcomings in Duquesne's proposal, one merely must consider Duquesne's own testimony concerning the ramifications that would flow from an inappropriate design for CGCs in particular. HSS/ARI M.B. at 83.

With respect to one of those ramifications, Lahtinen testified,

> [i]f the CGC is set below the actual market price, customers will have an artificial incentive to stay with Duquesne. The result

> could hinder competition and retard the development of a competitive retail electricity market.

Duquesne St. 5 at 56. Unfortunately, the setting of an unreasonably low CGC that will hinder competition and retard the development of a competitive retail market are the precise outcomes that will occur if Duquesne's proposal is adopted. That is the only conclusion one can reach in view of the RFP Duquesne conducted last summer. HSS/ARI M.B. at 83-84.

HSS/ARI will not repeat the numerous flaws in Duquesne's 1997 RFP that demonstrate that the type of solicitation Duquesne intends will understate even a valid wholesale, let alone a retail market price in Duquesne's service territory. However, HSS/ARI would reiterate one fact, i.e., that Duquesne's version of a CGC would not even provide a bidder "headroom" to recover its overhead or a profit margin. Notwithstanding that fact, or maybe because of it, Lahtinen actually suggested that alternate suppliers will be willing to sell indefinitely at a loss. N.T. 740-743; Duquesne St. 5 at 62. Thus, acceptance of Duquesne's proposal only would "hinder competition and retard the development of a competitive retail electricity market," a result at odds with the very intent of the Act. As such, Duquesne's proposed methodology for setting CGCs and CTCs should be summarily rejected. HSS/ARI M.B. at 84.

(e) **<u>The PRA's Position</u>**

The PRA merely notes in this proceeding two vastly different methods of calculating the CTC/CGC have been presented. The first approach calculates the CTC as the residual resulting from the "fall out" of existing capped rates. This is the approach supported by Duquesne and DII. The second approach is that advocated by the OCA which is to calculate

the CTC as a specific number, not as a residual of what remains after subtracting T&D and the market generation rate from existing capped rates. OCA St. 2A at 4; PRA M.B. at 67.

(f) <u>The Environmentalists' Position</u>

The Environmentalists posit the unbundling of rates is where the rubber meets the road for the ratepayers, for this tells customers how much of their bill they can take shopping for alternative suppliers. The generation or shopping credit is the most critical number in the unbundled rates to both the ratepayers (because it is the amount they can take shopping to find a lower price from another supplier) and for the alternate suppliers (because the degree to which they can undercut the generation credit will determine to a very large extent their ability to attract customers). Without a healthy shopping credit, shopping will not produce meaningful savings for customers, customers will not shop, EGSs will not find customers and will not survive. Suppose they had a market and nobody came. Env. M.B. at 29.

Duquesne's unbundling methodology pays off the CTC at the expense of the shopping credit. The Company calculates the transmission charge, the distribution charge and the generation charge and then the entire remainder up to the rate cap is considered the CTC. The Environmentalists oppose this methodology and instead support the approach taken by the Commission in the PECO Energy restructuring Order which instead computed the CTC and left the shopping credit as the residual. Id.

The Environmentalists contend that once the stranded cost level is determined by the Commission, it is then a straightforward task to determine the unbundled CTC. The allowed level of stranded costs, plus the return allowed on those stranded costs, should be amortized over

the seven-year recovery period specified in the Act (1999 through 2005) using the utility's cost of money. A reasonable assumption for expected load growth over that seven-year period should be used to determine expected annual sales. The system-average CTC per kWh is simply the stranded cost recovery in each year divided by the expected sales in that year. Id. at 29-30.

There are several problems with the Duquesne methodology. First, by having the CTC expand to the rate cap, Duquesne provides no savings to customers, which the Environmentalists submit was the primary purpose of the Act. Second, the Duquesne methodology discourages competition because it results in a low shopping credit. Id. at 30.

(g) Enron's Position

Enron explains Duquesne's methodology for unbundling of rates subtracts its proposed T&D rate from the present total and then sets the Competition Generation Charge ("CGC") at a wholesale market price, calculated through an annual RFP conducted by Duquesne. The residual is then declared the CTC.[144] Enron M.B. at 24-25.

The Company described its methodology thusly:

> . . . Duquesne has established rates for transmission, distribution and ancillary services, these charges will be deducted from current rates and the remainder will represent the maximum generation costs that can be recovered from customers.
>
> This residual amount will then be divided into two parts - a market-based generation component ("CGC") and an above market cost component. The CGC will be set using the market values from Duquesne's annual competitive bid solicitation; these market prices will be adjusted to account for differences among customer class consumption patterns, transmission losses, and Pennsylvania

[144] Duquesne St. 1 at 4.

gross receipts tax. As adjusted, the market prices will be used to determine customer class CGCs and customer-specific CTCs. Customers will also receive annual credits for certain ancillary service revenues collected from retail suppliers.[145]

Whatever the level of the CTC residual, this is what Duquesne proposes to recover in transition or stranded costs subject to a true-up between 2002 and 2003. Id. at 25.

Such an approach, while in furtherance of Duquesne's objective to impede competitive development until at least it recovers all of its stranded costs, is not consistent with the Act's objectives. First, Duquesne's proposed RFP approach would preclude the Commission from determining the level of Duquesne's transition or stranded costs in this restructuring proceeding and instead would leave that determination to future RFPs in violation of the Act.[146] Second, by unbundling rates in a manner that treats the CTC rather than the CGC as the residual, Duquesne "pegs" the generation or shopping credit at Duquesne's RFP estimate of prevailing market prices for each year of the CTC recovery period, thereby turning the Electric Competition Act, and the PECO Energy approach on their heads.[147] Further, as MAPSA witness Russell concluded, under this scenario, "the proposed rates will stifle any nascent competitive options. Native loads of the existing franchised utilities will remain monopolistic markets

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[145] Duquesne St. 5 at 9. Thus, Duquesne's unbundling methodology makes the CTC the residual after deducting market price from the calculated generation portion of the rate. The CTC, therefore, is set precisely at Duquesne's version of market price.

[146] This is explained in detail in the "stranded cost recovery section of MAPSA's brief, adopted by Enron in Section IV, above.

[147] Duquesne's estimate of prevailing market prices for the residential class starts at 2.03¢/kwh in 1999, however the actual market price used to establish the generation or shopping credit will be determined through a 1998 Duquesne RFP. Duquesne Exh. JAL-15. By way of comparison, in the PECO Energy, the Commission estimated that the system wide shopping credit resulting from the decision would equal 4.46¢/kwh in 1999 and the residential shopping credit was established at 5.23¢/kwh. PECO Compliance Filing Order, Appendix D.

throughout the 1999-2005 period and potentially well beyond that time into the future."[148] Enron M.B. at 25-26.

Additional evidence of the unreasonableness of this CGC can be seen by comparing the calculated delivered market prices developed by OCA witness Smith. The system average delivered market price produced by the OCA model (including a share of generation A&G) is 2.529¢/kwh which escalates to 4.062¢ in 2005.[149] Duquesne's system average CGC is 1.973¢/kwh.[150] Thus, the generation credits produced by Duquesne's methodology would actually be below the likely delivered cost of power that suppliers will have to incur. Thus, simply to offer the same rate as the generation credit proposed by Duquesne, suppliers would have to sell to customers at rates below their cost. Of course, as the record here reflects, for

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[148] MAPSA St. 1 at 21. The Commission agrees. In evaluating the 2.8¢/kwh system-wide generation credits contained in the PECO Partial Settlement, the Commission stated:

> . . . Yet even without the testimony of the opposing witnesses, we must at least conclude that the Partial Settlement's ECC [energy and capacity credits] will be below the market prices available to many customers from 2000 to 2003 and is therefore at odds with the record in this case.
>
> * * *
>
> Given the testimony of witness Hieronymous and other witnesses, the record can only support the conclusion that the Partial Settlement's EEC will protect PECO's present monopoly position at least for the period 2000 to 2003. As such, the Partial Settlement's Energy and Capacity Credits hinder creating a competitive retail electric generation market, a major purpose of the Act.

PECO Energy at 17-18.

[149] OCA Exh. LS-7.

[150] See, Enron Cross-Exam Exh. 3.

suppliers to attract any level of customer interest, they must offer 10-20% savings on a customer's energy bill.[151] The evidence is overwhelming, therefore, that if Duquesne's plan is adopted, competition will literally be reversed (since the small number of pilot customers would actually see their bills increase when full direct access began to be phased in and would likely return to Duquesne). Id. at 27.

Of course, this is exactly Duquesne's design. Unfortunately for Duquesne, but fortunately for the consuming public in its service territory, Duquesne's proposed plan is not compliant with the Act's mandate to open up the generation supply market to competition. Duquesne conveniently misinterprets the Act's paradigm and attempts to delay competition until after it has collected its claimed level of stranded costs rather than opening up its market as a condition of standard cost recovery as the Act demands. Id.

Fortunately, the Commission has demonstrated through its PECO Energy Order that it understands the Act's paradigm very well. Through its PECO decision, the Commission rejected PECO's "bottoms up" approach which treated the CTC as the residual and, instead, adopted a "top down" approach, which establishes the just and reasonable level of transition and stranded costs and treats the CGC as the residual. The Commission's approach is fully consistent with the Act and should be considered binding precedent in this proceeding. The Commission adopted a 5-step methodology as follows:

1) First, transmission and distribution rates are unbundled through evaluation of the EDC's proposed allocation of costs. Costs which are not properly

[151] N.T. 1056-61.

allocated to transmission and distribution are reallocated to generation.[152]

2) Next, the level of known and measurable transition or stranded costs is calculated based upon evaluation of which costs in the EDC's claim "would be recoverable under a regulated environment, but which may not be recoverable in a competitive electric generation market."[153]

3) Once the Commission approved level of transition and stranded costs is established, a revenue requirement analysis is conducted to determine the level of CTC collections which are necessary to recover all transition and stranded costs. The revenue requirement analysis should include a cost of capital equal to the EDC's long term debt rate, inclusive of all tax effects.[154]

4) The CTC rate is then designed to recover the CTC revenue requirement on a levelized basis, over a set period of time, on a "per kwh" basis assuming annual sales with a presumed growth rate (subject to reconciliation).[155]

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[152] PECO Energy, at 49-63. In the Orders, the Commission reallocated a portion of PECO's Administrative and General ("A&G") costs to generation. One aspect of the Commission's Opinion and Order with which Enron strongly disagree is whether, once reallocated to generation, these A&G costs should be recovered as transition or stranded costs. In Enron's view, the law is clear that A&G costs associated with generation do not qualify as transition or stranded costs because these costs are fully recoverable in a competitive environment. Enron has appealed the PECO Energy to the Commonwealth Court on these grounds.

[153] PECO Energy at 63-102. 66 Pa. C.S. §2803. In determining the level of stranded costs, the Commission utilized the Office of Consumer Advocate's market price projections. While PECO and Duquesne depart in their approach to stranded cost calculation (PECO utilized an asset valuation approach and Duquesne proposed a "market sale" approach), both approaches require reference to market prices as the benchmark for evaluation of stranded cost levels.

[154] PECO Restructuring Order at 103-09; PECO Compliance Filing Order at 6. Duquesne's long term debt rate is identified by the Company on the record as 7.57%; OCA Exh. MIK-5.

[155] PECO Restructuring Order at 109-13. In the PECO case, the Commission established an 8½-year recovery period. However, the length of the recovery period should be established based upon consideration of the amount of stranded costs to be recovered – to balance the desire for as short a recovery period as possible with the need to establish generation or shopping credits which enable market entry and provide for the desired level of discounts for consumers.

5) The residual of T&D plus the CTC less the current bundled rates becomes the generation or shopping credit.[156] None of this residual should be converted into a short-term tariffed rate decrease[157] to be provided to consumers outside of the competitive marketplace since such short-term rate decreases are not consistent with the Act and restrain the development of a competitive market and the prospect of even greater savings that competition will bring.[158] Moreover, as the Commission held in the PECO Restructuring Order, if Duquesne wants to reduce its rates it has that authority under Chapter 13. Duquesne has not sought to reduce its rates during this restructuring case, when it had ample opportunity to claim that it was overearning.

6) Finally, the generation credit needs to be compared to the evidence of the cost of delivered power to assure that the Act's mandate that a competitive market develop will occur. If the generation credit will not produce the margin over costs necessary, several options are available including extension of the CTC recovery period and back-end loading of the CTC (with an equivalent NPV stranded cost level).

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[156] As the Commission described its methodology, "The shopping credit is not a selected number. It is the number that results from the difference between a particular customer's total rate as of January 1, 1997 and the sum of T&D and CTC rates established pursuant to this order." PECO Restructuring Order at 42. It is noteworthy that this residual does not necessarily track market prices. Nor should it! While utilization of undependable long term market price projections is an unavoidable component of determining the level of stranded costs, nothing in the Act requires or even explicitly or implicitly links the unbundling of rates and the design of the CTC to market prices.

[157] Contrary to OCA's apparent position. See, OCA Exh. LS-7.

[158] As the Commission stated in reaching this determination:

> Relying principally on changing rate tariffs to deliver price benefits to ratepayers will not foster the competitive retail electric market that the Act requires for all customers, not just the largest users. In fact, providing temporary rate cuts through tariffed generation rate reductions will leave the customers without a competitive market that is their only real protection under the Act. Indeed, once the temporary rate cuts expire, customers would experience the equivalent of a horrible hangover if little or no competition exists to provide the competitive benefits the Act intends.

PECO Restructuring Order at 43.

This six step "top down" approach closely tracks the Act by unbundling and designing distribution, transmission and generation rates in a manner which promotes, not impedes, the development of meaningful competition. In fact, it is arguably the only methodology which fully complies with the Act. There is absolutely no distinction which could reasonably justify departure from this approach in this restructuring proceeding. The approach of the PECO Restructuring Order as to the unbundling of distribution, transmission and generation rates and CTC design should be considered binding precedent and should be followed by the Commission in reaching a decision in this proceeding. Enron M.B. at 28-30.

An example of application of the PECO methodology to Duquesne can be illustrated by comparing OCA's proposed T&D and CTC rates versus Duquesne's overall system average rate. OCA's proposed system average T&D rates are 2.113¢/kwh, which would be assumed for each year of any CTC recovery period. Next, the determined stranded costs would be converted to an annual CTC, recovered over 8½ years and levelized, allowing a return on the unamortized portion at Duquesne's cost of debt. If for illustrative purposes the levelized CTC is 2.3¢ (which implies a total stranded cost recovery consistent with the OCA recommendation recovered over 8½ years), the CTC would be calculated as follows:

Total Rate	8.930[159]
T&D	2.113[160]
Levelized CTC	2.30 [161]
System Average Generation Credit	4.517

If the various components were determined at the levels assumed, this resulting generation credit would likely be sufficient to permit suppliers to offer sufficient savings to allow the development of a competitive market in Duquesne's service territory. Id. at 30-31.

Enron notes Duquesne's brief spends a good bit of time attempting to make arguments in support of its "market price" based proposal for calculating a CGC. Quoting testimony by its witness Mr. Marshall, it claims that a "calculation" is necessary because of the "rate cap," and that it has a right to a "calculated" CGC approach using its market evidence because it has invoked the provisions of the Electric Competition Act which, it claims, permits it to utilize any revenues that otherwise would be reflected as rate decreases to mitigate stranded costs.[162] It even claims that, because it has asserted a claim under this particular provision of the Electric Competition Act its position is somehow different than that presented to the Commission in PECO and that a different result (from that in PECO) should obtain.[163] Duquesne's insistence on a "calculated" generation credit is to further its claim that the CTC should be established as the residual of its entire generation related rate. Not only does

[159] OCA Exh. LS-7.

[160] Id. The Commission should substitute individual class T&D rates as calculated by Enron witness Reising.

[161] The levelized CTC would be calculated using the mandated recovery period and a rate of return equivalent to the Company's long term debt rate inclusive of all tax effects.

[162] Duquesne M.B. at 60-65; 66 Pa. C.S. §2804(4)(v).

[163] Id.

Duquesne's proposal turn the PECO Order on its head, such an approach would simultaneously allow Duquesne to recover stranded costs at a maximum level and, at the same time, assure that competitors have no hope of winning customers in its service territory. Enron R.B. at 14-15.

Duquesne's position is, of course, incorrect. As was set forth carefully in Enron's Main Brief, the PECO paradigm does not "calculate" a "CGC" using any projections, guesses or assumptions about market prices. As the Commission determined in PECO, the CGC is a residual number which is not calculated but produced after determinations of the portions of Duquesne's rates which were associated with transmission and distribution and CTC. When those elements are determined and removed from Duquesne's current rates, the remainder – whatever that may be – is the customer generation credit. The Commission stated as follows:

> The shopping credit is not a selected number. It is the number that results from the difference between a particular customer's total rate as of January 1, 1997 and the sum of T&D and CTC rates established pursuant to this order." PECO Restructuring Order at 42. The residual establishment of a shopping credit does not purport to track a market price for generation but is the Commission's determination of what is necessary to create incentives for customers to want to shop and for sellers to be able to offer savings, therefore building the foundation for a competitive market. Nothing in the Act explicitly or implicitly links the unbundling of rates and the design of the shopping credit to market price.[164]

While, as MAPSA and Enron have pointed out, it may be necessary in some cases to review that resulting level to make sure that a competitive market can continue to develop, that step is an incidental one after the initial calculations are made. In this respect, Duquesne cannot complain about the level of CGC because it is entirely its responsibility; it alone is responsible for the

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[164] PECO Restructuring Order at 42; Enron M.B. at 29.

level of generation rates that it has required and charged to customers over the years. It alone could have filed for a voluntary rate decrease if it found these levels too high (and still can). The PECO paradigm merely recognizes that fact and also recognizes the obvious principle that whatever is not declared to be uneconomic as a result of the advent of competitive market – that is that portion that is not a stranded cost – is the generation revenue requirement associated with Duquesne's generation business that will continue after restructuring. Enron R.B. at 15-16.

Moreover, the PECO paradigm is completely consistent with the section of the Act that gives an EDC the ability to maintain rates at existing levels after its restructuring. Indeed, the PECO paradigm works from the basic proposition that the development of competition should respond to the rates being charged for the product, e.g., the utility's present rates. Id. at 16.

In addition to Duquesne, the OCA and Duquesne Industrial Intervenors have advocated that the CGC be "calculated" based upon market prices. Both of these customer representatives also argue that the "generation credit," should be a calculated number based upon some determined "market price."[165] Duquesne and OCA/DII quickly diverge with Duquesne, of course, after this point, arguing that the annual CTC should be determined using their respective "margin" models and that, after subtracting: (1) the resulting CTC; (2) the market based CGC; and (3) the determined Transmission and Distribution rates, the "residual" should be transformed into rate decreases for customers.[166] Both claim that achieving rate decreases

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[165] See, OCA M.B. at 57-58, 62-63, 64-65; DII M.B. at 75-76.

[166] Id.

for customers was a principal goal of the Electric Competition Act and is necessary once the PUC determines the CTC and the "market based" CGC.[167] Id. at 16-17.

But the "rate reductions as residual" argument suffers from a number of infirmities. Most importantly, both the OCA and DII (and, as noted, Duquesne for that matter) assume incorrectly that the "shopping credit" should be or is "calculated and that it should equate to some version of the delivered market price for power. As the Commission established in PECO (and as referenced above) this is incorrect. The Competition Act does not support the position that the CGC should be a "calculation" or that it should equate to some "estimation of the market generation price." Id. at 17.

First, there is nothing in the Act that supports a calculated CGC. Indeed, the Act's principal goal to establish a competitive retail electric market would be completely frustrated by a market calculated CGC. Moreover, the record does not support the OCA/DII position. The OCA/Duquesne II approach would, in effect, require a one-time rate decrease to all customers based upon a predetermined market price based upon a government imposed determination of the record. But market prices are really determined by the market — many suppliers selling electricity to many customers. To achieve a competitive market, regulation must not be used to control price. It is for this reason that all suppliers[168] and some customer representatives[169] have advocated that rate reductions should come from a vigorous market and that the PECO paradigm should be applied to Duquesne. Id. 17-18.

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[167] Id.

[168] E.g., MAPSA M.B. at 28-29.

[169] Env. M.B. at 29-30.

Further, to effectuate regulated rate decreases, the Commission would need to make a finding that the portion of Duquesne's rate which is associated with generation but not identified as stranded is unjust and unreasonable. While such evidence might well have been submitted (and presumable still could be in some future proceeding)[170] it has not been put forward. Id. at 18.

In addition, the OCA/DII approach suffers from the fact that they require accurate calculations not just of the generation market price but a host of "adders" to reflect such items as retail costs, line losses, load factor, etc. The Commission implicitly rejected this exercise in PECO. Id.

OCA contends the Commission should reverse course from its PECO approach because mandated rate decreases will benefit all customers, not just those who shop.[171] But the PECO Order determined that establishing the generation credit as the residual would produce the necessary "headroom" to assure that savings would be forthcoming from the competitive market itself. This is far preferable than government imposed, once and done, rate reductions because the former course not only delivers rate reductions to customers in the near term it simultaneously allows the development of a robust competitive market. This, in turn provides the potential for even greater savings and benefits to customers, in the form of new products and offers, better service and greater efficiencies overall. The potential for benefits from this competition enhancing strategy is thus unbounded. Id. at 18-19.

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[170] The Act establishes January 1, 1997 rates as caps not floors; Duquesne's rates will continue to be subject to Chapter 13 of the Public Utility Code and could be reduced if a case was made that they were unjust and unreasonable. PECO Reconsideration Order at 21.

[171] OCA M.B. at 62.

In contrast, establishing the shopping credit at the market means no or virtually no competition developing. As noted, a competitor has little chance to attract customers away from the incumbent if the utility is permitted to provide a credit that reflects the same (or lower) price that suppliers are required to offer in order to recover their costs. How can there be competition, one must ask, if the incumbent's price and the new entrant's price are mandated to be the same? Indeed, since even Duquesne acknowledges that suppliers have to be able to offer 10-20% savings if they have any hope of attracting customers,[172] establishing the CGC at the retail "market price" means competitive markets simply will not develop and customers will likely never see the additional benefits that vigorously competitive markets bring. Id. at 19.

Moreover, OCA's fundamental premise – that savings produced from the competitive market will not benefit all customers – is not based upon any empirical evidence. Indeed, it is only common sense that if Duquesne's present customers are offered 10-15% savings, all those who wish to benefit from such discounts will exercise their right to choose. Those who wish to achieve savings but who want to stay with their traditional supplier can do so – simply by arranging for service with a Duquesne competitive affiliate or division. The notion that, once direct access is available to them, any customer who wants savings will be denied them under the PECO approach simply is not supportable.[173] Id.

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[172] N.T. 1056-61.

[173] The OCA's other argument for diverging from the PECO approach is that after the phase-in period (January 1, 2001), "customers who do not choose are to be served by the utility or a commission-approved alternative supplier at 'prevailing market prices', subject to the rate cap . . . ." Certainly the Commission should not provide an incentive to competition which will suddenly disappear two years after the beginning of competition. OCA M.B. at 62-63. But OCA's argument suffers from a misunderstanding of the provision establishing rates for (continued...)

Enron submits that both Commission precedent, the requirements of the Act and the need to take steps to create a competitive market all mandate that the Commission follow the PECO paradigm and unbundle Duquesne's rates by (1) establishing T&D rates for each class; (2) establishing a CTC and recovery period for each class; and (3) removing items 1 and 2 above from the total rates and establishing the remainder as the generation credit (unless changed pursuant to Public Utility Code Chapter B). Id. at 20.

Pursuant to PECO, this generation credit will apply to all customers and be the generation charge for all customers who: cannot choose, do not choose or who choose and then return to Duquesne unless and until (a) Duquesne voluntarily changes those rates pursuant to Chapter 13 of the Code; or (b) the rate for such "Provider of Last Resort" customers is changed pursuant to a formula established by the Commission pursuant to regulations. Id.

(h) MAPSA's Position

MAPSA argues Duquesne's proposed CGC is too low to allow for the development of meaningful competition for retail sales of electric energy and should be rejected. It is axiomatic that an electric utility's restructuring plan must promote the development of a competitive market in accord with the policy of the Commonwealth set forth in the Competition Act. 66 Pa. C.S. §2802. Indeed, a restructuring plan, which had been agreed to by many

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[173](...continued)
"default" customers. As Enron explained in its Main Brief, that section, on its face, simply does not mandate that the rate for such service will be "prevailing market prices," but that power will be acquired at "prevailing market prices" and sold at a rate that recovers that price "together with all reasonable costs." 66 Pa. C.S. §2807(e)(3). That total rate presently equates to Duquesne's residual generation credit since that is the only rate that recovers all of Duquesne's non-stranded generation costs. See, Enron M.B. at 48.

stakeholders and which provided only for rate cuts and other significant "concessions" by an electric utility, but which was also found to hinder the development of a "competitive retail electric market and [which made] competition for many residential and other low-load factor customers economically impossible until 2003 at the earliest," was rejected by the Commission as being contrary to the public interest. PECO at 14; MAPSA M.B. at 29.

Specifically, it is the "level of the ECC [also referred to as the "generation credit" or the "shopping credit," and specifically called the "CGC" in Duquesne's case] [which] impacts whether the Act is a success or failure." PECO at 15. As further stated by the Commission:

> *If the ECC [or Duquesne's CGC] in any year is too low,* competition will be harmed or even destroyed. 'There are many ways in which a restructuring plan can result in a de facto monopoly in the electric supply market. Perhaps, the most important of these is the establishment of generation credits that are set below market prices for electricity.'

PECO at 16. Thus, contrary to the position of Duquesne as expressed by its chief policy witness, Mr. Marshall, in this proceeding, the CGC must be set to allow for competition starting in 1999. MAPSA M.B. at 29.

The Commission has made it clear that, in the context of reviewing the level of the generation or shopping credit to determine whether a restructuring plan promoted competition under the Act, it is the market retail price of fully delivered power (and not the wholesale price) which is the key determinant:

> Setting the ECC or [CGC] below price levels at which even the most efficient competitors could sell electricity or below market prices strangles competition by making it economically impossible to compete for retail customers. Simply put, if set too low, the ECC or [CGC] will mean that electric customers in PECO's [or Duquesne's] service territory will have few or no competitors competing for their business.

PECO at 16. Where the record establishes, as it did in PECO, that a proposed generation or shopping credit (ECC or CGC) protects a utility's present monopoly position, even for the period from now until 2003, it must be found that the proposed generation credit hinders the creation of a competitive retail electric generation market, which is a major purpose of the Act. PECO at 18; MAPSA M.B. at 30.

MAPSA advocates a stranded cost approach, which focuses on administratively setting the CGC. Because of the mathematical relationship of the CTC and CGC, under MAPSA's approach, the CTC would be the resulting number. As pointed out in the argument immediately below, in PECO, the Commission did not follow MAPSA's approach as advocated in this case. Should the Commission feel bound to follow the PECO approach, MAPSA (which has not taken a specific position on Duquesne's stranded cost level), vigorously disputes Duquesne's methodology, endorses the PECO methodology, and relies upon other Intervenor's methodologies for calculating stranded costs. Id.

In order to rectify a restructuring plan (as proposed in a settlement) which contained a shopping credit that was too low to allow for competition, the Commission set the CGC as the residual of non-bypassable charges under the rate cap. PECO. This method identifies the utility's rates that should be subject to competition, after adequately compensating the utility for the use of its distribution and transmission systems and allowing recovery of 100% of its non-mitigable stranded costs. As stated by the Commission:

> This Opinion and Order establishes for the first time an unbundled T&D [transmission and distribution] rate for consumers of PECO. This Opinion and Order also establishes a CTC that consumers are obligated to pay PECO for every kWh consumed. The shopping consumer pays only the T&D rate and the CTC to the EDC [electric distribution company] when purchasing generation in the

> competitive market. The addition of the T&D rates and the CTC produces a total sum of charges that when compared to the customer's in effect as of January 1, 1997 gives rise to the concept of a 'shopping credit.' The shopping credit is not a selected number. It is the number that results from the difference between a particular customer's total rate as of January 1, 1997 and the sum of T&D and CTC rates established pursuant to this order.

PECO at 42; MAPSA M.B. at 31.

And, once the CTC and the resultant shopping credit is derived, it is appropriate for the Commission then to review the record testimony in order to determine whether the resulting shopping credit itself, as well as "the mechanism of the shopping credits," will provide a competitive market. As stated by the Commission:

> The Commission is convinced from the record testimony that the shopping credits [4.46¢/kWh, on a system average basis] and the mechanism of the shopping credits [levelized] will provide a competitive market. Again it is only genuine competition that will deliver long term price benefits to the customers of the PECO service territory. The Commission's approach avoids creating a de facto monopoly that delivers temporary and short-term rates cuts.
>
> It creates real incentives for electric suppliers to compete for customers and for customers to shop for electricity. As such this decision will create a market featuring many buyers of electricity and many sellers of electricity.

PECO at 44; MAPSA M.B. at 31-32.

Using the PECO method, however, may raise an additional question in this case, because the credit in PECO was found to be large enough to allow for competition: Namely, what are the Commission's options, if the resultant shopping credit is not sufficient to enable full workable and robust retail competition as was the case in PECO? Clearly, there are two immediate remedies, if it is found that a shopping credit is not large enough to promote robust

competition. First, the level of the CTC can be adjusted; for example, in PECO, wherein the utility had proposed a "front-end loaded" CTC (higher in the early years and lower in the later years), the Commission directed that the CTC should be levelized or flattened. PECO at 41. In addition, under the terms of the statute, 66 Pa. C.S. §2808(b), the length of the period for recovery of the CTC can be extended. PECO at 104, fn. 102. Either of these tools, levelizing the CTC or extending the recovery period, has the effect of lowering the CTC, thereby increasing the mathematically related CGC to a level, which will support the development of a workable competitive market. Another tool available to the Commission to promote competition is to increase the CGC by adding to it a Customer Participation Credit ("CPC"), as suggested by Mr. Russell in this case, and expressly adopted by the Commission for the Pilots. Pilot Order at 68-70; MAPSA M.B. at 32.

In summary, the following steps are involved in determining an appropriate CTC and CGC.

1) Calculate the electric utility's stranded cost in accordance with the record evidence and the methodology set forth in PECO.

2) Derive a CTC to collect those reasonable and non-mitigatable costs over an appropriate period (for example, the nine year period provided for in 66 Pa. C.S. §2808(b)).

3) Calculate the appropriate T&D rates.

4) Mathematically calculate the CGC, by adding the transmission, distribution and CTC charges, and subjecting the total of these three charges from the level of rates in effect on January 1, 1997.

5) Determine whether the resulting CGC will allow for competition, based upon the record evidence of what a fully delivered retail price of power is.

6) Make appropriate adjustments to the CTC/CGC, if the CGC (shopping credit) is not large enough to allow for competition (e.g., flatten the CTC, "back-end load" the CTC, lengthen the recovery period, or provide for a CPC).

Because MAPSA has taken no position as to the appropriate level of Duquesne's stranded costs, the first, second, third, and fourth steps of the analysis must be based upon the CTC and T&D levels proposed by other intervenors in this proceeding. However, when arriving at the fifth stage of the analysis which was approved in the PECO decision, namely, analyzing the CGC to determine whether it will allow for competition, MAPSA's concerns are implicated. MAPSA M.B. at 32-33.

Simply stated, Duquesne's proposed CGC will not allow for competition, because it is too low to allow suppliers to compete. Duquesne has adopted a methodology for determining the CGC that is the opposite of that set forth by the Commission. Namely, Duquesne proposes to calculate the CGC and use the CTC as a "fall-out." In using the CGC as the "driving" number in the equation, Duquesne has used a wholesale market price, based upon the results of its flawed RFP process, rather than attempting to set a fully-delivered retail price. MAPSA M.B. at 33-34.

The fact that Duquesne's CGC is based upon a wholesale market price is not disputed by Duquesne, rather, Duquesne's CEO defiantly declares that if suppliers cannot deliver power and provide benefits at a price equal to or less than the wholesale market price, the Competition Act is not a "good idea." N.T. 136. Duquesne's own witnesses acknowledge that suppliers will be unlikely to recover additional costs and provide a fully-delivered retail price that would be under the CGC. N.T. 497. Duquesne believes that in the restructured world, at least as long as Duquesne is serving as the supplier of last resort, competition will exist

primarily between Duquesne, as the supplier of last resort, and the competitive suppliers as a unified mass. N.T. 137. Duquesne believes that suppliers should be placed at risk for possible fluctuations or differences in the market price, but that Duquesne should not shoulder that same risk. N.T. 493. Duquesne believes that it should be insulated from the possible changes in the market price of power. Id. Essentially, Duquesne's proposal is to set up a "competitive" scenario where there is no competition; a sentiment echoed by Duquesne's own witness who states that competition envisioned by the Act is potential competition, i.e., a potential for suppliers to compete in Duquesne's service territory, not actual competition, where suppliers actually can compete. N.T. 765; MAPSA M.B. at 34.

One can only conclude from a review of Duquesne's position in this case that Duquesne does not believe the CGC, which it has proposed in this case, will allow for the development of competitive market. In fact, Duquesne appears to defy the Statute's mandate for the development of a competitive market and it does not even attempt to disguise the fact that its market price is a wholesale market price and that competitors will be unable to deliver power at that price or below it. Therefore, Duquesne's proposed CGC is contrary to the law and must be modified. Id. at 35.

In modifying a CGC, the Commission should look at the record evidence in order to determine what level of CGC would be sufficient to allow for the development of a competitive market. The only evidence of what fully-delivered retail charge would satisfy the development of a competitive market was presented by MAPSA witness Russell. Mr. Russell testified that the preferred approach for setting the CGC is to determine it administratively, based on the long-run marginal cost. MAPSA St. 1 at 29. If that approach should endanger a

utility's opportunity to recover its legitimate and verifiable stranded costs within the nine year period established in the Act, Mr. Russell recommends that the Commission extend the nine year period to a later date. Id. at30. Further, after the first year of collection, the CGC should be adjusted to reduce the gap between the CGC and the actual market price which evolved in the prior year. The CGC then would be adjusted to reflect anticipated changes in the market with this process continuing until the end of the recovery period. MAPSA M.B. at 35.

Alternatively, MAPSA witness Mr. Russell suggested that it would appropriate to look at market indices for the price of energy, and to those figures add: the value of additional services (and costs), which must accompany the raw price of energy in order to make it useful. These necessary additions to the market indices for the raw energy value include:

- The value of capacity adjusted to the load factor of the customer class, including the cost of capital additions.
- The value of installed reserves adjusted to the load factor of the customer class.
- The cost of ancillary services.
- Marketer's costs and home office overhead.
- Losses.
- Profit.

MAPSA St. 1 at 32; MAPSA M.B. at 35-36.

It is necessary to add such items as the cost of marketing, home office overhead, and profit for the simple reason that, no matter what entity is selling the energy, that entity will incur these costs, and, in deriving the CTC, utilities Duquesne included their costs of marketing and home office overhead. N.T. 767-769. Accordingly, the CGC payable to competitors should

be adjusted upward in order to put the utility's costs of marketing and home office overhead at risk in the competitive market. MAPSA St. 1 at 33; MAPSA M.B. at 36.

MAPSA witness Mr. Russell testified that the CGC, at a minimum, must fall within a range of at least 2.9¢/kWh up to 4.1¢/kWh. MAPSA Exh. 4. He also advocated an additional customer participation credit equal to that of Duquesne's Pilot Program. MAPSA St. 1 at 54. Obviously this level of CGC is far in excess of the 1.8¢/kWh proposed by Duquesne. MAPSA M.B. at 36.

Duquesne's approach for calculating its stranded cost is seriously flawed for all of the foregoing reasons and leads to the development of rates, which will preclude the development of a competitive market. Accordingly, its approach must be rejected as contrary to the Competition Act. PECO; MAPSA M.B. at 36.

MAPSA's approach, which focuses upon setting the CGC based upon a realistic retail price of power as opposed to a suppressed wholesale price of power, will produce a competitive market, and MAPSA urges the Commission to adopt its suggested approach. MAPSA recognizes, however, that the Commission's approach contained in its PECO Order focuses upon calculating the stranded costs, and thereafter deriving a CTC to collect the stranded cost. By this method, the CGC, or shopping credit, is not a selected number; rather, it is the number that results from the difference between a particular customer's total rate as of January 1, 1997, and the sum of the transmission, distribution and CTC rates. PECO at 42; MAPSA M.B. at 37.

Should the Commission follow its PECO methodology and not adopt MAPSA's suggested approach focusing on setting a competitive CGC in the first instance, MAPSA leaves

the Commission to its discretion in adopting one of the stranded costs methodologies or a combination thereof proffered by the other intervenors in this proceeding. Significantly, however, Mr. Russell's testimony concerning the CGC is still relevant and probative.. In short, evidence regarding the level of the CGC which is necessary to produce a competitive market is a subject which was specifically considered by the Commission in PECO. The Commission, after deriving the CTC with the resultant shopping credit, reviewed both the credit and its "mechanism" of collection, to determine whether a competitive market would be created. PECO at 44; MAPSA M.B. at 37.

MAPSA finds Duquesne claims its methodology was adopted by this Commission in PECO, as being the appropriate methodology for setting a CGC. Duquesne M.B. at 62. Duquesne's characterization is wholly inaccurate, and completely self-serving. Duquesne appears to believe that the shopping credit that it proposes is intended to reflect current market prices. While Duquesne conveniently ignores the fact that its "market price" is a wholesale market price, which obviously will not allow for competition, the record evidence is clear on this point. Duquesne ignores the fact that the shopping credit is the price against which competitors will have to compete and, if the shopping credit is not sufficient to allow for competition, there will be no competition and, therefore, no stranded costs. The guarantee in question is not that the shopping credit will reflect current market prices (or Duquesne's distorted view of market prices) but, rather, whether the shopping credit will guarantee the development of a robust competitive market. Duquesne continues to mistakenly rely upon 66 Pa. C.S. §2804(4)(v) for the proposition that it has the continuing statutory right to collect its

current bundled rate. Duquesne's analysis must be rejected in favor of the correct application of the mandates of the PECO decision and the Competition Act. MAPSA R.B. at 8-9.

Duquesne attempts to justify its annual adjustment of the CGC based on the results of its RFP. Duquesne M.B. 62-64. Duquesne's RFP is a flawed mechanism for predicting a wholesale market price and has no chance of ever producing a result that would reflect a fully-delivered price of energy which is required of a shopping credit. Because Duquesne's proposed adjustment methodology relies upon its RFP, which is incapable of producing an accurate result, its proposal must be rejected. It also is quite apparent that Duquesne ignores the methodology for calculating a CGC set forth in the PECO decision as being the appropriate methodology. Duquesne's proposal should be rejected on that basis alone. MAPSA R.B. at 9.

Duquesne's proposal ignores the fact that there is the potential cost-shifting within customer classes if it is allowed to implement a customer-specific or premise-specific CTC. Duquesne M.B. at 65. Duquesne's position ignores the Order of the Commission in PECO, that the CTC be collected on a per kWh basis in order to send the appropriate price signals to customers. Duquesne's arguments to the contrary - merely stating that MAPSA's position is "intellectually indefensible" - ignore the fact that Duquesne's proposal is legally indefensible and must be rejected. MAPSA R.B. at 10.

Duquesne argues that, while MAPSA criticizes its RFP proposal, MAPSA fails to offer any alternative to the RFP. Duquesne M.B. at 68. Duquesne asserts that MAPSA's failure to offer an alternative is fatal to its criticism. Attempting to fix Duquesne's RFP proposal is akin to attempting to repair a car which has been put through a car shredder. "What's the point?" The fact that the criticisms offer no alternative fails to address the merits

of the perfectly valid criticism, namely, that the RFP process if fatally flawed. MAPSA R.B. at 10.

2. Other Conceptual Disputes

(a) CGC Calculation: Annual Adjustments v. Fixed Schedule

(i) Duquesne's Proposal

The Company finds the Duquesne and OCA methods differ in that Duquesne's shopping credit will adjust each year (per the RFP results for that year), while the OCA sets a fixed shopping credit in advance for each year of the transition period. The differences in approach are vitally important because of the rate cap, as explained by Mr. Marshall:

> The OCA and DII propose to set CGCs at a fixed level throughout the transition period, using their computer forecasts of market prices. They readily concede that, under this approach, if market prices rise to levels above the fixed CGC, customers will return to Duquesne and take service at the rate cap. "Taking service at the rate cap" means, for purposes here, purchasing unbundled generation from Duquesne at a price equal to the CGC. When market prices rise above that level, purchasing from Duquesne is clearly preferable to paying a marketer the actual (higher) market price. In such a scenario, the customer is protected and Duquesne is protected, given that the CGC was set on the basis of a market price prediction that, in retrospect, was too low. However, the suppliers are harmed (they contend) because customers will have an artificial incentive to return to service from Duquesne.
>
> Now consider the opposite scenario - in which market prices fall below that projected in the CGC. In this situation, customers are again protected because they are not required to purchase power from Duquesne at the CGC. Consequently, one would expect them to purchase power in the open market at lower rates. Suppliers too will benefit under this scenario, given that customers are less likely to continue purchasing from Duquesne under the rate cap. The loser in this scenario, of course, is Duquesne. Duquesne will fail to fully recover its stranded costs

> because the fixed CGC, in retrospect, was set too high and, hence, the CTC was set too low.
>
> As the foregoing illustrates, customers have a natural incentive to "lock in" the CGC because they gain "certainty" without any adverse economic effects associated with the resulting loss of accuracy in forecasting the CGC. The suppliers, on the other hand, have the incentive to adjust the CGC on an annual basis to reflect actual market prices. Suppliers also, however, have an incentive to fix the CGC in advance, provided that it is set so far above market prices that they bear no material risk of market prices exceeding the CGC in any year. The latter incentive is illustrated by Mr. Russell's proposal to set the CGC on the basis of the cost of constructing a new generating unit, even though he concedes that ECAR has excess capacity. . . .
>
> The only fair resolution is to set the CGC at the market price and that is precisely the purpose of Duquesne's RFP proposal. I recognize that many parties have criticized the RFP as producing prices that are "too low". While this is not the point – the goal is to establish a method that measures actual market prices – I note that the market prices produced by the eight-year RFP are nearly identical to those forecast by the OCA, with the sole exception of an artificial "bump" in market prices that OCA predicts will occur in 2003 due to the addition of new capacity. Whether or not this spike in prices actually occurs is, of course, a matter of speculation, but, from the results of the eight-year RFP, the market is predicting that it will not occur. More to the point, however, none of the parties (with the exception of Mr. Boonin) offers any concrete alternative for calculating the true market price of power in the Duquesne region. In the absence of any such alternative, the Commission should accept Duquesne's proposal.

Duquesne St. 1-R at 21-23 (emphasis in original). For the reasons stated by Mr. Marshall (and explained further by Messrs. Schnitzer and Lahtinen, Duquesne St. 3 at 40-45; Duquesne St. 5 at 56), the Commission should adopt Duquesne's proposal to adjust the shopping credit each

year to reflect actual market prices.[174] The methodology for doing so (the annual RFP) is addressed in more detail, supra. Duquesne M.B. at 62-63.

(ii) <u>The OCA's Position</u>

The OCA relates part of the Company's final valuation proposal is to adjust the CGC annually to reflect market prices. Annual adjustment of the CGC presents a number of problems. Perhaps most important is that there may be significant controversy over the price which is produced by Duquesne's auction, requiring Commission monitoring and possibly review of this process. Additionally, use of an annual auction would make it difficult to establish rates during the CTC recovery period today. *Consequently*, OCA recommends that the Commission reject this approach in favor of setting the CGC in this proceeding. OCA M.B. at 65-66.

The OCA submits that Mr. Smith's market price forecast, as adjusted by OCA witness Lee Smith, provides a reasonable basis for establishing the initial shopping credit and provide certainty in the marketplace that will be helpful in growing an infant marketplace for electric generation. Then, at the end of the phase-in period, prevailing market prices will determine the CGC. 66 Pa. C.S. §2807(e)(3); OCA R.B. at 23.

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[174] Duquesne notes that to address a potential preference by some customers for a fixed CTC, Duquesne offered an option in its pilot program to fix the CTC in advance provided that electing customers waived their right to return at capped rates, but the proposal was uniformly opposed by the parties and was not accepted. Duquesne St. 1-R at 15.

(iii) **DII's Position**

DII suggests another conceptual difference among the CTC proposals in this proceeding is whether the schedule of CTC and CGC charges for each year of the transition period should be established definitively as part of this proceeding or whether the CGC and CTC should vary each year. DII and OCA propose to firmly establish the CTC responsibility for each customer class as part of this proceeding. DII St. 1 at 33; OCA St. 4 at 14-15. Duquesne, on the other hand, would like to delay the CTC and CGC determination until the year before the particular CTC is to be collected from ratepayers. Duquesne St. 5 at 56-62. Duquesne would determine the yearly CGC (and correlating CTC) based on its annual sale of a block of firm power ("the reverse RFP"). Id. at 56; DII M.B. at 78.

The establishment of a fixed schedule of CTC as part of this proceeding is clearly necessary under the Act. Duquesne's proposal for annual adjustments will hinder development of competitive markets. In addition, annual adjustments to the CTC are inconsistent with Commission precedent. See, PECO Restructuring Order, Slip Op. at 103-113; DII M.B. at 78.

The Duquesne proposal to adjust the CTC annually based on the results of a yearly reverse RFP will hinder the development of the competitive market. DII St. 1 at 23-25. In order for customers, and specifically large customers, to effectively participate in the market, customers must have sufficiently stable information to make decisions. DII St. 1-S at 13. Many large customers will want to enter into contracts for a duration of more than one year in order to lock in levelized, long term rates. Customers will not be able to evaluate these contracts if the CTC responsibility for the following year is not determined until Duquesne conducts the RFP. Id. at 12. This will sharply inhibit the willingness and ability of customers to enter into

this longer term supply option that clearly would occur in a competitive market place. DII M.B. at 78-79.

In addition, the fixed CTC methodology was adopted by the Commission in the PECO restructuring proceeding. PECO Energy, Slip Op. at 109-113. As aforementioned, use of the variable CTC injects substantial uncertainty into the supply decisions made by customers. Duquesne's ratepayers deserve at least the same level of certainty afforded to PECO's ratepayers in this regard. DII St. 1 at 25. The spirit of balancing stated in Chapter 28 mandates that the fixed CTC methodology also be used for design of Duquesne's CTC. 66 Pa. C.S. §2802(8); DII M.B. at 79.

Furthermore, use of a fixed CTC strikes the appropriate balance between Duquesne, its shareholders, ratepayers and competitors. 66 Pa. C.S. §2802(8). Under the Duquesne proposal, the variable CTC ensures that Duquesne (and its shareholders) will continue to collect at least the revenues it currently collects for generation. DII St. 1 at 24. The risk of the transition to the competitive market is placed entirely on customers and competitors. First, customers bear the risk that their pricing decision will not be the best deal that could have been made. Second, customers and competitors bear the risk that the price agreed to for electricity transactions will deviate from the results of Duquesne's reverse RFP. Customers and competitors bear the total risk of market price fluctuation, while Duquesne and its shareholders are essentially held harmless. This is not the balancing of interests contemplated by the Act. 66 Pa. C.S. §2802(8); DII M.B. at 79.

The DII approach of establishing fixed yearly CTCs is clearly superior. The Duquesne proposal to have a variable yearly CTC is inappropriate, detrimental to the

development of the competitive market, and contrary to the intention of the Act. The proposal must be rejected. DII submits that the Commission should establish a fixed schedule of CTCs for each year of the transition period as part of this proceeding using the methodology DII recommends. Id. at 80; DII R.B. at 39.

(iv) <u>The PRA's Position</u>

The PRA notes Duquesne desires to calculate actual market rates on an annual basis. Duquesne St. 1 at 6. This actual market price would be established by an auction of a block of power to be conducted annually be Duquesne. It should be noted that this methodology is also used to set the CTC, i.e., on an annual basis. OCA St. 1 at 9; PRA M.B. at 67-68.

The inherent problems and illegality of this annual true up method have been discussed previously, supra. Suffice it to say that the Legislature rejected such a proposal in enacting the Competition Legislation. The Act requires the establishment of the CTC (and by definition the CGC) in <u>this</u> proceeding. There is no provision for an annual true-up of the market price. The Legislature recognized the risk of this method by allowing for full recovery of a just and reasonable level of stranded investment with the ability to correct for variations and customer usage. This ability to correct provides a significant comfort level to utilities which see a decline in sales. Id. at 68.

The Act must be read as a whole and not in independent pieces. It must be read in the context of the entire piece of legislation. Annual calculation of the CTC/CGC was a legislative trade off to allow 100% recovery of a just and reasonable level of stranded investment. Id.

The PRA notes Duquesne is protected regardless of market price reaction. It admits that it is protected when market prices rise above the CGC, Duquesne M.B. at 63, because it is overcollecting the CTC charge. It is further protected if market prices fall below the established CGC because it can purchase power in the open market and its own costs of producing power declines with recovery of stranded costs making it more competitive in the retail generation market. The Act provides appropriate symmetry and adequately protects investors. PRA R.B. at 24.

(b) <u>Determination of Class Responsibility for Stranded Costs</u>

(i) <u>The OCA's Position</u>

The OCA explains 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, OCA witness Lee Smith recommended allocation of stranded cost responsibility to each class on the basis of the production capacity allocator utilized in the Company's last rate case." OCA St. 4 at 9. Ms. Smith pointed out that using a class residual CTC as proposed by the Company, and by DII, will likely produce results which are inconsistent with the allocation of stranded costs on the basis provided in the statute. Id. at 8-9. In particular, customer classes with discounted rates, such as Rule 4 customers, would pay lower CTCs, if CTCs are set as the residual than if they are based on a specific allocation. Id. at 9. Further, if the CTC residual

process were utilized for the entire CTC collection period, then discounted rate customers would end up being subsidized by other customer classes. Id.; OCA M.B. at 66.

In his rebuttal testimony, DII witness Baron contended that use of an allocation approach would violate the generation rate cap for several classes. DII St. 1R at 17. Mr. Baron contends that this will result, because the allocator doesn't reflect the fact that some HVPS sales are either interruptible, or entail "avoidance generation energy" and should result in lower responsibility for capacity. Id. However, as pointed out by OCA witness Lee Smith, the allocator was determined in the last base rate case after consideration of all factors utilized in the last base rate case does not recognize these characteristics. OCA St. 1-S at 7. Thus, Mr. Baron is simply criticizing the allocator as "being outdated or otherwise incorrect." However, the Act does not specifically allow for any "corrections" to previously utilized generation cost allocators. Id. In light of this dilemma, OCA witness Smith recommended that if allocation of the basis of utility production plant would result in violation of the rate cap for some classes, the Company must forgo these revenues "unless, for good cause shown, it requests and is granted a longer collection period for these classes." Id.; OCA M.B. at 66-67.

The Commission's Order in the PECO case adopted Ms. Smith's recommendation for use of the utility production plant allocator. PECO at 109-13. OCA submits that the same approach should be adopted here. OCA M.B. at 67.

In response to DII's position on this issue, the OCA submits that, contrary to DII's assertions, it is DII's proposal to not allocate class responsibility for stranded costs, but to simply make the CTC the residual, that is inconsistent with the Competition Act, which clearly requires that these costs be allocated consistent with the utility production plant allocator.

OCA M.B. at 66-67; 66 Pa. C.S. §2808(a). The Commission agreed with OCA in the PECO case and that recommendation should be adopted here. OCA M.B. at 67. Further, with respect to DII's concern over rate cap violation, OCA submits that, if there is any such problem, Duquesne must forgo these revenues unless, for good cause, it is granted an extension of the CTC recovery period to collect any shortfall from these customers, as OCA witness Lee Smith testified. Id. at 67; OCA R.B. at 24.

(ii) The OSBA's Position

The OSBA finds DII proposed that the CTC component of Duquesne's unbundled rates be determined as a residual after subtracting the unbundled transmission, distribution and estimated market generation components from the current bundled rates. DII St. 1 at 30. DII witness Mr. Baron asserted that since the CTC is calculated as a residual, there is no need to levelize and/or allocate the stranded cost revenue requirement to rate classes over the full transition period. DII St. 1 at 11. Instead, Mr. Baron argued that maximum CTC revenues should be collected, as available, from all rate classes to effectively amortize Duquesne's stranded cost balance as quickly as possible. OSBA St. 1R at 3. The OSBA does not agree. OSBA M.B. at 17.

OSBA witness Mr. Kalcic asserts two reasons why early termination of the CTC recovery period would not be appropriate even where it is otherwise possible: (i) an extension of the CTC recovery period allows stranded costs to be allocated to rate classes – resulting in a more equitable assignment of stranded cost responsibility to rate classes than would be the case in the event of an earlier termination, and (ii) an extension of the time period for stranded cost

recovery could provide all ratepayers with an immediate (1999) rate reduction, independent of their eligibility in the phase-in process; a reduction which would not be available under an "accelerated" amortization proposal such as DII's. OSBA St. 1R at 4. OSBA is not alone in this proceeding in advocating that market-based CGCs be combined with an allocation of the CTC revenue requirement to rate class. The OCA witness, Ms. Lee Smith, also recommended this approach. OCA St. 4 at 9-10; OSBA M.B. at 17-18.

Under the DII proposal, all classes would pay CTC charges equal to the full difference between their existing generation rate cap and the market generation component rates. In essence, classes with more "space" under their existing generation rate cap would pay CTCs for those classes that had less space, until Duquesne recovered its total stranded costs. OSBA St. 1R at 5. This method is inappropriate, since the available margin that a class exhibits under the generation rate cap is a function of its current rates. Id. Those classes, which implicitly pay larger "premiums" for generation, should receive greater benefits from direct retail access. Id. This follows from the premise that competition will eliminate all generation premiums paid by ratepayers. If, however, generation premiums are used to amortize Duquesne's stranded costs as quickly as possible (as is the case in the DII proposal), an interclass shift of CTC cost responsibility from low premium to high premium classes would result, effectively denying the latter classes their proportionate share of benefits during the period of stranded cost recovery. Id at 5-6. This result violates the statutory mandate against interclass and intraclass cost shifting in Section 2808(a) of the Competition Act. 66 Pa. C.S. §2808(a); OSBA M.B. at 18.

The inequity of denying high premium classes their proportionate share of benefits during the stranded cost recovery period can be mitigated by extending the collection of the

CTCs over a longer portion of the statutory seven year period. OSBA St. 1R at 6. The extension of the stranded cost recovery period would provide the opportunity to equitably allocate stranded cost to rate classes in proportion to each class' current share of Duquesne's production-related capacity costs. Id. It would also provide each class with a generation credit that would allow meaningful customer choice. Id.; OSBA M.B. at 18-19.

Moreover, an extension of the recovery period would not require the full residual under the generation rate cap to be used for the CTCs. OSBA St. 1R at 6. This "unused" residual becomes the aforementioned immediate rate reduction, and the second reason not to accelerate the stranded cost recovery period. Id.; OSBA M.B. at 19.

Finally, the OSBA observes that in PECO Energy, the Commission did not adopt an accelerated stranded cost amortization period as advocated by DII witness Baron in this proceeding. Rather, the Commission adopted a plan which allocated stranded costs to rate classes with those costs to be recovered over an 8½ year period. PECO Energy, at 109-110. Accordingly, to be consistent with the Commission precedent established in the PECO Energy, and for the aforementioned policy reasons, OSBA recommends that the DII accelerated amortization proposal should be rejected. OSBA M.B. at 19.

The OSBA notes DII claims that the OSBA's proposal to allocate stranded costs to ratepayers is inappropriate in this proceeding because it would result in cost-shifting and possible rate cap violations. DII M.B. at 80. To the contrary, OSBA asserts that it is DII's proposal with respect to the accelerated recovery of stranded costs that would result in cost-shifting. OSBA M.B. at 18. Further, OSBA asserts that DII's claim regarding possible rate cap violations is disingenuous. OSBA R.B. at 5.

Class allocation-based CTCs cannot be known until such time as Duquesne's total stranded costs and length of recovery period are determined. MAPSA M.B. at 33. Should potential rate cap concerns arise, the Commission can take appropriate steps to adjust the CTC so as to allow for meaningful competition, as it did in its PECO decision. OSBA R.B. at 5.

The OSBA is proposing an allocation of stranded cost responsibility which preserves the meaningful customer choice inherent in the residual-CTC methodology. The difference between the DII proposal and that of OSBA lies in the attempt of DII to collect the maximum available CTC revenues from all rate classes as quickly as possible. OSBA St. 1R at 3. DII asserts that the residual-CTC methodology results in an appropriate assignment of costs without the need for allocations. DII M.B. at 80. OSBA strongly disagrees. OSBA R.B. at 5.

The OSBA does not agree with DII that use of the residual-CTC methodology appropriately assigns the stranded cost revenue requirement to rate classes. DII St. 1 at 11. Instead, the allocation of rate classes affords a more equitable assignment of stranded cost responsibility to rate classes and could provide all ratepayers with an immediate rate reduction. OSBA M.B. at 17-19. Moreover, this potential rate reduction would not otherwise be available under the DII proposal. OSBA R.B. at 6.

Summarily, the OSBA asserts that the DII residual-CTC methodology would violate the statutory mandate against interclass and intraclass cost shifting in Section 2808(a) of the Competition Act. 66 Pa. C.S. §2808(a). However, should the Commission decide to adopt DII's approach, OSBA asserts that it would remain feasible and appropriate to allocate stranded cost responsibility to rate classes. In DII's residual-CTC approach, each class should be allocated it share of the beginning stranded cost balance with CTC revenues tracked by class.

OSBA St. 1R at 8. Each class would then pay (maximum) residual CTCs up to its respective generation rate cap, but with CTC revenues credited against its class-specific stranded cost allocation. In this modified DII approach, CTCs for a given class would end when its allocated stranded cost share was amortized. Id. OSBA's recommended modification would prevent DII's residual-CTC methodology from shifting cost responsibility from low premium to high premium classes. Id.; OSBA R.B. at 6.

(iii) DII's Position

DII finds another dispute regarding establishment of the CTC for recovery of Duquesne's properly claimed, quantified, and recoverable stranded costs is whether the CTC methodology should specifically assign an allocation of the total stranded cost to each rate class. Duquesne and DII do not perform specific allocations of stranded cost to rate classes. Duquesne St. 5 at 56-62; DII St. 1 at 33-34. The CTC residual methodology used by DII and Duquesne results in an appropriate determination of each class's stranded cost liability based on the "stranded" costs currently in bundled rates. DII M.B. at 80.

The OCA and OSBA propose a specific assignment of stranded costs to each class based on a production demand allocation factor. See, OCA St. 4 at 9; OSBA St. 2-R at 2-4. Use of this methodology is inappropriate, because it results in cost-shifting and possible rate cap violations, both of which are prohibited by the Act. 66 Pa. C.S. §§2804(4) & 2808(a). In addition, the residual CTC methodology utilized by DII (and the Company) results in an appropriate assignment of these costs without the need for complex allocations. The DII residual CTC methodology should be accepted by the Commission. DII M.B. at 80.

Although the allocated methodology was accepted in the PECO proceeding, use of that methodology would be inappropriate for this proceeding because it would result in needless violations of the rate cap and anti-cost shifting provisions of the Act. 66 Pa. C.S. §§2804(4) & 2808(a). Proposals submitted by the OCA and the OSBA violate the generation rate cap provision of the Act for a number of rate schedules including rate HVPS. DII St. 1-R at 17; DII St. 1-S at 18-19. Although OCA acknowledges the potential for rate cap violation, it offers no definitive solution; OCA simply states that the rate cap will take precedence. OCA St. 4-S at 7. DII submits that this represents a fundamental flaw in the allocated CTC methodology. It is inequitable to endorse such disparate treatment of customer class. 66 Pa. C.S. §2804(7). This situation is clearly antithetical to the development of the competitive market envisioned by the Act. DII M.B. at 80-81.

In addition, use of the allocated CTC methodology will result in the need for complex allocations regarding services such as Interruptible Service, Generation Avoidance Energy and special contracts. If these customers, who currently take service under rate HVPS are assigned fully loaded transmission and distribution charges, expected market generation costs, and fully allocated CTC revenues, the total rate will exceed the customers' current rates. DII St. 1-R at 17; DII St. 1-S at 18-19. If the allocation methodology is not adjusted to account for Interruptible Service, Generation Avoidance Energy and special contracts, the resulting CTC violates the rate cap and shifts recovery of stranded costs away from other ratepayers. Id.; DII M.B. at 81.

Stranded costs must be unbundled as they are contained in current rates. Pursuant to this allocation methodology the Act prohibits interclass or intraclass cost shifting. 66 Pa.

C.S. §2808(a). The OCA blindly adheres to its allocation methodology by stating "the Act does not specifically allow for any corrections to previously utilized allocators." OCA St. 4 at 7. However, the Commission in developing the CTC for the recovery of Duquesne's stranded costs must adhere to both of the requirements. 66 Pa. C.S. §2808(a). To blindly adhere to an obviously flawed allocation methodology, despite concrete evidence of unauthorized cost shifting, is clearly unwarranted under the Act. Id.; DII M.B. at 81.

Moreover, the residual CTC methodology proposed by DII is entirely consistent with the Act's directive on cost shifting and allocation issues. 66 Pa. C.S. §2808(a). The residual CTC methodology calculates stranded cost responsibility based on the difference between the generation-related cost within each class's current rates (the total generation component of the rate) and the anticipated market price for that rate. DII St. 1-S at 18. The difference between embedded costs in current rates as determined and allocated in the last base rate proceeding, and the current anticipated market price for each rate schedule is the true stranded cost created by customers in that rate schedule by the opportunity to access the competitive market. Id. Thus, the residual CTC methodology adheres to the rate cap provision of the Act, the anti-cost shifting provision of the Act, and the concept that stranded costs should be allocated in the manner implicit in the rates established in the last base rate proceeding. 66 Pa. C.S. §2808(a); DII M.B. at 81-82.

It is unnecessary to specifically allocate portions of Duquesne's total stranded costs to rate schedules for recovery. The residual CTC methodology used by DII permits CTC establishment that complies with the Act without need for complex adjustments to an allocation factor. In addition, if the OCA/OSBA recommendations are accepted, the generation rate cap

is exceeded unless the allocation factors are adjusted. OCA and OSBA do not provide an adequate adjustment to address DII's concerns. DII submits that use of the CTC residual methodology is clearly the superior approach that should be accepted to determine each rate class's stranded cost responsibility. Id. at 82.

DII notes the OCA and OSBA object to the DII proposal on two general bases. First, they object to the DII proposal on the basis that it represents an interclass cost shift. OSBA M.B. at 18; OCA M.B. at 66. Second, OSBA objects to the DII proposal because it accelerates recovery of stranded costs rather than providing for immediate rate reductions. OSBA M.B. at 17-19. Both of these arguments are misguided. DII R.B. at 39.

The DII proposal does not shift interclass cost responsibility. DII proposes to allocate stranded cost recovery to classes based on a CTC residual methodology. DII M.B. at 80-82 & 87. The CTC residual methodology subtracts an expected market price from the capped generation component of current rates to determine CTC responsibility. Id. The OSBA objects to the DII proposal using the following argument:

> This method is inappropriate since the available margin that a class exhibits under the generation rate cap is the function of its current rates. Those classes which implicitly pay larger "premiums" for generation should receive greater benefits from direct retail access. This follows from the premise that competition will eliminate all generation premiums paid by ratepayers. If, however, generation premiums are used to amortize Duquesne's stranded costs as quickly as possible (as is the case in the DII proposal), an interclass shift of CTC cost responsibility from low premium to high premium classes would result, effectively denying the latter classes their proportionate share of the benefits during the period of stranded cost recovery.

OSBA M.B. at 18 (citations omitted). OSBA's argument is flawed in two respects. DII R.B. at 39-40.

First, the OSBA (and OCA) are incorrect that so-called lower premium rate classes should face a lower CTC responsibility. If regulation continued, Duquesne would collect less revenue per kWh from lower premium rates than from higher premium rates. In some cases, this lower premium is because alternative supply possibilities exist, such as a customer switching to fuel oil. In other cases, the lower premium exists because of a specified usage constraint in the rates (such as interruptible service) or because of a higher load factor usage by customers on that rate schedule. By permitting the lower premium classes to access the competitive market, Duquesne loses the revenue difference between the current capped generation component of those class rates and whatever price Duquesne can obtain for the sale of the same amount of load that the former low premium customers used. Under the DII proposal, each customer class is responsible for this difference between the current capped rate and the price that Duquesne can obtain on the open market for sale of the same electricity, which Duquesne's true "stranded cost" caused by that class's access to competitive supply. DII M.B. at 80-82; DII R.B. at 40.

Second, although OSBA is correct that competition is expected to eliminate some of the differences in class premiums, this will occur only after the CTC is eliminated and all customers can purchase electricity freely on the market. After these premiums are eliminated, customers in the former "higher premium" classes will receive greater long-term benefits from competition. Assuming the alleged "premiums" are artificially created because of the lack of competition, the "higher premium" rate classes will gain savings in the amount of that premium when full competition is realized; the "lower premium" will logically gain less savings.

Consequently, it is appropriate for higher premium classes to bear a proportionately higher share of the CTC responsibility. DII R.B. at 40-41.

The OSBA also faults the DII proposal for not providing immediate rate reductions. OSBA M.B. at 17-19. OSBA states "an extension of the time period for stranded cost recovery could provide all ratepayers with an immediate (1999) rate reduction, independent of their eligibility in the phase-in process; a reduction which would not be available under an 'accelerated' amortization proposal such as DII." OSBA M.B. at 17-18 (citations omitted). The OSBA argument is short-sighted. The Commission recognized in the PECO proceeding that stranded cost recovery is a significant interference in the operation of the competitive market. PECO Energy, Slip. Op. at 15. If OSBA truly believes that competition will eliminate the premiums that exists between class rates, then OSBA should logically desire to eliminate any interference with the competitive market as soon as possible. OSBA appears content to sacrifice the longer term development of a robust competitive market for an immediate quick fix in the form of rate reductions. OSBA is misguided. DII R.B. at 41.

In addition, the Act clearly contemplates that stranded cost recovery be terminated as quickly as possible: "The competitive transition charge shall be included on bills to customers for a period not to exceed nine years from the effective date of this chapter unless an alternative payment methodology is mutually agreed upon by the customer and the utility or unless the Commission in its discretion and for good cause shown orders an alternative payment period." 66 Pa. C.S. §2808(b). In addition, the rate caps provided by the Act apply for a specified time "or until an electric distribution utility is no longer recovering its transition or stranded costs through a competitive transition charge or intangible transition charge . . .

whichever is shorter . . . ." Id. §§2804(4)(i) & (ii). The Act specifically acknowledges and requires that the CTC recovery period be accomplished as quickly as possible. DII R.B. at 41.

DII explains its proposed CTC residual methodology appropriately allocates stranded cost responsibility classes in a manner that is both consistent with the utility's last base rate case and that does not affect inter-class cost shifting. See, DII M.B. at 75-87. The DII proposal fulfills both requirements of Section 2808(a) of the Act. The OSBA and OCA, in their attempt to adhere blindly to the production capacity allocator, submit proposals that promote interclass cost shifting and violate the rate cap. The OCA and OSBA proposals to determine stranded cost responsibility on a customer class basis must be rejected. DII R.B. at 41-42.

(iv) HSS/ARI's Position

HSS/ARI observe a separate problem concerning Duquesne's CGC and CTC rate design results in an overstatement of particular classes' stranded cost responsibility in the event that Duquesne is authorized to recover any such amount. It should be noted that the overstatement of stranded cost responsibility does not require a reallocation of costs, although, in effect, Duquesne is shifting stranded cost responsibility among classes in violation of the Act. 66 Pa. C.S. §2808(a); HSS/ARI M.B. at 84.

The problem is identified in Mr. Lahtinen's testimony. He stated that 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 St. 5 at 25. That reduction obviously was required and is appropriate. HSS/ARI M.B. at 85.

However, for certain other rate classes, "where costs are below revenue levels, [Lahtinen] adjusted the generation component to meet, but not exceed, 1996 revenues." Duquesne St. 5 at 25:5-7. That latter upper adjustment clearly is inappropriate. HSS/ARI M.B. at 85.

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. According to Mr. Lahtinen, the classes whose revenue responsibility was written up would be those whose allocated cost of service is less than the allocated 1996 revenues on page 2 of Exh. JAL-3 at 2. Thus, Duquesne's rate proposal should be modified by reducing revenue responsibility for the following classes: RS, GS/GM, GL, SH and Traffic Lights. See, Exh. JAL-3 at 2; HSS/ARI M.B. at 85.

(v) The PRA's Position

The PRA posits stranded costs should be allocated in the manner required by the Commission in the PECO proceeding. PRA M.B. at 68.

(c) Levelized CTC v. Other Methods

(i) The OCA's Position

The OCA recommends the establishment of a levelized rate reduction. As shown on Exh. LS-7 (Revised), a levelized rate reduction calculated to allow full recovery of stranded

costs, produces a declining CTC because of the estimated increase in market prices. Using this approach, Ms. Smith calculated sample residential rates. OCA recommends this approach. OCA M.B. at 67.

(ii) <u>DII's Position</u>

DII finds another issue related to the CTC methodology is whether a levelized CTC will be used. The use of a levelized CTC provides for the recovery of approximately the same portion of the Company's stranded cost during each year of the transition period. The opposite of the levelized recovery would be a CTC that varies each year based on factors such as expected market price or, theoretically, based on no rational factor at all. <u>See</u>, e.g.,, OCA St. 4 at 14-15; DII M.B. at 82.

Use of a levelized CTC for the recovery of Duquesne's stranded costs may be inappropriate, because, depending on the total stranded costs authorized in this proceeding, levelizing recovery of those costs over the transition period may prevent some customers from participating in the competitive market. Unlike the residual CTC methodology, under a levelized recovery, no inherent relationship exists between the expected market price in a year and the CTC to be recovered from the customer during that year. DII St. 1 at 32-34. Because of the rate cap, unless a relationship is manufactured between the levelized CTC and the market price, the total of the allocated CTC revenues in any given year, plus the anticipated market price could exceed the rate cap. In such situation, customers would logically return to the utility's bundled service and abandon the competitive market. Ironically, because market prices are expected to rise throughout the transition period, this "customer flight" back to bundled

service could occur in the latter years of the transition period when the goal should be to encourage the further development of a robust competitive market. DII M.B. at 82-83.

The use of a levelized CTC that does not have an inherent correlation with the expected market prices will thrawt the pro-competitive goals of the Act. Neither the OCA nor the OSBA proposal contains any relationship to the anticipated market price of electricity; as a result, DII shows each will violate the rate cap for HVPS customers. DII St. 1-R at 17; DII St. 1-S at 18-19. Because neither party has adequately addressed this obvious flaw in the allocated levelized CTC methodology, DII respectfully requests that the Commission reject the levelized CTC. DII M.B. at 83.

DII notes the OCA proposes a levelized rate reduction with a declining (not levelized) CTC. OCA M.B. at 62. As DII shows, however, the OCA proposal violates the rate cap for some customer classes and must be rejected. See DII M.B. at 75-83, 86-87. Both a pure "levelized" CTC approach and the OCA's approach are inappropriate and should be rejected. DII R.B. at 42.

(iii) The PRA's Position

The PRA argues the CTC should be calculated in this proceeding. It should be adjusted solely on the basis of variations in sales as required by the Act. 66 Pa. C.S. §2808(f). The Act clearly rejects the creation of a levelized CTC. Again it should be recalled that the Act contemplates a radical departure from existing ratemaking principles. The Legislature did intend for the parties to achieve certainty in pricing or rates. Rather, for better or for worse, the

Legislature has mandated that "competitive forces" shall now set generation prices in this Commonwealth. PRA M.B. at 69.

A levelized CTC recovery period is consistent with the Act. The actual CTC unit rate will change, however, from year to year because of the reconciliation required by the Statute. Thus, contrary to DII's claims, it is impossible to create a relationship between the CTC and CGC even under the residual CTC methodology. PRA R.B. at 25.

(iv) The Environmentalists' Position

The Environmentalists contend that the Act implies straight amortization of stranded costs.[175] Reconciliation should be structured to recover the stranded costs in equal annual amounts. This will conform to §2808(f) and will most closely resemble the market, where prices fluctuate because of natural market conditions but not because of a misplaced attempt to engineer rates. The Environmentalists recommend that the CTC recovery be equal throughout the collection period, and because of the assumption of a slight load growth, the kilowatt-hour CTC charge should be able to decrease slightly over time. Env. M.B. at 29-30.

(d) Duquesne's Rate Redesign Proposal

(i) Duquesne's Proposal

Duquesne has proposed to redesign its rates in a manner that "will allow customers to make more efficient consumption decisions, while also providing additional revenues that can be applied to mitigate stranded costs." Duquesne St. 1 at 11. Duquesne's rate

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[175] 66 Pa. C.S. §2808(f).

redesign proposal "mov[es] a significant portion of generation-related costs into a fixed customer charge, which results in a lower variable (per kWh) charge than exists today." Id. This, in turn, produces a reduction in marginal rates of 25% on average and a 50% reduction in rates for residential customers, thereby moving rates much closer to the marginal cost of production. Duquesne St. 5 at 34. These more efficient rates will encourage increased usage, which will increase stranded cost mitigation. Duquesne St. 1 at 11; Duquesne St. 5 at 33.[176] While the dollar impact of this mitigation is difficult to predict, it may equal or exceed $15 annually. Duquesne St. 5 at 34. The proposal also has no downside: there is no cost-shifting between classes and "no customer will pay more than he does today" for the same level of usage. Id. at 32; Duquesne M.B. at 65.

Despite the clear efficiency of this proposal, and its significant mitigation benefits, a range of parties oppose it. These parties essentially raise three arguments. The first is that it "shifts risk" from shareholders to ratepayers by moving a portion of stranded costs into a fixed customer charge. DII St. 1 at 51-52; OCA St. 2 at 8. This is incorrect and, in any event, is no longer even an issue. First, the assertion would be true only if Duquesne's customer demand fluctuated widely each year, thereby posing significant risks if fixed costs were recovered solely through a variable charge; however, no party alleges such facts and they do not exist. Duquesne's customer demand is relatively flat, increasing slowly each year. Duquesne Exh. DJC-3 at 2. As Dr. Makholm testified, "it is my opinion that the fixed customer charge will have little or no effect on Duquesne's risk." Duquesne St. 12 at 37. Second, and in any

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[176] Mr. Lahtinen explained the derivation and effect of the redesigned rates, and the underlying assumptions regarding demand elasticity, in excruciating detail in direct testimony. Duquesne St. 5 at 32-47.

event, in response to the concerns of the intervenors, Duquesne has now made the rate redesign optional for customers. Duquesne St. 5-R at 45. This means that, for customers that expect their usage to drop, they can choose not to use the rate redesign;[177] and for customers that expect their usage to increase, they can select rate redesign and reduce their marginal rates significantly. Duquesne M.B. at 65-66.

The second criticism is that the proposal "shifts costs" between customers and/or rate classes, which is a meritless contention advanced only by MAPSA's Mr. Russell. As other witnesses concede (albeit grudgingly),[178] and as Mr. Lahtinen demonstrated in detail, cost shifting is simply not possible under Duquesne's proposal:

> 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 Duquesne Exh. 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 maintains 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

[177] Despite this offer of optional service, the OCA's Ms. Smith, in surrebuttal, continued to oppose the rate redesign proposal; however, given that she did not mention this offer, and her continued concern regarding customers that reduce their usage and hence pay more (on a total $ basis) with a fixed customer charge, OCA St. 4-S at 8, it is not clear she was aware of the offer.

[178] DII St. 1 at 52 ("specific costs have not been explicitly shifted under the Company's proposal").

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 rate class.*

Duquesne St. 5-R at 41 (emphasis in original). Mr. Russell's unwillingness to acknowledge this obvious point (MAPSA St. 1-S at 6) is "intellectually indefensible." Duquesne St. 5-R at 6; Duquesne M.B. at 66-67.

The third claim is the OCA contention that the redesigned rates may be too low – i.e., that they may not even "equal . . . the full marginal cost" of providing distribution service. OCA St. 4 at 8. As Mr. Lahtinen explained, however, this is a baffling assertion (Duquesne St. 5-R at 39) given that OCA has claimed that Duquesne's rates "must" be reduced (OCA St. 1 at 15) and has proposed reducing them by 18%. OCA Exh. LS-4. Tellingly, the OCA offers no evidence in support of this assertion (OCA St. 4 at 8) and, as Mr. Lahtinen explained, it is meritless. Duquesne St. 5-R at 44-45; Duquesne M.B. at 67-68.

In sum, Duquesne's rate redesign proposal should be accepted, including the modification that makes redesign optional for customers; with that modification, there is no legitimate reason for not approving the proposal. Id.

(ii) The OCA's Position

The OCA explains the Company has proposed a two-part Customer Transition Charge which includes a fixed (customer-specific) charge and a usage-based (class-specific) charge, based on the Company's view that a lower usage-based charge will encourage greater consumption and, thereby, mitigate stranded costs. Duquesne St. 5 at 32-47. The result is a relative increase in fixed cost recovery from customers who use less generation, and a relative

reduction in rates for customers who use more. OCA submits that this is an unreasonable result. OCA submits that the efficiency benefits of the rate redesign are speculative and the proposal should be rejected. OCA St. 4 at 8; OCA 4-S at 7-8. OCA submits that promotional rates that encourage greater energy usage are inappropriate. OCA M.B. at 67.

The OCA finds this proposal is a promotional rate that rewards customers with higher energy usage by reducing the burden of the CTC for those customers. OCA disagrees with this plan because it provides greater fixed cost recovery from ratepayers than under current rates at the same time that the Company will be collecting fewer costs as some customers obtain their generation service from competitive suppliers. The Company claims that the proposal has no downside and may increase revenues because usage rates are lower. While the Company argues that customer demand is relatively flat and that the fixed customer charge will have "little or no effect on Duquesne's risk," OCA submits that these claims are unproven and the proposal should be rejected in favor of a usage charge to collect the CTC. See, also, Env. M.B. at 31-32 (urging rejection of this rate that encourages sale of additional electricity). OCA R.B. at 24.

(iii) The OSBA's Position

The OSBA relates through the Company's rate redesign plan, Duquesne proposes to reduce current rate levels over 25% on average for consumption above 1996 levels. Duquesne St. 5 at 31. This proposed rate reduction on incremental usage has a dual purpose: (i) to provide more efficient price signals, and (ii) to encourage economic load growth. Id.; OSBA M.B. at 19.

The CTC forms the cornerstone of the Company's rate redesign. As originally filed, the Company proposed to split its CTC charge into two components: (i) a variable usage charge, and (ii) a customer-specific fixed charge.[179] The variable CTC charge would be set at a level which would significantly lower the current total charge associated with energy usage. Duquesne St. 5 at 31. The resulting discount that would be associated with a customer's baseline consumption would be recouped in the form of a customer-specific fixed CTC charge. If a customer's usage level post-restructuring is unchanged from those established in 1996 (the Company's baseline year), the customer would experience the same total bill after unbundling. OSBA M.B. at 19-20.

On the other hand, the Company's initially proposed fixed CTC charge would result in larger bills for any customers with baseline consumption levels that were higher than normal. For example, a higher than normal baseline consumption could be expected if a consumer upgraded to more energy efficient appliances post-1996. OSBA St. 1 at 13. Additionally, the same would hold for a consumer who elected to weatherize his or her home with more efficient windows, caulking, and insulation post-1996. Moreover, as Mr. Kalcic stated, a business customer who experienced an exceptional sales year in 1996 might also exhibit an "inflated" baseline usage level. Id. In all of the aforementioned scenarios, the customer would be worse off due to the Company's rate redesign. OSBA M.B. at 20.

The Competition Act at Section 2808(a) states that stranded costs should not be recovered from customer classes in a manner that causes either inter-class or intra-class cost

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[179] As discussed below, Duquesne later modified its rate redesign plan to give the customer the option of an all variable CTC.

shifts. 66 Pa. C.S. §2808(a). The Company's plan, as initially proposed, violated Section 2808(a) of the Competition Act. OSBA M.B. at 20.

Recognizing the above, the OSBA advocated an amendment to the Company's original plan whereby a customer could select an all-variable CTC or a fixed/variable CTC dependent upon which plan would best suits the customer's needs and anticipated consumption. OSBA St. 1 at 14. OSBA asserted that providing a customer option within the rate redesign plan would afford it an opportunity to produce the elasticity-related benefits that the Company attributed to its plan while eliminating its inherent inequities. Id.; OSBA M.B. at 20.

The Company adopted the amendment proposed by OSBA, noting that this change causes its rate redesign plan to be more reasonable with respect to the customer's interests. Duquesne St. 5-R at 45. The OSBA agrees. OSBA M.B. at 21.

(iv) DII's Position

DII notes Duquesne proposes a mandatory rate redesign that collects 50% of the customer's monthly CTC charge on a fixed dollar per month basis and 50% on a consumption basis. See, Duquesne St. 5 at 63-69. DII submits that the Commission must reject this proposal because, as set forth in more detail below, it violates the rate cap and anti-cost shifting provisions of Chapter 28 (66 Pa. C.S. §§2804(4) & 2808(a)) and because Duquesne has presented no valid justification for the extraordinary proposal. In addition, the proposal is contrary to the purpose and intent of Chapter 28 because it harms all customers whose load may be decreasing due to negative business concerns. DII M.B. at 83.

The Duquesne proposal violates the rate cap and anti-cost shifting prohibitions contained in Chapter 28. 66 Pa. C.S. §§2808(a) & 2808(4). The rate redesign amounts to a "take-or-pay" charge for 50% of stranded cost recoverable by Duquesne. DII St. 1 at 49-53. No such take-or-pay liability is currently in Duquesne's bundled rates for large service customers Consequently, on a risk adjusted basis, Duquesne customers forced to use the rate redesign will pay higher rates than they will otherwise pay under currently applicable bundled service rates. Id. at 52. The "redesign" changes cost allocations based on embedded costs in Duquesne's bundled rates that are specifically mandated to remain constant under Chapter 28. 66 Pa. C.S. §2808(a). A proposal with such blatant defects cannot be accepted by the Commission. DII M.B. at 84.

In addition, the Duquesne proposal is contrary to the economic development goal of Chapter 28 regarding retention of businesses in the Commonwealth. One of the policy findings of Chapter 28 is that "the cost of electricity is an important factor in decisions made by businesses concerning locating, expanding and retaining facilities in this Commonwealth." 66 Pa. C.S. §2802(6) (emphasis added). As OSBA explains:

> Duquesne proposes to make its rate redesign mandatory for all customers. Accordingly, the Company's proposed Fixed CTC charge will result in larger bills for all customers with baseline consumption levels that are for any reason higher than normal (compared to the all-variable CTC case). Relative to existing rates, this equivalent to a shift in CTC revenue responsibility from customers with growing loads to customers with declining loads.

OSBA St. 1 at 13-14. The Duquesne proposal is clearly inconsistent with the business retention purposes of the Act because the Duquesne proposal will place higher costs on a struggling business at the precise time that the business must be cutting costs to survive. The Duquesne

proposal will either cause the business to fail or to move to a more cost-effective environment. A proposal that obviously impedes the economic development purposes of the Act must be rejected. DII M.B. at 84.

Furthermore, the Duquesne rate design is an exclusively self-interested proposal. Through the customized rate design, Duquesne is able to inappropriately shift to customers the risk of the variability of usage. DII St. 1 at 51. The imposition of this take-or-pay charge substantially reduces the risk of recovery associated with 50% of the otherwise applicable stranded cost recovery through the CTC charge. Id. This proposal benefits only Duquesne and must be rejected. DII M.B. at 84-85.

This shifting occurs without valid justification from the Company. The Company failed to produce any evidence to support its claim that economic efficiency will be enhanced by the proposal. Id. Because the proposed rate has not become effective, Duquesne has the burden of establishing its reasonableness. 66 Pa. C.S. §§315(a) & 332(a). The only evidence produced by Duquesne is the unsupported assertion of efficiency gains. DII has clearly demonstrated that the proposal has serious anti-competitive effects and otherwise violates Chapter 28. DII M.B. at 85.

The proposed rate redesign inappropriately shifts the risk of recovery for a substantial portion of Duquesne's stranded costs away from the Company and on to ratepayers. This shift violates the rate cap and anti-cost shifting provisions of the Act. DII submits that the proposal is unreasonable and without valid justification. The proposed rate redesign should be rejected. Id.

In its rebuttal testimony, the Company states that it will offer its rate redesign on an optional rather than mandatory basis. Duquesne St. 5-R at 45. In the event that the Commission rejects DII's arguments to completely eliminate the rate redesign, the Duquesne alternative proposal would be acceptable. DII St. 1-S at 14; DII M.B. at 85.

DII further observes Duquesne expends considerable effort to justify its rate redesign proposal, which it has now made optional. Duquesne M.B. at 65-68. As DII illustrates, the Duquesne proposal is clearly inappropriate, because it amounts to a "take-or-pay" charge for 50% of a customer's stranded cost. DII M.B. at 83-85. This take-or-pay liability significantly reduces, if not eliminates, any risk that Duquesne could not recover that amount of stranded cost in the fixed portion of the rate. Id. The Duquesne proposal is clearly inappropriate and must be rejected. DII R.B. at 42.

(v) <u>The PRA's Position</u>

The PRA finds Duquesne proposes to radically modify its existing rate structure. It proposes to unbundle its charges so that a portion of the CTC is collected through a fixed charge component while the residual is collected in the energy rate. There are several problems with this methodology. PRA M.B. at 69.

As the OCA explains, Duquesne has not conclusively shown that its proposal results in a more efficient charge since it has not presented a marginal cost study demonstrating that such charges are equal to full marginal cost. OCA St. 4 at 8. Further, as noted by DII, the implication of this unjustified, radical change is that (i) the fixed cost component is paid regardless of consumption and thus equates to a take-or-pay charge; (ii) 89% of Duquesne's

stranded costs will be recovered on a fixed (i.e., non-usage) basis; (iii) the proposal shifts a substantial risk of the market transition to customers by eliminating any potential variability due to usage changes (recall that the reconciliation mechanism eliminates the variations in usage issue); (iv) Duquesne is assured that half of its stranded costs is recovered on a risk-free, levelized basis greatly increasing its cash flow; and (v) the proposal inappropriately shifts the risk associated with the move to a competitive retail generation market from shareholders to customers for a substantial portion of Duquesne's future revenue requirement. DII St. 1 at 50-53; PRA M.B. at 69-70.

(vi) <u>The Environmentalists' Position</u>

The Environmentalists oppose the rate redesign proposal, which Duquesne has attempted to insert into its restructuring plan. Duquesne proposes to shift costs from volume-based charges to fixed customer charges. The Environmentalists oppose this change for several reasons. Env. M.B. at 31.

First, in rate cases where the utility wants to completely redesign rates away from the rate design principles which have been followed for a long period of time, the general rule is that extensive and detailed studies are require to justify the change. The justification provided in this docket would not be adequate to support such a major change in rate design if this were a rate case. The restructuring docket should not be used as an opportunity for Duquesne to implement rate design changes without proper and adequate scrutiny. Id.

Second, this new rate design is a promotional rate which will encourage the sale of additional electricity and discourage energy efficiency and conservation. The use of a fixed charge serves to artificially reduce the cost of electricity the more a customer purchases. Id.

Third, the use of a fixed charge causes the burden of stranded cost recovery to disproportionately affect low energy users and low-income customers, thus causing an intra-class shifting of rates. Id. at 32.

The Environmentalists recommend that the Commission reject this rate redesign as unsound and inappropriate and require the Company to structure the CTC on a mils per kWh basis. The Company can insure against the risk of under-collection by implementing a true-up at the end of each year. Id.

For the same reasons, the Commission should reject any proposal to collect transmission and distribution costs on a fixed charge rather than a per kWh basis. Id.

(vii) MAPSA's Position

MAPSA relates Duquesne has proposed to calculate and collect a customer-specific competitive transition charge. In essence, Duquesne's proposal is to use a previous years' usage to determine a customer's future year total CTC allocated share and then to charge a customer a fixed CTC based upon the previous years' usage. MAPSA M.B. at 27.

Duquesne's proposal is contrary to law. First, the proposal violates the Commission's mandate that CTCs be charged on a per-kWh basis. See, PECO at 111. To do otherwise does not send the appropriate consumption signals to consumers. If a customers' usage in a succeeding year declines, under Duquesne's proposal, the customer will not recognize

a concomitant reduction in its CTC. Therefore, the Duquesne proposal imposes a penalty upon customers who, for whatever reason, may reduce their consumption. MAPSA M.B. at 27-28.

Duquesne's proposal tends to encourage increased consumption by allowing customers to maintain a one-year buffer in the growth of any CTC rates by only recalculating the customers' CTC share on an annual basis. If a customers' usage increases dramatically in a given year, the customer will not see a resultant increase in its CTC allocation until the succeeding year. As pointed out by MAPSA witness Russell, MAPSA St. 1 at 37, Duquesne's proposal has the potential to cause intraclass cost shifting. The Act specifically prohibits the development of a CTC, which will "shift . . . intraclass costs." 66 Pa. C.S. §2808(a). Under Duquesne's proposal it is possible that two customers in 1999, having the exact same load, will pay different CTCs. The reason is that the CTC will have been computed based upon the customers' 1996 load. Another factor to consider is the fact that, while Duquesne and the intervenors characterize the fixed monthly CTC as "customer-specific," the charge is actually premise-specific. Namely, the CTC is calculated for each meter, regardless of the occupant of the premises. It is easy to imagine a situation where different residents of the same premises will have widely varying consumption patterns. MAPSA M.B. at 28.

Duquesne's fixed, customer-specific, CTC collection proposal is potentially discriminatory among customers, causes intraclass cost shifting, and, quite possibly, will prove to be competitively disadvantageous to similarly-situated customers. For these reasons, Duquesne's proposal should be rejected. Id.

(e) Other Conceptual Disputes

(i) The OCA's Proposals

(1) Calculation of the CGC/Avoidable Generation Credit

Company witness Lahtinen proposed to determine the CGC - the avoidable generation credit - by taking the market price established in Duquesne's RFP, developing rates for each individual rate class based on hourly market values and class load shapes, and then adjusting that price for transmission and (as modified in rebuttal) distribution losses and gross receipts tax. Duquesne St. 5 at 56-57: Duquesne St. 5-R at 21-22 & JAL-15. Sample pro forma CGCs are shown in Exh. JAL-11 for each rate class based on the most recent RFP. OCA M.B. at 67-68.

Consistent with OCA's recommendations, OCA witness Lee Smith designed the CGC beginning with the use of Mr. Smith's market price projections which are presented as an all-hours market price. OCA St. 4 at 11. Because data for each rate class was unavailable, Mr. Smith also calculated a load-following market price using the combined Duquesne and APS load shape for 1999 through 2005. Id. Ms. Lee Smith then adjusted these market prices for line losses using the ratio of total generation to total sales as reported in FERC Form 1, which was 5.1% and for GRT. Id. These calculations are shown in Exh. LS-2. Id. Ms. Smith testified that class specific CGCs should be calculated from class load shapes when such data is available. Id.; OCA M.B. at 68.

Ms. Smith then adjusted this price to reflect normal costs that will be required to bring this power to the retail market. OCA St. 4 at 11-12. These include "administrative and general costs that will be required to market, aggregate load, reconcile load and supply, write

contracts" and other activities necessary to get power to customers. Id. Ms. Smith estimated these costs from the Company's COS study, including pensions, benefits and insurance that are reflected in on-going production costs, regulatory expenses, and other A&G, consistent with Mr. Catlin's allocation of A&G in his testimony. Id. The result is an addition of 0.368¢/kWh ($1999) which she adjusts for inflation through the CTC recovery period. OCA St. 4-S at 8-9; Exh. LS-7 Revised. OCA M.B. at 68.

While Company witness Lahtinen contends that there is evidence that marketers are willing to serve retail customers at levels close to (or even below) wholesale market prices, Mr. Lahtinen misses the point. Duquesne St. 5 at 62. The point is that by recovering through the regulated portion of rates costs that competitive suppliers incur, the Company gains an unfair competitive advantage. OCA St. 4 at 13. OCA submits that this adjustment should be adopted. OCA M.B. at 68.

(2) <u>Class Reconciliation of CTCs</u>

Consistent with the statutory requirement for annual reconciliation and with OCA's proposal to allocate stranded costs by rate class, stranded costs should also be reconciled annually on a class-specific basis. OCA St. 4 at 14-16. This approach is necessary to avoid inter-class stranded cost shifting and was specifically adopted in the <u>PECO Order</u>, Slip Op. at 113. OCA M.B. at 69.

(3) **ECR Roll-In Issue**

The Company proposes to roll its Energy Cost Rate (ECR) in at a rate higher than was in effect on January 1, 1997. Duquesne St. 2 at 8. Specifically, the Company proposes to include energy costs at a rate of 14.7 mills/kWh even though the applicable rate at the effective date of the Act was only 12.8 mills/kWh. Id., n.1. The Company claims that it should be entitled to charge a rate of 14.7 mills/kWh because the Ft. Martin settlement established this as the cap on ECR rates. Id.; Duquesne St. 5-R at 59-60; OCA M.B. at 69.

While OCA's proposal to provide immediate rate reductions would render Duquesne's proposal moot, OCA submits that, if a different approach is adopted, rates should not be permitted to be implemented at a level which is higher than was in effect on January 1, 1997, the effective date of the Act. 66 Pa. C.S. §2804(4)(ii). Although Duquesne's rate cap could reflect the higher rate allowed in the Fort Martin settlement, the Company is not entitled to that higher rate unless it is justified by higher actual fuel costs. Furthermore, as OCA witness Kahal testified, the rate increase should be rejected because the Company's own projections indicate that Duquesne's earnings are expected to be very strong and its rates are already among the highest in the state. OCA St. 1 at 12; OCA M.B. at 69.

(ii) **DII's Position**

DII notes the OCA proposes that the statutory annual reconciliation of the CTC must be done on a class-specific basis. OCA M.B. at 68-69. DII acknowledges that the Commission adopted this approach in the PECO decision. DII continues to believe, however, that it is not appropriate to reconcile and track stranded cost on a class specific basis. DII St.

1 at 31. Tracking and reconciliation on a class basis will lead to different CTC termination times for each customer class. This does not result in an orderly transition to competition as required by the Act. See, 66 Pa. C.S. §2804(14). DII respectfully requests that the OCA proposal be rejected. DII R.B. at 42.

(iii) The Environmentalists' Position

(1) Reconciling on the Basis of Market Price

The Environmentalists explain true reconciliation of the CTC requires reconciliation of the difference between the projected market price and the actual market price. The Environmentalists have already addressed the weaknesses of Duquesne's proposal to fix a market price by selling a block of power each year on the open market. Env. M.B. at 32.

(2) Reconciling on the Basis of Sales

To avoid an over-recovery of stranded costs, the Environmentalists claim the CTC should be reconciled to reflect changes in sales. Because the CTC are charges added to each kilowatthour, the total CTC recovery is directly dependent on the number of kilowatt-hours sold throughout the collection period. Even a very small discrepancy between projected sales and actual sales will result in a large difference in collections. The Act directs the Commission to "establish procedures for the annual review of the competitive transition charge" and to "reconcile the annual revenues received from the charge" at the approved level[180] and it should do so. Env. M.B. at 32-33.

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[180] 66 Pa. C.S. §2808(f).

(c) Reconciling Without Cost Shifting

In designing the reconciliation mechanism, the Environmentalists assert it is critical to prevent cost shifting between customer classes. The CTC should be assigned to each class and reconciliation should occur within each class.[181] This is important because of the different growth rates for the different classes. For example, if high growth is experienced in the residential class, and low growth in the industrial class and reconciliation was calculated on a system-wide basis, CTC recovery would be shifted to residential customers from the industrial customers.[182] With reconciliation by class, the residential CTC charge under this scenario would be reduced or shortened (to reflect the faster recovery) and the industrial CTC charge would be increased or lengthened (to make up for the under-recovery). Env. M.B. at 33.

B. Other Disputes Regarding Specific Proposals

1. Duquesne's Position

(a) Duquesne's Proposal

Duquesne proposed to adjust the shopping credit to reflect the results of an annual RFP for the sale of firm power. Duquesne St. 5 at 56. The point of the RFP was to objectively establish the prevailing market price of power during the transition period and to make available to customers and suppliers a local source of power. Duquesne St. 3 at 40-45. MAPSA and HSS, however, vehemently criticize the RFP proposal. Three points in response are sufficient.

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[181] This position is shared by others. See, OCA St. 4 at 11-12.

[182] This hypothetical is exactly what has occurred this decade. The residential and commercial classes have experienced load growth, but the industrial class has seen a drop in number of customers, peak load and energy consumption.

First, while Mr. Lahtinen has rebutted each criticism, Duquesne St. 5-R at 6-26; Duquesne Exh. JAL-14; Duquesne St. 5-Rej., the telling point is that these parties fail to offer any realistic alternative to the RFP. Duquesne St. 5-R at 12. While their spirited attacks on the RFP may be entertaining to them, this strategy is utterly unproductive in advancing the important objective of establishing a market-based shopping credit – an objective with which neither party quarrels. Duquesne M.B. at 68-69.

Second, to simplify the disputed issues in this case, and to demonstrate its good faith, Duquesne offered to modify the RFP proposal as follows:

> [S]everal parties have criticized the contract terms for the proposed power sale. Duquesne's response is two-fold. First, Duquesne is willing to submit its proposed power sale auction (both the proposed contracts and the solicitation procedures) to the Commission for prior approval. Consequently, the Commission will have the opportunity to satisfy itself that the terms of the solicitation are adequate to set a market-based CGC. Second, Duquesne will cease using the RFP process if an index for market clearing prices is established in the Duquesne area that is representative of the market prices for Duquesne-supplied generation. While such an index does not exist today, it is possible that during the transition period one may develop. Should such an index be established, the need for an RFP would no longer exist and Duquesne would petition the Commission to substitute index prices for the prices resulting from Duquesne's RFP.

Duquesne St. 1-R at 3. This offer should have eliminated the disputes with HSS and MAPSA regarding the procedure for setting a shopping credit, but these parties remain undeterred. HSS fails to acknowledge any benefits of this offer, simply asserting that it "recogniz[es]" the RFP is "inherently flawed." HSS St. 1-R at 40. This is hardly fair, as Mr. Marshall's testimony suggests nothing of the kind. For its part, MAPSA contends that the offer is "unclear" and suggests that Duquesne may have hidden intentions. MAPSA St. 1-SR at 9. Again, this simply

underscores the fact that MAPSA has no interest in a constructive debate regarding a market-based shopping credit. Duquesne M.B. at 69-70.

Finally, the heart of the MAPSA and HSS claims is that the terms of the RFP "artificially" depressed the bid prices received by Duquesne. MAPSA St. 1 at 25; HSS St. 1 at 26. The obvious implication is that market prices are above the RFP bids and Duquesne could have received better prices if it had designed a better RFP. The proof, however, is in the evidence and all the data in the record on actual market transactions (not forecast prices) matches the winning bid prices produced by the RFP:

Record Citation	Source of Data	Price (¢/kWh)
Duquesne St. 5 at 73-74	FERC Form 714	1.79
Duquesne St. 5 at 76	Power Markets Week	1.82
Duquesne St. 7 at 4	Prior Duquesne Sales	1.75
Duquesne St. 7 at 10	Duquesne 1-Year RFP	1.82

It is thus wrong to suggest that, if the RFP's supposed "design flaws" (HSS St. 1 at 27) were rectified, higher bids would have been forthcoming. The foregoing data show that there is very little uncertainty regarding the market price for power in ECAR today. The problem is that MAPSA and HSS don't like these low prices, which are apparently unhelpful to their pursuit of an artificially low CTC for Duquesne. Duquesne M.B. at 70-71.

(b) Other Proposals

In addition to the conceptual disputes discussed previously as to the OCA and DII proposals, Duquesne finds there remain significant disputes regarding the implementation of their CTC design proposals, particularly with respect to deferred taxes, Duquesne St. 2-R at 44, in a manner that would allow Duquesne to recover (after tax) the amount of stranded costs

determined to be just and reasonable. These complex issues are better addressed in the compliance phase of the case, if their proposals are adopted. Duquesne M.B. at 71.

2. DII's Position

(a) Duquesne's Proposal

DII observes Duquesne proposes to use the CTC residual methodology where the CTC/CGC will be determined on an annual basis according to the results of Duquesne's reverse-RFP for a portion of its load. Although DII supports the use of the CTC residual methodology, Duquesne's proposal to use the annual RFP results is inappropriate. The CTC for each year of the transition period must be firmly established as part of this proceeding and cannot vary annually. Use of a CTC that varies annually will inhibit the ability of customers to participate in the competitive market. This is clearly contrary to the goals of the Act. DII M.B. at 85-86.

Duquesne states that it would be willing to establish a fixed schedule of CTCs for customers willing to give up their right to return to bundled service at the rate cap. N.T. at 541-542. The Company's "compromise" in this regard ignores the balancing of interests reflected in the Act. As long as Duquesne is permitted to recover "stranded" costs, Duquesne must offer customers bundled sales service at the rate cap levels. 66 Pa. C.S. §2804(4). The existence of captive ratepayers to recover stranded costs during the transition period necessitates the need to protect those captive customers during the stranded cost collection period. For Duquesne to offer to provide customers with the CTC certainty that is clearly appropriate under the Act only if the customers are willing to give up their statutory right to a rate cap under the

Act, evinces an intent to exploit the transition to a competitive market to the Company's advantage and to the ratepayers' detriment. DII M.B. at 86.

The Act entitles ratepayers to the protection of a rate cap. As explained in the previous sections, DII believes customers are also entitled to a fixed schedule of CTCs. To suggest that customers must give up this right in order to have a guaranteed CTC level eviscerates the intended balancing of interests reflected in the Act. 66 Pa. C.S. §2802(8). Duquesne's attempts to force a "compromise" between ratepayers and the Company in this regard are inappropriate and must be rejected. DII M.B. at 86.

(b) **The OCA's Proposal**

DII notes the OCA recommends a CTC design based on an allocated, levelized methodology. OCA St. 4 at 9, 14. As previously discussed, use of this methodology is clearly inappropriate and has been shown by DII to result in inappropriate cost shifting. In addition, the OCA CTC calculations for customers other than the residential class lead to potential violations of the statutory rate caps because of this cost shifting. DII St. 1-R at 17. For these reasons, the OCA proposal is clearly inappropriate and cannot be accepted by the Commission. DII M.B. at 86-87.

(c) **DII's Proposal**

DII proposes to use the CTC residual methodology to produce a fixed schedule of CTCs to be recovered from each customer class for each year of the transition period. DII St. 1 at 33-35. The yearly CTC is calculated by subtracting the projected market price for that

year from the unbundled generation component of each class's rates. This market price is the same market price used in DII's calculation of the Company's stranded generation cost. The DII method appropriately recognizes that stranded costs and the CTC are a part of current bundled rates; stranded costs are not simply a number derived disjunctively from the unbundling process and grafted onto each rate schedule (as stranded costs are treated under other proposals). The DII CTC methodology allows customers concrete information upon which to make choices in the competitive market. In addition, because of the relationship between projected market price and the CTC, the DII approach offers better opportunity for customers to economically participate in the competitive market during the transition period. On the whole, the DII methodology is the most appropriate CTC methodology to obtain the goals of the Act. DII respectfully requests that the Commission adopt the DII CTC methodology. DII M.B. at 87.

(d) Other Proposals

DII finds the OSBA endorses a CTC methodology similar to the OCA's allocated, levelized approach. See, OSBA St. 1-R at 2-9. As previously explained, both the OCA and OSBA CTC proposals result in inappropriate cost shifting and violate the rate cap. These results make the OSBA proposal inappropriate for Commission adoption. DII M.B. at 87.

3. MAPSA's Position

MAPSA argues Duquesne's proposal fails to acknowledge the fact that the RFP was designed to produce a wholesale market price and not to reflect the fully-delivered cost of power at retail, as admitted by Duquesne's witnesses. N.T. 763. Duquesne's attempt to set the

"shopping credit" based on this wholesale price is contrary to the intent of the Competition Act and the clearly-expressed intent of this Commission in PECO. Arguing that MAPSA has no interest in the "constructive debate" regarding a shopping credit is simply a smokescreen. MAPSA has stated a specific proposal for the development of a shopping credit sufficient to allow for competition - an evidentiary point which Duquesne has completely ignored. MAPSA St. 1 at 29-37. The PECO Order clearly requires: the present-day evaluation of Duquesne's stranded generation assets, which MAPSA asserts is best accomplished by an immediate auction; the setting of an appropriate CTC designed to recover those stranded costs; and, the derivation of a "fallout" shopping credit. The analysis then examines that shopping credit to determine whether it is sufficient to allow for the development of a robust competitive market. If not, the CTC recovery should be extended or levelized. Duquesne's failure to even recognize the existence of the precedent indicates Duquesne's unwillingness to engage in a productive discussion and defies the reality of the Commission's intentions. PECO; MAPSA R.B. at 10-11.

MAPSA does not dispute that the RFP produces prices that are reflective of the discrete product offered for sale in the RFP. However, MAPSA does take issue with the product itself. Namely, MAPSA argues that the product offered in the RFP was a wholesale power product, which would be only a single component of the portfolio of supply requirements necessary for a competitive supplier to provide service to retail customers. Also, as MAPSA witness Whitfield Russell testified, Duquesne's RFP result did not reflect all of the ancillary or additional services that would be required of a supplier. MAPSA St. 1 at 32-33. This was admitted by Duquesne's witness. N.T. 136. The reason that MAPSA opposes using the low prices produced by the RFP is that these prices are reflective of a discreet wholesale transaction,

not a fully-delivered retail price. Duquesne's RFP results must be rejected as an indication of a "market price," for the purposes of setting a CGC or CTC. MAPSA M.B. at 22-24; MAPSA R.B. at 11.

C. Other Issues Addressed in PECO Energy

1. Duquesne's Position

In PECO Energy, Duquesne observes the Commission accepted evidence that, with respect the CTC proposed by PECO, a long-term debt rate represented the appropriate cost of capital. PECO Energy, Slip Op. at 107. While Duquesne does not agree with that finding, it is not pertinent here. Duquesne has not proposed a "fixed" CTC that is "trued up" each year for changes in sales levels, as was proposed in PECO Energy. Rather, Duquesne has proposed an ROE spillover and a commitment to amortize a minimum of $1.7 billion in stranded costs over the transition period. According to testimony not directly disputed by any witness,[183] this proposed "places risk on Duquesne's shareholders that is greater than it would be under traditional regulation." Duquesne St. 12 at 37 (emphasis added). In particular, the proposal places asymmetric risk on Duquesne that simply does not exist today:

> Under Duquesne's proposal, shareholders will bear the risk that cost containment measures are not sufficient to generate the savings necessary to satisfy this commitment while maintaining earnings. If, to the contrary, revenues exceed expectations or additional cost savings are available, Duquesne has established an ROE "spillover" mechanism that will ensure that the related

[183] Each witness that criticized Duquesne's stranded cost recovery proposal carefully avoided contending that the proposal would, taken as a whole, including the $1.7 billion minimum amortization commitment, place less risk on Duquesne's shareholders than exists today.

> revenues are used to mitigate stranded costs, rather than to permit shareholders to earn higher than a fair return.

Duquesne St. 1 at 5 (emphasis in original). Consequently, the findings in PECO Energy do not apply to this case. Duquesne M.B. at 71-72.

In summary, Duquesne urges approval of its CTC design proposal, as described and supported by Mr. Lahtinen. Duquesne St. 5. If the immediate auction is accepted, Duquesne is willing to accept a CTC design that generally is consistent with the method used in PECO Energy, as discussed, supra. Duquesne M.B. at 72-73.

2. DII's Position

In order to ensure that the Company does not over-recover stranded costs, a CTC revenue tracking mechanism must be established. DII suggests that the Company should track CTC revenues on a monthly basis. The Company will begin the stranded cost recovery period with the unamortized total stranded cost balance authorized in this proceeding to be recovered from ratepayers. This balance will accrue interest monthly at the revenue requirement level (i.e., fully grossed-up cost of capital). Each month, the Company will accumulate the CTC revenues produced that month by each rate schedule. The unamortized stranded cost balance will be reduced each month by the accumulated monthly CTC revenues until the balance is fully amortized at a $0 level. At that point, CTC collection will be terminated. The DII proposal represents a reasonable and timely method to track CTC collection and should be adopted by the Commission. DII St. 1 at 30-31; DII M.B. at 87-88; DII R.B. at 43.

In conclusion, DII asserts its CTC calculation methodology based on a CTC residual approach with fixed yearly CTC determined based on anticipated market price is clearly appropriate and balances interest of all participants during the transition period. DII M.B. at 88.

The DII proposal encourages development of the competitive market by providing all customer classes with a realistic opportunity to benefit from obtaining competitive supply. The DII CTC methodology should be accepted by the Commission. The Duquesne CTC methodology is clearly inappropriate. The Duquesne methodology does not provide customers with the level of certainty necessary to make rational and well informed decisions during the transition period. DII submits that the Duquesne proposal does not adequately further the goals of the Act; consequently, the Duquesne methodology must be rejected. Id.

The OCA/OSBA methodology to determine CTCs based on a levelized, allocated recovery is not appropriate. As DII illustrates, the OCA and OSBA proposals contain inherent and fundamental flaws that violate the anti-cost shifting and rate cap provisions of the Act. 66 Pa. C.S. §§2808(a) & 2804(4). Because of this inconsistency with the requirements of the Act, DII submits that the OCA and OSBA proposals must be rejected. DII M.B. at 88-89; DII R.B. at 43.

D. Recommendation

On the subject of Competitive Transition Charge, this Commission explained in the only restructuring application to date to receive final review, PECO Energy, Slip Op. at 103-104:

The definition of competitive transition charge (CTC) in Section 2803 requires the Commission to establish an appropriate CTC "designed to recover an electric utility's transition or stranded costs as determined by the Commission under Sections 2804 and 2808." Section 2804(13) specifies that "the Commission has the power and duty to approve a competitive transition charge for the recovery of transition or stranded costs it determines to be just and reasonable to recover from ratepayers. Section 2804(14) provides that the transition to competitive markets shall "provide the investors in Pennsylvania electric utilities with a fair opportunity to fully recover the amount of transition or stranded costs that the Commission determines to be just and reasonable."

Section 2808(a) identifies several directives for the Commission to implement in establishing the CTC. First, "every customer accessing the transmission or distribution network shall pay a CTC to the electric distribution company in whose certificated territory that customer is located." Second, the "costs to be recovered shall be allocated to customer classes in a manner that does not shift inter-class or intra-class 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." The definition of CTC in Section 2803 makes clear the legislative intent that the CTC shall be "nonbypassable". Section 2808(b) specifies the general requirement that the CTC shall be collected from consumers for a period not to exceed 9 years from the effective date of the Act, ending by 12/31/05.[184] Section 2808(b) also provides that "in establishing the length of the period for collection of the

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[184] Thus, the Act adopts a general rule that the CTC is to be collected for no longer than seven years from the onset of competition on January 1, 1999. The Act presumes that in adopting a collection period of seven years or less, the Commission must consider the "effect on the ability of the Commonwealth to compete in attracting industry and jobs, on the financial health of the electric utilities, and other relevant factors." In addition, Section 2808 contemplates several possibilities for a longer collection period. First, an individual customer and the utility may agree on an alternative collection methodology. Second, the Commission may "in its discretion and for good cause shown" adopt an alternative payment period. Lastly, in the event that a utility securitizes any portion of its stranded investment pursuant to Section 2812, the definition of "transition bonds" in Section 2812(g) authorizes a collection period of up to ten years for collection of the Intangible Transition Charge (ITC), thereby superseding any CTC recovery period.

> competitive transition charge, the Commission shall consider the effect on the ability of the Commonwealth to compete in attracting industry and jobs, on the financial health of the electric utilities and other relevant factors."

After reviewing the record in that case, the Commission concluded:

> . . . [T]hat PECO should receive its authorized transition and stranded cost recovery of $5.024 billion over a levelized period of 104 months, or 8½ years. The CTC shall be calculated on a "per kwh" basis assuming annual sales of 33,569,358 MWH in 1999, escalating at 0.8% annually throughout the transition period. PECO shall calculate the CTC with a cost of capital of 7.47% on the unamortized balance. CTC revenues shall be allocated on a class basis consistent with the allocation methodology for utility production plant accepted by the Commission in the company's 1990 general rate case proceeding.

PECO Energy, Slip Op. at 109-110.

In the most perfect of worlds, one could calculate the appropriate CTC by first, finding the appropriate amount of costs stranded due to the transition and determining the length of the recovey period. Second, one could determine the system average kWh rate, using current rates. Next, one could subtract from that latter figure the appropriate costs of unbundled T&D costs. The remainder would include both the CTC, which would contribute to recovery of stranded costs, and a CGC, which would represent the market price of generation. The CGC is a regulatory concept and is nowhere defined in the Act, although the parties in this case define and calculate the CGC in different fashions. In this perfect world example, one could determine the appropriate CTC by merely subtracting from the remainder the CGC, which would equate with the prevailing market price of generation. While the foregoing example is an oversimplification, this exercise underlies the Company's RFP proposal in this application.

However, we live in an imperfect world. We do not know what the prevailing market price of generation is at this time, because that market is in its infancy. To replicate that market, Duquesne presents its RFP proposal. The RFP proposal has received a great deal of justified criticism from every party to this case and no need exists here to reiterate those criticisms. It is sufficient to note the RFP proposal fails to produce the equivalent of a "retail" price for electric generation in a sufficiently wide market under terms flexible enough to attract a significant number of purchasers. Perhaps, in a more mature market, the Company's RFP proposal could possess some merit. Under present circumstances, even Commission supervision can not cure the problems inherent in the proposed RFP process. Moreover, setting the RFP annually will stifle any nascent competition, which the Commission found to be of paramount importance in PECO Energy.

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 exceeds 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.

I agree with the OCA that its 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. 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 Exhbit 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).

Section 2808(b) specifies the general requirement that the CTC must be collected from customers for a period not to exceed nine years from the effective date of the Act, ending by December 31, 2005. No definitive proposal to extend the transition period has been made in this proceeding. Therefore, unless a party can show good cause, the Commission should

direct Duquesne to complete the transition period and cease collecting any CTC from its customers by December 31, 2005.

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).

The Commission should deny Duquesne's proposal to redesign its rates pursuant to a two-part Customer Transition Charge, which would include a fixed (customer-specific) charge and a usage-based (class-specific) charge. This proposal violates the prohibition in the Act against intraclass cost shifting. 66 Pa. C.S. §2808(a). Under this proposal, 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. Moreover, the fixed monthly "customer-specific" charge is actually premise-specific, since the CTC is calculated for each meter, regardless of the occupant of the premises. For these reasons, the Commission should decline to adopt this proposal.

The Commission should also adopt the OCA's proposals to calculate an avoidable generation credit for administration and general costs, which competitive suppliers incur. Consistent with the statutory requirement for annual reconciliation and with OCA's proposal to allocate stranded costs by rate class, stranded costs should also be reconciled annually on a class-specific basis. This approach is necessary to avoid inter-class stranded cost shifting and was specifically adopted in PECO Energy, Slip Op. at 113.

The Company proposes to roll its Energy Cost Rate (ECR) in at a rate higher than was in effect on January 1, 1997. Duquesne St. 2 at 8. Specifically, the Company proposes to include energy costs at a rate of 14.7 mills/kWh even though the applicable rate at the effective date of the Act was only 12.8 mills/kWh. Id., n.1. Rates should not be permitted to be implemented at a level which is higher than was in effect on January 1, 1997, the effective date of the Act. 66 Pa. C.S. §2804(4)(ii).

Any remaining disputes concerning the implementation of the CTC design proposed in this case, particularly with respect to deferred taxes, should be addressed in the compliance phase of this case.

VIII. Rate of Return/discount Rate

A. Duquesne's Proposal

Duquesne's witness, Dr. Makholm, performed a fully supported Discounted Cash Flow ("DCF") analysis in order to calculate the Company's return on equity ("ROE"). See, Duquesne St. at 12 and Duquesne St. at 12-R. Based on this DCF analysis, Dr. Makholm concluded that an 11.65% ROE for Duquesne was fair and reasonable. Duquesne St. 12 at 3. To be conservative, Duquesne is requesting an 11.5% ROE. Duquesne St. 2 at 47; Duquesne M.B. at 73.

Of the interveners, only OTS witness Mr. Van Jeschke presented a rebuttal, in any detail, to Dr. Makholm's testimony. OTS St. at 1.[185] Mr. Van Jeschke's testimony raises three major issues: (i) composition of the proxy group used for the DCF analysis; (ii) use of an adjustment to correct for the effect of the "ex-dividend date," and (iii) inclusion of a factor to account for flotation costs. Duquesne M.B. at 73.

The first issue is the composition of the proxy group. The two major disagreements on selection criteria centered on whether the group should include utilities with nuclear generation and whether utilities involved in a merger should be included. Dr. Makholm did not include utilities that met either of these criteria, while Mr. Van Jeschke did. Duquesne

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[185] OCA witness Mr. Kahal arbitrarily picked an ROE of 10% because this number was used in the "PECO QRO" case. OCA St. 1 at 26. But returns on equity are not "fungible"; they are company specific, as any responsible analyst would acknowledge. Duquesne St. 12 at 12; Duquesne St. 12-R at 15-16. Mr. Kahal's unsupported analysis should be rejected. Duquesne St. 12-R at 15-16. Mr. Muehl, on behalf of David Hughes, presented testimony concerning Duquesne's level of return, DH St. 2; however, as explained by Dr. Makholm, Duquesne St. 12-R at 17-19, Mr. Muehl's understanding of the utility regulatory process is so flawed that his testimony must be rejected.

St. 12-R at 3-6; OTS St. 1 at 15-20, 41-42. Dr. Makholm's selection criteria should be accepted. His analysis is more conservative and more reliable because he excluded utilities that met these criteria. Duquesne St. 12-R at 4-6. Utilities that own nuclear generation have higher risk (and ROEs) than those that do not. Id. Furthermore, the stock price of utilities involved in mergers can swing wildly, thus producing unreliable DCF results. Id.; Duquesne M.B. at 74.

The two remaining disputes concern adjustments to the DCF calculations themselves. The first adjustment made by Dr. Makholm was to adjust for the ex-dividend date. As Dr. Makholm explains, the DCF model contains certain assumptions regarding the ex-dividend date, and if a correction is not made the resulting DCF calculation will result in an ROE that is too low. Duquesne St. 12 at 21-22; OTS St. 1 at 43-44; Duquesne St. 12-R at 7-8. Mr. Van Jeschke does not deny that this effect exists; however, he testifies that there is no "conclusive" evidence that the stock price change can be attributed solely to this effect, and further, that the effect should average out over time. OTS St. 1 at 43-44. Dr. Makholm, however, provides ample evidence of the existence of, and need to correct for, this effect and demonstrates that it does not average out over time. Duquesne St. 12 at 21-22; Duquesne St. 12-R at 7-8. Thus, Dr. Makholm's adjustment for the ex-dividend date should be accepted. Duquesne M.B. at 74-75.

The second adjustment made by Dr. Makholm is to account for flotation costs. Duquesne St. 12 at 26-29. Without this adjustment, the net proceeds from the issuance of common equity will be less than the sales price of that issuance. These costs typically are allowed to be recovered on debt and preferred equity issuances. Id. Dr. Makholm recognized that the Commission, however, typically denies recovery of these costs, holding that flotation

costs are already included in the market price of the stock that is used in the DCF calculation (Id. at 28; OTS St. 1 at 45-46), but Dr. Makholm shows that there is no evidentiary support for this in the financial literature. Duquesne St. 12-R at 11-13. Moreover, it is inconsistent to allow the recovery of these costs on debt and preferred equity issuances and to deny their recovery on common equity issuances. Duquesne St. 12 at 28. Accordingly, Duquesne has made this adjustment (of 5%), and it should be accepted by the Commission in this proceeding.[186] Duquesne M.B. at 75.

B. The OTS' Position

1. Introduction

The OTS explains a fair and reasonable overall rate of return is one which will allow a utility the opportunity to recover those costs prudently incurred by all classes of capital used to finance the rate base during the prospective period that the Company's rate will be in effect. It is the Company's burden, in this case, to prove that its recommended 11.65% return on common equity is required to cover capital costs and to assure confidence in the financial integrity of the utility so as to maintain credit and attract capital at reasonable rates. See, Bluefield Waterworks and Improvement Company v. Public Service Commission of West Virginia, ("Bluefield") 262 U.S. 679 (1923); Federal Power Commission v. Hope Natural Gas

[186] Dr. Makholm also performed a simple reasonableness test of each witnesses' recommended ROE. He compared the recommendations against the range of electric utilities ROE's authorized by regulatory commission throughout the country between April 1995 and March 1997. From this comparison, it is apparent that Dr. Makholm's recommended ROE is in the middle of the range, while those of Mr. Van Jeschke and Mr. Kahal are at the extreme low end, or even outside of, the range. Duquesne St. 12-R at 14-16.

Company, ("Hope") 320 U.S. 591 (1944). OTS submits that the evidence submitted by Duquesne in support of its 11.65% recommended return on equity fails to meet this standard. OTS M.B. at 55.

In Bluefield, supra, the United States Supreme Court provided a criteria by which regulators are to be guided for purposes of determining a fair rate of return for a public utility. In this case the Court stated:

> A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures. The return should be adequate, under efficient and economic management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties. A rate of return may be reasonable at one time and become too high or too low by changes affecting opportunities for investment, the money market and business conditions generally.

See, Bluefield; OTS M.B. at 55-56.

In Hope, the Court focused particularly upon the equity return. The Court stated:

> . . . It is important that there be enough revenue not only for operating expenses but also for the capital costs of the business. These include service on the debt and dividends.
>
> . . . By that standard the return to the equity owner should be commensurate with risks on investments in other enterprises having corresponding risks. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and capital.

See, Hope at 603; OTS M.B. at 56.

The Pennsylvania Supreme Court has provided additional analysis to the Hope decision. In Pennsylvania Electric Co. v. Penna. Public Utility Comm., 509 Pa. 324, 502 A.2d 130 (1985); appeal dismissed, 476 U.S. 1137, 106 S. Ct. 2239, 90 L.Ed.2d 687 (1986), the Pennsylvania Supreme Court stated:

> We do not believe, however, that the Hope decision stands for the proposition . . . that the end result of a ratemaking body's adjudication must be the setting of rates at a level that will, in any given case, guarantee the continued financial integrity of the utility concerned.
>
> Rather, the Hope decision requires only that the regulatory authority balance consumer and investor interests to determine "just and reasonable" rates.

The Penelec decision interprets Hope as requiring a balancing of consumer and investor interests to determine just and reasonable rates. OTS contends that the 11.65% return on equity proposed by Duquesne in the case at bar provides rates that would be far greater than the level needed to satisfy the standards set forth in Hope. OTS M.B. at 56-57.

The determination of a fair rate of return requires an analysis of the proportion of each type of capital which has financed the rate base and an assignment of a cost rate to each. The cost rate of debt is fixed and can usually be computed accurately. The cost rate of common equity varies and is much more difficult to measure. Id. at 57.

2. Duquesne's Position

Duquesne's witness, Dr. Jeffrey D. Makholm, concluded that the Company should be afforded an opportunity to earn an 11.65% return on common equity. This return recommendation is based upon Dr. Makholm's use of a discounted case flow ("DCF") model

analysis performed on a proxy group of U.S. Electric Utilities. Duquesne St. 2 at 2-7. Although Company witness Makholm's recommended cost rate for common equity is 11.65%, the direct testimony of Duquesne witness D.J. Clayton states that 11.5% is the Company's claimed cost of common equity. According to Mr. Clayton, this 11.5% claim is conservative. Duquesne St. 2 at 47. Correspondingly, according to Mr. Clayton, the Company's after tax discount rate for use in computing present value of stranded costs is 7.83%. Company Filing, Volume IX, Item No. L-8, page 1 of 1; OTS M.B. at 58.

3. The OTS' Position

In ascertaining a fair and reasonable rate of return, OTS adopted the Company's test year capital structure which consists of 50.23% long-term debt, 9.69% preferred stock, and 40.08% common equity. Additionally, those cost rates accompanying long-term debt and preferred stock were also adopted. Duquesne Filing, Volume VII, Items Nos. H-2 and H-7 and OTS St. 1 at 26; OTS M.B. at 58.

OTS' major source of contention with the Company's rate of return recommendation lies in the area of the cost of common equity. It is OTS' position that the cost of common equity should be no more than 10.5%. Correspondingly, OTS admits that, not only is the 11.65% recommended by Duquesne witness Makholm excessive but so is the 11.5% recommendation made by Duquesne witness Clayton. Id. at 59.

In arriving at his 10.5% cost of common equity recommendation, OTS witness Jeschke did not utilize the barometer group of the U.S. Electric Utilities as did Dr. Makholm. Instead, witness Jeschke composed a barometer group of 13 electric companies from the eastern

and central United States with risk factors similar to Duquesne and nuclear generating generally in excess of 30% since Duquesne's nuclear capacity is approximately 29%. Id.

It should be mentioned that, in adopting Duquesne's capital structure, OTS witness Jeschke examined the historical common equity ratios for the electric barometer group. This analysis indicated that the Company's recommended 40.08% common equity ratio is lower than the average of the group. OTS Exh. 1, Sch. 3. Since common equity rates cost more than debt and preferred stock, the use of Duquesne's lower than average common equity ratio will result in lower than average overall cost of capital. Generally, a higher common equity ratio indicates lower financial risk. Therefore, while Duquesne's capital structure is acceptable, a higher than average cost of equity is warranted. OTS St. 1 at 11; OTS M.B. at 59-60.

(a) Cost Rate of Common Equity

To ascertain a fair and reasonable cost rate for common equity, comprehensive financial analysis is necessary. The determination of a cost rate for common equity requires the exercise of informed judgement based on financial data and investors expectations during various segments of the business cycle. It is necessary to consult the market place for insight into the cost rate for common equity since investors determine the price at which common equity capital will be provided. It is also necessary to review historic and current financial and economic data as well as prospective estimates of inflation rates, interest rates, and the state of the economy in general. Properly matching these costs indicators to the current expected phase of the business cycle will provide a reasonable, but not excessive, return on common equity. Thus,

the Company will be able to compete for new capital in the market place with companies of comparable risk. OTS St. 1 at 12; OTS M.B. at 60.

(i) **Discounted Cash Flow ("DCF") Analysis**

To determine a recommended cost of common equity, OTS witness Jeschke utilized the discounted cash flow method. This method has been consistently approved by the Commission to develop equity costs. To compute the various components of the DCF method, Mr. Jeschke replied upon current, historic and forecasted market data for his electric barometer group. He also analyzed historical, current and prospective interest rates. Such an analysis is necessary to insure that one's recommended market determined cost of equity reflects changes in economic conditions. OTS M.B. at 60-61.

The underlying principles of the DCF method recognizes that when investors buy stock they expect to receive a total return consisting not only of dividends, but also of capital appreciation. The cost rate yielded by the DCF technique for a public utility is the sum of the expected dividend yield on the stock during the coming year and the expected growth in dividends per share. The formula for the DCF method is:

$$k = D1/Po + Gn$$

where:

k	=	expected rate of return
D1	=	indicated dividend payment expected during the course of the next year
Po	=	current stock price
Gn	=	dividend growth expected over the long-run period "n"

OTS M.B. at 61.

(1) Dividend Yield

In theory, the DCF advocates the use of the most current dividend yield. For purposes of ratemaking, a dividend yield that is representative of the prospective period for which new rates will be in effect must be determined. Ratemaking is a forward looking as well as a long run process. Therefore, an analysis cannot be based solely upon short term spot market data. This is because investors are continually changing their opinion concerning the relative worth of debt and equity on a monthly, weekly, or in some cases, a daily basis, depending on changes in the economy or the financial position of the company. A spot rate of return which may seem appropriate for current ratemaking purposes may be too high or too low at a later point in time depending upon changing economic conditions in the market place. OTS M.B. at 61-62.

Mr. Jeschke determined the dividend yield portion of the DCF formula by simply dividing an expected dividend by a representative stock price. To do this, Mr. Jeschke used the indicated expected dividend payment and representative stock price found in publications such as Standard and Poors Stock Guide and Barrons National Business and Financial Weekly. Specifically, in the present case, Mr. Jeschke utilized the current dividend yield presented in the September 1, 1997 Barrons National Business and Financial Weekly and a 52 week average dividend yield. OTS St. 1 at 14; OTS M.B. at 62.

In the case at bar, Mr. Jeschke determined the dividend yield by giving weight to the 52-week average dividend yield, the current dividend yield and the medians. The dividend used to determine the dividend yields for each company is the current dividend reported in the September 1, 1997 Barrons National Business and Financial Weekly. The median 52-

week and median current dividend yield is 6.91 and 6.86%, respectively. OTS Exh. 1, Sch. 4. The average 52 week and average current dividend yield is 7.02 and 6.92%, respectively. OTS Exh. 1, Sch. 4. Mr. Jeschke utilized 7% as a presentative dividend yield in his DCF analysis. The 7% is the unadjusted dividend yield that was used to develop OTS's discounted cash flow method results. OTS Exh. 1, Sch. 7; OTS St. 1 at 26; OTS M.B. at 62-63.

Mr. Jeschke also computed a yield adjustment by multiplying the 7% dividend yield by one-half of the next period's dividend growth rate. This adjustment was made because the dividend yield from the Barrons National Business and Financial Weekly may not reflect the annualized increases in quarterly dividends. Therefore, this adjustment reflects any annualized effect if increases in quarterly dividends occur. Mr. Jeschke has adjusted the dividend yield by one-half of the 2.5 - 3.5% dividend growth rate recommendation to produce an adjusted dividend yield. This adjustment causes the yield to increase by 9 - 12 basis points to a range of 7.09 - 7.12%. OTS Exh. 1, Sch. 1; OTS Exh. 1, Sch. 7, Note 1; OTS St. 1 at 26-27; OTS M.B. at 63.

(2) **Growth Rate**

The growth rate component of a DCF methodology is more subjective and somewhat more difficult to determine than the dividend yield. The growth rate is used to estimate perpetual capital appreciation. One way to derive a dividend growth rate is to use historical data. However, it is important not to solely rely on historical information since utilities can increase dividend payments as earnings per share rise and, since earnings per share drive dividends per share, dividends per share will tend to rise in the future reflecting increased

earnings per share forecasts. Thus, when reputable analysts forecasts are available such as those found in the Value Line Investment Survey or Standard and Poors Earnings Guide, historical information should not be the sole source driving ones growth rate calculation. The DCF analysis which is developed by utilizing analysts forecasted growth rates is indicative of estimated future economic conditions and specific company and industry risk factors. OTS St. 1 at 27; OTS M.B. at 63-64.

To calculate his DCF growth rate, OTS witness Jeschke analyzed historical growth and dividends per share ("DPS") and earnings per share ("EPS") for the electric barometer group. Mr. Jeschke also reviewed the forecasted earnings and growth rates as shown by Value Line and Standards and Poors. OTS Exh. 1, Sch. 8; OTS M.B. at 64.

In his testimony and exhibits, Mr. Jeschke shows the results of the historical compound dividend (normalized five year) and historical log-linear dividend (five years). The time covered in this analysis is a five year historical and a five year forecast. The historical compound dividend and log-linear dividend is 1.64% and 1.77% while the medians are 2.21% and 1.45%. On the other hand, the average historical compound earnings and log-linear earnings growth rate is 2.73% and 2.92% while the medians are 3.09% and 4.09%. OTS Exh. 1, Sch. 8; OTS St. 1 at 28; OTS M.B. at 64-65.

Forecasted dividends from the Value Line Investment Survey for the electric barometer group reflect an average of 0.38% and a median of 0.50%. Correspondingly, forecasted earnings from the Value Line Investment Survey for the electric barometer group reflect an average of 3.58% and a median of 3.50% while forecasted earnings from the Standard

and Poors Earnings Guide for the electric barometer group reflect an average of 2.92% and a median of 3.0%. OTS Exh. 1, Sch. 8; OTS M.B. at 65.

In his testimony Mr. Jeschke stated that in determining the growth rate for use in his DCF model he gave primary weight to expected earnings growth rates. This is because earnings for utilities can be volatile and growth rates computed from those earnings may not be indicative of long term growth potential. Yearly fluctuations in earnings can result in distorted growth rates. On the other hand, dividend growth rates are less volatile and more indicative of management's long term earnings expectations. One finds more information is implicitedly contained in expected earnings growth rates. The historical data, on the other hand, is accounted for both in the forecasted growth as well as in the expectation of the wide array of economic variables. Thus to give significant rate to historical growth information would have the effect of considering this information twice in a single calculation. OTS St. 1 at 29; OTS M.B. at 65-66.

Mr. Jeschke determined that a 2.5% - 3.5% growth rate is appropriate in this case. OTS Exh. 1, Sch. 8. Mr. Jeschke's opinion is based upon the fact that the average historical earnings and dividend growth rates are in the 1.64 - 2.92% range. The average forecasted earnings growth rates are 2.92 and 3.58% and the average forecasted dividend growth rate is 0.38%. The median forecasted growth rates are 3.0 and 3.5% with a forecasted dividend growth rate of .50. The median historical earnings and dividends growth rates range from 1.45 to 4.09%. However, the historical earnings growth rate of 4.09% is unlikely to be sustainable for the electric barometer group. Therefore, the forecasted earnings growth rate of 3.0 and

3.5% reflect sustainable growth which Mr. Jeschke utilized in his DCF analysis. OTS M.B. at 66.

(3) **DCF Results**

In OTS Exhibit No. 1, Schedule 7, Mr. Jeschke sets forth the results of his DCF analysis. First, Mr. Jeschke adjusted the 7% recommended dividend yield by 1/2 of the 2.5% low end of his growth rate range. The adjusted dividend yield is 7.90%. The 9.95% low end of Mr. Jeschke's DCF range is the sum of the adjusted dividend yield (7.9%) and the 2.5% growth rate. OTS Exh. 1, Sch. 7; OTS M.B. at 66-67.

Additionally, Mr. Jeschke adjusted the 7% recommended dividend yield by 1/2 of 3.5% high end of his growth range. The adjusted dividend yield is 7.12%. The 10.62% high end of OTS's DCF range is the sum of 7.12% adjusted dividend yield in the 3.50% growth rate. Id.

Based on this analysis, it is OTS' position that 9.50% - 10.50% represents a reasonable cost range of common equity for a publically traded electric company. OTS St. 1 at 31-32; OTS M.B. at 62.

OTS did not apply the DCF analysis for DQE. This is because, in comparison to Mr. Jeschke's 7% recommended dividend yield for the electric barometer group, DQE's current yield is unusually low. OTS contends that this is probably due to investors' expectation of a 20% increase in the dividends that would result from DQE's merger of Allegheny Power System. It is clear that DQE's current dividend yield is not reflective of the company's long term earnings potential. Therefore, OTS submits that it is inappropriate to use DQE's current

dividend yield in a current DCF analysis to determine Duquesne Light Company's cost rate of common equity. Id.

(ii) **Barometer Group Selection**

As stated previously, in order to determine a market based cost of common equity, OTS witness Jeschke utilized a 13 company barometer group of publicly traded electric companies. This is because Duquesne is a wholly owned subsidiary of DQE. Consequently, it is necessary to use a suitable proxy or barometer group of publically traded electric companies that provide services similar to those provided by Duquesne, to determine the rate of return on common equity for Duquesne. Though the companies will certainly differ in some aspects, if one focuses on similarities of companies one can determine which companies will compose a barometer group. This can be accomplished by analyzing some of the key market information and risk indicators. Mr. Jeschke's barometer group in this case included the following companies:

1. Atlantic Energy, Inc.
2. Baltimore Gas and Electric Company
3. Boston Edison Company
4. Carolina Power and Light Company
5. Dominion Resources, Inc.
6. Duke Power Company
7. GPU, Inc.
8. IEF Industries
9. PECO Energy Company
10. PP&L Resources, Inc.
11. Public Services Enterprises Group, Inc.
12. Rochester Gas and Electric Corporation
13. Unicom Corporation

OTS St. 1 at 16; OTS M.B. at 67-68.

OTS contends this group of 13 electric companies satisfies certain criteria that are important to fairly determine Duquesne's rate of return on common equity. This criteria include their location, financial risk, and nuclear generating capacity. Id.

(iii) Risk Comparison

Since Duquesne does not have market data available which can be utilized in a risk analysis, OTS witness Jeschke employed DQE's market data set as a proxy for Duquesne. This is particularly appropriate, since 92.5% of DQE's operating revenues are derived from Duquesne's sale of electricty. Additionally, the percentage of electric operating revenues to total revenues in Mr. Jeschke's 13 company electric barometer group is 91.46% of total revenues. OTS Exh. 1, Sch. 3; OTS M.B. at 69-70.

In analyzing risk indicators, Mr. Jeschke considered nuclear generation percentage, total capacity, equity ratio, beta safety rank and financial strength. When these indicators are carefully scrutinized, it is clear that the barometer group is a very close representation of an electric utility with DQE's characteristics. Id.

For example with regard to nuclear generation, the average percentage of nuclear generation for the barometer group is 35.85% and the median is 32% with the range from 15%-67%. Correspondingly, DQE's data reflects nuclear generation of 29%. The significance of this factor is that the barometer group of the electric companies is largely exposes to risks associated with nuclear generation. Since DQE's percentage of nuclear generation is slightly lower than the median of the range, this indicates a lower risk associated with nuclear generation on the part of DQE, than the average. Id.

In relation to financial risk, DQE's common equity ratio of 45.15% and Duquesne's common equity ratio of 40.08% is lower than the barometer group's average of 47.58% and median of 47.01%. The range of common equity ratios for the electric barometer group is 43.74%-53.66%. Id.

When one takes investment risk into consideration, DQE's beta of .75 compares favorably to the electric barometer group's of 0.78 and median of 0.70. DQE's safety rank of 2 is higher than the electric barometer group's average of 2.4 and median of 3.0. Additionally, DQE's financial strength with a rating of "A" is higher than the electric barometer groups rating of "B++" and median of "B++". This clearly indicates that DQE is somewhat financially stronger than the electric barometer group. OTS Exh. 1, Sch. 3. When all these factors are taken into consideration, it is apparent that the electric barometer group is a very close representation of an electric utility with DQE's characteristics. OTS St. 1 at 18-20; OTS M.B. at 70.

(iv) Alternative Investments

OTS's analysis incorporates the effect of changing business and economic conditions by utilizing market based data. This is because financial markets take all factors into account when accessing investments. OTS witness Jeschke compared the electric barometer group's common stock dividend yields to yields on Moody's A-Rated Public Utility Bonds, long term government bonds, intermediate term government bonds and short term government issues for the period 1981-1996. OTS Exh. 1, Sch. 5; OTS M.B. at 70-71.

This analysis indicates that the 12-month average for 1996 for the electric barometer group's common stock yield dividends and yields on utility bond and government securities are at relatively low levels in terms of yields experienced since 1981. Mr. Jeschke's analysis clearly shows that the electric barometer group's dividend yields and long term bond yields are near the low end of the 1981 - 1995 range. It also indicates that shorter term government securities tend to become more volatile than long term bonds and utility stock yields. OTS St. 1 at 22-23; OTS M.B. at 71.

The significance of this analysis is to demonstrate that the electric company dividend yields reflect changes in yields on alternative income paying investments such as bonds. Since the dividend yield composes the greatest portion of the expected total return for electric utilities, it is only logical that assumptions made about the level and trend of dividend yields and yields on alternative investments generally hold true for the total expected return on common equity. Id.

OTS witness Jeschke also summarized bond yield forecasts as presented by the Blue Chip Financial Forecast. These Forecasts are published monthly. Mr. Jeschke analyzed the short term forecasts and the long term estimates concensus published in October 1997 and June 1997 respectively. The purpose of reviewing the October 1997 forecast was to note the direction yields are expected to take over the short run (fourth quarter of 1997 through the first quarter of 1999). The long range concensus demonstrates the continuity of the forecast. Id. at 71-72.

A review of the results of the October 1997 forecasts show a expected decrease in "A" rated utility bonds of 20 basis points from the fourth quarter of 1997 through the first

quarter of 1999 (7.60-7.40%). OTS Exh. 1, Sch. 6. The same holds true for the long term treasury bond yield. In fact, between the fourth quarter of 1997 through the first quarter of 1999, the long term treasury bond yield is expected to decline by 10 basis points from 6.5% - 6.4%. OTS St. 1 at 24; OTS M.B. at 72.

OTS witness Jeschke also analyzed the long range concensus forecasts. These forecasts relate to bond yields and the prime rate is presented on OTS Exhibit No. 1, Schedule 6. The long range estimates are provided both separately for the years 1998 through 2002 and collectively as one forecast for the years 2003-2007. This concensus clearly indicates that "A" rated utility bonds are expected to decline from 7.7% in 1998 to 7.2% in 2002, and to 7.0% from 2003 to 2007. The long term treasury bond yields reflects a similar decline. OTS Exh. 1, Sch. 6; OTS St. 1 at 24-25; OTS M.B. at 72.

(b) Additional Analysis

OTS witness Jeschke an additional analysis to determine the expected return on common equity for the next three to five years for the electric company barometer group. He calculated the expected total of DCF method return for Value Line Electric Utilities using forecasted information found in the Value Line Investment Survey. OTS Exh. 1, Sch. 9; OTS M.B. at 73.

The reason that this additional analysis was performed is because Value Line provides forecasted growth rates for both earnings and dividends and dividend yields for the coming year. In his analysis Mr. Jeschke used the forecasted dividend yield and growth rates provided to investors by the Value Line Investment Survey. The growth rate is forecasted three

to five years into the future. Thus, the results of the analysis reflect current and forecasted data. OTS St. 1 at 33; OTS M.B. at 73.

Mr. Jeschke found that the mean total expected common equity for the electric company barometer groups utilizing Value Line's forecasted dividend growth rate is 7.17%. The median of the total common equity return using dividend growth is 7.5% while the range of total equity returns using dividend growth is 3.10-9.10%. Mr. Jeschke also calculated the mean total expected common equity return of the electric barometer group utilizing Value Lines earnings growth rate of being 10.37% and the median of the total expected equity return using earnings growth rates as 10%. Thus the total expected equity returns using earnings growth rate 8.50-13.10%. Id. at 73-74.

At first blush, it becomes apparent that there are significant differences between the forecasted total equity return using dividend growth and the forecasted total equity return using earnings growth. According to Mr. Jeschke, this difference is due to the fact that earnings growth rates are expected to continue to increase during the forecasted periods while dividend growth rates are not expected to increase during that period at the same pace.

Mr. Jeschke states that, in the electric utility markets, investors should not look for significant increases in dividends during the next three to five years. He opines that, in response to a perceived increase in business risk resulting from the transition to a competitive environment, dividend growth is being restrained in order to strengthen equity ratios. It is apparent that the electric environment is changing and those electric utilities that will fair best are those with low rates relative to their competitors and those that are financially strong. However, low rates will slow earnings growth and, consequently, dividend increases. It is

readily apparent that the results in the Value Line Analysis support the reasonableness of OTS' recommended 9.50% to 10.5% recommendation of a fair and reasonable return on common equity. OTS St. 1 at 34-35; OTS M.B. at 74.

It is OTS' position that, based on the 9.50% to 10.50% recommended cost rate for common equity for the electric barometer group, a 10.50% return on common equity is appropriate in this case for Duquesne. The reason for this recommendation is because Duquesne's test year capital structure represents a below average business position and a current BBB+ senior debt rating. Duquesne has a lower common equity ratio which suggests higher financial risks. Because of this slightly higher financial risk, OTS recommends that the return on common equity for Duquesne should be at the upper end of OTS' calculated range. OTS St. 1 at 36; OTS M.B. at 75.

(c) Overall Weighted Cost of Capital

OTS submits that a 10.5% cost rate for common equity combined with the Company's historic test year's December 31, 1996, capital structure and the embedded cost of 8.51% for long term debt and a 7.45% cost rate for preferred stock results in an overall rated cost of capital 9.20%. OTS Exh. 1, Sch. 1; OTS M.B. at 75.

(d) Pre-Tax Interest Coverage

OTS witness Jeschke also performed an interest coverage analysis to check the reasonableness of his 9.20% overall rate of return recommendation. This analysis clearly indicated that OTS's recommendation was fair and reasonable. As can be seen in OTS Exhibit

No. 1, Schedule 9, OTS' recommended 9.20% overall rate of return provides that pre-tax interest coverage of 2.97 times. OTS M.B. at 75-76.

Mr. Jeschke utilized the Standard and Poors utility financial benchmark ratios for electric utilities. This study is found in the Standard and Poors Global Sector Review of July 1994. According to this publication, the current data for the Duquesne Light Company is a investment grade of BBB+. The pre-tax coverage benchmark for an "A" rating ranges between 2.75-4.50 times and for a BBB rating in the range of 1.75-3.50 times. Therefore, the pre-tax coverage of 2.97 times which OTS derives from its overall rate of return recommendation is clearly within the range of coverage of the electric barometer group. OTS St. 1 at 39-40; OTS M.B. at 76.

(e) <u>Discount Rate</u>

OTS witness Jeschke calculated the after tax weighted cost of capital for the company to utilize in its present value calculation related to the determination of the company's stranded costs. OTS contends that Mr. Jeschke's recommended 10.50% cost rate for common equity, combined with the Company's historic test year, December 31, 1996, capital structure and the embedded cost rates for long term debt and preferred stock results in an overall weighted discount cost of capital of 7.43%. This is 40 basis points lower than the Company's recommendation of 7.83%. OTS Exh. 1, Sch. 1; OTS St. 1 at 40; OTS M.B. at 76.

(f) <u>Duquesne's Cost of Capital Position</u>

OTS contends that Duquesne's witness Makholm's cost of capital testimony is flawed for a number of reasons. These flaws have caused Dr. Makholm to over estimate the Company's cost of equity requirement. OTS M.B. at 77.

One area in which OTS disagrees with Duquesne witness Makholm is his barometer group selection. OTS contends that Dr. Makholm's selection of his barometer group is inappropriate. This contention is based upon the fact that Dr. Makholm's barometer group lacks substantial similarity to Duquesne because of the 17 company barometer group which he choose, eight of these companies do not have nuclear power generation. Additionally, 13 of his 17 companies have purchased power of a large portion of their generation. Though Dr. Makholm admits these flaws, he states that these are not important factors in this case. Duquesne St. 12 at 20. OTS disagrees. This office submits that the barometer is not a representation of an electric utility with DQE's characteristics and, therefore, is not a fair and reasonable proxy to determine a market based expected cost for common equity for Duquesne. OTS M.B. at 77.

Specifically, for Duquesne witness Makholm to include a large number of companies which do not have nuclear power brings his proposed barometer group under severe scrutiny. Nuclear power plants will impact revenues in the future because of the high expense of recovery. The percentage of nuclear generating is a variable where an expected large stranded cost associated with nuclear plant is found. Id. at 77-78.

Another problem with Duquesne witness Makholm's analysis is that he performed an ex-dividend cost date adjustment on all stock prices. This, he claims, is to remove the known

effect that the next quarterly dividend will have on the stock price. This adjustment is made by removing from the stock price the portion of the dividend which is already accrued. Duquesne St. 12 at 21- 23; OTS M.B. at 78.

It is OTS' contention that such an adjustment for an ex-dividend is not appropriate for use in the DCF analysis. First, Dr. Makholm used a 52-week closing price average for the stock price. This negates any use of an adjustment to the stock price and any change in stock price for seasonal or quarterly events would average out. Id.

Secondly, the stock price change cannot, in any way, be attributed to one factor such as a dividend accumulation of payment. The market price a stock moves up or down due to many factors and events and cannot be attributed to any single factor. OTS St. 1 at 43; OTS M.B. at 78.

OTS contends that a third factor that causes Dr. Makholm's analysis to be flawed is that he utilized an inappropriate growth rate. The results Dr. Makholm's individual growth rate analysis produced a 3.47 and 4.31 rate an average of 3.89%. According to the Company's Exhibit JDM-7, ten of the 17 companies in Dr. Makholm's barometer group have an average growth rate below 3.50%. Therefore, a growth rate above 3.50% is clearly not sustainable and such a growth rate should not have been utilized by the Company in its DCF calculations. Id. at 78-79.

It is OTS's position that a fourth problem with Dr. Makholm's analysis is that he utilizes 5% for selling and issuance costs in his DCF model calculation. Duquesne St. 12 at 28. OTS contends that this is clearly inappropriate. The selling of issuance cost are an additional cost of capital that incurred at the time of issuance. The current market price of common stock

already reflects these items as investors have already capitalized the expenses in determining the market price at the time of purchase. OTS St. 1 at 45; OTS M.B. at 79.

It must be remembered that Duquesne's last offering was September of 1981. Duquesne St. 12, Exh. JDM-11. Thus, any analysis would have already taken these items into consideration. And, therefore, there is no reason to make additional adjustments to account for selling and issuance costs. In fact, it seems that the only purpose that this adjustment serves is to overstate Duquesne's cost rate of common equity. There is absolutely no evidence that Duquesne is issuing any new common stock at the present time. OTS St. 1 at 45-46; OTS M.B. at 79.

(g) Conclusion

Because of the foregoing, OTS submits that Dr. Makholm's 11.65% recommendation is overstated by at least 115 basis points. OTS recommends the Commission should give weight only to the DCF method to determine the cost rate of common equity. This means that only reasonable and supportable growth rates and the proper dividend rate such as OTS witness Jeschke's 7% on DCF based cost of common equity. Thus, the Commission should permit a rate of return on common equity of no more than 10.50%. Additionally, the Commission should allow a discounted cost of capital of no more than 7.43% for Duquesne's stranded costs. OTS St. 1 at 47; OTS M.B. at 80.

The OTS observes the Company states that it disagrees with OTS's position in regard to rate of return on three major issues. The first of these issues is the composition of OTS's Barometer Group for its discounted cash flow analysis. OTS R.B. at 12.

The Company's witness, Dr. Makholm, did not include any utilities that have nuclear generation or that were involved in a merger. According to the Company, this caused Dr. Makholm's analysis to be more conservative and more reliable because he excluded utilities that met these criterion. Duquesne M.B. at 74; OTS R.B. at 12.

OTS submits that Dr. Makholm is clearly wrong in his conclusion. From his analysis, it is apparent that Dr. Makholm does not understand the importance of the similarities of companies in selecting a suitable barometer group. OTS witness Jeschke focused on similarities such as electric companies located in the eastern United States with similar financial risks to Duquesne and nuclear generating capacity. DQE's investment which profile reflects a beta of 0.75 which compares favorably to the barometer groups average of 0.78 and a median of 0.70. Similarly, DQE's financial strength at "A" is higher than the barometer groups average rating of B++ and median of B++. Id. at 13.

OTS submits that nuclear generation exposure is the most important variable that needs to be similar. The percentage of nuclear generation in a variable where the expected large stranded costs associated with nuclear plant is possible. DQE's data reflects nuclear generation of 29%. The median percentage of nuclear generation for OTS' barometer group is 0.32%. Clearly, based on Mr. Jeschke's analysis of the risk indicators for DQE and the barometer group, the barometer group is a very close representation of an electric utility with DQE's characteristics. In addition, it must be noted that, not only are companies that own nuclear generation more suited to be compared to each other; but, also, the stranded costs must be viewed in light of the nuclear generation. Id.

The Company also states that those four companies in Mr. Jeschke's barometer group which are involved in potential mergers should be excluded. According to the Company, this is because stock prices can be volatile during the time of a potential merger. Duquesne M.B. at 74; OTS R.B. at 14.

It is OTS's position that the volatility of stock prices is minimized by Mr. Jeschke. This is because, in determining Mr. Jeschke's dividend, he afforded significant weight to the 52-week average dividend yield of 7.02%. This reflects closely with the current dividend yield of 6.92%. Therefore, any stock price volatility due to potential mergers has been adjusted for Mr. Jeschke's calculations. With this adjustment, it is important to include these four companies in Mr. Jeschke's barometer group because of their other similarities with DQE. Id.

The second dispute which the Company has with OTS's DCF calculation is that Company witness Makholm made an adjustment for the ex-dividend date. According to witness Makholm, if a correction for the ex-dividend is not made the resulting DCF calculation will result in a rate of return that is too low. Duquesne M.B. at 74; OTS R.B. at 14.

OTS contends that an ex-dividend adjustment does not belong in the DCF model. The DCF calculation as applied by OTS witness Jeschke is the accepted academic method. OTS contends that there is no academic evidence which supports an ex-dividend to dividend yields as it relates to the DCF model. Id. at 14-15.

Additionally, there are no financial publications that provide for ex-dividend adjusted dividend yields to investors for their investment-making decision. This adjustment is clearly not found in the mainstream of financial decision makers. In fact, it seems that the only

purpose for the ex-dividend is to justify unreasonably high rates of return for utilities when calculating their cost of equity. Id.

Finally, the Company would have an adjustment made to account for flotation costs. According to Dr. Makholm, without this adjustment, the net proceeds from the issuance of common equity would be less than the sales price of that issuance. Id.

It is OTS' position that any adjustment for flotation costs should be rejected by the Commission. As stated in OTS' Main Brief, the selling of issuance cost is an additional cost of capital that is incurred at the time of issuance. The current price of common stock already reflects these items as investors have already capitalized the expenses in determining the market price at the time of purchase. OTS M.B. at 79. Additionally, as Dr. Makholm admitted, the Commission has typically denied these costs in other proceedings. Duquesne M.B. at 75; OTS R.B. at 15.

In conclusion, it is OTS' position that Mr. Jeschke's recommended return on common equity in this case of 10.50%, is very reasonable in light of recent Commission decisions. Specifically, the rate of return on common equity that the Commission allowed PECO Energy Company was 10.0% while "A" rated public utility bond yields at the time of that Opinion and Order were 7.89%. Bond yields have gone down since the PECO Opinion and Order and this would indicate, if anything, that OTS witness Jeschke in the present case could justify a much lower recommendation. See, Pa.P.U.C. v. PECO Energy Company, Docket No. R-00973877 (1997). OTS R.B. at 16.

C. The OCA's Position

The OCA submits a return on equity of 10.0% should be utilized in determining the level of stranded costs at 1/1/99, consistent with the Commission's adoption of a 10.0% return on equity in PECO's securitization proceeding and in PECO Energy as part of adoption of OCA's Market Value estimate. PECO Energy, Slip Op. at 101; OCA M.B. at 69; OCA R.B. at 25.

D. HSS/ARI's Position

In his direct testimony, HSS/ARI witness Dr. Weisenmiller pointed out that the enactment of the Act dramatically reduced the risk of stranded cost recovery facing Duquesne, inter alia, by authorizing a non-bypassable CTC charge. HSS/ARI St. 1 at 84. Based upon that reduced risk, Dr. Weisenmiller recommended that Duquesne's ROE be reduced to reflect Duquesne's lower risk. Id. at 84-86; HSS/ARI M.B. at 85.

The Commission now has had the opportunity to rule on the appropriate rate of return issue in the context of considering PECO's stranded cost claim. In that proceeding, the Commission adopted the same approach advocated by Dr. Weisenmiller, finding that the risk of non-payment of CTCs is minimal, and that recovery of PECO's full principal amount is assured through the reconciliation mechanism of Section 2808(f). PECO Energy, Slip Op. at 108. Thus, the Commission concluded that the level of risk of collecting CTCs does not compare to the risk associated with generation charges collected under regulated rates. Id. As a result, the Commission ruled that PECO's long-term debt rate of 7.47% should be used to calculate PECO's revenue requirement for the recovery of CTCs. Id. Consistent with that

ruling, Duquesne should be authorized to use its long-term debt rate for purposes of calculating its CTC-related revenue requirement if it is granted any stranded cost recoveries in this proceeding. HSS/ARI M.B. at 85-86.

E. Recommendation

In PECO Energy, Slip Op. at 108, the Commission stated it:

> . . . agree[d] that the risk of non-payment of the CTC is minimal. PECO has a large service territory with well over 1 million customers legally required to pay the CTC. Recovery of the full principal amount is assured through the reconciliation mechanisms in Section 2808 (f). The level of risk does not compare with that associated with generation charges pursuant to regulated rates. Under regulated rates, a utility only had the opportunity to earn a reasonable return. There was no guarantee of any return at all. The utility was at risk that sales lower than projected would erode its return. PECO is protected from such risks with the CTC. It should be noted that the CTC costs would not be recoverable under traditional ratemaking principles.
>
> Under such circumstances, we conclude that the record in this proceeding supports adopting PECO's revised long-term debt rate of 7.47% to calculate the revenue requirement for the recovery of the CTC over the 8½ year transition period. This result is between the low range proposed by OCA, PAIEUG, Navy and IPALCO and the 9.52% proposed by PECO. It is close to the 7.53% proposed by NEV. Our proposal of 7.47% reflects the low risk associated with the CTC and therefore achieves a just and reasonable result. We shall use 7.47% for calculating the CTC revenue recovery in this proceeding.

Consequently, the Commission allowed that utility a return on equity of 10%. While several parties urge the Commission to impose the same rate of return in this proceeding, no evidence exists anywhere in this record to provide a comparison between the financial circumstances of Duquesne and PECO, and so justify imposition of a comparable rate of return.

However, the Company's proposed rate of return of 11.5% does not reflect the reduced level of risk inherent in the CTC procedure for collection of stranded costs. Since substantial evidence supports the OTS' proposed 10.5% rate of return, I recommend it to the Commission.

IX. Special Customer Classes

A. Rule 4 Contracts

1. Duquesne's Proposal

Rule 4 Contracts are executed "as a mitigation strategy to attract or retain incremental load that Duquesne would have otherwise lost to a competitive alternative." Duquesne St. 6-R at 4; See, also, N.T. 1029-30. Two issues have arisen regarding these contracts. First, DII contends that Rule 4 contracts should be unbundled so that customers can gain access to the competitive market. DII St. 1 at 54. This contention should be rejected. Rule 4 contracts were entered into between sophisticated parties and were tailored to the specific circumstances of each customer. Duquesne St. 6-R at 4. They have provided benefits to these customers and to the region as a whole. Id. at 4-6. As in PECO Energy, these contracts should "remain in effect according to their terms." PECO Energy, Slip Op. at 120.[187] Duquesne M.B. at 76.

The second contention is OCA's argument that the revenue effect of Rule 4 "discounts" class should be imputed, for CTC calculation purposes, to the class receiving the discounts. OCA St. 4 at 8-10. This proposal is based on a misunderstanding of the nature of a Rule 4 contract. Duquesne St. 6-R at 6. Rule 4 "discounts" do not represent lost revenues; they represent discounts applicable to incremental load and, hence, represent additional revenues that would not otherwise have been earned. Id. The factual basis for the OCA proposal - that the discounts create a loss of revenue - is therefore mistaken. If, however, the OCA proposal,

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[187] Of course, if the contracts themselves permit unbundling, Duquesne will, at the request of the customer, unbundle them consistent with the methodology for all other customers, consistent with PECO Energy, Slip Op. at 120.

which forces Duquesne's shareholders to bear an economic loss, is adopted, Duquesne reserves the right to cease economic development activity under Rule 4. Duquesne M.B. at 76-77.

2. The OCA's Position

The OCA submits the Company's CTC rates to other classes should not be increased to recover stranded costs which are allocated using a utility production plant allocator but cannot be recovered from such customers because of contractual limitations it has with Rule 4 customers. OCA M.B. at 70.

The OCA observes DII takes issue with Duquesne's proposal that Rule 4 contracts not be unbundled. DII M.B. at 89-90. While OCA does not oppose the unbundling of these contracts, OCA submits that, as discussed in the section on class responsibility for stranded costs, stranded costs appropriately allocated to discounted rate customers based upon the utility production plant allocator should not be shifted to other customer classes. If a CTC based on this allocator would violate the rate cap for these customers, OCA submits the Company must forego these revenues unless, for good cause shown, it requests and is granted a longer collection period for these classes. OCA M.B. at 66-67. This is consistent with the Commission's Order in PECO Energy, Slip Op. at 109-13. OCA R.B. at 25.

3. DII's Position

DII claims Duquesne inappropriately denies customers currently taking service under Rule 4 contracts the right of choice of electricity supplier guaranteed to them by the Act because Duquesne refuses to unbundle these contracts. Duquesne St. 6-R at 4. This refusal is

anti-competitive, contrary to the Act and must be rejected by the Commission. Rule 4 customers must be granted their statutory right to direct access unless the particular contract clearly prohibits the customer from accessing competitive supply in the deregulated environment for the duration of the transition period. DII St. 1 at 54; DII M.B. at 89.

Rule 4 contracts have given the Company discretionary pricing ability with customers in order to address "changing business needs or operating conditions." Duquesne St. 5, Exh. JAL-12 at 7. Instead of losing this load, Duquesne has flexibility under its tariff to enter into special contracts at price levels less than tariff rates. Duquesne St. 6-R at 4. Customers are required to sign a five to ten-year contract in order to take advantage of this service. Duquesne St. 5, Exh. JAL-12 at 7. Consequently, some customers are bound by this contractual obligation despite the movement to a deregulated market beginning on January 1, 1999. DII M.B. at 89.

Rule 4 contract customers must be permitted to access alternative suppliers, unless the specific contract between the customer and Duquesne prohibits such access. DII St. 1 at 54. As recognized in the PECO restructuring decision, "there is no statutory suggestion that any class of customers can be denied the opportunity to shop." PECO Energy, Slip Op. at 118. The Commission required PECO to unbundle existing contracts for customers as long as that contract does not prohibit accessing alternative supply. Id. at 120. The Commission must require that Duquesne also unbundle its special contracts. DII offers as suitable method for unbundling Rule 4 contracts. DII St. 1 at 54. The CTC derived from this analysis will be applicable to the customer, if it continues taking service from Duquesne or if it begins taking service from an alternative supplier. Id.; DII M.B. at 89-90.

The DII unbundling methodology of Rule 4 contracts is consistent with the Commission's Order in the PECO restructuring proceeding and should be accepted by the Commission for the unbundling of Duquesne's Rule 4 contracts. See, PECO Energy, Slip Op. at 116-121. The Act and the Commission are clear that no class of customers can unreasonably be denied access to the competitive market. Duquesne's refusal to unbundle Rule 4 contracts is a blatant and unwarranted attempt to deny these customers access to the competitive market that must be rejected. DII respectfully requests the Commission require Duquesne to unbundle Rule 4 contracts on the basis set forth above. DII M.B. at 90.

DII finds Duquesne refuses to unbundle Rule 4 Contracts and permit those customers to have access to competitive generation supply. Duquesne M.B. at 76-77. Duquesne's selective quotation of the PECO restructuring decision in this regard must be rejected. Id. at 76. The Commission in PECO Energy clearly states:

> We conclude that PECO should unbundle existing contracts for customers not prohibited from shopping based on the same guidelines as we have provided for interruptible customers.

Slip Op. at 120. PECO proposed (and the Commission accepted) the following treatment for special contracts: "Existing customers under contracts that are silent concerning future opportunities to chose competitive suppliers will be permitted to enter into separate generation contracts." Id. at 119. In other words, the correct interpretation of PECO Energy is that, unless a contract specifically prohibits unbundling and access to competitive supply, that contract must be unbundled and the customer must have the opportunity to obtain competitive supply. DII M.B. at 89-90. The Duquesne interpretation of the PECO Energy precedent is flawed. DII R.B. at 44.

Enron suggests that Duquesne should be forced to fulfill only the non-generation portions of its Rule 4 contracts. Enron M.B. at 31-33. Enron misconstrues the PECO decision as requiring that any generation-related competitive rate or rider, currently offered by Duquesne, can no longer be offered in a competitive environment; rather, PECO Energy mandates that Duquesne must unbundle those rates in order to provide customers with the opportunity for direct access. PECO Energy, Slip Op. at 119-20. Customers' right to direct access is guaranteed in the PECO decision and under the Act, not the alternative suppliers' right to prevent Duquesne from serving customers under its tariff in effect as of January 1, 1997. Moreover, it is not only possible, but mandatory, that Duquesne unbundle Rule 4 Contracts. DII M.B. at 89-90; DII R.B. at 44.

4. HSS/ARI's Position

HSS/ARI support Duquesne's continued ability to offer Rule 4 contracts. HSS/ARI also believe, consistent with Duquesne's proposal, that existing Rule 4 contracts should remain in effect during their term. However, parties with Rule 4 contracts should not be deprived of benefits that result from this proceeding. Accordingly, if the rates ordered as a result of this proceeding are lower than the rates that would apply under a particular Rule 4 contract, the rates ordered herein should be available to the particular Rule 4 customer in lieu of the higher rates set by the Rule 4 contract. That result is required, because in the circumstance described, the Rule 4 rates would not be just and reasonable. HSS/ARI M.B. at 86.

5. PRA's Position

The PRA asserts Duquesne's proposal to deny Rule 4 customers' access to a competitive retail generation market is illegal. It is in violation of the law and PECO Energy's underlying decision. It must be rejected. PRA R.B. at 26.

6. Enron's Position

In PECO Energy, the Commission established standards governing the application and continuance of certain tariffs and riders available to special customer classes. As a general rule, the Commission required that "[a]ll existing tariffs shall remain available throughout the transition period and all special contracts shall remain in force, except as modified pursuant to this Opinion and Order or other tariff modifications approved by the Commission."[188] The Commission went on to conclude:

1. No class of customers can be denied the opportunity to shop.
2. Interruptible service must be made available to all classes of customers.
3. The EDC "must file tariffs for distribution and transmission service applicable to customers in all classes, who choose to shop."[189]
4. The EDC must allocate all existing discount provisions between the T&D and the generation components of the service and make each tariff or rider available as a T&D service with the allocated T&D discounts so that an eligible customer can purchase the discounted T&D service and still shop for generation service.

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[188] PECO Energy at 117.

[189] Id. at 118.

5. "Competitively priced" tariff offerings associated with generation will be eliminated and will remain available only to those customers, who are not yet eligible for choice.

6. All existing EDC contracts will be honored and need not be assigned.

7. For contracts which do not preclude shopping, the EDC must unbundle the contract and allocate the discounts as set forth for interruptible tariffs above; and

8. No customers may avoid the CTC obligation.[190]

Clearly all of these standards reflect Commission policy decisions, which should not vary from case to case or from EDC to EDC. Accordingly, they should be adopted by the Commission in this proceeding. Enron M.B. at 31-32.

Duquesne's proposal to continue to offer its special contract "economic development rates" (Rule 4 and a Rider applicable to smaller customers)[191] to existing customers and in some instances to <u>new customers</u> may in some cases, be inconsistent with the Commission's policy as described above. Duquesne's rates should be consistent with the following:

- Special tariffs or economic development rates that Duquesne proposes to keep should be unbundled so that each rider or rate discount is available to customers for distribution service.[192] As Rule 4 Contracts are negotiated unbundling would not seem possible; however, Rule 4 contracts should be limited to distribution services <u>only</u> once direct access begins.

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[190] Id. at 117-121.

[191] Duquesne St. 6 at 16-19.

[192] Duquesne's plan appears to be that upon restructuring, it will assign economic development discounts to the CTC and that customers will be able to use alternative suppliers. This is appropriate and consistent with the <u>PECO Energy</u>. It should be implemented for all economic development rates Duquesne plans to continue to offer.

- Rates or Riders offering discounted generation service will not be available to customers not presently on such rates or to prospective customers once these customers are eligible for choice. (Such customers may receive discounted service from competitive suppliers or the unregulated affiliate or division of Duquesne itself.)

A customer is eligible for choice, when a portion of its load is eligible to be supplied by competitive suppliers. Enron M.B. at 33.

The general thrust of Duquesne's testimony appears to recognize the inappropriateness of continuing to offer special contracts or discount riders as they apply to generation.[193] This is appropriate, but the Commission should assure that all Duquesne "economic development" or discount rates comply with this directive. The Commission should limit the continued availability of these rates (as to generation) in favor of allowing customers to receive even greater benefits through a robust competitive market. Id.

7. Recommendation

On the subject of special customer classes, the Commission, in PECO Energy, Slip Op. at 116, stated:

> Section 2804(7) requires the Commission to implement the Act "in a manner that does not unreasonably discriminate against one customer class to the benefit of another." Different classes of customers have received service upon different terms and conditions under traditional regulation. The transition to competition means that the market will determine many of these terms of service as they apply to competitive generation. As a result, the Commission must consider the special circumstances of several customer classes in order to ensure that all classes are provided a fair opportunity to achieve the advantages anticipated under the Act.

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[193] Duquesne St. 6-R at 4.

Further, Section 2804(3) provides that "the Commission shall require the unbundling of electric utility services, tariffs, and customer bills to separate the charges for generation, transmission and distribution." However, several tariffs serving special customer classes were designed without granting the customers an opportunity to choose an alternative generation supplier. In such instances, the Commission found:

> As a general rule, our approach to these special classes of customers is to treat them the same as all other customers concerning all regulated rates and services including transmission, distribution and generation services provided by PECO as an EDC, including CTC obligations. All existing tariffs shall remain available throughout the transition period, and all special contracts shall remain in force, except as modified pursuant to this Opinion and Order or other tariff modifications approved by the Commission. Our goal is to permit customers to continue to receive the economic benefit of these tariffs to the extent that such benefits can be applied to the regulated portion of the bill.

However, there is a statutory mandate to ensure that an EDC makes transmission and distribution service available to such customer classes. 66 Pa. C.S. §2804(2). Section 2804(2) specifies the Commission:

> . . . shall allow customers to choose among electric generation suppliers in a competitive generation market through direct access. Customers should be able to choose among alternatives such as firm and interruptible service, flexible pricing and alternate generation sources, including reasonable and fair opportunities to self-generate and interconnect. These alternatives may be provided by different electric suppliers.

Thus, the Act specifies that interruptible options must be available. In PECO Energy, Slip Op. at 118, the Commission noted:

> Interruptible service provides customers with an opportunity to save because they do not contribute to more expensive peak load. Interruptible service also provides an important reliability benefit

to all consumers because it provides an organized way to reduce load under peak demand.

Accordingly, an EDC must file tariffs for distribution and transmission service applicable to customers in all classes, who choose to shop. Id. The EDC must do so in a manner that properly allocates the costs and existing discount provisions to each of the transmission, distribution and generation components of service. Id. "Even interruptible service has a distribution and transmission system benefit at times of times of peak load." Id. Discounts allocable to generation should remain available to customers purchasing generation from the EDC, but not to customers purchasing generation from other suppliers, who will likely offer alternative savings of their own. Id. To the extent any portion of the discount is properly allocated to distribution or transmission, however, the EDC's unbundled transmission and distribution tariffs must retain that benefit for a customer choosing to shop. Id. The EDC's compliance filing must include proposed tariffs to implement these results and otherwise comply with the applicable rate cap provisions of Section 2808(4). Id.

Existing contracts containing language covering the future availability of competitive generation services will be governed by the terms of the contracts. Id. at 119. Existing customers under contracts that are silent concerning future opportunities to choose competitive suppliers will be permitted to enter into separate generation contracts. Id. "Now that all customers will have competitive choices, it is no longer necessary to provide such 'competitively priced' services pursuant to 'regulated rates' approved by the Commission...." Id. Customers will have the opportunity to obtain competitive rates from any supplier in the market and the EDC is free to provide competitive rates through its competitive affiliates or divisions. Id.

The EDC must honor all existing contracts and be permitted to continue to negotiate these special contracts with any customer, who has not yet been phased-in to customer choice. Id. Existing contracts specifying requirements upon the commencement of competitive generation generally should remain in effect according to their terms and it is not necessary to assign such existing contracts to an affiliated competitive supplier. Id. at 119-120. Customers on these contracts may retain regulated generation service from the EDC throughout the transition period, just as all other customers can. Id. Finally, the Commission concluded that the EDC should unbundle existing contracts for customers not prohibited from shopping based upon the same guidelines that it established for interruptible customers. Id.

On the subject of CTC payments by special customer classes, Section 2808(a) requires the Commission to adopt a CTC that recovers authorized stranded costs "allocated in a manner that does not shift interclass or intraclass costs and maintains consistency with the allocation methodology utility production plant" presently used to establish rates. Id. The Act does not permit customers to bypass payment of the CTC. Id. Accordingly, no contract or tariff may permit a customer to bypass payment of the full CTC allocable to its use of the transmission and distribution system. Id. Any existing contract that does so must be modified to require full payment of the CTC, while providing a comparable dollar value offset on the regulated transmission, distribution or generation rates. Id. at 120-121. The terms of service for these classes of customers may make it appropriate to design a CTC that collects the customer's full share of stranded costs in a manner different than the general "per/kWh" methodology. Id. The EDC's compliance filing may propose alternative methods, provided it otherwise complies with the Commission's decision in PECO Energy and the Act. Id.

Duquesne's contracts and tariffs for special customer classes should be modified to comply with the foregoing requirements.

B. Riders 8 and 20

1. Duquesne's Position

Duquesne offers the following three economic development tariff riders: (i) Rider 8, which offers discounts for incremental consumption by existing industrial customers; (ii) Rider 9, which offers discounts for new load from large new customers; and (iii) Rider 20, which offers discounts for both incremental consumption by existing commercial customers and new load from new commercial customers. Duquesne St. 6 at 16. The issue presented here is whether Duquesne, as it has proposed, should eliminate the discounts for incremental load from existing customers (Rider 8 and part of Rider 20), but not discounts for new load from new customers. Duquesne St. 6 at 18; Duquesne St. 6-R at 3. DII contests this proposal (DII St. 1 at 58-59), but it is clearly appropriate. Duquesne has made this proposal, because the riders regarding existing customers are no longer necessary; Duquesne's proposed rate redesign does the same thing: it provides a discount on incremental usage by existing customers. Duquesne St. 6-R at 3-4. Accordingly, if the riders were retained, these customers would simply receive a "discount on a discount," which is not economically efficient or consistent with stranded cost mitigation. Duquesne St. 6-R at 3-4; Duquesne M.B. at 77-78.

2. DII's Position

DII notes Duquesne proposes to eliminate the economic development incentive rates currently available to existing customers in Tariff Rider 8 "Industrial Economic Development Rider for Customers at Existing Service Locations" and Tariff Rider 20 "Small Business Development Rider." Duquesne Light Company Supplement to No. 4 to Tariff Electric Pa. P.U.C. No. 17, issued May 28, 1997, pp. 71-76 & 100-103 (hereinafter "Duquesne Tariff"). These rates are proposed to be phased-out as customer contracts expire over the next five years. Duquesne St. 6 at 18. This phase out is clearly inappropriate under the Act and must be rejected. DII M.B. at 90.

Chapter 28 guarantees that the generation component of rates is capped at the January 1, 1997, level for the entirety of the transition period. 66 Pa. C.S. §2804(4)(ii). Eliminating the credits before the end of transition period will increase the rates of current Rider 8 and 20 customers above the January 1, 1997 level. Under Rider 8, existing customers receive a percentage discount to incremental capacity and energy charges when the customer's usage for a month ("current Billing Demand") exceeds a baseline monthly usage established by Duquesne for the customer ("Monthly Base Period Billing Demand") by a specified percentage ("5%"). Duquesne Tariff at 71-72. The more a customer's usage exceeds the baseline, the higher the percentage discount provided to the customer. Id.; DII M.B. at 90-91.

Rider 20 provides the following economic incentive credit to Rate GS/GM customers:

> A qualifying customer will earn a separately stated credit equal to the Billing Demand minus the Monthly Base Period Billing Demand multiplied by the discounted Incremental Unit Capacity Charge of Rate GS/GM. The minimum Monthly Base Period

> Billing Demands for new or existing customers will be five (5) kW. The percentage discount is 50% for the first 36 months, 30% for the next 12 months and 15% for the last 12 months the customer is on this rider.

Duquesne Tariff at 100; DII M.B. at 91.

These discount schedules were part of customers' rates as of the effective date of the Act. Eliminating the discounts raises the rates of Rider 8 and 20 customers above January 1, 1997, levels in the amount of the previously available discounts, in violation of the Act's rate cap. 66 Pa. C.S. §2804(4). The Commission must not endorse such an obvious violation of the Act. DII M.B. at 91.

In addition, the Commission stated in the PECO decision that,

> All existing tariffs shall remain available through the transition period, and all special contracts shall remain in force, except as modified pursuant to this Opinion and Order or other tariff modifications approved by the Commission.

PECO Energy, Slip Op. at 117. The Commission mandated that PECO continue to offer rates such as the PECO's Economic Efficiency Rider ("EER") to existing customers until the end of the transition period. Id. at 118. The Commission should afford equivalent protection to the existing customers on economic development rates in the Duquesne service territory. The Company's proposed elimination of the Rider 8 and 20 credits prior to the end of the transition period must be rejected. DII M.B. at 91.

Moreover, the Company proposes to continue to offer economic incentive rates to new customers at new service locations. Duquesne St. 5, Exh. JAL-12 at 104-107. This discriminatory treatment is unwarranted. The Act clearly recognizes that the attraction and retention of businesses is necessary to promote the economic welfare of the Commonwealth.

66 Pa. C.S. §§2802(6) & (7). Elimination of the credits prior to completion of the transition period may increase current customers' energy cost, which, as recognized by the Act, "is an important factor in decisions made by businesses concerning locating, expanding and retaining facilities in this Commonwealth." 66 Pa. C.S. §2802(6). Apparently, Duquesne is only willing to support the business attraction goals of the Act and intends to completely ignore the business retention goals. 66 Pa. C.S. §§2802(6) & (7); DII M.B. at 91-92.

In addition, the Act requires that "restructuring of the electric utility industry be implemented in a manner that does not unreasonably discriminate against one customer class to the benefit of another." 66 Pa. C.S. §2804(7). Duquesne's elimination of the Rider 8 and 20 credits for existing customers blatantly discriminates against existing customers. DII St. 1 at 59. This discrimination is unreasonable because there is no rational basis to distinguish between the business attraction goals of the Act and the business retention goals. 66 Pa. C.S. §2802(6). Both attraction, retention and expansion are necessary for economic prosperity.[194] Finally, the discriminatory treatment may create competitive disadvantage situations between existing and new customers. DII St. 1 at 59. This is clearly contrary to intentions of the Act and is not the equitable balancing of interests required during the transition period. 66 Pa. C.S. §2802(8); DII M.B. at 92.

Duquesne's proposal to eliminate Riders 8 and 20 for existing customers is clearly contrary to the Act and must be rejected. Elimination of the Riders circumvents the generation rate cap that is available to all customers as a consumer protection, while Duquesne collects

[194] Duquesne's proposal may also impact decisions regarding the expansion of current facilities, if the discount on incremental load is not available.

stranded costs. In addition, elimination of the credits for existing customers, while continuing the availability for new customers is discriminatory, unreasonable and contrary to the Act's economic development goals. DII respectfully requests the Commission mandate Riders 8 and 20 remain available to existing customers throughout the transition period. Id. at 92.

In response to the DII argument, Duquesne states that the riders are unnecessary because Duquesne's proposed rate redesign will accomplish the same objective for incremental usage. Duquesne M.B. at 77-78. The Company is misguided. The Commission's Order in the PECO restructuring proceeding specifically requires that: "All existing tariffs shall remain available through the transition period, and all special contracts shall remain in force, except as modified pursuant to this Opinion and Order or other tariff modifications approved by the Commission." PECO Energy, Slip Op. at 117; DII M.B. at 90-92. PECO is required to continue to offer its Economic Efficiency Rider to existing customers Id.; Duquesne should be required to do the same.[195] DII R.B. at 45.

Moreover, the Company claims that continuing availability of the riders will provide customers with "a discount on a discount." Duquesne M.B. at 78. This assertion only applies (if it applies at all) when customers take advantage of Duquesne's rate redesign proposal, which is now optional. Furthermore, it is illogical to call economic efficiency riders to existing

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[195] Duquesne supports the elimination of these riders based on the availability of its proposed rate redesign. Duquesne M.B. at 77-78. The availability of this optional redesign is irrelevant. The Act clearly requires that all current tariff offerings continue to be provided throughout the transition period. If the rate redesign truly satisfies the same goals as the economic development riders, then the customers on those riders will logically and naturally take advantage of the rate redesign. However, DII submits that the decision to switch from the development rider to the rate redesign must be the customer's and the existing tariff riders must remain in effect.

customers as a "discount on a discount" without also calling the economic development riders that will be available to new customers the same. The Company's purported rationale is baseless and must be rejected. DII R.B. at 45.

3. **PRA's Position**

The PRA also notes Duquesne proposes to eliminate these economic development incentive rates currently available to customers. This is in violation of the Act in that it increases the customer's rate above the rate cap imposed on January 1, 1997. Moreover, Duquesne's action is inappropriate when considered in light of its discriminatory treatment of providing special treatment to new customers at new service locations by authorizing access to the competitive retail generation market far earlier than existing customers. The Act recognizes, as a Commonwealth public policy, that the retention of existing business is vital to the competitive position of the Commonwealth. PRA R.B. at 26-27.

4. **Recommendation**

In PECO Energy, Slip Op. at 119, the Commission noted these contracts provide rate discounts in order to retain or expand customers or load as competitive pressures limited the EDC's ability to continue to charge full regulated rates. In recognition of the increasing competitive pressures that led to adoption of the Act, the Commission approved such tariffs or individual contracts provided the EDC received at least the marginal cost of service and no foregone revenues were shifted to other customers. Id. The Commission then stated:

> Now that all customers will have competitive choices, it is no longer necessary to provide such "competitively priced"

> services pursuant to "regulated rates" approved by the Commission through the [discount tariffs]. Customers will be able to obtain competitive rates from any supplier in the market and [the EDC] is free to provide competitive rates through its competitive affiliates or divisions.

Id.

Since all existing customers under a special discount contract will have the opportunity to fully shop for generation no later than the final phase-in on January 1, 2001, the Commission should approve Duquesne's proposal to phase-out these special customer discount contracts as they expire over the next five years, provided the affected customers are fully phased-in to direct access to the generation market at the time of contract expiration. On the other hand, the Company's offering special discount contracts to new customers or existing customers with new load constitutes discriminatory treatment proscribed by the Act. 66 Pa. C.S. §2804(7). Duquesne can acquire new customers or new load in the competitive generation marketplace. For these reasons, the Commission should approve the Company's proposal for Rider 8, as herein modified, and deny the Company's proposal for Riders 9 & 20.

C. Self-Generation

1. Duquesne's Proposal

The Company notes the Environmentalists recommend that Duquesne promote the use of self-generation facilities, such as solar and fuel cells, through a "net metering" arrangement. Env. St. 1 at 7-8. This proposal conflicts with the Act, because it would permit customers who install generation to avoid paying an equitable portion of stranded costs. Duquesne St. 5 at 79-80. Section 2808(a) of the Act provides that if a customer installs on-site

generation "which significantly reduces the customer's purchases of electricity through the transmission and distribution network, the customer's fully allocated share of transition or stranded costs shall be recovered from the customer through the competitive transition charge." 66 Pa. C.S. §2808(a); PECO Energy, Slip Op. at 124. The proposal should be rejected. Duquesne M.B. at 78.

2. The Environmentalists' Position

(a) Distributed Energy

The Environmentalists observe the Act appears to envision an energy future, which is very similar to today's world, in which the generation of electricity is dominated by large central-generating stations. The Environmentalists have advanced a different view that our generation future will be marked by more decentralized, distributed systems. The challenge facing us is to design a marketplace, which can accommodate not only the large central plants, but also the energy future of small turbines, roof-shingle photovoltaics and dishwasher-size fuel cells. We need marketplace rules, which allow these new distributed energy sources. Env. M.B. at 34.

(b) Interconnection

Small distributed energy projects, which face endless interconnection obstructions and high fees will never succeed. To remove unnecessary barriers to interconnection, the Environmentalists recommend several changes to the connection provisions of the tariff. First, the technical standards should be simplified and made consistent with IEEE, UL and other

national standards. Second, for photovoltaic and other simple systems, the engineering review should be replaced with an inspection designed to confirm that the systems meet IEEE and UL standards and the cost of this review should be capped at $35. The interconnection review fee for other installations should be capped at $250. Third, the tariff should allow a customer three metering options at the customer's choice: a non-ratcheted bidirectional meter; two meters; or a smart meter. There should be no additional meter-reading fee. Env. M.B. at 34-35.

(c) Net Metering

Duquesne currently does not have a net metering tariff. The Environmentalists recommend that, as a condition for receiving stranded cost recovery, Duquesne should implement a net metering tariff for renewable energy and fuel cell projects by any customer class, which are 10 kW or less. In addition, the net metering provisions should specify retail-in/retail-out up to net each month and customers should be able to carry forward a generation credit (at the retail-out rate) for up to 12 months. The net metering provisions must address what happens when the customer is purchasing power from an alternate supplier. Env. M.B. at 35.

3. Recommendation

The Environmentalists proposal for using a "net metering" arrangement should be rejected as violating the Act's mandate for a non-bypassable CTC. 66 Pa. C.S. §2808(a); PECO Energy, Slip Op. at 124. The remaining issues raised by the Environmentalists should be more appropriately considered in generic proceedings.

D. Other Tariff-Related Issues

1. DII's Position

DII posits three other tariff-related issues must be addressed in this proceeding. Duquesne proposes changes to its current tariff for Interruptible Service (Rider 7), Time-of-Day Service (Rider 5) and High Voltage Power Service (HVPS) that are inappropriate and must be rejected. All Duquesne tariff offerings must remain intact throughout the transition period in order to provide customers with the rate cap protection mandated by the Act. 66 Pa. C.S. §2804(4). Only tariff changes necessary to unbundle rates and introduce competition for generation supply are appropriate during the transition period while customers are captive to the payment of a CTC. DII M.B. at 93.

(a) Interruptible Service (Rider 7)

Duquesne submits a tariff for Interruptible Service that makes two significant changes to the rate. Duquesne St. 5, Exh. JAL-12, pp. 95-97; compare, Duquesne Tariff at 68-70. Both changes are unreasonable and not necessary to introduce the competitive generation supply option to Duquesne's service territory. DII M.B. at 93.

Duquesne's proposed tariff rider for Interruptible Service contains the following provision:

> Customers must contract under this rider prior to December 31, 1998 and must take full service from the Company as defined in the applicable rate schedules to qualify.

Duquesne St. 5, Exh. JAL-12 at 95. This provision places two restrictions on the availability of Interruptible Service, neither of which is in the current tariff. Duquesne Tariff at 68-70. These restrictions are inappropriate and must be rejected. DII M.B. at 93.

First, the Act authorizes submission of tariff changes only to the extent necessary to modify the current tariff to accommodate:

> . . . unbundled prices or rates for generation, jurisdictional transmission, distribution and other services; a proposed competitive transition charge; a proposed universal service and energy conservation cost-recovery mechanism; procedures for ensuring direct access to all licensed electric generation suppliers . . . .

66 Pa. C.S. §2806(e). The proposed availability restrictions are not connected to any of these purposes. DII St. 1 at 56. Consequently, the charges can't be categorized as authorized or necessitated by the Act. DII M.B. at 93-94.

Furthermore, customers must have the option to remain on Interruptible Service for a portion of their load. Under the DII proposal for the phase-in of retail access, all customers may participate in the first and second stages of the phase-in for a portion of their load. If the DII pro-rata phase-in is adopted, interruptible customers wanting to participate in the market during the phase-in will be forced to revert to Duquesne's firm service for the remaining portion of the load, because they will no longer qualify as "full service customers." DII St. 1 at 55-56. This reversion will result in a rate increase for these customers (in violation of the Act's rate caps) and will deter their ability to participate in direct access during phase-in. The Duquesne proposal will not foster the competitive market sought by the Act. DII M.B. at 94.

In addition, the Company offers no justification for the proposed restrictions. The Company's rebuttal testimony regarding tariff issues fails to mention DII's objections. Duquesne St. 5-R, Exh. JAL-14 at 19; Duquesne St. 6-R at 2-7. Because the proposed changes in the Interruptible Service rider have not become effective, Duquesne has the burden of establishing

the reasonableness of its proposal. 66 Pa. C.S. §§315(a) & 332(a). Duquesne fails to satisfy this burden. The proposed restrictions on the availability of Interruptible Service are unsupported by the Company and unnecessary to introduce the competitive market for generation supply. DII M.B. at 94.

The Duquesne restrictions on the availability of Interruptible Service are unreasonable and not authorized under the Act. The only tariff changes permissible in the context of this restructuring proceeding are those necessary to introduce a competitive market for generation supply in Duquesne's service territory. DII submits that limiting Interruptible Service to customers taking full requirements service as of December 31, 1998, is not necessary or appropriate under the Act to introduce competition in the Duquesne service territory. Moreover, Duquesne fails to support the reasonableness of the proposed restrictions. DII requests the Commission reject the proposed availability restrictions on Interruptible Service. Id. at 94-95.

(b) Time-of-Day Rates (Rider 5)

Duquesne proposes to restrict the availability of Time-of-Day service (Rider 5) to customers that contract prior to December 31, 1998. Duquesne St. 5, Exh. JAL-12 at 92. This restriction is not present in the current tariff. Duquesne Tariff at 65-66; DII M.B. at 95.

The arguments stated in the previous section regarding Interruptible Service apply with equal force to the proposed change in the availability of Time-of-Day service. DII St. 1 at 56-57. Duquesne fails to establish the reasonableness of its proposed tariff change. 66 Pa.

C.S. §§315(a) & 332(a). DII submits that the change is unreasonable and must be rejected. DII M.B. at 95.

(c) **HVPS**

The Company's proposed tariff omits the provision in the HVPS tariff with regard to "Generation Avoidance" energy. Duquesne St. 5, Exh. JAL-12 at 60-66. Generation avoidance is designed to permit an HVPS customer that produces a portion of its energy requirement for its own use with internal generating equipment to purchase electricity from Duquesne and avoid the use of alternative energy sources when its equipment fails. DII St. 1 at 57. The Company acknowledges that generation avoidance was inadvertently omitted and agrees to reinsert the provision in the final tariff to be submitted as part of the compliance filing in this proceeding. Duquesne St. 5-R, Exh. JAL-14 at 19. This reinsertion of the provision alleviates DII's concerns with respect to Generation Avoidance in this part of the proceeding. DII St. 1-S at 14. DII recommends that the Commission require the Generation Avoidance section to be reinserted in the compliance filing by Duquesne in this proceeding. DII M.B. at 95; DII R.B. at 46.

2. **Recommendation**

For the reasons advocated by the DII, the Commission should deny the Company's proposed changes to its current tariffs for Interruptible Service (Rider 7), Time-of-Day Service (Rider 5) and High Voltage Power Service (HVPS).

X. Competitive Safeguards

A. Code of Conduct

1. Duquesne's Proposal

Duquesne proposes a Code of Conduct to ensure an adequate separation of the regulated and unregulated portions of its business. Duquesne Exh. FH-2. Many parties, however, paid no attention to it, such as Enron. Enron criticizes a different code of conduct – *the code adopted in* Duquesne's *pilot proceeding – not the one proposed by* Duquesne *in this* case. Compare Enron St. 1.0 at 7-8 with Duquesne Exh. FH-2. Whatever the level of attention (or inattention) to this matter, this is an issue that should be decided on a generic basis for all EDCs and suppliers in the Commonwealth. Duquesne St. 6-R at 28; Duquesne M.B. at 79.

2. The OCA's Position

In its filing, Duquesne submitted a proposed Code of Conduct to apply to the Company's provision of regulated and unregulated services. Duquesne Exh. FH-2. OCA witness Alexander reviewed the Company's filing, as well as Codes of Conduct adopted in Massachusetts and California, and made recommendations to address several gaps in Duquesne's Code of Conduct. OCA St. 5 at 53. Specifically, she notes the Company's failure to propose its future corporate structure under retail competition. Id. at 54. Additionally, Ms. Alexander made the following proposals, discussed in detail in her testimony, to supplement or clarify Duquesne's proposed Code of Conduct:

1) The proposed Standards should distinguish between the "transmission or distribution function" and the "generation function."

2) There should be no subsidization of the unregulated affiliates or divisions by the regulated division, which is accomplished by permitting the regulated affiliate to purchase only generally available tariffed items and strictly defining any shared A&G support services.

3) The Duquesne Light regulated utilities and the corporate marketing affiliate should not conduct joint marketing.

4) Completely sensitive information should not be transmitted to employees providing unregulated services unless the information is already available and known to be available (through an OASIS-type data central system) to nonaffiliates.

5) The dispute resolution procedure to address complaints alleging violations of the Code of Conduct should include, at a minimum, a procedure to designate a person to conduct an investigation of the complaint and report the results of this investigation to the complainant in writing within 30 days after the complaint is received, including a description of any action taken in response to the complaint and the complainant's option to complain to the PUC if not satisfied with the results of the investigation.

Id. at 54-56. The OCA submits that proper resolution of the Code of Conduct is a critical issue and will have a great deal to do with the development of a competitive market. Id. at 53; OCA M.B. at 70-71.

With regard to EDC conduct in the context of an Application for Service, Ms. Alexander recommended certain minimum procedures to guard against the use of Duquesne's regulated entity to unfairly market the unregulated entity. Id. at 34-36. Ms. Alexander's proposals are set forth fully in her testimony. OCA M.B. at 71.

The Commission also addressed this issue in PECO Energy and found that it was appropriate to adopt an interim Code of Conduct that contained appropriate detail to apply before the regulations concerning competitive safeguards and customer supplier interaction are adopted. Slip Op. at 129. Additionally, the Commission also made a number of changes to the Company's proposed Code of Conduct to address the need to have functional separation between

the Company's regulated and unregulated entities and comparable direct access for all affiliates. Id. at 129-131. The OCA agrees with the Commission's concern and submits that Duquesne be directed to adopt OCA witness Alexander's modifications to its proposed Code of Conduct. OCA M.B. at 71.

The OCA notes the Company has stated that it has proposed an adequate Code of Conduct, and that any further resolution of this issue should be decided "on a generic basis for all EDCs and suppliers in the Commonwealth." Duquesne M.B. at 79. Having reviewed the Company's filing, the OCA presented several specific proposals that OCA witness Alexander made to Duquesne's proposed code of conduct to supplement or clarify the Company's proposal. OCA M.B. at 70; OCA St. 5 at 52-56; OCA R.B. at 25-26.

These amendments are necessary to address the appropriateness of Duquesne's Code of Conduct on an interim basis. As these issues are raised in generic proceedings, the OCA will participate in those proceeding as well. However, it is necessary that an appropriate Code of Conduct to address interaction between Duquesne's regulated and unregulated functions be put in place at this time, since it is anticipated that these rulemakings will not be concluded prior to the implementation of customer choice. The Commission reached a similar decision in PECO Energy. Slip Op. at 129. As such, the OCA submits that the Duquesne's proposed Code of Conduct be modified as set forth in the OCA's Main Brief, as well as OCA witness Alexander's testimony. OCA M.B. at 70-71; OCA St. 5 at 34-36, 53-56; OCA R.B. at 26.

3. The PRA's Position

The PRA finds an appropriate Code of Conduct is absolutely an imperative predicate for development of a competitive retail generation market. It places all market participants on notice as to inappropriate conduct thus providing a level of comfort to Duquesne's employees. PRA R.B. at 27.

4. Enron's Position

Through passage of the Act, Enron notes the General Assembly set forth a statutory foundation for bringing the full benefits of retail competition to Pennsylvania consumers and businesses. However, unless the Act is implemented in a manner which creates a "level playing field" between all generation suppliers - utility affiliates and non-affiliated suppliers alike - the promise of the Act will not be realized. While complete divestiture or structural separation is the preferred safeguard, at a minimum, complete functional separation enforced by a strong Code of Conduct is critical to meaningful competitive development.[196] Moreover, a

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[196] The Commission and Enron witness Steffes are in total agreement on this point. As Mr. Steffes stated:

> [I]t is essential to the development of competition that the Commission establish a clear separation between the monopoly, regulated operations of Duquesne and its unregulated supplier and other affiliate roles . . . [Duquesne's] Code of Conduct does not deal in any way with the need for separation of Duquesne's regulated and unregulated activities or for the need to establish cost accounting and other cost separation rules.

Enron St. 1.0 at 7-8.

In strikingly similar fashion, the Commission states in the PECO Energy:

(continued...)

strong Code is necessary regardless of whether Duquesne intends to offer "unregulated services to customers."[197] A Code of Conduct is necessary to insure that an EDC does not obtain or convey a competitive advantage to its generation service operation - whether it provides unregulated services or not. An EDC's control of monopoly distribution facilities - if unfettered - would permit it to manipulate information and access to such facilities in order to retard competition and enhance the market position of the EDC in its role as "provider of last resort."[198] Enron M.B. at 34-35.

While it is clear a permanent Code of Conduct will be established for all EDCs in the context of the Commission's rulemaking docket on this subject,[199] it is critical that the Commission establish in this proceeding an interim Code of Conduct for Duquesne which will be immediately effective. As Enron witness Steffes explained:

> A strong code of conduct is equally critical in the early stages of direct access. If EDCs are permitted to leverage the advantages

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[196](...continued)

> In our view, functional separation of regulated EDC functions and competitive generation functions is essential for the development of a vibrant competitive market. Structural separation through the establishment of fully independent entities is preferable whenever possible. With the development of competitive generation, the EDC must not have reason to treat its competitive suppliers differently than any other competitive supplier. Functional separation without legal separation must not provide a basis for any competitive advantage or opportunities for the marketing entity.

Slip Op. at 128.

[197] Duquesne St. 6 at 15.

[198] Enron St. 1.0 at 7.

[199] Competitive Safeguards - Proposed Rulemaking Order adopted January 29, 1998.

> inherited from their historic monopoly status and pass through or transfer those advantages to their affiliates, no unaffiliated supplier will be able to attract customers even if that supplier is offering lower priced or superior service.[200]

Enron M.B. at 35.

Direct access begins in January of 1999. Accordingly, marketing activity will commence only months after Commission entry of a final Duquesne Restructuring Order. While Enron understands that the Commission has recently initiated a proposed rulemaking docket to codify a generic statewide code of conduct, it is likely that due to its controversial nature, the rulemaking will require 12 - 18 months prior to final promulgation of regulations. In no conceivable circumstance will the rulemaking be completed in time to govern the initial marketing activity that will precede the start of direct access on January 1, 1999. Accordingly, it is critical that the Commission establish a Code of Conduct to govern the activities of Duquesne and its affiliates/divisions during the pendency of a binding regulation,[201] in order to have a Code in place for the initial customer selection and marketing process. Enron M.B. at 36.

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[200] Enron St. 1.1 at 4.

[201] Of course, the Commission recognized the necessity to implement competitive safeguards immediately by establishing an interim Code of Conduct applicable to PECO and its affiliates in PECO Energy. As the Commission stated in reaching a determination to establish an interim Code of Conduct for immediate application to PECO:

> The rules adopted herein shall be applicable in PECO's distribution territory until changed. In particular, we note that the Commission is in the process of adopting regulations covering competitive safeguards in Docket L-0097 and Customer Supplier Interaction at Docket No. M-00960890F0011.

Id. at 129.

It is equally clear that the Code of Conduct proposed by Duquesne is not adequate, even on an interim basis. As will be explained below, Duquesne's proposed Code is extremely limited in scope and fails to cover crucial aspects of the EDC/affiliate or division relationship. Enron strongly advocates application of the Code of Conduct that was proposed by another EDC, Portland General Electric Company ("PGE") as part of its customer choice program filed last year. The PGE Code of Conduct is eminently fair both to suppliers and to the Company and, given that it was proposed by an electric distribution company, it can hardly be claimed that it is biased in favor of suppliers.[202] The PGE standards are much more comprehensive than those proposed by Duquesne, however. In addition to remedying the shortcomings of Duquesne's Code of Conduct in the area of functional separation, the PGE Code ensures that services, products, and information are all provided and utilized on a comparable basis among all suppliers. Additionally, it prevents the incumbent EDC from promoting any affiliated supplier, either through direct promotions or representations, or by identifying the affiliate using the name, logo, or trademark of the EDC. Id. at 36-37.

Alternatively, given the precedent established in PECO Energy, and recognizing the need for a uniform statewide governing Code of Conduct, Enron would find it appropriate to follow the rules established by the Commission in PECO Energy, with a clarification and one addition. As the Commission has recognized on numerous occasions, the content of competitive safeguards is a generic issue which must be determined on a statewide basis. Establishment of such a uniform Code of Conduct avoids the necessity of parsing each EDC's Code of Conduct

[202] This fact alone refutes Duquesne witness Hoffman's contention that Enron's comments on Duquesne's Code of Conduct stem from its interest in "handicapping" Duquesne and its affiliates. Duquesne St. 6-R at 28.

in order to resolve the inevitable claims that certain acts are or are not prohibited by the Code in question. The PECO interim Code of Conduct is fully supported by the record in this proceeding and should be adopted pending codification of final regulations. Id. at 37.

The PECO interim Code of Conduct reads as follows:

> The Company and its divisional and/or affiliated EGSs ("PECO Supplier") shall comply with the following Interim Code of Conduct:
>
> 1. The Company, in its role as the Electric Distribution Company ("PECO EDC"), shall not give a PECO Supplier preference over a non-affiliate in the provision of goods and services, such as processing requests for information, complaint processing and responses to service interruptions. PECO EDC shall provide comparable treatment without regard to the customer's chosen supplier.
>
> 2. PECO EDC shall supply services and apply the rules and other provisions of its Tariffs to non-affiliates in the same manner it applies them to a PECO Supplier.
>
> 3. PECO EDC shall not sell non-power goods or services to a PECO supplier at a price below the cost or market price, whichever is higher, for said goods or services. PECO EDC will not purchase non-power goods or services from a PECO Supplier at a price above the market price for said goods or services. No transaction between PECO EDC and a PECO Supplier shall involve an anti-competitive cross-subsidy, and all such transactions shall apply with applicable law.
>
> 4. PECO EDC shall simultaneously make available to all EGSs any market information, not in the public domain, that it provides to a PECO Supplier.
>
> 5. Employees of PECO EDC who have responsibility for operating the distribution system, such as receiving requests for power, purchasing power, scheduling delivery, or billing and metering, shall not be shared with a PECO Supplier, and their offices shall be physically separated from the office(s) used by those working for the PECO

Supplier. Such employees of PECO EDC may transfer to a PECO Supplier provided such transfer is not used as a means to circumvent this Interim Code of Conduct. Any PECO Supplier shall have its own direct line management. Any shared facilities shall be fully and transparently allocated between the PECO EDC function and the PECO Supplier function. PECO EDC accounts and records shall be maintained such that the costs a PECO Supplier incurs may be clearly identified.

6. PECO EDC shall not condition the provision of any PaPUC jurisdictional regulated services on the purchase of power from a PECO Supplier.

7. Neither PECO EDC nor a PECO Supplier may directly or by implication falsely and unfairly represent:

- that the PaPUC jurisdictional regulated services provided by PECO EDC are of a superior quality when power is purchased from a PECO Supplier; or
- that the merchant services (for power) are being provided by PECO EDC rather than a PECO Supplier;
- that the power purchased from an EGS that is not a PECO Supplier may not be reliably delivered;
- that power must be purchased from a PECO Supplier to receive PECO EDC PaPUC jurisdictional regulated services.

7b. PECO EDC shall not jointly market or jointly package its PaPUC jurisdictional regulated services with the services of PECO's Suppliers unless it offers the same promotion of services to non-affiliated Suppliers.

8. PECO EDC shall establish and file with the Commission a dispute resolution procedure to address complaints alleging violations of these rules.

Enron M.B. at 37-39.

Enron acknowledges that the Commission's February 5, 1998 Compliance Filing Order did not include the underlined portion of Rule 7 above. However, the PECO Compliance Filing Order did reaffirm that Rule 7 must be interpreted to preclude the EDC from promoting "its competitive affiliate any differently than non-affiliated suppliers."[203] Of course, such an interpretation precludes any joint marketing or joint packaging of services between the EDC and its affiliated suppliers unless the same opportunity is provided to non-affiliated suppliers. While Enron accepts and strongly supports the Commission's declaration of its intended interpretation of Rule 7, it appears preferable to clarify the rule through the additional proposed language to avoid future disagreement. Id. at 39.

Second, the PECO interim rule does not include a prohibition against the use of the name of the EDC – a crucial protection against anti-competitive activity. Id.

While Enron endorses use of the language in the PECO Code of Conduct as outlined above, if the Commission chooses to work from the language of Duquesne's proposed Code, it must first make a number of revisions to bring it up to the level of PECO's original proposal, even prior to being able to impose the modifications subsequently made by the Commission in the PECO restructuring. Summarily, the required changes just to make the Duquesne code compliant with PECO's initial position are as follows:

1) Duquesne's proposed Code contains no prohibition on preferential treatment between affiliated and non-affiliated suppliers. PECO Rule 1.[204]

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[203] PECO Compliance Filing Order at 45-46.

[204] All comparisons with PECO's proposed code of conduct refer to PECO St. No. 15, Exh. GAC-2, which is the PECO proposed code which the Commission modified and clarified. See, PECO Energy at 129.

2) Duquesne's proposed Code does not require all tariffed services to be offered in the same manner to affiliates and non-affiliates, but only prohibits "undue discrimination." PECO Rule 2.

3) Duquesne's proposed Code does not include any prohibition on anti-competitive pricing. PECO Rule 3.

4) Duquesne's Code does not require it to make confidential market information available simultaneously to all suppliers but merely to make such information available to non-affiliated suppliers "upon request."[205] PECO Rule 4.

5) Duquesne's proposed Code does not require physical separation of employees, and does not require segregated accounts and records or allocation of shared facilities. PECO Rule 5.

6) Duquesne's proposed Code contains no provision which prohibits the tying of regulated and unregulated services. PECO Rule 6.

7) Duquesne's proposed Code contains no provision which limits the use of the EDC brand name. PECO Rule 7.

Enron M.B. at 40-41.

In addressing the further modifications and clarifications required by the Commission, first the Commission further mandated that affiliate or divisional transactions "for all goods and services, including power, must not involve any anti-competitive cross-subsidy."[206] Second, the Commission barred an EDC from making available any goods and services to its supplier affiliate unless those goods and services are also made available to other suppliers on comparable terms and conditions. Such provisions appropriately preclude EDC promotion of

[205] Of course, non-affiliated suppliers will have no way of knowing what confidential information has been made available to affiliates in order to request such information from Duquesne.

[206] PECO Energy at 130 (emphasis supplied).

its competitive business affiliate's efforts. Duquesne's proposed Code does not include such a prohibition on cross-subsidization. Id. at 41.

Third, all EDC functions were required to be separately staffed from all competitive supplier functions, including management responsibility, and all employee transfers are made subject to functional separation requirements.[207] While Duquesne has included rules on "Separation of Functions" and "Officers and Directors" in its proposed Code, the provisions are not broad enough to comply with the Commission's standard in that they do not contain appropriate restrictions on employee transfers, and do not apply at all to the individuals having management responsibility over such employees. Id.

Fourth, the Commission additionally required that comparable treatment be provided to both affiliated and non-affiliated suppliers and supplier customers for all customer goods and services.[208] The nondiscrimination provision in Duquesne's proposed Code of Conduct only prohibits "preferential treatment" of affiliated suppliers and "undue discrimination" against customers. This provision should be modified to clarify that, if necessary, positive efforts must be made in order to provide comparable treatment. Overall, the Commission established the general standard that the EDC must "treat all competitive suppliers in a comparable non-discriminatory manner with similar terms, conditions and access to information, goods and services."[209] This Commission mandate provides for equal access, both

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[207] Id. at 130.

[208] Id. at 131.

[209] Id.

in terms of timing and method of disseminating information, for all information, not just certain types of information as Duquesne has proposed. Id. at41-42.

Fifth, the Commission went beyond the PECO proposal and prohibited the tying of the EDC service with any other goods or services both as a condition of the provision of service and as a condition on the availability of certain terms and conditions.[210] Duquesne's Code of Conduct is silent on this subject, and should be modified appropriately. Id. at 42.

Sixth, the Commission required a provision which bars the EDC from using its name or any other method to imply, directly or indirectly, that EDC service will be superior if an affiliate is subscribed to, that the reliability of service is inferior if a non-affiliate is subscribed to or that generation services are in fact being provided by the EDC. Duquesne has no comparable provision in its proposed code, which must be modified to achieve compliance. Id.

Finally, the Commission barred EDCs from promoting their competitive affiliate any differently than non-affiliated suppliers. Again, Duquesne's code does not address this, and must be modified accordingly. Id.

Clearly, to the extent the Commission considers adopting Duquesne's own proposed Code as the interim Code of Conduct to be applied to Duquesne, far reaching modifications are necessary to achieve compliance with the standards set forth in PECO Energy. The most efficient course for the Commission would be to order the implementation of the Code it ordered be implemented in the PECO proceeding (with the clarification and addition discussed

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[210] Id.

above). In that manner, the Commission can be assured that the same rules are applicable to similarly situated jurisdictional utilities. Id. at 43.

5. MAPSA's Position

MAPSA finds Duquesne has proposed a Code of Conduct in this proceeding, which would apply only if Duquesne offers unregulated services to customers within its own service territory. MAPSA St. 1 at 47. Duquesne further states that while it currently does not plan to compete in its service territory, those plans are not yet final. N.T. 493. Duquesne's proposal ignores the reality that much of the expense of doing business is the start-up, and that it is at the start-up that the opportunity for improper exchange of resources is greatest. MAPSA St. 1 at 47. Duquesne also proposes to limit the applicability of its Code of Conduct to affiliate transactions within its own service territory, although Duquesne presumably would not be required, under its proposal, to engage its Code of Conduct and protect ratepayers and competitors if it competes in the service territories of other utilities. MAPSA St. 1 at 47. Finally, MAPSA proposed an interim Code of Conduct that would apply until the Commission's final rules are implemented. MAPSA St. 1, Attachment II; MAPSA M.B. at 38.

Duquesne's Code of Conduct proposal should be rejected for at least two reasons, as pointed out by MAPSA's witness in this case. First, if there is even the most remote possibility that Duquesne might compete in its own service territory, it should be required to implement a Code of Conduct, before undertaking any activity precedent to engaging in that activity. The same should be true if Duquesne intends to compete outside of its territory, because many of the same cost-shifting and cross-subsidization concerns are implicated,

regardless of where the Company is competing. Duquesne's proposed code of conduct would allow Duquesne to continue to control the market in anti-competitive ways, and will hinder the ability of competitive suppliers to enter the market and compete thus preserving Duquesne's monopoly position in the market place and eliminating the possibility of cost savings for customers. One way to ensure that a nondiscriminatory structural and operational relationship is developed between Duquesne and competitive suppliers and between Duquesne and any affiliates, is to establish an interim Code of Conduct in this proceeding. In spite of the Commission's determination to treat the issue generically, at least an interim Code of Conduct must be established in this restructuring proceeding. A rulemaking, by its very nature is general, and not company-specific. While the rulemaking, which will take at least a year to compete, may set detailed guidelines, it will require specific filings to be made by each utility; those filings in all likelihood, will be subject to further adjudicatory proceedings, which may not be resolved until well into the first year of competition, even assuming that final rules are adopted by the end of 1998. Id. at 38-39.

MAPSA observes that Duquesne argues an appropriate Code of Conduct is a generic issue and it must not be resolved in this proceeding. Duquesne M.B. at 79. However, Duquesne's argument denies the practical reality that it is unlikely that a final rulemaking will be in place in time for the January 1, 1999 transition to competition. Duquesne's proposed Code of Conduct is wholly inadequate, as evidenced by the intervenors' testimony. Therefore, Duquesne's Code of Conduct proposal must be rejected and one of the intervenors' Codes of Conduct, (e.g., MAPSA St. 1, Attachment II) should be adopted as an interim Code, until final regulations are enacted. MAPSA R.B. at 12.

6. Recommendation

In PECO Energy, Slip Op. at 128-129, the Commission stated:

> The [d]eclaration of policy in Section 2802 directs this Commission to implement a transition to a competitive retail generation market in Pennsylvania. In particular, Section 2802(12) expresses the purpose of the Act as the creation of "direct access by retail customers to the competitive market for the generation of electricity." Section 2803 defines "Direct Access" required under the Act as "the right of electric generation suppliers and end-use customers to utilize and interconnect with the transmission and distribution system on a non-discriminatory basis at rates, terms, and conditions of service comparable to the transmission and distribution company's own use of the system to transport electricity from any generator of electricity to any end-use customer." The declaration of policy at 2802(13) requires that the "procedures established under this chapter provide for a fair and orderly transition."
>
> Thus, the Commission must ensure in this decision that the competitive market will be permitted to operate fairly in a way that fulfills the statutory directives. In order to do so, it is appropriate to adopt certain competitive safeguards.

As in the present case, the EDC in PECO Energy proposed a Code of Conduct that would be in effect until such time as the Commission adopts regulations establishing a permanent Code of Conduct. The Commission is in the process of adopting regulations concerning competitive safeguards in Docket L-0097 and Customer Supplier Interaction at Docket No. M-00960890F0011. Until those regulations are formulated, an interim Code of Conduct must be established in this proceeding. Id. at 129. In PECO Energy, the Commission accepted the EDC's proposed Code of Conduct with certain modifications. Id.

To bring Duquesne's proposed Code of Conduct within the parameters established in PECO Energy, the Commission should direct the Company to modify it in the following respects:

1) Duquesne's interim Code of Conduct must prohibit preferential treatment between affiliated and non-affiliated suppliers.

2) Duquesne's interim Code of Conduct must require all tariffed services to be offered in the same manner to affiliates and non-affiliates alike.

3) Duquesne's interim Code of Conduct must include a prohibition on anti-competitive pricing.

4) Duquesne's interim Code of Conduct must require it to make confidential market information available simultaneously to all suppliers, affiliated and non-affiliated alike.

5) Duquesne's interim Code of Conduct must require physical separation of employees, and must require segregated accounts and records or allocation of shared facilities.

6) Duquesne's interim Code of Conduct must prohibit the tying of regulated and unregulated services.

7) Duquesne's interim Code of Conduct must preclude the EDC from promoting "its competitive affiliate any differently than non-affiliated suppliers."

B. Pro Forma Tariffs

1. Duquesne's Proposal

The Company suggests this section relates to another proposal by Enron that should be addressed by the Commission on a generic basis, not in this case. The proposal is for a new "Pro Forma Electric Generation Supplier Tariff." Enron Exh. LRC-2. As its title indicates, the Tariff bears no relation to the particular circumstances of Duquesne and thus, not surprisingly, many of Mr. Cole's assertions regarding the "inadequacies" of Duquesne's direct access proposal ignore the specifics of that proposal. In any event, the issue is generic and need not be resolved here. Duquesne St. 7-R at 1-4; Duquesne M.B. at 79.

2. Enron's Position

(a) Supplier Tariff

Enron has presented a Pro Forma Electric Generation Supplier Tariff, which it intends to define suppliers' jurisdiction and responsibilities in relation to meeting customers' loads and all necessary involvement with the EDC.[211] This tariff should be adopted by the Commission for all Pennsylvania utilities. Such a measure will appropriately protect reliability. Enron M.B. at 43.

Finally, and perhaps most important, the pro forma supplier tariff will establish a clear and enforceable set of rules and procedures to govern the multifaceted relationship between Duquesne and suppliers seeking to deliver power to customers using Duquesne's distribution system. The Commission endorsed the need for a supplier tariff in its Compliance Order in the PECO restructuring proceeding.[212] The Commission's Order succinctly stated the required filing:

> We [previously had] required the filing of a Supplier Services Tariff as a means to establish the basic requirements for EGS/EDS interactions in a standard format through a standardized consistent process. This would provide specific useful information to all current and future market participants concerning protocols and other requirements.
>
> PECO is directed to file an appropriate Supplier Services Tariff which delineates supplier obligations, provides definitions of terms, fully discloses the Company's EGS "Policies and Procedures" and specifies its procedures for customer sign-ups, switching, balancing, billing and data exchange. The tariff should

[211] Enron St. 5, Exh. 5, LRC-2.

[212] PECO Compliance Filing Order at 38.

be consistent with applicable PJM and FERC requirements and Commission Orders.[213]

Duquesne's response to the Enron call for the filing of a Supplier Services Tariff – now a PUC requirement – was to claim that such a tariff was "unnecessary," because many of the provisions are covered and controlled by Duquesne's FERC approved Open Access Tariff.[214] But Duquesne's position is clearly overstated. While general topics suggested in the Enron Supplier Tariff may be contained in FERC-filed tariffs, many others having to do specifically with retail distribution service, are not. In any event, suppliers would benefit by a comprehensive listing of functions, services, and procedures, to the extent that Duquesne's FERC tariff does not provide such rules and services. Moreover, the Commission has made clear that the Supplier Tariff should contain provisions on "customer switching," "billing" and "data exchange" – issues that are not included in Duquesne's FERC tariff. Enron M.B. at 43-44.

In this regard, Enron witness Coles detailed several specific issues and services which, if they are not covered by FERC-jurisdictional tariffs, must be included in a reasonable manner in Duquesne's PUC-approved Supplier Tariff. These issues include:

- Supplier obligation, energy balancing and load reconciliation.

To ensure reliable electric service to ultimate end-users there must be a clear, detailed understanding among all suppliers as to their obligations and balancing and reconciliation methods. This relationship must be detailed in advance of the implementation of

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[213] Id.

[214] Duquesne St. 7-R at 1-2.

retail access to enable suppliers to know how the system will work, to ensure a level playing field in retail access and to ensure that a particular competitive player is not given a market advantage. Enron's Pro Forma Supplier Tariff presents specific procedures for determining each supplier's load obligations. Id. at 45.

- Energy Imbalance Service

Enron's Pro Forma Supplier Tariff provides a mechanism to handle energy imbalance service. Suppliers need a system to be in place which will determine a load aggregator's hourly responsibility for supply delivery to meet the needs of customers and a means of balancing supplies and actual loads. FERC has explicitly provided for energy imbalance services for wholesale and state-authorized retail transactions as part of Open Access transmission tariffs. These arrangements provide the foundation for energy imbalance service to suppliers and customers under Pennsylvania's retail access[215] and should be utilized as much as possible. For situations not covered by the FERC tariff such as customers with monthly metering, a load-estimating method and settlement mechanism implemented in conjunction with the EDC should be used, similar to that proposed by Enron, whereby the EDC would use actual monthly metered loads to calculate and prorate the estimated difference between delivered amounts and estimated actual loads in terms of on-peak and off-peak energy. Each supplier could seek to trade mismatches with other suppliers.[216] These procedures are included in Enron's proposed Supplier Tariff and should be adopted as presented there.[217] Id. at 45-46.

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[215] Enron St. 5.0 at 10-12.

[216] Id. at 11.

[217] Enron St. 5, Exh. 5, LRC-2, Rule 4.2.

- Supply Planning and Planning Reserves

Enron witness Coles has set forth a series of important factors that should be considered by the Company and the Commission in the process of conducting supply planning and accounting for planning reserves.[218] The Commission should direct that Duquesne include consideration of these factors and goals in all future planning. Id. at 46.

b. Conclusion

The Commission should direct that Duquesne file a supplier tariff consistent with that proposed by Enron witness Coles, the PECO Compliance Filing Order, and Duquesne's FERC tariff and any applicable ECAR requirements, and to incorporate witness Coles' recommendations with respect to supply planning and planning reserve in its future decisions. Enron M.B. at 46.

3. Recommendation

For the reasons cited by the Company, the issue of a Pro Forma Electric Generation Supplier Tariff is better suited for a generic proceeding.

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[218] Enron St. 5.0 at 15-21.

XI. Duty to Serve

A. Service to Returning Customers

1. Duquesne's Proposal

The Company proposes that customers returning to "rate cap" service must remain with Duquesne for 12 months thereafter to address certain "gaming" opportunities. Duquesne St. 5 at 69-70. The proposal will protect Duquesne against customers leaving the system during low cost periods and returning to rate cap service during high cost periods (e.g., the summer peak period). Id. The OCA objects to this requirement as "discouraging participation in the competitive market," OCA St. 5 at 52, yet offers no real alternative. The OCA suggests that Duquesne could charge an unspecified "fee," whenever a customer switches "more than twice in any twelve month period." Id. This proposal has several problems. First, it has an arbitrary limitation on the number of switches; it takes only one switch per year to avoid purchasing from the market during the peak (i.e., expensive) summer months. Second, the OCA fails to specify a fee that could adequately compensate Duquesne for the resulting harm (and we question whether any "set" fee would be workable, given the significant price fluctuations that occur during these months).[219] Its proposal should, therefore, be rejected. Duquesne M.B. at 80-81.

[219] OCA also suggests that Duquesne's rate redesign proposal, which the OCA opposes, adequately addresses this concern. OCA St. 5 at 52. This characterization is untrue and elevates "bootstrapping" to a new level - claiming that one proposal opposed by the OCA supports the rejection of another proposal opposed by the OCA. The claim, if taken seriously, simply reflects the OCA's failure to recognize that the rate cap imposes real risks on Duquesne that cannot be so cavalierly disregarded. Duquesne St. 1-R at 21-23.

2. The OCA's Position

As the competitive market develops, the OCA suggests a customer, who has been "phased-in" and who has chosen to select an alternate energy supplier, may want or need to return to Duquesne for generation service. The OCA submits the provisions of Chapter 56 will continue to apply to this customer, and the §2804 rate caps will still apply. OCA St. 5 at 49-51. However, Duquesne has also proposed that a customer, who returns to Duquesne, must remain on the Company's system for a minimum 12-month period. OCA M.B. at 71.

OCA witness Alexander explains that there may be a number of reasons that a customer returns to Duquesne, and the 12-month requirement will serve to "discourage customers from freely entering the competitive market." OCA St. 5 at 52. Ms. Alexander submits that, "the Company's concerns about gaming will be met by its proposal to price this service closer to market prices (subject to the rate caps discussed above) or by imposing an appropriate fee when the customer makes use of this service more than twice in any 12-month period." OCA St. 5 at 52. As such, the OCA submits that the Company's proposal is overly broad and restrictive and should not be adopted. OCA M.B. at 71-72.

The OCA notes Duquesne submits this proposal to address the Company's "gaming" concerns. Duquesne M.B. at 80. The Company criticizes OCA witness Alexander's proposal to impose a fee on anyone who switches more than twice in a given year, and complains that the OCA failed to specify what fee should be charged. Id.; OCA R.B. at 26.

The OCA submits the Company's arguments should be rejected. In short, the OCA submits the Company's requirement that a customer returning to rate cap service remain with Duquesne for 12 months is unduly restrictive. As OCA witness Alexander stated, there

are many reasons that Duquesne customers may need to return to generation service that have nothing to do with an attempt to game the system. OCA St. 5 at 51-52. Moreover, such restrictions may hinder the development of the competitive market. Thus, the OCA submits this requirement has not been shown to be necessary at this time. OCA R.B. at 26-27.

3. DII's Position

DII posits the Commission must not eliminate the statutory right of all customers to return to service from Duquesne at the capped rate levels specified in the Act during the transition period. 66 Pa. C.S. §2804(4)(i) & (ii). As DII explains, supra, the rate cap is a necessary consumer protection that must not be impinged. DII M.B. at 43-44 & 75; DII R.B. at 46.

4. Enron's Position

During the early years of direct access, Enron asserts service to returning customers[220] must be offered by an EDC under regulated, tariffed rates. This was the holding in PECO Energy.[221] In its Order on Reconsideration in that case the Commission stated:[222]

> PECO, as an EDC, remains a regulated utility and may only offer Commission-approved, tariffed rates. . . . Protected by the statutory rate caps, customers who do not shop remain regulated rate customers of PECO on the same terms and conditions of services unless changed by the Commission Order. . . . [T]he

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[220] Returning customers are eligible for direct access and choose a competitive supplier and then, for any reason, return to the EDC for electric supply.

[221] PECO Energy at 133-34.

[222] PECO Reconsideration Order at 21.

> "shopping" credit is not relevant to a customer who does not shop. Customers who do not shop pay the approved tariff rate divided into unbundled generation, transmission, and distribution charges.

This status will exist until the Commission promulgates regulations under §2807(e)(2) at the end of the transition period. After transition, the rules under which service to returning customers must be provided will be governed by 66 Pa. C.S. §2807(e)(3), which states:

> If a customer contracts for electric energy and it is not delivered or if a customer does not choose an alternative electric generation supplier, the electric distribution company or commission-approved alternative supplier shall acquire electric energy at prevailing market prices to serve that customer and shall recover fully all reasonable costs.

Enron M.B. at 47.

While the Commission has stated it will consider and implement 66 Pa. C.S. §2807(e)(3) by regulations at a later date,[223] and though Duquesne's view on this provision is not clear, Enron believes it is important to consider that issue now as the Commission plans for the future. Consistent with the effect of its holding in the PECO restructuring with respect to the transition period, it is imperative that the Commission apply §2807(e)(3) in a manner that will not thwart electric competition after the phase-in period is over. Enron M.B. at 47-48.

Although the Act does not define the phrases "prevailing market prices" and rates that "recover fully all reasonable costs" under §2807(e)(3), that rate should be interpreted to be the same as the generation credit determined by the Commission. Conversely, generation credits should be designed to represent reasonable approximations of the projected delivered market prices for energy, including an allowance for retail costs, and are thus surrogates for the market

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[223] PECO Energy at 134.

price "plus" standard. Accordingly, they should be rates which reflect the same as "prevailing market prices" which "recover fully all reasonable costs." Establishing the generation credit as both the "cap" and the "floor" price payable by returning customers after transition will promote competition by providing an incentive to such customers to leave default service if the actual market price falls below the applicable generation credit by choosing competitive suppliers that offer lower prices. It will also provide customers with the benefit of significant rate reductions prior to the time that they may choose an alternative supplier.[224] Enron M.B. at 48.

5. Recommendation

No evidence exists in this record to suggest a problem will arise with returning customers engaging in "gaming" to the detriment of Duquesne. A 12-month "stay-in" provision appears, on its face, to be a serious impediment to competition. Therefore, the Commission should deny the Company's proposal until it can satisfactorily demonstrate that a serious problem exists.

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[224] Contrary to some arguments, establishing the rate applicable to default customers as the residual generation credit does not mean that these rates cannot decrease. If Duquesne wishes it can file a Public Utility Code Chapter 13 tariff filing to reduce its rates to reflect reductions in its costs of providing default service. In the alternative, the Commission could order that the "default" rate be established annually after review and approval by the Commission, and be set at the determined generation market price, plus all delivery and generation related A&G and retail sales costs. This would assure that the EDC, would not be able to "flex down" in an anti-competitive manner and would allow EGSs to determine, for a period that allows proper planning, the generation cap and "prevailing market price" levels they need to "beat" in order to provide savings to consumers.

B. Provider of Last Resort

1. Duquesne's Position

Duquesne observes the Environmentalists have proposed the same "Better Choice Plan" that was rejected in PECO Energy, Slip Op. at 135. The Commisssion should decline to adopt it here. Duquesne M.B. at 81.

2. The OCA's Position

Even as the market develops, the OCA finds there will be customers who choose not to shop, are unable to find an alternative provider to serve them, or who may return to Duquesne for service for a variety of reasons. Duquesne has, by statute, the "full obligation to serve" these provider of last resort ("POLR") customers, at least during the CTC or ITC collection period or until 100% of customers have choice, whichever is longer, unless an alternative supplier is approved by the Commission to provide this service. 66 Pa. C.S. §2807(e)(1). By the end of the phase-in period, the Act requires the Commission to develop regulations to govern the POLR service. 66 Pa. C.S. §2807(e)(2). In its restructuring filing, Duquesne proposed to provide this service by pricing the power supply portion of its unbundled bill based on prices obtained from a competitive RFP process. OCA St. 5 at 51. Although Duquesne has made this proposal to explore competitive solicitation, the OCA submits that more detail is required before this proposal is adopted. OCA St. 5 at 51. Therefore, the OCA recommends that the Commission refrain from adopting Duquesne's proposal at this time. This should be considered as part of the regulatory process that will determine how to set "prevailing

market prices" for Duquesne or an alternative POLR pursuant to §§2807(e)(2) and (3). OCA M.B. at 72.

(a) **Better Choice Plan**

The OCA notes the Environmentalists presented the Better Choice Plan to address issues concerning the creation of a more diverse market. Env. M.B. at 35-41. The OCA addressed its concerns with the Environmentalists' Better Choice Plan, supra, OCA M.B. at 6. While the OCA recognizes the issues addressed by the Environmentalists through the proposal, the OCA agrees with the Commission's decision in PECO Energy and submits it is more appropriate to revisit this plan, when the Commission addresses the issues regarding the provision of service in regulations pursuant to §2807(e)(2) and (3). OCA R.B. at 27.

(b) **POLR Generation Rates**

The OCA also finds Enron recommends that the Commission consider now how it will effectuate the requirements of §2807(e)(3) of the Act (requiring that the POLR provide electric service at the "prevailing market prices"). Enron M.B. at 48. Enron suggests the Commission should order that the "prevailing market price . . . " is equivalent to the generation credit set in this proceeding. Id. According to Enron, setting the market price for POLR service at the generation credit level will create an incentive for POLR customers to "shop" for a better deal. Id.; OCA R.B. at 27-28.

The OCA submits Enron's proposal is both premature and inconsistent with the Act. First, the Act requires the Commission to issue regulations regarding POLR service, and

the Commission has already determined that it will decide these issues via a rulemaking. PECO Energy, Slip Op. at 135. Second, Enron's argument ignores the possibility that a POLR customer simply may not be able to "shop." When competition arrives, there will be some customers that marketers may be unwilling to serve. Enron's "incentive" will deny these customers any rate savings from this move to competition. Third, Enron's argument that if Duquesne would like to offer POLR customers a rate reduction it can make a Chapter 13 filing or the Commission can set the rate "annually after review and approval by the Commission" is untenable and inconsistent with the Act's direction to move away from the regulation of generation. 66 Pa. C.S. §2802(14). Fourth, the plain language of the statute states that POLR service will be provided at "prevailing market price." As Enron must recognize, the generation credit, set by the method it proposes, may bear no relationship to a "prevailing market price" in the future. In short, the OCA opposes Enron's position on this issue and urges the Commission to reject it as well. OCA R.B. at 28.

3. The Environmentalists' Position

The Environmentalists posit a just and reasonable set of unbundled rates is an essential condition to creating a robust competitive market, but an adequate generation credit alone is not enough to ensure all customers have meaningful choices of electricity suppliers and services. The Commission must also address the problem of market domination by Duquesne by virtue of its status as the monopoly supplier in this region for the last century. As Environmentalists' witness Bruce Biewald testified,

> A great many of Duquesne's electricity customers are unlikely to make any choice at all regarding their electricity supplier. . . . If

> the Company is designated the default supplier of these customers, then it will be granted a significant market share without incurring the marketing and transaction costs that would be required of competitive utilities. This formidable advantage would add to the numerous tangible and intangible competitive advantages that are typically enjoyed by incumbent utilities.[225]

To address the problem of market domination by Duquesne, the Environmentalists proposed a system for allocating non-choosing customers to alternative suppliers serving Duquesne's service territory. They call this the Better Choice Plan.[226] Env. M.B. at 35-36.

Before reviewing the specifics of this proposal, it is important to understand the distinction between the concepts of "provider of last resort" and "default supplier." The provider of last resort is the "entity that is assigned the responsibility of ensuring that all electricity customers will have access to a reliable supply of electricity at reasonable prices, terms and conditions."[227] The provider of last resort is required to serve customers who, for a variety of reasons, cannot obtain generation services from any alternative supplier. The Act makes the electric distribution company the provider of last resort[228] and provides a funding mechanism to cover the cost of those services for those unable to pay.[229] The Environmentalists recommend that Duquesne be the provider of last resort. Id. at 36-37.

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[225] Env. St. 2.0 at 9.

[226] The genesis of the Better Choice Plan was the experience in the long distance telephone industry, where the Federal Communications Commission in 1985 sought to end the market domination of AT&T and encourage meaningful competition by setting up a market allocation pool of other carriers to provide long distance service to customers who failed to select a carrier.

[227] Env. St. 2.0 at 56.

[228] 66 Pa. C.S. §2807(e).

[229] 66 Pa. C.S. §2804(8) and (9).

The Better Choice Plan introduces the concept of a "default supplier," which is very different from the provider of last resort. The default supplier is the supplier that serves the default customers, or those customers who are eligible to choose an alternative generation supplier but have failed to do so. Under the Environmentalists' Better Choice Plan, a more diverse market is created because the alternative suppliers active in the market can volunteer to become part of the default supplier group which will serve the customers who fail to choose. Id. at 37.

Before describing the mechanics of the proposal, two other concepts must be addressed - the default customer and the default supplier group. Id.

(a) The Default Customer - The Failure to Choose

It is widely acknowledged that when an industry moves from a regulated monopoly to an open market, many customers stay with the monopoly supplier. Some argue that these customers are "choosing not to choose" and that it is inappropriate to interfere in this "choice." But Environmentalists' witness Roger Colton showed the error in this argument:

> Consumer choice implies that given an opportunity, a consumer will use his or her knowledge of available alternatives to translate wants into satisfaction.
>
> In fact, however, considerable consumer research finds that there is no conscious exercise of discretion in the failure of consumers to choose an alternative supplier of service when an industry moves from a regulated monopoly to a competitive model. Indeed, "staying put" is the antithesis of exercising discretion. It is the failure to choose.[230]

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[230] Env. St. 3.0 at 2.

Mr. Colton suggested three reasons why many customers fail to choose and noted that the Better Choice Plan promoted competition by helping customers overcome all three barriers:

> In each case, jump-starting the competitive electric market will help address the factors that led to the consumer paralysis in decision-making. Allocating the non-choosing consumers among alternative suppliers will help generate consumer experience that will overcome confusion and skepticism. Allocating consumers among alternative suppliers will help generate experience in seeking out and understanding information. Allocating consumers will help overcome the simple consumer inertia that leads to a consumer failure to act.[231]

Mr. Colton testified that a transitional market mechanism such as the Better Choice Plan was an appropriate and helpful response to these temporary customer difficulties. Id. at 37-39.

(b) **The Default Supplier Group**

Under the Environmentalists' Better Choice Plan, suppliers can volunteer to participate in the default supplier group if they agree to seven conditions. These conditions are designed to protect the customers and to advance some important public interest goals. This *quid pro quo* is fair and appropriate because participation in the group is entirely voluntary and the participating suppliers receive from the Commission the private benefit of an allocation of default customers without incurring the costs and effort to recruit these customers. Id. at 39.[232]

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[231] Env. St. 3.0 at 3.

[232] The Environmentalists state their Recommended Public Interest Standards for Participation in the Default Supplier Group at Env. M.B. at 39.

(c) Allocating Default Customers

The Environmentalists' Better Choice Plan begins with customers selecting their generation suppliers, just as they would under the Act and the other proposals.[233] At no time does the Better Choice Plan interfere with any election by any customer to be served by a particular supplier. A customer will always be able to select a particular supplier and that selection will prevail. A reasonable time following the expansion of eligibility to each new group of customers, the results of the selection process will be published and evaluated to determine Duquesne's share of the customers. Id. at 40.

For purposes of measuring Duquesne's market share, the Duquesne share would be defined to include (i) the customers who had made an affirmative selection of Duquesne, (ii) the customers who had made an affirmative selection of one of Duquesne's affiliated generation suppliers,[234] and (iii) the default customers (i.e., those who failed to make any selection at all). If the Duquesne share is less than 50%, nothing further would happen under the Better Choice Plan. The 50% figure is used as a threshold to identify the point at which Duquesne's market share threatens the health of the competitive market. If that share is less than 50%, then the remedy of the Better Choice Plan is unneeded. If the Duquesne share is 50% or more, then the Better Choice Plan's allocation mechanism would be triggered. Id.

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[233] The mechanics of the Better Choice Plan are discussed in Env. St. 2.0 at 44-49.

[234] Because of the competitive advantage a supplier affiliated with Duquesne would have over other competitors (simply because of the affiliation), the Environmentalists suggest that for purposes of the market share determination, the customers of a Duquesne affiliate be considered Duquesne customers. These affiliates would not be eligible to participate in the default supplier pool.

When the Duquesne share is 50% or more, the Better Choice Plan would allocate all default customers to be served by the default supplier group. The default customers would be allocated on a random basis between the suppliers in the default supplier group in proportion to the market share of each member supplier. Id. at 41.

The Environmentalists acknowledge that implementation of the Better Choice Plan is possible only after additional work to address some of the unresolved issues, but the Commission should include it in the final Order to prevent the serious threat of market domination by the monopoly provider which would be fatal to the emergence of a competitive market. Id.

(d) Provider of Last Resort

The Act requires each EDC to acquire electric energy at prevailing market prices to serve customers who do not obtain generation from another electric supplier.[235] The Commission's Universal Service Guidelines require that the restructuring plans propose an initial supplier of last resort and address how it will be utilized.[236] Id. at 51.

Duquesne's plan states that it "will fill this role by default," but the plan fails to describe how the "prevailing market rates" for this power will be determined and passed on to customers.[237] This is an important issue, since it is likely that many low-income customers will, for a variety of reasons, be unable to obtain their power from an EGS and instead will be in

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[235] 66 Pa. C.S. §2807(e)(3).

[236] Final Order Re: Guidelines for Universal Service and Energy Conservation Programs (Order entered July 11, 1998), Docket No. M-00960890F0010, Section B(2)(a) at 30.

[237] Duquesne St. 14-R, Exh. JPF-1 at 4.

effect captive customers of Duquesne. For this reason, the universal service plan needs to address a fair and effective mechanism for obtaining power and charging market rates for it. Id. at 51.

4. Enron's Position

Enron suggests the OCA presents somewhat conflicting views of the approach that should be used to establish the rates applicable to "Provider of Last Resort" customers. As OCA notes, these include customers who: (i) choose not to shop; (ii) cannot find a supplier (presumably including those who legally are not yet permitted to shop); and (iii) those who may return to Duquesne for service for various reasons.[238] As OCA states in its "Provider of Last Resort" discussion, the rates for such customers - which include all but pilot customers prior to January 1, 1999 - should be established in accordance with procedures that the Commission establish in a "POLR" rulemaking.[239] Enron agrees with this approach, but would note that the rulemaking-derived generation rates that would have to be established pursuant to the Act, would not reflect simply some derived market price for generation as OCA implies.[240] The Act requires that POLR customers (which as noted above would include customers who legally cannot choose) would be charged either Duquesne's generation charge or a rate that reflects prevailing rates for power but which recovers all associated costs.[241] That rate may well be

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[238] OCA M.B. at 72.

[239] Id.

[240] OCA M.B. at 57-58, 62.

[241] Enron M.B. at 48.

Duquesne's present generation credit, since presumably that rate was established to recovery Duquesne's price for power (its prevailing market prices) plus all reasonable associated costs.[242] At any rate, as the OCA has agreed here, the determination of precisely what rate is applicable to such customers should be made in the context of the contemplated rulemaking. Enron R.B. at 21-22.

5. Recommendation

In PECO Energy, Slip Op. at 135, the Commission expressed doubt whether the Environmentalists' Better Choice Plan assignment of customers to suppliers is permissible under the Act. Accordingly, the Commission stated its preference to consider this option when it promulgates regulations required by Sections 2808(e)(2) & (3). Nothing in this record should convince the Commission to reconsider that decision. As to the second issue raised here concerning the provider of last resort providing electric service at "prevailing market prices," all parties apparently now agree this matter should await the proposed POLR rulemaking.

C. Electric Transmission and Distribution Service

1. Unbundling Other Customer Services

(a) Introduction

(i) Duquesne's Position

Duquesne suggests the issues addressed in this section (the unbundling of "revenue cycle services") are principally matters of generic policy that the Commission should decide on

[242] Id.

a fair and consistent basis for all EDCs and suppliers in the Commonwealth in a generic proceeding. Duquesne St. 8 at 3; Duquesne St. 8-R at 3-4. This also is consistent with PECO Energy, where the Commission held it "not appropriate or necessary" to require PECO to unbundle revenue cycle services in that proceeding. PECO Energy, Slip Op. at 138. While there is thus no requirement to address these matters in detail (Fifth Prehearing Order at 3), Duquesne will discuss each briefly. Duquesne M.B. at 81-82.

(ii) The OTS' Position

The OTS explains rate unbundling is the breaking down of a total rate into its cost components. Specifically, a distribution rate will have costs components consisting of metering, billing, universal service and service drop lines. According to 66 Pa. C.S. §2806(e), an electric distribution utility is required to unbundle its distribution rate. Thus the law requires Duquesne in this case, to submit unbundled prices for generation, jurisdictional transmission, distribution and other services. OTS St. 3 at 10; OTS M.B. at 81.

(iii) The OCA's Position

The OCA notes several parties to the restructuring proceeding have either supported further unbundling in billing and metering or argued that further exploration of these issues not be foreclosed by decisions in this proceeding. The OCA has made recommendations regarding metering, billing and other customer services to assure that options for competitive provision of these services are not foreclosed. The OCA sets forth its specific recommendations below. OCA M.B. at 72-73.

(iv) IBEW's Position

IBEW posits numerous provisions of the Public Utility Code and the Commission's regulations require that billing and metering for public utility services must be provided by a public utility. As a consequence, marketers must be prohibited from billing or metering public utility services. IBEW M.B. at 9.

Before discussing the specific legal restrictions, it is important to note that when IBEW uses the term "public utility services" it is referring only to the regulated transmission and distribution of electricity by Duquesne. That is, IBEW's position is that it is unlawful for anyone other than Duquesne to bill for and meter Duquesne's electricity distribution service. IBEW does not dispute the ability of non-utilities to provide their own bills solely for the supply of electricity or for other non-utility services. Id.

The legal analysis of this issue must begin with the definition of "public utility." As amended by the Competition Act, Section 102 of the Public Utility Code, 66 Pa. C.S. §102, excludes "electric generation supplier companies" from the definition of public utilities. The Act also defines "electric generation supplier" as "a person or corporation" that "sells to end-use customers electricity or related services utilizing the jurisdictional transmission or distribution facilities of an electric distribution company." 66 Pa. C.S. §2803. In contrast, that same Section defines an "electric distribution company" to be a "public utility" that provides "facilities for the jurisdictional transmission and distribution of electricity to retail customers." Id.

Thus, as a preliminary matter, jurisdictional transmission and distribution services must be provided to end-users of electricity by an electric distribution company. That electric distribution company, Duquesne in this case, must be a public utility. IBEW M.B. at 10.

The next step in this analysis is to determine whether billing and metering services are part of the "distribution services" that are provided by a public utility. Again, Section 102 of the Public Utility Code provides the answer. That Section of the Code defines "service" to include "any and all acts done, rendered, or performed, and any and all things furnished or supplied, and any and all facilities used, furnished, or supplied by public utilities . . . in the performance of their duties under this part to their patrons, employees, other public utilities, and the public. . . ." Further, Section 102 defines "facilities" to include "all plant and equipment of a public utility, including all tangible and intangible real and personal property without limitation, and any and all means and instrumentalities in any manner owned, operated, leased, licensed, used, controlled, furnished, or supplied for, by, or in connection with, the business of any public utility." It also should be noted that Commonwealth Court has held that the terms "service" and "facilities" as used in the Code are to be broadly construed. Country Place Waste Treatment Co., Inc., v. Pa. P.U.C., 654 A.2d 72, 76 (Pa. Commonwealth Ct. 1995); IBEW M.B. at 10.

Thus, when the Act speaks of "distribution services" that are provided by a public utility, that term is defined to include all acts performed and all property used by the distribution utility in serving its customers and the public. There is no question that the electric meter is property that is "used . . . or supplied by public utilities" in providing regulated electric distribution service to their customers. There also is no question that the rendering of a bill for

distributing electricity is an "act done" in providing regulated electric distribution service to the utility's customers. Id. at 10-11.

In other words, under the Public Utility Code, the metering and billing for the distribution of electricity are part of the provision of service by a public utility. As of this point in time, Duquesne is the only public utility that is authorized to provide electric distribution service within its service territory. Any marketer (or other entity) that desires to meter and bill for electric distribution service first must receive a certificate of public convenience and necessity to provide public utility service. 66 Pa. C.S. §1101; IBEW M.B. at 11.

This interpretation of the law is fully consistent with numerous other provisions in the Public Utility Code and in the Commission's regulations. The following provisions evidence a strong legislative intent that only a public utility should be permitted to bill for and meter utility services. The Commission's regulation of such billing and metering services is pervasive precisely because such services are essential to the provision of utility service. As IBEW explains in the following paragraphs, if such services are provided by marketers and other non-utilities, then the Commission would not have the statutory authority to regulate those services. Id.

Chapter 15 of the Public Utility Code (Service and Facilities) contains several provisions that require a public utility to bill for and meter utility services. Initially, Section 1504 gives the Commission the authority to regulate: "(2) . . . the measurement of quantity, quality, pressure, initial voltage or other condition pertaining to the supply of the <u>service</u> of any and all <u>public utilities</u>. (3) . . . the examination and testing of <u>such service</u>, and for the measurement thereof. (4) . . . the accuracy of all meters and appliances for

measurement. (5) . . . the examination and testing of any and all appliances used for the measurement of any service of any public utility." 66 Pa. C.S. §1504 (emphasis added). That is, the Commission's authority to regulate the metering of electricity, including the testing of meters, applies only to meters that are used to provide "service" by a "public utility." If the Commission were to permit non-utilities, such as marketers, to provide metering services, the Commission would have no authority to regulate the non-utilities' meters. IBEW M.B. at 11-12.

Section 1507 of the Code requires every "public utility, furnishing service upon meter" to maintain records of the meters' accuracy, as well as equipment "for testing and proving the accuracy of meters furnished by such public utility for use." Moreover, the Commission is required to approve and inspect these meter testing facilities. 66 Pa. C.S. §1507. Importantly, though, these testing and record-keeping requirements apply only to a "public utility" that furnishes "service." Once again, if the Commission desires to ensure that all electric meters are tested in a certified laboratory, the meters must be "furnished by" a "public utility." The Commission has no jurisdiction over measuring devices that are used by entities that are not public utilities. Id. At 12.

Similarly, Section 317 of the Code permits the Commission to restrict the amount that "public utilities" may charge "for the testing of their instruments of precision and measuring apparatus." 66 Pa. C.S. §317(b). Here again, the Commission cannot regulate the amount that is charged for testing a meter by any entity that is not a "public utility." IBEW M.B. at 12.

The Code contains several other provisions that empower the Commission to regulate the rendering of bills by "public utilities," but that does not apply if a non-utility were to render a bill for a utility service. Section 1509 of the Code sets forth restrictions on the

billing procedures that are used by "a public utility as defined in paragraph (1)(i), (ii), (vi), or (vii) of the definition of 'public utility' in section 102 . . . to its service customers . . . ." 66 Pa. C.S. §1509. For example, this Section contains requirements concerning the allowable time period for paying a utility bill and the way in which information must be displayed on the utility bill. However, these restrictions apply only to "public utilities" that are delineated in specified portions of the definition in Section 102 of the Code. As noted previously, marketers are specifically excluded from that definition. Thus, the Commission's statutory ability to regulate the content and payment period on a bill for electric distribution service exists only when the bill for such service is "rendered by a public utility." IBEW M.B. at 12-13.

Similarly, Subchapter B of Chapter 15, 66 Pa. C.S. §§1521-1533, sets forth billing, collection, and termination requirements that must be met for public utilities that supply service to leased, residential premises. However, these provisions are limited to "public utilities as defined in paragraph (1)(i) and (ii) of the definition of 'public utility' . . . ." 66 Pa. C.S. §1522(a). Thus, again, because marketers are not defined as public utilities, they are not subject to the statutory provisions regarding the discontinuance of utility service to leased premises. In order for these statutory provisions to apply to electric distribution service, the bill and meter for that service must be provided by a public utility. IBEW M.B. at 13.

All of these provisions of the Public Utility Code are designed to protect consumers and to ensure that a minimum level of regulated, utility service is provided within the Commonwealth. It is possible to implement these provisions only if a public utility is responsible for the electric meter and renders the bill for electric distribution service. Id.

In passing the Act, the General Assembly was aware of these restrictions when it permitted electric generation suppliers the right to bill for their own services and nothing more. In Section 2807(c), the Code provides: "Subject to the right of an end-use customer to choose to receive separate bills from its electric generation supplier, the electric distribution company may be responsible for billing customers for all electric services, consistent with the regulations of the commission, regardless of the identity of the provider of those services." 66 Pa. C.S. §2807(c) (emphasis added). That is, the statute does not permit electric generation suppliers to bill for all services; that right is reserved to the distribution utility. Instead, the generation supplier only has the ability to render a separate bill for the services that it provides and then only if the customer requests it. IBEW M.B. at 13-14.

Section 2807(c) then sets forth requirements for how the electric distribution utility must perform the billing for services provided by others. These provisions cover the form and content of the bill, the furnishing of data to the distribution utility, and the allocation of payments. 66 Pa. C.S. §§2807(c)(1) to 2807(c)(3). Importantly, the Code does ***not*** contain comparable provisions that define similar obligations for electric generation suppliers performing the same function. 66 Pa. C.S. §2809. The absence of a parallel obligation for generation suppliers provides further support for the conclusion that the statute does not permit anyone other than the distribution utility to bill for distribution services. IBEW M.B. at 14.

In addition, there is no doubt that distribution utilities are required to provide other services that are directly related to the billing function. Section 2807(d) states:

> The electric distribution company shall continue to provide customer service functions consistent with the regulations of the commission, including meter reading, complaint resolution and

collections. Customer services shall, at a minimum, be maintained at the same level of quality under retail competition.

66 Pa. C.S. §2807(d) (emphasis added). It is difficult to understand how it would be possible for the electric distribution utility to continue providing these services, unless it is also the entity that is billing for the services that it provides. This is particularly true for complaint resolution and collections, both of which are directly related to the actual bill that the customer receives. IBEW M.B. at 14.

Further, several important provisions in the Commission's regulations do not apply to electric generation suppliers. Under the Act, the only provisions of the Commission's regulations that are made directly applicable to generation suppliers are the "standards and billing practices" found in 52 Pa. Code Ch. 56. 66 Pa. C.S. §2809(b). It makes sense for these requirements to apply if the generation supplier is going to render a separate bill for service that it provides, as customers may request pursuant to 66 Pa. C.S. §2807(c). IBEW M.B. at 14-15.

However, the Act does not provide that the requirements in Chapters 57 and 58 of the Commission's regulations apply to generation suppliers. Specifically, these regulations contain the following requirements, among others, with which electric distribution utilities must comply:

- Limitations on the fees for meter testing, 52 Pa. Code §57.22;
- Procedures for adjusting bills for meter errors, 52 Pa. Code §57.24;
- Procedures for engaging in sales promotion practices, 52 Pa. Code §§57.61-57.67;
- Maintenance of customer records that enable the utility to implement a low-income usage reduction program, 52 Pa. Code Ch. 58.

Each of these requirements, among the many others that appear in Chapter 57, applies only to public utilities that provide electric distribution service. As noted previously, that term does not include marketers or other electric generation suppliers. Moreover, it would be extremely difficult, if not impossible, for electric distribution utilities to comply with many of these requirements if the electric distribution utility is not the entity that renders the bill to the customer, performs collection efforts, and is otherwise the primary contact point with the customer. IBEW M.B. at 15.

Furthermore, there is nothing in the Act that requires a different result. Numerous provisions of the Act state that the purpose of the Act is to provide for competition in the supply of electric generation to customers. For example:

> a. "Because of advances in electric generation technology and federal initiatives to encourage greater competition in the wholesale electric market, it is now in the public interest to permit retail customers to obtain direct access to a competitive generation market . . . ." 66 Pa. C.S. §2802(3) (emphasis added).
>
> b. "The purpose of this chapter is to modify existing legislation and regulations and to establish standards and procedures in order to create direct access by retail customers to the competitive market for the generation of electricity . . . ." 66 Pa. C.S. §2802(12) (emphasis added).
>
> c. "The procedures established under this chapter provide for a fair and orderly transition from the current regulated structure to a structure under which retail customers will have direct access to a competitive market for the generation and sale or purchase of electricity." 66 Pa. C.S. §2802(13) (emphasis added).
>
> d. "This chapter requires electric utilities to unbundle their rates and services and to provide open access over their transmission and distribution systems to allow competitive suppliers to generate and sell electricity directly to consumers in this Commonwealth. The generation of electricity will no longer be regulated as a public utility function except as otherwise

> provided for in this chapter." 66 Pa. C.S. §2802(14) (emphasis added).
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> e. "It is in the public interest for the transmission and distribution of electricity to continue to be regulated as a natural monopoly subject to the jurisdiction and active supervision of the commission." 66 Pa. C.S. §2802(16) (emphasis added).

That is, there is nothing in the Act, or anywhere else in the Public Utility Code, that authorizes any entity other than a public utility to furnish an electric meter or to render a bill for electric distribution service. On the contrary, there are numerous provisions in the law that require that only a public utility can provide such services for its customers. IBEW M.B. at 15-16.

In summary, it is unlawful for any entity other than Duquesne to provide a meter and render a bill for the electric distribution services that Duquesne provides. Id. at 16.

IBEW observes Enron leaves the impression that California already has competitive billing and metering for utility services, and that such competition is necessary in order to have a competitive market for electric generation. Enron M.B. at 55-56. In fact, though, California has only issued an order that permits such competition for residential and small commercial customers to begin in 1999. There is no experience in that state with the provision of billing and metering services to small customers by non-utilities. IBEW R.B. at 3.

Moreover, while California's order may be of some academic interest to the Commission, the Commission already has ruled on this issue and found that competitive billing and metering is not required in order for competition in electricity supply to occur. The Commission held in its PECO decision that it is not necessary to unbundle metering and billing in order to have a competitive generation market. See, IBEW M.B. at 19, citing PECO Energy, Slip Op. at 139; IBEW R.B. at 4.

Interestingly, the New York Public Service Commission has reached precisely the same conclusion. In Opinion and Order Establishing Regulatory Policies for Competitive Metering, In the Matter of Competitive Opportunities Regarding Electric Service, Case 94-E-0952, Opinion No. 97-13 (NY PSC Aug. 1, 1997), that commission concluded that "competitive metering is not a necessary precondition for the introduction of retail electric competition." Id., Slip Op. at 3. The New York commission, therefore, refused to allow anyone other than an electric utility to provide metering services to residential and small business customers. IBEW R.B. at 4.

Finally, IBEW notes Enron cites to this Commission's Customer Services Order. Final Order Re: Guidelines for Maintaining Customer Services at the Same Level of Quality Pursuant to 66 Pa. C.S. §2807(D), and Assuring Conformance with 52 Pa. Code Chapter 56 Pursuant to 66 Pa. C.S. §2809(E) and (F), Docket No. M-00960890 F. 0011 (Pa. PUC July 11, 1997). Enron M.B. at 59-60. In so doing, however, Enron cited to the Commission's Order of July 11, 1997, rather than to the Commission's Order in that same docket on August 21, 1997, Final Order Re: Guidelines for Maintaining Customer Services at the Same Level of Quality Pursuant to 66 Pa. C.S. §2807(D), and Assuring Conformance with 52 Pa. Code Chapter 56 Pursuant to 66 Pa. C.S. §2809(E) and (F)-Petition for Reconsideration, Clarification, Rescission, and Amendment of the International Brotherhood of Electrical Workers' Pennsylvania Utility Caucus, Docket No. M-00960890 F. 0011 (Pa. PUC Aug. 21, 1997). In its August 21st Order, the Commission acknowledged that IBEW's Petition for Reconsideration, Clarification, Rescission, and Amendment raised several legal issues that the Commission had not considered. As the Commission stated: "[W]e do recognize that all of the arguments

presented by IBEW have not been considered by the Commission in setting up these guidelines or in any other electric competition proceeding. Rather than being addressed here, we anticipated that metering and billing issues would be addressed in each restructuring case." Id. at 3-4; IBEW R.B. at 4-5.

The Commission then concluded its Reconsideration Order by stating that it intended only to direct the parties to "consider this guideline" in the restructuring cases, concluding that the July 11th Order "is not a final disposition on these issues." Id. at 5.

Consequently, the Commission's July 11th Order, on which Enron relies, is without legal significance. The Commission subsequently acknowledged that it had not considered all of the relevant legal issues and that it was merely asking the parties to do so in each restructuring case. That is precisely what IBEW has done in this case, where it has demonstrated that Enron's proposals would violate numerous provisions of the Public Utility Code. Id.

(v) <u>Enron's Position</u>

(1) <u>Competition In and Unbundling of Non-Wire Services</u>

Enron explains the provision of non-wire services[243] has nothing to do with the actual distribution of power and energy and is not part of a natural monopoly.[244] Accordingly, Enron submits that each of the non-wire services in Duquesne's service territory should be provided competitively in accordance with appropriate standards and protections to assure safety, reliability and consumer protection.[245] Enron M.B. at 49.

In addition, Duquesne's costs and prices for these services must be unbundled from Duquesne's charges for distribution-related services.[246] Permitting non-wire services to be provided competitively but allowing their costs to be bundled with Duquesne's distribution service, would require the customer to pay twice and actually limit access to the competitive

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[243] The term "non-wire services" specifically identifies the functions of providing a meter; obtaining meter and usage data and distributing the information to consumers, utilities and any other appropriate energy service providers; billing consumers for energy service costs; and providing related information/communication services to consumers in connection with their energy service. They are distinct from the provision of "wire" services (i.e., the transmission and distribution of electricity). They are sometimes referred to as "revenue cycle services." Enron St. 3.0 at 2-3.

[244] Enron St. 2.0 at 27.

[245] Enron St. 3.0 at 2. Enron provided extensive testimony on this issue. <u>See</u>, Enron St. 3.0 and 3.1 generally, together with Enron St. 2.0 at 20-22, 26-28 and Enron St. 4.0 at 2-6 and 4.1 at 2-4.

[246] The Act specifically provides that "the Commission may require the unbundling of other services." 66 Pa. C.S. §2804(3).

market for new entrants.[247] This is obviously unfair and is inconsistent with a level competitive playing field. Id. at 49-50.

Duquesne should be ordered to undertake these steps, as interim measures, subject to the promulgation of final rules on the subject. Duquesne, however, opposes unbundling, claiming that it does not believe there are much savings to be offered to the customer through unbundling.[248] However, the study performed and introduced by Enron witness Reising showed that more than 15% of Duquesne's "distribution" costs are actually related to billing and metering,[249] and that based on Duquesne's unbundled costs as of December 31, 1996, revenue cycle (non-wire) services were more than $31,000,000.[250] Neither the percentage nor the amount it reflects is insignificant.[251] In his study, Mr. Reising actually unbundled the non-wire services of meter/meter reading and billing from Duquesne's distribution rate and calculated the specific amounts which are appropriately assessed for each of the components.[252] More specifically,

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[247] Enron St. 3.0 at 9. For example, EDCs could retrofit existing meters with their chosen version of new technology, while a competitor would be forced to construct a new automated meter reading gateway downstream of the EDC's meter. This would require entry to the customer's home, perhaps modification or removal of portions of a wall or the movement of the circuit breaker box. This construction would result in increasing costs as well as delays, and aesthetic concerns for consumers. Enron St. 3.0 at 9-10.

[248] Duquesne St. 8 at 18.

[249] Enron Exh. 2, PDR-5, at 1.

[250] Enron Exh. 2, PDR-10.

[251] Moreover, regardless of the amount of savings, unbundling will still create a competitive market, likely resulting in enhanced savings in the future. Enron St. 3.0 at 21.

[252] Enron Exh. 2, PDR-7.

Mr. Reising's analysis justifies the establishment of a revenue cycle service credit of $3.27 per month for secondary non-demand billing customers.[253] Id. at 50-51.

Mr. Reising also showed that the costs or "credit" allocated to the unbundled service must be the fully embedded cost of providing that service.[254] Duquesne, however, asserts that when and if unbundling takes place it will give customers who choose alternative suppliers a credit based only on "avoidable" costs.[255] By proposing to limit the customer credit to incremental costs, Duquesne, in effect, is asking both competitors and ratepayers to subsidize its costs and to pay twice.[256] This position should be rejected. Id. at 51.

Finally, there is good reason to unbundle non-wire services from distribution services at this time even if they are not immediately made competitive – so that the customer will know what the charges are for such services.[257] Id.

(2) <u>Open System Architecture</u>

In order to facilitate competition and unbundling, an open system architecture will also be required. As explained by Enron witness Brown, this means that all metering devices must be able to be interconnected with Duquesne's system so that they can be integrated with

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[253] Enron St. 2.1, Exh. 2.1, PDR-10 at 3.

[254] Enron St. 2.0 at 21-22, 27.

[255] Duquesne St. 8-R at 7-8.

[256] Enron St. 3.1 at 4.

[257] Enron St. 2.0 at 21; Enron St. 4.0 at 3-4.

a communications link to provide data readable to Duquesne and to any other affected supplier.[258] Enron M.B. at 51-52.

Mr. Brown also encouraged the efficient exchange of usage and billing information between necessary parties by an information open access ("IOA") system.[259] IOA will operate in a manner similar to the electronic interfaces presently being implemented in the telecommunications industry[260] by allowing both the EDC and the EGS access to the necessary information to provide comprehensive, high quality service to customers.[261] Id. at 52.

It is not clear whether Duquesne will utilize open system architecture. Duquesne has entered into a 15-year "full-service" contract with Itron, Inc. to provide an electronic communication link to its customers.[262] This is known as the Customer Advanced Reliability System ("CARS") and is discussed more fully below. Duquesne's Itron system is described by Enron witness Brown as a one-way interface subject to the complete control of Duquesne.[263]

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[258] Enron St. 3.0 at 11. Such systems allow "the hardware, software and data of multiple parties to interconnect and communicate with each other seamlessly, thereby permitting the marketplace to operate with minimal switching barriers, and at the same time providing complete protection for proprietary customer data." Enron St. 3.0 at 2.

[259] Enron St. 3.0 at 15.

[260] Enron St. 3.0 at 15. The Commission is familiar with the concepts underlying IOA from the electronic interfaces between incumbent local exchange carriers and competitive local exchange carriers - Operation Support Systems - which have been required under the *Telecommunications Act of 1996*. *Id.*

[261] Enron Exh. 3, JAB-5.

[262] Duquesne St. 8 at 5-6.

[263] Enron St. 3.0 at 13. "Under such a system, Duquesne would control the content and format of information its competitors receive and would establish itself as communications 'gatekeeper' for its competitors. This type of system would not be the type of open network (continued...)

Mr. Brown contrasted this proposed Duquesne system with Enron's two-way IOA system, which permits both EDCs and EGSs equal access to request customer information while preserving the customer's proprietary concerns. Regardless of the existence of CARS, the Commission should require Duquesne to provide the necessary open system architecture that will make it possible for all EGSs to obtain easily the data and information they need to serve their customers. Id. at 52-53.

(3) Reasons for Immediate Unbundling

Contrary to the arguments offered by Duquesne, Enron has convincingly demonstrated through its testimony that numerous reasons in the record support the immediate unbundling and competitive provision of non-wire services:

(1) Reduced Costs. Competition in non-wire services will lower the costs of these services to consumers, eliminate cost duplications and stimulate innovative responses to customer specific requirements. Based on past experience with deregulated markets, Mr. Brown showed that the unbundled market for billing and customer account services will likely exhibit major cost reductions and value added enhancements by third party providers that focus upon one, or a few, services.[264] Mr. Brown further showed that competition will also reduce metering

(...continued)
architecture system necessary to enable full competitive development." Enron St. 3.0 at 14.

[264] Enron St. 3.0 at 10-11. This occurred in the telecommunications industry where local exchange carriers reduced their own billing and customer costs by 28%. Enron Exh. 3, JAB-1. However, these same companies realized that utilizing third party billing companies, who could concentrate on the specifics of the billing function, could produce even larger savings, between 20% and 62% below their initial expense levels. Enron Exh. 3, JAB-2.

costs.[265] Such reductions would, in turn, foster the growth of the pertinent technology and would likely result in the introduction of new pricing options by EGSs that would enable consumers to lower their bills for usage.[266] Enron M.B. at 53-54.

(2) Expanded Choice. The introduction of innovative metering and metering services will bring expanded choice for Pennsylvania consumers.[267] This is one of the primary purposes of the Act. Advanced metering technology at a competitive cost is already available.[268] The use of these meters will allow EGSs to offer pricing options to cost-sensitive consumers to manage their demand for electricity to times of the day or the year when electricity prices are at their lowest and enable them to reduce their electric bills. New services could also be provided as part of the non-wire services.[269] Id. at 54.

(3) Improve Success of Restructuring. Unbundling the cost of providing all non-wire services is crucial to the success of retail restructuring. Because these types of services represent a large proportion of small consumers' monthly bills, competitive suppliers may be unable to market effectively to these small customers unless unbundling and competitive provisioning is permitted.[270] Id.

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[265] Enron St. 3.0 at 16-17.

[266] Id.

[267] Enron St. 3.0 at 11, 17.

[268] Enron St. 3.0 at 17.

[269] Mr. Brown testified these would include appliance monitoring, latchkey services, toxic gas detection, time-of-use pricing, and outage detection. Enron St. 3.0 at 11; Enron Exh. 3, JAB-3.

[270] Enron St. 4.0 at 6.

(4) Added Value. Competition in non-wire services will bring customers substantial benefits that would not be obtainable if competition is limited to the supply of generation, because only then will they be able to offer services and products in addition to "commodity" price competition. Conversely, absent the ability to offer such services competitively, they will be placed at a competitive disadvantage vis-a-vis Duquesne's monopoly, and will be unable to provide added value to consumers.[271] Id. at 54-55.

(5) The California Experience.[272] Enron believes that experience in California supports the immediate unbundling of non-wire services in Pennsylvania. In 1991, when the California Public Utility Commission unbundled natural gas transportation and procurement, it limited unbundling and competition for smaller customers to only the commodity itself. As a result, the incumbent gas utilities were able to reduce their cost of gas to meet the competition for gas prices. Competitors did not have the ability to create additional value for customers by providing better or less expensive service in other areas, such as metering and billing. Consequently, the number of competitive marketers has severely declined.[273] The California Commission has recognized this problem, and is attempting to rectify it.[274] Id. at 55.

Significantly, the California Commission avoided the same mistake in restructuring the electric industry. In its Opinion on the Unbundling of Revenue Cycle

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[271] Enron St. 3.0 at 3.

[272] Enron St. 3.0 at 4-6.

[273] While nearly 50 marketers entered the California market, only three remained at the end of 1996. The net result has been fewer competitors and less value for these smaller customers. Enron St. 3.0 at 4.

[274] Enron St. 3.0 at 4-5.

Services,[275] the California Commission allowed non-wire services to be provided competitively as of January 1, 1998, except for smaller customers (20 kW or less) which it deferred until January 1, 1999.[276] Id. at 55-56.

The California Commission's decision to allow the competitive provisioning of non-wire services has already produced dividends. For example, Cellnet Data Systems recently announced that it is constructing a metering communications network in California to bring new products and services to customers at lower costs. Absent the action of the California Commission to unbundle and allow competition in non-wire services, Cellnet would not have been able to make those competitive new services available to customers.[277] Id. at 56.

This Commission should avoid the primary and evident mistake made by the California Commission in the deregulation of gas - the failure to fully unbundle non-wire

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[275] Enron St. 3 at 5-6, citing Decision 97-05-039 (May 6, 1997) at 8. The California Commission there stated with respect to the unbundling of non-wire services:

> There are long-run issues that might motivate this Commission to consider the merits of allowing energy suppliers to offer these services some time in the future. What prompts us to ask these questions now is a concern that direct access opportunities to residential and small commercial customers in 1998 might be severely limited if we fail to allow energy providers to provide these services and to offer their customers the resulting savings.

[276] Decision 97-05-039 at 16-17.

[277] Enron St. 3.0 at 6. As Enron witness Brown observed, Duquesne witness Allison (Duquesne St. 8 at 16-17, Exh. FRA-4) refers to an article written by the vice president of Cellnet, Chris S. King. Mr. Brown observed that Cellnet - and Itron, the supplier of CARS - have often testified to their technologies' dependence upon economies of scale. However, Cellnet is now entering the competitive market even without economies of scale, and even though it has no assurance of a large customer base for its service, Cellnet has made a large investment in California's unbundled and competitive market. Enron St. 3.0 at 6, n. 3.

services – and take advantage of its experience in unbundling those services in the deregulation of electricity. Id.

(6) The Duquesne "Itron" meter reading system demonstrates the potential benefits from competitive non-wire services. Ironically, the testimony of Duquesne's own witness, Mr. Allison, demonstrates the potential values that could be obtained from an environment that encouraged the installation and use of advanced meters and remote meter reading. CARS is an advanced meter and meter reading system which permits cost savings from remote meter reading and other efficiencies, the offering of all sorts of advanced services such as customized billing, real time and "on demand" readings and better service.[278] Id. at 57.

Mr. Allison testified that, over a 15-year period, Duquesne anticipated it would save $58 million just from the ability to utilize remote meter reading.[279] This does not include savings from other efficiencies such as quicker billing and processing of payment receipts. The CARS system is also expected to allow the non-utility installer and operator, Itron,[280] to offer a host of revenue producing services such as "energy management,"[281] power outage notification and "defined cycle billing."[282] The provision of these types of services is projected to produce more than $25 million in revenues over the 15-year planning period, a portion of which ($1

[278] Duquesne St. 8 at 9.

[279] N.T. 863-64; Duquesne Exh. FRA-7 at 48-50.

[280] N.T. 859-60.

[281] Duquesne St. 8-R at 14.

[282] Duquesne Exh. FRA-7 at 43.

million) will accrue to Duquesne.[283] None of these cost savings or additional revenues are included as offsets to Duquesne's claimed distribution rates.[284] Mr. Allison's testimony illustrates both the potential advantages to customers if competitive metering were permitted and why EDCs - like Duquesne - are so opposed to allowing any other entity to provide such services. The utility wants to keep these savings and revenues to itself even though it has no right to such exclusive provision (a meter is obviously not a monopoly service any more than generation is and EDCs never received exclusive franchises for "metering"), and even though its position will obviously slow the deployment of such meters and deny customers their benefits (for Duquesne that means the prospect of even more advanced meters and services in response to competitive pressures - if such were allowed), for years to come. It also refutes the contention by some that only a utility could be trusted to install, operate and maintain meters. Id. at 57-58.

Both Duquesne and IBEW oppose the proposal of Enron and other parties, including OTS[285] and OCA,[286] to unbundle non-wire or revenue cycle services, especially billing

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[283] N.T. 870-71; Exh. FRA-7 at 44.

[284] N.T. 864-65.

[285] OTS M.B. at 81-85; OTS concludes: "Billing and metering costs should also be specified on the customers' bills so that they can make informed decisions as to their choices for the provision of these services. If a less expensive supplier can provide those services at a lower cost, the customer should have the right to know this and act accordingly." Id. at 85 (emphasis added).

[286] OCA M.B. at 72-76. OCA points out that Duquesne's CARS automatic metering system should make it easier to interface with EGSs to allow the supplier total bill option; that Duquesne should unbundle the current costs of some features associated with metering and provide a credit to any customer who obtains an alternative meter or whose meter is electronically read by an EGS; and that Duquesne should be prepared for installation of and (continued...)

and metering. Duquesne's and IBEW's arguments misinterpret the Act, are not supported by the record in this proceeding and are inconsistent with the best interests of consumers as both the OCA and OTS have pointed out.[287] Enron R.B. at 22.

(4) Duquesne's Position

Enron notes Duquesne suggests that resolution of these issues should be handled generically,[288] relying principally on the Commission's rulemaking orders, such as the Customer Services Order[289] and Advanced Meter Order[290]. Duquesne also relies on the PECO Restructuring Order,[291] where the Commission determined not to require PECO to unbundle

[286](...continued)
billing for alternative meters by suppliers. OCA expressed some concerns with Enron's agency proposal in connection with the supplier complete bill option, especially with regard to consumer protection issues. OCA M.B. at 76; OCA St. 5R at 7-9. Enron believes that it has addressed these issues. Enron M.B. at 64, 68-71; 72-73.

[287] Enron M.B. at 49-68. Enron comprehensively presented its legal, factual and policy arguments in support of the unbundling of and competitive entry into revenue cycle services in its Main Brief and will not repeat those arguments here except as necessary to respond to specific arguments raised by either Duquesne or IBEW.

[288] Duquesne M.B. at 81-82.

[289] Final Order Re: Guidelines for Maintaining Customer Services at the Same Level of Quality Pursuant to 66 Pa. C.S. §2807(D) and Assuring Conformance with 52 Pa. Code Chapter 56 Pursuant to 66 Pa. C.S. §2809(E) and (F), M-00960890F.0011 (July 11, 1997) ("Customer Services Order") .

[290] Rulemaking Re: Advanced Meter Deployment for Electricity Providers; 52 Pa. C.S. §57.250-57.257, L-00970128 (November 24, 1997) ("Advanced Meter Order").

[291] Duquesne M.B. at 81-83.

those services at this time based on the record before it.[292] Enron addressed, in detail, the Commission's treatment of revenue cycle services in the PECO Restructuring Order and demonstrated why revenue cycle services should now be unbundled in Duquesne's service territory based on the record of this proceeding.[293] Enron R.B. at 23.

The fact of the matter is that the Commission has expressly determined that the appropriateness of unbundling and competitive entry into revenue cycle services should be decided on the record of each restructuring proceeding. In the Commission's Customer Services Order, the Commission stated just that:[294]

> Utility restructuring plans should provide for the contingency of allowing suppliers to (1) render at the customer's request a consolidated bill that includes both EDC and supplier charges, and (2) engage in complaint handling.

Id. at 23-24. And again, as the Commission specifically concluded pertaining to supplier billing:[295]

> We will not repeat our prior comments in their entirety, but we will reiterate some of the key points which we believe make it appropriate, both legally and as a matter of policy, to sustain this guideline so that parties may continue to explore in the Restructuring Filing of each utility the contingency of allowing a supplier single bill.[296]

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[292] PECO Restructuring Order at 138-40.

[293] Enron M.B. at 53-58, 61-62, 67.

[294] Customer Services Order, Appendix B, Section II.B.

[295] Customer Services Order at 30.

[296] See, also, Customer Services Order at 10-11, 30, Appendix B, Section II.B. and II.H.I. and OCA M.B. at 73-74. In its Customer Services Order, the Commission further stated that provision of these services by EGSs would be dependent on their conformance with (continued...)

Notwithstanding Duquesne's assertions to the contrary, the Commission's firm determinations not only support, but require, that revenue cycle service issues be addressed in each EDC restructuring filing and in each litigated restructuring proceeding. Duquesne cannot be permitted to avoid these issues in this case and the Commission's determinations must be based on the specific record of this proceeding. Id. at 24.

Duquesne's position regarding metering is particularly hard to accept given the fact that it is phasing itself out of the provision of metering services and has contracted out a substantial portion to Itron, a third party provider, which will own and operate meters in Duquesne's service territory.[297] Duquesne has admitted that such third party participation is not compliant with the Advanced Meter Order, which required the EDC to own and operate all meters.[298] Duquesne believes this inadequacy can be cured by obtaining an exemption if the Advanced Meter Order becomes the final rule.[299] However, Duquesne does not believe the Commission need be concerned with system reliability, because although Itron is not subject to the Commission's jurisdiction, it is bound to comply with metering standards "by contract."[300] Id. at 24-25.

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[296](...continued)
Commission regulations and guidelines applicable to these customer service functions and expressed its intent that the EGS's performance of these services must maintain the same level of quality. Id. at 7-8.

[297] N.T. 856-57.

[298] N.T. 858-59.

[299] N.T. 859.

[300] N.T. 859-60.

Enron agrees with many of Duquesne's assertions regarding metering. For example, Enron agrees that third parties other than the EDCs can provide safe and reliable metering services compliant with the Commission's metering standards.[301] Enron also agrees that these metering services have the potential to be more advanced and efficient than the EDC's traditional "one size fits all" approach. However, Enron does not agree that only an EDC-selected vendor is qualified to provide metering services, or that such restricted third-party metering is either fair or nondiscriminatory. While Duquesne has no choice but to agree that the Act permits the provision of metering services by entities other than the EDC,[302] its view that only EDCs' selected third-party vendors should be exempted from a requirement that EDCs provide metering services, is absurd on its face. In light of the fact that Duquesne has been able to use outside contractors to take substantial advantage of advanced metering technology to achieve cost savings and increase revenues, fairness requires the unbundling of and competitive entry into metering services in Duquesne's service territory now, and the Commission should take the appropriate steps to do so in its decision in this proceeding. Id. at 25-26.

(5) IBEW's Position

Enron finds the IBEW, on the other hand, presents a frontal attack on the Commission's legal authority to require the unbundling and competitive provisioning of non-wire

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[301] In fact, the Commission is in a better position to regulate EGS metering services than Itron's metering services, since although EGSs are not "public utilities" they are at least subject to the Commission's jurisdiction.

[302] If IBEW's legal interpretation of the Act – that unbundling of and non-EDC provision of metering services is illegal – is accepted, then the provision of metering services by Itron would be illegal since Duquesne can not be exempted from a statutory requirement.

services. Notwithstanding the fact that the Commission has already determined these legal issues adversely to IBEW's position in the Customer Services Order.[303] The Commission's determination regarding legality is consistent with the Act and should be affirmed here. Enron R.B. at 26.

(A) Impact of the Act on the Code

In order to understand the legality of the Commission's authority to unbundle and competitive entry into non-wire services, Enron submits it is necessary to consider the impact of the Competition Act on preexisting provisions of the Public Utility Code. So long as the furnishing of electricity was entirely a regulated utility service, no fine lines were necessary regarding the classification of those services. Admittedly, the Public Utility Code was drafted with the presumption that all electric service, and related services, would be provided by the franchised monopoly. Indeed, as IBEW asserts, the terms "services" and "facilities" were defined broadly in the Public Utility Code to include the vast majority of activities conducted by public utilities, including EDCs.[304] Enron R.B. at 26-27.

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[303] See, Enron M.B. at 59-67.

[304] 66 Pa. C.S. §102; IBEW M.B. at 9. The fact that the statutory term "services" is defined broadly in 66 Pa. C.S. §102 is irrelevant to interpretation of the statutory phrase "transmission and distribution of electricity" in 66 Pa. C.S. §§ 2802 and 2803 which the General Assembly has found should remain subject to regulation as a "natural monopoly." The record in this proceeding is undisputed that revenue cycle services are not "natural monopolies" and are provided by a wide variety of entities in other industries. Enron St. 2.0 at 27; Enron St. 3.0 at 10-11; Enron Exh. 3, JAB-1 and JAB-2. In fact, as IBEW acknowledges (IBEW M.B. at 14-15), the Act expressly authorizes suppliers to provide billing services. Furthermore, Duquesne has already phased itself out of the provision of metering and has contracted out the provision of metering services to Itron - which is not a public utility.

However, the "competition" overlay that was introduced by the Competition Act – which requires a comprehensive restructuring of the electric industry – has completely revamped the statutory rules under which the restructured industry will operate. To make a competitive retail electric market a reality, as required by that Act, competition must be permitted in every aspect of the retail electric business that is not a natural monopoly in order to maximize value to consumers.[305] Only transmission and distribution service – the wires service – are required to be maintained as EDC monopoly services. Accordingly, all preexisting provisions of the Public Utility Code, as applied to the electric industry, must be understood and interpreted in light of the newly enacted amendments to the Code embodied in the Electric Competition Act. From this perspective, billing and metering are clearly not part of the monopoly utility service because they have nothing to do with physical distribution of electricity.[306] Instead, they are service functions, which are essential components of both the delivery and sale of the commodity and fully associated with and support the distribution, transmission and generation supply service categories. Id. at 27-28.

Consistent with the avowed purposes of the Electric Competition Act, to develop retail electric competition to the greatest extent possible,[307] only those services or facilities which remain natural monopolies and for which unbundling is not technically feasible or for which it is shown that competition will sacrifice system safety and reliability should be permitted to

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[305] Enron St. 1.0 at 5-6; Enron St. 4.0 at 5-6.

[306] Enron St. 2.0 at 27.

[307] See, 66 Pa. C.S. §§2802(5), (7), (8), (12), (14) and (15).

justify the continuance of the utility's monopoly status.[308] The only utility service that meets this standard is the actual "wire" distribution network of each utility. All other services and service functions should be unbundled to the extent technically feasible so that competitive alternatives can become available. Id. at 28.

IBEW's arguments interpret the pro-competitive provisions of the Act as if they are restricted by the traditional view that utility services are subject to a monopoly, and attempt to apply preexisting provisions of the Code in a manner which would defeat the Act's intent. Instead, these statutory provisions must not be read in isolation but must be interpreted consistent with the General Assembly's overriding objective to restructure the electric industry in a manner which brings the full benefits of retail competition to Pennsylvania's consumers and businesses. Id.

(B) Authority to Unbundle "Other Services"

Enron argues the second gross error in IBEW's rationale is its failure to consider Section 2804(3) of the Act. Indeed, it is not surprising that reference to this important subsection is noticeably absent from IBEW's brief. Section 2804 of the Act delegates responsibility to the Commission to define standards and assure compliance with a utility's unbundling obligation in the context of its review of each utility's restructuring plan. This Section then provides as follows in relevant part:

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[308] The Commission can obtain policy guidance by following the policies reflected in the federal law governing the development of telecommunications competition, which recognizes that marketplace development cannot occur unless the monopoly is required to unbundle its services to the greatest extent that is technically feasible. Section 251(c)(3) of the Telecommunications Act of 1996, 47 U.S.C. §251(c)(3).

> The following interdependent standards shall govern the Commission's assessment and approval of each public utility's restructuring plan, oversight of the transition process and regulation of the restructured electric utility industry:
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> * * *
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> (3) The Commission shall require the unbundling of electric utility services, tariffs and customer bills to separate the charges for generation transmission and distribution. The Commission may require the unbundling of other services. (Emphasis added.)

Enron R.B. at 29.

The General Assembly's delegation of discretionary authority to unbundle "other" services in addition to the three primary service categories clearly establishes that there must be services other than the three types mentioned that can be unbundled. Furthermore, this clause provides ample authority for the Commission to establish standards requiring and implementing the unbundling of non-wire services. In fact, the statutory reference to "the unbundling of other services" is almost certainly a direct reference to such services.[309] Furthermore, Section 2804(3) makes it clear that required unbundling should extend not only to services,[310] but also to

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[309] The declaration of policy found at 66 Pa. C.S. §2802(14) creates two distinct mandatory obligations on the part of EDCs: "to unbundle their rates and services and to provide open access over their distribution and transmission systems." (Emphasis added.) Compliance with both obligations is absolutely necessary for compliance with the Act and the meaningful development of retail competition. Moreover, while costs of non-wire services and service functions are presently included in Duquesne's rates, those services and functions themselves are not part of Duquesne's energy delivery system. Enron St. 2.0 at 27. Accordingly they are subject to the unbundling requirement of "other services" imposed by the General Assembly.

[310] The only conceivable purpose of unbundling services is to allow the competitive provisioning of those services subject to unbundling. The only exception to this general rule is the unbundling of services like distribution and transmission which is necessary to define jurisdictional lines (i.e., distribution services are regulated by state and a transmission services (continued...)

"tariffs" and "bills." IBEW completely ignores this important provision and the authority it confers on the Commission. The truth of the matter is that the General Assembly has expressly provided the Commission with discretionary authority to unbundle revenue cycle services. None of IBEW's creative, but unreasonable, arguments can change this simple fact. Id. at 29-30.

(C) The Effect of the EDC's Requirement to Provide Customer Services

Enron submits IBEW improperly relies upon and misreads Section 2807(d) of the Act - which requires that each utility continue to provide customer services to its customers at the same level of quality as it does now - to assert that only an EDC may legally provide those services. But this provision does not prohibit the unbundling or the competitive provision of these services (any more than it precludes the competitive provision of electric generation, or other services "traditionally provided by EDCs") by those same suppliers. Nothing in the language of Section 2807(d) can reasonably be interpreted to establish the EDC as the exclusive provider of non-wire services or restrict the Commission's express authority under Section 2804(3) to establish standards for the unbundling and competitive entry of such services. Enron R.B. at 30-31.

This statutory language, as noted in the Customer Services Order, "is merely a reflection that the EDC must stand ready to provide these customer service functions"[311] if requested to do so. But, it obviously does not establish the EDC as the exclusive provider. In

(...continued)
are regulated by the FERC).

[311] Customer Service Order at 10.

fact, in the billing area under Section 2807(c), as IBEW itself notes,[312] the Act continues to impose quality of service requirements on EDCs while at the same time expressly providing that EGSs can also provide billing services to customers. Furthermore, in Duquesne's case, it has turned over ownership and operation of many of its meters to Itron, subject only to a contract between the two companies. IBEW has unsuccessfully argued its interpretation of Section 2807(d) to the Commission in other dockets and its arguments are no more convincing here. Id. at 31.

(D) The Customer Services Order

In the Customer Services Order, the Commission, upon careful consideration of the legal issues that had been raised, ruled that it does indeed have the legal authority to require the unbundling and competitive provisioning of non-wire services.[313] The Commission also issued guidelines for maintaining "customer services" at the same level of quality under retail competition[314] and to assure conformance with Chapter 56 of the Commission's regulations.[315]

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[312] IBEW M.B. at 14-15.

[313] See, Customer Services Order at 10-11, 29 (quoted, in part, in Enron M.B. at 59-60). The Commission cited as the statutory basis for this option, 66 Pa. C.S. §2803 (which defines Electric Generation Supplier to include brokers, marketers, and aggregators and recognizes that suppliers may engage in "related services"), 66 Pa. C.S. §2804(3) (which authorize the Commission to unbundle "other services"), and 66 Pa. C.S. §2809(e) (relating to regulation of EGSs).

[314] As required by 66 Pa. C.S. §2807(d).

[315] As required by 66 Pa. C.S. §§2809(e) and (f).

It also required that these guidelines be addressed in each of the various restructuring proceedings.[316] Enron R.B. at 31-32.

Significantly, in requiring that the unbundling and competitive provisioning of these non-wire services be considered in each restructuring, the Commission also required the assurance that any EGS providing those services maintain the same quality of service as provided by regulated utilities.[317] This is a short and complete answer to IBEW's completely speculative contention that competitive provisioning will lead to a decline in service quality.[318] Id. at 32.

(E) Refutation of IBEW's Arguments

Enron posits IBEW parses the provisions of the Competition Act and other provisions of the Code in such a way – reading them in isolation – to fabricate an argument that the unbundling and competitive provision of non-wire services are unlawful. As demonstrated above, IBEW's arguments have no merit and are no more than an attempt to revisit issues the Commission has already conclusively decided. Its newly developed arguments, as explained below, are no more convincing than previous arguments already raised before and correctly rejected by the Commission. Enron R.B. at 32-33.

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[316] Customer Services Order at 11, 29, Appendix B, Sections II.B and II.H.

[317] Customer Services Order at 7-8.

[318] IBEW's views regarding service reliability in a competitive environment are not only completely speculative but are inconsistent with the experience in other industries in which the service quality billing services has increased through the introduction of competition. Enron St. 3.0 at 10-11.

1. IBEW asserts that EGSs are not public utilities, but that only public utilities can provide non-wire services.[319] IBEW is half right. It is true that EGSs are not "public utilities" except for the limited purposes described in Sections 2809 and 2810.[320] However IBEW's contention that only a "public utility" can provide non-wire services, because those services were traditionally provided by public utilities prior to the enactment of the Electric Competition Act, is simply concocted from whole cloth. Such a view completely ignores the requirements of Section 2802(14), which requires electric utilities to unbundle their rates and services and to provide open access, as well as Section 2804(3), which explicitly delegates to the Commission the authority to require the unbundling of services other than generation, distribution and transmission service, which would include non-wire services.[321] If this argument were true, suppliers wouldn't be able to provide generation services or anything else "traditionally" provided by "public utilities." Id. at 33.

2. IBEW also overlooks the fact that while the definition of an EDC is narrowly constructed in the Act as "providing facilities for the jurisdictional transmission and distribution of electricity to retail customers," an EGS is defined with a broader scope as one

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[319] IBEW Brief at 9-11.

[320] 66 Pa. C.S. §102 defines "public utility" in part as follows:

"(2) The term [public utility] does not include:

* * *

(vi) Electric generation supplier companies except for the limited purposes as described in sections 2809 . . . and 2810 . . . ."

[321] As indicated previously, acceptance of IBEW's view would render illegal the metering services presently provided by Duquesne via Itron.

that sells "electricity or related services" to end-use customers.[322] By definition, therefore, an EGS may additionally provide retail customers with "related" services, which clearly includes and was specifically intended to reference non-wire services. While IBEW may be correct that jurisdictional T&D services must be provided by an EDC,[323] that begs the question as to non-wire services, because they are not T&D services but are "other services" under Section 2804(3).[324] Id. at 33-34.

3. IBEW ignores the objectives and definitions contained in the Electric Competition Act, and relies instead on a misreading of 66 Pa. C.S. §102 which contains the broad definition of "service" and "facilities."[325] As noted above, the scope of these terms must be interpreted within the context of the overlay of the Act, and any restrictions on unbundling or competitive entry are expressly limited to services involving the transmission and distribution of electricity; they do not apply to all EDC services and facilities as IBEW argues. Id. at 34.

4. IBEW likewise ignores the provisions of the Electric Competition Act to argue that an electric meter must be considered utility property because it is used or supplied by public utilities, or that a bill rendered for distributing electricity is an "act done" in providing

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[322] 66 Pa. C.S. §2803 (emphasis added).

[323] IBEW M.B. at 10.

[324] The fact that the term "facilities" is defined broadly in Section 102 also has no bearing on interpretation of the definition of "electric distribution company" in Section 2803 since under Section 2803 only those facilities which pertain directly to the "transmission and distribution" or delivery function are within the scope of the definition.

[325] IBEW M.B. at 10.

regulated distribution services.[326] The fact of the matter is that non-wire services are not delivery services and do not involve the physical distribution and transmission of electricity, but are service functions which not only support distribution and transmission services, but are integral components of generation supply. There is simply no basis, as this Commission has already held,[327] to require these services to be provided only by an EDC. Id. at 34-35.

5. IBEW contends that Section 2807(c), which specifically recognizes the right of an EGS to render a separate bill to a customer, thereby precludes the EGS from rendering a single bill.[328] IBEW claims that since the provisions of that section otherwise apply specifically to EDCs, this somehow precludes EGSs from performing the same functions.[329] Of course, as the Commission has established, this provision only requires the nonexclusive continuation of such services by the EDC to customers who need or desire such services from the EDC, and the Commission has so ruled:[330]

> Although §2807(C) recognizes that the EDC "may be" responsible for the billing of all electric services, there is nothing in this passive provision or anywhere else in the Act that makes the EDCs the exclusive provider of this customer service function.

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[326] IBEW M.B. at 10-11. Each of these argument can just as easily be characterized as a generation function since a meter and a bill are necessary to provide generation service. The term "generation service" is not defined in the Act and could easily be construed to include these items, which the Act clearly does subject to competition.

[327] Customer Services Order at 10-11.

[328] IBEW M.B. at 13-14.

[329] IBEW M.B. at 14..

[330] Customer Services Order at 29 (emphasis added). Although, the Commission has interpreted the language of Section 2807(c) as providing discretionary authority to allow EGSs to provide a single supplier bill, in Enron's view, Section 2807(c) mandates that the EGS provide a single supplier bill if a single supplier bill is requested by a customer.

Moreover, to the extent that an EGS provides those functions, the Commission can and should require that the EGS be required to do so subject to all the applicable requirements of the Public Utility Code, not only Section 2807(c).[331] Id. at 35-36.

6. IBEW points to a number of sections of the Public Utility Code[332] that it claims require public utilities only to bill and meter utility services.[333] These provisions, however, merely contain certain billing, collection, termination and metering procedures that must be met by public utilities for service to customers (except for bills for installation charges). However, none of these sections specifically direct that only "public utilities" may provide any of these functions, nor do they preclude EGSs from doing so subject to similar regulations by the Commission.[334] Moreover, certain of the provisions, 66 Pa. C.S. §1521-33, apply to the rights of tenants where a utility proposes to terminate electrical service to a landlord. This would have nothing at all to do with an EGS, which cannot terminate service.[335] Id. at 36.

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[331] The Commission has in fact done so in the guidelines in Customer Services Order at 7-8.

[332] 66 Pa. C.S. §§317(b), 1504, 1507, 1509, and 1521-33.

[333] IBEW M.B. at 11-13.

[334] In fact, virtually all of the requirements in the provisions of the Code identified by IBEW are repeated in Chapter 56, which as IBEW points out already govern suppliers. For example, the statutory due date for payments provided for in 66 Pa. C.S. §1509 is codified by regulation at 52 Pa. Code §56.21; and the landlord-tenant provisions of 66 Pa. C.S. §§1521-1523 are codified almost verbatim at 52 Pa. Code §§56.121 et seq.

[335] To the extent that an EGS cancels its own electricity supply service under any circumstances, the EDC or some other Commission designated supplier would still be required to provide such service as the provider of last resort. To the extent consumer protections in addition to those currently included in Chapter 56 are required to assure the continuous flow of electricity, those protections should be implemented as soon as possible. Neither the Customer Services Order nor Enron's position in this case in any way remove termination and (continued...)

7. IBEW also incorrectly states that allowing the unbundling of non-wire services would remove the protections provided by relevant Commission regulations,[336] especially Chapters 57 and 58, because they are not specifically required to be applicable to EGSs under the Electric Competition Act, as is Chapter 56.[337] This argument is ludicrous. There is nothing to preclude the Commission - which, after all, promulgated all those requirements - from imposing all necessary standards on EGSs as a condition of unbundling.[338] In fact, Enron consistently has advocated, and continues to agree, that the relevant portions of Chapters 57 and 58 of the Commission's regulations should be applied to generation suppliers that wish to provide metering services. This could be accomplished as part of the Commission's final order in this case, as well as in its metering docket. Id. at 37.

8. IBEW relies on various "purpose" provisions of Section 2802 of the Act to argue that EGSs should not be permitted to provide billing and metering services.[339] However, IBEW misapprehends these provisions. As demonstrated above, their primary purpose of the Act is to create a competitive retail electricity market. While this is accomplished primarily by unbundling and introducing competition into the generation supply market, the

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reconnection authority from the EDC; indeed, paragraph L of the Customer Services Order confirms such authority.

[336] IBEW M.B. at 14-15.

[337] 66 Pa. C.S. §§2809(e),(f).

[338] The record reflects that Itron, not Duquesne, is providing metering services to approximately 50% of Duquesne's customers and that while Commission quality of services regulations are not directly applicable to Itron, such standards are imposed on Itron through its contract with Duquesne. N.T. 859 (December 18, 1997).

[339] IBEW M.B. at 15-16.

General Assembly empowered the Commission with discretion to unbundle (and introduce competition) in other services consistent with the public interest. In addition to that explicit statutory language, the Commission has implicit authority to carry out its statutory duties.[340] Under its implicit authority, the Commission is authorized to act in furtherance of the statutory objectives identified in the Electric Competition Act.[341] For all the reasons set forth herein, and in the Customer Services Order, such unbundling is necessary and should be permitted. Id. at 37-38.

(6) MAPSA's Position

MAPSA finds Duquesne's proposal does not allow for the competitive provision of the metering or billing functions. Duquesne St. 8 at 3. Duquesne believes that in order to comply with the mandate of the Act, it is not necessary to unbundle metering and billing, in fact Duquesne's testimony could lead one to believe that the Act would forbid competitive provision

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[340] As an agency of delegated powers, the Commission has both those powers explicit in its enabling statute and implicit as necessary to exercise of those express powers. Pennsylvania Public Utility Commission v. Philadelphia Electric Company, 460 A.2d 734 (Pa. 1984); Metropolitan Edison Co. v. Pennsylvania Public Utility Commission, 437 A.2d 76 (Pa. Cmwlth. 1981).

[341] The fact that an administrative agency or other governmental unit is a creature of statute does not mean that all details of its scope of delegated authority must be expressly or separately enumerated in the enabling statute, but only that the basic policy choices must be made by the Legislature which guides and restrains the exercise of administrative functions. Gilligan v. Pennsylvania Horse Racing Commission, 422 A.2d 487 (Pa. 1980); Hospital Association v. MacLeod, 410 A.2d 731 (Pa. 1980); William Penn Parking Garage, Inc. v. City of Pittsburgh, 346 A.2d 69 (Pa. 1975); Charters Valley Joint School District v. County Board of School Directors, 211 A.2d 487 (Pa. 1965); Pennsylvania Builders Association v. Pennsylvania Public Utility Commission, 483 A.2d 1025 (Pa. Cmwlth. 1984); Western Pennsylvania Water Company v. Pennsylvania Public Utility Commission, 311 A.2d 370 (Pa. Cmwlth. 1973).

of these services. Id. at 4. Duquesne does acknowledge, however, that the statute does allow the Commission to order it to unbundle other services. N.T. 852. MAPSA witness Russell testified that in order to have a truly competitive market, in which suppliers are permitted to provide all of the services that the utility can provide, it is necessary to allow suppliers the single bill option, and to allow supplier provision of the metering function. MAPSA St. 1 at 42-43; MAPSA M.B. at 39-40.

Duquesne believes that in the period that it is still providing supplier of last resort service, that the only competition that will exist will be between suppliers and the company – with the company providing service at the rate cap. N.T. 136. Under Duquesne's competitive scenario, the company – the same entity that will be competing with suppliers for business – will continue the monopoly provision of the most important customer service functions. As an alternative to Duquesne's proposal, which allows Duquesne to further entrench its monopoly position, the Commission should consider adopting the Metering and Billing Principles which are proposed in this proceeding by MAPSA witness Russell. MAPSA St. 1, Attachment I. Application of MAPSA's principles will allow for the competitive provision of those services which are critical to the development of the customer's relationship, and will allow for true competition to develop. MAPSA M.B. at 40.

MAPSA notes Duquesne argues its position on the unbundling of revenue-cycle services, namely, that those services should be unbundled, if at all, pursuant to a generic rulemaking proceeding and that the Commission need not address unbundling here. Duquesne M.B. at 81-82. Indeed, it is Duquesne which makes the most compelling argument for the unbundling of the metering and billing functions. Duquesne's new, real-time metering system

(CARS) will make unbundling far less complicated than it would be with other utilities. N.T. 858-873. Duquesne has no technical reason not to unbundle these services, except that it desires not to have competitors engaging in the functions of metering and billing. Duquesne simply would prefer to maintain its monopoly position. Duquesne should be required to unbundle these services now. MAPSA R.B. at 12.

(b) Resolution in Generic Proceedings v. Resolution in This Case

(i) Duquesne's Position

Duquesne posits the unbundling of revenue cycle services is a generic issue that should be addressed in a rulemaking proceeding. The Commission has already initiated rulemakings to address several of these issues through a collaborative process. Duquesne St. 8-R at 3 (citing Guidelines for Maintaining Customer Services, Docket No. M-00960890F0011, 1997 PaPUC LEXIS 42 (July 11, 1992) (customer billing) ("Customer Services Guidelines); Advanced Meter Deployment for Electricity, Docket No. L-00970120, 28 Pa. Bull. No. 5 (Jan. 31, 1998) (customer metering) ("Proposed Rulemaking" or "Advanced Metering Guidelines"). Duquesne M.B. at 82.

(ii) The OCA's Position

The OCA recognizes there are several generic proceedings at the Commission that could potentially resolve some of the issues presented here. However, it is important to address certain issues during this proceeding so that appropriate interim procedures are in place for the onset of competition, particularly since it appears that some of the generic rulemakings will not

be completed by January 1, 1999. See, also, OCA St. 5 at 30. As such, the OCA submits that certain issues must be resolved on an interim basis. OCA M.B. at 73.

(iii) IBEW's Position

As early as January 1997, IBEW asked the Commission to establish a generic proceeding to resolve the important legal, policy, and factual issues concerning the provision of billing, metering, and meter reading services by Marketers and other non-utilities. See, Comments of IBEW in Tentative Order Re: Electric Utility Restructuring Filings Made Pursuant to 66 Pa. C.S. §2806(e), Docket No. M-009608980 F. 0003, dated January 30, 1997 pages 1-5. IBEW believed that these issues were best decided before any of the utilities' specific restructuring plans were filed. However, the Commission determined that it preferred to decide these issues on a case-by-case basis in each restructuring plan, rather than in a generic proceeding. Order Re: Electric Utility Restructuring Filings Made Pursuant to 66 Pa. C.S. §2806(E), Docket No. M-00960890 F. 0003 (Pa. PUC Feb. 13, 1997), Slip Op. at 8-11; IBEW M.B. at 16-17.

In July 1997, IBEW again raised generic issues questioning the legality of non-utilities providing billing, metering, and meter reading services. Petition for Reconsideration, Clarification, Rescission, and Amendment of the International Brotherhood of Electric Workers' Pennsylvania Utility Caucus, Final Order Re: Guidelines for Maintaining Customer Services at the Same Level of Quality Pursuant to 66 Pa. C.S. §2807(D), and Assuring Conformance with 52 Pa. Code Chapter 56 Pursuant to 66 Pa. C.S. §2809(E) and (F) ("Customer Service Order"), Docket No. M-00960890 F. 0011, dated July 24, 1997; IBEW M.B. at 17.

In denying that Petition, the Commission stated very clearly that it would not consider IBEW's arguments generically. Rather, the Commission stated that it "anticipated that metering and billing issues would be addressed in each restructuring case." Order, Petition for Reconsideration, Clarification, Rescission, and Amendment of the International Brotherhood of Electrical Workers' Pennsylvania Utility Caucus, Docket No. M-00960890 F. 0011 (Pa. PUC Aug. 21, 1997), Slip Op. at 3-4. The Commission went on to state:

> Although we declined to open up generic proceedings on these and other issues because of the limited time period allowed for hearing and resolution of the restructuring proceedings, we did recognize that the proceedings on the electric utility restructuring plans would examine transition issues, such as metering and billing, that involve employees of EDCs. In fact, the content of the restructuring plans required under Section 2806(d) must discuss the impacts of the proposed plan on the utility's employees. See 66 Pa. C.S. §2806(e). We specifically noted that this issue along with other important issues would be explored in the restructuring proceedings . . .

Id., Slip Op. at 4 (citations and footnotes omitted); IBEW M.B. at 17-18.

The Commission closed its August 21 Order by noting that IBEW (and other interested parties) should actively participate in the restructuring proceedings. The Commission noted its preference for developing these issues in that forum, because "we will have the benefit of a full briefing schedule and an administrative law judge's initial decision before having to decide these issues." Id., Slip Op. at 6; IBEW M.B. at 18.

It appears, therefore, that while the Commission has now ruled on the issue of competitive billing and metering in other proceedings (as IBEW discusses below), the parties must address in this case any facts that might lead to a result, which is different from that reached by the Commission in other cases. Id.

Within the past few months, the Commission has addressed this question on two separate occasions. Both times, the Commission has held that the electric distribution company (EDC) is the only entity that is authorized and permitted to provide metering and meter reading services, and it is the only entity that is authorized and permitted to bill for regulated distribution charges. As IBEW will explain, infra, the record in this case does not contain any information that would lead to a different result. Id.

First, on November 24, 1997, the Commission issued a Proposed Rulemaking Order that requires each EDC to own, install, and maintain all electric meters used to serve its customers. Rulemaking re Advanced Meter Deployment for Electricity Providers, 52 Pa. Code §§57.250-57.257, Docket No. L-00970128 (Pa. PUC Nov. 24, 1997). In that Order, the Commission concluded "that metering should remain a regulated function of the EDC at this time. Metering can remain a regulated function of the electric distribution utility, retaining all existing requirements and procedures for meter installation, reliability, safety, accuracy and the like." Id., Slip Op. at 12; IBEW M.B. at 18-19.

Second, in its recent decision involving the restructuring of PECO Energy, he Commission reached a similar conclusion. PECO Energy. Slip Op. In that decision, the Commission rejected Marketers' attempts to bill for PECO's distribution services and to take responsibility for metering and related services. Specifically, regarding billing, the Commission held: "We . . . cannot conclude that it is appropriate to unbundle billing based on this record. Therefore, PECO shall provide all billing services, including billing for generation services, unless a customer indicates a preference to receive a separate bill directly from the supplier for generation services." Id., Slip Op. at 139. On the issue of metering, the Commission referred

to its rulemaking docket (discussed above) and held that "we do not believe that it is necessary to unbundle metering as a competitive service at this time. . . . While PECO, as a regulated EDC, shall be responsible for all physical work related to the meter, the customer and/or the EGS [electric generation supplier] may select the qualified meter to be used and shall pay as a regulated rate any net incremental cost incurred by PECO as a result of the metering choice." Id., Slip Op. at 140-141; IBEW M.B. at 19.

In summary, on the only two occasions where the Commission has addressed this issue, it concluded that billing, metering, meter reading, and other customer service functions must be provided by as a regulated distribution service by a public utility. There is absolutely no reason to reach a different result in this case. Id. at 19-20.

(iv) Enron's Position

Enron notes Duquesne argues that the unbundling of non-wire services should not be considered in this restructuring case, but should be addressed as part of the collaborative generic rulemaking process in progress.[342] Duquesne gives no good reason for its position, which is not consistent with the Act's objectives. Duquesne essentially seeks simply to delay the advent of unbundling in order to enhance its own competitive position. Enron M.B. at 58.

Duquesne's proffered reasons for delay are that (i) issues still need to be resolved so as not to compromise reliability; and (ii) establishing a generation market should be the first priority and many details still have to be worked out in that regard. Id.

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[342] Duquesne St. 8-R at 19.

With respect to the first reason, the ongoing collaborative process Duquesne refers to actually supports immediate unbundling because it shows there is already a process in place to resolve the fine details of unbundling. Id. at 59.

As to its second contention, the unbundling of non-wire services will not interfere with establishing a competitive generation market; it will enhance it. Duquesne again simply attempts to create barriers to competition by equating choice with confusion. This is nonsense. There is no reason why consumers cannot choose non-wire services in conjunction with direct access; competition can and should be implemented and advanced in all possible areas. So long as there is an adequate statewide consumer education program, consumers will understand their options and be able to make reasonable choices. California and Arizona have both resolved such details and are unbundling non-wire services. Other states, understanding and recognizing the benefits of competition, are also moving toward the unbundling of these services.[343] There is no reason for Pennsylvania to lag behind.[344] This Commission has already ruled that such unbundling and competitive entry are legally permissible. In its Customer Services Order, the

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[343] Enron St. 3.1 at 3.

[344] IBEW witness Moran also opposes unbundling. He contends that only the employees of an EDC have the ability to deal with safety requirements. Safety is a concern, but there is no reason that employees of an EGS, if properly trained and if they meet the requirements imposed by the Commission, would not be able to provide the same safe services. Indeed, Duquesne's present metering system is owned and operated by non-utility personnel. N.T. 859-60. The basic thrust of Mr. Moran's testimony is that meter and billing activities should remain a monopoly with the local utilities. IBEW St. 1 at 8. This view is contrary to the pro-competitive purpose of the Act and taints all of his so-called concerns about safety and other factors in Enron's proposed distribution service tariff. He simply does not wish to accept competition in this area whether or not it is beneficial for the consumer or the union. His testimony should be rejected.

Commission recognized the right to unbundle and competitively provide the billing and supplier complaint functions under the Competition Act. The Commission stated:[345]

> [We] simply disagree with the conclusions . . . that only EDCs can provide these customer service functions. We submit that there is nothing in the Act that would prohibit the supplier single bill option and supplier complaint handling. Although §2807(C) recognizes that the EDC "may be" responsible for the billing of all electric services, there is nothing in this passive provision or anywhere else in the Act that makes the EDCs the exclusive providers of these customer service functions.
>
> We believe that the Act's reference to the EDC's responsibility to provide customer service functions under §2807(D) is intended to maintain the status quo and is merely a reflection that the EDC must stand ready to provide these customer service functions. However, concerning the two specific customer service functions at issue; namely, billing and complaint resolution, we do not read this provision or any other provision of the Act as excluding suppliers from providing these functions. In fact, we believe this interpretation is consistent with the declared policy of the Act to create a competitive market for the generation of electricity.

This ruling is also directly applicable to the legality of furnishing competitive metering. While the Commission did not implement this guideline immediately, it retained it as an option to be explored in the context of the restructuring filing of each utility. Although the Commission has strongly indicated it will consider and likely implement such unbundling in the future, Enron submits that unbundling of non-wire services is vital now, at the beginning of direct access, when pure price pricing competition for generation services will be restricted by the imposition on all customers - regardless of their selection of an electric generation supplier - of CTCs/ITCs. Making metering and other non-wire services subject to competition immediately will bring all the above-described benefits of competition to Pennsylvania consumers

[345] Id. at 10-11; See, also, id. at 29.

and businesses, which will enhance the overall value of direct access. As Mr. Brown observed, requiring unbundling in this proceeding to allow competition in the non-wire service areas will allow efficient EGSs "to differentiate themselves from their competitors and attract customers to their products based on comprehensive and innovative service offerings, while at the same time offering real value and benefits to Pennsylvania's consumers." Id. at 59-61.

Enron observes IBEW claims the Commission has resolved these issues in the PECO Restructuring Order and the Advanced Meter Rulemaking. But, neither of these decisions is dispositive here. In the PECO proceeding, the Commission relied specifically on the record in that case and has recently indicated a continuing interest in the supplier complete bill option.[346] As for metering, IBEW's citation is to a proposed rulemaking which can be accorded no legal weight until finalized. As indicated previously, the Commission has unequivocally declared the legality of the unbundling of and competitive entry into non-wire services and has indicated that the timing of such unbundling should be considered within the context of these restructuring proceedings. As the Commission stated in its Advanced Meter Order:[347]

> The Act does not require unbundling of metering at this time, but certainly anticipates that unbundling may occur in the future.

While the Act does not require immediate unbundling, the record of this proceeding does, and the Commission should act accordingly. Enron R.B. at 38-39.

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[346] See, PECO Compliance Filing Order at 22.

[347] Advanced Meter Order at 13.

(c) Interim Rules Applicable to Duquesne

(i) *Enron's Position*

Regardless of its determination whether to allow the competitive furnishing of non-wire services at this time, Enron asserts the Commission should require the unbundling of those services in Duquesne's rates in any event, so that customers will know what they are paying for these various non-wire services.[348] Enron further urges the Commission to allow the competitive furnishing of non-wire services at this time on an interim basis and subject to final rulemaking. This is especially important in the case of Duquesne so that its CARS does not become so entrenched before unbundling of metering occurs that it becomes impossible to allow competitive provisioning. Enron M.B. at 61.

(d) Specific Services

(i) Customer Billing

(1) Duquesne's Proposal

Duquesne observes the main issue here is whether the Commission should allow customers to receive a single bill from their chosen generation supplier that includes billing of EDC charges. The Commission should not require this. Duquesne St. 8-R at 21-22. The Commission's rulemaking governing interaction between customers, suppliers and EDCs also supports not implementing a supplier billing option at this time.[349] Furthermore, in PECO

[348] Enron St. 2 at 21, 27.

[349] Customer Service Guidelines, 1997 Pa. PUC LEXIS 42 at 26 ("[W]e believe an approach that initially focuses on implementation of the two billing option explicitly set forth at (continued...)

Energy, while the Commission recognized that there may be potential benefits to the third billing option, it nevertheless ordered PECO to provide all billing services, including generation services billing, unless a customer was to choose to receive a separate bill directly from its supplier. PECO Energy, Slip Op. at 139; Duquesne M.B. at 82-83.

(2) **The OTS' Position**

The OTS posits the universal service charge should appear on the customer bills as a separate line item. OTS' position is based upon the fact that, as a separate line item, this charge and its resultant and costs will be easier to track. It will also hold Duquesne more accountable for these costs and inform the customers of these costs. OTS M.B. at 82.

OTS submits that whenever specific charge is being billed to customers, the customers should have such a charge as a specific line item on their bill so that they are aware of how the money they are paying to the utility is being utilized. Id.

Although there are some costs that are difficult to ascertain and delineate, this universal service charge is, clearly, not difficult to calculate. The cost per customer is readily obtainable and the customers should have the ability to see this charge on their bills to make them aware that this specific charge is being paid by them. Additionally, it will allow the customers to be educated as to exactly how much they are individually, responsible to pay for this service charge. OTS contends, that unless the Company is trying to avoid the scrutiny of their customers, or is not willing to advise the customers of how the revenues from those

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[349](...continued)
§2807(c) is necessary to maintain customer service functions at the current levels of quality as required by Section 2807(d).")

customers are being used, there is absolutely no reason for the universal service charge not to appear as a separate line item on Duquesne's customers' bills. OTS St. 3 at 10; OTS M.B. at 82.

(3) **The OCA's Position**

(A) **Supplier-Only Billing**

The OCA claims the proposed billing options contained in Duquesne's initial filing did not conform to the Commission's July 11, 1997 Order on Maintaining Customer Service at the Same Level of Quality (Docket No. M-00960890 F0011). OCA St. 5 at 44. Of the three billing options that the Commission has mandated (single bill from the EDC for all charges, two bills - one from EDC, one from supplier, or a single bill from the supplier containing all charges), Duquesne has not included a supplier-issued total bill as an option. Duquesne St. 8 at 10. The OCA submits that Duquesne has not presented a compelling reason for not complying with the Commission's Order and should be required to correct this in its compliance filing. OCA M.B. at 73.

The OCA submits that Duquesne should be in the proper position to implement such a change, particularly since it is in the process of implementing the CARS system, a new automated metering system that would allow interface with alternative suppliers. Indeed, while on the stand, Duquesne witness Allison agreed that with the proper exchange of information, suppliers could provide a single bill for all customer charges. N.T. 878-880. As such, Duquesne should be directed to include this in its compliance filing. OCA M.B. at 73.

(B) <u>Billing Complaint Resolution</u>

The OCA is in general agreement with the Company's proposals regarding complaint resolution relating to billing. OCA St. 5 at 46. The OCA submits, however, that the Company failed in its initial filing to specifically address how a complaint would be handled for a supplier-only bill. OCA St. 5 at 46. Specifically, OCA witness Alexander, while recognizing that "Duquesne probably has no obligation to handle disputes relating to supplier charges when the supplier has billed the customer directly," recommended that in the case of a dispute affecting both the Supplier and EDC (i.e., a meter reading dispute) the EDC "own" the complaint. OCA St. 5 at 46. She urged the Commission to require Duquesne to provide protocol to address the joint EDC/Supplier dispute. OCA St. 5 at 46-47; See, also, Order Maintaining Customer Service at the Same Level of Quality at 7-8, 33. The OCA submits that Duquesne should provide these procedures as part of its compliance filing for review by all parties and the Commission. OCA M.B. at 74.

(C) <u>Billing Format</u>

The OCA observes Duquesne provided two bill formats with its filing--one showing a bill for both delivery and generation service and one for delivery service alone. Filing Requirement P.13. OCA witness Alexander reviewed Duquesne's proposed bill formats and recommended several changes to the formats. In summary, these changes include: a) the bill should identify regulated versus competitive services; b) the bill should provide additional room for supplier information and generation materials with information presented in the same manner regardless of the supplier; c) the bill should include a uniform method of disclosing

prices such as the per kWh charge for T&D and generation for residential customers; d) the proposed bill format should use plain language and not include an unnecessary number of elements; e) the outside supplier should be allowed to include its own billing page in the Duquesne provided bill; and f) the bill should include disclosure on fuel sources. OCA St. 5 at 31-34. The OCA submits that Duquesne should be directed to provide revised bill formats in its compliance filing that reflect these proposals. OCA M.B. at 74.

(4) IBEW's Position

Even if the law did not prohibit the Marketers from metering and billing for electric distribution services, IBEW argues the evidence of record in this case demonstrates that it is not in the public interest for metering and billing services to be provided by the Marketers. The Marketers' proposals, therefore, must be rejected. IBEW M.B. at 20.

At the outset, IBEW notes the Marketers' proposals constitute a solution in search of a problem. IBEW witness Moran accurately stated: "This is not a case where regulation doesn't work." IBEW St. 1 at 8. He went on to explain that Duquesne's customers "are receiving high-quality service: service orders are filled on time, metering and billing are performed accurately and on-time every month, payments are processed promptly and accurately, and customers can contact us 24 hours a day, 7 days a week." Id. Simply, there is no compelling reason to change from the current system, where the distribution utility is responsible for all billing and metering functions. IBEW M.B. at 20.

Rather than being interested in "customer choice," it is clear the Marketers want to be able to control the billing and metering process. Enron witness Reising makes that

abundantly clear in his proposed "Distribution Services Tariff." Enron St. 2, PDR-6. This proposed tariff sets out the rules that Enron would like to see govern the relationship between Duquesne (the "EDC" in the tariff), Marketers (the "Customer" in the tariff), and the utility customer (the "End User" in the tariff). Those proposed rules make it clear that the Marketers would be able to choose who serves the customer. Specifically, proposed rule 10.1 states: "The Customer [that is, the Marketer], or at its election, the EDC [that is, Duquesne] shall be the Meter Service Provider and shall provide, own and maintain any meter or meters required in the supply of service." The rules continue, giving the Meter Service Provider the responsibility for reading meters and for rendering bills to End Users (that is, to Duquesne's customers). Id., Rules 11.1 to 11.4. Importantly, there is nothing in Enron's proposed tariff that would allow the End User to decide who provides it with a meter, bill, or other customer services. Under the proposed tariff, that choice rests solely with the marketer. IBEW M.B. at 20-21.

Enron's position is reinforced by the provisions in its proposed "Electric Generation Supplier Tariff" sponsored by its witness Coles. Enron St. 5, LRC-2. That tariff also fails to give Duquesne's customers any choice about who provides them with billing and metering services; instead, the Marketers are the only ones who have any choice. Specifically, proposed Rule 4.5 states: "Suppliers shall be responsible for billing all services to the Customer, including the EDC's charges for Energy Delivery Service, Transmission Service, Ancillary Services and other related charges, unless <u>the Supplier elects</u>: (1) to have the EDC bill its charges separately to the Customer or (2) to have the EDC bill all charges including all of the Supplier's charges." Id. at 6 (emphasis added). In other words, Enron's proposal is to give

the Marketer the choice of billing options. Neither Duquesne nor its customers would have any choice in how Duquesne meters or bills its customers. IBEW M.B. at 21.

IBEW witness Moran discussed these, and other, problems with Enron's proposed tariffs. Mr. Moran concluded that several of Enron's proposals "could result in serious problems with the safety and reliability of electric service to Duquesne's customers." IBEW St. 1 at 3. As he explained, not only would these proposals result in serious coordination problems between employees of Duquesne and the marketers, but those coordination problems could lead directly to unsafe and hazardous conditions within Duquesne's distribution system. Id. at 3-5. Similar problems could be created for Duquesne's customer service personnel in attempting to determine whether termination requirements (among others) have been met. Id. at 7; IBEW M.B. at 21-22.

IBEW submits the Marketers' proposal cannot be adopted. This proposal violates the provisions of the Act. Section 2807(c) specifically states that the customer has "the right . . . to choose to receive separate bills" from the marketer and Duquesne. 66 Pa. C.S. §2807(c). That section also states that if the customer fails to choose to receive separate bills, then Duquesne is responsible for rendering bills for all electric services. Id. Thus, the Marketers' proposal to give themselves the right to choose billing and metering options must be rejected as violating the provisions of the Act. IBEW M.B. at 22.

Enron responded to IBEW's testimony concerning the loss of customer choice by asserting: "The Customer is given the right to choose the Supplier. Different Suppliers may have differing arrangements with the EDC concerning the method of billing." Enron St. 5.1 at 3. In other words, Enron does not deny that its proposal fails to give a customer the right to

choose its billing option. Instead, Enron proposes that the customer's choice of generation supplier should be based on that supplier's billing method. Of course, what Enron fails to mention is the possibility that all suppliers choose the same method of billing customers. If that were to occur, under Enron's proposal, customers would completely lose any right to choose the billing options that Section 2807 guarantees to them. IBEW M.B. at 22.

Simply, then, Enron's proposal fails to give customers the right to choose their billing option. Instead, Enron proposes to give this option solely to generation suppliers. This is not consistent with the requirements of Section 2807 and must be rejected. Id. at 23.

Not only do the Marketers' proposals violate the express language of the Act, IBEW asserts they also would result in unwarranted discrimination among similarly situated utility customers. By giving a Marketer the power to choose whether it will provide billing or metering services to a customer, the Marketer is free to skim off those customers that can be served at relatively low cost; leaving higher-cost customers to be served by Duquesne. IBEW witness Moran addressed these concerns as follows:

> Today, we have a system that ensures that everyone receives electric service of the same high quality. Customers who live in remote areas, who have low incomes, or who have special needs receive the same service at the same cost as customers who live in densely populated areas and make no demands on our customer service personnel. This type of universal service at a uniform price will be in serious trouble if we let other companies pick and choose the customers they want to provide revenue cycle services to. I have no doubt that Enron or NEV or one of the other potential suppliers could provide customer service to ***some*** of our customers at less than our ***average*** cost of providing customer service. So could [Duquesne]. But that's not the point. Right now, [Duquesne] employees are able to provide high-quality customer service to ***all*** of our customers. The monthly customer charge is the same for every customer who takes the same type of service. It doesn't matter if a customer calls us five times a month

> or once every ten years; it doesn't matter where they live or what their income is. The low-cost customers make it possible to serve the high-cost customers at the same price and same high quality. If competitors are allowed to skim off the low-cost customers (higher incomes, fewer demands, living in more densely populated areas), then it will not be possible to continue serving the higher cost customers at the same price, because the average cost will increase significantly.
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> It's similar to the way that the U.S. Postal Service is set up. The goal is to provide a service (first class mail) to everyone at the same price. Of course others could deliver mail in New York City at less than the average, nationwide cost of delivering mail. But those people are not also willing to provide service to rural Montana or Alaska at the same price. Serving the high-cost customers is made possible by the ability to also serve the low-cost customers.
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> Exactly the same thing is true for [Duquesne]'s revenue cycle services. It's possible to provide a full range of customer services - metering, meter reading, billing, collections, and customer service - at the same price to everyone only because we serve everyone. Take away our low-cost customers and the average cost to serve the remaining customers will increase.

IBEW St. 1, Sch. TM-1 at 10-11 (emphasis in original);[350] IBEW M.B. at 23-24.

Simply, the Marketers believe that they should be permitted to bill utility customers for <u>regulated</u>, <u>distribution</u> <u>services</u> at any price they choose - without regard to Duquesne's tariffed rate for providing such service. Under the Public Utility Code, Duquesne would be powerless to respond to the Marketers' efforts to skim off its lowest cost customers. Section 1304 prohibits a "public utility" from discriminating among similarly situated customers or from charging a rate that is either higher or lower than its tariffed rate. 66 Pa. C.S. §1304.

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[350] Mr. Moran's Schedule TM-1 is the testimony of the president of another IBEW local in a different restructuring case. Mr. Moran adopted this testimony as his own. IBEW St. 1 at 2.

See, also, 66 Pa. C.S. §1303, requiring public utilities to adhere to the provisions in their tariffs. But because the Marketers are not "public utilities" they believe that they should be allowed to charge different rates for precisely the same regulated, distribution service. Moreover, the effect of such pricing tactics would be to increase the average cost of serving those customers who are left on the Duquesne system. IBEW M.B. at 24.

The Marketers obviously contend that their proposals would enhance competition and would benefit consumers. In fact, exactly the opposite is true. IBEW witness Moran, testified as follows about the problems that would result, if each Marketer could provide its own meter:

> I am very concerned about what would happen if a customer changed electric suppliers with the frequency that some customers change their long-distance telephone supplier or the supplier of other competitive goods and services. If each generation supplier installs its own meter, then a customer could see frequent changes of his or her electric meter. As I mentioned before, an electric meter is not just an appliance that can be unplugged. The work is potentially hazardous, must be done properly, and should not be done frequently to avoid the possibility of wear or damage to the customer's meter base. Further, there can be considerable inconvenience to the customer of having a meter changed. Depending on the location of the meter, the customer may need to be at home in order to have the meter changed. And in all cases, the customer will suffer a power outage while the meter is being changed. These kinds of outages will be very inconvenient to the customer. . . .
>
> Q. Do you agree with the other witnesses that allowing generation suppliers to provide the electric meter will improve the level of competition to customers?
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> A. Obviously, I am not an economist and I can't point to any studies on this question. But based on some very simple facts and my personal experience, I think that it is more likely that allowing competition for metering will actually result in reducing customer choice for generation supply.

Q. Why do you say that?

A. I am speaking from my experience and the experience of my friends, neighbors, and family. From my experience, many customers do not have a great deal of loyalty to specific suppliers. Many people will go to three or four different stores to buy groceries because of what's on sale. The next week, they'll buy a different set of items and different brands at different stores. Many people will watch the ads and coupons carefully and change their buying habits accordingly. If you get an offer from a long-distance telephone company that looks good, many people will change long distance suppliers, and then change to another supplier when they get a better deal. But customers will not do this if it is expensive or inconvenient to change suppliers. Just imagine how many people would change long-distance telephone suppliers if you had to schedule an appointment, have someone come to your house, lose telephone service for a period of time, and have to pay a substantial charge in order to switch suppliers.

It's also obvious to me that allowing suppliers to provide the electric meter will make it more difficult for smaller suppliers to break into the market. The small wind farm or hydroelectric dam, the factory producing some excess power, and other small power producers would be locked out of the market because they cannot provide metering and billing services.

In other words, it looks to me like having the generation supplier provide the electric meter will result in less customer choice, not more.

IBEW St. 1, Sch. TM-1 at 4-6; IBEW M.B. at 24-25.

IBEW claims these problems are serious. Customers will be reluctant to change suppliers, if it means having to obtain a different electric meter. Safety can be compromised, if the meter is changed frequently or if several different meter suppliers must be contacted before a building can be serviced. Meter installers that are not subject to the supervision and control of a public utility would have to be licensed, and the procedures for such licensing do not exist today. Id. at 26.

What's going on? Why are the marketers proposing a system that is cumbersome, discriminatory, anti-competitive, and inconvenient? Why do they want to inhibit the entry of small suppliers into the generation market and cause serious concerns about the safety and reliability of electric service (both to the public at large and to utility workers)? The answer is money. Like a breath of fresh air, NEV witness Day provided the real reason that marketers want to provide billing and metering services. It has nothing to do with customer choice. As she testified:

> Q. Why is distribution service unbundling an essential element of the restructured energy services market?
>
> A. The simple answer is profitability. Without the unbundling and competitive provision of distribution services, new market entrants will eventually be starved out of the market. This will be the inevitable result when the margins on the sale of electricity are too small to support the new market entrant's service delivery overheads.

NEV St. 2 at 3; IBEW M.B. at 26.

In other words, it will be hard for marketers to make money by doing what the law allows them to do – sell electricity. The profit margins will be small; the market will be very competitive. It will be hard to differentiate one marketer from another. It will be hard to compete head-to-head with efficient energy producers. It will be much easier for marketers to make money if they can also skim off the desirable customers and provide them billing and metering services at less than Duquesne's average cost. And, just to make sure that they can make money by cream skimming, the marketers also want to prevent Duquesne from competing by charging anything other than Duquesne's average cost for billing and metering services. Id. at 26-27.

To be blunt: It doesn't matter to the marketers if it's inefficient, inconvenient, unfair, unlawful, or discriminatory. The marketers will be able to make more money, so it must be a good idea. The Commission should reject the marketers' proposals, and do so in no uncertain terms. There is no reason why the marketers should be allowed to provide billing and metering services. There certainly is no reason why Duquesne should be compelled to allow a marketer to bill a Duquesne customer for the distribution services that Duquesne provides to that customer. Id. at 27.

(5) Enron's Position

Enron explains billing and collection are competitive functions that an EGS should have the option of providing. Duquesne should be required to separate and unbundle its billing and collection functions as part of its restructuring, as the Commission has held it has legal authority to require.[351] Otherwise, customers will be required to pay for the EDC's billing and collection activities even though they choose to receive billing services from their supplier as the Act permits.[352] Enron M.B. at 61-62.

The Commission should further require Duquesne to implement and comply with full customer choice of billing services as part of its restructuring. This objective requires that customers be permitted to choose one of the following billing options:[353]

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[351] Customer Services Order at 10-11. In the recent PECO restructuring case, the Commission declined to require the third billing option "on the record" before it. PECO Energy at 138. We submit the instant record shows the clear benefits and requires a different result.

[352] 66 Pa. C.S. §2807(c).

[353] Enron St. 4.0 at 7.

(1) Single EDC bill. Under this option, Duquesne would provide all billing services - for the services it provides and on behalf of the customer's supplier of choice - including billing for non-wire services and the *generation portion of the bill*;

(2) The Two Bill Option. Under this option, Duquesne would continue to bill for its distribution, transmission and competitive transition charges (i.e., CTC and ITC charges), while EGSs would provide a separate bill for all services the customer chooses to receive from the supplier (including generation services and other non-wire services to the extent the customer chooses to utilize the supplier for such services);

(3) The "Supplier Single Bill" or "Complete Bill" Option. EGSs would provide a single or complete bill in which the EGS would bill not only for the services that it is providing (i.e., generation and, if chosen by the customer, non-wire services) but also for services provided by Duquesne including transmission, distribution, CTC and ITC.

Enron M.B. at 62.

Of the three billing options, the supplier complete or single bill option is the option which allows suppliers to add the most value for customers. The supplier single bill option would enable the provision of service functions such as advanced metering, demand management and all "TLC" customer services, plus a host of as yet unforeseen products and services to fulfill consumer desires. Furthermore, specialized or customized billing can provide or enable detailed information about electric use for customers who choose time-of-use pricing, information about the amount of energy certain appliances utilize, automatic notification to customers when electric use reaches a pre-specified level and many other products and enhancements which customers desire and in which they find value.[354] Id. at 62-63.

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[354] Enron St. 4.0 at 8-9.

Enron finds Duquesne opposes the supplier bill option.[355] Its reasons are somewhat difficult to understand, but apparently center around its alleged experience in the Customer Choice Pilot Program.[356] None of its claims is valid, and they ignore the fact that the very purpose of the pilots is to shake out implementation problems.[357] Id. at 63.

Maybe most important, there is no potential downside to customers that could result from the fully competitive provisioning of billing services. No customer will be required to choose this option; the EGS will be forced to convince customers of the benefits that would result from allowing the EGS to provide non-wire services in addition to generation supply.[358]

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[355] Duquesne St. 8-R at 21

[356] Duquesne makes a big point out of its contention that six of the 17 suppliers participating in the pilot require their customers to adopt the two-bill option. Duquesne St. 8-R at 21-22. The fact that six of 17 suppliers require their customers to adopt the two-bill billing option does not contradict Enron's position, but actually supports it because it shows that billing choices should be permitted. For those customers who do not mind receiving two bills, it gives the EGS the opportunity to provide some other competitive service as a trade-off for receiving two bills. Moreover, if six of the 17 suppliers are requiring the two-bill billing option, that means that 11, or nearly twice as many, are not. Finally, it is interesting to note that Duquesne has provided no information about the six suppliers. Duquesne does not state whether they serve residential customers and what their success in the pilots has been. It does not state whether they have attempted to provide any counter-balancing incentives. One would need to know why they required this and whether it was for purposes of the pilot only or will still be a requirement when direct access begins. In any event, that is what competition is all about. Enron St. 4.1 at 4-6.

[357] Duquesne further claims that the exchange of information with suppliers by electronic media during the pilot has been somewhat problematic. Id. That is the very reason why the General Assembly called for a pilot program - to work out implementation problems. Moreover, Enron witness Muench testified that it was his understanding that a substantial cause of these problems lies with Duquesne. For example, Duquesne was late in distributing its customer lists and its lists did not include customer account numbers. This made it difficult for suppliers to utilize those customer lists accurately and efficiently. Enron St. 4.1 at 6.

[358] OCA witness Alexander also criticizes the supplier bill option because it would lead
(continued...)

Furthermore, any customer who is dissatisfied with any aspect of the EGS's service, would have the right to return to the EDC or switch another EGS.[359] Id. at 63-64.

The ability to obtain all services from competitive providers will maximize the customer's choices - and competition. The customer should have the right to obtain, and the EGS to provide or acquire as agent for the customer, all services, including delivery services. This will enable the EGS to maximize value in all areas; increase efficiencies; and insulate Duquesne from risk of consumer nonpayment by making the supplier responsible for remitting to Duquesne for the service used by the consumer. Moreover, the important element of billing is the obligation to have collections and customer care in accordance with Chapter 56 provisions.[360] From Enron's perspective, this implies that the uncollectible expense must be unbundled from the distribution rates. The key is that with the bill go all of the collection responsibilities. Id. at 64-65.

Enron asserts IBEW's policy arguments against unbundling metering and billing should also be rejected. Its first assertion - that current EDC provision of non-wire services is

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(...continued)
customers back to "bundled" services. OCA St. 5R at 6-9. This is not accurate. Since there will be competition, different suppliers will offer different services that will allow the customer to choose the type of billing he or she wishes. Even if some of those services are bundled, the situation is far different under competitive choice than the bundling that exists under the current regulated, monopoly "single bundle" environment.

[359] The steps needed to implement the three billing services are set forth in Enron St. 4.0 at 10.

[360] Enron St. 4.0 at 12-14.

accurate and prompt[361] – totally disregards the premise underlying the Act that competition will improve, not deteriorate service to customers. IBEW's argument could also be made – and was implicitly rejected by the Commission – with respect to retaining generation as a monopoly-EDC function. IBEW's contention demonstrates only that it does not share the General Assembly's confidence that competition, not regulation, is the best and most efficient method for bringing lower-priced, higher quality service to consumers.[362] Moreover, the Commission makes administrative notice of the thousands of complaint it receives each year from consumers alleging billing errors, slow (or fast) meters, meter reading errors, collection and termination transgressions and numerous other violations of Chapter 56. Clearly, the evidence submitted by Enron demonstrates, given the experience of other industries, that competition improves, not detracts from, the quality of billing and customer services. Enron R.B. at 39-40.

IBEW next argues that Enron's proposal would eliminate customer choice in violation of §2807(c), because the EGS would determine who does the billing and metering.[363] But, as Enron has demonstrated, ultimately it is the end-users who will determine their preferred service provider through their determination and selection of an EGS.[364] If the end-user does not choose to have the EGS do billing and metering, it can select an EGS – including even an

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[361] IBEW M.B. at 20.

[362] 66 Pa. C.S. §2802(5).

[363] IBEW M.B. at 20-23. Again, this is as silly as arguing that consumers will not have "customer choice" because they won't be able to dictate where a particular supplier procures its generation.

[364] Enron St. 4.1 at 7-8; Enron St. 5.1 at 3.

EGS affiliated with the EDC (Duquesne) – who will utilize the EDC to provide such services. IBEW argues that it is possible that all EGS will provide only the same choice.[365] While improbable, if it did occur, it would be because that is what customers want; and if it were a feature not desired by end-user customers, it is virtually certain either that many competitors would offer the choices customers desire. What IBEW fails to recognize is that in a competitive market, customer preferences will determine what choices are available. Such a premise is not only consistent with §2807(c), but is the underlying premise of a competitive market. Id. at 40.

Enron claims IBEW also sets up a straw man, claiming that EGSs would be able to charge any price they want for non-wire services, while EDCs would be required to charge for these services under their tariffed rates.[366] Aside from the fact that this is practically an admission that utilities are overcharging for these services, IBEW ignores the fact that, once unbundled, these services would become competitive, and could be provided competitively by Duquesne or suppliers or even Duquesne's affiliates. Customers would always be able to use utility provided meters, if they wished. IBEW's arguments merely demonstrate its protectionist view of the EDC's business, regardless of whether the approach it advocates is consistent with the Act or beneficial to consumers. Id. at 40-41.

IBEW next throws out safety and reliability warnings if metering becomes competitive.[367] However, Duquesne has already that non-EDC metering does not adversely impact the safety and reliability by contracting out much of its metering services to Itron under

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[365] IBEW M.B. at 22.

[366] IBEW M.B. at 23-24.

[367] IBEW M.B. at 21-25.

which the only protections for maintaining safety and reliability result from a contract between Duquesne and Itron.[368] IBEW's alleged concerns with safety and reliability are no more than a red herring, as Enron's testimony demonstrates.[369] In any event, the General Assembly has spoken otherwise. Id. at 41.

Finally, IBEW has the temerity to challenge unbundling by claiming that the only reason Enron and other suppliers are for it is because it hopes to make money.[370] However, IBEW ignores the fact that no competitive market for any service is possible without a profit motive. The unbundling of and competitive entry into non-wire services will not only provide EGSs with more opportunity to be profitable but will also provide EGSs with more opportunities to add value for consumers. If consumers do not find added value, they will simply go elsewhere for their service or will remain with the EDC. Once its veil is dropped, IBEW's arguments represent nothing more than an attempt to impede competitive development and to protect the EDC from customer choice.[371] Id. at 42.

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[368] N.T. 859-60. Nowhere in its papers has IBEW identified any concerns with the provision of metering services by Itron – a third party provider, which is not even subject to the Commission's jurisdiction as a generation supplier.

[369] Enron St. 2.1 at 6-7; Enron St. 3.1 at 10-13; Enron St. 4.1 at 3-4, 9; Enron St. 5.1 at 3-4. Enron has consistently urged the Commission to maintain existing industry-wide standards for meter and meter reading safety, accuracy, installation, and performance. The introduction of competition will require the Commission to develop additional standards with respect to meter reading including minimum data elements, timely data access, open architecture storage and communications, security, and enforcement procedures. Enron continues to endorse the working group format as the appropriate venue to develop these additional guidelines.

[370] IBEW M.B. at 26-27.

[371] Moreover, Enron believes the competitive provisioning of non-wire services is likely to create many more jobs as utilities and others expand to attempt to provide such services.

(6) NEV's Position

Under the current regulatory system, NEV claims many customers, who receive service on multiple meters throughout an EDU's service territory, are discriminated against when compared to customers with similar loads served through a single meter. NEV St. 1 at 19. In particular, a customer with multiple meters, who is on the same rate schedule and who places the same type of non-distribution related load on the system as a single-meter customer, is being charged more than that single-meter customer. Id. at 19; NEV M.B. at 1-2.

Although the Act is silent on this specific issue, it does give the Commission authority "to approve flexible pricing and flexible rates, including negotiated, contract-based tariffs designed to meet the specific needs of a utility customer and address competitive alternatives." Section 2806(h); See, also, Section 2804(2) ("Customers should be able to choose among alternatives such as . . . flexible pricing. . . ."). Moreover, leveling the playing field for multiple-meter customers is in keeping with the Act's undisputed purposes, among others, of creating a competitive market and promoting economic development in the Commonwealth. NEV M.B. at 2.

In PECO Energy, the Commission exercised its authority to remedy the existing discriminatory billing practices affecting multiple meter customers by approving billing consolidation, such that aggregated customers will be billed based on the load that they place on the system. In its restructuring plan, PECO had defined "customer" to include a single point of delivery. In rejecting that definition, the Commission stated:

> In challenging PECO's position, it was asserted that EGSs should be permitted to treat customers with multiple locations as a single service for purposes of billing for transmission and CTC-related charges. In other words, transmission and CTC-related

> charges would not change with the number of installations or meters, as they currently do, but with the amount of load placed on the system.
>
> PECO's restriction is inappropriate in a competitive generation market because it makes it more difficult with multiple sites to aggregate their load with a single EGS. Accordingly, we shall permit billing consolidation. For administrative ease, billing consolidation should only apply to customers who have multiple meters on the same rate tariff. This change shall not apply to distribution charges because customers with multiple meters may impose a cost on the system that is different than a similar load from a single location associated with the distribution of the service.

Slip Op. at 140 (emphasis added);[372] NEV M.B. at 2-3.

The Commission's decision in PECO Energy is entirely consistent with NEV's testimony in this proceeding regarding the need to eliminate the current discriminatory effect on customers with multiple meters by permitting alternative generation providers to treat these customers as a single service for purposes of billing for transmission and CTC-related charges. NEV St. 1 at 19-20. In particular, when a customer has multiple metering locations, the customer should be permitted to elect to consolidate the bills for any or all of its meters served under the same rate. Transmission and CTC-related charges would not change with the number of installations or meters, as they currently do, but with the amount of load placed on the system. Id. at 20. As stated by the Commission in PECO Energy, for administrative ease, this

[372] The Commission reaffirmed its intention that billing consolidation be implemented in its subsequent Opinion and Order on Compliance Filing, adopted and entered on February 5, 1998, in the same restructuring proceeding involving PECO Energy Company (at pages 12 and 14).

billing consolidation should only be for customers of record, who have multiple meters on the same rate tariff. NEV St. 1 at 19-20;[373] NEV M.B. at 3-4.

Elimination of this present discriminatory effect on multiple meter customers is particularly important now that competition – and the innovation it will inevitably bring – has been introduced into the system. NEV St. 1 at 20-21. More and more customers will be metered so that hourly loads can be determined, enabling consolidated billing. Id. Competition also challenges the necessity of demand-based billing, particularly if customers are paying for the burden they place upon the system virtually on an hourly basis. Id. At bottom, competition highlights the importance of electric prices in economic competitiveness, and eliminates any excuse for the type of blatant discrimination which exists under the current system. Id. Duquesne Light has introduced no evidence against the adoption of consolidated billing. NEV M.B. at 4.

Accordingly, NEV urges the Commission to adopt NEV's proposal that alternative generation providers be allowed to consolidate bills for customers with multiple meters within a single tariff, in accordance with PECO Energy. NEV St. 1 at 21. Only through this modification can the Commission prevent the discrimination that exists under the current system. NEV M.B. at 4.

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[373] The Commission would not need to take action with respect to generation itself because the price of generation is deregulated and the EDU already has the right to issue a customer a bill for its generation services on a consolidated basis. Id. at 17. Nor would this proposed change apply to distribution charges, as the Commission noted in its December 23, 1997 Order in the PECO proceeding, because customers with multiple meters may impose a cost on the system that is different than a similar load from a single location associated with the distribution of the service. Id. Therefore, distribution charges should be billed as they are currently. Id.

(7) **Recommendation**

On the subject of customer billing, the Commission stated in PECO Energy, Slip Op. at 139:

> Section 2807(c) of the Act provides that the EDC may be responsible for billing customers for all electric services while granting the customer the right to choose to receive a separate bill from its generation supplier. The manner and details of the interaction between customers, suppliers, and EDCs are governed by the rulemaking at Docket No. M-00960890, F0011. The Act explicitly specifies a presumption that the EDC shall have the duty to provide a single bill, including competitive generation services, to all customers unless the customer chooses to receive a separate bill directly from its EGS.
>
> Several parties have argued for a "third" billing option that would permit customers to choose to receive a single bill from their EGS that includes billing of the EDC charges. PECO and others conversely maintained that the EDC should be the entity responsible for billing except when a customer elects to receive one bill from the EDC and a separate bill for generation from the EGS.
>
> We recognize there may be potential benefits of such proposals but cannot conclude that it is appropriate to unbundle billing based on this record. Therefore, PECO shall provide all billing services, including billing for generation services, unless a customer indicates a preference to receive a separate bill directly from the supplier for generation services.

Accordingly, Duquesne must provide all billing services, including billing for generation services, unless a customer indicates a preference to receive a separate bill directly from the supplier for generation services. The "third" billing option, permitting customers to opt to receive a single bill from their EGS that includes billing for the EDC charges, cannot be determined on the basis of this record and should await the results of the Commission's generic rulemaking on this subject. Finally, the Commission should permit billing consolidation for

customers with multiple sites to aggregate their load with a single EGS. PECO Energy, Slip Op. at 140.

(ii) Metering

(1) Duquesne's Proposal

The Company finds the main issue here is whether to unbundle metering services, which several intervenors urge the Commission to do. OCA St. 5 at 41-42; MAPSA St. 1 at 42-46; Enron St. 4 at 5-6; Enron St. 1 at 5; Enron St. 3 at 22; NEV St. 1 at 21; NEV St. 2 at 4. These proposals must fail under PECO Energy, Slip Op. at 140 ("As indicated in our rulemaking at Docket No. L-00970120, we do not believe it is necessary to unbundle metering as a competitive service at this time"). Duquesne M.B. at 83.

(2) The OTS' Position

The OTS posits billing and metering costs should also be specifically delineated on the customers bills. These costs are borne by the ratepayers. OTS submits that the generation supplier can offer billing and metering at a lower cost than the distribution company, the ratepayer should have the option of choosing the least expensive alternative. This can only be known and measured by the ratepayer if these costs are unbundled. Once again, unless the Company is concerned that it will lose its customers because the customers will choose a more advantageous billing and metering system, the Company should be willing to unbundle these services. OTS M.B. at 83.

It must be remembered that, if one is committed to competition, the only way that competition becomes effective is if the customers for whom the electric distribution companies compete are fully and clearly advised as to what their alternatives are. This can only be accomplished if the customers know how much each service costs them when provided by the electric distribution company so they can make an intelligent choice as to whether or not they wish their services continue to be provided by that company or by an alternative source. OTS St. 3 at 10; OTS M.B. at 83-84.

(3) The OCA's Position

Upon review of Duquesne's filing, OCA witness Alexander noted that the Company is opposed to unbundling the metering function. OCA St. 5 at 40. At the same time, Duquesne is in the process of significantly upgrading its metering capability with the CARS system, installed by Itron, Inc. As Ms. Alexander explains:

> This system will allow automated communications of the customer's usage and power reliability data via an electronic communications link. As a result of this installation, which Duquesne proposes to be paid for by current customers in the distribution charges, the Company will position itself with a tremendous advantage in marketing electricity and electric services should it choose to do so in the future or if the merger with Allegheny Power is approved.

OCA St. 5 at 41; OCA M.B. at 75.

Indeed, as OCA witness Alexander notes, while the Company recognizes that a customer may have an alternate meter installed, Duquesne will not unbundle any part of its current metering costs. Ms. Alexander states that "this approach is unnecessarily narrow, even at this initial stage of the exploration of the concept of increased competition for meters and

meter services." OCA St. 5 at 41. Therefore, OCA witness Alexander makes the following recommendations: (i) Duquesne's short term policies should be compatible with the possibility of increased competition in metering and metering services; (ii) Open architecture standards should be developed by the stakeholders and approved by the Commission; (iii) Duquesne should be prepared to unbundle the current cost of some features associated with metering and provide a credit to any customer who obtains an alternative meter or whose meter is electronically read by a supplier; (iv) Duquesne should be prepared for installation and billing for alternate meters by suppliers; (v) Standard load profiles used for low use residential and small commercial customers should be updated frequently and approved by the Commission; and (iv) Duquesne has not proposed any charges to provide usage or billing information to suppliers for access to customer-specific usage information, therefore none should be imposed. OCA St. 5 at 41-44. The OCA requests that the Commission adopt these recommendations. OCA M.B. at 75.

(4) Enron's Position

Not only should the choice of who bills the customer be decided by the customer, Enron argues meters should also be provided competitively. Admittedly, meter installation and repair need to be conducted by properly trained personnel in accordance with appropriate standards. But there is no merit to Duquesne's contention that only employees who work for an EDC are capable of being so trained.[374] As noted, Duquesne's present metering system for residential customers has been "outsourced" to a non-utility company. EDC concerns can and

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[374] Duquesne St. 8 at 17-18; IBEW St. 1, Attachment at 2-5).

should be addressed by having the Commission establish minimum qualifications and training for installation personnel and to require EGS services to meet the same service standards as the EDC.[375] There is no reason why EGS personnel cannot perform the meter and billing related services with at the same level of competence and safety as customers presently enjoy.[376] Enron M.B. at 65-66.

In its Customer Services Order, Enron notes the Commission reviewed the provision regarding meter reading under Section 2807(d) of the Act and concluded that all "physical activity" relating to metering should be performed by the EDC.[377] This matter was further reviewed at the Commission's metering docket[378] where the Commission recently issued an order proposing regulations.[379] Both the Commission's Customer Services Order and

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[375] As Enron witness Brown testified, the introduction of competition will require that the Commission develop additional standards with respect to meter reading, including minimum data elements, timely data access, open architecture storage and communications, security and enforcement procedures. These new standards should not dictate the use of specific metering devices, communication protocols employed at the customer site, hardware, software, ownership of meters, or other terms of commercial service agreements. Finally, as the Commission institutes the unbundling of metering service, Enron would recommend that a working group format is an appropriate venue to develop the additional guidelines for interim implementation with permanent standards established in the rulemaking. Enron St. 3.0 at 14.

[376] A similar argument was made - in the years before the break-up of AT&T - that only Bell System employees could do such work. Today, the vast selection available in the purchase of phone equipment, how much more convenient it is to have a phone installed and how phone equipment has improved through innovation is taken for granted.

[377] Customer Services Order at 22-23, 26.

[378] Rulemaking re Advanced Meter Deployment for Electricity Providers, Docket No. L-00970128 ("Advanced Meter Order").

[379] Order entered November 24, 1997.

Advanced Meter Order would appear to allow a competitive EGS to act as the customer's agent to order the EDC to purchase the meter and then read the meter, if it can be done remotely, i.e., nonphysically, so long as the meter is physically installed by the EDC.[380] But the Commission's small step will do little to promote new and innovative meters and meter reading. The Commission's current proposal actually requires the customer or the supplier to buy an "approved" meter for the EDC. This requirement basically denies the ability of suppliers to provide the enhanced meters and meter reading to their customers economically and completely prevents the use of "proprietary" or customized advanced meters that suppliers might themselves wish to provide. It also calls into question the ability of a supplier to offer enhanced and special services -- in the same way that Duquesne itself provides (or plans to provide) with its CARS system. Id. at 66-67.

Although the Commission stated in the Advanced Meter Order, as well as in the PECO Energy, that it will not require unbundling of metering services at this time, it has recognized and anticipates that it may be appropriate to do so in the future after market participants have obtained more experience.[381] At the same time, the Commission continued to recognize that the choice of generation supplier requires the opportunity for customers and

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[380] Customer Services Order at 22-23; Advanced Meter Order at 14-15, 17, 19; proposed regulations Sections 57.252(a), 57.253(b), 57.254(a), (b). The proposed regulations also recognize the ability and right of the EGS to read advanced meters, but propose to keep the physical aspects of metering, including the physical reading, with Duquesne. Since the supplier will have the ability to read the meter remotely, it appears that the only "physical" reading required is the two-year physical examination under Chapter 56 to make sure that a meter is working properly. 52 Pa. Code §56.12(5)(ii).

[381] Advanced Meter Order at 12-13.

suppliers to choose advanced metering equipment necessary to support the new generation services that will be available.[382] Enron urges the Commission, based on the record in this case, to take the next logical step and allow EGSs not only to select the type of advanced meter, but to provide it competitively. Following the Commission's ruling on the legality of unbundling billing and customer service functions, there is no rational or legal reason that would preclude the unbundling and competitive entry into metering and metering functions. The same rationale which allows the unbundling of billing will allow the unbundling of metering. Id. at 67.

(5) Recommendation

On the subject of metering, the Commission stated in PECO Energy, Slip Op. at 140-141:

> As indicated in our rulemaking at Docket No. L-00970120, we do not believe that it is necessary to unbundle metering as a competitive service at this time. However, we do believe that advanced metering offers substantial opportunities for the development of competitive generation products and that this Commission must facilitate development of those products and services. The right to choose a competitive EGS is inherently related to the ability to choose alternative generation services and products made possible by advanced metering. Customers must have a reasonable choice of advanced meters in conjunction with the services offered by their chosen EGS. In our rulemaking, we have outlined the standards and procedures to ensure that customers have real options for competitive metering while retaining all physical work related to metering as a regulated EDC function.
>
> Therefore, all customers may, in conjunction with their EGS, request use of a "qualified meter" that has been approved by this Commission based on the recommendations of a working

[382] Id. at 14-15.

committee composed of interested parties. This Commission will ensure that the list of qualified meters includes all meters necessary to support market services such as two-way communication, remote readings, time-of-use capability, and net metering. While PECO, as a regulated EDC, shall be responsible for all physical work related to the meter, the customer and/or the EGS may select the qualified meter to be used and shall pay as a regulated rate any net incremental cost incurred by PECO as a result of the metering choice.

Accordingly, Duquesne must allow customers the option, in conjunction with their EGS, to request the use of a "qualified meter" that has been approved by this Commission as stated in PECO Energy. As the regulated EDC, Duquesne shall be responsible for all physical work related to the meter and the customer shall pay as a regulated rate any net incremental cost incurred by Duquesne as a result of the metering choice.

2. Agency

(a) Duquesne's Position

Duquesne defines the issue as whether a supplier can act as an agent for the customer and provide a "total electric package," including billing and collection. Enron St. 3 at 13. The proposal should be rejected because: (i) the Act does not authorize this type of agency arrangement and the Commission's Customer Services Guidelines would appear to prohibit it (1997 Pa. PUC LEXIS 42 at *1); (ii) if the supplier were to act as agent, it would have to provide metering and disconnection services, Duquesne 8-R at 22, but under the guidelines only the EDC, Duquesne, can provide metering services for customers, Id. at *1, *51; and (iii) agency is inextricably linked with the single supplier bill option, Enron St. 3 at 13, but the

Commission has not yet endorsed the supplier bill option. Customer Services Guidelines, 1997 Pa. PUC LEXIS 42 at *26; PECO Energy, Slip Op. at 139; Duquesne M.B. at 84.

(b) The OCA's Position

The OCA observes Enron proposed a Supplier Complete Bill Option that would create an agency relationship between the customer and Enron, such that Enron could obtain all of the necessary services on the customer's behalf and provide a single bill for these services. OCA witness Alexander identified several concerns with Enron's proposal, particularly with regard to consumer protection issues. These concerns are discussed in Ms. Alexander's rebuttal testimony. OCA St. 5R at 7-9. For these reasons, the OCA submits that Enron's proposal raises significant concerns that must be thoroughly explored before approval. OCA M.B. at 76.

The OCA observes Enron claims such an offering will maximize a customer's choices and options. Enron M.B. at 64, 68-71. The OCA states Enron's proposal raises a significant number of concerns that must be thoroughly explored before it is adopted. OCA M.B. at 76. OCA witness Alexander explained her concerns with the proposal:

> 1. Ms. Muench proposes that under a Supplier Complete Bill Option, only the supplier would be Duquesne's customer of record. In this scenario, that supplier would be the single point of contact with the customer. This would require the suppler to take complete responsibility for compliance with Commission billing and consumer protection rules, including Chapter 56. According to Ms. Muench, under this approach the supplier would be able to issue an order to the distribution utility to physically disconnect a customer. This option, if implemented as proposed, would vastly complicate the Commission's ability to monitor and assure compliance with Chapter 56 and other consumer protection provisions.

2. Ms. Muench's testimony does not distinguish between disconnection of service for failure to pay for regulated distribution services and the collection remedy of contract cancellation for failure to pay for supplier services, as required by the Commission's Licensing Order.

3. Enron's proposal does not contemplate that customers may want a supplier-only bill, but may not want to select the full agency relationship for all aspects of electric service.

4. The Supplier Bill Option, if not carefully crafted may lead customers unwittingly back to "one-stop" bundled electric services.

OCA St. 5R at 7-9; OCA M.B. at 29.

For these reasons, the OCA submits that this proposal needs to be thoroughly evaluated before it can be implemented, to ensure, among other things, that customers will retain the necessary consumer protections. Thus, Enron's proposal should not be adopted here. Id. at 30.

(c) <u>Enron's Position</u>

Enron observes it is undisputed in marketing circles, regardless of the commodity, that the vast majority of consumers, if given the choice, will seek and subscribe to a provider that can offer a comprehensive service package to the customer. In a competitive market, market pressures will require market participants to provide products and services which meet customers' needs. Enron M.B. at 68.

Given that fact, in the competitive electric generation market, most customers will want their preferred provider to serve not only as their supplier of electricity, but also as their "single point of contact" with the utility. Since transmission and distribution services will remain a monopoly under the Act, in order to ensure that consumers have complete freedom of

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