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June 22, 2004

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James J. McNulty, Secretary  
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Commonwealth Keystone Building, 2<sup>nd</sup> Floor, 7 North  
400 North Street  
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PA PUBLIC UTILITY COMMISSION  
SECRETARY'S BUREAU

DOCKETED  
JUL 21 2004

Re: Pennsylvania Public Utility Commission v. PGW  
Petition of Philadelphia Gas Works to Establish Cash Receipts Reconciliation Clause  
Docket Nos. R-00049157, P-00042090

Discontinuance of CEPA's participation in R-00049157, P-00042090

Dear Secretary McNulty:

Community Legal Services, Inc. represents Action Alliance of Senior Citizens of Greater Philadelphia, Association of Community Organizations for Reform Now (ACORN), Tenants' Action Group (TAG) and Consumers Education and Protective Association (CEPA) in the above-captioned matter.

Consumers Education and Protective Association (CEPA) is no longer active as a consumer advocacy and membership organization. Accordingly, CEPA's participation in these proceedings docketed at R-00049157 and P-00042090 is discontinued.

Community Legal Services, Inc. will continue to represent Action Alliance of Senior Citizens, ACORN and TAG in these proceedings.

If you have any questions concerning this matter, please do not hesitate to contact me us at 215-981-3702.

Very truly yours,

  
PHILIP A. BERTOCCHI, ESQUIRE  
LAURA MOSKOWITZ, ESQUIRE

Attorneys for Action Alliance, ACORN  
TAG and CEPA

cc: Certificate of Service

Administrative Law Judge Charles E. Rainey, Jr.

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## CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of this letter upon the following parties in the manner described below:

Dated: June 22, 2004

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June 22, 2004

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James J. McNulty, Secretary  
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RE: Pa. Public Utility Commission  
v.  
Philadelphia Gas Works  
Docket No. R-00049157

Petition of Philadelphia Gas Works  
Regarding Cash Receipts Reconciliation  
Clause  
Docket No. P-00042090

Dear Secretary McNulty:

Enclosed for filing please find an original and nine (9) copies of the Office of Consumer Advocate's Reply Brief. in the above-referenced proceeding.

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

Sincerely,

Stephen J. Keene  
Senior Assistant Consumer Advocate

Enclosures

cc: All Parties of Record  
Honorable Charles E. Rainey, Jr. (via overnight mail)  
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BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pa. Public Utility Commission

v.

Philadelphia Gas Works

Petition of Philadelphia Gas Works  
Regarding Cash Receipts Reconciliation  
Clause

Docket No. R-00049157

Docket No. P-00042090

**ORIGINAL**

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OFFICE OF CONSUMER ADVOCATE'S  
REPLY BRIEF

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JUN 23 2004

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## **I. INTRODUCTION**

On June 14, 2004, the parties filed their Main Briefs in this proceeding setting forth their positions regarding the proposal by Philadelphia Gas Works ("PGW") to implement a Cash Receipts Reconciliation Clause ("CRRC"). Main Briefs were filed by the Office of Consumer Advocate ("OCA"), Philadelphia Gas Works ("PGW"), the Office of Trial Staff ("OTS"), the Office of Small Business Advocate ("OSBA"), Philadelphia Industrial and Commercial Gas Users Group ("PICGUG"), Action Alliance, et.al. ("Action Alliance"), Senator Vincent J. Fumo, et.al. ("Philadelphia Public Officials") and the Philadelphia Housing Authority ("PHA"). The OCA's Main Brief effectively sets forth its opposition to the CRRC proposal. The OCA's focus in this Reply Brief will be to address arguments of the other parties in a manner that will assist the Commission in making a determination in this proceeding.

## **II. REPLY ARGUMENT**

### **A. Introduction.**

The Company's primary argument in support of the proposed CRRC is that it needs this mechanism as a "backstop" or "insurance policy" against shortfalls in collections, in order to avoid a downgrade of its bonds by the rating agencies. The OCA has addressed this issue at length in its Main Brief, and it is not necessary to repeat those arguments here. However, the OCA would note that no one from any of the rating agencies, nor the City's bond advisor, testified in this proceeding about what the rating agencies were looking for from PGW in order to maintain the Company's investment grade bond ratings. Instead, what was offered was nothing more than speculation by two PGW witnesses, Mr. Bogdonavage and Mr. Knudsen, that absent the CRRC, the rating agencies would downgrade PGW. The OCA submits that such speculation cannot form the basis for implementation of such a drastic remedy as the CRRC.

In fact, what the rating agencies are looking for was adequately expressed in the reports issued by Standard & Poor's ("S&P") and Fitch Ratings ("Fitch"). The focus of the S&P report is on PGW's collections and support from the City. The April 2003 S&P report states:

Ratings will be lowered further if PGW's financial profile weakens over the near term and collection rates and cash margins do not improve materially. Additionally, any of the following events could have negative ratings implications: if access to short-term borrowing is restricted, if suppliers place additional liquidity demands on PGW, or if certain support from the city is not forthcoming. The lowered ratings are predicated on the city providing annual payment forgiveness to PGW for at least the next four years, and on the city allowing PGW to defer its \$45 million loan payable until 2008. In the absence of such support, ratings will be lowered further.

PGW CRRC-5, Exh. TEK-1 at 2.

This report was issued on April 9, 2004. Id. At the time, PGW had less than \$11 million in cash reserves and was reporting an 87% collections rate. Id. Since that time, PGW's collections and cash reserves have improved. PGW's own witness projects that the Company will finish the current fiscal year on August 31, 2004 with a collection rate of between 90.5% and 93% and cash reserves of \$31-36 million. PGW St. CRRC-1R at 2; Sch. JRB-10; Tr. 323. In addition, the City has agreed to forego the \$18 million City Payment for the next five years. This amounts to an injection of \$90 million of cash into the Company over the next five years. Therefore, the conditions necessary for PGW to maintain its investment grade rating that S&P noted in its April report have been met. The Company's professed need for a "backstop" was never referred to by the rating agencies.

The OCA submits that such a remedy is unnecessary, unprecedented and should be rejected by the Commission. The OCA submits that such a backstop has no basis in the Public Utility Code. The Commission sets PGW's rates on a cash flow basis during a base rate case. Rates must be set at a level that permit the Company to recover reasonable operating expenses and meet its bond coverages. There is nothing that requires the Commission to install an additional "backstop" to this process.

**B. PGW Does Not Need The CRRC Since Its Collections And Financial Condition Have Shown Improvement Since The Time PGW Filed The CRRC Petition.**

PGW argues in its Main Brief that the CRRC is needed to provide sufficient cash to pay PGW's obligations and to provide assurance to the bond rating agencies. PGW M.B. at 9-23. The OCA has addressed this argument in detail in its Main Brief and it is not necessary to repeat those arguments. OCA M.B. at 9-15. The OCA acknowledges that PGW is in a financially weakened position due to its failed collections efforts last year. However, the solution is not to impose a rate increase upon ratepayers who are already struggling to pay historically high natural gas bills. Instead, the focus should be on improving PGW's collection efforts to bring more cash in the door. The OCA submits that this is exactly what the Commission has done in its June 2 Order when it initiated an investigation into PGW financial and collections issues. Investigation Into Financial and Collections Issues Regarding The Philadelphia Gas Works, Docket Nos. P-00042090, R-00049157, M-00021612 and P-00032061 (Order entered June 2, 2004)(June 2 Order). A comprehensive review of PGW's collections practices and procedures should help PGW improve its collection efforts. Improved collections will lead to an improved financial condition for the Company. Every increase of one percent in the collection rate for PGW is an increase of \$8 million in cash. PGW St. CRRC-1 at 5. Therefore, if PGW can improve its collection rate to 94% or 95%, the cash crisis will be averted.

There is substantial evidence in the record that PGW has seen improvement in its collection activities. For example, PGW reports that the total amount of dollars collected through Intel-A-Check payments for the period January through March 2004 has increased by 77% over the same period last year. OCA Cross-Exh. 1 at 8. PGW witness Knudsen testified that there is no question that increased Intel-A-Check payments will lead to an increase in PGW's collection rate. Tr. 374. In addition, PGW reports that the number of payment arrangements for the period January through March 2004 has increased by 76% over the same period last year. OCA Cross-Exh. 1 at 9. This increase in payment arrangements will also lead

to improved collections. Tr. 374. PGW witness Bogdonavage testified about the improvement in PGW's current collections:

For the 12 months ending March 2004, receipts, as a percentage of billed revenues, is 90.46% (JRB-7). Moreover, as of April 2004, PGW's cumulative percentage receipts compared to billings is over 7% better than PGW's experience last year at this time (80% v. 75.27%). *If this improvement continues through the fiscal year, PGW's collections experience could be 93%* (JRB-8).

PGW St. CRRC-1R at 2 (emphasis added). PGW witness Knudsen testified that PGW's collection rate could climb as high as 94% for the current fiscal year. Tr. 354.

The OCA submits that the focus should continue to be on improving PGW's collections, not on imposing an additional rate increase on customers who cannot afford it. PGW has already shown improvement in its collections as a result of the collection initiative. Further improvement can be expected as a result of the Commission investigation. Therefore, the CRRC is not necessary and should be rejected.

The Company continues to claim that it still needs additional rate relief in the form of the CRRC to appease the bond rating agencies. PGW St. CRRC-1R at 4. PGW witness Bogdonavage speculates in his testimony that he believes PGW needs to have \$60 million in end of year liquidity in order to maintain investment grade status. *Id.* However, the Company provides no sworn testimony about this issue from anyone in the investment community or from the City's bond advisor as it has in past rate proceedings. Moreover, the proposed CRRC will not have any effect on this year's cash position, since it would not become effective until September 1, 2004. Therefore, there is no way that the CRRC would have any impact whatsoever on PGW's cash position at the end of the current fiscal year on August 31, 2004. Tr. 325.

In previous rate proceedings, PGW has argued that it needed \$35-40 million of cash at year-end in order to remain viable. PGW St. CRRC-1 at 7. However, the Commission has never explicitly acknowledged this in any of its Orders. Tr. 332. Nevertheless, PGW

projects that it will finish the current fiscal year with between \$31 million and \$36 million of cash reserves. This is more cash on hand at year-end than in any year since the Commission assumed jurisdiction of PGW. Action Alliance Cross-Exh. 1. But still the Company claims that this is not enough and seeks additional rate relief. The OCA submits that PGW's claim that it needs to have \$60 million in year-end cash to avoid a downgrade is simply not credible and should be rejected.

A close examination of the rating agencies' reports does not indicate any specified level of cash liquidity at year's end. Instead, the focus of the S&P report is on improvement in PGW's collections and support from the City in the form of forgiveness of the \$18 million City Payment. PGW St. CRRC-5, TEK-1 at 2. At the time the S&P report was issued in April 2003, PGW's cash reserves were less than \$1 million and it was reporting an 87% collections rate. TEK-1 at 1-2. As noted above, the year-end forecasts have improved significantly since that time as a result of improved collections efforts and the City's agreement to grant back the \$18 million City Payment.

The OCA submits that given PGW's improved collection forecasts and the City's agreement to grant back the \$18 million City Payment, PGW will have sufficient liquidity at year end to avoid a further downgrade. Therefore, there is no need for PGW to backstop its currently high rates with a CRRC mechanism.

**C. The CRRC Is Not The Proper Method To Address PGW's Cash Working Capital Concerns.**

In its Main Brief, PGW claims that the CRRC is superior to any other method of addressing PGW's cash receipts issues. PGW M.B. at 24-29. In its Main Brief, the OCA pointed out the numerous reasons why the proposed CRRC is flawed and inconsistent with the Public Utility Code and Commission precedent. OCA M.B. at 15-23. The OCA submits that uncollectible expense does not lend itself to recovery through an automatic adjustment clause. Automatic adjustment clauses are typically limited to specifically identified expenses that are not

under the control of the Company. OCA St. 1 at 15. The record in this case demonstrates that collections are within the Company's control. As soon as the Company initiated its collections initiative, the collection rate increased. The OCA submits that this provides a strong incentive for the Company to limit its uncollectible expense. OCA St. 1 at 16. To move uncollectible expense into a reconcilable surcharge would eliminate this important incentive.

In addition, the Company's proposal constitutes impermissible single-issue, retroactive ratemaking. The OCA has fully addressed this issue in its Main Brief. OCA M.B. at 18-22. The OCA submits that if the Company needs to address cash flow and cash working capital issues – which does not appear to be the case based upon the record in this proceeding – it should do so within the context of a base rate case. To simply isolate one element of expense that has increased since the last rate case and seek to implement a surcharge to recover that increase violates sound ratemaking tenets.

**D. Commission Precedent Does Not Support Recovery Of Uncollectible Expense Through An Automatic Adjustment Mechanism.**

PGW claims in its Main Brief that PGW's CRRC proposal is supported by authority in the Public Utility Code and consistent with prior Commission determinations. PGW M.B. at 29-38. PGW's proposal is made pursuant to Section 1307(a) which authorizes the Commission to establish a sliding scale of rates or other method for the automatic adjustment of rates of a public utility. 66 Pa.C.S. §1307(a). However, the Commission has only authorized 1307(a) mechanisms in very limited circumstances. For instance, the Commission has authorized recovery of Demand Side Management ("DSM") costs through an automatic adjustment mechanism. Pa. Industrial Energy Coalition v. Pa.P.U.C., 653 A.2d 1336 (Pa.Comwlth. 1995), *aff'd per curiam*, 543 Pa. 307, 670 A.2d 1152 (Pa. 1996)(PIEC). In addition, other examples of where the Commission has authorized the use of Section 1307(a) for cost recovery include, the recovery of "take-or-pay" ("TOP") costs by natural gas utilities, 52 Pa.Code §69.181; "gas supply realignment costs" and "stranded costs" resulting from FERC

Order 636, 52 Pa.Code §69.341(b); and principal and interest due on PennVest obligations, 52 Pa.Code §69.363.

The OCA submits that the types of costs that the Commission has permitted to be recovered through Section 1307(a) are easily distinguishable from PGW's request to recover uncollectible expense through the CRRC. With respect to TOP costs and Order 636 costs, the Commission permitted recovery of these costs through a 1307(a) mechanism since they were costs that were limited in life and were not ongoing costs. *See e.g.*, 69 Pa.Code §69.181(g); 19 Pa.Bull. 3311. In fact, in adopting the policy statement on TOP costs, the Commission found that:

Since these are, in fact, non-recurring, non-gas costs, it is reasonable to amortize them, through a surcharge, over a specific period of time ... the use of the surcharge is a rate design device which merely recognizes that these costs do not represent ongoing costs and have a limited life.

19 Pa.Bull. 3311. In fact, once all Pennsylvania gas utilities completed their TOP recovery process, the TOP policy statement was then revoked in 1996. 26 Pa.Bull. 1380. *See also*, Recovery of FERC Order 636 Transition Costs, Docket No. M-930389, 23 Pa.Bull. 5405 (Order entered October 7, 1993)[finding that costs associated with Order 636 are non-recurring, non-gas costs similar to TOP costs and therefore subject to Section 1307(a) recovery].

The Commission has found that PennVest costs were also approved for Section 1307(a) cost recovery, 52 Pa.Code. §69.363, because the PennVest statute specifically provides for "expedited approval of rate relief" to ensure repayment of principal and interest on PennVest loans. 35 Pa.C.S. §751.14. DSM cost recovery is explicitly provided for by Section 1319 of the Public Utility Code. 66 Pa.C.S. §1319.

The OCA submits that there is no statutory or prior Commission authority that would allow a utility to recover uncollectible expense through an automatic adjustment mechanism. Commission precedent has long provided for recovery of uncollectible expense through a utility's base rates. There is nothing in PGW's proposed CRRC that would support a departure from this long-established precedent.

The Company also argues that the Commission has already used an automatic adjustment mechanism to allow PGW to recover increased uncollectible expense. In 2001, the Commission approved a settlement between the Commission's Law Bureau, PGW and the City of Philadelphia that allowed PGW to collect an additional \$7 million through its GCR to account for additional bad debt expense. Pa.P.U.C. v. Philadelphia Gas Works, Docket Nos. R-00005654, R-00005619 (Order entered February 22, 2001). The settlement arose as a result of PGW's appeal of the Commission's Order granting PGW \$11 million in interim rate relief. Pa.P.U.C. v. Philadelphia Gas Works, Docket No. R-00005654 (Order entered November 22, 2000). However, that action represented an extraordinary settlement at a time when PGW was facing an imminent financial crisis. PGW had just received interim rate relief and was in the process of making a base rate filing. The \$7 million was a one-time infusion of cash that PGW had overcollected as part of its GCR. The additional cash allowed PGW to meet its bond coverages and operating expenses. The Commission specifically noted in its February 22, 2001 Order that:

We assure the parties that our approval for the recovery of a portion of bad debt expense through the GCR *under the limited and specific circumstances* described in the Joint Petition does not reflect any intent to permit such treatment in future GCR proceedings.

February 22, 2001 Order at 6 (emphasis added). The Commission also explicitly noted that the resolution of this issue was "of no precedential value in subsequent proceedings." Id.

Therefore, the OCA submits that the precedent cited by PGW is inapplicable to the instant case and PGW's proposed CRRC should be rejected.

**III. CONCLUSION**

For the reasons set forth above, and in its Main Brief, the Office of Consumer Advocate respectfully requests that the Petition of Philadelphia Gas Works to Establish a Cash Receipts Reconciliation Clause be denied.

Respectfully submitted,



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Re: Pennsylvania Public Utility Commission  
v.  
Philadelphia Gas Works  
Docket No. R-00049157

Petition of Philadelphia Gas Works Regarding  
Cash Receipts Reconciliation Clause  
Docket No. P-00042090

I hereby certify that I have this day served a true copy of the foregoing document, the Office of Consumer Advocate's Reply Brief, upon parties of record in this proceeding in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant), in the manner and upon the persons listed below:

Dated this 22<sup>nd</sup> day of June, 2004.

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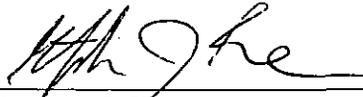
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Dear Secretary McNulty:

Community Legal Services, Inc. represents Action Alliance of Senior Citizens of Greater Philadelphia, the Association of Community Organizations for Reform Now (ACORN), and the Tenants' Action Group (TAG) (collectively "Action Alliance et al.") in the above-captioned matter.

Enclosed please find for filing an original and nine (9) copies of Action Alliance et al.'s Reply Brief in Opposition to the Petition of Philadelphia Gas Works to Establish Cash Receipts Reconciliation Clause.

As evidenced by the attached Certificate of Service, all active parties to the proceeding are being served with copies of this Brief by e-mail and/or by First Class U.S. Mail.

Very truly yours,

PHILIP A. BERTOCCI

Attorney for Action Alliance et al.

cc: Certificate of Service

Administrative Law Judge Charles E. Rainey, Jr.

Enclosures

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JUN 22 2004

PA PUBLIC UTILITY COMMISSION  
SECRETARY'S BUREAU

**ORIGINAL**

BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission : Docket No. R-00049157  
: Docket No. P-00042090

v. :

Philadelphia Gas Works :

**DOCKETED**  
JUN 24 2004

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ACTION ALLIANCE et al.'s REPLY BRIEF  
- IN OPPOSITION TO PETITION OF  
PHILADELPHIA GAS WORKS TO  
ESTABLISH CASH RECEIPTS  
RECONCILIATION CLAUSE

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JUN 22 2004

PA PUBLIC UTILITY COMMISSION  
SECRETARY'S BUREAU

**DOCUMENT  
FOLDER**

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Date: June 22, 2004

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ACORN and Tenants' Action Group

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## **I. Introduction.**

Action Alliance of Senior Citizens of Greater Philadelphia, the Association of Community Organizations for Reform Now (ACORN) and Tenants' Action Group (TAG) (collectively "Action Alliance et al."), three Philadelphia consumer membership and advocacy organizations hereby submit the following Reply Brief in Opposition to Petition of Philadelphia Gas Works to Establish Cash Receipts Reconciliation Clause.<sup>1</sup>

## **II. For PGW To Preserve Investment Grade Ratings, the Bond Rating Agencies Only Require that PGW Maintain At Least Its Historical Collections Ratio.**

In its Main Brief, PGW places great weight on the statement in the Standard & Poor's Rating Services (hereinafter "S&P") April 9, 2004 ratings notice that "[r]atings will be lowered further if PGW's financial profile weakens over the near term and collection rate and cash margins do not improve materially." PGW St. CRRC-5, Exhibit TEK-1; PGW Main Brief, at 12.

Throughout its Main Brief, PGW repeatedly misinterprets this statement to mean that PGW will be downgraded without further warning as early as the Fall, if the CRRC is rejected and/or if PGW's Petition for Waiver does not result in significant relaxation of Chapter 56 consumer protections relating, inter alia, to security deposits, payment arrangement terms and service termination for non-payment procedures.<sup>2</sup> The Company also unjustifiably interprets in a similar

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<sup>1</sup> The Consumers Education and Protective Association (CEPA) is no longer active as consumer advocacy and membership organization, and should not be listed as a party in this proceeding.

<sup>2</sup> For instance, PGW claims that this statement means that "neither a base rate increase, nor any other possible solution ... [CRRC and Chapter 56 Waivers] to PGW's cash crisis would provide a response in time to address the financial community and ratings companies' admonition to improve cash and collections immediately – or else." PGW Main Brief, at 8

vein the April 23, 2004 Fitch Ratings notice and the June 8, 2004 Moody's Investors Service notice. The Fitch notice maintained PGW at investment grade, albeit at a lower level. The Moody's notice maintains PGW at its existing investment grade Baa2 level, while placing it on Credit Watch.<sup>3</sup> PGW's misinterpretation is a calculated exaggeration. Without justification, it transforms rating agency concerns about the effectiveness of PGW collections into concerns as to whether PGW's rate structure and mechanisms and PUC customer service regulations provide an appropriate level of support to PGW operations. The Commission should reject this patent manipulation intended to bludgeon the Commission, the Commission's Bureau of Consumer Services and PGW customers into acceptance of the Company's one-sided and self-serving proposals.

Action Alliance et al. submit that the S&P, Fitch and Moody statements themselves are the only reliable source of information concerning what the bond rating agencies expect from PGW in the period between the time of issuance of the notices and the next review in early calendar year 2005. Those statements simply do not support PGW's distorted interpretations. As Action Alliance et al. demonstrated in its Main Brief, those pronouncements primarily recognize the significance of the City's commitment to grant back \$18 million to PGW for five years, starting at the end of FY2004, and to extend the repayment date of the interest free \$45 million City Advance from FY2006 to FY2008. These actions were sufficient to preserve

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(emphases in original). Throughout its Main Brief, this refrain in one form or other is appears continually, as if repeating a false statement makes it somehow accurate. See, e.g., pp. 4, 5, 7, 12, 43, 45, 58, 50.

<sup>3</sup> See CRRC-5, Exhibit TEK-1 (S&P); CRRC-5, Exhibit TEK-2 (Fitch) and Moody's Investors Service Global Credit Research Rating Update - PGW (June 8, 2004) [www.moodys.com/moodys/cust/research/genoa/report/rating%20Update8062](http://www.moodys.com/moodys/cust/research/genoa/report/rating%20Update8062).

PGW's investment grade ratings, albeit at a lower level, and counterbalance for now the rating agencies' concerns prompted by PGW's low collections ratio in FY2003 and by the failure as of February - March, 2004 to demonstrate levels of collections performance sufficient to regain at least PGW's historical 92% collections ratio in FY2004.

A. The Rating Agencies Do Not Require Improvement of PGW's Collections Ratio Above the 92% Historical Level.

In reading the S&P and the Fitch notices, it is important to recognize the time frame within which the research on which they were based was conducted. This time frame was February and early March, 2004, when PGW itself had acknowledged that its collections ratio for FY2003 was a disturbing 87% and its projections at that time for FY2004 were not much better – 89%.<sup>4</sup> All three notices observe that PGW's collection performance in FY2003 was not up to the Company's 92% historical standards – collection rates which had “deteriorated appreciably” in the past year (S&P), a “sharply deteriorated liquidity position” (Fitch), a “cash flow crunch due to slowed payment by customers of record high gas bills” (Moody's). The notices do not suggest that PGW's 92% historical collection rate is insufficient to maintain ratings at existing levels. As of March 1, 2004, PGW was itself still projecting that its collections ratio in FY2004 would be only 89%, well below the historical 92% collections ratio. When PGW's projected collections ratio for FY2004 stood at 89%, following 87% actual in FY2003, the rating agencies naturally would sound an alarm. The rating agencies' call for “improvement” was a call for

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<sup>4</sup> The rating agency reviews on which rating downgrades were based occurred in the January-February, 2004 time frame. May 11, 2004 Evidentiary Hearing Transcript (hereinafter “Transcript”), at 369-70, 339.

improvement at least up to historical levels.

However, there is nothing in the rating agency notices which suggests that a downgrade is imminent, as PGW claims, unless PGW can show an improvement in a few months which is “material” improvement over the 92% historic collections levels. PGW Main Brief, at 7. It was not until early May, a week before the evidentiary hearings, and well after the issuance of the S&P and Fitch notices, that PGW disclosed that its projected collections ratio for FY2004 had risen materially into the 90.5-93% range. PGW St. CRRC-1R, Exhibit JRB-10. Contrary to PGW’s contentions, the rating agency notices do not “admonish” PGW to obtain regulatory approval of a CRRC or to obtain relaxation of consumer protections thought to hamper collections, “or else.” PGW Main Brief, at 8. Rather, they warn that PGW can not indefinitely maintain its present ratings unless it improves its collections to its historical 92% level.

**B. The Rating Agencies Do Not Require that PGW Achieve a \$60 Million Fiscal Year End Cash Balance.**

One prong of PGW’s argument that the Commission must grant its CRRC Petition is that PGW’s level of year end cash, even at this year’s projected \$30-36 million range, is not sufficient to satisfy the bond rating agencies. According to PGW, the Company needs \$60 million in year end cash to “satisfy the bond rating agencies” and “to retain an investment grade rating.” PGW Main Brief, at 21-22.

This claim is totally without support in the rating agency notices. Those notices contain no statements concerning year end cash, let alone statements concerning ta specific desired level of year end cash. The only support in the record for this claim is a statement of PGW’s chief

financial officer that he “believed” that the rating agencies require liquidity equal to 30 days average revenue. PGW St. CRRC-1R, at 4.

Action Alliance et al. submit that this is not a reasonable interpretation of the bond rating statements. While this 30 day test might represent a rule of thumb applicable to investor owned businesses, the rating agencies have given no indication that this standard is applicable to the municipally owned PGW. Moreover, as the record shows, PGW has maintained investment grade bond ratings for years with year end cash or cash equivalents in the \$3.5 to \$12.5 million range.<sup>5</sup> The Commission has never recognized PGW’s need for year end cash above this level either.<sup>6</sup> Although PGW TXCP program has recently been reduced from \$100 million to \$80 million, this reduction is substantially offset by the \$18 million cash infusion provided by the City’s commitment to grant back the \$18 million City payment for FY2004 and the following four years.

C. The Rating Agencies Do Not Require that PGW Obtain Approval of the CRRC.

Far from placing great hopes in the CRRC, the S&P notice observes that “while the outcome of the cash receipts-related rate filing remains uncertain, even if such relief were granted, it is unclear that collections and cash-basis coverage of fixed charges would improve.” This statement exhibits a well-founded lack of confidence in the appropriateness of a measure which seeks to increase gross sums collected by raising rates for a customers already straining

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<sup>5</sup> Action Alliance Cross-Examination Exhibit 1; Transcript, at 334-336 (cited in Action Alliance et al. Main Brief, at 19).

<sup>6</sup> Transcript, at 332 (cited in Action Alliance et al. Main Brief, at 19).

under the highest rates in the region. Rather, at bottom, as PGW itself recognizes, S&P instructs PGW to improve its collection rate so as to improve its cash margins.<sup>7</sup>

The S&P notice is far from the mandate for immediate approval of the CRRC that PGW claims it to be. When S&P wants immediate rate adjustments, it is not shy about stating its views. Contrast the language of the February 12, 2002 S&P Notice, which prompted the Commission to grant an Extraordinary Rate Increase in the Spring, 2002. There, S&P observed:

This rate shortfall, combined with the warmer-than-budgeted weather this winter and higher receivables, contributes to poor liquidity, which is not appropriate for the current rating level. "If the PUC approves an emergency rate request, Standard & Poor's will review the adequacy of the increase and determine if ratings will be affirmed or lowered." said Standard & Poor's credit analyst Aneesh Prabhu.<sup>8</sup>

Here, S&P recognizes steps taken by the City to support PGW, and emphasizes the need for PGW to regain its 92% historical collections ratio.

Fitch also says nothing which can be interpreted to command creation of a CRRC. The ratings agency expresses concern about PGW's increase in accounts receivable in its April 23, 2004 ratings notice. However, without admonition, it observes that the restructuring proceeding, which contributed to PGW's "collection delays" has been completed. It opines that the CRRC, which would only provide additional cash if PGW's collections ratio fell below 92%, would improve collections.

Moody's adopts a similar attitude toward the CRRC. As one would expect, Moody's also

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<sup>7</sup> As PGW CEO Knudsen conceded in his CRRC Rebuttal Testimony, "We believe that improvement of our cash receipts performance so as to collect ninety two cents on the dollar billed is a minimum requirement for PGW to be able to issue those bonds." CRRC St.5, at 9.

<sup>8</sup> Pa. Pub.Util.Comm'n v. Philadelphia Gas Works, Docket No. R-00017034-0002, PGW Exh. BCB-1 (S&P's February 12, 2002 "Credit Watch Update").

affirmed the need for PGW to maintain its “more aggressive rate collection effort” and to improve its “liquidity,” while observing that this effort, as well as “other elements of PGW’s plan to improve cash flow” including but not limited to the “success of legislative and regulatory changes to rates and/or collection rules” would form the basis of future judgments. There is nothing in this language which constitutes an “admonition” to approve a CRRC that PGW claims is there; rather, the notice makes passing reference to a change in “rates” only as a possible aid among many others to increased liquidity. Although Moody’s could have downgraded PGW’s senior lien revenue bonds from Baa2 to Baa3, while still preserving their investment grade, it refrained from doing so.

D. The Rating Agencies Do Not Require that PGW Obtain Chapter 56 Waivers.

As with the CRRC, the rating agencies reference Chapter 56 protections and standards as a potential, but not the only, means of increasing liquidity. The rating agencies’ emphasis, however, is not on the method chosen to improve liquidity, but on the result that must be obtained -- improvement of PGW’s collections ratio at least to historical levels.

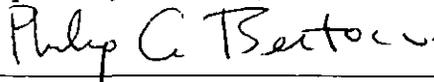
Standard & Poor’s does not even mention waiver or relaxation of consumer protections as the type of measure likely to improve the collections rate. In contrast to PGW’s repeated assertions that the Commission’s Chapter 56 prevents improvement in PGW’s collection rate, S&P stresses in two (2) separate occasions that PGW benefits from a “relatively supportive regulatory environment,” and that “PGW’s regulatory environment as favorable to credit quality” In contrast, Fitch opines that “proposed changes to shut-off and payment plan rules would

improve PGW's collections," while recognizing that PUC approval would not occur until the "summer at the earliest." As stated above, Moody's refers to possible "legislative and regulatory changes to rates and/or collection rules," as potential aids among others to increasing PGW's liquidity. However, there is nothing in Moody's notice that could be taken as an "admonition" to approve Chapter 56 waivers.

### **III. Conclusion.**

For all foregoing reasons, Action Alliance et al. respectfully request that the Commission deny PGW's CRRC Petition.

Respectfully submitted,



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June 22, 2004

CERTIFICATE OF SERVICE

ORIGINAL

I hereby certify that I have this day served a copy of this Reply Brief upon the following parties in the manner described below:

Dated: June 22, 2004

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JUN 22 2004

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IN REPLY PLEASE  
REFER TO OUR FILE

June 22, 2004

ORIGINAL

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

Re: Pennsylvania Public Utility Commission  
v.  
Philadelphia Gas Works  
Docket No. R-00049157

DOCUMENT  
FOLDER

Petition of Philadelphia Gas Works to Establish  
a Cash Receipts Reconciliation Clause  
Docket No. P-00042090

Dear Secretary McNulty:

Enclosed for filing please find an original and nine (9) copies of the  
**Reply Brief** of the Office of Trial Staff (OTS) in the above-captioned proceeding.

Copies are being served on all active parties of record.

Sincerely,

Johnnie E. Simms  
Senior Prosecutor  
Office of Trial Staff

SECRETARY'S BUREAU

2004 JUN 22 PM 12: 07

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Enclosure

c: Parties of Record  
Office of Special Assistants

23



## I. INTRODUCTION

On June 14, 2004, the Office of Trial Staff (“OTS”) and several of the active parties, including but not limited to, the Office of Consumer Advocate (“OCA”), the Office of Small Business Advocate (“OSBA”), Action Alliance et al (“AA”), the Philadelphia Public Officials (“PPO”), the Philadelphia Industrial and Commercial Gas Users Group (“PICGUG”), the Philadelphia Housing Authority (“PHA”) and Philadelphia Gas Works (“PGW”) filed Main Briefs in accordance with the modified Procedural Schedule. OTS’ Main Brief set forth the evidence in support of an alternative mechanism for the Pennsylvania Public Utility Commission’s (“Commission”) consideration by proposing a way to adjust the allowance for uncollectible expense upward or downward with each change in the 1307(f) rate.

OTS’s Reply Brief is limited to those matters raised by the respective parties Main Briefs not specifically addressed by OTS in its Main Brief and to those matters previously addressed by OTS, but which require additional discussion as a result of the other parties’ Main Briefs.

## II. ARGUMENT

The parties in this proceeding have presented both technical and legal criticisms of OTS's Alternative Mechanism. OTS will address the criticisms in this Reply Brief however, before proceeding to address the criticisms OTS will reiterate its position in this proceeding. In that regard, OTS's Alternative Mechanism is an attempt to provide PGW with an opportunity to materially improve its cash margins in the near term. OTS's Alternative Mechanism is to adjust the allowance for uncollectible accounts expense upward or downward with each change in the 1307(f) rate, which will provide recognition of the relationship between increasing gas costs and its impact on uncollectible accounts expense.

### 1. The Parties' Technical Criticism of OTS's Alternative Mechanism Is Unfounded

In their respective Main Briefs, OCA, OSBA, PPO, AA and PGW raised certain criticisms of the Alternative Mechanism proposed by OTS. OCA, OSBA, PPO and AA essentially made the same technical criticisms by relying solely upon the testimony of OSBA witness Knecht.<sup>1</sup> Mr. Knecht provided brief criticism of OTS's proposal in that he claimed that "it was unclear to how Mr. Weakley established the base PGC rate from which the OTS surcharge is measured in that there is a disconnect between OTS's proposed base 1307(f) rate and the current uncollectible expense." While OCA, OSBA, PPO and AA resoundingly relied upon the direct testimony of OSBA witness Knecht, the parties failed to recognize

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<sup>1</sup> OCA Main Brief at pages 41-43; OSBA Main Brief at page 28; PPO Main Brief at pages 22-24 and AA Main Brief at 23

that OTS correctly and effectively responded to the criticism in surrebuttal testimony. OTS respectfully submits that if the parties had recalled OTS's surrebuttal testimony and PGW's witness Bogdonavage's rebuttal testimony, the parties would have concluded that OSBA witness Knecht's criticism of OTS's Alternative Mechanism was without merit. While OSBA witness Knecht criticized that \$3.18 was the cost of gas included in the base rate component of rates charged to ratepayers, it is clear that he either did not read PGW witness Bogdonavage's rebuttal or did not know first-hand that PGW utilizes a pro forma cost of gas in calculating its base rate revenue requirement not \$3.18. PGW witness Bogdonavage testified that when PGW calculated its base rate revenue requirement it utilized a pro forma cost of gas of \$346,100,477 or the average gas cost rate of \$6.097/Mcf.<sup>2</sup> However, the analysis must go beyond the determination of the average gas cost rate of \$6.097/Mcf versus \$3.18/Mcf in that it must be determined whether the \$6.097/Mcf is the correct rate to be included in the OTS Alternative Mechanism. In addressing whether \$6.097/Mcf should be included in the OTS Alternative Mechanism, OTS witness Weakley testified as follows:

No. The pro forma cost of gas included \$30.3 million of CRP discounts and conservation programs which have since been removed from the 1307(f) rate during the PGW's rate restructuring. The \$30.3 million was included in the third quarterly 1307(f) filing on June 1, 2002. In order to compare the gas cost rate included in base rates

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<sup>2</sup> PGW St. No. CRRC-1R at page 13.

to the current 1307(f) gas cost rate that amount must be removed. Therefore, the adjusted gas cost rate that was included in base rates is \$6.097 less \$0.5327 (\$30.3 million ÷ 56,883,616 Mcf) which equals \$5.5643/Mcf.<sup>3</sup>

Unlike OSBA witness Knecht, OTS recognized that PGW witness Bogdonavage was correct in noting that in calculating its base rate revenue requirement, PGW used a pro forma cost of gas of \$346,100,477 or the average gas cost rate of \$6.097/Mcf. As explained above, the only question that remained is whether the \$6.097/Mcf should be included in OTS's Alternative Mechanism. Since PGW's pro forma cost of gas included the CRP discounts and conservation programs (now removed in the Restructuring proceeding), OTS Alternative Mechanism was revised by subtracting the \$5.5643/Mcf for a recommended rate of \$0.1798/Mcf based upon PGW's 1307(f) second quarterly report filed on March 1, 2004.<sup>4</sup> There is no record evidence that OSBA witness Knecht noted that revision in his analysis of OTS's Alternative Mechanism.

Another criticism cited by the parties based upon OSBA Knecht's direct testimony was that there was no rationale for setting the base 1307(f) rate at the level that was in effect at the last fully litigated case, since there was \$36 million rate increase in a subsequent base rate proceeding, albeit as a result of a black box settlement.<sup>5</sup> OTS respectfully submits that the \$36 million increase was the result of the emergency rate relief and as previously noted a black box settlement, which resulted in no increase over the emergency allowance and is the gas costs PGW

<sup>3</sup> OTS St. No. 1 SR at page 4.

<sup>4</sup> OTS St. No. 1 SR at page 4.

<sup>5</sup> OSBA St. No. 2 at page 5.

included in rates and reflected in the OTS Alternative Mechanism. Quite frankly, OSBA Knecht is simply incorrect and off-based in his comments. Notably, on being cross-examined as to whether PGW has received uncollectible expense allowances from the Commission in its rates, OSBA witness Knecht invoked the testimony presented by OTS witness Weakley to support his answer to the question.<sup>6</sup>

Finally, PGW in its technical criticisms of OTS's Alternative Mechanism argues the following:<sup>7</sup>

1. The OTS proposal fails to consider the entirety of of PGW's cash receipts shortfall.
2. The OTS proposal fails to offer relief to PGW for current undercollections relating to gas costs.
3. The OTS formula could operate to lower PGW's Commission-established uncollectible accounts expense and therefore deprive PGW of much-needed cash working capital.

It is not the intent of OTS in proposing its Alternative Mechanism to have a true-up of all the ills associated with PGW's uncollectible accounts expense. One of the ways for PGW to address one of the ills associated with its uncollectible accounts expense problem is its collection efforts initiative. OTS's Alternative Mechanism has been designed to temporarily address or eliminate increasing gas costs as one of the contributors to the ills of PGW's uncollectible accounts expense. It is OTS's hope that by implementing its Alternative Mechanism along

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<sup>6</sup> See Tr. 483-484.

<sup>7</sup> PGW Main Brief at page 48-51.

with PGW's collection efforts initiative that PGW's near term cash margins will improve sufficiently enough as to satisfy the credit rating agencies. The combined implementation of OTS's recommendation and the collection efforts initiative may stave off any further reduction in PGW's credit rating. In the absence of such an action, any reduction in PGW's credit rating will cost the customers significantly more in rates than what is being proposed in OTS's Alternative Mechanism.

In large part PGW's criticism of OTS's proposal is what separates the PGW's CRRC proposal and OTS's Alternative Mechanism. In that regard, PGW's CRRC proposal is a guarantee of monies for PGW to address all of the ills associated with the collection efforts of PGW, while OTS's proposal deals solely with how increasing gas costs is contributing to the uncollectible accounts expense. Simply put, OTS's Alternative Mechanism was not intended to be a *guarantee*, but rather, to be used as a tool in combination with PGW's other collection efforts. Clearly, PGW's criticism of OTS's Alternative Mechanism is without merit.

2. **The Legal Argument Should Be Viewed In the Context Of The Mandates Associated With Philadelphia Gas Works**

There are a number of legal authorities to suggest to the Commission that PGW's proposal and OTS's Alternative Mechanism may be against the norm of ratemaking in the Commonwealth of Pennsylvania. OTS respectfully submits that the majority of the legal authorities were decided by the Commission and the Appellate Courts before the Commission assumed jurisdiction of PGW. Such

legal doctrine as “single rate issue” was issued long before the Commission assumed jurisdiction of PGW with its mandates of a cash flow utility, bond coverage and annual payments to the City of Philadelphia. If it is a desire to use the investor-owned legal authorities in addressing the problems associated with PGW, a parties’ Main and Reply Briefs can cite case law into infinity; however the General Assembly mandated certain requirements upon this Commission that must go beyond the normal legal authorities for ratemaking purposes in dealing with the problems associated with PGW. To not do so, may lead PGW to a credit rating status that will ultimately be more costly to the PGW customers overall than the amounts presently being discussed in this proceeding.

The parties can be restricted by the legal authorities dealing with investor-owned utilities or the parties can began to think “outside of the box” and begin to deal with the problems of a cash flow, yet cash strapped, low credit rating utility, such as PGW with a credit rating one step above “junk bonds” status. OTS respectfully submits that parties and this Commission have operated “outside of the box” on other occasions, such as the Three Mile Island incident, that same effort must be done with PGW. In the absence of such an effort, as OTS witness Weakley testified, “the death spiral associated with PGW’s cash flow problem (collections) will continue.”<sup>8</sup> Interestingly, other than PGW, no other party in this

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<sup>8</sup> OTS St. No. 1 at page 16.

proceeding appears to be interested in a collaborative with all of the interested parties for the purpose of dealing with the problems of PGW on a long term basis as suggested by OTS.<sup>9</sup>

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<sup>9</sup> OTS St. No. 1 at pages 15-16.

### III. CONCLUSION

For the reasons presented in the Office of Trial Staff's Main and Reply Briefs, along with Direct and Surrebuttal Testimonies of Charles T. Weakley, III, the Office of Trial Staff's Alternative Mechanism should be adopted by the Pennsylvania Public Utility Commission for a period of two years.

Respectfully submitted,

  
Johnnie E. Simms  
Senior Prosecutor

Dated: June 22, 2004

BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission :  
v. : Docket No. R-00049157  
Philadelphia Gas Works - 1307(f) :  
Petition of Philadelphia Gas Works to :  
Establish a Cash Receipts Reconciliation : Docket No. P-00042090  
Clause :

**CERTIFICATE OF SERVICE**

I hereby certify that I am serving the foregoing **Reply Brief**  
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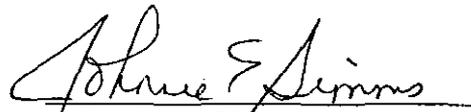
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Dated: June 22, 2004  
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# ORIGINAL

June 22, 2004

**VIA HAND DELIVERY**

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PA Public Utility Commission  
Commonwealth Keystone Bldg., 2nd Floor,  
400 North Street P.O. Box 3265  
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# DOCUMENT

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Re: Philadelphia Gas Works Cash Receipts Reconciliation  
Clause, Docket No. R-00049157  
Petition of Philadelphia Gas Works to Establish a Cash  
Receipts Reconciliation Clause, Docket No. P-00042090

Dear Secretary McNulty:

On behalf of Philadelphia Gas Works, enclosed for filing please find an original and nine copies of its Reply Brief with regard to the above referenced matter. A copy has been served on the parties listed on the attached Certificate of Service.

Very truly yours,

*Daniel Clearfield*  
Daniel Clearfield

For WOLF, BLOCK, SCHORR and SOLIS-COHEN LLP

DC/lww  
Enclosure

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Kim Pizzingrilli, Commissioner  
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BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

DOCKETED  
JUN 23 2004

Pennsylvania Public Utility Commission,

v.

Philadelphia Gas Works

Petition of Philadelphia Gas Works to Establish a  
Case Receipts Reconciliation Clause

R-00049157

P-00042090

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PHILADELPHIA GAS WORKS' REPLY BRIEF

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## I. INTRODUCTION<sup>1</sup>

The Philadelphia Gas Works (“PGW”) filed its Petition and testimony, and put on its case to establish a Cash Receipts Reconciliation Clause (“CRRC”) for one crucial reason: PGW’s financial house is on fire. There is just no other way to describe it. Following a cold winter with high gas demand, coupled with extremely high gas costs, customer bills and resulting severe cash receipts shortfalls, PGW has woefully insufficient cash working capital which will get worse if its cash receipts do not improve to historic levels. Moreover, it is and is being threatened with a disastrous downgrade to junk bond status if it does not find some way to stabilize the situation and make material improvements in its position.

PGW sees the fire. When it first smelled smoke, it instituted a comprehensive collections initiative, sought and received additional financial support from its owners, the City of Philadelphia, and brought this action seeking the CRRC mechanism to ensure cash receipts at historical levels. But these steps have not stopped PGW’s debt rating to now hover just above junk status.<sup>2</sup> It has gone further and has proposed that the Commission grant additional collections tools and to enhance state funding for low income customers, but these steps only provide the hope that the fire will be controlled. The basic back-stop of the CRRC continues to be a key step, along with these others, to stave off the rating agencies.

Despite the overwhelming evidence of fire, many parties either will not even acknowledge the fire at all, or even pick up a bucket. The Office of Consumer Advocate (“OCA”), Action Alliance of Senior Citizens et als. (“Action Alliance” or “CEPA”) and Philadelphia Public Officials do not acknowledge the fire. They think PGW’s financial house is in fine shape. The Office of Small Business Advocate (“OSBA”), Philadelphia Industrial and Commercial Gas Users Group (“PICGUG”) and the Philadelphia Housing Authority (“PHA”) see the fire, but offer no assistance. The Office of Trial Staff (“OTS”) also sees the fire, and to

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<sup>1</sup> All discussion and response to the brief of Philadelphia Housing Authority (PHA) in this Reply Brief is being made under the direction and control of PGW Assistant Counsel Greg Stunder.

<sup>2</sup> For the convenience of the Commission, attached hereto as Attachment A are Standard and Poor’s Ratings Direct (PGW Exh. TEK-1), Fitch Ratings Credit Watch (PGW Exh. TEK-2), and Moody’s Investors Service Rating Update (PGW MB at 5 ft. 3).

its credit has run to the building with buckets of water, but has stopped short of calling 911 to get the real help that will put out the fire.

The key question, of course, is does this Commission see the fire and will it give PGW the necessary tools to get it under control and then put it out? Or, will it allow a valuable asset not only to be destroyed but potentially to harm its municipal owner as well? The Commission has within its power the ability to help PGW substantially to douse the flames with a decision finding that the CRRC mechanism, under these extreme circumstances, is the most reasonable and balanced means by which to address the issues that ignited and fanned the flames. PGW respectfully requests this Commission to step up and adopt the CRRC as in the public interest.

The parties opposing this just and reasonable relief have presented their cases and filed their briefs. They raise no novel arguments. They offer no particularized record evidence in support of their various (and cacophonous) positions. Most raise general but inapplicable ratemaking rules. Many take unsupported and unnecessary swipes at a PGW management that, on the contrary, the record demonstrates has acted quickly and responsibly in the face of this crisis. PGW in reply files this brief, which analyzes the fictions put forth by the opposing parties and supplies the facts necessary to highlight the truth.

## **II. THE OPPOSING PARTIES FICTITIOUS ARGUMENTS FALL WHEN EXPOSED TO THE FACTS**

The opposing parties raise a series of fictions, some factual, some legal, in support of their efforts to defeat the CRRC. With the notable exception of OTS, which recognizes PGW's financial situation and calls for some relief (however imperfect), the remaining parties appear content to fight *any* relief, without any consideration for the natural and probable consequences of their calls to inaction. Their fictions must be exposed and the facts made known to help this Commission carry out its true responsibilities in this matter.

### **Fiction 1: PGW'S Financial Condition Is Really Not Perilous – It Has Sufficient Liquidity To Maintain Its Operations and to Maintain Its Investment Grade Bond Rating<sup>3</sup>**

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<sup>3</sup> Philadelphia Public Officials MB at 2-3; OCA MB at 1-2, 9-16; Action Alliance MB at 4-20.

**Facts:** An \$800+ million revenue per year company cannot survive with a likely fiscal year-end cash liquidity position of \$1-6 million.<sup>4</sup> It requires no special financial skills or accounting genius to figure that one out. Yet, some opposing parties continue willfully to ignore this harsh financial reality, choosing instead to indulge the thin fiction that postponing the payment of a major bill (\$30 million for gas storage) for a few months equates with financial stability (when this one, life-saving transaction is backed out, the record shows that PGW's end of year cash to be between \$1-6 million, even considering the grant-back of the \$18 million City fee).<sup>5</sup> Ostrich-like, certain parties flock to this position,<sup>6</sup> but neither the Company nor this Commission can afford the luxury of joining them, heads in sand, as PGW slips into insolvency.

PGW has testified orally and in writing concerning its financial condition for fiscal year 2004. The numbers are not in material dispute; all parties accept them.<sup>7</sup> Before taking certain recent extraordinary measures, PGW faced a cash shortfall for fiscal year end 2004 of some figure between negative \$12 million and negative \$17 million.<sup>8</sup> No party contests these numbers. These numbers fully accounted for PGW's expected revenues and expenses for the year. They reflected PGW's obligation to the City for an \$18 million payment. They reflected PGW's obligation to a consortium of private banks of another \$80 million on a fully extended loan package.<sup>9</sup> They did not reflect PGW's obligation to the City of an additional \$45 million from a fully extended short-term line of credit; or PGW's recent deferred payment of \$30 million in gas storage injection expenses otherwise due in fiscal year 2004 into fiscal year 2005.<sup>10</sup>

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<sup>4</sup> PGW MB at 22.

<sup>5</sup> PGW MB at 19.

<sup>6</sup> Philadelphia Public Officials MB at 2-3; OCA MB at 1-2, 9-16; Action Alliance MB at 4-20.

<sup>7</sup> Action Alliance points out that the \$30 million gas payment deferral might actually run as high as \$53 million (Action Alliance MB at 14), but it does not understand that only \$30 million of the deferral will occur in the FY 2004 fiscal year. Moreover, this is a distinction largely without a difference, since the money must be repaid in December of calendar year 2004 (fiscal year 2005). Tr. 312.

<sup>8</sup> PGW St. CRRC-1R.

<sup>9</sup> PGW MB at 23, n. 68; Tr. 318.

<sup>10</sup> PGW MB 19-20.

When it realized the magnitude of this deficit, PGW took emergency action.<sup>11</sup> It prevailed upon the City to postpone repayment of the \$45 million line of credit for two years. It prevailed upon the City to grant-back the \$18 million fee.<sup>12</sup> Even with these drastic steps, however, the Company still faced a likely end of year liquidity balance of only \$1 million (which could range as high as \$6 million depending on eventual collections success).<sup>13</sup> It was only after the Company took the drastic and unusual step of deferring a \$53 million payment for winter gas storage (\$30 million of which affected FY 2004), a payment that it must make within the next several months, that it was able to raise its liquidity projections to the cited levels of \$31 to \$36 million for the end of the current fiscal year.<sup>14</sup>

Amazingly, and contrary to the established facts and their inescapable conclusions, some opposing parties argue that PGW actually is in good overall financial condition because its projected fiscal year end 2004 liquidity is better than that attained in any recent years. They trumpet the PGW cash flow projections of \$31 to \$36 million for fiscal year end 2004 as a sign of PGW's financial good heath.<sup>15</sup> Some argue that the bond rating agencies will be satisfied by the City's grant-back of PGW's \$18 million payment and deferral of the repayment of the \$45

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<sup>11</sup> In addition to the relief sought from the City, PGW, as the record shows, instituted a massive Collections Initiative, involving nearly one-third of the Company, that has produced positive results, but is still expected to fall short of historic averages for this fiscal year. PGW MB at 20-21.

<sup>12</sup> PGW MB at 19.

<sup>13</sup> A 90.5% collection rate yields fiscal year end 2004 liquidity of \$1 million; a 93% collection rate yields the \$6 million figure. The more likely year end result will be in the neighborhood of 91%. PGW MB at 22.

<sup>14</sup> In addition to paying the \$30 million gas deferral in the coming months, PGW eventually will need to repay the \$45 million City line of credit; the \$80 million loan; and one day resume payment of the \$18 million to the City. These obligations will not simply vanish; they must be paid from cash receipts, and this cash is not presently available to PGW.

<sup>15</sup> OCA MB at 12-13; Action Alliance MB at 18-19; Philadelphia Public Officials MB at 2-3, 16. Interestingly, OSBA concedes that PGW has a "current financial predicament." OSBA MB at 13. Consistent with its case, OTS recognizes that PGW needs financial relief. OTS MB at 12-14.

million line of credit, and that these agencies are not really poised to lower PGW's long term debt to junk status.<sup>16</sup> There is no record evidence to support any of this fantasy.<sup>17</sup>

The Commission should not see this as a swearing contest between PGW and its sworn opponents, however. Objective observers – the bond rating agencies – have already ruled on the matter and have found PGW wanting. They have said with absolute clarity that PGW's present position, while sufficient to temporarily stave off a downgrade, needed to be improved materially in order to stop a downgrade of PGW's debt to junk status – this is a fact.<sup>18</sup> Standard & Poor's **recognized** that PGW had instituted a Collections Initiative to improve collections to historic levels and had accomplished the gas storage deferral transaction. It also recognized that the City had made concessions concerning the \$18 million fee and deferral of the short term \$45 million loan, **but still stated** that "Ratings will be lowered further if PGW's financial profile weakens over the near term and collection rates and cash margins do not improve materially."<sup>19</sup> In its downgrade statement, Fitches Investment Service noted that **despite** the City's commitment to PGW's success as evidenced by the grant-back and the loan repayment deferral, the City had its own financial difficulties, and PGW still needed to improve cash flow in order to meet its financial commitments.<sup>20</sup> Moody's just a few weeks ago indicated that unless there was material improvement over PGW's present projections in the next 90 days it would downgrade the Company's debt.<sup>21</sup>

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<sup>16</sup> E.g., OCA MB at 13-14; Action Alliance MB at 11-12. In contradistinction to these positions, OTS acknowledges that PGW's debt hovers slightly above junk status, and that PGW's overall financial profile and cash margins must improve in addition to the City's action on loan deferment and grant-backs. OTS MB at 6.

<sup>17</sup> A detailed refutation of this argument and portrait of PGW's true financial condition are set forth at Section III(A) of PGW's Main Brief.

<sup>18</sup> PGW St. CRRC-S at 5-10; Attachment A hereto. (The City action and the storage deferral deal resulted in the bond rating agencies only downgrading PGW one level – to just above junk status – but with the admonition that improvement had to occur immediately to prevent further downgrade.)

<sup>19</sup> PGW St. CRRC-5 at 6; *see also* PGW Exh. TEK-1 (emphasis added).

<sup>20</sup> PGW Exh. TEK-2.

<sup>21</sup> *See* Attachment A.

It bears repeating that, for PGW, a downgrade to junk bond status would be a disaster for PGW its customers and employees, as well as the City of Philadelphia in general. If PGW can't raise enough funds from the long term capital markets, it cannot, like most investor owned utilities, cancel or reduce shareholder dividends (it has, in effect already done this), borrow on a short term basis until the crisis passes (it has NO available short term borrowing capability available) or simply put off buying natural gas until its cash flow hopefully improves (its already done that to the maximum extent possible). There are no "shareholders" on which to pass this problem onto. The shareholders and the customers are one and the same. To the extent that the Commission fails to take action and disaster occurs, sooner or later ratepayers will bear the cost of those actions.

The City's actions have been helpful; despite recent downgrades, PGW continues (barely) to maintain an investment grade rating on its debt. But let no one be fooled: PGW is in serious financial trouble, and the rating agencies know it. The City's actions alone will not satisfy these agencies; the opposing parties' assertions to the contrary can only be described (charitably) as wishful thinking. It is easy for entities who do not have ultimate responsibility to ensure that PGW is able to continue to deliver natural gas to its customers safely and reliably to simply deny the existence of the crisis until it actually occurs. But, neither the Company nor this Commission has this luxury.

**Fiction 2: Standard and Poor's Threats Should Not be Taken Seriously Because It Was Looking at Bad Results.<sup>22</sup>**

**Facts:** OCA also insinuates that S&P's demand for material improvement in collections came at a time when its cash receipts levels were far below normal and its cash working capital was just \$1 million, presumably before the effect of the City grant back was considered.<sup>23</sup> This is demonstrably false. The S&P report specifically acknowledges PGW's Collections Initiative and indicated that it "expects these initiatives will at the very least stem any further decline in collection rates."<sup>24</sup> Moreover, the grant back of the City Fee and the deferral of the City Loan

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<sup>22</sup> OCA MB at 13.

<sup>23</sup> OCA MB at 13.

<sup>24</sup> TEK-1 at 2 (Attachment A hereto).

were also considered. Notwithstanding the addition of cash working capital caused by the grant back, S&P nonetheless found PGW wanting absent material improvement.<sup>25</sup>

**Fiction 3: A Base Rates Case Is Superior to the CRRC to Address the Company's Financial Situation.**<sup>26</sup>

**Facts:** A base rates case is the least preferable mechanism to address PGW's financial situation.<sup>27</sup> Base rates cases are costly, time-consuming and inflexible.<sup>28</sup> They cannot be focused on rectifying a particular need or issue most pertinent to a situation or a company. Also, given PGW's current financial situation, gas costs and customer demographics, a base rate case could lead to a rate increase of \$74 to \$94 million, a result that PGW must attempt to avoid. Once approved, the new base rates would remain in effect until another time and resource-intensive base rates proceeding reshaped rates, irrespective of PGW's improvements in collections, cash flow, uncollectibles expense or operations.<sup>29</sup>

Several opposing parties continue to insist that a base rates case is preferable to the CRRC.<sup>30</sup> The gist of their argument is that a base rates proceeding would provide for detailed scrutiny of all PGW rates, costs and expenses, and somehow would afford the Commission greater insight into utility performance.<sup>31</sup> This suggested approach is misguided.<sup>32</sup>

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<sup>25</sup> *Id.*

<sup>26</sup> Philadelphia Public Officials MB at 17-19; PICGUG MB at 7-8; OCA MB at 7.

<sup>27</sup> A complete discussion of why the CRRC is actually far superior to a base rates case is set forth in Section III(B)(2) of PGW's Main Brief.

<sup>28</sup> *National Fuel Gas Distribution Corp. v. Pa. P.U.C.*, 473 A.2d 1109, 1121 (Pa. Cmwlth. 1984); *Petition of Pennsylvania-American Water Company*, 1996 Pa. PUC LEXIS 182, \*13.

<sup>29</sup> PGW MB at 26.

<sup>30</sup> *E.g.*, OCA MB at 16-17; Philadelphia Public Officials MB at 17-18; PICGUG MB at 7. OTS, however, recognizes that a base rates case will only exacerbate customer difficulty in paying their bills. OTS MB at 11.

<sup>31</sup> For instance, PICGUG states "[B]ecause the CRRC does not provide for the detailed scrutiny of a utility's costs that normally occurs in a base rate proceeding, [it] should not be implemented in this proceeding." PICGUG MB at 7. In fact, considering the review and approval process that is required for PGW's operating and capital budgets, as well as the general review activities of these entities, PGW believes that it is the most reviewed utility in the State.

Most critically, neither a base rate increase, nor any other possible rate increase solution to PGW's cash crisis would provide a response in time to address the financial community and ratings companies' admonition to improve cash and collections immediately – or else. Moreover, the opposing parties conveniently fail to point out the limitations inherent in a base rates case generally, and the particular inapplicability of this massive proceeding to the instant situation. PGW's current problems are due primarily to high gas costs, which in turn have resulted in higher customer bills and additional cash collection shortfalls. This Commission has regularly approved, under Sec. 1307 of the Public Utility Code, similar targeted flexible automatic adjustment mechanisms to address a wide array of expenses across a broad cross-section of the state's public utilities.<sup>33</sup> Were it to accept the opponents' arguments, this Commission would abandon its Sec. 1307(a) statutory directive to establish a "sliding scale of rates or other method for the automatic adjustment of the rates of the public utility..." outside of the Sec. 1308 requirement for a full base rates case.<sup>34</sup> There are situations where a narrowly tailored and expense-appropriate adjustment clause can address the current need while sparing and preserving the state's regulatory and business resources, consistent with the recognized legislative purpose underlying Sec. 1307(a): "to permit the reflection in customer charges of changes in one component of a utility's cost of providing the public service without the necessity

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<sup>32</sup> Some parties, such as the OCA, have a long history of dogmatic opposition to automatic adjustment clauses despite seemingly all circumstances. For example, the OCA sounded the same cries it has raised in this proceeding while opposing Jackson Sewer Company's sewer treatment automatic adjustment clause, the establishment of water utilities' distribution system improvement automatic adjustment clauses, and the Commission's policy encouraging automatic adjustment clauses for the recovery of PennVEST debt. *Pennsylvania Public Utility Commission, et al. v. Jackson Sewer Corp.*, 2001 Pa. PUC LEXIS 53, \*\*58-64; *Petition of Pennsylvania-American Water Company*, 1996 Pa. PUC LEXIS 182, \*7; *Policy Statement re: PENNVEST Loan Obligations for Water and Sewer Companies*, 1993 Pa. PUC LEXIS 100, \*\*5-6; see PGW MB at 31-35. Indeed, the OCA even opposed the use of an automatic adjustment clause for the recovery of customer education costs related to the promotion of natural gas choice and competition. *Creation and Implementation of a Statewide Consumer Education Program for Natural Gas Competition*, 2000 Pa. PUC LEXIS 12, \*37. As it does here, the OCA asserted that these costs were simply "costs of doing business," not appropriate for automatic adjustment treatment, that should have been recovered through base rates akin to other "business expenses." *Id.* In all of these instances, the Commission rejected the OCA's reflexive opposition to automatic adjustment clauses, and it should do the same here.

<sup>33</sup> PGW MB at 31-32.

<sup>34</sup> PGW MB at 29 (citing language of Sec. 1307(a) directive).

of the broad, costly and time-consuming inquiry required in the case of rate increases generally.”<sup>35</sup>

In addition, all of these arguments ignore the fact that the Commission has recently, initiated an investigation into PGW’s collections practices, its universal service programs and the billing and collection rules applicable to PGW. By all accounts, these cover all the areas that could affect PGW’s cash receipts and uncollectible experience. Accordingly, to the extent that the Commission was concerned with taking action without considering all relevant factors, its June 2 Order assures a comprehensive review will occur, and a base rate increase is unnecessary to accomplish this purpose.

Finally, it is difficult to accept that the calls for a base rate case are indeed, sincere. PGW fully suspects that the same parties that are demanding that the Commission deny the Company’s CRRC request in favor of a base rate proceeding would be the first to oppose, in whole or in substantial part, PGW’s request for a base rate increase. It is hard to avoid the conclusion that the parties are practicing the art of temporizing (i.e., putting something off for no reason other than to avoid dealing with it) at its best. This is particularly true when counsel for at least one of the intervenors (Action Alliance, et al.; its counsel is Community Legal Services) is also a party to PGC/City Council budget proceedings and knows full well that there are no cost items that could have decreased so dramatically as to make up for the huge shortfall in cash receipts and uncollectibles.<sup>36</sup>

**Fiction 4: The CRRC Is Unprecedented In Pennsylvania And Inconsistent with Section 1307(f) and Therefore Deserves Rejection.**<sup>37</sup>

**Facts:** Although this precise clause has not before been seen in Pennsylvania, the CRRC has ample precedent in Pennsylvania Commission cases establishing automatic adjustment clauses pursuant to broad authority granted by valid Pennsylvania statutes. There is a veritable laundry list of automatic adjustment mechanisms that the Commission has approved (and the

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<sup>35</sup> *National Fuel Gas Distribution Corp.*, 473 A.2d at 1121. PGW MB at 32.

<sup>36</sup> See PGW St. CRRC-5, Exh. TEK-5.

<sup>37</sup> OCA MB at 16-23; Philadelphia Public Officials MB at 7-9, 11-12; PICGUG MB at 3-4.

courts have upheld against attack) under Sec. 1307(a) and (e) of the Code, many of which PGW lists in its main brief at pages 31-32. Recognizing the weakness of their claim, the opposing parties attempt to limit their argument to the narrow confines of the particular CRRC mechanism, claiming either that it is this mechanism itself that is unprecedented,<sup>38</sup> or that the use of this mechanism for uncollectible accounts is unprecedented or illegal.<sup>39</sup> Both arguments are wrong.<sup>40</sup>

First, the argument that natural gas distribution companies may only establish automatic adjustment clauses pursuant to section 1307(f) and only to recover natural gas costs<sup>41</sup> is not supported by any fair reading of the Act. Under section 1307(f), natural gas distribution companies may have a sliding scale of rates *as to natural gas costs* only pursuant to that subsection.<sup>42</sup> As the Public Officials point out, the definition of natural gas costs specifically do not include uncollectibles or cash receipts shortfalls associated with natural gas purchases. However, nothing in that section limits an NGDC from establishing a sliding scale of rates mechanism for an item *other than* a natural gas cost pursuant to Section 1307(a).<sup>43</sup>

Similarly without merit is the argument that, because the PUC has never before established a clause of this type, it should reject PGW's proposal. Under the logic of the opposing parties' arguments, this Commission never should have established *any* automatic adjustment mechanisms because, at one time, *none* of these mechanisms had any precedent in Pennsylvania law. Each one of these automatic adjustment clauses required the Commission, at one time or another, to *establish* a precedent. In each circumstance, the Commission was compelled to set aside the opponents' narrow mindset and act within the flexible statutory authority granted it to act in the broader public interest. Had the Commission given any

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<sup>38</sup> PICCUG MB at 3. *Accord*, Philadelphia Public Officials MB at 3 (CRRC is an "extraordinary" proposal.)

<sup>39</sup> *E.g.*, OCA MB at 16-17.

<sup>40</sup> A complete recitation of the Pennsylvania and foreign jurisdiction statutory and precedential support for PGW's proposal is set forth at Section III(C) and (D) of PGW's Main Brief.

<sup>41</sup> Public Officials MB at 7-9.

<sup>42</sup> 66 Pa. C. S. § 1307(f).

<sup>43</sup> PGW MB at Section III(C)(1)-(3).

credence to the flawed “logic” that the opposing parties now proffer, the state still would be careening bumper car-like from one base rates case to the next in a never ending attempt to micro-manage particularly narrow issues with particularly overbroad, unsuitable proceedings.

**Fiction 5: Out Of State Precedent Directly Establishing Similar Adjustment Mechanisms Does Not Apply Or Otherwise Is Distinguishable.<sup>44</sup>**

**Facts:** There is recent and authoritative out-of-state precedent directly on point establishing flexible automatic adjustment clauses to address utility undercollections resulting from higher gas bills and reduced customer payment. The Commission decisions in Ohio and Tennessee are particularly on point, and have been described in detail in PGW’s main brief at 39-41. The bottom line is that both commissions established clauses targeted to help reduce gas utility undercollections. The Ohio Order is particularly apt, finding that high gas costs and related uncollectibles are largely not within the control of gas utilities, and that a special clause to remedy the undercollections through *pro forma* and amortized charges was just, reasonable and in the public interest.<sup>45</sup>

OCA argues that the Ohio, Tennessee and other cases establishing CRRC-like automatic adjustment clauses ought not be followed in Pennsylvania, urging this Commission instead to look to an older North Carolina Utility Commission (“NCUC”) decision denying a somewhat similar request.<sup>46</sup> This is a curious and somewhat contradictory approach. The recent Ohio and Tennessee cases (decided in 2003 and 2004 respectively) address and redress the need for CRRC-like clauses in the context of the most recent utility experiences with higher gas costs, higher customer bills, weather-induced demand and higher uncollectibles expense. They are directly on point, and align with other, similar decisions from the time period contemporaneous with the NCUC case that OCA cites.<sup>47</sup> The NCUC case is clearly a minority decision. It is

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<sup>44</sup> OCA MB at 23-26; PICGUG MB at 4-5.

<sup>45</sup> *In the Matter of the Joint Application of The East Ohio Gas Co. et al.*, No. 03-1127-GA-UNC at 10-12 (OH 2003); *see also*, *Petition of Chattanooga Gas Co. et al* No. 03-00209 (TN, 2004). PGW MB at 39-41.

<sup>46</sup> OCA MB at 23-26. Interestingly, other parties make no attempt to address relevant law from other jurisdictions addressing similar clauses, choosing instead to confine their arguments to rote recitations from Pennsylvania cases concerning single issue and retroactive ratemaking.

<sup>47</sup> *See Petition of United Cities Gas Co.*, No. 14422 (GA, 2001); *Petitions of Atmos Energy Corp. and Roanoke Gas Co.*, PUE 2002-00373 and 2002-00002 (VA, 2002).

inconsistent not only with other similar cases decided at that time (2001), but also is inconsistent with the recent cases based on more immediate and appropriate experience in the industry.<sup>48</sup> The weight of out-of-state authority clearly and persuasively rests with PGW and offers further, firm support for the decision that this Commission should make: a CRRC mechanism is not unique and has been approved by other regulatory bodies as a reasonable way in which to deal with similar problems.

**Fiction 6: The CRRC Will Result In Unjust and Unreasonably High Rates.<sup>49</sup>**

**Facts:** The CRRC may result in a rate increase, and, depending upon collections success between now and August 31, it may not. If it does, it will establish the increase at only that amount of money necessary to guarantee PGW's historic (and PUC-approved) collections percentages, and recognizing PGW's already approved uncollectible expense allowance of \$55.7 million embedded in its base rates, consistent with the regulatory intent behind Sec. 1307(a) generally and Sec. 1307(f) specifically. It will assure PGW of the cash working capital it needs both to sustain operations and to satisfy the rating agencies.

Several parties argue that the CRRC somehow will result in rates that are unjust and unreasonable, contrary to the general requirements of Sec. 1301.<sup>50</sup> They have it exactly backwards. The CRRC is specifically designed and targeted only to assure that PGW attains its

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<sup>48</sup> OCA also argues that the Ohio decision should not control because it involved base gas rates established some years earlier than those involving PGW. OCA MB at 23-25. This is a distinction without difference. The evidence is clear that between 2002 and 2004, PGW's gas costs and average residential bill both increased about 50%. PGW MB at 14-15. This is precisely the type of volatility that the Ohio and Tennessee Commissions cited in establishing their respective adjustment clauses.

<sup>49</sup> Philadelphia Public Officials MB at 9-11; OCA MB at 26-41; OSBA MB at 19-21; PHA MB at 7-11; PICGUG MB at 3-6; Action Alliance MB at 24-26.

<sup>50</sup> *See, e.g.*, Action Alliance MB at 23-24 (PGW rates are already high; higher rates could only be unconstitutional); PICGUG MB at 3; PHA MB at 7-9. PHA cites cases for the proposition that rate increases may not be proper in the case of financial mismanagement. PHA fails to appreciate that its cited cases typically involve specific investigations into customer complaints and particularized instances of bad management. In the present case, the only competent record evidence proves that extraordinarily high gas costs, economic conditions, and weather, factors clearly beyond PGW management's control, have caused the current financial crisis. The record evidence also demonstrates PGW management's prompt response, including instituting the successful billing initiative. PHA's argument is totally misplaced and must fail for many reasons, not the least of which is an utter and total failure of proof. Finally, all of these arguments ignore the fact that the Commission has, indeed, initiated an investigation into PGW's collections practices, its universal service programs and the billing and collection rules applicable to PGW.

historic collections percentages consistent with the PUC's past base rate determinations. It is nothing more than a keep whole mechanism, designed not to increase the Company's coffers, but to protect them against the ravages of volatility-induced undercollections. It does not ask the Commission to make any new substantive determinations.

Moreover, it may not even result in an actual rate increase. There are many possible scenarios that will result in a CRRC of zero.<sup>51</sup> The rate increase that the parties claim most to fear is the very increase they will cause if PGW is forced to file a broad, untargeted base rates case. It is that result that the opposing parties should (but do not) strain to avoid; instead, they seem hell-bent on making that very case a reality. The Commission has the discretion to step in and redirect the parties to a solution short of the base rate case. The CRRC will address the real issue here, and obviate any concern with base rates.

**Fiction 7: The PUC Should Deny the CRRC Because Rates are Already Too High.**

**Facts:** OCA has also made the remarkable argument that, because PGW's rate are already high any further increase would be per se unreasonable.<sup>52</sup> This is simply not legally supportable. The Gas Choice Act mandated that PGW was entitled to rates that permitted it to recover all of its expenses plus a reasonable amount of working capital.<sup>53</sup> Further, the Act requires that the Commission permit PGW rates which permit the Company to satisfy all of its bond covenants, one of which being that it have sufficient funds to pay all of its bills when they come due.<sup>54</sup> To the extent that PGW demonstrates that it needs the CRRC mechanism to assure the necessary level of cash to accomplish that result (which it has), the Commission cannot side step this responsibility because rates are already high.

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<sup>51</sup> PGW MB at 27-29. OSBA, however, persists in its discredited "doomsday" scenario espoused by Mr. Knecht that the CRRC will result in stunningly high rates in the coming years. OSBA MB at 20-21. Dr. Peach has thoroughly discredited this misuse of his testimony and models, persuasively explaining that a properly applied model with real world constraints justifies establishing a workable and realistic CRRC. PGW MB at 45.

<sup>52</sup> OCA MB at 28-29.

<sup>53</sup> 66 Pa. C.S. § 2212(e).

<sup>54</sup> *Id.* Notably, the Act also requires the Commission to set rates and charges that will afford the Company the ability to pay an annual fee to the City. 66 Pa. C.S. § 2212(f).

**Fiction 8: PGW's Collections Efforts Should Be Given More Time To Work Before The Commission Takes Any Rate Action.<sup>55</sup>**

**Facts:** Some opposing parties point to PGW's recent collections improvement as a reason to deny any relief in this matter.<sup>56</sup> They argue that PGW's renewed emphasis on collections should obviate any cash receipts deficiency that PGW currently suffers. They miss the point of the CRRC mechanism and the contradiction of their other arguments.<sup>57</sup>

The entire point of the CRRC mechanism is to put into place the insurance policy, the backstop, needed to assure PGW's historic collections percentage as contemplated in base rates. Importantly, the CRRC also will assure PGW's bondholders and rating agencies that PGW will sustain the cash working capital it needs to maintain its investment bond rating. There is no doubt PGW has experienced recent success with its revamped collections efforts, but that effort was not expected to and, indeed, likely will not do more than return PGW's collections levels to historic levels. For example, in spite of the fact that natural gas costs have increased to some of the highest levels in recent memory, the Company, nonetheless is projecting that it will improve its collection rate by 4% from the prior year – to 92%. While this success is welcomed, the high gas prices means that, even at a 92% collections rate, its total dollars uncollected are still more than \$10 million over the \$55.7 million assumed in PGW's base rates.<sup>58</sup> Moreover, gas prices in FY 2005 are expected to increase still more – by some \$77 million. It will be very difficult to continue that momentum at these higher prices. The real problem occurs if, despite its best efforts, PGW finds that higher gas costs persist, the Philadelphia economy does not improve for its customers, and colder than normal weather prevails in the fall and winter months (thus increasing gas demand). All could lead to the same cycle of higher bills, lower collections and impaired cash working capital that have landed the parties here in the first instance. The facts

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<sup>55</sup> OCA MB at 15-16; Philadelphia Public Officials MB at 19-21; OSBA MB at 16; Action Alliance MB at 17.

<sup>56</sup> OCA MB at 14; OSBA MB at 16; Action Alliance MB at 17.

<sup>57</sup> For instance, these same parties claim that PGW's problems result from poor management and inadequate collections, not high natural gas costs, cold weather and the general impacts of customer demographics. Yet, under this argument, they claim that PGW is doing so well with its collections that it just needs more time and all will be fine. The truth is that on both points these parties are flat wrong.

<sup>58</sup> See, PGW St. CRRC St. 1, Exh. JRB-6 (modified to reflect a 92% collections percentage).

show that materially improved results – as demanded by the rating agencies – simply will not occur without additional tools, including the assurance of the CRRC.

The CRRC exists only to rectify a shortfall that may occur despite PGW’s best efforts. The opposing parties are free to argue the irresponsible position that PGW, despite its current financial condition, should continue to attempt to collect its bills without any financial safety net or plan in place to deal with the largely uncontrollable contingencies that could lead to lessened collections. PGW and this Commission do not share that luxury.<sup>59</sup> There is not sufficient time to play “wait and see.” The time has come to act – the proper course is to permit and to encourage PGW to continue its improved collections, but with the proper backstop of the CRRC in place should those efforts fall somewhat short.

**Fiction 9: The CRRC Constitutes Single Issue and/or Retroactive Ratemaking.<sup>60</sup>**

**Facts:** The CRRC clearly fits neatly within mainstream Pennsylvania regulatory law and policy, and similar adjustment clauses have been upheld against attack both here and in other jurisdictions.<sup>61</sup> The general prohibition against single issue ratemaking has been found specifically not to apply to automatic adjustment mechanisms under Sec. 1307, which by their very nature are intended to address significant expense items subject to volatility and lack of utility control,<sup>62</sup> that do not warrant the “broad, costly and time-consuming inquiry” required of a base rates case.<sup>63</sup> Likewise, Pennsylvania law recognizes that in the context of ratemaking generally, and in Sec. 1307 ratemaking specifically, recovery for historic extraordinary expenses

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<sup>59</sup> See Attachment A.

<sup>60</sup> Philadelphia Public Officials MB at 11-14; OCA MB at 18-22; PICGUG MB at 5; OSBA MB at 25-26; OTS MB at 8-10; Action Alliance MB at 21-33.

<sup>61</sup> Section III(C)(2) and (4) of PGW’s Main Brief offer a complete refutation of these claims.

<sup>62</sup> PGW MB at 32-33, citing *inter alia*, *PIEC v. Pa. PUC*, 653 A.2d 1336 (Pa. Cmwlth. 1995).

<sup>63</sup> PGW MB at 33, citing, *inter alia*, *National Gas Distribution Corp. v. Pa. PUC*, 473 A.2d 1109 (Pa. Cmwlth. 1984).

not otherwise in base rates, diligently pursued and properly amortized, will be immune to legal attack as an exception to the general prohibition against retroactive ratemaking.<sup>64</sup>

Failing to recognize the specific authorities directly supporting PGW's requested relief, several parties pithily cite cases stating the general proscriptions against single-issue and retroactive ratemaking.<sup>65</sup> The cited cases in some instances actually uphold the very E-factor-type relief that PGW seeks here.<sup>66</sup> Importantly, none of the parties note that, even if they were correct, the retroactive ratemaking claim would only apply to the E-factor portion of the CRRC and would not act as a bar to its general adoption. Indicative of the fact that their position is completely meritless, many parties simply ignore one of the leading Pennsylvania cases establishing E-factor-like recovery for a similar uncollectible accounts arrearage, in effect conceding its relevance and authority.<sup>67</sup>

PGW does not dispute that general ratemaking principles frown upon single issue and retroactive ratemaking, and that there are Pennsylvania authorities stating this point. Rather, PGW vigorously asserts that its proposal falls squarely within the well-recognized Pennsylvania statutory and case law exceptions to these general legal principles, exceptions clearly authorizing both the establishment of the CRRC in the first instance and PGW's recovery of current extraordinary uncollectibles or cash receipts shortfalls through proper amortization. PGW welcomes the Commission's careful reading of Pennsylvania law<sup>68</sup> on these points.

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<sup>64</sup> PGW MB at 35-38, citing many authorities including *inter alia* *Columbia Gas of Pa. v. Pa. PUC*, 613 A.2d 74 (Pa. Cmwlth. 1992).

<sup>65</sup> OCA MB at 18-22; Action Alliance MB at 29-32; Philadelphia Public Officials MB at 11-14.

<sup>66</sup> *E.g.*, OCA discusses at length the *Popowsky* case, where the court *upheld* E-factor type relief for a utility's past expenses not otherwise included in base rates. OCA MB at 21. Action Alliance cites the *Columbia Gas* case for the general proposition that ratemaking must be prospective, but totally ignores the court's holding and rationale permitting the utility to recover historic uncollectible accounts arrearages through an E-factor type amortization. Action Alliance MB at 30.

<sup>67</sup> *E.g.*, OCA, OSBA and Philadelphia Public Officials do not even cite the *Columbia Gas* case (see PGW MB at 36) in their briefs. As noted, Action Alliance cites the case for a general proposition of law *contrary* to the exception that the case establishes in favor of utilities like PGW seeking recovery of current or past uncollectibles expense.

<sup>68</sup> Some parties point to the interpretations of Messrs. Knecht and LeLash on the issues of single issue and retroactive ratemaking. *E.g.*, OCA MB at 13; Philadelphia Public Officials MB at 11. With due respect to

**Fiction 10: The CRRC is Too Speculative.**

**Facts:** OCA and other parties have stated that the CRRC is “speculative” and subject to manipulation.<sup>69</sup> Nothing could be further from the truth. PGW’s proposal is that the going forward CRRC will be set based upon the actual collections percentage from the prior fiscal year. Unlike uncollectible expense (which does involve some projection) the cash receipts percentage is actual billings compare) to actual receipts during the same period. In fact, there is no estimation involved.

**Fiction 11: The CRRC Cannot Properly Reconcile Identified Costs.<sup>70</sup>**

**Facts:** The precise workings of the CRRC are not in issue. PGW has explained the mechanics behind the clause, and the parties appear to understand how the clause would operate in a given year.<sup>71</sup> Some of the opposing parties believe, however, that the CRRC cannot reconcile identified costs, at least in part because the \$55.7 million uncollectibles account expense number is suspect.<sup>72</sup> They are wrong on both counts.

First, the CRRC is designed as a make-whole mechanism – it is meant to assure PGW’s cash receipts at historic levels. It is not a reconcilable clause.<sup>73</sup> Opposing arguments to the effect that the clause is not conducive to reconciliation are therefore mere tautology. They mean nothing and prove nothing. Second, the argument that the CRRC cannot work because the true adjusted size of PGW’s current \$55.7 million uncollectible accounts expense is unknown

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these gentlemen, PGW prefers that the case be decided in accordance with the interpretations given these legal concepts by this Commission and the learned Commonwealth and Supreme Courts of Pennsylvania.

<sup>69</sup> OCA MB at 8; PICGUG at 3, 6.

<sup>70</sup> OCA MB at 16-18; Philadelphia Public Officials MB at 7-9; OTS MB at 9-10; Action Alliance MB at 24 - 28.

<sup>71</sup> PGW MB at 24-29.

<sup>72</sup> Action Alliance MB at 25, 28; OCA MB at 8.

<sup>73</sup> OCA and others apparently *continue to misunderstand or misconstrue* the concept, if not the math workings, of the CRRC. Once again: any dollar of uncollected cash may or may not become permanently uncollectible. The amount the CRRC recovers does not depend on that contingency. If a customer pays that dollar later, it simply adds to PGW’s cash receipts for that year and increases PGW’s collection percentage. Customers will get the benefit of that additional collected dollar in the automatic adjustment of the CRRC. PGW MB at 47.

likewise is fallacy. The Commission established the \$55.7 million allowance in PGW's last fully-litigated rate case. This is the amount for which ratepayers are, in affect, being charged for uncollectible expense, despite the fact that the Company's actual expense is tens of millions of dollars higher.<sup>74</sup>

Moreover, the \$55.7 million allowance is the last PUC pronouncement on the subject. The more recently settled rate case was a "black box" settlement that did not apportion the dollars. The Commission here can choose to follow its last established number; if it chooses to attempt to apportion dollars from the last settlement, it should increase PGW's uncollectibles allowance by \$2.7 million to a total of \$58.4 million.<sup>75</sup> There is nothing unknowable or incalculable here. It is rather a simple math exercise, and ought not stand in the way of the CRRC.

**Fiction 12: The CRRC Would Remove PGW's Incentive To Collect Its Bills.<sup>76</sup>**

**Facts:** PGW retains a strong incentive to collect its bills, and nothing about the CRRC in theory or practice will remove this incentive. The most powerful incentive, as discussed many times, is that the rating agencies have made clear that collections improvement must occur in order to avoid a disastrous downgrade to junk status. For this reason, Mr. Knudsen made it abundantly clear at the hearing that PGW must increase its cash receipts, and is irrevocably committed to the collections initiative to bring in the necessary cash.<sup>77</sup> Even small changes in collections percentages equate with millions of dollars in receivables, and PGW does not have the luxury to relax its collections efforts at all.<sup>78</sup>

Several opponents persist in their discredited positions that the CRRC somehow theoretically will reduce PGW's incentive to collect its bills,<sup>79</sup> or will create some bizarre

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<sup>74</sup> PGW MB at 16; *see also* *Id.* at 9-11.

<sup>75</sup> PGW MB at 47.

<sup>76</sup> OTS MB at 8-9; PICGUG MB at 17-18; OCA MB at 22-23.

<sup>77</sup> PGW St. CRRC-5; Tr. 858-859.

<sup>78</sup> PGW MB at 43.

<sup>79</sup> *E.g.*, OCA MB at 22; OSBA MB at 17-18; PICCUG MB at 6.

gaming scenario.<sup>80</sup> The opposite is actually true. The CRRC actually increases PGW's incentive to bill its customers. As it increases collections to percentages above historic levels, PGW increases its cash working capital. Customers realize the benefit as well, since the CRRC, if any, will be established at zero for the following fiscal year, the Company will retain its bond rating, and eventually will be able to lower its short and long term debt, make its annual payment to the City, and repay the City loan all of which inure to the benefit of the customers.<sup>81</sup>

**Fiction 13: The Public Generally Are Against The CRRC.<sup>82</sup>**

**Facts:** Some opponents trumpet the testimony of citizens and their representatives in the public forums leading up to the hearings as a reason for denying the CRRC.<sup>83</sup> PGW notes initially that few members of the public will ever speak out publicly or privately in favor of a utility rate increase, or probably any other rate increase. This is just a matter of pocket-book common sense, which the Pennsylvania authorities have recognized and discounted when considering rate increases.<sup>84</sup>

But the public testimony also should be discounted for the simple reason that it displayed a basic misunderstanding of the ratemaking process. Members of the public railed at PGW for attempting to collect bad debt from citizens with good payment records.<sup>85</sup> But, that is precisely what the ratemaking process both permits and requires. All utilities (and other companies as well) have uncollectible accounts expenses, both actual and projected, which must be considered and recovered in base rates.<sup>86</sup> The public *always* pays for the bad debts of others; it is part of the

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<sup>80</sup> PICCUG MB at 6. Thankfully, the remaining opponents seem to have ignored this earlier aspect of their case in these briefs. Mr. Knudsen and the other PGW executives clearly are not interested in playing games.

<sup>81</sup> PGW MB at 25-26.

<sup>82</sup> Action Alliance MB at 24, 32; OCA MB at 29-41; Philadelphia Public Official MB at 9.

<sup>83</sup> OCA MB at 29-41; Action Alliance MB at 24, 32.

<sup>84</sup> *Accord, Popowsky v. Pa. PUC et al.*, 706 A.2d 1197 (Pa. 1997).

<sup>85</sup> *E.g.*, testimony summaries in Action Alliance MB at 24, 33; OCA MB at 40-41.

<sup>86</sup> PGW MB at 10.

price of every good or service that we purchase. Attempting to collect bad debt expense from those customers who fail to pay their bills would not be particularly productive.

This basic economic fact has been lost in the rhetoric, along with other facts that a fully informed body politic needs to know.<sup>87</sup> PGW has been working to improve its operations, service quality, customer relations and overall financial position.<sup>88</sup> It faces gas cost challenges largely beyond its control.<sup>89</sup> It struggles to maintain high quality service to an economically challenged customer base.<sup>90</sup> It is beyond cavil that a solvent gas utility working on their behalf to deliver high quality service is in the public interest. It cannot truly be in anyone's interest to produce a financially-ravaged shell struggling to keep the gas flowing (and flowing safely) as it slides further into insolvency. Since the public understandably did not have all of these facts in front of them their opinions are not a valid basis on which the Commission could draw any conclusions (other than the public doesn't like rate increases or to pay for others who don't pay.)

**Fiction 14: The CRRC Constitutes Impermissible Rate Discrimination Between Classes of Customers.**<sup>91</sup>

**Facts:** The CRRC mechanism, if and when activated, would simply operate much in the same fashion as the current uncollectible accounts expense mechanism operates today. Consistent with standard regulatory and business practice, it would spread the costs of undercollection over the ratepayer base. The idea is to collect authorized revenues to cover the entirety of authorized expenses in order to secure the necessary cash working capital to meet operating costs and pay down short and long term debt.

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<sup>87</sup> For instance, many participants in the public input hearings based their opposition on the misplaced assumption that the past mismanagement and alleged criminal activity of the Company's prior management continues today. *See, e.g.*, Tr. 54, 116, 130. Such is clearly not the case.

<sup>88</sup> PGW MB at 20-21.

<sup>89</sup> PGW MB at 13-19.

<sup>90</sup> PGW Sts. CRRC-4 and CRRC-4R. This raises another point of fine irony. Although flayed by certain politicians and some members of the public in the recent hearings, PGW does more as a company for the poor and elderly than any other utility in Pennsylvania. In fact, PGW's programs are so extensive that OSBA witness Knecht criticized them as being overly generous, and suggested that PGW should prevail upon the regulators to reduce benefits to senior citizens and the poor. OSBA St. No. 1 at 21-22. Now, those very programs are being investigated by the Commission in a related docket.

<sup>91</sup> OSBA MB at 19-21; PHA MB at 12-14.

Certain parties claim that this accepted mechanism somehow would result in unreasonable discrimination between business and residential customers, or between certain classes of residential customers, since some customers with better payment histories would be asked to shoulder more of the burden of those customers with payment difficulties. These claims must fail.<sup>92</sup>

Pennsylvania law clearly recognizes the authority and necessity for this Commission to establish just and reasonable rates supported by competent evidence, even where those rates will have differing impacts on classes of customers.<sup>93</sup> The *Pennsylvania Retailers'* case is directly on point. There, the Commission approved as just and reasonable a telephone company's rates for vertical features, even though the rates were set at multiples of their true cost with the intent to help subsidize residential users of basic service. A consortium of business users appealed, arguing that the high profit margins associated with vertical services unreasonably discriminated against them as heavy users of these services, and in favor of residential basic service users. The Court flatly rejected this claim, and upheld the Commission with a ringing endorsement from an earlier case that also favorably decided a similar issue:

**There is no requirement that the rates for different classes of service must be either uniform or equal or that they must be equally profitable. Differences in rates between classes of customers...are not only permissible but often are desirable and even necessary to achieve reasonable efficiency and economy of operation.** Rate structure, which is an essential, integral component of ratemaking, is not merely a mathematical exercise applying theoretical principles. Rate structure must be based on the hard economic facts of life and a complete and thorough knowledge and understanding of all the facts and circumstances which affect rates and services; and the **rates must be designed to furnish the most efficient and satisfactory service at the lowest reasonable price for the greatest number of customers, i.e., the public generally.**<sup>94</sup>

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<sup>92</sup> *Id.*

<sup>93</sup> *Pennsylvania Retailers' Associations et als. v. Pa. PUC et als.*, 440 A.2d 1267 (Pa. Cmwlth. 1982).  
*Accord, The Public Advocate et als. v. City of Philadelphia et al.*, 26 Phila. 527 (Common Pleas 1993).

<sup>94</sup> 440 A.2d at 1271 (citing *Philadelphia Suburban Transportation Co. v. Pa. PUC*, 281 A.2d 179, 186 (Pa. Cmwlth. 1971)) (emphasis added).

This Commission is perfectly justified, on the record before it,<sup>95</sup> to continue to enforce the greater public interest through the proper balancing of rates among the different classes of PGW's customers. This may cause some classes of customers to shoulder more of undercollection burden than others, but will result in an overall benefit to the public at large.<sup>96</sup>

**Fiction 15: PGW Lacked Authority To Seek The CRRC.<sup>97</sup>**

**Facts:** The brief of the Philadelphia Public Officials raises at this late date and for the first time the argument that this Commission should not consider PGW's Petition for a CRRC on the grounds that PGW lacked authorization from the Philadelphia Gas Commission. This argument is totally without merit and should be rejected summarily.

First, the Commission need not address the arguments regarding the internal governance of PGW and its authority to make filings with the PUC because those arguments are, in reality, a request that the Commission dismiss PGW's Petition without reaching the merits, a claim which should have been raised in a preliminary motion under Section 5.101 of the Commission's regulations. Having failed to do so, this issue has been waived.<sup>98</sup>

Second, the Commission has independent authority, both generally under Section 1307 of the Code and specifically pursuant to Section 2212, to regulate PGW, establish rates, tariffs, rules and procedures for it, and waive or modify any existing provisions of law (other than Section 2212) when necessary to meet the unique needs of the Company. This plainly includes

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<sup>95</sup> See PGW Sts. No. CRRC-4 and CRRC-4R; Tr. 403-408.

<sup>96</sup> *Public Advocate v. City of Philadelphia, supra.* (Commission was justified in establishing what otherwise would appear to be a discriminatory rate for stormwater collection absent clear record evidence of unreasonable discrimination or Commission abuse of discretion).

<sup>97</sup> Philadelphia Public Officials MB at 3-7, 24-26.

<sup>98</sup> See *Blue & White Lines, Inc. v. Waddington*, Docket A-00108279C9301, Initial Decision (May 24, 1994) at 15; Pa.R.C.P. 1032 (Commission regulations are generally interpreted consistently with the Rules of Civil Procedure). *Accord, Beaver Valley Alloy Foundry Co. v. Therma-Fab, Inc.*, 814 A.2d 217, 225 (Pa. Super. 2002) (stating the well-settled rule that when a party fails to raise objections or defenses in a preliminary objection or answer the matters are waived). This issue has not been raised in any answer to the CRRC Petition. 52 Pa. Code § 5.61(c) (facts deemed admitted). Importantly, the argument raised by the Public Officials regarding PGW's authority to make the CRRC filing does not raise a question of the Commission's jurisdiction to decide this Petition. The Commission clearly has subject matter jurisdiction over requests for automatic adjustment clauses, afforded by Section 1307(a), and it has jurisdiction over PGW pursuant to Section 2212(b) and (c) of the Public Utility Code.

establishing a CRRC. Whether PGW did or did not comply with the municipal approval requirements, if any, is not relevant to the PUC's obligations and authority under the Public Utility Code.

Moreover, the arguments that PGW needs to obtain approval by PGC and/or City Council of its filings to this Commission are beyond the Commission's jurisdiction to resolve. Nothing in the Public Utility Code empowers the Commission to resolve disputes between the board of directors of a utility and entities related to or affiliated with that utility's owners (i.e., City Council and the PGC.) Similarly, nothing in the Code affords the PUC jurisdiction to interpret and apply Philadelphia's First Class City Home Rule Charter or its Management Agreement Ordinance in order to resolve questions about what actions PGW's board of directors (the PFMC) may take and under what conditions it must obtain prior approval from other City bodies in order to take them.

Notably, the Public Officials appear to equate City Council and the PGC to PGW's "governing corporate board."<sup>99</sup> The Philadelphia Facilities Management Corporation (PFMC) is the "governing corporate board" or board of directors of PGW. The PFMC did approve the filing of PGW's CRRC Petition. Indeed, City Council and the PGC, while important voices therein, do not even equate to the Company's owner or shareholders; which is, of course, the City of Philadelphia.

To the extent that a response to the merits is deemed necessary, PGW denies Philadelphia Public Officials' claims that PGW lacked the authority to submit this Petition and that some prior approval from Council or the PGC was required to make that or any other filing with the Commission. Section I(1) of the Management Agreement, which governs the relationship between PGW's board, the PFMC, and the City, clearly authorizes the PFMC to "manage and operate" the Gas Works. The management and operation of PGW plainly includes taking the steps necessary to satisfy legal requirements imposed by state statutes, as well as interacting with the Company's regulators, at this time the PUC.<sup>100</sup> Moreover, to the extent that the Public

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<sup>99</sup> Public Officials MB at 6.

<sup>100</sup> The Management Agreement, a part of the record in numerous proceedings before this Commission and actually an Ordinance of Philadelphia City Council, is attached hereto as Attachment B.

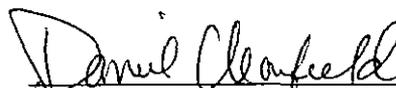
Officials are relying upon provisions in the Home Rule Charter or the Management Agreement authorizing either PGC or City Council to set or approve rates for PGW or make such other determinations that approach or infringe those powers and duties now lodged with the Commission, such authority is either inapplicable or has been abrogated by the Gas Choice Act.<sup>101</sup>

Thus, whether the Commission deems this argument waived procedurally, beyond its jurisdiction to decide, or simply erroneous on the merits, it should reject the Public Officials' position on the Company's authority to file the CRRC Petition.

### III. CONCLUSION

PGW respectfully requests that the Commission reject the arguments of the opposing parties, and approve the Petition of PGW to establish a Cash Receipts Reconciliation Clause mechanism.

Respectfully submitted,



\_\_\_\_\_  
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Date: June 22, 2004

<sup>101</sup> Gas Choice Act, Act 1999-21, §§ 4 and 8 (provisions of Home Rule Charter, First Class City Home Rule Act, and First Class City Government Law abrogated); *Philadelphia Facilities Management Corp. v. Biester*, 431 A.2d 1123, 1132-33 (Pa. Cmwlth. 1981) (City's ownership and operation of PGW is a private, proprietary and business function, and not a municipal function, and therefore the First Class City Home Rule Charter Act is inapplicable and the conduct may only be undertaken in accordance with state law).

# ATTACHMENT A

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## Your Connection to Standard & Poor's Utilities Ratings Team

Standard & Poor's is pleased to provide ongoing service to the investment community.

### Philadelphia Gas Works Senior Bond Rating Lowered to 'BBB-'

**Publication date:** 09-Apr-2004

**Analyst(s):** Jeanny Silva, New York (1) 212-438-1776;  
Aneesh Prabhu, New York (1) 212-438-1285

#### Rationale

Standard & Poor's Ratings Services lowered its rating on Philadelphia Gas Works' (PGW) senior revenue bonds to 'BBB-' from 'BBB'. At the same time, Standard & Poor's lowered its rating on PGW's subordinate revenue bonds to 'BB+' from 'BBB-'. The outlook remains negative.

PGW is the nation's largest municipally owned gas utility and the only local gas distributor serving approximately 498,000 customers within the city limits of Philadelphia, Pa. The utility has approximately \$1 billion in total debt outstanding.

The ratings downgrade reflects a weakened liquidity position and declining credit measures fueled by collection rates that deteriorated appreciably in the last year. Standard & Poor's had anticipated collection rates to improve; however, as gas prices and customer bills climbed in the last year, collection rates deteriorated even further. The demographics of PGW's service territory are weak and structural impediments to collection are exacerbated as gas prices rise.

PGW's unrestricted cash reserves are currently below \$1 million, representing less than 1 day's cash. Cash flow from operations, which takes into account PGW's low collection rates, is generally insufficient to cover the utility's fixed charges in high gas price years. Throughout the year, its \$80 million commercial paper program is often fully drawn. To deal with the current liquidity strain, PGW has entered into gas storage deferral contracts, is seeking cash receipts-related rate relief from the Pennsylvania Public Utility Commission (PUC), and has requested annual payment forgiveness from the city of Philadelphia for the next five years. The lowered ratings assume that PGW will obtain annual payment forgiveness from the city even though such payment forgiveness is still subject to City Council approval. Historically, PGW has depended on a variety of one-time financial transactions to meet coverage of fixed charges. Fixed charges have historically included a mandatory \$18 million payment to

the city. The aforementioned one-time financial transactions have included obtaining a \$45 million loan from the city and monetizing guaranteed investment contracts connected with a portion of PGW's sinking fund reserves.

Although PGW's gas storage deferral contracts delay cash outlays in liquidity tight summer months, Standard & Poor's believes that the contracts affect PGW's overall cost structure and as such its cash margins. Moreover, while the outcome of the cash receipts-related rate filing remains uncertain, even if such relief were granted, it is unclear that collections and cash-basis coverage of fixed charges would improve. In the end, the demographics of PGW's service territory make it difficult for the utility to stem declining credit measures, particularly as gas prices remain elevated.

PGW's lowered ratings reflect exposure to below-average markets and low collection rates that reduce the efficacy of PGW's gas cost recovery mechanism and expose the utility to fuel price risk. Other credit weaknesses include high debt levels, thin margins, and a weak liquidity position. These weaknesses are partially offset by a relatively supportive regulatory environment, a lack of competitors, and modest levels of support from the city of Philadelphia.

Over the past five years, Philadelphia's population has declined by approximately 1.2% per year on a compounded annual basis. In addition, the city's median household effective buying income is only 74% of the national average. PGW's exposure to weak markets has contributed to a significant lag in the collection of receivables. Nearly 60% of PGW's gross receivables are currently more than 90 days in arrears. In 2003, bad debt reserve as a percent of gross receivables was 71.1%. Although poor collections have plagued PGW for some time, the situation seems to have worsened in the past year. In 2003, PGW collected less than 87% of billed gas revenues. The utility's historical average is 92%. Standard & Poor's recognizes management's recent efforts to address PGW's low collection rates. These include a recent campaign to notify 130,000 delinquent customers of service termination in the event payment arrangements are not made and increasing eligible customer participation in federal home energy assistance programs such as LIHEAP. Standard & Poor's expects these initiatives will in the very least stem any further decline in collection rates.

PGW's debt per customer is currently about \$2,000 per customer, which is high when compared to other municipal utilities. Moreover, as capital expenditures are not currently internally funded, debt is projected to increase. PGW's collection problems contribute to thin cash margins. During 2003, cash flow from operations plus certain non-operating revenues over fixed charges declined to 0.92x from 1.23x in 2002. Going forward, Standard & Poor's projects that should collection rates remain at 2003 levels (87%), PGW's cash-basis coverage of fixed charges (excluding its annual payment to the city) will remain at or below 1x. As such, the utility's liquidity position is likely to remain challenged.

The PUC, which regulates PGW's rates, has in recent years provided supportive rate relief to the utility. Standard & Poor's views PGW's regulatory environment as favorable to credit quality. Standard & Poor's also assumes that the city will provide modest levels of operational support to PGW going forward. Such support includes a suspension of PGW's annual payment to the city for the next five years and a deferral of PGW's \$45 million city loan-related bullet maturity until 2008.

## Outlook

Ratings will be lowered further if PGW's financial profile weakens over the near term and collection rates and cash margins do not improve materially. Additionally, any of the following events could have negative ratings implications: if access to short-term borrowing is restricted, if suppliers place additional liquidity demands on PGW, or if certain support from the city is not forthcoming. The lowered ratings are predicated on the city providing annual payment forgiveness to PGW for at least the next four years, and on the city allowing PGW to defer its \$45 million loan payable until 2008. In the absence of such support, ratings will be lowered further.

Complete ratings information is available to subscribers of RatingsDirect, Standard & Poor's Web-based credit analysis system, at [www.ratingsdirect.com](http://www.ratingsdirect.com). All ratings affected by this rating action can be found

on Standard & Poor's public Web site at [www.standardandpoors.com](http://www.standardandpoors.com); under Credit Ratings in the left navigation bar, select Find Ratings, then Credit Ratings Search.

For a complete list of ratings, please click the hyperlink provided here

<http://www2.standardandpoors.com/NASApp/cs/ContentServer?pagename=sp/Page/FixedIncomeRatingActionsPg>

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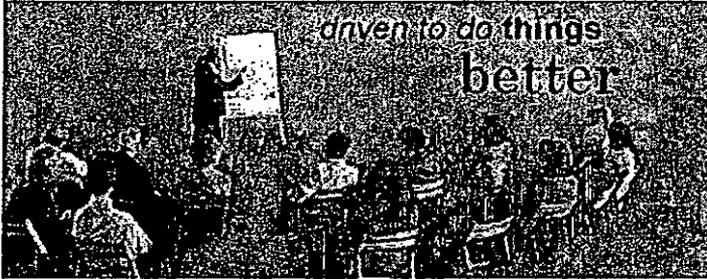
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# FitchRatings



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## Fitch Lowers Philadelphia Gas Works Revs to 'BBB-'/ 'BB+';

23 Apr 2004 1:53 PM (EDT)

Fitch Ratings-Washington, D.C.-April 23, 2004: Fitch Ratings downgrades to 'BBB-' from 'BBB+' its rating on revenue bonds (1975 ordinance) and \$594.0 million of outstanding gas works revenue bonds (senior 1998 ordinance bonds is lowered to 'BB+' from 'BBB'. The Rating Outlook on all outstanding revenue bonds is revised to 'Stable'.

The rating actions primarily reflect PGW's sharply deteriorated liquidity position and the limited at current levels. PGW can not currently generate sufficient cash from operations to meet all of its financial needs from external sources for liquidity. While the city appears committed to PGW's success, as evidenced by a proposal to grant back its annual \$18 million payment from PGW in each of the next five years, years given its own financial difficulties. Fitch rates the city's general obligation bonds 'A-' with a 1998 fund deficit of \$8 million. For PGW, regaining a Stable Outlook could be achieved by the successful implementation of the enhanced collections program and/or a strengthening of the city's weakened financial position.

A major contributor to PGW's current financial difficulties is a dramatic rise in accounts receivable. In 2002, PGW officials largely attribute the increase to pass-through of rising commodity prices that necessitated modifications to the billing system related to implementation of the commonwealth's gas choice law and collection delays. These modifications are substantially complete.

PGW has implemented an aggressive program to collect outstanding bills, including an unprecedented program during the heating season. Under current rules, the utility is prohibited from shutting off gas during the winter. PGW has approved a surcharge, equal to \$80 per year for the average customer, to offset cash flow problem. Collections have improved, but required PUC approval is not expected until this summer at the earliest.

Debt service coverage showed modest improvement in fiscal 2003 compared to very slim margins in 2002. Debt service coverage, was 1.28 times (x) in 2003 and PGW was in compliance with all applicable rate covenants on its debt. Debt service coverage is estimated to be 1.29x, assuming successful implementation of the enhanced collections program. Debt service coverage is based on estimated cash received, not on actual cash received. Fitch calculates that cash generated from operations is less than 1.0x coverage of all debt service obligations.

PGW expects to renew its \$80 million letter-of-credit backed commercial paper line over the next present critical cash flow challenges to PGW and the successful engagement of external sources of revenue bonds later this year to finance normal capital expenditures.

Contact: Joseph D. Mason +1-703-245-3068, McLean or Karl Pfeil +1-212-908-0516 or Amy R. Li

Media Relations: James Jockle +1-212-908-0547, New York.

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**Moody's Investors Service**

Global Credit Research

Rating Update

8 JUN 2004

**Rating Update: Philadelphia (City of) PA Gas Enterprise**

**MOODY'S PLACES PHILADELPHIA GAS WORKS CREDIT RATINGS ON WATCHLIST**

**MOODY'S WILL EVALUATE PGW PLAN, INCLUDING PROGRESS ON RATE COLLECTIONS**

Gas Utilities  
PA

**Opinion**

NEW YORK, Jun 8, 2004 -- Moody's Investors Service has placed on Watchlist the credit ratings of the Philadelphia Gas Works (PGW) for possible downgrade. The Watchlist action affects the Baa2 credit rating on PGW's outstanding \$917 million senior lien revenue bonds and Baa3 credit rating on the \$25 million subordinate lien bonds.

PGW has faced a significant cash flow crunch due to the slowed payment by customers of record high gas bills. While PGW has demonstrated that management is focused on the problem and the current marginal cash position allows for the business to continue to operate, further improvement to PGW's liquidity are required to maintain the current rating level. Moody's plans to evaluate the success of the more aggressive rate collection effort; the success of legislative and regulatory changes to rates and/or collection rules; the certainty and terms of the renewal of the utility's commercial paper program; and other elements of PGW's plan to improve cash flow. Moody's evaluation of these items will form the basis of a Watchlist rating action within the next 90 days.

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# ATTACHMENT B

AGREEMENT

Between

THE CITY OF PHILADELPHIA

AND

THE PHILADELPHIA FACILITIES  
MANAGEMENT CORPORATION

FOR THE MANAGEMENT AND OPERATION  
OF THE PHILADELPHIA GAS WORKS

PRINTING DATE: January, 1996  
Original Agreement Dated December 29, 1972  
Includes Amendments Through December 31, 1995

Original Agreement between the City of Philadelphia and the Philadelphia Facilities Management Corporation was executed on December 29, 1972, for the management and operation of the Philadelphia Gas Works, pursuant to an Ordinance of City Council, approved December 29, 1972 (Bill #455), and to Resolutions of the Board of Directors of the Corporation adopted at a meeting held on December 13, 1972.

Agreement amended, pursuant to an Ordinance of City Council, approved December 14, 1973 (Bill #1021), relating to gas rate discount for Senior Citizens.

Agreement amended, pursuant to an Ordinance of City Council, approved May 30, 1975 (Bill #1870), relating to Gas Works Revenue Bonds.

Agreement amended, pursuant to an Ordinance of City Council, approved November 1, 1976 (Bill #396), relating to Company's management fee.

Agreement amended, pursuant to an Ordinance of City Council, approved June 22, 1978 (Bill #1410), relating to Temporary financing.

Agreement amended, pursuant to an Ordinance of City Council, approved April 10, 1979 (Bill #1874), relating to Company's management fee.

Agreement amended, pursuant to an Ordinance of City Council, approved June 11, 1979 (Bill #1948), relating to Management personnel provided by company; production purchase and delivery of gas; paving requirements; natural gas standards; heating value standards; attendance at meetings; classification of service; definitions and indemnifications.

Agreement amended, pursuant to an Ordinance of City Council, approved September 5, 1980 (Bill #319), relating to Company's management fee.

Agreement amended, pursuant to an Ordinance of City Council, approved September 5, 1980 (Bill #320), relating to Company's management fee.

Agreement amended, pursuant to an Ordinance of City Council, approved September 5, 1980 (Bill #321), relating to Gas Works Temporary Loan Notes.

Agreement amended, pursuant to an Ordinance of City Council, approved June 23, 1981 (Bill #750), relating to Temporary Financing.

Agreement amended, pursuant to an Ordinance of City Council, approved September 22, 1982 (Bill #1315), relating to change in fiscal year basis.

Agreement amended, pursuant to an Ordinance of City Council, approved December 3, 1982 (Bill #1314), relating to Temporary Financing.

Agreement amended, pursuant to an Ordinance of City Council approved April 11, 1990 (Bill #787), relating to compensation.

Agreement amended, pursuant to an Ordinance of City Council approved December 28, 1995 (Bill #1258), relating to Company's management fee.

*Marginal notes are not part of the agreement, but are provided for convenience of use.*

AGREEMENT made this 29th day of December, 1972,  
by and between the CITY OF PHILADELPHIA (hereinafter  
called "City"), and PHILADELPHIA FACILITIES  
MANAGEMENT CORPORATION, a corporation organized  
and existing under the laws of the State of Pennsylvania  
(hereinafter called "Company").

*Parties and dates*

WITNESSETH:

WHEREAS, the City is the owner of a group of real  
and personal assets known as the Philadelphia Gas Works  
("Gas Works"); and

WHEREAS, the City desires to provide quality gas  
services to its citizens at reasonable rates; and

WHEREAS, the Company is a non-profit corporation  
organized for the specific purpose of operating the  
Philadelphia Gas Works.

NOW, THEREFORE, the parties to this Agreement,  
intending to be legally bound, agree as follows:

SECTION I

*General*

1. The City hereby authorizes Company on the  
terms and conditions herein set forth to manage and  
operate all the property, real and personal, collectively  
known as the Gas Works, for the sole and exclusive benefit  
of City; provided, however, City may retrieve from the Gas  
Works any property or equipment which City determines to  
be unnecessary to the efficient and economic operation of  
the Gas Works.

*Authority to  
manage and operate  
PCW property*

*City may retrieve  
surplus property or  
equipment*

2. City, to the extent that it has or shall have the authority or power so to do, authorizes and empowers Company to maintain, change, alter, replace, repair and operate the Gas Works and appurtenances along and beneath the surfaces of the highways, streets, avenues, lanes, alleys, ways and public places in City, for the supply and distribution of gas, subject to provisions hereinafter set forth. For these purposes Company may enter upon, occupy and open all said highways, streets, avenues, lanes, alleys, ways and public places, and supply and distribute gas through pipes laid therein.

*Right to enter highways*

3. During the term of this Agreement, Company will maintain the Gas Works for the sole and exclusive benefit of the City, including all additions, extensions, betterments, and improvements made thereto, in good order and efficient operating condition. Upon termination of this Agreement by expiration of the term or by any other means, City, its agents, servants, or employees shall be entitled without further payment to Company to use all processes established at the Gas Works for the manufacture or distribution of gas of any type or kind. To the extent that use of any such process is authorized by a contract with a third party, City may at its option either continue the use of such process in accordance with the terms of such contract or may discontinue use of such process.

*Company to maintain Gas Works*

*City's use of processes upon termination*

4. Company shall not assign or subcontract this Agreement or any rights hereunder to any person or corporation, nor delegate any duties hereunder.

*Agreement not assignable*

5. Company's primary obligation shall be to apply the highest standards of management practice and diligence to the operation of the Gas Works.

*Highest management standards -*

\*"Recommendations" in the Ordinance.

6. Company shall provide the following personnel for the operation of the Gas Works:

*Management .  
personnel provided  
by Company*

- (a) a chief executive officer;
- (b) a chief operating officer;
- (c) a chief financial officer; and
- (d) such other personnel as deemed appropriate by Company.

All such personnel shall be subject to the approval of the Gas Commission, which approval shall not be unreasonably withheld. In the event the Gas Commission fails to approve any such personnel they shall be replaced by approved personnel forthwith.

*Personnel subject to  
Gas Commission  
approval*

7. Company shall file semi-annual reports with the Gas Commission setting forth all salaries, fringe benefits, expenses and costs incurred by Company in carrying out its duties and responsibilities under the terms and conditions of this Agreement.

*Company to file  
semi-annual reports*

## SECTION II

### *Production, Purchase and Delivery of Gas*

1. The Company shall take all reasonable steps to insure that the capacity of the Gas Works to manufacture, provide and distribute gas is at all times sufficient for the estimated maximum requirements of gas users in the City of Philadelphia.

*Capacity shall  
meet requirements*

2. Company may purchase natural gas or other gas from other parties pursuant to contracts and agreements for such purchases which are first submitted to the Gas Commission for its recommendations and approved by City Council; except that in temporary or emergency situations, Company may purchase natural or other gas from other parties and then seek the approval for such purchase or purchases from the Gas Commission and City Council within 30 days after the initiation of such purchase. In the event such temporary purchase shall be disapproved such supply if continuing shall immediately terminate.

*Approval of purchase of gas*

Company shall have the right to contract with others for the distribution and/or transmission of such gas to the Gas Works or its facilities which are ancillary, attendant or related in any manner to purchase of gas after such contracts are first submitted to the Gas Commission for its recommendations and approved by City council.

*Approval of natural gas delivery facilities*

3. Company, to the extent permitted by the lawfully constituted authorities, may enlarge or extend the facilities for the distribution of gas to an agreed-upon customer meter location as may be necessary to meet the demand for gas. In any situation where such enlargement or extension of the Gas Works' facilities will place an unreasonable financial burden upon the then existing customers, in view of the anticipated revenues to be expected from such enlargement or extension Company shall make reasonable charges for the same as defined from time to time in Company regulations which are approved by the Gas Commission.

*Charges to customers for extensions*

4. The intention of this Agreement is that all changes, additions, extensions, betterments, improvements, alterations and replacements in the Gas Works and in the mains, pipes and appurtenances thereof, and in the property needed to meet the demands for gas as herein provided, shall be made in such a way and manner as shall maintain the Gas Works in good order and condition with the best and most economical processes in use that are customary in the best regulated gas works, to the extent permitted by funds available for said purposes.

*Company shall maintain Gas Works in good order*

5. All openings, excavations and repaving shall be made subject to such general rules, regulations, specifications, ordinances and such Acts of Assembly as may apply, as from time to time shall be in force concerning the opening, excavation and repaving of streets and the protection of travel along the same, and the trenches shall be refilled and repaved with the same material and character of paving as before they were opened, unless otherwise ordered by the Streets Commissioner. Refilling and making opening safe for traffic shall be completed by Company within five (5) days after the pipe, services, or mains have been laid, and said repaving shall be completed, weather permitting, within sixty (60) days thereafter.

*Paving requirements*

6. All ordinances, rules and regulations of City regulating the safety of the piping and fixtures of houses or buildings shall be binding upon Company.

*Safety regulations*

### SECTION III

#### *Standards of Gas*

##### 1. *General*

Company may supply straight natural gas in accordance with the standards provided for in the General Terms and Conditions of the supplier Company's Tariffs on file with the Federal Energy Regulatory Commission and incorporated by reference in the Agreements for the purchase of natural gas, to which the Company, City and Supplier companies are parties. Also for supplemental purposes, the Company may, as necessary, supply other gases interchangeable and compatible with natural gas.

*Natural gas standards*

*Interchangeable supplemental gases*

2. *Testing--Facilities and Inspection*

Adequate facilities for testing the heating value and purity of the gas shall be provided at the Gas Works' expense and equipped with calorimeters for continuously determining the heating value of the gas, apparatus for determining presence of sulphureted hydrogen in the gas, apparatus for determining total sulphur content, apparatus for determining total ammonia content, apparatus for determining specific gravity of the gas and such other apparatus customary and necessary for such purposes, or which will be found to improve the rapidity and accuracy of such testing.

*Plant testing facilities*

The location of testing facilities shall be selected by Company, and approved by Gas Commission.

*Location of testing facilities*

The design and accuracy of all testing apparatus when desired by City, Gas Commission or Company shall be certified by the United States Bureau of Standards.

*Certification of test equipment*

Standards and tests specified herein may be changed and altered from time to time as recommended by Company and approved by Gas Commission.

*Change in standards and tests*

City and Gas Commission shall have the right at all times by its proper officers, during the term of this Agreement, to test the quality and pressure of gas. Full facilities for these purposes shall be afforded by Company. All such tests shall be made in the presence of a representative of Company. Accurate written records of such test shall be maintained by Company.

*City and Gas Commission have right to inspect*

3. *Heating Value--Requirements And Determination*

The monthly average total heating value of the gas, when determined as provided below, shall not be less than 950 British Thermal Units per cubic foot, measured at a temperature of 60° Fahrenheit and a pressure of 30 inches of mercury.

*Heating value standards*

The daily average total heating value shall not differ from the monthly average total heating value to such extent as to interfere with the satisfactory functioning of consumer appliances.

The total heating value of the gas shall be continuously recorded daily unless prevented by circumstances beyond the Company's control.

*Daily recording*

The monthly average total heating value of the gas shall be the average of the daily averages of the total heating value for that month.

*Average monthly value*

The daily average total heating value shall be the average of 24-hourly readings.

*Average daily value*

#### 4. *Purity--Requirements and Determination*

*Sulphureted Hydrogen*--The gas shall contain not more than a trace of sulphureted hydrogen. The gas shall be considered to contain not more than a trace of sulphurated hydrogen if a strip of white filter paper moistened with a solution containing five per cent by weight of lead acetate is not distinctly darker than a second paper freshly moistened in the same solution after the first paper has been exposed to the gas for one and one-half minutes in an apparatus of approved form through which the gas is flowing at the rate of approximately 5 cubic feet per hour, the gas not impinging directly from a jet upon the test paper.

*Sulphureted hydrogen*

*Total sulphur*--The gas shall contain in each 100 cubic feet not more than 30 grains of total sulphur.

*Sulphur*

*Ammonia*--The gas shall contain in each 100 cubic feet not more than 5 grains of ammonia.

*Ammonia*

5. *Pressure Regulations*

Company shall maintain pressures throughout the City within limits compatible with the satisfactory utilization of gas and as more fully defined in the Rules and Regulations\* of the Company's Tariff and as approved from time to time by the Gas Commission.

*Gas pressure requirements*

Company shall take pressure readings continuously in representative locations throughout the City, which readings shall be available to representatives of City and the Gas Commission upon request for a period of one year prior to the date of such request, or in compliance with the rules issued from time to time by the Gas Commission.

*Pressure readings*

Gas Commission may order Company by written notice to adjust pressures to acceptable limits for satisfactory utilization of gas, and due diligence shall be employed by Company to adjust pressures at such points to within such acceptable limits. If compliance with the order of the Gas Commission shall require the installation of new apparatus or mains, Company shall be allowed six (6) months, after the necessary financing has been secured to obtain permits for opening of streets and for the laying of the mains and the installation of the necessary apparatus.

*Adjustments of pressures*

*Delay in compliance*

SECTION IV

*Accounting Methods; Operating Budget and Forecast; Capital Budget and Forecast; Temporary Financing and Financial Statements*

1. *Accounting Methods*

(a) *In General*

The accounts and reporting shall be on the accrual methods in which the accounting for depreciation shall be as described in subsection 1(b) herein.

*Accounting to be on accrual method*

The Gas Works revenues and expenses shall be operated and accounted for an extended period basis from July 1, 1981 to August 31, 1981, and on a fiscal year basis commencing September 1, 1982 and terminating August 31, 1983 and from September 1 to August 31 from year to year thereafter. Accounting shall be employed to show separately the operating accounts and the capital accounts. Operating and capital accounts shall follow generally the classifications specified by the Public Utility Commission of Pennsylvania, expanded or altered, as required by the Director of Finance to portray the special charges and special accounting prescribed in this agreement.

*Fiscal year  
September 1 to  
August 31*

*Accounting to follow  
PUC*

*(b) Depreciation*

There shall be established and maintained a reserve for depreciation reasonably estimated to be adequate to care for the retirement (due to exhaustion, wear and tear and obsolescence) of property at original cost. The amount necessary to be credited to the reserve each year for such purposes shall be charged to operations.

*Depreciation on  
original cost*

*(c) Employee Retirement Costs*

There shall be provided for and charged to operations annually retirement cost for retired employees and employees still in service on the following basis:

For retired employees, the amount necessary to meet current payments to them under their retirement schedules.

*Retired employees*

An additional amount, as determined by the Director of Finance, shall be placed in a retirement fund to be held and invested by the Sinking Fund Commission. Such additional amount shall be determined by the Director of Finance after taking into consideration the current payrolls, the retirement schedules then in effect applicable to various classes of employees and the extent to which it appears desirable and reasonable to build up such fund in current and future years.

*Pension fund*

To this end, the Director of Finance at appropriate times shall obtain competent actuarial advice and shall have available at all times a report made within the immediately preceding five (5) years by a competent actuary based upon an actuarial investigation of the pertinent factors with the costs to be paid by the Gas Works. Payment out of such funds shall be subject to the approval of the Director of Finance as to amounts and when and how payable.

Any proposed change in the retirement plan, schedule or system recommended by Company first shall be transmitted to the Director of Finance for his approval and then transmitted to City Council for its approval, for which purpose there shall be made available to the City Council an appropriate actuarial report prepared under the direction of the Director of Finance.

*Retirement plan changes*

No employee of Company shall be entitled to be paid a retirement or separation allowance unless and until he can establish his direct and immediate and exclusive connection as such employee with the Gas Works whether under the present operator or former operator.

*Employee eligibility for pensions*

All such retirement and separation allowances which are paid during the continuance of this agreement and the terms of which, as so approved, require their continued payment after its termination, shall be thereafter paid by City, or City shall cause the same to be paid by any person succeeding to the operation of the Gas Works.

*Obligation of City to continue to pay pensions*

## 2. Budgets

### (a) Operating Budget and Forecast

There shall be prepared annually an operating budget for the ensuing year and an operating forecast for four (4) years comprising the ensuing year and the three (3) years next following.

*Operating budget*

Such budget and forecast shall be prepared by Company with the aid of the Director of Finance; shall be consistent with the accounting methods prescribed in Section IV (1); and in general shall be in form and extent satisfactory to the Director of Finance and Gas Commission. The operating budget and forecast shall be subject to the approval of the Gas Commission.

*Approval of  
operating budget by  
Gas Commission*

*(b) Capital Budget and Forecast*

There shall be prepared annually a proposed capital budget for the ensuing year and a forecast for six (6) years comprising the ensuing year and the five (5) years next following. Such budget and forecast shall be prepared by Company; shall be consistent with the accounting methods prescribed in Section IV (1); and in general be in form and extent satisfactory to the Director of Finance and the Gas Commission.

*Capital budget:*

The proposed budget and forecast first shall be transmitted to the Director of Finance and the Gas Commission for their recommendations thereon. The Director of Finance and Gas Commission shall transmit such budget and forecast together with their recommendations thereon to City Council for its approval. The submission of the proposed budget and forecast to the Director of Finance and Gas Commission by Company shall be made in sufficient time for their review and for the Director of Finance and Gas Commission in turn to submit the said budget and forecast together with their recommendations thereon to City Council no later than the middle of the fourth month preceding the beginning of the Gas Works' fiscal year, so that City Council may act on it at least thirty (30) days prior to the next ensuing fiscal year.

*Approval of capital  
budget by City  
Council*

The capital budget and forecast shall include a showing of the nature of the proposed capital additions and replacements, the amounts needed therefor and how the funds required are to be supplied as between--

*Nature of capital  
items*

(i) funds generated within the business through charges to customers or otherwise; and

(ii) funds to be obtained through capital loans.

*Capital loans*

At any time during the fiscal year, or before the budget accounts are closed for the year, the division between (i) and (ii) above may, if conditions so warrant, be changed or the total thereof increased upon recommendation of the Director of Finance and the Gas Commission and upon approval by City Council.

*Approval of changes*

In the event that capital loans are required in any year under (ii) above, plans therefor shall be submitted to the Director of Finance for approval of the amount of loan and the method of effecting it, and then transmitted to City Council for its approval.

*Approval of capital loans*

### *(c) Expenditures Pursuant to Budgets*

All expenditure and commitments therefor shall be made pursuant to such approved budgets and subject to rules and regulations, if any, promulgated by the Gas Commission in connection therewith.

*Gas Commission rules regulate expenditures*

### *3. Temporary Financing*

Short-term loans not exceeding twenty million dollars in amount or twelve months in duration may be negotiated in anticipation of revenues, except that short-term loans exceeding twenty million dollars but not exceeding forty-five million dollars in amount may be negotiated in anticipation of revenues for Fiscal Year 1982 of the Gas Works and may be outstanding during the period July 1, 1981 through June 30, 1982. If such loans are required, plans therefor shall be submitted to the Gas Commission and the Director of Finance for approval of amount of loan. The amount of any such loan shall also be subject to the approval by resolution or by ordinance of City Council.

*Approval of short term loans*

The Gas Works may also receive temporary advances from the City in anticipation of revenues which are anticipated to be received by the Gas Works provided that such advances do not exceed twenty million dollars in amount or twenty-four months in duration; provided further, however, that during the period June 30, 1981 through June 30, 1983, such advances may exceed twenty million dollars but shall not exceed forty-five million dollars in amount. The amount of each such advance shall be subject to the prior approval of the Director of Finance and the Gas Commission and to the approval by resolution or by ordinance of City Council.

In addition to the foregoing authorized borrowings, loans not exceeding one hundred million dollars in aggregate principal amount at any time outstanding may be incurred for financing accounts receivable and the purchase of inventory for the Gas Works, as authorized by applicable law. If such loans are required, plans therefor shall be submitted to the Gas Commission and the Director of Finance for approval of the aggregate principal amount of such loans which may be outstanding at any single time. Such aggregate principal amount shall also be subject to approval by resolution or by ordinance of City Council.

#### 4. *Financial Statements*

Company shall within a reasonable time after the close of the Gas Works' fiscal year furnish to the Mayor, the Gas Commission, the City Controller, the City Solicitor, the Director of Finance and City Council a financial statement of such year in form and extent satisfactory to the Director of Finance and Gas Commission. Such financial statement shall be audited by a certified public accountant in accordance with generally accepted accounting principles.

*Furnishing of financial statements by Company*

*CPA to audit financial statement*

All books, records and accounts of the Gas Works shall be kept separate and apart from all other books, records and accounts of Company. The City Controller and the Director of Finance and Gas Commission may examine or cause to be examined the books, records and accounts of Gas Works for the purpose of auditing and reporting upon

*Books, records and accounts of PGW to be kept separate*

such financial statement to the Mayor, the Gas Commission, the City Council, the City Solicitor and the Director of Finance; and the Director of Finance, Gas Commission and the City Controller shall at all times hereafter, for such purpose or for the purpose of ascertaining any facts in relation to the operation of the Gas Works and the performance of the obligations of Company, have full and free access at all reasonable hours to the related books, records and accounts of Gas Works.

*City controller,  
Director of Finance  
and Gas Commission  
may audit books*

Company shall furnish the Mayor, the Gas Commission, the City Controller, the City Solicitor, the Director of Finance and City Council with copies of regular interim financial or operating reports, prepared for periods within the fiscal year, which any such parties may reasonably request.

*Furnishings of  
regular interim  
reports by company*

## SECTION V

### *Insurance; Eminent Domain*

#### *1. Insurance*

Company shall insure against loss the buildings, machinery, and equipment and other property of the Gas Works and other risks to the Gas Works, all of which shall be insured to the extent that such property and risks of gas companies are usually insured except that the Gas Commission may provide otherwise in its discretion.

*Adequate insurance  
to be provided*

#### *2. Eminent Domain*

In the event that Company shall be lawfully required to remove or reconstruct any portion of the Gas Works, or to acquire additional land or property therefor, in consequence of the taking of any of the land or property of the said Gas Works by the United States, the State of Pennsylvania or the City of Philadelphia, in the exercise of the right of eminent domain, or for any other reason whatsoever, the cost and expense thereof shall be accorded appropriate accounting treatment.

*Exercise of right of  
eminent domain*

## SECTION VI

### *Gas Commission*

1. The Gas Commission as it is presently constituted shall be retained.

*Retained*

2. The Gas Commission shall consist of the City Controller, two members appointed by City Council and two members appointed by the Mayor.

*Membership*

3. The members of the Gas Commission appointed by the Mayor shall be designated for four year terms to hold office until their successors are appointed and qualified. The City Controller shall hold office during his incumbency and until his successor has been elected and qualified. The members of the Gas Commission appointed by City Council shall be designated for four year terms, to hold office until their successors are appointed and qualified. The terms of all members of the Gas Commission shall terminate if this agreement is terminated by either party prior to the expiration of their respective terms.

*Terms of office*

4. Members of the Gas Commission shall receive compensation as fixed by City Council from time to time.

*Compensation*

5. The Gas Commission shall have the power and authority to obtain such professional services and to employ experts, consultants and such other personnel as in its judgment shall be deemed necessary, their compensation and expenses to be considered an operating expense of the Gas Works.

*Power to hire experts*

6. A statement of the expenses of the Gas Commission shall be filed annually by the Gas Commission with the City Controller and copies thereof transmitted to the Mayor, the City Solicitor, the Director of Finance and City Council.

*Statement of expenses to be filed annually*

7. Company shall keep the Gas Commission fully informed of its plans for operation, improvement, extension and betterment of the Gas Works.

*Company to keep Gas Commission fully informed*

8. The Gas Commission shall hold regular meetings and shall conduct all Commission business thereat. The City Solicitor and the Director of Finance or their designates or deputies shall and the Chief Executive Officer of the Gas Works or his designates may attend all such meetings of the Gas Commission.

*Regular meetings*

9. The Gas Commission shall have the responsibility for the overseeing of the operation of the Gas Works by the Company. All power not specifically granted to the Company shall reside in the Gas Commission.

*Responsibility, powers, and duties.*

## SECTION VII

### *Gas Rates*

1. The Gas Commission shall fix and regulate rates and charges for supplying gas to customers, other than the City and the Board of Education, without further authorization of City Council, which (together with revenues for gas supplied to the City and to the Board of Education and other revenues of the Gas Works qualifying as "project revenues" as such term is defined in Section 2 of The First Class City Revenue Bond Act) will, in each fiscal year produce revenues, at a minimum:

*Gas commission shall fix rates*

*"Project Revenues"*

*First Class City Revenue Bond Act*

(a) Sufficient to pay all of the operation and maintenance costs and expenses of conducting the Gas Works enterprise and to pay the interest and amortization becoming due in such fiscal year on debt incurred for the Gas Works, including, but not limited to:

*Rates to include  
Operating and  
maintenance costs  
Interest and  
amortization on  
debt*

(i) Charges for depreciation as prescribed in Section IV 1. (b);

*Depreciation*

(ii) Charges for employees' retirement costs as prescribed in Section IV 1. (c);

*Retirement costs*

(iii) A management fee to Company equal to the actual cost to Company of managing the Gas Works but not to exceed the sum of:

*Management Fee*

(A) The amount needed to pay or provide for the payment of base salaries for the Chief Executive Officer, chief Operating Officer and Chief financial Officer and to pay the other expenses of the Company, not to exceed the following amounts for the specified fiscal years:

*Salaries*

FY1996	\$700,000
FY1997	\$725,000
FY1998	\$750,000
FY1999	\$775,000
FY2000	\$800,000

FY2001 and thereafter The prior fiscal year's maximum amount adjusted to reflect the percentage change in the Consumer Price Index for All Urban Consumer (CPI-U) All Items Index, Philadelphia, Pennsylvania, United States Department of Labor, Bureau of Labor Statistics, as most recently published and available to the Director of Finance on March 1 of each such fiscal year; and

(B) Incentive compensation, if any, awarded to Company management at the discretion of Company's Board of Directors, in total amount not to exceed \$150,000 per annum and in an amount per employee not to exceed \$75,000 per annum. Incentive compensation shall be payable only pursuant to performance standards established, and performance measured against such standards, by the Board of Directors of the Company. The performance standards shall include standards which the Board of Directors determines, from time to time, to be important for the improved operations of the Gas Works such as the achievement of the Gas Works' financial plan, customer service, billing and collection efficiencies and development of new revenues (other than from general rate increases).

*Incentive  
compensation*

The Gas Works shall reimburse Company against vouchers on the first day of each calendar month for monies expended for the operation of the Gas Works in the previous calendar month.

(iv) Expenses of the Gas Commission; and

*Gas Commission  
expenses*

(v) All sinking fund charges payable in respect of principal and interest on all obligations of the City issued for or with respect to the Gas Works and, with respect to Gas Works Revenue Bonds issued pursuant to The First Class City Revenue Bond Act, such additional amount as may be required to comply with any rate covenant and sinking fund reserve requirement approved by ordinance of City Council in connection with the authorization or issuance of Gas Works Revenue Bonds.

*Sinking fund  
charges in  
connection with Gas  
Works Revenue  
Bonds*

(b) Sufficient also (together with the excess on a cumulative basis of internally generated funds available for the purposes set forth below in this subparagraph (b) of prior years beginning after June 30, 1974, to the extent that such excess shall not have been applied to such purposes and shall be available for the payment of general expenses of such fiscal year and, subject and subordinate to the payment or provision for payment of all operation and maintenance costs and all sinking fund and sinking fund reserve

*General expenses*  
-

requirements as set forth in subparagraph (a) of this subsection 1., together with the excess funds provided by revenues of such fiscal year not required for such purposes):

(i) To make base payments to the City in the aggregate annual *principal* amount of \$18,000,000 payable in the amount of \$4,500,000 on each February 1, March 1, April 1 and May 1, provided that the Gas Works may defer this payment to any time between said due date and June 30 of each year in which event it shall be assessed interest on the principal amount of prevailing rates, to be determined by the Director of Finance and the Gas Works, from the said due date of the date of payment or such different amounts at such different times, not greater in annual aggregate principal amount, as City Council shall prescribe;

*Payments to City*

(ii) To provide appropriations, to the extent not otherwise provided, for prepayment of debt and for capital additions which have been determined by the Gas Commission to be reasonable and which have been approved by City Council; and

*Debt reduction and capital additions*

(iii) To provide cash, or equivalent, for working capital in such reasonable amounts as may be determined by Company to be necessary and as shall be approved by the Gas Commission.

*Working capital*

(c) Anything to the contrary herein contained notwithstanding, Company may continue to budget and report revenues and expenses in the form and by the methods heretofore used and the Gas Works shall continue to pay out of its revenues all of the expenses set forth in this subsection 1, and all other expenses necessary and proper to the operation of the Gas Works, excepting only the Company's own personnel and administrative costs which are payable out of the management fee.

*Non-cash expenses included in estimates of revenue requirements*

For the purposes of clauses (a) and (b) of this subsection 1., to the extent that operating expenses do not represent an actual outflow of funds (e.g., depreciation) such amount may be included in ascertaining whether revenues are sufficient to meet other costs, expenses and requirements of said clauses (a) and (b). Company shall at all times to the extent of its authority observe and comply with all terms, covenants and provisions of all ordinances enacted by City Council relating to the Gas Works including without limitation, ordinances enacted pursuant to The First Class City Revenue Bond Act authorizing Gas Works Revenue Bonds.

*Company to comply with terms of City Council ordinances*

2. Upon any change in the rates for gas, the Gas Commission, at least thirty (30) days prior to the effective date thereof, shall notify City Council and give public notice by advertisement once in one or more daily newspapers having a circulation of at least 10,000 published in the City of Philadelphia, of the rates for gas to be charged.

*Public notice of rate change*

3. Company shall furnish to the City and the Board of Education, delivered in their various public buildings along the lines of its mains, such amounts of gas as may be required by the City or the said Board. Rates for gas for such public purposes shall be established from time to time by the Gas Commission upon the recommendations of Company and subject to approval by City Council.

*Gas Rates for municipal purposes*

4. In connection with any gas rate study or matter related thereto, Company shall furnish the Gas Commission such data as may reasonably be required therefor.

*Company to furnish rate data to Gas Commission*

5. In the determination of rate schedules for gas, the Gas Commission shall establish and apply non-discriminatory rates based on suitable and reasonable classification of the services provided, taking into consideration the preparation of such schedules, the nature and purpose of the use, the quantity\* used, the time of year when used, the available supply of gas and other competing fuels, the maximum demand, and such other factors, including state, and federal laws, regulations or guide lines,

*Non-discriminatory rates*

*Classification of service*

\* "quantity" in the Ordinance

as may be appropriate to the economics of the purchase, manufacture, distribution and sale of gas and consistent with the intent and purpose of this ordinance and/or Agreement. Such rates may provide for sufficient revenue to stabilize them over a reasonable number of years.

6. If conditions warrant, the Company shall pay to the City, but only from any excess described in clause (b) of subsection 1. of this Section VII, such amounts, in addition to those set forth in clause (b) (i) of subsection 1. of this Section VII, as may be determined and agreed upon by the Gas Commission and City Council.

*Additional city payments*

7. The Gas Commission is authorized to establish rates for gas users authorizing a reduction in gas rates, in the amount of 20% of charges for non-heating and heating purposes to his residence, for any individual 65 years of age or older, residing in the City of Philadelphia, who directly makes payment to the operator of the Gas Works for gas services at his residence. In order to qualify for any rate reduction a person must first apply to the Philadelphia Gas Works for a rate reduction at least thirty days before the next scheduled meter reading. The reduction shall then take effect at the start of the succeeding billing period.

*Senior Citizen rate*

8. Notwithstanding any provisions to the contrary contained herein, no payments will be made to the City under subparagraph (b) of Paragraph 1 or under Paragraph 6 of this Section VII until the \$20,000,000 Gas Works Temporary Loan Note, Series of 1980, of the City has been paid in full with interest.

*Temporary Loan Notes*

## SECTION VIII

### *Purchases and Sales of Non-Gas Items*

1. Except in the purchase of unique articles or articles which for any other reason cannot be obtained in the open market, competitive bids shall be secured, pursuant to

procurement standards adopted and promulgated by the Gas Commission, before any purchase, by contract or otherwise, is made or before any contract is awarded for material and supplies, construction, alterations, repairs or maintenance or for rendering any services to Company other than professional services or for the purchase of any other item, thing or service, and the purchase shall be made from or the contract shall be awarded to the lowest responsible bidder.

*Purchases to be made by competitive bids*

*Gas Commission to set purchasing standards*

2. All residuals and by-products from operations, unserviceable property or equipment shall be sold to the highest responsible bidder pursuant to standards adopted and promulgated by the Gas Commission in a manner similar to that required for awards of contracts for the purchase of goods and services.

*Residuals to be sold to highest responsible bidder*

3. All acquisitions, sales and leases of real estate proposed by or for the Gas Works by Company shall be submitted to the Gas Commission for its action and approval, and shall be submitted to City Council for its approval by ordinance.

*Real estate transactions to be approved by Gas Commission and City Council*

## SECTION IX

### *Legal Services*

The Law Department of the City of Philadelphia shall be the legal advisor for the Gas Commission and the Gas Works. It shall supervise, direct, and control all of the law work of the Gas Commission and the Gas Works including, but not limited to, litigation or other legal representation, investigation, and drafting of documents including contracts, bonds and all other legal instruments for the Gas Commission and the Gas Works.

*Law Department: legal advisor for Gas Commission and PGW*

*Duties of Law Department:*

The City Solicitor shall determine whether legal services for the Gas Works shall be performed by other counsel, and in such event he shall designate such counsel and the compensation therefor in his sole discretion.

*City Solicitor shall designate other counsel*

All legal services rendered, by the Law Department and by other special legal counsel, to the Gas Commission and to the Gas Works shall be billed to the Gas Works and shall be payable out of gas revenues.

*PGW shall pay for legal services*

## SECTION X

### *Company's Obligations During Disputes*

No disputes between City and Company concerning any of the terms or provisions of this Agreement shall release Company from its obligations to manufacture, provide and supply gas in accordance with the terms and provisions hereof during the existence of this Agreement.

*Disputes between City and Company*

## SECTION XI

### *Definitions*

The following terms are defined for purposes of this Agreement as set forth below:

1. *Director of Finance* - The Director of Finance of the City of Philadelphia.
2. *City Solicitor* - The City Solicitor of the City of Philadelphia.
3. *City Controller* - The City Controller of the City of Philadelphia.
4. *Mayor* - The Mayor of the City of Philadelphia.

5. *City Council* - The City Council of the City of Philadelphia.

6. *Streets Commissioner* - The Commissioner of the Department of Streets of the City of Philadelphia.

7. *Gas Works* - All of the property, both personal and real, including mains and pipes, which together constitute the plant and equipment of the Philadelphia Gas Works.

8. *Non-Gas Items* - Non-gas items include but are not limited to every tangible or intangible article, item or thing except natural gas and substitute natural gas.

## SECTION XII

### *Term*

The term of this Agreement shall be for a period of two (2) years commencing January 1, 1973. Said term shall be subject to cancellation by City at any time, or upon the expiration of said two (2) years, upon ninety (90) days notice. No such cancellation shall be effective unless and until such cancellation shall have been approved by resolution or ordinance of City Council. In the absence of such notice, the term shall be extended for further two (2) year periods upon the terms and conditions herein.

*Two year term*

*Termination by City*

## SECTION XIII

### *Other Agreements*

1. Unless approved by the Gas Commission, no contract or agreement with a third party, including without limitation any union contract covering Gas Works personnel, entered into by Company or at its direction on behalf of the Gas Works during the term of this Agreement shall provide by its terms that it shall terminate or expire in the event that this Agreement between City and Company shall terminate or expire.

*Contracts shall not terminate with this*

2. The City agrees and hereby does, indemnify and hold harmless the Directors, the officers and the employees of Company, individually and collectively, while acting within the scope of their employment, against and from any and all personal liability, actions, causes of action, and any and all claims made against them whatever in their capacities as Directors, Officers or employees of Company with regard to this Agreement.

#### SECTION XIV

##### *Counterparts*

This Agreement may be executed in counterparts, all of which taken together shall constitute one document.

#### SECTION XV

##### *Effectiveness*

This Agreement shall not be effective or binding upon the parties unless it has been approved by an effective ordinance of City Council and has been ratified by the Board of Directors of Company.

IN WITNESS WHEREOF, the parties hereto have duly executed this Agreement, the corporate seal of the City of Philadelphia has been duly affixed by the Mayor of said City, and the corporate seal of the Philadelphia Facilities Management Corporation has been duly affixed by an authorized officer thereof, the day and year first above written.

CITY OF PHILADELPHIA

Attest:(s) Pace Reich  
Deputy to the City Solicitor

By: (s) Frank L. Rizzo  
Mayor

By: (s) William A. Costello  
Commissioner of Public Property

PHILADELPHIA FACILITIES MANAGEMENT CORPORATION

Attest: (s) Stephen S. Gardner  
Secretary

By: (s) F. Eugene Dixon, Jr.  
President

Approved for the City of Philadelphia  
as to correctness and form:

(s) Martin Weinberg  
City Solicitor

## CERTIFICATE OF SERVICE

I hereby certify that I have on June 16, 2004, served a true copy of the foregoing document of Philadelphia Gas Works' upon the participants listed below in accordance with the requirements of § 1.54 (relating to service by a participant).

### VIA FIRST CLASS MAIL AND E-MAIL

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SECRETARY'S BUREAU

2004 JUN 22 PM 4: 21

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Daniel Clearfield, Esq.

Dated: June 22, 2004

COMMONWEALTH OF PENNSYLVANIA



DOCUMENT

ORIGINAL

OFFICE OF SMALL BUSINESS ADVOCATE  
Suite 1102, Commerce Building  
300 North Second Street  
Harrisburg, Pennsylvania 17101

William R. Lloyd, Jr.  
Small Business Advocate

July 13, 2004

(717) 783-2525  
(717) 783-2831 (FAX)

DOCKETED  
JUL 14 2004

HAND DELIVERED

James J. McNulty, Secretary  
Pa. Public Utility Commission  
Commonwealth Keystone Building  
P. O. Box 3265  
Harrisburg, PA 17105

Re: Pennsylvania Public Utility Commission v.  
Philadelphia Gas Works (GCR Proceeding)  
Docket No. R-00049157

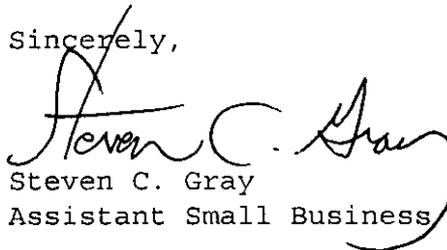
Petition to Establish a Cash Receipts Reconciliation Clause  
Docket No. P-00042090

Dear Secretary McNulty:

Please be advised that the Office of Small Business Advocate will not be filing exceptions in the above captioned proceeding. As evidenced by the enclosed certificate of service, a copy has been served on all active parties in this case.

If you have any questions, please contact me.

Sincerely,

  
Steven C. Gray  
Assistant Small Business Advocate

Enclosures

cc: Hon. Charles E. Rainey, Jr.  
Administrative Law Judge

Cheryl Walker Davis, Director  
Office of Special Assistants

Parties of Record

Robert D. Knecht

RECEIVED  
2004 JUL 13 AM 11:36  
PA PUC  
SECRETARY'S BUREAU

BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

PENNSYLVANIA PUBLIC UTILITY :  
COMMISSION :  
 :  
v. : DOCKET NO. R-00049157  
 :  
PHILADELPHIA GAS WORKS :  
 :  
 :  
PETITION TO ESTABLISH A CASH : DOCKET NO. P-00042090  
RECEIPTS RECONCILIATION CLAUSE :

RECEIVED  
2004 JUL 13 AM 11:36  
PA PUC  
SECRETARY'S BUREAU

CERTIFICATE OF SERVICE

I certify that I am serving a copy of the foregoing document on behalf of the Office of Small Business Advocate by FAX and first class mail upon the persons addressed below:

Hon. Charles E. Rainey, Jr.  
Administrative Law Judge  
Pa. Public Utility Commission  
1302 Philadelphia State Office Bldg.  
Broad and Spring Garden Streets  
Philadelphia, PA 19130  
(215) 560-2105  
(215) 560-3133 (fax)  
[crainey@state.pa.us](mailto:crainey@state.pa.us)

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Alan C. Kohler, Esquire  
Wolf, Block, Schorr & Solis-Cohen  
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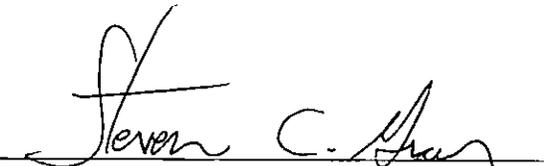
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Committee  
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Cheryl Walker Davis, Director  
Office of Special Assistants  
Pa. Public Utility Commission  
P.O. Box 3265  
Harrisburg, PA 17105-3265

  
Steven C. Gray  
Assistant Small Business Advocate

Date: July 13, 2004

DATE: July 14, 2004

SUBJECT: R-00049157, P-00042090

TO: Office of Administrative Law Judge  
Susan Hoffner

FROM: James J. McNulty  
Secretary  
nvl

Pennsylvania Public Utility Commission

R-00049157

V.

Philadelphia Gas Works

Petition of Philadelphia Gas Works to Establish  
a Cash Receipts Reconciliation Clause

P-00042090

Copies of the Recommended Decision have been served upon all parties.

No exceptions have been received by the Commission. This matter is referred to your office for whatever action you deem necessary.

cc: Office of Special Assistants

P.S. Please note that exceptions or reply exceptions may come in timely with certificate of mailings. A second memo will not be released for these exceptions.

**DOCUMENT  
FOLDER**

**DOCKETED**  
JUL 14 2004

ORIGINAL

WolfBlock

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SECRETARY'S BUREAU  
PA PUC

212 Locust Street, Suite 300, Harrisburg, Pennsylvania 17101  
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Mark S. Stewart  
Direct Dial: (717) 237-7191  
Direct Fax: (717) 237-7161  
E-mail: mstewart@wolfblock.com

July 30, 2004

VIA HAND DELIVERY

James McNulty, Secretary  
PA Public Utility Commission  
Commonwealth Keystone Bldg., 2nd Floor,  
400 North Street P.O. Box 3265  
Harrisburg, PA 17105-3265

DOCUMENT  
FOLDER

Re: Philadelphia Gas Works Cash Receipts Reconciliation  
Clause, Docket No. R-00049157  
Petition of Philadelphia Gas Works to Establish a Cash  
Receipts Reconciliation Clause, Docket No. ~~R-00049157~~ R-00047090

Dear Secretary McNulty:

On behalf of Philadelphia Gas Works, enclosed please find an original and three copies of its Attachment 1 to Appendix A of the Petition for Reconsideration that was filed on July 22, 2004. Attachment 1 was inadvertently omitted at the time of the filing. A copy has been served on the parties listed on the attached Certificate of Service.

Very truly yours,



Mark S. Stewart

For WOLF, BLOCK, SCHORR and SOLIS-COHEN LLP

MS/lww

Enclosure

- cc: Terrance J. Fitzpatrick, Chairman w/enc.
- Robert K. Bloom, Vice-Chairman w/enc.
- Glen R. Thomas, Commissioner w/enc.
- Kim Pizzingrilli, Commissioner w/enc.
- Wendell F. Holland, Commissioner
- Hon. Charles H. Rainey, Jr. w/enc.
- Office of Special Assistants w/enc.
- Attached Certificate of Service w/enc.

DSH:41991.1/PHI211-220875

74

Actual/Estimate Weather 4,335 degree days  
 City Loan \$45.0 MM Fully Outstanding @ 8/31/04  
 TXCP \$80.0 MM with \$79.8 MM Outstanding @ 8/31/04  
 Collection Factor 92.0%  
 \$18.0 M City Payment Forgiven  
 Natural Gas Pymt. Deferral \$60.0 M @ 9.2 Bcf May-Sept  
 Projected FY 2004 Cash Impact \$34.5 Million  
 7/20/04

BUDGET OF CASH RECEIPTS AND DISBURSEMENTS  
 FISCAL YEAR ENDING AUGUST 31, 2004  
 (Millions of Dollars)

	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ESTIMATE	FORECAST	FORECAST	
	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	June	July	Aug	TOTAL
OPENING BALANCE - CASH INCLUDES \$74.0 TXCP RECEIPTS	\$0.1	(\$2.5)	(\$1.3)	(\$0.6)	\$3.5	\$0.3	\$1.8	\$0.0	\$3.1	\$2.1	\$12.2	\$22.1	\$0.1
Gas	34.0	42.3	39.3	58.9	77.6	94.4	116.7	85.1	66.2	54.2	44.0	43.0	755.7
Other	2.2	1.7	0.1	0.4	2.8	0.4	0.3	0.3	0.5	3.7	0.5	0.4	13.3
Drawn from Capital Funds - Principal (\$94.2MM)	18.6	9.6	12.4	4.3	33.5	(0.1)	(10.5)	8.2	(13.2)	(12.8)	30.0	(20.0)	60.0
Drawn from Capital Funds - Interest	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	1.0	1.0
Drawn from Lease Funds - Principal (\$X.XMM)	0.0	1.2	0.0	0.0	0.0	0.0	0.0	2.0	0.0	0.0	0.0	0.0	3.2
Drawn from Lease Funds - Interest	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Pension Draw	0.8	2.2	1.5	1.6	1.6	1.6	1.6	1.6	1.6	1.6	0.0	0.1	15.8
City Loan	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>TOTAL RECEIPTS</b>	<b>55.6</b>	<b>57.0</b>	<b>53.3</b>	<b>65.2</b>	<b>115.5</b>	<b>96.3</b>	<b>108.1</b>	<b>97.2</b>	<b>55.1</b>	<b>46.7</b>	<b>74.5</b>	<b>24.5</b>	<b>849.0</b>
<b>TOTAL</b>	<b>55.7</b>	<b>54.5</b>	<b>52.0</b>	<b>64.6</b>	<b>119.0</b>	<b>96.6</b>	<b>109.9</b>	<b>97.2</b>	<b>58.2</b>	<b>48.8</b>	<b>86.7</b>	<b>46.6</b>	<b>849.1</b>
DISBURSEMENTS													
Labor	10.4	12.2	10.8	11.4	12.2	11.9	10.8	12.5	10.9	11.2	11.2	11.2	136.7
Natural Gas	28.7	32.5	35.7	41.4	55.9	63.2	51.2	39.4	28.9	25.2	22.7	30.0	454.8
Debt Service	0.0	2.0	0.0	0.0	23.3	8.4	0.0	2.0	4.6	0.0	39.0	15.0	94.3
TXCP: Interest	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.0	0.4	0.2	0.2	1.7
Repayment of City Loan	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Sales Tax Liability	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
City Fee	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Disbursements	16.5	11.1	10.2	10.2	10.4	12.2	13.8	10.0	11.7	11.3	11.0	11.0	139.4
<b>TOTAL DISBURSEMENTS</b>	<b>55.7</b>	<b>57.9</b>	<b>56.8</b>	<b>63.1</b>	<b>101.9</b>	<b>95.8</b>	<b>75.9</b>	<b>84.1</b>	<b>56.1</b>	<b>48.1</b>	<b>84.1</b>	<b>67.4</b>	<b>826.9</b>
MONTHLY CASH FLOW	(0.1)	(0.9)	(3.5)	2.1	13.6	0.5	32.2	33.1	(1.0)	(1.4)	(8.6)	(42.9)	22.1
CUMULATIVE CASH FLOW	(0.1)	(1.0)	(4.5)	(2.4)	11.2	11.7	43.9	77.0	76.0	74.6	65.0	22.1	
OPENING TXCP	74.0	74.0	71.5	73.6	77.8	79.8	63.0	64.0	30.0	0.0	11.5	31.0	74.0
TXCP ISSUED DURING MONTH	0.0	2.1	4.2	2.0	0.0	1.0	0.0	0.0	0.0	11.5	19.5	48.8	89.1
TXCP ISSUED PAID DOWN DURING MONTH	2.5	0.0	0.0	0.0	16.8	0.0	34.0	30.0	0.0	0.0	0.0	0.0	83.3
ENDING TXCP	71.5	73.6	77.8	79.8	63.0	64.0	30.0	0.0	0.0	11.5	31.0	79.8	79.8
OPENING BALANCE - CASH	0.1	(2.5)	(1.3)	(0.6)	3.5	0.3	1.8	0.0	3.1	2.1	12.2	22.1	0.1
MONTHLY CASH FLOW	(0.1)	(0.9)	(3.5)	2.1	13.6	0.5	32.2	33.1	(1.0)	(1.4)	(8.6)	(42.9)	22.1
NET TXCP ACTIVITY MONTHLY	(2.5)	2.1	4.2	2.0	(16.8)	1.0	(34.0)	(30.0)	0.0	11.5	19.5	48.8	5.8
ENDING BALANCE - CASH	(2.5)	(1.3)	(0.6)	3.5	0.3	1.8	0.0	3.1	2.1	12.2	22.1	28.0	28.0
CITY LOAN AVAILABLE - END OF MONTH	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
CITY LOAN UTILIZED - END OF MONTH	45.0	45.0	45.0	45.0	45.0	45.0	45.0	45.0	45.0	45.0	45.0	45.0	45.0
CASH POSITION NET OF TXCP AND CITY LOAN	(119.0)	(119.9)	(123.4)	(121.3)	(107.7)	(107.2)	(75.0)	(41.9)	(42.9)	(44.3)	(53.9)	(96.8)	

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Actual/Estimate Weather 4,335 degree days  
 City Loan \$45.0 MM Fully Outstanding @ 8/31/04  
 TXCP \$80.0 MM with \$79.8 MM Outstanding @ 8/31/04  
 Collection Factor 92.0%  
 \$18.0 M City Payment Forgiven  
 No Natural Gas Pymt. Deferral Transaction  
 Negative Impact on FY 2004 Cash Balances \$34.5 M  
 7/20/04

BUDGET OF CASH RECEIPTS AND DISBURSEMENTS  
 FISCAL YEAR ENDING AUGUST 31, 2004  
 (Millions of Dollars)

	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ESTIMATE	FORECAST	FORECAST		
	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	June	July	Aug	TOTAL	
OPENING BALANCE - CASH INCLUDES \$74.0 TXCP RECEIPTS	\$0.1	(\$2.5)	(\$1.3)	(\$0.6)	\$3.5	\$0.3	\$1.8	\$0.0	\$3.1	\$2.1	\$1.2	(\$0.9)	\$0.1	
Gas	34.0	42.3	39.3	58.9	77.6	94.4	116.7	85.1	66.2	54.2	44.0	43.0	755.7	
Other	2.2	1.7	0.1	0.4	2.8	0.4	0.3	0.3	0.5	3.7	0.5	0.4	13.3	
Drawn from Capital Funds - Principal (\$94.2MM)	18.6	9.6	12.4	4.3	33.5	(0.1)	(10.5)	8.2	(13.2)	(12.8)	30.0	(20.0)	60.0	
Drawn from Capital Funds - Interest	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	1.0	1.0	
Drawn from Lease Funds - Principal (\$X.XMM)	0.0	1.2	0.0	0.0	0.0	0.0	0.0	2.0	0.0	0.0	0.0	0.0	3.2	
Drawn from Lease Funds - Interest	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Pension Draw	0.8	2.2	1.5	1.6	1.6	1.6	1.6	1.6	1.6	1.6	0.0	0.1	15.8	
City Loan	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
<b>TOTAL RECEIPTS</b>	<b>55.6</b>	<b>57.0</b>	<b>53.3</b>	<b>65.2</b>	<b>115.5</b>	<b>96.3</b>	<b>108.1</b>	<b>97.2</b>	<b>55.1</b>	<b>46.7</b>	<b>74.5</b>	<b>24.5</b>	<b>849.0</b>	
<b>TOTAL</b>	<b>55.7</b>	<b>54.5</b>	<b>52.0</b>	<b>64.6</b>	<b>119.0</b>	<b>96.6</b>	<b>109.9</b>	<b>97.2</b>	<b>58.2</b>	<b>48.8</b>	<b>75.7</b>	<b>23.6</b>	<b>849.1</b>	
<b>DISBURSEMENTS</b>														
Labor	10.4	12.2	10.8	11.4	12.2	11.9	10.8	12.5	10.9	11.2	11.2	11.2	136.7	
Natural Gas	28.7	32.5	35.7	41.4	55.9	63.2	51.2	39.4	28.9	36.2	34.7	41.5	489.3	
Debt Service	0.0	2.0	0.0	0.0	23.3	8.4	0.0	2.0	4.6	0.0	39.0	15.0	94.3	
TXCP: Interest	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.0	0.4	0.2	0.2	1.7	
Repayment of City Loan	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Sales Tax Liability	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
City Fee	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Other Disbursements	16.5	11.1	10.2	10.2	10.4	12.2	13.8	10.0	11.7	11.3	11.0	11.0	139.4	
<b>TOTAL DISBURSEMENTS</b>	<b>55.7</b>	<b>57.9</b>	<b>56.8</b>	<b>63.1</b>	<b>101.9</b>	<b>95.8</b>	<b>75.9</b>	<b>64.1</b>	<b>56.1</b>	<b>59.1</b>	<b>96.1</b>	<b>78.9</b>	<b>861.4</b>	
<b>MONTHLY CASH FLOW</b>	<b>(0.1)</b>	<b>(0.9)</b>	<b>(3.5)</b>	<b>2.1</b>	<b>13.6</b>	<b>0.5</b>	<b>32.2</b>	<b>33.1</b>	<b>(1.0)</b>	<b>(12.4)</b>	<b>(21.6)</b>	<b>(54.4)</b>	<b>(12.4)</b>	
<b>CUMULATIVE CASH FLOW</b>	<b>(0.1)</b>	<b>(1.0)</b>	<b>(4.5)</b>	<b>(2.4)</b>	<b>11.2</b>	<b>11.7</b>	<b>43.9</b>	<b>77.0</b>	<b>76.0</b>	<b>63.6</b>	<b>42.0</b>	<b>(12.4)</b>		
OPENING TXCP	74.0	74.0	71.5	73.6	77.8	79.8	63.0	64.0	30.0	0.0	0.0	11.5	31.0	74.0
TXCP ISSUED DURING MONTH	0.0	2.1	4.2	2.0	0.0	1.0	0.0	0.0	0.0	11.5	19.5	48.8	89.1	
TXCP ISSUED PAID DOWN DURING MONTH	2.5	0.0	0.0	0.0	16.8	0.0	34.0	30.0	0.0	0.0	0.0	0.0	83.3	
ENDING TXCP	71.5	73.6	77.8	79.8	83.0	64.0	30.0	0.0	0.0	11.5	31.0	79.8	79.8	
OPENING BALANCE - CASH	0.1	(2.5)	(1.3)	(0.6)	3.5	0.3	1.8	0.0	3.1	2.1	1.2	(0.9)	0.1	
MONTHLY CASH FLOW	(0.1)	(0.9)	(3.5)	2.1	13.6	0.5	32.2	33.1	(1.0)	(12.4)	(21.6)	(54.4)	(12.4)	
NET TXCP ACTIVITY MONTHLY	(2.5)	2.1	4.2	2.0	(16.8)	1.0	(34.0)	(30.0)	0.0	11.5	19.5	48.8	5.8	
ENDING BALANCE - CASH	(2.5)	(1.3)	(0.8)	3.5	0.3	1.8	0.0	3.1	2.1	1.2	(0.9)	(6.5)	(6.5)	
CITY LOAN AVAILABLE - END OF MONTH	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
CITY LOAN UTILIZED - END OF MONTH	45.0	45.0	45.0	45.0	45.0	45.0	45.0	45.0	45.0	45.0	45.0	45.0	45.0	
CASH POSITION NET OF TXCP AND CITY LOAN	(119.0)	(119.9)	(123.4)	(121.3)	(107.7)	(107.2)	(75.0)	(41.9)	(42.9)	(55.3)	(76.9)	(131.3)		

## CERTIFICATE OF SERVICE

I hereby certify that I have on July 30, 2004, served a true copy of the foregoing document of Philadelphia Gas Works' upon the participants listed below in accordance with the requirements of § 1.54 (relating to service by a participant).

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Mark S. Stewart, Esq.

Dated: July 30, 2004



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August 2, 2004

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James J. McNulty, Secretary  
PA Public Utility Commission  
400 North Street  
Keystone Building  
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RE: Pa. Public Utility Commission  
v.  
Philadelphia Gas Works  
Docket No. R-00049157  
Petition of Philadelphia Gas Works  
Regarding Cash Receipts Reconciliation  
Clause  
Docket No. P-00042090

Dear Secretary McNulty:

Enclosed are an original and three (3) copies of the Office of Consumer Advocate's Answer to the Petition for Reconsideration of Philadelphia Gas Works, in the above-referenced proceeding.

Copies have been served upon all parties of record as shown on the enclosed Certificate of Service.

Sincerely,

Stephen J. Keene  
Senior Assistant Consumer Advocate

Enclosures

- cc: All Parties of Record
- Honorable Charles E. Rainey, Jr.
- Terrance J. Fitzpatrick, Chairman
- Robert K. Bloom, Vice-Chairman
- Glen R. Thomas, Commissioner
- Kimberly Pizzingrilli, Commissioner
- Wendell F. Holland, Commissioner
- Office of Special Assistants

DOCUMENT  
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ORIGINAL

BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

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PA PUC  
SECRETARY'S BUREAU

Pennsylvania Public Utility Commission :  
v. : R-00049157  
Philadelphia Gas Works :  
Petition of Philadelphia Gas Works to :  
Establish a Cash Receipts Reconciliation : P-00042090  
Clause :

**DOCKETED**  
AUG 3 2004

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OFFICE OF CONSUMER ADVOCATE'S  
ANSWER TO THE PETITION FOR RECONSIDERATION  
OF PHILADELPHIA GAS WORKS

---

Pursuant to Section 5.572 of the Commission's Rules of Administrative Practice and Procedure, the Office of Consumer Advocate files the following Answer to Philadelphia Gas Works' Petition for Reconsideration in the above-captioned proceeding. The OCA does not object to PGW's alternative request in its Petition to expedite consideration of its Chapter 56 waiver requests by dispensing with the preparation of a Recommended Decision in that proceeding. The OCA strongly opposes, however, PGW's request for reconsideration of the merits of the Commission's July 8, 2004 Order in the Cash Receipts Reconciliation Clause ("CRRC") Petition proceeding. As the Commission found in its July 8 Order, the Company's request for a cash receipts reconciliation clause must be rejected for a host of legal, policy and financial reasons. The OCA submits that nothing in the PGW Petition for Reconsideration justifies reconsideration of the Commission's Order at this time.

**DOCUMENT  
FOLDER**

## I. INTRODUCTION

On July 8, 2004, an Opinion and Order ("*July 8 Order*") was entered in the above-captioned proceeding involving the Philadelphia Gas Works' ("PGW") request for permission to establish a cash receipts reconciliation clause ("CRRC").

In its *July 8 Order*, the Commission rejected PGW's proposed CRRC for several reasons. As a matter of law, the Commission found the CRRC proposal to be single-issue and retroactive ratemaking. *July 8 Order* at 14-18. The Commission also held that the proposed CRRC was not the type of automatic adjustment mechanism that would be permitted by Section 1307 of the Public Utility Code. *July 8 Order* at 11-13. The Commission also found that PGW failed to meet its burden of proof and did not demonstrate that its financial condition warrants actions by the Commission that would depart from adherence to Pennsylvania ratemaking law and principle. *July 8 Order* at 8-11.

The Commission also rejected the CRRC on public policy grounds, finding that the proposed CRRC would reduce the incentive for PGW to improve or maximize its collections and would only exacerbate PGW's collections problems. *July 8 Order* at 24-26. In balancing the equities between PGW's financial conditions and the hardship and fundamental unfairness that the CRRC proposal would impose upon ratepayers, the Commission concluded that PGW did not present sufficient rationale for unique treatment. *July 8 Order* at 27-28.

The Company filed a Petition for Reconsideration on July 22, 2004. The OCA now files this Answer to the Company's Petition for Reconsideration and, for the reasons set forth below, respectfully requests that the Company's Petition be denied.

## II. ANSWER

### A. Legal Standard.

Petitions for rehearing, reconsideration, clarification and amendment to an order must meet certain legal requirements. *Pa.P.U.C. v. T.W. Phillips Gas & Oil Co.*, 75 Pa. P.U.C. 237, 239 (1991). Section 703(f) of the Public Utility Code states:

**(f) Rehearing.** – After an order has been made by the commission, any party to the proceedings may, within 15 days after the service of the order, apply for a rehearing in respect of any matters determined in such proceedings and specified in the application for rehearing, and the commission may grant and hold such rehearing on such matters. No application for a rehearing shall in anywise operate as a supersedeas, or in any manner stay or postpone the enforcement of any existing order, except as the commission may, by order, direct. If the application be granted, the commission may affirm, rescind, or modify its original order.

66 Pa.C.S. § 703(f).

Section 703(g) provides:

**(g) Rescission and amendment of orders.** – The commission may, at any time, after notice and after opportunity to be heard as provided in this chapter, rescind or amend any order made by it. Any order rescinding or amending a prior order shall, when served upon the person, corporation, or municipal corporation affected, and after notice thereof is giving to the other parties to the proceedings, have the same effect as is herein provided for original orders.

66 Pa.C.S. § 703(g).

The standard that the Commission applies in considering a request for rehearing or reconsideration under Section 703 of the Public Utility Code was delineated by the Commission in *Duick v. Pa. Gas & Water Co.*, 56 Pa.P.U.C. 553 (1982). There, the Commission stated:

A Petition for Reconsideration, under the provisions of 66 Pa.C.S. 703(g), may properly raise any matters designed to convince the Commission that it should exercise its discretion under this code section to rescind or amend a prior order in whole or in part.

In this regard, we agree with the court in the Pennsylvania Railroad Company case, wherein it was said that:

Parties ... cannot be permitted by a second motion to review and reconsider, to raise the same questions, which were specifically decided against them.

What we expect to see raised in such petitions are new and novel arguments; not previously heard or considerations which appear to have been overlooked by the Commission.

*Duick*, 56 Pa.P.U.C. at 559.

For the reasons set forth below, the OCA submits that the Company has failed to meet the standard for reconsideration of the Commission's *July 8 Order*.

B. The Company's Request That The Commission Should Reconsider Its Decision On The Proposed CRRC Should Be Rejected Since It Presents No New Or Novel Arguments.

PGW's Petition for Reconsideration fails to meet the standard set forth in *Duick* since it is simply a rehash of the arguments presented in the Company's Main and Reply Briefs. The Commission considered these arguments and rejected PGW's proposed CRRC on a host of legal grounds and policy reasons. The Company's attempt to revisit these issues on reconsideration presents no new or novel arguments and therefore does not meet the standard set forth in *Duick*.

The Company's first basis for seeking reconsideration is that the Commission erred in its conclusion that PGW would have between \$31-36 million of cash on hand at the end of the current fiscal year. The Company once again repeats the same argument that it made in its

Briefs, that once the \$30 million derived from the deferral of gas storage payments is removed from the cash flow projections, the Company will only have only \$1-6 million of cash at year end. This is the exact same argument presented by the Company in its Main and Reply Briefs. PGW M.B. at 22; PGW R.B. at 3-4. PGW witness Bogdonavage confirmed that the \$30 million deferral of gas storage payments has been finalized. Tr. 325. The cash impact of that transaction must be reflected in the cash flow analysis. This results in PGW finishing the current fiscal year on August 31, 2004 with between \$31-36 million in cash. Therefore, PGW's implication that it somehow might end up the year with only \$1-6 million in cash is incorrect.

In essence, what PGW is trying to do is present a normalized year-end cash position by backing out the cash derived from the gas storage payment deferral transaction from its cash flow analysis. If that is done, then the Company presents a year-end cash position of only \$1-6 million. The OCA submits that it is unreasonable not to consider the \$30 million derived from the gas storage payment deferral since the transaction has been finalized and will most certainly increase PGW's cash position at year end by \$30 million. Furthermore, PGW's attempt to normalize the cash flow analysis only makes an adjustment for this year's \$30 million deferral transaction. PGW ignores the cash effect of a similar transaction, a forward sale of gas inventory that it entered into last year that deferred \$15 million of gas costs from last fiscal year (FY2003) into this fiscal year (FY2004). *See* PGW St. CRRC-1 (Bogdonavage) at 8. Thus, the cash flow analysis for the current fiscal year included \$15 million of gas payments deferred from FY2003. The OCA submits that in order to truly normalize PGW's cash flow for the current fiscal year (FY2004), the cash effect created by last year's deferral transaction must also be considered. Therefore, if the \$30 million derived from this year's deferral of gas storage

payments is going to be normalized out of the cash flow analysis, then the payment of the \$15 million of deferrals from last year must also be normalized out of the cash flow analysis.

In support of its Petition for Reconsideration, the Company also relies upon an updated cash flow projection attached to its Petition for Reconsideration as Appendix A. Once again, PGW seeks to reverse a Commission decision based upon extra-record evidence that the parties have not had an opportunity to scrutinize or challenge.<sup>1</sup> The OCA submits that such evidence cannot form the basis for a reversal of the Commission's decision. Due process should not fall by the wayside due to PGW's constantly shifting financial forecasts.

This is not the first time that PGW has attempted to use extra-record evidence in support of a Petition for Reconsideration. In a prior base rate proceeding, docketed at No. R-00006042, PGW attempted to attach a verified statement of PGW witness Bogdonovich which provided an update to bad debt expense for FY2001 and provided a projected cash flow estimate resulting from the awarded base rate increase of \$33.5 million. *Pa.P.U.C. v. Philadelphia Gas Works*, Docket No. R-00006042, Order at 24, 26 (Order entered December 6, 2001) (“*December 6, 2001 Order*”). The Commission correctly rejected this attempt by PGW to rely upon extra-record evidence:

We will reject the Verified Statement of Mr. Bogdonavage for several reasons. First, as noted by the OTS, adoption of this document as proposed by PGW provides no opportunity to test the technical veracity of this data. We arrive at a similar conclusion regarding the inclusion of FY2000 data. Second, we find that PGW should not be permitted to selectively update supporting information for certain expense claims without updating all other claims.

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<sup>1</sup> Indeed, the OCA did not receive Attachment 1 to Appendix A until the afternoon of Friday, July 30, 2004. Attachment 1 contains the schedules supporting the revised projections in Appendix A. Since Answers to PGW's Petition for Reconsideration are due Monday, August 2, 2004, the OCA has only had an opportunity to do a cursory review of these supporting schedules.

*December 6, 2001 Order* at 26. Therefore, the OCA submits that the verified statement of PGW witness Bogdonavage attached to PGW's Petition for Reconsideration as Appendix A should be rejected and not relied upon by the Commission.

PGW also claims that recent actions by the financial community further warrant reconsideration of the Commission's decision to reject the proposed CRRC. In support of this, PGW again cites to extra-record evidence in the form of a recent Standard & Poor's ("S&P") Bulletin dated July 9, 2004. Petition for Reconsideration, App. B. The OCA submits that such extra-record evidence should be treated skeptically. The July 9 S&P Report is not evidence of record in this proceeding. It was not presented as evidence at the evidentiary hearings, nor has PGW moved to have it admitted into the record as a late-filed exhibit. PGW has not offered up a witness to sponsor this exhibit, nor have the parties had any opportunity to do discovery regarding this exhibit. PGW simply attached the July 9 S&P Report to its Petition for Reconsideration as an Appendix and commenced to quote freely from it. The OCA submits that such evidence should not be relied upon by the Commission in making its decision.

Furthermore, as the OCA noted in its Reply Brief in the Chapter 56 Waiver proceeding, no one from S&P has ever testified before the Commission in any of PGW's proceedings, despite the fact that PGW has continuously tried to utilize such reports from the rating agencies to extract relief from the Commission. If such evidence can be used to dictate the relief that this Commission grants in regulatory proceedings such as this, then the Commission is being asked to effectively cede its oversight of this Company to an S&P analyst in New York. None of the rating agencies are tasked with the duty to ensure that PGW is providing safe, adequate and reliable service. Under the Public Utility Code, that responsibility rests solely with the Commission. 66 Pa.C.S. § 1501.

The Company also argues that the Commission was mistaken in its finding that PGW's proposed CRRC was violative of the rules against single-issue and retroactive ratemaking, and the Commission's conclusion that such a recovery mechanism was not permitted by Section 1307 of the Public Utility Code. Yet these are the very same arguments that the Commission flatly, and correctly, rejected in its *July 8 Order*. The OCA submits that it is impermissible for PGW to present these same arguments on reconsideration. For reasons set forth by the OCA in its Main and Reply Briefs, the Commission reached the correct conclusion on these issues in its *July 8 Order*. OCA M.B. at 16-22; OCA R.B. at 5-8.

The OCA submits that the Commission's *July 8 Order*, fully addressed the issues raised by the Company in its Petition for Reconsideration. There is nothing new or novel about the arguments raised by PGW in its Petition for Reconsideration. These arguments were fully litigated and rejected by the Commission. Therefore, the *Duick* standard is not met and reconsideration should be rejected.

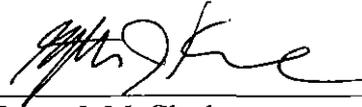
C. PGW's Alternative Request That The PUC Certify The Company's Chapter 56 Waiver Requests For Direct And Expedited Commission Decision.

In the alternative, PGW requests that the Commission expedite its decision on PGW's Chapter 56 waiver requests by dispensing with preparation of a Recommended Decision by the ALJ and certifying the record on the Chapter 56 waiver requests directly to the Commission. The OCA does not oppose PGW's alternative request for relief.

### III. CONCLUSION

For the reasons set forth above, the Office of Consumer Advocate respectfully requests that Philadelphia Gas Works' Petition for Rehearing and Reconsideration be denied.

Respectfully submitted,



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CERTIFICATE OF SERVICE

Re: Pennsylvania Public Utility Commission  
v.  
Philadelphia Gas Works  
Docket No. R-00049157

Petition of Philadelphia Gas Works Regarding  
Cash Receipts Reconciliation Clause  
Docket No. P-00042090

I hereby certify that I have this day served a true copy of the foregoing document, Office of Consumer Advocate's Answer to the Petition for Reconsideration of Philadelphia Gas Works, upon parties of record in this proceeding in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant), in the manner and upon the persons listed below:

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