

PENNSYLVANIA PUBLIC UTILITY COMMISSION
Uniform Cover and Calendar Sheet

1. REPORT DATE: May 12, 1998	2. BUREAU AGENDA NO. MAY-98-OSA-211*
3. BUREAU: Office of Special Assistants	
4. SECTION(S):	5. PUBLIC MEETING DATE:
6. APPROVED BY: Director: C.W. Davis 7-182 Supervisor: A. Arnold 7-8032	
7. PERSONS IN CHARGE:	May 14, 1998
8. DOCKET NO.: R-00973954	DOCKETED MAY 19 1998

9. (a) **CAPTION** (abbreviate if more than 4 lines)
 (b) **Short summary of history & facts, documents & briefs**
 (c) **Recommendation**

(a) Application of Pennsylvania Power & Light Company for Approval of Restructuring Plan Under Section 2806 of the Public Utility Code

(b) On April 1, 1997, Pennsylvania Power & Light Company (PP&L), filed its restructuring plan to implement direct access to a competitive market for the generation of electricity pursuant to Section 2806(d) of the Electric Generation Customer Choice and Competition Act. Numerous parties filed petitions or letters of intervention. The matter was assigned to the Office of Administrative Law Judge per Administrative Law Judge (ALJ) George M. Kashi. Numerous evidentiary hearings and thirteen Public Input sessions were held. The Recommended Decision was issued April 1, 1998. Several parties filed Exceptions and Replies to Exceptions.

(c) The Office of Special Assistants recommends that the Commission conduct a nonbinding Poll of the issues presented by the Exceptions filed with respect to the Recommended Decision of ALJ Kashi.

**DOCUMENT
FOLDER**

10. MOTION BY: Commissioner Chm. Quain Commissioner Hanger - Yes
 Commissioner Rolka - Yes
SECONDED: Commissioner Bloom Commissioner Brownell - Yes

CONTENTS OF MOTION: 1) The Restructuring Plan of PP&L as modified by the body of this Motion, be adopted by the Commission; and
 2) that the Office of Special Assistants, in conjunction with

R-00973954

CONTENT OF MOTION: the Law Bureau, prepare an Order for entry consistent with this Motion.

Note: The Chairman polled the Commissioners on the remaining issue, the phase-in portion of the proceeding, this poll to be included in the Office of Special Assistants preparation of the final Order to be considered at Public Meeting June 4, 1998.

Statements of Commissioner John Hanger attached.
Statement of Commissioner David W. Rolka attached.

PENNSYLVANIA PUBLIC UTILITY COMMISSION
Harrisburg, Pennsylvania

APPLICATION OF PP&L FOR
APPROVAL OF RESTRUCTURING
PLAN UNDER SECTION 2806 OF
THE PUBLIC UTILITY CODE

PUBLIC MEETING-
MAY 14, 1998
MAY-98-OSA-211*
DOCKET NO. R-00973954

STATEMENT OF COMMISSIONER JOHN HANGER

PPL proposes that 33% of the non-coincidental peak load of each tariff class shall have direct access on January 1, 1999, that 66% shall have direct access on January 1, 2000, and that all customers shall have direct access on January 1, 2001. PPL argues that this phase-in schedule is the only one permitted under the Act, and attempts to distinguish this case from the Commission determination in PECO. In PECO, the Commission adopted a phase-in schedule permitting a maximum of 33% of the peak load of each class to be eligible for direct access on January 1, 1999, a maximum of 66% to be eligible for direct access on January 2, 1999, and all customers to be eligible for direct access on January 2, 2000. In this case, PPLICA (a coalition of 19 industrial companies, the U.S. Department of Defense, and the Federal Executive Agencies) and the Competitive Interveners (Enron, MAPSA, NEV, the Pennsylvania Petroleum Association, and the Pennsylvania Association of Plumbing, Heating, and Cooling Contractors) support the PECO schedule as both consistent with the Act and necessary to alleviate competitive disadvantages. PECO agrees with PPL concerning the statutory direction for the phase-in, but argues that the Commission should adopt the same phase-in for PPL as adopted for PECO in order to remain consistent with the reciprocity and fairness concepts of the Act.

PPL argues in its Reply Brief that the phase-in schedule adopted by the Commission in PECO was permissible because the Partial Settlement included the agreement of PECO and other parties to use that schedule. Such a distinction must be rejected. The Commission rejected the Partial Settlement that was an "all or nothing" proposal, so inclusion of any issue resolved in the Partial Settlement provided no basis for the Commission decision in the case. Moreover, it is unreasonable to argue that the Commission can rely on the agreement of the parties to ignore a statutory directive if, as PPL argues, the Act permits only one precise phase-in schedule.

To the contrary, the Commission bases its decision on the precise statutory language, and as PPL concedes, Pennsylvania Courts accord the Commission wide discretion in interpreting the Public Utility Code. We conclude that Section 2806 provides the Commission with the discretion to adopt a phase-in schedule that permits a maximum of 33% of the non-coincidental peak load of each tariff class to have the opportunity for direct access on January 1, 1999, a maximum of 66% to be eligible for direct access on January 2, 1999, and all customers to be eligible for direct access on January 2, 2000. This schedule is in the public interest in order to provide the benefits of direct access expeditiously. Moreover, the schedule is appropriate both to minimize competitive

disadvantages among customers and among EDCs and to facilitate an orderly transition without confusion due to different phase-in schedules for different EDCs in overlapping media markets.

PPL argues that the phase-in schedule adopted in PECO is contrary to the "compromise" supporting passage of the Act. However, this Commission must apply the language that is actually in the Act. PPL provides no support for its argument that its proposed phase-in schedule is more consistent with the Act or more "orderly" than that adopted by the Commission.

Section 2806(b) provides that:

"Recognizing that approximately 5% of the peak load will have retail access through pilot programs, the following schedule for phased implementation of retail access shall be adhered to unless a determination is made by the commission under subsection (c):

(1) As of January 1, 1999, a maximum of 33% of the peak load of each customer class shall have the opportunity for direct access.

(2) As of January 1, 2000, a maximum of 33% of the peak load of each customer class shall have the opportunity for direct access.

(3) As of January 1, 2001, all customers of electric distribution companies in this Commonwealth shall have the opportunity for direct access.

(4) within each customer class, the customers that are eligible for direct access prior to full direct access shall be determined on a first-come-first-served basis unless otherwise determined by the commission ...to prevent competitive disadvantages among similarly situated customers within a customer class."

The plain language of Section 2806(b) does not support PPL's interpretation that the Act provides the Commission with no discretion. Any argument that the Commission has no discretion to adopt a phase in schedule within the parameters of Section 2806(b) ignores the phrase "a maximum of" that directly grants the Commission discretion. As PPL argues in its Reply Brief, rules of statutory construction do not permit an interpretation of the Act in a manner that would render specific language superfluous. If the legislature intended "a maximum of" to mean "exactly", the phrase "a maximum of" would not have been used.

Moreover, this interpretation is further supported by the general rule in subsection (a), "consistent with the commission's discretion under this section." If the Commission's discretion were limited to extending the schedule pursuant to subsection (c), the language in subsection (b) would have provided a precise load for phase-in on a precise date instead of using the phrases "a maximum of" and "as of."

The phrase "as of" does have several meanings in the English language, including "on," "no later than", "by", and "commencing on." However, consideration of the entire statutory language does not support PPL's argument that the language may only be interpreted to mean "commencing on."

Even if the phrase "as of" is interpreted to mean "on," our schedule is fully consistent with the language of the Act. On January 1, 1999, there will be a maximum of 33% eligible for direct access; on January 1, 2000, there will be a maximum of 66% eligible for direct access; on January 1, 2001, all customers will be eligible for direct access.

Similarly, if the phrase "as of" is interpreted to mean "by," our schedule is fully consistent with the language of the Act. By January 1, 1999, there will be a maximum of 33% eligible for direct access; by January 1, 2000, there will be a maximum of 66% eligible for direct access; by January 1, 2001, all customers will be eligible for direct access.

If the phrase "as of" is interpreted to mean "no later than," our schedule is fully consistent with the language of the Act. No later than January 1, 1999, there will be a maximum of 33% eligible for direct access; no later than January 1, 2000, there will be a maximum of 66% eligible for direct access; no later than January 1, 2001, all customers will be eligible for direct access.

In contrast, interpreting the phrase "as of" to mean only "commencing on" requires a conflict with the very provision being interpreted. Section 2806(a) defines a "transition and phase-in period beginning on the effective date of this chapter (January 1, 1997) and ending, consistent with the commission's discretion under this section, January 1, 2001." Section 2806(b) begins with the statement, "Recognizing that approximately 5% of the peak load will have direct access through pilot programs..." Clearly the transition began on January 1, 1997, the effective date of the Act, and the phase-in to direct access began with the phase-in of 5% of customer load during the pilots. Interpreting "as of" to mean "commencing on" would require ignoring the cited provisions.

Lastly, the statutory directive in Section 2806(b)(4) grants the Commission both the discretion and the responsibility to adopt a phase-in plan that "prevents competitive disadvantages among similarly situated customers within a customer class." We conclude that the phase-in schedule that we adopt is the simplest, most effective means to minimize such competitive disadvantages and is in the public interest.

May 14, 1998
DATED

John Hanger
JOHN HANGER, COMMISSIONER

APPLICATION OF PENNSYLVANIA
POWER AND LIGHT COMPANY FOR
APPROVAL OF ITS RESTRUCTURING
PLAN UNDER SECTION 2806 OF THE
PUBLIC UTILITY CODE

PUBLIC MEETING-
MAY 14, 1998
MAY-98-OSA-211
DOCKET NO. R-00973954

STATEMENT OF COMMISSIONER JOHN HANGER

With this decision, the Commission implements faithfully the Electricity Generation Customer Choice and Competition Act for the ratepayers and shareholders of Pennsylvania Power and Light Company (PP&L). It provides the shareholders of PP&L with recovery of \$2.864 billion of stranded costs. That amount is 100% of the stranded costs that have been established to actually exist in the record of this case. These stranded costs will be recovered by a system average 1.783 cents per kilowatt-hour competitive transition charge. Stranded costs will be collected from January 1, 1999 to June 30, 2007.

It cannot be forgotten that the Act requires genuine competition, not just stranded cost recovery. Consequently, the decision also empowers consumers with a system average shopping credit of 3.73 cents per kilowatt-hour in 1999. This shopping credit is slightly higher than the PP&L pilot program, system average shopping credit of 3.58 cents per kilowatt-hour that was established in August 1997.

Given that the pilot program shopping credit has successfully fostered competition for all customers, including residential customers, the system average shopping credit of 3.73 cents will create a genuine competitive market in the PP&L service territory. This robust market will have many suppliers and many buyers of electricity. As a result of the shopping credit, this decision is true to the central purpose and promise of the Act.

Some may ask, why is the shopping credit in this case less than the 4.46 cents shopping credit established for PECO Energy or the 4.01 credit for Duquesne Light Company (DLC). The shopping credit in this case is less, because PP&L's existing rates are less than PECO's and DLC's. The system average bundled rate for PECO, DLC and PP&L are 9.96 cents per kilowatt-hour, 8.93 cents per kilowatt-hour, and 7.21 cents per kilowatt-hour respectively.

In addition to stranded investment recovery and the shopping credit, there are many other important parts to this decision. For example, rate cap protections for customers who do not wish to shop are implemented; expansion of an energy conservation program will occur; expansion of universal service protections for low-income customers are included to meet the universal service goals of the Act; and a massive consumer education effort will be launched.

The consumer education part of this decision is particularly important since customers must have the information necessary to make informed choices for competition to work optimally. Since the changes that this decision mandates are large, a certain amount of confusion and learning is

unavoidable. But with a professional, well-funded consumer education effort, consumer confusion can be lessened. The consumer education effort will have a budget of \$21.62 million that will fund consumer education for the next four years.

By giving customers genuine competition and by giving suppliers incentive to compete for customers, this decision creates incentives that will spur technological innovation in Pennsylvania's electric industry. This innovation as well as the power of choice that will be in the hands of consumers offers new opportunities for environmental improvement. For example, for the first time in decades, consumers are very likely to be offered green power products and access to renewable energy for those customers who want it will increase.

The bottom line of this decision, however, is that it will foster an economic environment that will help job creation and preservation. As such this decision will help families and businesses pay their bills. That makes this a great day and step forward.

May 14, 1998
DATED

John Hanger
JOHN HANGER, COMMISSIONER

PENNSYLVANIA PUBLIC UTILITY COMMISSION
Harrisburg, Pennsylvania 17105-3265

Application of Pennsylvania Power &
Light Company for Approval of its
Restructuring Plan Under Section 2806
of the Public Utility Code

PUBLIC MEETING -
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STATEMENT OF COMMISSIONER DAVID W. ROLKA

I agree with the conclusions contained in the motion, however, on a very limited issue I do so for a different reason. The issue is the allowance for recovery of investment in capacity previously excluded from rates as excess capacity, not used and useful to serve jurisdiction retail customers.

As noted in the motion, prior rate cases did not entirely exclude the capacity from rates. Rather, the Commission determined that PP&L had 945 MW of excess capacity due to the addition of the newly built nuclear plant. The Commission further determined that a rate of return adjustment should be made that was specifically tied to the new plant. The Commission, therefore, disallowed the common equity return on the 945 MW of the plant, concluding that disallowance of a total return on the plant would amount to a penalty on a prudently built plant.

Additionally, the Commission considered and rejected a proposal that would have provided for a deferral of the equity return. I do not support the finding "... that the capacity would be necessary capacity to serve jurisdictional customers, if not for the transition to a competitive market..." However, I find the resultant treatment here to be fairly consistent with prior Commission determinations that intended to deprive the Company only of an equity return on its investment.

May 14, 1998
DATED

David W. Rolka
DAVID W. ROLKA, COMMISSIONER

PENNSYLVANIA PUBLIC UTILITY COMMISSION
Harrisburg, Pennsylvania

**APPLICATION OF PENNSYLVANIA
POWER & LIGHT COMPANY FOR
APPROVAL OF ITS RESTRUCTURING
PLAN UNDER SECTION 2806 OF THE
PUBLIC UTILITY CODE**

**PUBLIC MEETING-
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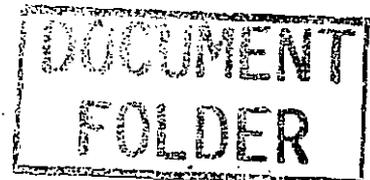
**MOTION OF THE CHAIRMAN AND COMMISSIONERS
TO DISPENSE WITH NON-BINDING POLLING**

On April 1, 1997, Pennsylvania Power & Light Company ("PP&L" or "Company"), pursuant to Section 2806 of the Electricity Generation Customer Choice and Competition Act¹ filed a restructuring plan to implement direct access to competitive electric generation.

The restructuring proceeding conformed to the directive language of the statute, and the Administrative Law Judge ("ALJ") provided our Commission with a record in this case and with a Recommended Decision. After a review of the record in this proceeding, we adopt the PP&L restructuring plan as filed with the modifications set forth in this Motion and the series of Attachments hereto. In those areas where it may be helpful to comment on the reasoning that underlies this Motion, we will offer that commentary. This Motion disposes of the necessity for a non-binding poll with the exception of the issue of phase-in timetable.

In modifying the Company position, we would note that the parties have addressed the issues and that in many instances the parties recommend similar proposals on the basis of the record in this case and consistent with their positions in other restructuring cases. Each case is, of

¹ 66 Pa. C.S. §2801, *et seq.*, Act of December 3, 1996, P.L. 802, No. 138.



course, considered on the basis of its own record but in the light of the requirements of the Act and our earlier decisions.

In considering modifications to the Company's proposal, we are persuaded in several areas by the reasoning of the Office of Consumer Advocate, ("OCA"). We employ their calculations, as a point of departure, but with modifications that will be addressed in this Motion.

For ease of reference, we will provide an Executive Summary which immediately follows this section. We will then briefly address the Recommended Decision. We will then make specific findings ("Commission Findings") followed, where appropriate, by a "Discussion."

Executive Summary

This case presents a substantial discussion of assumptions and modeling directed to predicting the operations of PP&L in a restructured "Customer Choice" environment. We acknowledge and appreciate the efforts of all of the parties to present their different approaches, and we thank them for their effort.

Our point of departure is the presentation of the OCA, using an asset valuation approach. This approach allows us to more easily compare and contrast the various presentations and adjustments, reflecting on the restructuring decisions we have previously made.

The OCA would permit PP&L to recover \$1.08 billion in stranded costs from its customers during the seven year period ending 2005. The CTC for recovery of the stranded costs would be reconciled annually by rate class. OCA computes a combined transmission and distribution rate of 1.7 cents/Kwh. OCA would require the company to provide basic utility

service at a current market rate for generation services. The OCA combination results in a 32% reduction in present rate recovery.

In contrast, PP&L has requested recovery of \$4.04 billion of their claimed \$4.46 billion in stranded costs through 2005. PP&L computes a transmission and distribution rate of 1.8 cents/Kwh. PP&L would compute a market based price for energy and capacity to be applied to each customer's bill. The difference between the market based pricing and the current bundled bill would be used to defray stranded costs after payment of the transmission and distribution charges.

The Commission has rejected both approaches in the past, preferring to compute a transmission and distribution charge and a specific CTC for stranded cost recovery. The residual difference between those charges and the present bundled rate is then available to customers to use as a shopping credit to offset their new supplier charges.

From our review of the record, we believe that the OCA has undervalued the stranded costs of the Company. Our adjustments to their presentation provide for the Company's jurisdictional separations, recognition of the effects of generation based administrative and general costs, and recognition of Company claims for capacity additions, taxes other than income, productivity and the life of the Keystone and Conemaugh generation units. Further, we have accepted the Company estimate of capacity factors for non-utility generation ("NUG"). We have accepted OCA's computation of transmission and distribution charges at 1.7 cent/Kwh, which rejects the Company proposed depreciation reserve swap.

The combination of these adjustments results in a finding of \$2.864 billion in stranded costs. Based upon the record, the law, and guiding precedent, this amount should be recovered over eight and one half years. We have provided for the Company to earn a pretax return of 10.86% on the unamortized balance of stranded costs. This provides a just and reasonable recovery of stranded costs for the company. The system average shopping credit will be 3.73 cents/Kwh in 1999.

The Company has deferred any filing for securitization of their stranded costs pending the outcome of this restructuring proceeding. We believe that securitization of a substantial portion of our stranded cost finding would benefit all consumers and the Company.

The Recommended Decision

While acknowledging the complexity and novelty of each restructuring case, we cannot accept a large part of the Recommended Decision because it is not appropriately consistent with the Act nor with Commission precedent in applying the Act. We understand that the judge did not have the advantage of reflecting upon our decisions in the *Duquesne* and *West Penn/APS* restructuring cases. We do have that advantage, however, and we feel that consistency in application, so far as that is possible in light of the specifics of each case, is very important.

The Recommended Decision is correct that prior Restructuring Orders are not binding precedent in an absolute sense. Each case has a different record and each decision must be made on the record of that case. The parties to the cases have, however, presented many of the same

issues, presented similar testimony, often from the same witnesses, and recommended consistent proposals in each case.

The Commission must ensure that its decisions are consistent with each other for several reasons. The Commission must ensure that utilities, consumers and competitive suppliers are treated fairly across Pennsylvania. An inconsistent result that establishes a restrictive, imbalanced playing field in one service territory while permitting robust competition in another would be *inconsistent with Act, unfair to one Electric Distribution Company (“EDC”), burdensome for suppliers, and unfair and confusing to customers.*

The Recommended Decision sometimes resolves issues without regard to existing Commission direction. In that sense, the Recommended Decision falls short in its stated attempt, “. . . not to break new ground where it was not necessary.” With our experience in the implementation of the Act and the application of precedent, it is incumbent upon us to assure consistency wherever possible.

There are several areas of the Recommended Decision which we specifically cannot accept.

Of perhaps greatest importance, the Recommended Decision does not incorporate the concept of a Shopping Credit, providing no opportunity for customers to save or suppliers to compete during the transition period. Such an approach is inconsistent with the Act and contrary to Commission decisions.

The Recommended Decision would impose a Competitive Transition Charge (“CTC”) as a residual charge that requires a shopping customer to continue to pay PP&L for the embedded cost

of generation. The Act requires the unbundling of the embedded cost of generation. A shopping customer no longer pays the EDC the embedded cost of generation except for a temporary amount, (the CTC) to permit the utility to recover its authorized stranded costs. The Shopping Credit, not the CTC, must be that residual amount.

The Act requires that the Commission facilitate the creation of and transition to a competitive generation market, restructuring the electric industry. In this transition, there are likely to be stranded costs: costs associated with previously used and useful plant now rendered uneconomic by competition. Stranded cost recovery is also a challenging issue and we must take care in announcing the basis for any decision. We cannot agree with the Recommended Decision's conclusion that the Act requires the Commission to grant a utility recovery of 100% of its stranded costs either upon constitutional principles or a "regulatory compact" theory. The decision in this case, however, renders such issues moot because the Commission exercises its discretion and finds it just and reasonable to grant PP&L recovery of its stranded costs demonstrated in the record to actually exist.

The Legislative history of the Act indicates that there is no intent to provide recovery of 100% of a utility's stranded investment. Senator Brightbill, one of the sponsors of the Act, noted that a key difference between the Act and California's statute is that the Act does not mandate 100% recovery of a utility's stranded investment.² Similarly, Representative Tulli, a sponsor in the House of Representatives, said: "... it is important to emphasize that we took pains to do things with this bill that would not mandate the full recovery of stranded investment by utilities,

²180 *Legislative Journal of the Senate of Pennsylvania* 2692 (November 25, 1996).

nor would it prevent them from petitioning the PUC and possibly getting it.”³ The Act is clear that the Commission has discretion but may grant recovery of only a, “just and reasonable” amount of stranded costs.

The “just and reasonable” standard carries over from traditional regulation. Even under traditional regulation, a utility was never entitled to a guaranteed recovery of revenues. Under traditional regulation, rates were set to provide a reasonable opportunity for the utility to earn an anticipated revenue requirement, including an authorized return on its investment.

The Recommended Decision would provide a utility in a competitive generation market a guarantee of recovery of all revenues that are authorized, but not guaranteed, under traditional regulation. In a competitive generation market, such expanded guaranteed revenues are inappropriate. In a competitive market, utilities retain the opportunity to earn a reasonable return on transmission and distribution assets while being set free to earn as much on their investment in de-regulated generation as their efficiency in the market can provide.

Summary of Unbundling, CTC and Shopping Credit

Commission Findings:

Design of the Competitive Transition Charge- The rate of return to be incorporated into the CTC recovery calculation has been argued as part of sharing responsibility. OCA argued that no return should be provided in the CTC calculation and that straight amortization be employed. Conversely, the Company argued for a full, pre-tax cost of capital rate of 13.54 %. We believe

³180 *Legislative Journal of the House of Representatives* 2567 (November 25, 1996)

that a rate of 10.86% should be incorporated into the CTC recovery calculation as just and reasonable given the reduced risk profile of the recovery mechanism versus historic ratemaking.

CTC Reconciliation and Tracking- We adopt the OCA position that the CTC must be reconciled on a class basis. This avoids the potential for intra-class shifting of CTC obligations which would be inequitable and contrary to the Act.

Discussion: PP&L presented its bundled system average rate in 1995 of 7.21 cents/kwh, a rate that is below the average Pennsylvania electric utility rate of 7.93 cents/kwh.

The following Table summarizes the unbundling of existing rates, the Competitive Transition Charge ("CTC") and the Shopping Credit that will be available on a system-wide average basis in 1999 as a result of today's decision. Each customer class will experience somewhat different results that will be finalized upon acceptance of PP&L's filing in compliance with today's decision. ⁴

⁴In the Table, "Unbundled T&D" is the rate for transmission and distribution services that customers now pay and will continue to pay. "Unbundled G" is the rate that all customers now pay PP&L for generation and that only non-shopping customers will continue to pay PP&L for generation. The CTC is a transition period charge that all shopping customers will pay to compensate for stranded costs. The Shopping Credit is the amount leftover that a shopping customer will have available to purchase generation from a competitive Electric Generation Supplier ("EGS").

For Customer Not Shopping: System Average

a. Existing Bundled Rate	7.21 cents/kwh
b. Unbundled T&D	1.7
c. Unbundled G	5.51
d. Total Price Paid	7.21
(d = a = b+c)	

For A Shopping Customer:

a. Existing Bundled Rate	7.21 cents/kwh
b. Unbundled T&D	1.7
c. Unbundled G	5.51
d. CTC	1.78
e. "Shopping Credit"	3.73
(e=a-b-d)	

The CTC was developed to permit PP&L recovery of \$2.864745 billion in stranded and transition costs until June 30, 2007. The amount includes \$1551.78 million for utility generation, \$548.29 (est) million in regulatory assets, that includes \$21.62 million for consumer education, \$128.99 for nuclear decommissioning expense and \$635.69 million for non-utility generation contracts.

Phase-In Issues

Timetable: The timetable for phase-in is to be polled.

Phase-in/ Method of Customer Selection

Commission Findings: We adopt the Judge's recommendation which supports system-wide "first-come, first-served" selection for residential customers, the Office of Small Business Advocate ("OSBA") proposal to split small commercials on a "first-come, first-served" basis, and a pro-rata

subscription for industrial and large commercial customers. In its compliance filing, PP&L shall provide a division of GS-1 and GS-3 classes into large users and small users and provide supporting documentation. Small commercial customers will be enrolled on a first come, first-served basis following the same procedure as residential customers. Large commercial customers will be enrolled following the same procedures as industrial customers, with the participating load of each customer reduced pro rata in the event that its tariff class is oversubscribed. Partial load purchased from a competitive supplier shall be considered first through the meter unless the customer has metering that permits actual load following throughout the course of the day.

Discussion: PP&L proposes that all customer classes be included within each phase-in schedule on a “first-come, first-served” basis with a lottery if any class is oversubscribed. OSBA indicates that PP&L recognizes that full load participation of a customer within a phase-in group could provide it with a competitive advantage compared to similar customers not yet permitted to shop and proposes to review and attempt to resolve such matters on a case-by-case basis. PP&L witness Baumann agrees that the company presents no guidelines or procedures for such a review.

The PP&L Industrial Customers Alliance (“PPLICA”) advocated the same partial load inclusion on a pro rata basis as the industrial groups in *PECO Energy*. OSBA makes a similar proposal for Rate GS commercial classes. Enron supports pro rata industrial and commercial load participation in the event of oversubscription, suggesting that the partial load served by the EGS either should be considered “first through the meter” or following the customer’s load at a fixed percentage throughout the day.

Competitive disadvantages for customers excluded from the earlier phase-in groups is a material concern for commercial and industrial customers, as reflected in the proposals of OSBA and PPLICA. We address the PPLICA and OSBA concerns by applying the PPLICA proposal to large commercial customers and all industrial tariff classes.

We refer the parties to the Tentative Order adopted by the Commission on April 23, 1998, *Proposed Enrollment Procedures Applicable to Electric Distribution Companies and Electric Generation Suppliers During the Phased-In Implementation of Direct Access*. This Tentative Order is presently out for public comment, although a Final Order will be adopted in advance of PP&L's compliance filing. The precise dates and procedures for compliance with the phase-in will be established in the Order accepting the compliance filing.

The ALJ required parties to brief the inclusion of pilot participants in the new phase-in schedules. Pursuant to the PP&L Pilot Order, all pilot participants are automatically included in the first phase-in group to the extent of their pilot load. Thus, "grandfathering" pilot customers is not an issue in this case.

Unbundling of Existing Rates

Transmission and Distribution Service.

Commission Findings: The Delivery Charge, or combined Transmission and Distribution ("T&D") rate, must be identified because it is the combined T&D rate that is subject to the rate cap in Section 2804(4)(I)(b) that requires the total transmission plus distribution rate to be no higher than the capped rate in effect as of January 1, 1997. Separate unbundling of transmission and distribution service is necessary because transmission service is F.E.R.C. jurisdictional and

will be provided pursuant to the PJM Open Access Tariff. Customers may receive transmission service in one of three ways: directly from PP&L; directly from the Pennsylvania-New Jersey Maryland Interconnection ("PJM"); and through their Electric Generation Supplier ("EGS"). No customer must pay more than once for transmission service. PP&L retained all ancillary services as part of the transmission rates, apparently because all ancillary services are included as part of the F.E.R.C. approved open access tariff. We agree with this resolution for the present time.

However, many of these services are in fact provided through the generation function, and F.E.R.C. Order No. 888 contemplates the unbundling of these services to permit them to be procured competitively. Such unbundling will define certain ancillary services as transmission services and others as generation services, but no such unbundling or definition has yet to occur.

The Company proposed an average system rate of 1.8 cents per/kwh for delivery service. This proposal combines federal and state transmission and distribution charges. PPLICA proposed, and the Company accepted, the unbundling of the delivery charges into federal transmission charges and state distribution charges. We accept the PPLICA unbundling, which implements F.E.R.C. approved rates, separating the 1.8 cent per kwh delivery charge into two, unbundled charges for transmission and distribution. The unbundling of these charges is clearly contemplated under the Act and makes perfect sense in a competitive market for generation in which the educated consumer shops for and essentially re-packages his service.

Generation Service

Commission Findings: Section 2804(3) requires the unbundling of existing rates into separate generation, transmission and distribution components. The difference between the existing average system-wide embedded rate of 7.21 cents/kwh and the unbundled transmission and distribution rate of 1.7 cents/kwh is the unbundled generation rate. Non-shopping customers will pay PP&L this unbundled existing generation rate of 5.51 cents/kwh. A portion of this 5.51 cents/kwh existing rate for generation is stranded and recovered by PP&L through the system-average CTC of 1.78 cents/kwh. The remainder of the existing unbundled generation rate, or 3.73 cents/kwh, is the residual Shopping Credit. The Shopping Credit is the portion of the current generation rate that shopping customers will not pay to PP&L. The OCA's proposal to reduce the regulated rate for generation paid by non-shopping customers is rejected as inconsistent with the Act and unsupported by the record. This issue is discussed in greater detail below.

Depreciation Swap

Commission Findings: We adopt the OCA position not to permit the depreciation reserve shift, and the rejection of the PP&L position.

Discussion: PP&L proposes to transfer \$205 million of depreciation reserve from T&D to the production function as a mitigation measure, claiming that doing so will reduce stranded costs by

\$317 million. PP&L indicates that the excess reserves are available because the Commission approved extension of the depreciation lives of T&D facilities in the 1994 rate case.

OCA, the Department of Defense (“DOD”), and the Environmentalists object to this proposal as an anti-competitive cost shifting that inappropriately increases T&D rates. Regulated T&D customers have already funded the higher depreciation reserve and the proposed transfer of the excess reserve to the generation function effectively results in future distribution rates being higher than necessary.

As OCA notes, the inclusion in the Act of the reallocation of depreciation reserves as a potential mitigation measure in no way requires approval of any particular proposed reallocation that is not reasonable. For these reasons, the proposal is rejected. As noted below, retention of the excess depreciation reserve within the T&D function requires a corresponding increase in net book value for generating plant.

Transition and Stranded Costs

Commission Findings: Contrary to the conclusion in the Recommended Decision, the Commission is not required to grant a utility recovery of 100% of its claimed stranded costs upon either constitutional principles or a “regulatory compact” theory. The Act conveys authority to the Commission to approve a competitive transition charge (“CTC”) for the recovery of transition or stranded costs the Commission believes to be “just and reasonable” to recover from

ratepayers.⁵ In this case, we grant PP&L \$2.864 billion, which is 100% of PP&L's net, non-mitigable stranded costs as demonstrated in this record.

We adopt the OCA asset valuation methodology, as modified herein, as the primary analysis upon which to base our approvals for PP&L stranded cost recovery. We note, however, that the amount of stranded costs which we find to be reasonable is recoverable from the ratepayers, only, not from ratepayers and shareholders as the OCA contends.

The "lost revenues" approach is not conceptually sound. Utilities are not "guaranteed" the right to receive any particular level of revenue, or the authorized rate of return, under traditional regulation. We therefore reject as unsound a, "lost revenues" approach or any approach which incorporates guaranteed revenue neutrality, including return on investment, as part of the stranded generation principle amount.

Discussion: Overview- Section 2803 defines transition and stranded costs and provides the framework in which we must assess the various approaches and claims of the parties.

In particular, the definition of stranded costs requires that the costs are: 1) in fact stranded, meaning not recoverable in a competitive market; 2) stranded as a result of the transition to competitive markets; 3) generation related, not transmission or distribution costs; 4) known and measurable; 5) determined over the life of the asset; 6) only a "net" amount; 7) unmitigated; and 8) determined on a net present value basis as of January 1, 1999.

⁵See, 66 Pa. C.S. §§2804(13); 2808. See also, preceding discussion of the legislative history of the Act at page 6, herein.

A summary of recoverable stranded costs for utility generation, nuclear decommissioning expense, regulatory assets and NUG contracts is included as Attachment A. We note that this information is presented for summary purposes only, and that the precise numbers will be adjusted in the compliance filing as accepted by the Commission.

Stranded Utility Generation - PP&L's "lost revenues" Methodology. PP&L proposes to determine its stranded utility generation using a "lost revenues" methodology. Under this approach, PP&L witness Schadt performed a year by year assessment of the revenues that its generation assets would recover under existing rates, including PP&L's authorized rate of return, and compared those revenues to the amount that PP&L anticipated would be recovered by generation assets each year in the competitive generation market. The difference between these figures, the "lost revenues," was discounted to a net present value as of January 1, 1999, using PP&L's after tax weighted average cost of capital of 7.92% as the discount rate. Using this method, PP&L projects that its utility generation plant with a book value of \$3,820.86 million as of January 1, 1999, would result in lost revenues of \$3,494.64 million. This is the amount that PP&L requests for recovery as stranded utility generation.

The OCA and PPLICA used an "asset valuation" method, as adopted by the Commission in *PECO Energy*, *Duquesne*, and *APS/West Penn* to determine the value of stranded utility generation. Under an "asset valuation" method the net book value of the utility's generation plant as of January 1, 1999, is compared to the value of the plant in a competitive market.

We agree with PPLICA and OCA that the “lost revenues” approach is not conceptually sound because utilities are not guaranteed the right to receive any particular level of revenues, including its authorized rate of return, under traditional regulation. Rather, even under traditional regulated ratemaking, rates are designed to provide the utility an opportunity to earn the authorized rate of return. The lost revenues method proposal of PP&L would guarantee PP&L its regulated revenue requirement in the competitive market, even though such revenues were never *guaranteed under traditional ratemaking. The Act requires that we end the regulation of generation, not expand it. The task at hand is to determine stranded investment, not lost revenues.*

We also agree with OCA that the “lost revenues” approach used by PP&L requires other analytical leaps of faith that simply are unsupported under traditional regulation. PP&L’s method assumes perfect regulated ratemaking in each and every year of the remaining useful lives of PP&L’s generation plant. PP&L’s approach assumes that PP&L would have a full rate case each and every year, that the Commission would grant PP&L’s requests precisely, that there would be no regulatory lag, and that PP&L would earn precisely its authorized rate of return each and every year. Traditional regulation has never come close to matching PP&L’s assumption of *guaranteed revenues.*

OCA notes that the, “lost revenues” method, if properly done, can be adjusted to yield the same results because both fundamentally must consider the same assumptions concerning the competitive market, as will be discussed in greater detail below. However, we find no benefit to performing complex adjustments in order to “fix” the lost revenues method when the asset

valuation method may be used directly to determine the impact of the competitive market on the value of a utility's generation plant.

We must determine what portion of the value of PP&L's investment in utility plant will be stranded in the competitive market. We adopt PPLICA and OCA's conceptual approach, consistent with our decisions in *Duquesne* and *APS/West Penn*, because the asset valuation approach directly addresses our task. If this proceeding were intended to guarantee PP&L revenue neutrality as the transition is made to a competitive generation market, there would be no possibility of consumer savings and no development of competition during the transition to competition. Clearly that is not the intent under the Act. Thus, we reject as conceptually unsound a "lost revenues" approach or any approach which incorporates guaranteed revenue neutrality, including return on investment, as part of the stranded generation principal amount.

Since we reject PP&L's "lost revenues" approach as conceptually inappropriate, it is not necessary to review it in detail. However, some discussion is appropriate to reveal why it did not achieve comparable results as the asset valuation methods. In short, PP&L did not utilize the method properly.

First, PP&L assumed earning its authorized return of 11.5% each and every year and grossed up the revenue requirement for federal and state income taxes payable on the return. PP&L's use of the pre-tax rate of return is inconsistent with its use of the after-tax rate of return in discounting the revenue stream to a net present value. As OCA indicates in its Reply Brief, this error is the primary inconsistency that permits PP&L's proposal to bear no discernable relationship to the book value of its plant and greatly overstates stranded costs.

Second, as PPLICA witness Kollen explains, PP&L's method permits recovery of the present value of expenses that no longer exist. PP&L's argument would require consumer payment for income taxes due to equity financing in future years even though the CTC will accelerate the recovery of the underlying generation costs and no such taxes will be due. The taxes in future years beyond the CTC recovery period will never be incurred because the value of the underlying asset already will have been fully recovered during the shorter CTC recovery period. It is taxation that will actually exist during the recovery period that must be considered.

Net Book Value- Because this proceeding must determine the amount of PP&L's stranded investment in utility generation, and not just its "lost revenues," it is necessary to determine the net book value of PP&L's utility generation as of January 1, 1999. PP&L indicated that the net book value will be \$3,820.858 million. However, adjusting for the depreciation reserve swap previously discussed raises this value to \$4017.095 million.

Jurisdictional Allocation as a Component of Stranded Costs

Commission Findings: From the outset, we believe that it is critically important in this restructuring proceeding to consider issues related to unbundling as contemplated by the Act, and the proposed jurisdictional allocation of those unbundled assets. After considering the record in this case, we adopt the Company's jurisdictional allocation.

As we are starting our consideration from the OCA presentation which would remove the property through jurisdictional separation, the property in question must be restored to our calculations through the following adjustments to the OCA presentation⁶:

Net Plant	\$ 659,735,000
Market Value	(336,609,000)
NUG Contracts	4,068,000
Nuclear Decommissioning	<u>20,864,000</u>
Net Adjustments	\$ 348,058,000

Discussion: PP&L has included \$659.7 million in net book associated with plant presently in service to wholesale customers. PP&L includes this amount in its jurisdictional retail book value because the wholesale contracts will expire during the transition period. PP&L indicates that the expiration of the contracts is a fact, providing assurance that the increased book value is known and measurable. PPLICA supports PP&L's statement of the proper jurisdictional allocation.

OCA submits that the associated plant previously was excluded from rates as excess capacity not used and useful to serve jurisdictional retail customers. However, the 1982, 1984, 1994, rate cases did not entirely exclude the subject capacity from rates. A portion of this capacity is already in rates and only the return on the investment has been excluded from rates. In prior rate decisions in PP&L's last rate case in 1994, and more recently in energy cost recovery ("ECR") proceedings, the Commission rejected PP&L's proposed finding that the capacity would be required to serve retail customers when the contracts expire. Instead, the Commission deferred such a decision to a future time when such a determination would be required.

⁶Source: Table D - PP&L Brief

Such a determination is in fact necessary at this point in time, because the instant proceeding is the last in which regulated generation rates will be adopted. Now is the time that a stranded cost determination is being made. We agree with PP&L that the capacity was in fact built to serve jurisdictional customers and would be necessary capacity to serve jurisdictional customers, if not for the transition to a competitive market, and that a portion of the capacity already is included in rates. The previous excess capacity will be needed to meet reasonable reserve levels and to maintain reliability. The transition to competition in fact leaves such investment stranded. Thus, we reject OCA's jurisdictional adjustment.

Construction Work In Progress ("CWIP")

Commission Findings: We adopt the PP&L treatment of CWIP. PP&L points out that the initial values of the OCA do not include CWIP values for property being added in 1997 and 1998. During that time, PP&L expects to add \$108,928,000 to its generating property. The net plant in service of the OCA did not include this value. As this is a known and measurable change it should be reflected in the OCA calculations.

Discussion: All parties agree that the starting point for a determination of the net book value is the plant in service as of January 1, 1999. In its Initial Brief, PP&L indicates that its initial statement of the net book value of \$3,820.858 million includes CWIP that will be in service as of January 1, 1999. OCA agrees that the proper net book value must be determined as of January 1, 1999, to include CWIP in the adopted January 1, 1999, net book value. However, OCA submits

that the \$108.928 million in CWIP is only included in PP&L's Initial Brief, is not in the record of this case, and therefore must be excluded from consideration.

While PP&L's identification of the value of CWIP as \$108.928 million may have been first identified in PP&L's Initial Brief, PP&L clearly requested the recovered amount as part of its initial claim for \$3,820.858 net book value as of January 1, 1999, so no adjustment is required.

Market Valuations of PP&L's Utility Generation

Commission Findings: We find the net book value of PP&L's utility generation to be \$4,017.095 million. This is the number that must be compared to the market value of PP&L's utility generation to determine the amount that will be stranded due to competition. In this proceeding, PP&L witness Jones, OCA witness D. Smith, and PPLICA witness Falkenberg presented studies that forecast future energy prices and the likely dispatch of each unit to ascertain the revenue that can be expected from each plant. OCA and PPLICA offset the expenses necessary to produce those revenues, resulting in a net margin for each plant as a present value as of January 1, 1999, reflecting the price that a willing buyer would pay for each plant on January 1, 1999. The market value is then subtracted from the net book value as of that date to determine the value of stranded utility generation. The OCA and PPLICA method reflects the market valuation methodology that we adopt.

We find that OCA witness D. Smith's analysis presents the most reasonable determination of the market value of PP&L's generation assets in the record of this proceeding. OCA witness D. Smith's testimony is the most credible.

We further find that PP&L witness Jones' projections do not provide an independent, objective or credible result. We also conclude that PPLICA witness Falkenberg's analysis is generally credible, but not more reasonable than OCA witness D. Smith's, and conclude that it provides a useful check that confirms the overall reasonableness of OCA witness D. Smith's result.

Discussion: PP&L witness Jones' study is comparable in scope to that of OCA witness D. Smith and PPLICA witness Falkenberg to the extent that it presents a prediction of market prices for electricity and the dispatch of each plant. To this extent, PP&L witness Jones' study can be compared directly to those of OCA witness D. Smith and PPLICA witness Falkenberg to determine the most reasonable presentation of such issues in the record of this case.

PP&L witness Jones did not, however, complete the analysis to provide a market valuation of PP&L's utility generation. Instead, PP&L compared the projected revenues from each plant with the revenue requirements in current rates, including receipt of PP&L's authorized rate of return. PP&L seeks the difference between the regulated revenue requirement and projected revenues as its, "lost revenues" for which it seeks recovery as stranded costs. As discussed, PP&L's methodology does not provide a reasonable determination of stranded costs.

In addition, Environmentalists' witness Schoengold recommended that the value of PP&L's utility generation be determined through the divestiture of PP&L's generation assets. We reject this recommendation because Section 2804(5) of the Act specifies that the Commission may

permit, but may not require, divestiture of assets as part of a utility restructuring plan. PP&L has not indicated any interest in divesting its generation assets.

A market valuation is based upon a determination of the net margin of revenues that a generating plant can be expected to provide in the competitive market. While other factors can affect a sale price of an asset, the net margin is the basis for determining the price that a buyer would be willing to pay for the asset. In order to determine the net margin, it is necessary to assess the difference between the operating expenses of each plant and the revenues that it can be expected to earn. Many facts and assumptions are necessary to make this determination, and it is the total approach used by OCA witness D. Smith that we find the most credible and reasonable in the record of this proceeding.

Several specific facts and assumption were addressed by the parties. We will highlight several of these.

Fuel Prices

Commission Findings: We adopt the OCA pricing methodology for fuels, fuel price spread, and inflation. The OCA use of the Data Resources, Inc. ("DRI"), published estimates of fuel prices and inflation is a reasonable projection of future conditions. We conclude that the OCA presentation is the most well-founded and credible, and it is adopted.

Discussion: The forecast of fuel price is a crucial component of the market valuation, because it significantly affects the predicted market price of electricity and therefore the net margin of a

generating plant. PP&L witness Jones presented his own fuel price forecast solely for the purpose of presentation in this proceeding. He also provided PP&L's forecast of market prices of electricity. We agree with PPLICA witness Falkenberg's point that it is difficult for the Commission to have confidence that the results of such an exceedingly complex forecast have not been driven by the desire to produce a specific market price result. In fact, the Jones fuel forecast has serious problems. He began with 1996 fuel prices for 1996 that are 20% below actual prices and did not escalate them at all to year 2000 prices, the starting point of his analysis. From the year 2000, he escalated fuel prices at 2.5% annually, assuming that there would be no future occasional spikes in prices as there has been historically. He has therefore forecast declining real fuel prices over the life of the analysis.

In contrast, OCA witness D. Smith used the DRI Spring, 1997, fuel forecast which is a nationally respected objective forecast used by the industry for many purposes external to this case. The DRI forecast used by OCA witness D. Smith is significantly more credible.

A second fundamental issue in projecting net margin is the modeling of market bidding that determines plant dispatch by PJM. A generation unit must recover all of its costs through its market price, including start-up or "no load" costs. PP&L witness Jones does not adequately address this issue.

For all of these reasons, we conclude that OCA witness D. Smith's presentation is the most credible in the record of the case and is adopted.

Adjustments to market valuation

Adoption of OCA witness D. Smith's study establishes an initial determination that the market value of PP&L's generation assets in a competitive market is \$3,044.22 million, as indicated by OCA witness LaCapra. There are several adjustments to OCA's recommendations that have been raised by other parties.

Residual land value

Commission Findings: We reject the OCA's calculations for an escalation in land value used as an offset to stranded costs. Our primary reason for this, beyond computational problems, is that the land value is a portion of the net negative salvage realized from the decommissioning of the fossil unit. As we are not including the fossil decommissioning claim as a stranded cost, we should not include any escalated land value as an offset.

Discussion: In determining the market value of PP&L's generation assets, OCA included a separate value of \$66.09 million to reflect the residual value of the land upon which PP&L's non-nuclear units are situated. We cannot agree that this adjustment is known and measurable and supported by substantial evidence and conclude that PP&L presents several valid arguments in Statement 22-R that support rejection of the OCA proposal.

Keystone/Conemaugh life extension

Commission Findings: We reject the OCA's life-extension assumption, based on the record. We agree with PP&L and subtract \$71.3 million from the OCA's market value of PP&L's utility generation.

Discussion: OCA witness LaCapra, as well as PPLICA witness Kollen, adjust the market value of PP&L's generation by \$71.3 million to reflect additional net margin available from an assumed life extension for PP&L's ownership share in the Keystone and Conemaugh generating stations. They make the adjustment based on the record in the PECO proceeding in which PECO presented a longer remaining book life for its ownership interest in the same plants. OCA and PPLICA suggest that a consistent result is required because the generation unit is the same regardless of different ownership shares or book value.

We agree with OCA and PPLICA that the operating life of a plant, if in fact extended, is extended regardless of ownership shares. However, there is no evidence in the record of this case to support an assumption that the operating life of the plant will in fact be extended. Neither OCA nor PPLICA presents a life extension study or other evidence supporting the assumption. In contrast, PECO presented its own accounting treatment that supports a longer remaining life than does PP&L's. It was PECO that advocated use of the longer useful life without objection from any party.

In this case, PP&L has presented uncontroverted evidence that it is only a part owner of the plants that are operated by GPU and has no ability unilaterally to extend the operating life of

the plants. PP&L also indicates that the various owners of the plants use different useful lives for the plants for ratemaking purposes. For these reasons, we reject the life extension assumption based on the record of this case, and subtract \$71.3 million from the OCA's statement of the market value of PP&L's utility generation.

Plant retirement dates

Commission Findings: We reject the PP&L position. OCA principle witness LaCapra accepted the PP&L retirement dates with the exception of the Keystone and Conemaugh units, while OCA witness D. Smith did not assume any life extension to increase net margin.

Discussion: PP&L argues that the OCA utilizes a second life extension assumption. In determining the net margin that PP&L's plants will provide, OCA witness LaCapra used the plant lives presented by PP&L in all cases except for the Keystone/Conemaugh life extension discussed above. Thus, OCA made no other life extension assumption, and no adjustment is required.

PP&L is in fact arguing that OCA witness D. Smith's market prices for electricity are overstated because his determination of market prices for electricity do not reflect the book life retirement dates of PP&L's plants as incorporated in OCA witness LaCapra's net margin determination. PP&L witness Jones argues that lower priced new capacity will displace existing capacity from the market, lowering the market price. In his view, plant retirement dates, whether early, upon the end of book life, or following a life extension, is a primary determinant of the future market price of electricity. As discussed above, we reject PP&L witness Jones' reasoning.

PP&L argues that OCA witness Smith's market price analysis assumed that PP&L's plants will continue to operate throughout the period of analysis. PP&L argues that the plants should be assumed to retire on their scheduled date of retirement and that the market will provide replacement new capacity that is less expensive.

OCA witness D. Smith did not assume that PP&L's plants would continue to operate beyond their book lives. Smith correctly assumes that the cost of new entry or long-run marginal cost will substantially establish the market price of electricity in the years in question. Plant retirement dates, whenever they are, are not central to this analysis. We agree with OCA witness D. Smith's reasoning based upon basic economic principles.

Thus, PP&L's second, "life extension" argument misunderstands OCA witness Smith's analysis. No adjustment to the market value of PP&L's utility generation is appropriate.

Productivity Factor

Commission Findings: Productivity improvements are likely in a competitive generation market. Here we adopt the PP&L position as supported in the record.

Discussion: In most of its presentation of operating costs, PP&L assumed a 2.5% annual escalation in costs. For administrative and general costs, a component of operation and maintenance expense, PP&L reflected increased productivity of its generation by assuming a reduced cost escalation of 2% annually for each year from 1997-2001. The OCA analysis incorporated PP&L's productivity adjustment, but OCA witness LaCapra assumed an additional productivity improvement by reducing the OCA cost escalation factor by 0.2% annually for the

remaining lives of the plants. We agree that productivity improvements are likely in a competitive generation market and have adopted productivity adjustments in the other restructuring cases. In this case, however, OCA has not substantiated its proposal that its additional productivity adjustment is reasonable beyond that already proposed by PP&L and incorporated by OCA. Elimination of this additional OCA productivity adjustment decreases the OCA's statement of the market value of PP&L's generation by \$66.2 million.

Administrative and General Expense

Commission Findings: We adopt the Company position on Administrative and General Expenses.

PP&L addressed the OCA analysis on this point and states that the OCA analysis does not properly incorporate the impact of administrative and general expenses allocated to the production function. We agree that the full amount of A&G expense must be included as an operating cost to determine the net margin of PP&L's utility generation.

Discussion: PP&L argues that the generation portion of its A&G expense, totaling \$402.691 million, must either be added to stranded generation, permitting recovery as a stranded cost as part of the OCA market valuation, or returned to T&D and recovered through regulated rates. PP&L argues that the OCA approach essentially disallows recovery of these costs. PP&L notes that PECO allocated most of its A&G expense to T&D, while the Commission reallocated a portion of the A&G expense to generation instead, reducing the T&D rate and increasing the resulting utility generation stranded costs. We agree with PP&L that the full \$402.691 million

must be included as an operating cost used to determine the net margin of PP&L's utility generation.

Capital additions

Commission Findings: We direct that the treatment of capital additions be consistent with IRS guidelines, and that the OCA market value be reduced by \$165,318,000.

Discussion: PP&L, as part of its projections, has included capital additions to its generating facilities for their remaining life. The OCA has recognized these additions as expenses in its analysis, but the OCA treatment is in conflict with treatment of these additions for tax purposes. By treating these additions as expenses, a full deduction is taken for tax purposes in the year of the addition. The property, however, will have to be amortized for tax purposes under IRS tax depreciation guidelines. The OCA treatment, as proposed, creates an overstatement of net market revenue by overstating the tax deductions.

In its determination of stranded utility generation, OCA witness La Capra treats the expense of capital additions and the offsetting tax deductions as net expenses in the year in which they are incurred. PP&L argues that the tax deductions are in fact not available in the year of the expense, but only in later years. PP&L argues that OCA's approach therefore understates the actual cost of capital additions by overstating the impact of the associated tax deductions. We agree with PP&L. OCA's determination of market value should be reduced by \$165.3 million to reflect the actual timing of the expense and the related tax deductions.

Taxes other than income

Commission Findings: PP&L incorporated the capital stock and Public Utility Realty ("PURTA") taxes at their 1996 level, escalated at 2.5% over the life of each generating facility. PP&L is not assuming a tax rate increase, but an escalating tax revenue increase as the value of its assets escalates over time. We find PP&L's assumption more reasonable than an assumption that tax revenues would remain flat or decline, and therefore adopt an adjustment of \$133.795 as an increased operating expense in OCA witness La Capra's determination of net margin.

Accumulated Deferred Taxes

Commission Findings: The OCA accumulated deferred tax adjustment to its market value calculation must be adjusted to correct a beginning balance and provide for a jurisdictional separation.

Discussion: As part of its presentation on market value, the OCA has included an adjustment to reflect the 1999 balance of accumulated deferred taxes. This adjustment appears to attempt to reflect the historic Pennsylvania P.U.C. practice of offsetting rate base by the accumulated deferred tax balance. PP&L in its regulatory model also reflected this historic practice. This is a primary reason for a difference in perceived values between the OCA and PP&L from their methodologies. This offset reflects the concept that the source of the asset as part of the capitalization of the company is not from shareholders but from tax timing benefits. Our treatment of this asset is to provide for its recovery in the regulatory assets of the company, rather

than the generating plant assets. PP&L has argued that the value of OCA's accumulated deferred tax adjustment must be modified to reflect their market value adjustments in Table D of their Brief. That is a presumption that the source of recovery of the asset is from the market and stranded transactions. Since the recovery is from the regulatory assets, no market value adjustment is necessary under the OCA proposal. However, adjustment of the OCA proposal is necessary to reflect an incorrect 1999 beginning balance and jurisdictional assignment. An adjustment of \$76 million is being made to reduce the accumulated deferred tax balance for 1999 to reflect PP&L's Exhibit JRS-1a revised stranded cost claim and to provide for a jurisdictional separation of the balance.

Jurisdictional Allocation

Commission Findings: As discussed, we reject OCA's exclusion of capacity as wholesale contracts expire. Since we are including the book value of this capacity in our jurisdictional allocation of stranded costs, it also is appropriate to include the net margin that will be derived from the additional capacity in determining the market value of PP&L's utility generation. OCA's market value did not include this capacity. It is therefore appropriate to use the full jurisdictional allocation, increasing market value by \$336 million (est).

The value of some of the other recoverable stranded costs must be adjusted as well to reflect the appropriate jurisdictional allocation.

Summary of stranded utility generation:

Net Book Value	\$3,820.86 million
Depreciation Swap	+ <u>196.868</u>
TOTAL	\$4,017.095

Market Value	\$3,044.22 million
Life Extension ⁷	71.3
Productivity Factor	66.2
A&G expense	402.791
Capital Additions	165.3
Taxes Other Income	133.8
Jurisdictional Allocation	(336.61) (est)
Deferred Tax Adjustment	<u>76.2</u>
TOTAL	\$2,465.35

Utility Stranded Plant \$1551.765 million

Decommissioning Expense

Nuclear decommissioning expense

Commission Findings: Section 1 of the definition of, “transition or stranded costs” provides for full recovery of the unfunded portion of the utility’s projected nuclear generating plant decommissioning expense, and Section 2 provides that the Commission may find it just and reasonable pursuant to Section 2808(c)(3) of the Act to permit recovery of stranded non-nuclear plant retirement costs. It is incumbent upon this Commission to ensure full recovery of nuclear decommissioning expense pursuant to federal law, the Act, and basic health and safety concerns.

⁷Keystone and Conemaugh

We agree with OCA and PP&L that the stranded cost methodology is appropriate and adopt OCA's calculation, as adjusted to incorporate PP&L's jurisdictional allocation.

Discussion: PP&L indicates that the jurisdictional annual nuclear decommissioning expense is \$9.5 million and does not claim any current under funding or other adjustments to the contribution rate. PP&L initially includes the same \$9.5 annual decommissioning expense as on ongoing operating expense that is considered as part of the market valuation of utility nuclear generation. Thus, in its first proposal, nuclear decommissioning expense is part of the company's claim for stranded utility generation, and there is no separate recovery needed for ongoing nuclear decommissioning expense.

OCA witness Catlin recommends no specific changes to PP&L's claim, but separately identifies the nuclear decommissioning stranded cost as contemplated under the Act. OCA did not include the nuclear decommissioning expense as part of its determination of PP&L's stranded utility generation. Excluding the OCA jurisdictional allocation that we reject, the resulting stranded nuclear decommissioning cost has a net present value of \$128.9 million (est).

As a preferred alternative, however, PP&L proposes recovering decommissioning expense as a per kwh distribution charge for the duration of the useful lives of its nuclear facilities. Under this approach, PP&L would retain existing ratemaking treatment, with \$9.5 million of jurisdictional funding allocated to each class on a demand basis and calculating the charge on a per kwh basis.

PPLICA and OCA oppose the annuity method, arguing that no net consumer savings result and that it is preferable for ratepayer responsibility for nuclear decommissioning to end upon the conclusion of the transition period. The alternative proposal is not necessary in order to permit reasonable recovery of stranded costs while providing adequate opportunities for the development of a competitive market.

The Environmentalists opposed PP&L's proposals, arguing that PP&L must have an incentive to minimize nuclear decommissioning costs.

Fossil Decommissioning

Commission Findings: Section (3)(iv) of the definition of, "transition or stranded costs" in Section 2803 permits the recovery of non-nuclear plant retirement costs pursuant to the Commission's discretion under Section 2808(c)(3). PP&L does not request recovery of any stranded non-nuclear plant retirement costs that are presently included in rates. PP&L has not met its burden to prove that any particular future retirement cost is a recoverable stranded cost. PP&L has not presented any actual retirement plans, documented any known and measurable decommissioning expense that meets normal ratemaking standards, demonstrated that the costs would be recoverable under traditional regulation, demonstrated that the cost will in fact be stranded, or demonstrated that the costs will be non-mitigated. PP&L's claim therefore does meet the basic requirements for stranded cost recovery and must be rejected.

Discussion: PP&L does not seek direct recovery of any existing fossil decommissioning expense already included in rates as a separate stranded cost. Instead, PP&L incorporates a net present value of \$315.867 to reflect an operating expense for future fossil decommissioning expenses in the year of plant retirement and the subsequent two years. This operating expense is part of PP&L's determination of the lost revenues approach in the valuation of its stranded utility generation. PP&L argues that the Act requires recovery of such costs. Nothing in the Act requires recovery of fossil decommissioning costs that do not yet exist either as stranded costs or as a component of the calculation of future plant operating expense. Unlike nuclear decommissioning costs that are already included in rates, the possible future fossil decommissioning expenses are not already incorporated into rates.

Under traditional regulation, fossil decommissioning expense may be recoverable when the cost is incurred for the actual retirement of a plant. PP&L is correct that *Penn Sheraton* does not stand for the proposition that fossil decommissioning costs may not be recoverable under traditional ratemaking. Both *Penn Sheraton* and long-standing Commission precedent, however, preclude a present determination of recovery of prospective, speculative decommissioning expense. In order to be recoverable under traditional regulation, the cost must be known and measurable and actually incurred. PP&L has not met its burden to prove that any future fossil decommissioning expense will exist at a particular date and in a known and measurable amount. The Commission explicitly rejected PP&L claim for future fossil decommissioning expense in its last rate case, and essentially the same claim must be rejected now.

Our rejection of future fossil decommissioning expense is consistent with our rejection of an assumption that plant lives will be extended.

Prospective fossil decommissioning expense does not meet the standards for present incorporation into rates. As indicated in *PECO Energy, West Penn/APS, and Duquesne*, the traditional ratemaking standards for fossil decommissioning expense are clearly distinguished from those applicable to nuclear plant decommissioning. Nuclear plant decommissioning expense is already included in rates, is federally mandated for urgent public health and safety reasons, and is required under the Act. Future fossil plant decommissioning is neither federally mandated nor urgent for public health reasons, and is not required under the Act.

Regulatory Assets and Liabilities

Commission Findings: We adopt the position of the OCA as adjusted herein. PP&L presented a claim for regulatory assets on a net present value basis as of January 1, 1999, totaling \$384 million. During the course of this proceeding, PP&L revised its claim to \$354.326 million. PPLICA argues that PP&L has a net regulatory liability of \$55.588 million. OCA recommends recovery of net regulatory assets of \$259.249 million.

Deferred Fuel

Commission Findings: We will permit the recovery of \$76.815 million in net present value of deferred fuel expense.

Discussion: PP&L has claimed \$76.815 million in net present value of deferred fuel expense.

This amount reflects actual under recoveries for 1996, claimed under recoveries for 1997, and claimed under recoveries for 1998. The principle arguments against the claims were provided by the OCA and PPLICA, who would deny the 1997 and 1998 requests as not known and measurable. A major element of the claimed amounts is payments to fifteen non-utility generators operating on the PP&L system. These payments have been fully recovered under Pennsylvania ratemaking in the past in accordance with the Public Utility Regulatory Policies Act of 1978 ("PURPA"). These payments are also requested for recovery as a separate item for the post January 1, 1999. In PP&L Exhibit JMK 6, a full detail of these expenses updated to June, 1997, is provided. Unlike *PECO Energy*, where all NUG expenses were claimed to be at market, such is not the case with PP&L.

Therefore, in order to assure the recovery of NUG costs, we will permit the recovery of the claimed regulatory asset for deferred fuel at the level proposed by PP&L.

Employee transition and pension costs

Commission Findings: There are three components of PP&L's claim for employee transition and pension costs and an additional claim for an offsetting regulatory liability raised by PPLICA.

PP&L claims Voluntary Early Retirement Program, FAS-106 post-retirement benefit costs other than pensions, and employee severance and pension expenses.

VERP

In the 1994 rate case, the Commission allowed amortization of a Voluntary Early Retirement Program ("VERP") annual expense of \$13.132 million over 5 years, while reducing the related employee expenses included in base rates. No party challenges recovery of this previously authorized amount as a regulatory asset with a remaining net present value as of 1/1/99 of \$14.085 million.

FAS-106

PP&L claims a net present value of stranded FAS-106 post-retirement benefit costs of \$8.730 million. In 1993, PP&L changed from a cash basis to an accrual basis for SFAS 106 employee retirement benefits other than pensions. In the 1994 rate case, the Commission approved the change and permitted PP&L to defer the additional expense for amortization over a 20-year period. All parties agree that PP&L is entitled to recovery as a regulatory asset of \$8.73 million to reflect the present value of the unamortized balance as of December 31, 1998.

PPLICA argues that there is an offsetting regulatory liability of \$53.99 million to reflect the interest earned on trust fund balances which must be credited to ratepayers. PP&L makes no claim for the interest on trust fund earnings in this case. PP&L already has included recognition of such earnings in its formulation of the claim. Therefore, we reject the need for any additional adjustment.

Pension Overfunding

Commission Findings: The Commission adopts the OCA valuation which already includes reduced future pension expense.

Discussion: PPLICA argues that PP&L's pension plan is over funded by ratepayer contributions and that the Commission should reflect an associated regulatory liability. PPLICA presents the value of PP&L's pension fund as \$1,187.224 million as of December 31, 1996, with an accumulated benefit obligation of \$694.986 million and a projected benefit obligation of \$886.704 million, resulting in a regulatory liability of \$253.832 million as of December 31, 1998.

In *PECO Energy*, the Commission initially agreed with the industrial customers to recognize a regulatory liability to ensure that overfunding is credited to ratepayers since overfunding eventually would be reconciled to ratepayer benefit under traditional regulation. However, upon Reconsideration, the Commission reversed the initial resolution of this issue. The Commission concluded that recognition of pension overfunding could be recognized as a regulatory liability, but that it was inappropriate to do so in that case because the utility generation valuation methodology adopted by the Commission already incorporated the adjustment as a reduced future operating expense. Similarly, in this case, the Commission adopts OCA's valuation that already includes reduced future pension expense. This treatment increases the value of PP&L's generation, providing full credit to ratepayers as reduced recoverable utility generation stranded costs. Thus, no additional adjustment is appropriate.

Employee Transition Costs

Commission Findings: We accept PP&L's employee severance and pension expenses, but agree with PPLICA that the incremental cost of \$5.502 is the recoverable amount.

Discussion: PP&L requests recovery of additional projected 1997-2001 employee severance and pension expenses. PP&L claims a 1997 expense of \$5.014 million; 1998 expenses of \$6.782 million; 1999 expenses of \$4.157; 2000 expenses of \$3.118; and 2001 expenses of \$4.211 million. In formulating this claim, PP&L assumed a 5 year amortization of each year's costs, brought to a net present value as of January 1, 1999, and allocated a portion to generation, resulting in a total claim for \$17.106 million.

PPLICA argues that the entire claim should be rejected as highly speculative because PP&L did not document any specific plan for employee reduction during 1997-2001, precluding a finding of any known and measurable amount of the expense. OCA argues that a portion of this claim is covered by the previous retirement incentive programs.

Section (3)(v) of the definition of "transition or stranded costs" in Section 2803 includes, "costs of employee severance, retraining, early retirement, outplacement and related expenses, at reasonable levels, for employees who are affected by changes that occur as a result of the restructuring of the electric industry occasioned by this chapter." While we agree with PPLICA and OCA that PP&L's claim is not documented as well as perhaps it could be, the employee severance costs are clearly recoverable as a transition cost. PP&L's claim is not for past expenses covered by the 1994 rate order; it is for additional employee severance expenses as a result of the transition to a competitive generation market.

Both PPLICA and OCA argue that the pension plan is over funded in any event, so any recoverable amount would be limited to the incremental cash expense not presently covered in rates. As discussed, the Commission has separately considered the reduced operating expense that results from PP&L's employee transition plan as part of PP&L's productivity improvement, and rejected OCA's proposed additional productivity adjustment. Granting the full cash expense would effectively grant PP&L double recovery for the same productivity improvement. Assuming that the Commission allows the expense, PPLICA calculates the actual incremental cash expense as \$5.502 million.

DOE Assessments

Commission Findings: The 1992 Energy Policy Act Amendments to the Federal Power Act impose an assessment on utilities for Department of Energy expenses for decommissioning of its uranium enrichment facility. PP&L seeks recovery of \$16.361 million as a regulatory asset after agreeing with PPLICA and OCA that its initial claim would provide double recovery because the expense was also included as part of the operating expense of the Susquehanna nuclear plants in PP&L utility generation valuation. PP&L eliminated the claim from its stranded generation request and seeks recovery as a regulatory asset. We agree with PPLICA and OCA that the expense is properly considered as a fuel expense since that is how it is reflected on PP&L's books. Double counting would be inappropriate in any event. Since we adopt OCA's utility generation valuation methodology that considered the expense, no adjustment is necessary and we reject additional recovery as a regulatory asset.

Susquehanna deferred refueling expenses

Commission Findings: We find that there is no regulatory asset requiring additional recovery under this category.

Discussion: PP&L seeks recovery of a jurisdictional amount of \$7.996 million as the net present value of incremental O&M expenses during refueling and inspection outages. PP&L argues that under current ratemaking approved by the Commission since 1983, PP&L has deferred recognition of such expenses and amortized the prior expense until the next episode.

PPLICA, OCA and OTS argue that the Commission has never granted PP&L the authority to defer these costs and that no regulatory asset exists. Under traditional ratemaking, the expense is not a deferred regulatory asset for special amortization, just recoverable as a normalized expense through base rates. The 1983 Order approved only the right to seek recovery of the expense, which has never been included as an additional component in rates since that time. In the 1994 rate case, the expense was normalized as an annual expense and incorporated into base rates. There is no regulatory asset requiring additional recovery.

Net FAS-109 Taxes Recoverable

Commission Findings: We grant PP&L's revised claim as adjusted for our CTC recovery period on a net present value basis for a value of 397.6 million.

Discussion: During the development of the record in this case, all parties agreed that PP&L has a regulatory asset for SFAS-109 recoverable taxes that reflect tax benefits that already have been flowed through to ratepayers although PP&L still will have to pay the underlying taxes in the future. All parties also agreed that PP&L has an offsetting regulatory liability for FAS-109 Investment Tax Credits that have already been obtained by the company but have not yet been flowed through to ratepayers.

The value of the regulatory asset is not the revenue requirement pursuant to a taxing and ratemaking reimbursement that no longer exists. Instead, the value of the regulatory asset and the amount that consumers should pay PP&L is the net present value of the tax obligation that must be paid now that the recovery period has changed. It is the different tax consequences of the CTC recovery period that changes the value of the regulatory asset.

No party disagrees that the timing of taxes due to the government and payment to PP&L by consumers changes as a result of the end of regulated generation rates. The period for both payment of taxes to the government and reimbursement from ratepayers previously extended over a period of up to 30 years, while it is now being compressed into the duration of the CTC recovery period. The tax benefits, “reverse” at an earlier date to match the compressed CTC recovery period. This fundamentally changes the revenue requirements of the regulatory asset under traditional regulation.

PP&L’s initial claim for the SFAS-109 regulatory asset did not consider the changed revenue requirement of the SFAS-109 claim. PP&L’s initial claim therefore was significantly

understated, is inaccurate, and must be rejected as a basis for the recoverable asset notwithstanding the acceptance of the claim by PPLICA and OCA.

The correct claim must incorporate the reversal of taxes over the CTC recovery period. We therefore grant PP&L's revised claim of \$397.6 million based on its presentation in PP&L St. 8-R at 16-17.

1994 Rate Case Expense

Commission Findings: PP&L claims a regulatory asset of \$184,000 to reflect the unamortized balance of its 1994 rate case expense. That claim is rejected as a regulatory asset.

Discussion: As OTS and OCA argue, the 1994 rate case authorized recovery of a four year normalized rate case expense that is incorporated into existing rates, not deferral and amortization of a single rate case expense. In that case, PP&L did not object to normalization, only arguing that a shorter period should be used. Under traditional regulation, the Commission has routinely normalized rate case expense since 1980. PP&L's accounting treatment of rate case expense as an amortization is not relevant to ratemaking treatment. The claim is rejected as a regulatory asset.

Consumer Education

Commission Findings: Approved consumer education expenses pursuant to the Commission's Consumer Education Order and this decision are recoverable as transition costs. However, the

record provides no useable calculation of the expense. For purposes of this decision, we assume a consumer education budget of \$5 per residential customer for each of four years, for a total budget of \$21.62 million. This figure will be adjusted in the Commission’s compliance filing Order to reflect the approved consumer education plan.

Unchallenged Regulatory Assets

Commission Findings: PP&L also requests regulatory asset recovery for Common Plant in the amount of \$7.783 million, Susquehanna Early Window Costs in the amount of \$9.83 million, and Retired Miner Healthcare Costs in the amount of \$6.308. No party challenges these claims and they are granted.

Summary of Net Recoverable Regulatory Assets and Liabilities

Unrecovered Energy Costs	\$ 76.815 million
Employee Expenses	
VERP	14.09
FAS-106	8.73
Employee transition	5.502
FAS-109 Taxes	397.6
Consumer Education	21.62
Common Plant	7.783
Retired Minors Healthcare	6.308
SSES Early Window	9.83
 TOTAL	 \$ 548.278 million

Non-Utility Generating Contracts (“NUGs”)

Commission Findings: PP&L requests \$656.87 million in stranded costs for NUGS, including the costs of two buyouts. OCA values the claim at \$574.708 million and PPLICA values the claim

at \$556.30 million. OCA would use its forecast of market prices instead of PP&L's in determining the stranded cost. Since we adopt OCA's market price forecast as the most reasonable in the record of this case, OCA's market prices should be used in valuating the stranded costs of NUGs as well. For this reason, we use OCA's valuation of the NUG stranded cost of \$574.708 as the starting point for our determination.

OCA also would use its jurisdictional allocation. However we adopt PP&L's jurisdictional allocation, requiring an increase of OCA's stranded NUG costs in the stranded NUG cost of \$4.068 million. The OCA also adjusted PP&L's capacity factors for its NUGs. We also find that the PP&L's estimate is acceptable.

Discussion: PP&L assumed the actual capacity factors experienced over the 1994-1996 period to formulate its claim. OCA argues that the actual output experienced is very high and unlikely to be maintained over the long-run. OCA witness LaCapra assumes an 80% annual capacity factor for NUGs. While OCA may be correct that the NUGs may not be able to maintain their historic performance, there is no factual support in the record to assume capacity factors reduced to 80%. Therefore, the value of PP&L's stranded NUGs is increased by \$56.911, resulting in a total recoverable claim of \$635.687 million.

The Anthracite Region Independent Power Producers Association ("ARIPPA"), Gilberton Power Company, and Schuylkill Energy Resources argue that the determination of recoverable NUG contracts costs as stranded costs in this proceeding provides an economic incentive for PP&L to engage in, "contractual gamesmanship." In Exceptions, ARIPPA notes that the

Recommended Decision ignored the testimony arguing that PP&L will receive stranded costs related to the NUG contracts regardless of the actual power purchased. ARIPPA indicates that the NUGS only get paid based on actual power generated and delivered to PP&L, providing PP&L with an incentive to undermine the contracts or minimize delivered amounts, thereby permitting PP&L to retain the stranded cost without incurring the associated expense.

ARIPPA requests use of a separate reconciliation mechanism to ensure that PP&L actually purchases NUG power in an amount consistent with its related stranded cost recovery. We accept the legitimacy of ARIPPA's concerns. We caution PP&L not to permit ARIPPA's concern to become a reality.

Section 2808(a) does specify that, "The recovery of transition or stranded costs associated with existing generating facilities is contingent on continued operation at reasonable availability levels of the generation facilities for which recovery is approved" This section does not limit applicability to utility generation. If a NUG facility for which PP&L is recovering stranded costs does not operate at reasonable levels for which recovery has been approved, the contingency will have been violated. Under such circumstances, the Commission would have the authority to take appropriate action.

Cost of Capital

Commission Findings: In the absence of full recovery on January 1, 1999, PP&L agrees with our methodology in *PECO Energy* that the company should receive a return on the unamortized

principal balance of recoverable stranded costs. This is the method we adopt for calculation of PP&L's return related to its stranded costs.

We find that recovery of stranded costs pursuant to the CTC has a reduced risk compared to traditional ratemaking because recovery is reconcilable. PP&L proposes that its long-term debt rate, grossed up for taxes reflects the proper recovery. We conclude that it is just and reasonable to adopt PP&L's requested return on the unamortized principal balance of recoverable stranded costs of 10.86%, including the gross-up for taxes. This return represents a return of recovery through the CTC and is a, "floor" for PP&L's earnings. PP&L has no limit on the return it may achieve in the competitive market.

Mitigation

Commission Findings: Pursuant to their 1994 rate case, PP&L was ordered to reduce rates in 1999 by \$70 million. We find that the revenue requirement of each year's recoverable CTC should be reduced by \$70 million to use the savings to mitigate stranded costs and ensure that consumers receive the benefit of the savings. Under this proposal, the savings will end at the conclusion of the CTC recovery period. If a direct reduction to the bundled rate were to be adopted instead, consumers who shop would forego savings and the rate reduction would have to remain in effect not only for the rate cap period, but for an indeterminate thereafter. That result would distort regulated rates, since generation will no longer be a part of regulated rates upon expiration of the CTC. In contrast, linking the savings to the CTC reflects the fact that generation will be a competitive function after January 1, 1999, and provides for an expiration of the recovery period.

Discussion: PP&L indicates that its system average existing rate of 7.21 cents/kwh is below the statewide average of \$7.93 cents/kwh and that it has effectively worked to keep rates low in the past by taking advantage of lower market interest rates to refinance, limiting Operation & Maintenance (“O&M”) expenses to an increase that is below the rate of inflation, reducing employment significantly, reducing inventory, and investing in economic development initiatives to increase sales and spread its fixed costs over a larger sales base. We agree with PP&L that its efforts have avoided rate increases, but note that under traditional regulation a utility is expected to provide least cost service.

PP&L also presents several examples of future mitigation of stranded costs during the restructuring period through the buyout of NUG contracts, assumed reductions in O&M and A&G expenses, and reduced capital expenditures. The Act places a duty on utilities to mitigate stranded costs. Several parties argue that PP&L should be required to bear significantly greater mitigation responsibility. We accept PP&L’s position that its efforts are sincere and effective, but we cannot conclude that PP&L’s mitigation initiatives are either inadequate or superlative.

PP&L identifies a significant additional mitigation opportunity. In the 1994 rate case, the Commission approved PP&L’s proposal to switch Susquehanna depreciation in 1999 from the modified sinking fund method to straight line depreciation. The Commission approved PP&L’s request, which has the effect of reducing the annual depreciation expense for Susquehanna by \$70 million. The 1994 rate case Order required PP&L to reduce base rates by \$70 million in 1999 to reflect the reduced annual depreciation expense.

PP&L argues that the scheduled January 1, 1999, reduction of the bundled regulated rate is no longer appropriate because of the transition to competition and the rate caps. PP&L argues that when the 1999 rate reduction was adopted by the Commission, PP&L was entitled also to file a new rate case requesting an increase for other increased expenses. Now, with the rate cap in effect, such a rate increase is precluded and implementation of the previously authorized rate reduction in essence would be single-issue ratemaking.

Instead, PP&L proposes to use the \$70 million to accelerate amortization of regulatory assets and NUG stranded costs. OCA witness LaCapra argues that consumers must receive the benefit of the generation expense reduction. We agree with these concepts. The 1994 Order required the benefit of the reduced depreciation expense to be flowed through to ratepayers beginning on January 1, 1999. In addition, in this proceeding we must adopt a methodology that recovers a just and reasonable level of stranded costs.

Recovery of Transition and Stranded Costs and CTC Calculation

Commission Findings: We cannot accept PP&L's Basic Utility Service Rate and Customized Rate Design. The CTC shall be calculated on a per/kwh basis, allocated to each class. PP&L properly used the cost of service study in its most recent base rate proceeding for this purpose as required.

The revenue requirement of the CTC shall be allocated on a class basis to assure there is no interclass cost shifting. The record in this case supports the use of a declining CTC over the transition period and an extension of the recovery period to June 30, 2007.

Discussion: PP&L argues that it should be permitted to maintain current rates and to determine the CTC as a residual charge. Under its approach, PP&L would continue to collect its capped rates from all customers, while establishing a shopping credit based on the administratively determined price of energy for customers choosing to shop and determining the CTC as the entire residual amount. As discussed above, the Act requires that we determine the CTC, “from the bottom up” based on authorized recoverable stranded costs. A CTC calculated, “from the top down” as a residual amount bears no valid, enforceable relation to the determination of recoverable stranded costs in this proceeding and must be rejected. Moreover, as we enter the era of competitive, deregulated generation, this Commission will not establish an administratively determined market price for generation that directly imposes the parameters for savings from selecting a competitive supplier.

PP&L proposed a generation price for Basic Utility Service (“BUS”) for non-shopping customers based upon the annualized, average cost of such service, subject to the rate cap. As discussed above, the BUS price would also directly affect customers who shop, because PP&L proposes that we adopt a CTC that is the residual after the BUS amount is subtracted from the unbundled cost of generation in existing rates.

In addition, PP&L initially proposed a Customized Rate Design for the CTC that would be mandatory for non-residential customers, but made the proposal optional for all customer classes in response to the objections of PPLICA and OSBA. Under the proposal, the CTC rate would be different for each customer based on 1996 usage. In simplified form, PP&L proposes that half of each customer’s CTC would be collected through a fixed charge while the remainder would be

recovered based on the customer's usage. Under its proposal, a customer with the same usage as in 1996 would pay the same CTC as under a direct cents/kwh CTC. A customer increasing usage, however, would pay less towards the CTC while a customer reducing usage would pay more towards the CTC. PP&L argues that such a, "halfway" move towards marginal pricing will promote economic development by reducing the CTC on incremental usage and lessen the distorted price signals engendered by having a CTC.

OCA and the Public Interest Parties oppose the Customized Rate Design. OSBA and PPLICA initially opposed the Customized Rate Design, but do not object to its optional availability. We do not accept PP&L's arguments as support for adoption of its complex proposal. It is the fact that a CTC exists to permit a utility to recover stranded costs that distorts the price signals of a competitive generation market. It is the fact that the CTC exists to permit the utility to recover stranded costs that limits and delays the full opportunity for competitive generation to promote economic development. We also agree with many of the objections raised by OCA and the Public Interest Parties. The proposal intentionally encourages increased consumption, shifting the CTC burden and penalizing customers who reduce consumption. As PPLICA states, the proposal essentially adopts a, "take or pay" charge for half of recoverable stranded costs.

The Customized Rate Design must be viewed in concert with other issues in this case. PP&L proposed to charge capped rates, provide no consumer savings during the CTC recovery period, and not reconcile CTC revenues annually. This decision provides for consumer savings and the resulting economic development benefits directly through the competitive market. No

complex rate design is necessary to provide a marginal benefit. This decision provides for annual reconciliation of recovered CTC revenues. No complex rate design is necessary to ensure PP&L's recovery of CTC revenues.

Thus, PP&L's proposed Basic Utility Service Rate and Customized Rate Design are rejected.

The CTC must be calculated as the amount necessary to fully amortize the authorized recoverable stranded and transition costs over the recovery period, including a return on the unamortized principal balance as described above. All customers will pay the unbundled transmission and distribution rate. Non-shopping customers will pay the unbundled rate for generation such that the total rate will precisely reflect currently the existing rates. A proportionate amount of the unbundled generation rate collected from non-shopping customers will be allocated to CTC recovery.

Customers choosing to shop will pay their chosen supplier instead of PP&L for generation. These customers will continue to pay a temporary charge for PP&L's stranded generation related costs to PP&L through the CTC. The residual amount leftover from the unbundled generation rate and the CTC amount is the Shopping Credit.

The CTC shall be calculated on a, "per kwh" basis, allocated to each class. Section 2808(a) requires that the CTC be calculated in a manner that does not shift interclass or intraclass costs and is consistent with the allocation methodology for utility production plant accepted by the commission in the most recent base rate proceeding. We conclude that PP&L properly used the cost of service study in its most recent base rate proceeding for this purpose as required. The

revenue requirement of the CTC shall be allocated on a class basis to assure no interclass cost shifting.

Section 2808(b) provides that the utility and a customer may mutually agree on an alternative payment methodology. PP&L shall cooperate with consumer requests for an alternative CTC payment methodology that fully collects the same present value of CTC responsibility without bypass by the consumer or over collection by PP&L.

The CTC distorts market prices and directly impacts the competitive market because it limits the opportunities for consumers and competitive suppliers to achieve savings and earn profits, respectively. The parties have presented various proposals for adjusting CTC recovery levels in each year to address their concerns. We conclude that the facts of this case and the stranded recovery authorized herein support the use of a declining CTC over the transition period. We conclude that it is appropriate to use a declining CTC in order to properly balance PP&L's earnings in the early years of the transition and reasonable customer savings during the entire transition period.

Section 2808(b) provides a general rule that the CTC recovery period should expire by December 31, 2005. The Act modifies the general rule, however, if "... the Commission, in its discretion and for good cause shown, orders an alternative payment period." We find that PP&L's large amount of stranded costs supports an extended transition period until June 30, 2007, in order to permit PP&L full recovery of its stranded costs while ensuring that suppliers have a reasonable opportunity to compete and consumers have a reasonable opportunity to save during the transition period.

The CTC shall be calculated based on annual 1999 sales of 33,090,377 MWH, escalating at 1.5% annually and monthly receipt of revenues.

PP&L proposes an annual determination of over and under collections of CTC recovered dollars through a Section 1307 reconciliation proceeding. PP&L proposes that the actual CTC will not be adjusted to reflect actual recovery. Instead, the CTC recovery period would be shortened or extended as necessary. PP&L argues that there is good cause to adopt its proposal because rates will be at the capped level under its proposals. However, rates will be below capped levels, so the argument is moot. We conclude that the Act requires an annual reconciliation proceeding pursuant to Section 1307(e) based on actual sales and that good cause to adopt an alternative reconciliation method may only be found after hearings in the required *annual reconciliation proceeding*.

Tariff Issues

General Directions for Compliance Filing

Commission Findings: We find it appropriate to summarize our direction concerning individual tariffs and Special Customer tariffs in particular so that PP&L may submit a compliance filing that meets our expectations. These general directives should be incorporated in PP&L's compliance filing unless specifically indicated to the contrary in this decision.

All tariff classes should be unbundled, permitting all customer classes to procure generation competitively, based on the allocation and rate design in PP&L's last base rate case

and this decision. Specific tariff rules shall be those currently approved or directed by the Commission previously except as may be modified in this decision.

All existing special contracts remain in effect on their terms. A contract that explicitly prohibits shopping in contemplation of passage of the Act shall remain unchanged. However, any customer with a contract that does not explicitly prohibit shopping must be permitted to shop. Upon expiration, contracts need not be extended, but the rate caps remain applicable as provided in Section 2804(4).

No contract may permit bypass of the CTC. Any existing contract purporting to do so must assign customer payments to full recovery of the allocated CTC and provide the associated discount as a credit to the customer against other portions of the bill. As rates are unbundled, customers with existing discounts must receive an allocated discount to the distribution and transmission (“T&D”) portion of the bill unless the nature of the discount is exclusively on the generation component.

Small Business Rates

Commission Findings: PP&L proposes changes to its GS-1 rate design based upon its proposed administratively determined market price of energy. Since an administrative determination of market price is rejected, the proposal is moot.

Discussion: PP&L proposes to change its existing GS-1 and GS-3 rate design to recover all T&D charges through a flat energy and a fixed customer charge, eliminating the existing declining block

rates. OSBA correctly observes that the change would shift intraclass costs and has not been supported by the kind of studies usually presented by the parties and relied on by the Commission in adopting a rate design. As discussed, all existing tariffs generally should remain available on their present terms. A tariff change is appropriate if meeting the standards of traditional ratemaking or if the transition to competition requires a change. We cannot accept PP&L's argument that the simplicity of eliminating the declining blocks requires approval of this change since PP&L itself proposes a complex declining block rate structure for CTC recovery. The proposed change is denied.

Interruptible Tariffs

Commission Findings: We agree with PPLICA that PP&L's proposal is anti-competitive, impermissibly shifts costs, violates the rate caps, discriminates against customers who shop, and is contrary to reliability considerations by undermining the availability of interruptible service. We reject PP&L's changes to its other interruptible schedules as unsupported by substantial evidence. PP&L's compliance filing shall include tariff provisions which apply the interruptible based CTC charge for interruptible customers who shop rather than a firm based CTC charge consistent with this discussion.

Discussion: PP&L proposes limitations on the availability of Interruptible Rate Schedules IS-T and IS-P to customers purchasing all of their generation from PP&L. As discussed, customers on all tariffs are entitled to shop and are protected by the applicable rate cap. Each interruptible

tariff, as well as residential schedules RTD and RTS, for which PP&L proposes a similar limitation, must be unbundled to permit a customer to shop. While PP&L has done so, it proposes a higher CTC based on a firm rate schedule for customers that shop.

Economic Incentive Rates

Commission Findings: All existing, “competitive” tariffs shall continue to be offered to any eligible customer who does not yet have the opportunity to choose a competitive supplier. Once the phase-in is completed and all customers may choose a competitive supplier, the incentive rate schedule shall be closed to new customers. Regulated “competitive” tariffs will no longer be appropriate, although PP&L may offer competitive generation through its unregulated affiliate(s). We do not otherwise require the extension of any tariff schedule for an individual customer, but PP&L must provide a rate to all customers consistent with the rate cap.

Discussion: PP&L has several economic development incentive rates and riders, most of which are scheduled to expire during the transition period. PP&L makes several proposals regarding these incentive rates. First, PP&L proposes to extend the availability of some provisions until the individual customer has choice, while other provisions would remain available to existing customers through the end of the transition period. Second, PP&L proposes to close the availability of these provisions to new customers. Third, PP&L proposes to limit the availability of these provisions to customers purchasing generation from PP&L. PP&L recognizes that discontinuation of a customer on a beneficial rate schedule could violate the rate cap as applied to

that customer. PP&L's resolution does not completely assure compliance with the rate caps, however.

PP&L may not limit the availability of incentive rates to customers purchasing generation from PP&L. If the nature of the discount in the existing tariff is specifically within the generation component, a customer choosing to purchase generation from an EGS will receive no continuing benefit from remaining on the PP&L schedule. We do not agree that economic development rates are inherently allocable only to generation, however. Unless the existing benefits is specified as a generation benefit in the tariff, each rate must be unbundled in a manner that allocates the existing discount pro rata to each component of the bill. A shopping customer would lose the generation portion of the discount.

Consolidated Billing

Commission Findings: In its Exceptions, New Energy Ventures ("NEV") indicates that the Recommended Decision failed to address its testimony in support of consolidated billing, which PP&L did not oppose. We grant NEV's proposal to require consolidated billing.

Self Generation

Commission Findings: We conclude that PP&L must provide reasonable opportunities for both large and small customers to interconnect self-generation. We adopt the proposals of the Environmentalists for net metering and interconnection, except that we do not require PP&L to purchase the generation of any customer. With customer choice and direct access, a self-

generating customer may contract to buy and sell electricity with any willing EGS. PP&L must, however, as an EDC, provide the opportunity for self generation through reasonable net metering and interconnection provisions.

Discussion: Section 2804(2) provides that restructuring shall permit, “reasonable and fair opportunities to self-generate and interconnect” to the transmission and distribution system.

PP&L makes no proposals to address this statutory directive in its restructuring plan. PP&L proposes a new Rule 6A, paragraph E(5) that requires a customer installing self-generation after January 1, 1999, to pay a CTC for generation no longer purchased from PP&L. PP&L’s proposal does not consider the Section 2808(a) that provides that only self-generation that, “significantly” decreases use of the transmission and distribution network must be subject to a separate recoupment of otherwise avoided payment of a customer’s allocated CTC responsibility. As in *PECO Energy*, PPLICA proposes to define “significant” to permit a 25% reduction in system usage without additional CTC responsibility. We find that only reduced usage exceeding 10% of the pre-1999 use of the system requires payment of additional CTC.

As an EDC, PP&L must provide a reasonable and fair opportunity for customers to self-generate and interconnect pursuant to Section 2804(2). The Environmentalists propose net metering provisions and rules to facilitate interconnection of self generators with the transmission and distribution system.

Duty to Serve

Commission Findings: Section 2807(e)(1) of the Act requires that PP&L, as an EDC, shall have the continuing duty to serve all customers, including, “. . . the delivery of electric energy and the production or acquisition of electric energy for customers,” until the CTC collection period has ended. The Act imposes certain responsibilities on the EDC to provide Provider of Last Resort (“PLR”) services to all customers unless an alternative provider has been identified by the

Commission. PP&L, as an EDC, must provide all PLR services until directed otherwise. The duty to serve applies not only to customers who do not choose a competitive generation supplier. The duty also protects customers who cannot find a willing EGS and those whose supplier fails to deliver. All customers without a competitive supplier shall be served by PP&L pursuant to the applicable tariff and are entitled to the full protection of the applicable rate cap provisions.

PP&L’s proposal to use its Generation Supply Group, a licensed EGS, to provide PLR service must be rejected. Section 2807(e)(1) imposes the duty to serve on the Commission regulated EDC.

PP&L also proposes a Purchased Generation Cost Rate that would be applicable after the *phase-in to PLR customers without hourly meters*. The proposal includes an annual reconciliation of market priced energy and administrative charges. We agree with OCA that this proposal is premature. Section 2807 specifies that future provisions for the market-based pricing of PLR generation service shall be adopted by regulations at a later date.

Similarly, we must reject PP&L’s proposals for returning customers. The Act provides no basis for treating returning PLR customers any differently than customers who never chose

generation service from an EGS. A returning customer is still protected by the same rate cap as if they had not left, and a returning customer must be served on the same terms as would other similar customers who did not previously receive generation service from an EGS. No substantial evidence supports the need to impose any switching fee at this time. As with all other new costs of service related to the administration of direct access, we do not adopt any additional charges to the customer or EGS until a finding that a net incremental cost exists. We agree with OCA that rate RTS customers are entitled to the same opportunity to shop without penalty upon return as any other class of customer.

Competitive Safeguards

Commission Findings: A vibrant competitive market cannot develop without both customer choice and a level playing field among competitors. The EDC must treat all EGSs comparably, without preference or discrimination. We adopt the Enron position that PP&L not be permitted to serve ineligible customers through its affiliated EGS. These are Provider of Last Resort Customers, not EGS customers. If a customer chooses not to choose or is otherwise ineligible, they become a default customer of the EDC (the "delivery" group). Enron's contention here is well-taken. If the PP&L Generation Group secures ineligible customers during the phase-in, the EGS derives an unwarranted competitive advantage when those customers become eligible to choose or elect to choose. That is not appropriate, and it operates to the potential prejudice against competing suppliers.

Discussion: Unlike other electric utilities in Pennsylvania, PP&L has proposed no legally separate entity that will provide competitive market generation services. Instead, PP&L has proposed to operate a functionally separate, "Electric Delivery Group," or "EDG" now doing business under the name, "PP&L Access," and a functionally separate, "Generation Supply Group," now doing business under the name "PP&L Energy Plus."

Section 2804(5) is clear that the Commission may not require corporate reorganization as part of a restructuring plan. However, PP&L's proposed organizational structure raises serious competitive safeguard issues at the outset. Problems are immediately evident in PP&L's restructuring plan. The duty to provide PLR service is a duty of the regulated EDC. Yet, PP&L proposes to provide PLR service through the Generation Supply Group at competitive market rates. In effect, PP&L's proposal obscures any separation between the EDC and the EGS, or regulated rates and competitive market rates. We agree with Enron's criticism that PP&L's proposal would essentially have the PP&L EDC deliver a huge market share to its affiliated EGS at the onset of competition.

As discussed, the Act requires PLR service to be provided by the EDC at regulated rates for the present time. Structural separation of an EDC from fully independent generation entities is preferable to reliance on even the most well-intended functional separation. In the absence of divestiture or structural separation, functional separation must be implemented diligently. The EDC must have no reason or ability to treat its competitive supplier affiliates any differently than any other competitive supplier. Functional separation without legal separation must not provide any basis for any competitive advantage or opportunity for the marketing entity.

PP&L proposes a Code of Conduct to govern interaction between its EDC and EGS groups based on the consensus recommendations of the Competitive Supplier Working Group. This interim Code of Conduct would remain in effect until such time as final regulations adopting a Code of Conduct become effective. When the Commission issued proposed regulations for the Code of Conduct, the work product of the consensus working group was rejected as an inadequate, "least common denominator." It is not the proper starting place for an interim Code of Conduct.

PP&L agrees that a Code of Conduct should be uniform throughout Pennsylvania. We agree with the comments of several parties that, given its organizational structure, it may be difficult for PP&L to avoid non-comparable treatment of its competitive division, but it must do so nevertheless. Certainly the Commission cannot soften the standards that are applicable to other EGSs and EDCs because of the organizational form that PP&L has chosen.

We agree with Enron that the Interim Code applicable to PP&L should be the Pennsylvania Electric Association ("PEA") Code, as amended and adopted by the Commission in *PECO Energy* until final regulations are effective. *Order on Compliance Filing*, adopted February 5, 1998. This Code shall be effectively immediately for all matters related to the January 1, 1999, phase-in and thereafter, while the Pilot Code will continue to apply only to the pilot program and only until January 1, 1999.

Supplier Tariff

Commission Findings: PP&L did not propose a specific Supplier Tariff, although it did propose as part of its presentation many terms that would be included within a Supplier Tariff. We agree with the EGSs that implementation of retail direct access pursuant to the Act requires a comprehensive Supplier Tariff that includes all rules, procedures and protocols appropriate and necessary for the seamless and efficient implementation of retail direct access. We direct PP&L to include a specific Supplier Tariff as part of its compliance filing. The compliance filing Supplier Tariff must reflect all applicable F.E.R.C. and PJM rules while supplementing those rules to reflect all aspects of the interaction between PP&L and an EGS necessary and appropriate for the efficient implementation of retail direct access. The Supplier Tariff is not a services agreement; it is a set of rules and procedures. It should include no fees or other charges except as have been approved by the Commission upon documentation of incremental cost. The Supplier Tariff must address customer sign-up and switching, balancing, billing, and data exchange. The compliance filing Supplier Tariff shall be consistent with this Order and all other relevant Commission regulations and Orders, that have been adopted to date concerning relevant issues, procedures and protocols.

Unbundling of other Services

Commission Findings: The Recommended Decision generally states that other service issues shall be as provided in our other regulations and Orders. The Recommended Decision includes specific discussion of some of the issues presented in this proceeding, such as billing, metering,

collections, application of partial payments and customer switching of supplier. We agree that such regulations and Orders shall control all customer service issues and note that the discussion in the Recommended Decision generally is consistent with this result.

Metering, Billing and Collection Services

Commission Findings: Metering - We concur with and adopt the Judge's recommendation that

PP&L must allow customers the option, in conjunction with their EGS, to request the use of a, "qualified meter," that has been approved by the Commission. As the regulated EDC, PP&L 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 PP&L as a result of the customer's metering choice.

Consumer Education

Commission Findings: The Statewide committee is already at work on its proposals and we expect significant, if not final, focus for the consumer education requirements by the time that PP&L's compliance filing is approved. We shall assume funding of consumer education at \$5 per residential household for each of four years at the present time, for a total of \$21.62 million for PP&L. This amount may be adjusted by the time of the compliance filing approval. The final amount shall be fully recoverable as a transition cost pursuant to the CTC.

Discussion: We understand PP&L's preference for a final consumer education plan prior to adoption of a budget. However, funding for consumer education as a recoverable transition

expense must be adopted in this proceeding. Even the best thought out plan must be flexible enough to change with experience and perhaps require different funding levels or emphases.

PP&L filed its Restructuring Plan and its Consumer Education proposals prior to Commission adoption of a Statewide Consumer Education program administered by a committee. The Commission has determined that both a statewide campaign and a local initiative are necessary for effective consumer education. PP&L's plan identifies several important components of effective consumer education, but does not present the kind of comprehensive effort that we envision.

PP&L agrees to participate in the statewide consumer education program and provide a separate local program as well. The details of these programs will be adopted pursuant to the procedures outlined in the Consumer Education docket.

Universal Service and Energy Conservation

Commission Findings: The Act includes many provisions designed to ensure that electric service is universally available in Pennsylvania as we make the transition to a competitive generation market. Section 2802(9) declares that, "... electric service is essential to the health and well-being of residents, to public safety, and to orderly economic development, and electric service should be available to all customers on reasonable terms and conditions." Section 2802(10) declares that "... the Commonwealth must, at a minimum, continue the protections, policies and services that now assist customers who are low- income to afford electric service." Section 2803 defines, "Universal service and energy conservation," as, "... policies, protections and services

that help low-income customers to maintain electric service. The term includes customer assistance programs, termination of service protection and policies and services that help low-income customers to reduce or manage energy consumption in a cost-effective manner, such as the low-income usage reduction programs, application of renewable resources and consumer education.” Section 2804(9) of the Act requires that “. . . the Commission shall ensure that universal service and energy conservation policies, activities and services are appropriately funded and available in each electric distribution service territory.”

Section 2804(15) requires the restructuring plan to include an initial proposal indicating how the EDC’s universal service and energy conservation responsibility will be met. On July 10, 1997, the Commission issued a Final Order establishing Guidelines for such programs as part of each utility restructuring plan (“Guidelines”).

Funding Levels and Customer Enrollment- We agree with the OCA that the proposed Company funding levels for the CAP and LIURP programs are insufficient to meet the needs of PP&L’s customers. We adopt the OCA funding levels, though not the OCA enrollment numbers as that will be dependent upon the evaluation presently being conducted. Consistent with sound management, the CAP program should be expeditiously expanded to meet the community’s needs.

Renewables Pilot Program- We adopt the OCA recommendation. Further, we agree with both the OCA and Environmentalists that this area lends itself to development through a pilot program.

CAP Needs Assessment, Funding and Eligibility

Commission Findings: PP&L did not base its proposed CAP funding on any specific needs assessment. The record does not include useable net costs per customer. We adopt the OCA CAP funding level.

Discussion: Through census data, PP&L and Commission on Economic Opportunity ("CEO")

witness Kuennen both identify about 177,000 customers at or below 150% of the federal poverty guidelines in its service territory. PP&L says about 58,000 of these customers have been identified as payment troubled, rendering them eligible for Universal Service program participation.

PP&L has proposed to double its currently identified Universal Service funding of \$7.0783 million to \$14.3 million by 2002, with the increase directed to PP&L's On Track program. On Track is PP&L's Customer Assistance Program ("CAP").

On Track- PP&L proposes to establish its pilot On Track program as a permanent program, increasing enrollment from the current level of 1040 by 3000 annually to an enrollment target of 10,000 by 2002. In order to meet this enrollment ramp-up, PP&L proposes to spend approximately \$5.875 million in 1999, \$7.75 million in 2000, \$9.625 million in 2001, and the target \$9.1 million in 2002 and thereafter. PP&L did not base its proposed funding on any specific needs assessment.

PP&L's impact evaluation of On Track is due now, but the contractor preparing the evaluation does not expect to provide it until this summer at the earliest and perhaps by the end of

1998. The record does not include useable net costs per customer. PP&L has indicated a direct gross program cost of \$600 per customer, but that does not include any of the avoided costs of traditional collections, such as uncollectible expense, payment agreements and similar costs.

CEO argues that the target for On Track enrollment should be about 71,000, or about 40% of those below 150% of poverty. CEO supports annual funding at \$9 million in 1999, \$10.5 million by 2002 and \$12.5 million by 2005.

OCA witness Brockway argues that On Track should be ramped-up to funding of about \$11.7 million annually, serving about 18,500 customers. She argues that this funding level is substantially below the expenses currently allocated to low income uncollectibles, and that customers can be both better served and more cost-effectively served by increasing enrollment in On Track. We agree with OCA that redirection of existing low income uncollectible and other collections expenses can substantially fund increased On Track participation.

PP&L proposes a serious expansion of On Track, but we agree that the goals should be moderately increased through a slightly more aggressive ramp-up and adopt the OCA's proposal. PP&L should fund On Track at its proposed level of \$5.875 in 1999, \$8.0 million in 2000, \$10.0 million in 2001 and \$11.7 million in 2002. We agree with OCA that the administrative issues raised by expanding enrollment will be faced in expanding to PP&L's proposed enrollment levels. The additional administrative issues raised by a moderate further expansion of enrollment are not substantial.

PP&L proposes that On Track customers be permitted to choose a competitive supplier, but that On Track customers must receive a single bill only from PP&L. Additionally, PP&L

proposes that comparable program benefits must be provided by the EGS directly from their own funds. We reject both of these proposals. The Act gives customers a choice to obtain a separate bill for generation from their EGS. As discussed below, Universal Service program costs are fully recoverable from ratepayers. Even if the Commission had the authority to require an EGS to provide a bill discount to low-income customers, such a policy would require that the Commission allocate a portion of PP&L's Universal Service and uncollectible expense to the EGSs, instead of permitting PP&L to retain the entire amount of ratepayer funding.

In its compliance filing, PP&L shall indicate a fixed percentage of the On Track discount that will be applied to each portion of the bill pro rata, including generation. The generation benefit is portable and will not be lost if a customer chooses a competitive supplier.

WRAP Baseload Program and Renewables Pilot

Commission Findings: Providing LIURP services is a cost-effective way to reduce unpaid bills, and LIURP expansion is an important companion to the expansion of On Track. Section 2803 specifies the use of renewables as an appropriate component of a Universal Service and Energy Conservation Program, and we agree that such a pilot should be developed as part of the LIURP funding level. Further, PP&L must expand program availability for its usage reduction program to serve an appropriate number of non-heating, low-income customers. Customers above 150% of federal poverty guidelines with special circumstances should have usage reduction services available. Ratepayer funded utility programs should primarily serve low income customers below that 150% level.

Discussion: WRAP is the name of PP&L's Low-Income Usage Reduction Program ("LIURP").

Keep Warm is a similar program funded at \$1 million annually to serve customers from 151%-200% of poverty. PP&L proposes to retain existing funding for WRAP at \$3.0 million, for a constant total funding level of \$4.023 million. PP&L wants to retain its focus on electric heat customers, arguing that electric heat is a greater proportion of PP&L's residential service than for any other Pennsylvania electric utility. PP&L also wants to retain its current allocation of 25% of its usage reduction budget for households between 150% and 200% of poverty.

PP&L estimates that 32,500 low income electric heat customers are in need of LIURP services. The Commission on Economic Opportunity ("CEO") estimates that about 55,000 low-income customers use electric heat while 123,000 low income customers do not. CEO argues that the non-heating customers must be served as well, and that there are many cost-effective measures that can be used.

CEO proposes total usage reduction spending of \$4 million in 1999, \$5.25 million by 2002 and \$6.5 million by 2005. CEO provides substantial analysis of PP&L's funding and completion rate to document significant additional need for LIURP services. We agree that providing LIURP services is a cost-effective method to reduce unpaid bills, and that LIURP expansion is an important companion to the expansion of On Track.

OCA proposes spending a total of \$4.7 million, including a WRAP baseload program and a renewables pilot. Two-thirds of PP&L's low-income customers are non-heating customers that should be served. The OCA documents the success of baseload LIURP programs. In particular,

the refrigerator replacement program has already been piloted by PP&L and has been successful for several utilities. Within the proposed spending level that is only \$700,000 above PP&L's proposal, OCA witness Brockway advocates a substantial redirection of spending priorities to baseload customers and those below 150% of poverty.

Section 2803 specifies the use of renewables as an appropriate component of a Universal Service and Energy Conservation Program. PP&L did not propose any renewables program. The Environmentalists and OCA propose adoption of a pilot renewables program as adopted in *PECO Energy*. We agree that such a pilot should be developed as part of the LIURP funding level adopted.

We agree that PP&L must expand program availability for its usage reduction program to serve an appropriate number of its non-heating low-income customers. We also agree that customers above 150% with special circumstances should have usage reduction services available, but that ratepayer funded utility programs should primarily serve low-income customers below 150% of poverty. PP&L is directed to make these adjustments.

Cost Recovery

Commission Findings: There will be a reconcilable Universal Service Fund Charge ("USFC") that is separately identifiable for cost accounting but included within the distribution portion of a customer's bill. The USFC shall be reconcilable pursuant to Section 1307(f). The reconciliation will be based on all net program costs as indicated in the Guidelines.

Discussion: Section 2804(8) of the Act requires the Commission to establish, “. . . an appropriate cost recovery mechanism which is designed to fully recover the electric utility’s universal service and energy conservation costs over the life of these programs.” The Guidelines do not permit the funding for Universal service to be the last priority after rate cap or CTC considerations:

“[F]unding for universal service and energy conservation programs should not be determined after all other funding requirements are met. The total amount of dollars available under the rate cap should be adjusted to meet all of the requirements of the Act including universal service and energy conservation.”

The record is insufficient to conclude that implementation of the required funding levels requires any particular amount of additional funding in any given year or whether the targeted funding can be achieved within the rate caps during any year in which rates remain capped. Any incremental expense over the amount included in current rates, as determined pursuant to the Guidelines, is recoverable through a deferred regulatory asset to be collected after rate cap expiration.

PP&L proposes to allocate Universal Service and Energy Conservation Program costs on a per customer basis. A per customer allocation appears to require all customers to contribute equally but in fact would have little impact in spreading the costs of universal service. In the Guidelines, we indicated that we considered it inappropriate to adopt a single per kwh for all customer classes, but did not intend to suggest that per kwh pricing itself is inappropriate. Universal service program costs previously have been allocated only to the residential class and charged on a per kwh basis. In order to avoid cost shifting, we retain that principle.

Conclusion

On the basis of the reasoning set forth in this Motion, and as supported by the record in this case, this Motion results in a finding of stranded costs of \$2.864 billion, which, using a 10.86% return rate, computes to a CTC initially estimated at 1.78 cents/kwh for 1999. The rate will be adjusted each year for system sales growth. Our transmission and distribution calculations result in a 1999 rate of 1.7 cents/kwh. PP&L currently provides service at a bundled rate of 7.21 cents/kwh. The recovery of the CTC and the transmission and distribution charges should yield a 1999 shopping credit of 3.73 cents/kwh. Attached to this Motion is Attachment A detailing the basis for calculations offered by this Motion.

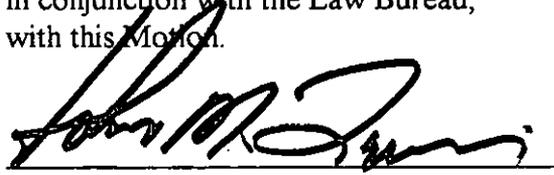
The Administrative Law Judge and the parties in this case have compiled a thorough record that allows us to make a reasoned decision in the restructuring of Pennsylvania Power & Light Company. With the Order that will result from this Motion, the restructuring requirements of the Act have been met.

THEREFORE, WE MOVE THAT:

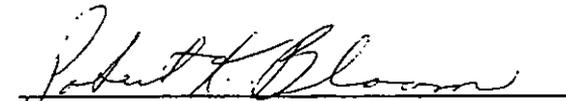
1. The restructuring plan of PP&L, as modified by this Motion, be adopted by the Commission;
2. That the Office of Special Assistants, in conjunction with the Law Bureau, prepare an Order for entry consistent with this Motion.

5-14-98

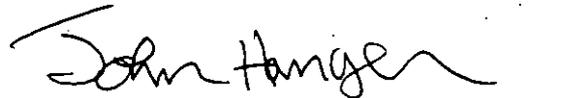
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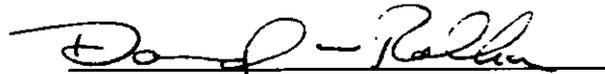
JOHN M. QUAIN
CHAIRMAN



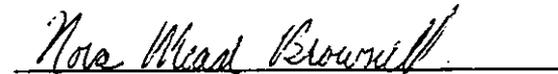
ROBERT K. BLOOM
VICE CHAIRMAN



JOHN HANGER
COMMISSIONER



DAVID W. ROLKA
COMMISSIONER



NORA MEAD BROWNELL
COMMISSIONER

Attachment A

Pennsylvania Power & Light Restructuring	
<u>Category/Item:</u>	<u>Amount</u>
Stranded Generation:	
Generating Plant Book Value	\$ 4,017.10
Generation Market Value:	\$ (2,465.3)
Total Stranded Generation:	\$ 1,551.78
Decommissioning:	
Nuke Decomm.	\$ 128.99
Fossil Decomm.	\$ -
Total Decommissioning	\$ 128.99
Net Regulatory Assets:	
Energy Costs	\$ 76.815
FAS 106/ PBOP	\$ 8.73
VERP	\$ 14.09
Employee Transition Costs	\$ 5.50
US DOE Assessments	\$ -
Susquehanna Early Window	\$ 9.83
Common Plant	\$ 7.78
Retired Miners Health Care Cost	\$ 6.31
Rate Case Expenses	\$ -
Susquehanna Deferred Refuel Costs	\$ -
Net Taxes Recoverable (FAS 109)	\$397.61
Consumer Education	\$ 21.62
Regulatory Liabilities	
Pension Overfunding	\$ -
Investment Tax Cr: Liability in Net FAS 109 Asset Amount	
TOTAL NET REGULATORY ASSETS	\$ 548.29
NUG Stranded:	\$ 635.69
TOTAL STRANDED:	\$ 2,864.745