

June 14, 2004

ORIGINAL

James J. McNulty, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building, 2nd Floor, 7 North
400 North Street
Harrisburg, PA 17120

Filed by Federal Express

Re: Pennsylvania Public Utility Commission v. PGW
Petition of Philadelphia Gas Works to Establish Cash Receipts Reconciliation Clause
Docket Nos. R-00041957, P-00042090

DOCUMENT
FOLDER

R-00041957

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 Main 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

PHILIP A. BERTOCCI

Attorney for Action Alliance et al.

cc: Certificate of Service

Enclosures

RECEIVED

JUN 14 2004

PA PUBLIC UTILITY COMMISSION
SECRETARY'S BUREAU

133

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility
Commission

:
:

R-00049157 ✓
Docket No. R-00041957
Docket No. P-00042090 ✓

v.

:

Philadelphia Gas Works

RECEIVED

JUN 14 2004

PA PUBLIC UTILITY COMMISSION
SECRETARY'S BUREAU

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

ORIGINAL

DOCKETED

JUN 21 2004

PHILIP A. BERTOCCI, ESQUIRE
I.D. 32329
LAURA MOSKOWITZ, ESQUIRE
I.D. 90817
COMMUNITY LEGAL SERVICES, INC.
1424 Chestnut Street, 4th Floor
Philadelphia, PA 19102
(215) 981-3702

Counsel for Action Alliance of Senior Citizens,
ACORN and Tenants' Action Group

Date: June 14, 2004

DOCUMENT
FOLDER

TABLE OF CONTENTS

	Page
Table of Contents	i
Table of Authorities	iii
I. Introduction and Summary of Arguments	1
II. PGW's Projections of its FY2004 Year End Cash Circumstances and Early FY2005 Financial Prospects Demonstrate No Impending Crisis and Fail to Justify Such An Extraordinary Measure As the CRRC	4
A. PGW's Anticipated Cash Flow Crisis.	4
B. An Extraordinary Measure Like the CRRC Is Not Necessary Because PGW Failed to Prove that a FY2004 Year End Cash Crisis Is Likely	8
1. <u>Introduction</u>	8
2. <u>City Commitment to Grant Back the \$18 Million City Payment for Five Years</u>	10
3. <u>Extension of Repayment Date for \$45 Million Interest Free City Advance</u>	12
4. <u>Year Extension of the Collective Bargaining Agreement From May 2004 to May 2005</u>	12
5. <u>Natural Gas Payment Deferral Arrangement Reducing FY2004 Disbursements by \$30 Million</u>	13
6. <u>Improved Collection Ratio Projections from 89% to 90.5-93% Range</u>	15

7.	<u>There Is No Reasonable Prospect of a FY2004 Year End Cash Crisis That Might Justify Any Form of Extraordinary Relief</u>	17
8.	<u>Weaknesses in PGW's General Financial Condition Alone Are Not Sufficient Reason to Adopt An Extraordinary Measure Like the CRRC</u>	20
C.	Conclusion	23
III.	The Proposed CRRC Violates Numerous Important Ratemaking Standards	24
A.	Just and Reasonable Standard	24
B.	Public Utility Code Section 1307	26
C.	Prohibition on Single-Issue Ratemaking	29
D.	Prohibition on Retroactive Ratemaking	31
IV.	Conclusion	34
	Proposed Findings of Fact	36
	Proposed Conclusions of Law	38

TABLE OF AUTHORITIES

<u>CASES</u>	<u>Page</u>
<i>Action Alliance v. Philadelphia Gas Commission</i> , 406 A.2d 1155 (Pa. Cmwlth. 1979)	24
<i>Cheltenham & Abington Sewerage Co. v. Pennsylvania Pub. Util. Comm'n</i> , 344 Pa. 366, 373, 25 A.2d 334, 338 (1942)	31
<i>Columbia Gas of Pa. v. Pennsylvania Pub. Util. Comm'n</i> , 149 Pa. Cmwlth. 247, 252, 613 A.2d 74, 76 (1992)	31
<i>Federal Power Commission v. Hope Natural Gas Co.</i> , 320 U.S. 591, 602, 64 S.Ct. 281, 288 (1944); 66 Pa.C.S. § 1301	24
<i>Masthope Rapids Property Owners Council v. Pennsylvania Pub. Util. Comm'n</i> , 581 A.2d 994, 991-1000 (Pa. Cmwlth, 1990)	28
<i>Pennsylvania Industrial Energy Coalition v. Pennsylvania Pub. Util. Comm'n</i> , 653 A.2d 1336, 1350 (Pa.Cmwlth.) 1995, <u>aff'd</u> , 543 Pa. 307, 670 A.2d 1152 (1996)	28
<i>Philadelphia Elec. Co. v. Pennsylvania Pub. Util. Comm'n</i> , 93 Pa. Cmwlth. 410, 422, 502, A.2d 722, 728 (1985)	33
<i>Pike County Light & Power Co. v. Pennsylvania Pub. Util. Comm'n</i> , 87 Pa. Cmwlth. 451, 456, 487 A.2d 118, 121 (1985)	31
<i>Popowsky v. Pennsylvania Pub. Util. Comm'n</i> , 695 A.2d 448, 451 (Pa. Cmwlth. 1997)	31
<i>Popowsky v. Pennsylvania Pub. Util. Comm'n</i> , 64 Pa. Cmwlth. 600, 643 A.2d 1146, 1149 (1994)	33
<i>Public Advocate v. Philadelphia Gas Commission</i> , 544 Pa. 129, 674 A.2d 1056 (1996)	24

ADMINISTRATIVE CASES

Pennsylvania Pub. Util. Comm'n, et al. v. Philadelphia Gas Works,
94 PA PUC 479, 483, 484, 2000 WL 3313808 (Pa. P.U.C.) 1

Pennsylvania Pub. Util. Comm'n, et al. v. Philadelphia Gas Works,
94 PA PUC 479, 2000 WL 33143808 (Pa. P.U.C.) 24

Pennsylvania Pub. Util. Comm'n, et al. v. Philadelphia Gas Works,
PUC Docket No. R-00021612 (Opinion and Order, March 31, 2003) 27

Pennsylvania Pub. Util. Comm'n v. PGW,
R-00006042, Opinion and Order (October 12, 2001) 15

Petition of Philadelphia Gas Works for Extraordinary Rate Relief
Pursuant to 66 Pa.Code § 1308(e), R-00017034F0002
(Opinion and Order, April 12, 2002) 2

STATUTES

66 Pa.C.S. § 1301 24

66 Pa.C.S. § 1307 2, 3

66 Pa.C.S. § 1307(a) 26, 27, 28, 29

66 Pa.C.S. § 1307(f) 27

66 Pa.C.S. § 1307 (h) 27

66 Pa.C.S. § 1308(e) 2, 10

66 Pa.C.S. § 2212(c) 24

I. Introduction and Summary of Argument.¹

On March 1, 2004, for the third time in less than four years, the Philadelphia Gas Works has requested the Pennsylvania Public Utility Commission (PUC) to grant it what amounts to extraordinary rate relief. In its Petition of Philadelphia Gas Works to Establish a Cash Receipts Reconciliation Clause (hereinafter "CRRC Petition"), PGW has once more submitted a request for a substantial rate increase, requested adjudication within an abbreviated time frame and upon the basis of a truncated record, and alleged that such treatment was necessary in order to prevent an imminent financial crisis which threatened PGW's financial stability.

In the two previous instances, the Commission granted rate relief. In response to PGW's August 2000 Petition for the Establishment of Interim Rates, the Commission granted just that amount of rate relief necessary to provide PGW with the opportunity to "to maintain a sufficient level of financial health during the winter months" and to avoid a "technical default" on bond covenants.² In response to PGW's February 2002 Petition of Philadelphia Gas Works for Extraordinary Rate Relief, the Commission granted a substantial base rate increase on the grounds that PGW had satisfied the Public Utility Code Section 1308 standard that such relief must be "immediately necessary" to protect

¹ Action Alliance et al. incorporate by reference the Statement of the Case set forth in the Office of Consumer Advocate's Main Brief.

² Pennsylvania Pub. Util. Comm'n. et al. v. Philadelphia Gas Works, 94 PA PUC 479, 483, 484, 2000 WL 3313808 (Pa. P.U.C.).

the utility's "financial stability" – in a situation where PGW's liquidity problems threatened to result not only in an imminent bond ratings downgrade below investment grade, but also significant disruptions to normal customer services.³ All in all, the results of these base rate increases and increases stemming from rising gas costs have caused total annual costs for a household using 100 Mcf per year to rise from \$867 in the fall of 2000 to \$1484 in the Fall of 2003, an increase of over 70%. PGW St. CRRC-2, Exhibit DM-3.

In this case once more, PGW's CRRC Petition is based on the premise that desperate circumstances justify extreme and unprecedented remedies. However, as became clear in PGW's Rebuttal Testimony and in the evidentiary hearings, the Company's financial circumstances as they have developed are not in the "crisis" that PGW anticipated and described in the CRRC Petition. The Company's actual financial circumstances would not justify extraordinary relief under Section 1308(e). Nor do they justify the ad hoc fashioning of an unprecedented automatic mechanism which does violence to the just and reasonable standard, Public Utility Code Section 1307 and traditional ratemaking prohibitions. To make matters still worse, PGW urges such departures from established legal standards on behalf of a proposal which unfairly transfers the risks associated with subpar collections practices from the Company to its paying customers, does not create any further incentive to improve collections, and which

³ Petition of Philadelphia Gas Works for Extraordinary Rate Relief Pursuant to 66 Pa.Code §1308(e), R-00017034F0002 (Opinion and Order, April 12, 2002).

as OSBA witness Knecht demonstrates, will ultimately aggravate rather than improve PGW's collection situation. OSBA St. 1, at 13-23.

In Part II of this Main Brief, Action Alliance et al. demonstrate in detail on the basis of the information submitted by PGW in this proceeding that PGW's FY2004 financial situation can not be fairly characterized in "crisis" terms. While PGW's financial condition may not be robust, there are adequate resources available to the Company in the short term, reasonable prospects for improved collections within the existing framework provided by Chapter 56, and always the prospect of a base rate case in which PGW would have the opportunity to demonstrate that any rate increase it may seek is "just and reasonable."

In Part III of this Main Brief, Action Alliance et al. review the multiple legal deficiencies of PGW's proposed Cash Receipts Reconciliation Clause. This analysis demonstrates that the CRRC violates many traditional ratemaking principles and policies, including the "just and reasonable" standard, Public Utility Code Section 1307, the prohibition on single issue ratemaking for expenses which are within a utility's control, and the prohibition on retroactive ratemaking.

II. PGW's Projections of its FY2004 Year End Cash Circumstances and Early FY2005 Financial Prospects Demonstrate No Impending Crisis and Fail to Justify Such An Extraordinary Measure As the CRRC.

A. PGW's Anticipated Cash Flow Crisis.

In its March 1, 2004 CRRC Petition and initial pre-filed Direct Testimony, PGW depicted itself as a Company on the edge of an abyss. That abyss took the form of an anticipated cash flow crisis which would become apparent on August 31, 2004, the end of PGW's fiscal year. This scenario, however, was based on projections which were subsequently altered in a manner favorable to PGW, and did not take into account later developments which materially improved PGW's cash situation. Nevertheless, PGW has persisted in its claims that a crisis continues to exist and that the CRRC is the solution. In the pre-hearing discovery period and at the evidentiary hearings, PGW had the opportunity to demonstrate by "substantial" evidence each element of its claim for relief, to show that the proposed rate was just and reasonable, and to offer argument that the CRRC was consistent with existing law.⁴ To measure PGW's supposed "proof" against its allegations, it is first necessary to review the anticipated circumstances which PGW claimed as sufficient justification for its proposed CRRC.

In this case, the desperate circumstances that PGW references have been allegedly driven largely by a significant increase in the price of natural gas billed to customers in FY2003 and FY2004, which increase is claimed to have provoked a spike in PGW's

⁴ Action Alliance et al. incorporate by reference the discussion of "Burden of Proof" contained in the Office of Consumer Advocate's Main Brief.

FY2003 and FY2004 uncollectible expense. PGW St. CRRC-1, at 5-6. As the CRRC Petition stated, PGW anticipated as of the date of filing that its “total cash and borrowing capability at the end of the present fiscal year [August 31, 2004] will be a **negative \$5 million.**”⁵ In addition to being unable to pay all obligations as they came due at the end of FY2004, PGW further anticipated that it would be “unable” to conduct the long term bond sale scheduled for this Fall which is necessary to continue its capital improvement program:

If this trend continues, PGW projects that it simply will be unable to pay all of its obligations when they become due in the Fall of 2004. Moreover, PGW has determined that, even if it repairs its cash receipts problem, it needs to sell another long-term bond in the Fall of 2004. Without such a sale, it will not be able to continue its capital improvement program.⁶

In the Direct Testimony accompanying the CRRC Petition, PGW’s chief financial officer states that the CRRC is justified by a “liquidity shortfall that ... [the Company] is currently experiencing and that could reach crisis proportions at the end of the current year.” He further testifies that PGW “is projecting a year end cash balance of negative \$5 million,” with “[a]ll sources of liquidity, including the \$80.0 million commercial paper program and the \$45.0 million City of Philadelphia loan ...fully utilized.” PGW St. CRRC-1, at 8. These year end cash or cash equivalent projections took into account \$14.7 million in cash savings in June, July and August 2004 stemming from two planned

⁵ CRRC Petition, at 2.

⁶ CRRC Petition, at 9.

PGW gas management transactions involving gas storage and gas payment deferrals. PGW St. CRRC-1, Exhibit JRB-5, p. 2. According to this testimony, this cash crisis could “[a]t worst substantially impede the Company’s access to the market place for capital funding.” PGW St. CRRC-1, at 9.

According to the CRRC Petition, in light of these projections, PGW regarded its available options as extremely limited. Although PGW had late last Fall begun a Collections Renewal Initiative with the assistance of Accenture, a “nationally known consulting group,” PGW did not project that this initiative will produce such immediate and dramatic results ... that the need for a clause would be eliminated.”⁷ Even if the Company were able to reduce operating expenses over which it had direct control by 20%, “the cash problem would be far from solved.”⁸

Claiming to have eliminated all alternatives to a problem attributed to the unaffordability of PGW’s bills for large numbers of residential and small business customers, PGW therefore decided that the only acceptable solution to its immediate liquidity problems was to seek additional revenues from its customers: “PGW simply has no choice but to request additional dollars from remaining ratepayers in order to make up this cash receipts shortfall.”⁹

⁷ CRRC Petition, at 10-11.

⁸ CRRC Petition, at 10.

⁹ CRRC Petition, at 10.

Having concluded once more that customers must bear the burden of PGW's collections failures, PGW then turned its attention to identifying the means by which rates would be increased. Because of time constraints, no rate increase alternative would resolve the immediate problem identified to justify a rate increase – the cash shortfall projected for FY2004 year end – because as PGW readily admits, there was no likelihood that even an expedited process would be completed before September 1, 2004.

Nevertheless, PGW's choice was consistent with past preferences. It rejected the base rate case option, which allows full scrutiny of all PGW's projected expenses and revenues and full application of the "just and reasonable" standard to balance the interests of the utility against the interests of customers in reasonable, efficient and affordable service. Rather, it chose to conceive and to propose a Cash Receipts Reconciliation Clause, an unprecedented automatic adjustment mechanism which aims to assure that regardless of collections performance, PGW will recover 100% of its allowed revenues in a manner which is not fully reconcilable on the customer side. This type of mechanism, which PGW euphemistically characterizes as a "laser focused" type of solution, exclusively considers PGW's supposed cash needs.¹⁰ What is clearly "out of focus" are the interests of good paying customers, old and young alike, in just and reasonable rates and sound regulatory practices.

¹⁰ CRRC Petition, at 11.

B. An Extraordinary Measure Like the CRRC Is Not Necessary Because PGW Failed to Prove that a FY2004 Year End Cash Crisis Is Likely.

1. Introduction.

Between March 1, 2004, when the CRRC Petition was filed, and May 12, 2004, the date of evidentiary hearings, events occurred which invalidated the projections which PGW had initially utilized in order to support its CRRC Petition:

- in connection with the annual February review of PGW's financial condition conducted by the bond rating agencies, PGW's owner, the City of Philadelphia, agreed to grant back PGW's annual \$18 million payment to the City for FY2004 through FY2008.
- as part of this same review process, the City agreed to extend the due date for payment of the interest free \$45 million City Advance from 2006 to 2008.
- PGW's concern about the possibility that its FY2004 collections activities would be jeopardized by a strike associated with the expiration in May 2004 of the collective bargaining agreement between PGW and its union was eliminated, when PGW management and the union agreed to a one year extension of the collective bargaining agreement.
- PGW successfully completed negotiations on a natural gas payment deferral

arrangement, which permitted cash savings of \$10 million monthly for the months of June, July and August, 2004, greater savings than had been anticipated when PGW was considering earlier arrangements which would have permitted savings of approximately \$4.9 million monthly for those same months.

- PGW's projections concerning its FY2004 "collection ratio" improved from 89% per the CRRC Petition, to somewhere between 90.5% and 93%, resulting in a projected increase in cash receipts of between \$12 and \$32 million.

Under these circumstances, PGW's year end cash projections rose from a negative \$5 million to a positive \$31 to \$36 million, a year end amount much greater than PGW has experienced in many years, and an amount sufficient to ensure that PGW will be able to complete a bond offering in the Fall of 2004. The City's commitment to provide \$90 million to PGW over five years, coupled with the extension of the due date for the interest free \$45 million City Advance, has significantly changed PGW's short range financial outlook – and effectively nullifies any need for the type of extraordinary rate relief represented in PGW's CRRC Petition. With regard to anticipated improvements in PGW's collection factor, a conservative estimate would recognize the volatility of the projections, while at the same time accepting CEO Knudsen's estimates that the FY2004 collection factor would be at least 90.5%. In this context, the City's assistance has bought

time for the Collection Renewal Initiative to begin to have a significant effect – and has provided PGW with time, if it so desires, to seek base rate relief through a standard base rate proceeding at some time in the future, rather than an ad hoc form of extraordinary relief, by whatever name.

2. City Commitment to Grant Back the \$18 Million City Payment for Five Years.

PGW's owner, the City of Philadelphia, has long resisted the Commission's suggestions that it would be appropriate for the City, as part of the effort to bring PGW back to fiscal health, to waive or grant back the \$18 million City Payment, which, under the Management Agreement, PGW is obligated to make to the City each year, regardless of the financial performance of the utility.¹¹ Under pressure from the bond rating agencies this Spring and from City Council, the City has now committed to grant back the \$18 million payment for FY2004 and for the years FY2005 through FY2008.

¹¹ See, e.g., the Commission's statement in the 2002 Opinion and Order granting PGW extraordinary rate relief: "An additional way for PGW to improve its liquidity and financial picture would be for the City to restructure the terms of the \$45 million City loan while granting back all or some of the \$18 million annual City payment as project revenues for at least the next three years. The record indicates that this could provide PGW with additional capital of up to 45 million at the end of three years.... While we have no authority to condition approval of extraordinary rate relief on these measures, we strongly urge the City and PGW to seriously consider these opportunities." Petition of Philadelphia Gas Works for Extraordinary Rate Relief Pursuant to 66 Pa.C.S. §1308(e), PUC Docket No. R-00017034F0002, Opinion and Order, April 12, 2002, at 28.

In his Rebuttal Testimony, PGW's chief financial officer testifies that the City has committed to grant back the \$18 million City Payment for FY2004, and this commitment is reflected on Exhibits JRB-10. PGW St. CRRC-1R, at 3. CEO Knudsen confirms the City's "professed willingness" to grant back the \$18 million City Payment at the end of FY2004. PGW St. CRRC-5. There is no credible suggestion in PGW's testimony that there is any uncertainty concerning whether the FY2004 \$18 million City Payment will be granted back to PGW. If PGW had any doubts, it would have explicitly expressed them, since the grant back undermines the case which it seeks to make for the CRRC.

Moreover, further evidence that such a grant back is certain is contained in the statements of bond rating agencies Standard & Poor's and Fitch. Standard & Poor's states explicitly that its decision to maintain PGW bonds at investment grade levels (albeit at lowered levels) "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."¹² In addition, Standard & Poor's makes clear that a further downgrade will take place if the City does not provide "certain support," an unmistakable reference to the grant back of the \$18 million City payment. Fitch, in turn, states that the City appears "committed to PGW's success, as evidenced by a planned repayment date extension of its \$45 million loan given in 2000 and a proposal to grant

¹² Standard & Poor's Statement (April 9, 2004), PGW St. No. CRRC 5, Exhibit TEK-1.

back its annual \$18 million payment from PGW in each of the next five years....”¹³

2. Extension of Repayment Date for \$45 Million Interest Free City Advance.

As in the case of the grant back of the \$18 million City Payment, there is no suggestion in PGW’s pre-filed testimony that any uncertainty exists concerning whether the due date for payment for the \$45 million City Advance will be extended from FY2006 to FYY2008. PGW St. CRRC-5 and Exhibit TEK-1, at 2. PGW presented no forecasts in this proceeding for FY2005, so that there is no evidence concerning what impact this deferment would have on PGW’s cash flow in the near term. OSBA St. No. 1, at 13. However such a deferral or extension can only help PGW and its customers. Moreover, further evidence that such a deferral will occur is contained in the statements of bond rating agencies Standard & Poor’s and Fitch, whose current investment grade ratings are premised in part upon this commitment.

3. Year Extension of the Collective Bargaining Agreement from May 2004 to May 2005.

Utility collections work is necessarily labor intensive, if it is to be conducted in accordance with Chapter 56 and sound business practice. PGW St. CRRC-3. Any work stoppage at a time when PGW must increase its collections factor would jeopardize

¹³ Fitch Statement (April 23, 2004), PGW St. No. CRRC 5, Exhibit TEK-2.

PGW's efforts to improve its collections factor to acceptable levels. At the time when PGW filed its CRRC Petition, PGW management was aware that there was a risk of such a work stoppage in connection with the renegotiation in May 2004 of the collective bargaining agreement with PGW's union, the Service Employees International Union, Local 686 (SEIU).¹⁴ After the filing of the CRRC Petition, however, PGW was successful in negotiating a one year contract extension between the SEIU and PGW. As CEO Knudsen testified in pre-filed May 3, 2004 Rebuttal Testimony, PGW

recently negotiated a one year extension of the existing collective bargaining agreement to enable management and labor to work collectively to find mutually agreeable ways of reducing force, improving productivity and service quality and allowing the entire company to focus on collections. Without such an extension, management would have had to plan for and work through a potential work stoppage, all but negating management's ability to deal effectively with the current financial crisis.

PGW St. CRRC-5, at 11.

4. Natural Gas Payment Deferral Arrangement Reducing FY2004 Disbursements by \$30 Million.

When it filed its CRRC Petition, PGW was in the process of negotiating gas storage and gas payment deferral agreements which were projected to save PGW \$4.9 million per month in cash disbursements for the months of June, July and August, 2004. PGW St. CRRC-1, Exhibit JRB 5, p. 2. The negotiations were sufficiently advanced so that PGW took these projected transactions into account in projecting end of the year cash

¹⁴ May 11, 2004 Evidentiary Hearing Transcript (hereinafter "Transcript"), at 377.

balances which, absent these transactions, would have been even more in the red than the negative \$5 million which was initially projected.

After the filing of the CRRC Petition, and the issuance of the Standard & Poor's and Fitch bond ratings in April 2004, PGW successfully negotiated a different deferred payment arrangement.¹⁵ This arrangement is described in JRB Exhibit 10 as a Natural Gas Payment deferral in the amount of \$53.4 Million involving 9.2 Bcf with a FY2004 impact of \$10 million per month in reduced natural gas disbursements in the months of June, July and August, 2004. There was further testimony at the evidentiary hearings that the cash flow impact of this transaction would extend into the Fall 2004, and that PGW would be obligated to actually pay for this gas beginning in December, at a time when its billings and receipts could presumably better support such payments.¹⁶

As a result of this new transaction, as well as more accurate information concerning March disbursements, PGW was, as of May 3, 2004, projecting gas disbursements in the remainder of FY2004 which were \$23.5 million less than projected at the time of the filing of the CRRC Petition. PGW St. CRRC-1, Exhibit JRB-5, p. 2; PGW St. CRRC-1R, Exhibit JRB-10.

¹⁵ At the evidentiary hearing, PGW testified that this transaction had been "finalized." Transcript, at 338. This statement carries one step further the statement in PGW St. CRRC-1R at 3, submitted May 3, 2004, that PGW "is currently attempting to finalize" this transaction.

¹⁶ Transcript, at 338.

5. Improved Collection Ratio Projections from 89% to 90.5-93% Range.

At the time of the filing of the CRRC Petition, PGW was projecting that its collections ratio (the ratio of total annual billings to total annual collections) for FY2004 would be 89%, “only slightly better than” the 86.5% FY2003 results, and well below the pro forma 92.4% figure which was the basis for its allowed uncollectible expense in the Company’s last litigated base rate case (2001).¹⁷ As PGW testified, in 2003, each percentage point that the collections ratio was below 92.4% meant approximately \$8 million less in cash collections. PGW St. CRRC-1, at 5.

PGW’s CRRC proposal is based on the premise that under current Philadelphia demographic and economic conditions, associated with the increase in gas costs over the past two years, the Company has virtually no more control over its collection ratio than over its gas costs. As the CRRC Petition states:

The proposed clause is a just and reasonable companion to the Company’s longstanding Gas Cost Rate, which provides for a customer pass through of gas costs due to the volatile nature of these costs and the fact that commodity price changes are outside the control of the Company. PGW’s recent dramatic increase in the level of non-payment is directly related to these same upward swings in natural gas price, and, similarly, PGW has little ability to control or reverse these effects.¹⁸

¹⁷ Pennsylvania Pub. Util. Comm’n v. PGW, R-00006042, Opinion and Order (October 12, 2001).

¹⁸ CRRC Petition, at 3.

Or again, as PGW testified, “[l]ike its GCR clause for the recovery of natural gas costs, PGW’s CRRC would recognize that the current downturn in PGW’s levels of uncollected cash receipts is largely outside its control.” PGW St. CRRC-1, at 10.

PGW’s premise that the Company has no more ability to control uncollectible expenses associated with increased gas costs than it does to control the gas costs does not correspond to reality, but rather appears driven by the wish to obtain Commission authorization to treat uncollectible expenses as if they were as uncontrollable by natural gas companies as gas costs. PGW itself implicitly recognizes in this filing that unlike gas costs, the Company can substantially affect its collections ratio by improving its collections practices – practices which the Company has only seriously begun to address operationally in the past several months. PGW St. CRRC-3; PGW St. CRRC-1, at 13; CRRC Petition, at 11, ¶18.

There is a world of difference between a gas cost expense, which is dictated by a market over which PGW has no control, and a collectibles- related expense, which reflects a myriad of factors within substantial control of the utility, such as the allocation of utility resources, technical competence in billing accurately and efficiently, customer service operations, formulation and adoption of appropriate collection strategies, etc. Consistent with this common sense reality, the Company continually asserts that it is making every effort to improve its collections. Despite the good will of individual PGW executives and managers, all non-PGW witnesses recognized the very real danger that

allowing a CRRC would have the effect of diminishing PGW's and the City's collective and institutional incentive to improve its collections, because the automatic mechanism shifts the financial risks of failure from the Company and its owner to PGW customers. OTS St. 1, at 4, 14; OCA St. 1, at 16; OSBA St. 1, at 23-24.

As everyone knows, a utility's actions do indeed have a significant effect on the collections ratio. PGW had to concede in the course of this proceeding itself the inconvenient fact that while its rates have not moderated, its efforts to improve collections of record high receivables appeared to be producing results – so much so that by the time of the evidentiary hearings, the Company was projecting that its collections ratio for FY2004 would be between 90.4% and 93%. PGW St. CRRC-1R, Exhibit JRB-10.¹⁹ The 90.4% projection was based on the Company's historical performance in the period April 2003 through March 2004, while the 93% estimate was based on 7 months actual FY2004 performance, and 5 months projected. PGW St. CRRC-1R, at 2.

6. There Is No Reasonable Prospect of a FY2004 Year End Cash Crisis That Might Justify Any Form of Extraordinary Relief.

The cumulative effect of these subsequent events is that the prospect of FY2004 year end cash crisis that PGW was anticipating when it filed the CRRC Petition no longer

¹⁹ In fact, in mid-April, PGW presented materials to the Philadelphia Gas Commission asserting that "FY04 Receipts as a % of Billings are currently projected at 94%." The graph which accompanied this Power Point presentation, showed actual (not budgeted) FY2004 results through mid-April, and projected, not budgeted, results for the remainder of the fiscal year. OCA Cross Examination Exhibit No. 1, at 2.

exists. As shown on the May 3, 2004 PGW Exhibit JRB-10, PGW's year end cash projections have risen from a negative \$5 million (as shown on the March 1, 2004 PGW Exhibit JRB-5, p. 2) to \$31 to \$36 million. PGW St. CRRC-1R, at 5 and Exhibit JRB-10.

In its Rebuttal Testimony and at the evidentiary hearings, the Company continued to resist explicitly recognizing this fact. In Rebuttal Testimony, PGW states that year end "cash and liquidity available will be just \$13-18 million" only later to admit that year end cash is \$31-36 million "if the \$18 City payment is granted back and considered as available cash" (emphasis added). At the time of submission of Rebuttal Testimony, it was absolutely clear that the \$18 million would be granted back, as discussed earlier. The grant back of the \$18 million was at that time no longer contingent. And in cross-examination, PGW conceded, without hesitation or qualification, that a grant back of the \$18 million City payment would be considered as a cash resource.²⁰

Furthermore, at the hearings, still resisting the obvious consequences of its own projections of \$31-\$36 million year end cash, the Company submitted PGW Rejoinder Exhibit 1 (JRB), a schedule analyzing its FY2004 cash flow, as if the \$53.4 million payment deferral transaction had never occurred!²¹ This Exhibit demonstrates, however, that even without this payment deferral transaction, PGW, with the help of the City grant

²⁰ Transcript, at 331.

²¹ PGW asserts that the gas payment deferral is a "one-time arrangement" (PGW St. CRRC 1-R, at 3) – but in fact, PGW has done such transactions in the past and can be expected to do them in the future under appropriate circumstances. OCA St. 1, at 45-47.

back of \$18 million, would have year end cash or cash equivalents of \$6 million.

Despite this change, PGW continues to assert that its financial circumstances are still so dire as to justify the extraordinary relief to be provided by the CRRC. Forced to abandon its prediction that it would end the year with a negative cash balance, the Company now claims that it needs at least \$60 million in year end liquidity, up from the claim contained in its initial filing that it needed \$35-40 million in year end liquidity.²² In fact, as PGW conceded under cross-examination, the Commission has never explicitly acknowledged that PGW needed even \$35-40 million in year end liquidity.²³ There is virtually no evidence in the record to support such a claim. According to OSBA witness Knecht, PGW informed him that it had not yet even developed a cash flow forecast for FY2005. OSBA St. 1, at 13. Moreover, such amounts are vastly greater than the year end liquidity which the Company has experienced, without crisis, in recent years, even after receiving various forms of extraordinary relief. For instance, PGW had year end cash or equivalents of \$5.9 million in FY2003, \$12.5 million in FY2002, \$3.5 million in FY2001 and \$8.4 million in FY2000.²⁴

In sum, PGW initially attempted to justify the CRRC as a measure necessary to remedy a year end FY2004 cash flow crisis and a consequent closing of the capital

²² Compare PGW St. CRRC-1, at 7, with jPGW St. CRRC-1R, at 4.

²³ Transcript, at 332.

²⁴ Action Alliance Cross-Examination Exhibit 1; Transcript, at 334-336.

markets to PGW. However, that potential cash flow crisis has been averted, with commitments by the City which will strengthen PGW's cash flow for FY2004 and several years into the future. There is no imminent or immediate danger to PGW's financial stability to justify either extraordinary rate relief or such an unprecedented measure as the CRRC.

7. Weaknesses in PGW's General Financial Condition Alone Are Not Sufficient Reason to Adopt An Extraordinary Measure Like the CRRC.

In its Rebuttal Testimony and at the evidentiary hearings, PGW attempted to justify the CRRC as necessary to help improve PGW's general financial condition. The CRRC was described as a "back stop," a "fail safe" mechanism, and a type of insurance policy. In advancing these arguments, PGW was replacing the invalidated primary argument for a CRRC with an argument which had previously been only ancillary. These arguments, which address the general financial condition of PGW, rather than any imminent crisis, by their very nature, should not be addressed in a truncated procedure with a focus which is both limited on a specific point in time, year end 2004, and on only one aspect of PGW's financial condition, its collection ratio. Rather, as all the non-PGW expert witnesses testified, arguments which go to the necessity for a longer term work out of PGW's situation, as suggested by CEO Knudsen, are best raised in the context of a base rate case. As OCA witness LeLash testified, "[t]o the extent that the Company

perceives a need to address its cash working capital situation or uncollectible expense, it can do so in a future base rate proceeding where all of the Company's expenses can be examined." OCA St. 1R, at 1. In a similar vein, OSBA witness Knecht stated that the "CRRC proposal is a ploy to avoid a base rates case." OSBA St.1, at 11, 13.

PGW's shift of grounds in supposed justification of the CRRC was evident in the Company's Rebuttal Testimony and live testimony at the evidentiary hearing. In his Rebuttal Testimony, PGW's chief financial officer testified, "The principal value of the CRRC is as a back stop or 'fail safe.'" PGW St. CRRC-1R, at 5. This "backstop" would mitigate collections risks posed by PGW's clearly subpar collections practices and the demographic and economic circumstances of the Company's residential customer base. As CEO Knudsen testified, "[i]mplementing a mechanism that backstops [PGW's]... efforts to deal with the decrease in cash collections due to the dramatically higher natural gas costs is an essential element of this workout plan." PGW St. CRRC-5, at 12.²⁵

In this fall-back position, PGW stressed that the insurance provided by the CRRC would help particularly with the bond rating agencies. As CEO Knudsen stated, "an approved CRRC is a major step in providing the bond investor with some assurance of PGW's viability." PGW St. CRRC-5, at 10. The chief financial officer testified that the CRRC is "crucial for PGW to maintain its current [investment grade] bond rating." PGW

²⁵ See also, PGW CRRC-5, at 2 (The CRRC would "at least provide some protection to our cash situation if current efforts to improve collections are not successful").

St. CRRC-1R at 4.²⁶ These considerations focus not on any imminent cash crisis, but on longer term issues concerning the appropriate level of PGW cash working capital, and cannot serve as a primary justification for an extraordinary measure like a CRRC.

Moreover, these statements by PGW senior management attempting to link the CRRC closely to the maintenance of PGW's bond ratings in the short term should be regarded with scepticism. Their interpretations go well beyond the actual words and reasonable inferences therefrom contained in the Standard & Poor and Fitch pronouncements. In these pronouncements, both Standard & Poor's and Fitch give specific approving discussion to the City's commitment to grant back the \$18 million City payment, which appears to have been a pre-condition for avoiding a downgrade to junk bond status. However, in comparison, the CRRC receives significantly less attention. Standard & Poor's only mentions that PGW is "seeking cash receipts-related rate relief" from the PUC, without opining on the appropriateness of a business strategy which seeks to improve cash flow by raising rates that were already admittedly too high for PGW's residential customers. Fitch devotes a few sentences to the CRRC proposal and states that adoption of the surcharge, among other measures, would "improve PGW's

²⁶ PGW's chief financial officer provided testimony that he believed that the rating agencies are looking for PGW to "maintain liquidity that represents about 30 days average revenue to be able to maintain an investment grade rating. For PGW, this translates to about \$60 million in end of year liquidity." PGW St. CRRC-1R at 4. There was no demonstration that the CRRC would produce this level of liquidity under existing base rates under any circumstances, whether the PGW collections rate rises to 93% or, more unlikely, sinks back to the FY2003 level. As OSBA witness Knecht observed, if one assumes that PGW's rebuttal testimony is correct, a base rates proceeding would be a necessity even if the CRRC were approved. OSBA St. 3, at 4.

collections,” while observing that “required PUC approval is not expected until this summer at the earliest.” PGW St. CRRC-5, Exhibits TEK-1, TEK-2. At the evidentiary hearing, PGW witnesses confirmed that the rating agencies did not instruct PGW to attempt to obtain a CRRC.²⁷ The S&P and Fitch pronouncements are not a sufficient basis to conclude that rejection of the CRRC alone would materially effect bond rating decisions down the line by either bond rating agency.

C. Conclusion.

For the foregoing reasons, the Commission should deny PGW’s CRRC Petition. It should also reject the alternative (hereinafter “OTS Alternative”) proposed by the Office of Trial Staff. OTS St.1, at 10-14; OTS St.1SR, at 2-6. As OSBA has indicated, the OTS Alternative, like the CRRC, avoids the type of scrutiny and balancing of interests which can only occur in a base rate case. Moreover, as OSBA witness Knecht points out, the OTS Alternative has several of the same defects as the CRRC – and likely has the same counterproductive tendencies involved in raising rates to paying customers when rates are already beyond the affordability of many customers. OSBA St. 2, at 1-5. At bottom, the OTS Alternative is an extraordinary measure, which is not justified by PGW’s financial circumstances.

²⁷ Transcript, at 342, 385.

III. The Proposed CRRC Violates Numerous Important Ratemaking Standards.

A. Just and Reasonable Standard.

It is well settled that in reviewing any PGW request for a rate increase, the Commission must apply the constitutionally based “just and reasonable” standard, which is contained in Section 1301 of the Public Utility Code.²⁸ This standard has long been applied to PGW, regardless of the identity of the regulatory body.²⁹ Moreover, because the standard is constitutionally based, the Commission may not waive the standard pursuant to Gas Choice Act Section 2212(c). 66 Pa.C.S. §2212(c). This ultimate test requires the ratemaker to balance the interests of the utility against those of its customers to determine whether in impact and effect, the rate is just and reasonable.³⁰

The CRRC proposed by PGW is patently unjust and unreasonable on its face in ways that are clear for all to see and understand. Testimony at the Public Input Hearings overwhelming condemned the concept of a CRRC to be levied under conditions where PGW customers already strain to pay the highest rates in the region. State Representative Dwight Evans and State Senator Allyson Schwartz and many others eloquently testified at

²⁸ Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591, 602, 64 S.Ct. 281, 288 (1944); 66 Pa.C.S. §1301.

²⁹ Public Advocate v. Philadelphia Gas Commission, 544 Pa. 129, 674 A.2d 1056 (1996); Action Alliance v. Philadelphia Gas Commission, 406 A.2d 1155 (Pa. Cmwlth. 1979); Pennsylvania Pub. Util. Comm’n v. Philadelphia Gas Works, 94 PA PUC 479, 2000 WL 33143808 (Pa.P.U.C.).

those hearings concerning the fundamental unfairness of the CRRC Proposal for the following common sense reasons: (1) the CRRC would require customers who have paid their bills in full for service provided in FY2004 to pay additional dollars to compensate for the fact that PGW failed to collect what was owed in the same period by other customers; (2) it would require good paying customers in FY2005 and FY2006 to pay more than what was allowed in base rates to compensate for the fact that PGW failed to collect what was owed by other customers.³¹

To these complaints, the technical testimony produced by the Office of Trial Staff, the Office of Small Business Advocate and the Office of Consumer Advocate added other glaring defects, including but not limited to:

(1) the \$55.7 million which is an integral part of the formula determining how much customers would pay under the CRRC does not accurately reflect whatever amount was allowed for uncollectibles in PGW's last base rate case. OCA St. 1, at 19, 20; OSBA St. 1, at 3; OTS St. 1, at 9.

³¹ Public Input Hearing Testimony, Representative Dwight Evans, May 6, 2004, 1 p.m., pages 1, 5 ("This proposal is the wrong solution, the wrong policy, a wrong precedent in rate making, and it is simply unfair to the decent, hard-working families who do everything they can to keep up with their expenses and pay their bills"); Public Input Hearing Testimony, Senator Allyson Schwartz, May 6, 2004, 1 p.m., page 1 ("Those customers who are respecting the rules, and bearing a great burden by paying for natural gas priced at historically high levels, in this instance, are not met with positive reinforcement. Rather, they are met with a demand they pay for those who, in many instances, do not have the same respect for rules. We should never effectively reward bad or illegal behavior. There is a segment of PGW customers who can pay but won't, work the system so as they do not have to").

(2) the CRRC is unfair to customers, because it transfers the risk of bad debt overruns from the Company to customers, but requires no refund to customers when PGW's actual bad debt expense is less than that allowed in base rates. OCA St. 1, at 15-16; OSBA St. 1, at 25-26; OTS St. 1, at 5-6.

(3) as proposed outside the context of a base rate case, the CRRC does not take into account offsetting cost savings achieved or achievable by PGW, nor consider the level of service provided to customers, and therefore does not permit the ratemaker to conduct an appropriate balancing of interests. OCA St. 1, at 13-15, 17; OSBA St. 1, at 11.

(4) while ostensibly intended to allow PGW to recover for uncollectible expense associated with increased gas costs, the mechanism in fact overreaches, allowing recovery for uncollectible underrecovery associated with base rate increases as well. OSBA St. 1, at 12, OTS St. 1, at 4.

B. Public Utility Code Section 1307.

PGW claims that the Commission has the authority to establish a sliding scale of rates for uncollectible expense allegedly closely linked to a sharp increase in the Purchased Gas Cost Rate pursuant to Section 1307(a). However, this contention is without merit.

Under the Public Utility Code, uncollectible expenses associated with gas costs are

recognized to be expenses largely within the control of the Company. If that were not the case, the General Assembly would have statutorily provided for the inclusion of uncollectible expenses associated with gas costs within the statutory definition of gas costs contained in Public Utility Code Section 1307(h), 66 Pa.C.S. §1307(h). As the Commission acknowledged recently in its Opinion and Order concerning PGW's Restructuring Plan, under Pennsylvania law, uncollectible expenses associated with gas costs may not be treated as gas costs under Section 1307(f) and 1307(h) (statutorily defining gas costs in a way which does not include gas cost associated uncollectible expenses). Consistent with existing law, the Commission flatly rejected PGW's argument that uncollectible expenses associated with natural gas costs could be recovered through the Purchased Gas Cost Rate.³² In not including such uncollectible expenses within the definition of gas costs, the General Assembly implicitly recognized that uncollectible expenses depend not merely on the level of gas costs, but on myriad factors which go to a utility's overall operational effectiveness. Because uncollectible expenses associated with gas costs are not largely beyond the control of a utility, they are not recoverable under a Section 1307(a) "sliding scale of rates."

This narrow statutory definition of gas costs reflects a legislative policy judgment in favor of base rate cases as opposed to automatic adjustment mechanisms. As the Commonwealth Court has stated, Section 1307 should have "limited application and the

³² Pennsylvania Pub. Util. Comm'n v. Philadelphia Gas Works, PUC Docket No. R-00021612 (Opinion and Order, March 31, 2003), at 26-28.

PUC should not use it to disassemble the traditional rate-making process.”³³ The record in this case amply demonstrates that PGW’s collection ratio, which is first reflected in its uncollectibles expense (reserve for uncollectibles) and ultimately in its write-offs, is largely within PGW’s control.

In addition, at the most, Section 1307(a) permits the establishment of a sliding scale of rates to permit rapid recovery of a cost which not only is volatile, and beyond a utility’s control, but which is a “specific identifiable expense item.”³⁴ However, as OCA witness LeLash testifies, in contrast to gas costs for instance, identification of the precise cost recoverable is not possible with regard to uncollectible expenses. OCA St. 1, at 8-9. This is because the \$55.7 million in the formula does not represent the exact costs actually incurred in any particular period, but is based only on estimates which are ultimately unverifiable in any precise sense.

The CRRC formula authorizes PGW to recover through the surcharge the difference between its total billing and its total collections, minus \$55.7 million. While the total billings minus total collections yields an identifiable gross shortfall, the third essential element in the formula, the \$55.7 million, does not stand for costs actually

³³ Pennsylvania Industrial Energy Coalition v. Pennsylvania Pub. Util. Comm’n, 653 A.2d 1336, 1350 (Pa.Cmwlth. 1995), aff’d, 543 Pa. 307, 670 A.2d 1152 (1996).

³⁴ Masthope Rapids Property Owners Council v. Pennsylvania Pub. Util. Comm’n, 581 A.2d 994, 991-1000 (Pa.Cmwlth.1990).

experienced by the utility in the relevant period.³⁵ Rather, it is only an allowed cost, and its use in the formula renders unidentifiable the resulting cost to be recovered. The cost to be recovered determined according to the CRRC formula is thus not an identifiable cost recoverable under Section 1307(a).

For this reason, the Commission has never allowed a utility to establish a “sliding scale of rates” to recover uncollectible expense overruns. Moreover, as OSBA’s witness testified, the CRRC is “not consistent with any other approved utility program in North America that PGW can identify” and is significantly broader in scope than the handful that PGW has identified. OSBA St. 3, at 3; OSBA St. 1, at 12, 31. As OCA witness LeLash testified,

[t]he mechanisms are not comparable concerning the scope of the recovery, their relationship to customer choice programs or percentage of income programs, and their associated true-up requirements....[T]he jurisdictions’ definitions of recoverable fuel costs and regulations involving such cost recovery differ between utilities and states, and it is unclear that they would be applicable in Pennsylvania.

OCA St. 1 at 16, 17.

C. Prohibition on Single-Issue Ratemaking.

The Commonwealth Court has stated that “[s]ingle- issue ratemaking is ... prohibited if it impacts on a matter that is normally considered in a base rate case.”³⁶ As

³⁵ Supplement No. 3 to Gas Service Tariff – Pa. P.U.C. No. 2, Third Revised Page No. 82 (Issued March 1, 2004 to be effective September 1, 2004); for explanation of the derivation of the \$55.7 million figure, see PGW St. CRRC-1, at 11-12.

³⁶ Pennsylvania Industrial Energy Coalition v. Pennsylvania Pub. Util. Comm’n, 653 A.2d 1336, 1350 (Pa.Cmwlth. 1995), aff’d, 543 Pa. 307, 670 A.2d 1152 (1996).

the OCA and OSBA witnesses testified, cash flow matters and uncollectible expenses are matters which are typically considered in base rate case, especially for a municipally owned utility whose base rates are set according to the cash flow method as set forth in the Management Agreement and applicable case law. Both OCA and OSBA experts concluded that the CRRC violates the traditional ratemaking prohibition on single-issue ratemaking. OSBA St. 1, at 23, 31; OCA St. 1, at 15. According to OCA witness LeLash, the “long established precedent for ... the vast majority of ... state utility commissions is to set uncollectible and bad debt allowances within the context of a base rate or budgeting proceedings.” OCA St. 1, at 17, 13-15.³⁷

The prohibition against single-issue ratemaking, which protects both utilities and customers depending on the case, is based on the ratemaker’s duty to consider all revenues and costs in the balancing process which allows formulation of a just and reasonable rate. While it is recognized that matters subject to a sliding scale of rates are not subject to the prohibition on single-issue ratemaking, PGW has yet to demonstrate the reasonableness of establishing a sliding scale of rates for cash receipts/uncollectibles. In this proceeding, PGW has clearly not met the heavy burden of demonstrating that the benefits of the CRRC for the utility and its customers are sufficient to overcome the policy reasons underlying the prohibition of single issue ratemaking.

³⁷ See also OSBA St. 1, at 11.

D. Prohibition on Retroactive Ratemaking.

Under the “Commission-made rate” doctrine, rates are set prospectively, and generally may not be adjusted to correct for any benefit or disadvantage to the utility or the customers prior to the date that the Commission approves a new rate.³⁸ Specifically, the Commonwealth Court has explained that “the Commission clearly may not establish rates which are calculated to retroactively recover surpluses or refund deficits created by inaccuracies in its prior rate authorizations.”³⁹ Moreover, “the general principle is that customers who use power should pay for its production rather than requiring future customers to pay for past use.”⁴⁰ This general principle applies equally to natural gas distribution rates.

One provision of the proposed CRRC would allow PGW to “collect an under collection realized in FY 2004 (12 months ended [sic] August 31, 2004) on a 3-year amortized basis to recognize the time period over which this problem has arisen....” CRRC Petition, at 13. PGW projects that this recovery for past uncollectibles arising FY2004 bad debt overruns will cost customers \$11.4 million annually over three years.

³⁸ See Cheltenham & Abington Sewerage Co. v. Pennsylvania Pub. Util. Comm’n, 344 Pa. 366, 373, 25 A.2d 334, 338 (1942); see also Columbia Gas of Pa. v. Pennsylvania Pub. Util. Comm’n, 149 Pa. Cmwlth. 247, 252, 613 A.2d 74, 76 (1992) (“Ratemaking is *prospective* in nature, that is, once established by the Commission, base rates are final for the period in which they apply.”) (emphasis in original).

³⁹ Pike County Light & Power Co. v. Pennsylvania Pub. Util. Comm’n, 87 Pa. Cmwlth. 451, 456, 487 A.2d 118, 121 (1985).

⁴⁰ Popowsky v. Pennsylvania Pub. Util. Comm’n, 695 A.2d 448, 451 (Pa. Cmwlth. 1997).

PGW St. No. CRRC 1, at 12. The retroactive character of this aspect of the CRRC proposal is highlighted by PGW's strained use of the term "E" factor to characterize this CRRC component. Thus, the Company contends that if its proposed CRRC were adopted, this bad debt overrun arising from a period when the CRRC did not even exist, should be treated like a GCR "E" factor.

All the non-PGW expert witnesses concluded that this provision of the CRRC runs afoul of the prohibition against retroactive ratemaking. OCA St. 1, at 9; OCA St. 1S, at 2, 4; OSBA St. 1, at 12, 29-31; OTS St. 1, at 6. Even if the Commission were to approve the proposed CRRC surcharge to be effective September 1, 2004, thereby allowing PGW to begin to recover for uncollectibles undercollections going forward, it would be improper to allow PGW to recover for shortfalls occurring prior to such effective date.

Although PGW may contend that charging for the unrecovered uncollectibles expenses incurred in FY2004 would not constitute retroactive ratemaking because the amount of recovery will be established after or around the same time as the PUC order authorizing the collection, this does not negate the fact that the shortfalls actually occurred in the twelve months prior to the entry of any such order. Customers paying bills during FY2004 were not on notice that PGW could charge them again for costs incurred during that time period. As OSBA witness Knecht explained, "PGW's customers had no warning that they were going to be required to pay for PGW's undercollections in FY2004 until PGW filed its application." OSBA St. 1, at 30-31. Many of

the witnesses who testified at the public input hearings expressed this concern in real-world terms: they budgeted and sacrificed to pay their gas bills, and now were being required to pay for those who had not paid their own bills.⁴¹

To the extent PGW claims that its proposal to amortize under recovered uncollectibles expenses for FY2004 over a three-year period is permitted under the exception to retroactive ratemaking, the Company is incorrect. The Commonwealth Court has recognized that, where unanticipated expenses are “extraordinary and nonrecurring,” these expenses may in some circumstances be recovered subsequently and amortized over a period of years.⁴² However, the Court has cautioned that “[e]xtraordinary cannot mean merely unanticipated, because then every unexpected occurrence or failure to predict an item would be recoverable and the exception would overwhelm the rule, making test years meaningless.” Rather, to be “extraordinary” there must be a “substantial, one-time expense or a substantial item that will not appear as a continuing expense and could otherwise never be recovered in rates because ... it would be normalized out of the test year as abnormal.”⁴³

⁴¹ See, e.g., Public Input Hearing testimony of Geralyn Chapuis, 3111 Bell Green Terrace, Philadelphia, PA 19154 : “We struggle to make ends meet. We reduce our heat, wearing an extra layer of clothing, just in order to pay the bills we have to pay We can’t go on like this and it’s not just the proposed increase to pay for people that don’t pay....” Public Input Hearing Transcript at 122-123.

⁴² Popowsky v. Pennsylvania Pub. Util. Comm’n, 164 Pa. Cmwlth. 600, 643 A.2d 1146, 1149 (1994) (citing Philadelphia Elec. Co. v. Pennsylvania Pub. Util. Comm’n, 93 Pa. Cmwlth. 410, 422, 502 A.2d 722, 728 (1985) and Pike).

⁴³ Id.

PGW cannot fit its CRRC request into this exception. First, based on its own justification for requesting the surcharge, PGW implies that the collections shortfall was not unanticipated, as it is largely attributed to “historically high natural gas rates,” as natural gas prices have been rising since 1999, and the known fact that PGW’s customer base consists of a large number of low-income households that have difficulty paying their bills.⁴⁴ Additionally, PGW seeks retroactive recovery of non–extraordinary collections short falls, since it seeks to recover any shortfall below the 92.38% allowed in its base rates, on the false premise that the Commission had guaranteed that PGW would be able to recover every penny of its allowed bad debt expense. Finally, assuming that PGW’s expert witness, H. Gil Peach, correctly predicts that the “upward trend in the price of natural gas” and the “continuing decline in real income in the City” are “likely to continue,” the purported dropoff in collections is not a non-recurring expense that could not be addressed in a base rates case. PGW St. CRRC-4, at 3.

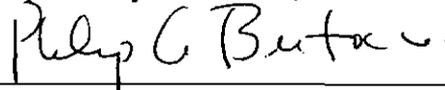
In sum, even if the Commission were to approve the prospective aspects of the CRRC, PGW has not shown that the amount it wishes to amortize based on uncollectibles in FY2004 is an “extraordinary” and “non-recurring” expense warranting an exception to the prohibition on retroactive ratemaking.

IV. Conclusion.

⁴⁴ CRRC Petition, at 2.

For all the foregoing reasons, Action Alliance et al. respectfully request the Commission to deny PGW's Petition to implement a proposed CRRC. PGW has not demonstrated that any form of extraordinary relief – let alone an illegal CRRC – may be authorized, because the Company's financial stability is not threatened and no imminent FY2004 cash crisis exists. Moreover, as State Representative Dwight Evans emphasized in his Public Input Hearing Testimony, the CRRC, if approved, would seriously undermine the Commission's ability to enforce the "just and reasonable" standard and would take away vital necessary protections from PGW's customers, and possibly other Pennsylvania customers affected by this dangerous precedent.⁴⁵

Respectfully submitted,



PHILIP A. BERTOCCI, ESQUIRE
LAURA MOSKOWITZ, ESQUIRE

Attorneys for Action Alliance of Senior Citizens of
Greater Philadelphia, ACORN and Tenants' Action
Group

⁴⁵ Public Input Hearing Testimony, Representative Dwight Evans, May 6, 2004, 1 p.m., page 6 ("If the PUC grants this petition, it will not be just the people of Philadelphia who will suffer. A new, bad, legal rate-making precedent would be established, and every other utility will come before the PUC asking for the same sickening sweet deal. Every other Pennsylvanian can look forward to automatic rate increases if the PUC sides with PGW. And it will not just be gas companies who will seek this. It will be all the utilities").

Proposed Findings of Fact

1. The City of Philadelphia will grant back to PGW the \$18 million City Payment for FY2004 and each year thereafter through FY2008. PGW St. CRRC-1R, at 3 and Exhibit JRB-10; PGW St. CRRC-5, at 8.
2. The grant back of the \$18 million City Payment increases PGW's cash resources for FY2004 by \$18 million and increases cash resources in FY2005-2008 by \$18 million more than would otherwise exist if the City Payment was not granted back. Transcript, at 331.
3. The City of Philadelphia will defer the due date for repayment by PGW of the \$45 million City Advance from FY2006 to FY2008. PGW St. CRRC-5 at 5 and Exhibit TEK-1, at 2. PGW presented no forecasts in this proceeding for FY2005, so that there is no evidence concerning what impact the deferral of repayment of the \$45 million City Advance from FY2006 to FY2008 would have on PGW's cash flow in the near term. OSBA St. No. 1, at 13. It may reasonably be inferred that such a deferral or extension can only help PGW and its customers.
4. At the time when PGW filed its CRRC Petition, PGW management was aware that there was a risk of a work stoppage in connection with the renegotiation in May 2004 of the collective bargaining agreement with PGW's union, the Service Employees International Union, Local 686 (SEIU). Such a work stoppage would have jeopardized PGW's efforts to maintain its collection ratio at least at its historical 92% level. Transcript, at 377. After the filing of the CRRC Petition, however, PGW was successful in negotiating a one year contract extension between the SEIU and PGW. PGW St. CRRC-5, at 11.
5. After the filing of the CRRC Petition, and the issuance of the Standard & Poor's and Fitch bond ratings in April 2004, PGW successfully negotiated a deferred natural gas payment arrangement. Transcript, at 338. This Natural Gas Payment deferral was in the approximate amount of \$53.4 Million involving 9.2 Bcf with a FY2004 impact of \$10 million per month in reduced natural gas disbursements in the months of June, July and August, 2004. PGW St. CRRC-1R, at 3 and Exhibit JRB-10. The cash flow impact of this transaction would extend into the Fall 2004, and that PGW would only be obligated to actually pay for this gas beginning in December, at a time when its billings and receipts could better support such payments. Transcript, at 338.
6. As a result of the Natural Gas Payment deferral arrangement, as well as more accurate information concerning March disbursements, PGW was, as of May 3, 2004,

projecting gas disbursements in the remainder of FY2004 which were \$23.5 million less than projected at the time of the filing of the CRRC Petition. PGW St. CRRC-1, Exhibit JRB-5, p. 2; PGW St. CRRC-1R, Exhibit JRB-10.

7. PGW's premise that the Company has no more ability to control uncollectible expenses associated with increased gas costs than it does to control its gas costs does not correspond to reality. PGW itself admits that the Company can substantially affect its collections ratio by improving its collections practices – practices which the Company only operationally begun to address several months ago. PGW St. CRRC-3; PGW St. CRRC-1, at 13; CRRC Petition, at 11, ¶18..

8. The effect of the CRRC would be to diminish PGW's and the City's collective and institutional incentive to improve PGW collections, because the automatic mechanism shifts the financial risks of failure from the Company and its owner to PGW customers. OTS St. 1, at 4, 14; OCA St. 1, at 16; OSBA St. 1, at 23-24.

9. At the time of the evidentiary hearings, the Company was projecting that its collections ratio for FY2004 would be between 90.4% and 93%. PGW St. CRRC-1R, Exhibit JRB-10. The 90.4% projection was based on the Company's historical performance in the period April 2003 through March 2004, while the 93% estimate was based on 7 months actual FY2004 performance, and 5 months projected. PGW St. CRRC-1R, at 2.

10. The cumulative effect of events occurring after the filing of PGW's CRRC Petition was to eliminate the prospect of the claimed FY2004 year end cash "crisis." PGW's year end cash projections have risen from a negative \$5 million (as shown on the March 1, 2004 PGW Exhibit JRB-5, p. 2) to \$31 to \$36 million. PGW St. CRRC-1R, at 3 and Exhibit JRB-10; PGW St. CRRC-1R

11. The Commission has never explicitly acknowledged that PGW needed even \$35-40 million in year end liquidity. Transcript, at 332. Such amounts are vastly greater than the year end liquidity which the Company has experienced, without crisis, in recent years, even after receiving various forms of extraordinary relief. PGW had year end cash or equivalents of \$5.9 million in FY2003, \$12.5 million in FY2002, \$3.5 million in FY2001 and \$8.4 million in FY2000. Action Alliance Cross-Examination Exhibit 1; Transcript, at 334-336.

12. PGW has not met its burden of showing that it faces an imminent cash "crisis" at year end FY2004, which would place in jeopardy its ability to operate and to sell bonds necessary to sustain its capital programs. Proposed Findings of Fact Nos. 1-11.

Proposed Conclusions of Law

1. The CRRC is not “just and reasonable” because it does not appropriately balance the interests of customers against the financial interests of the utility, in that, without a demonstrated imminent financial crisis:

(A) the CRRC would retroactively require customers who have paid their bills in full for service provided in FY2004 to pay additional dollars to compensate for the fact that PGW failed to collect what was owed in the same period by other customers;

(B) the CRRC would require good paying customers in FY2005 and FY2006 to pay more than what was allowed in base rates to compensate for the fact that PGW failed to collect what was owed by other customers.

(C) the \$55.7 million which is an integral part of the formula determining how much customers would pay under the CRRC does not accurately reflect whatever amount was allowed for uncollectibles in PGW’s last base rate case. OCA St. 1, at 19, 20; OSBA St. 1, at 3; OTS St. 1, at 9.

(D) the CRRC would transfer the risk of bad debt overruns from the Company to customers, but requires no refund to customers when PGW’s actual bad debt expense is less than that allowed in base rates. OCA St. 1, at 15-16; OSBA St. 1, at 25-26; OTS St. 1, at 5-6.

(E) as proposed outside the context of a base rate case, the CRRC does not take into account offsetting cost savings achieved or achievable by PGW, nor consider the level of service provided to customers, and therefore does not permit the ratemaker to conduct an appropriate balancing of interests. OCA St. 1, at 13-15, 17; OSBA St. 1, at 11.

(F) while ostensibly intended to allow PGW to recover for uncollectible expense associated with increased gas costs, the CRRC in fact overreaches, allowing recovery for uncollectible under recovery associated with base rate increases as well. OSBA St. 1, at 12, OTS St. 1, at 4.

2. The OTS Alternative is not “just and reasonable” because it does not appropriately balance the interests of customers against the financial interests of the utility in that, without a demonstrated imminent financial crisis:

(A) the OTS Alternative would require good paying customers in FY2005 and

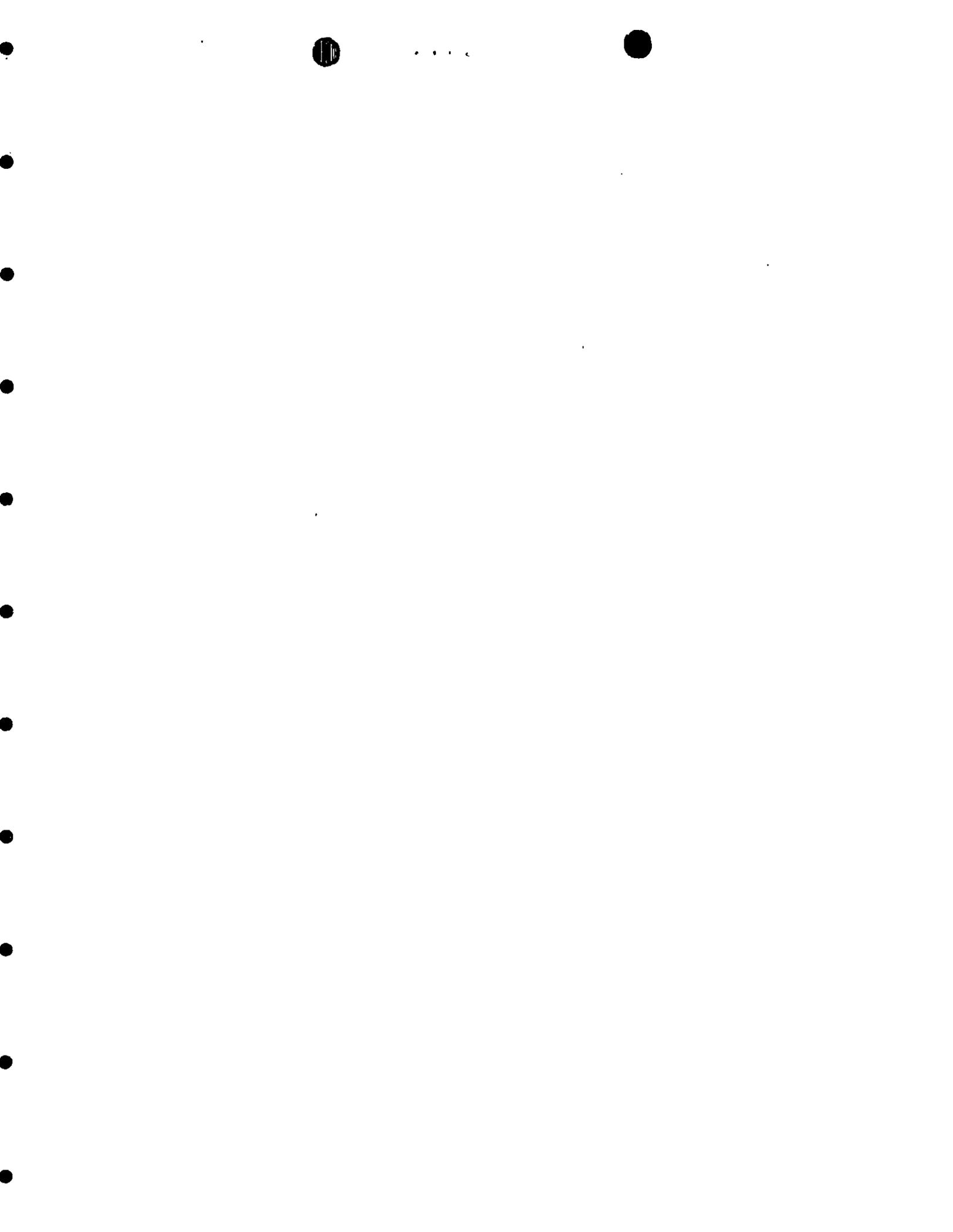
FY2006 to pay more than what was allowed in base rates to compensate for the fact that PGW failed to collect what was owed by other customers.

(B) as proposed outside the context of a base rate case, the OTS Alternative does not take into account offsetting cost savings achieved or achievable by PGW, nor consider the level of service provided to customers, and therefore does not permit the ratemaker to conduct an appropriate balancing of interests. OCA St. 1, at 13-15, 17; OSBA St. 1, at 11.

3. Public Utility Code Section 1307 does not authorize the Commission to create a sliding scale of rates to recover uncollectible expenses, as proposed by PGW and OTS, because uncollectible expenses associated with increased gas costs are not "gas costs," are not largely beyond the control of the utility, and are not an expense that can be "specifically identified" in the way that gas costs and any other costs recoverable pursuant to 1307(a) can be identified.

4. For the Commission to approve the CRRC or the OTS Alternative would be to violate the rule against single-issue ratemaking.

5. The CRRC's provision for the recovery of unrecovered uncollectible expenses arising from FY2004, before the date when the CRRC would be effective, violates the prohibition against retroactive ratemaking.



CERTIFICATE OF SERVICE

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

Dated: June 14, 2004

BY E-MAIL AND FIRST CLASS U.S. MAIL, POSTAGE PREPAID.

Daniel Clearfield, Esquire
Mark Stewart, Esquire
Wolf, Block, Schorr & Solis-Cohen, LLP
212 Locust Street, Suite 300
Harrisburg, PA 17101
dclearfield@wolfblock.com

Gregory J. Stunder, Esquire
Philadelphia Gas Works
800 W. Montgomery Avenue
Philadelphia, PA 19122
greg.stunder@pgworks.com

Johnnie E. Simms, Esquire
Pennsylvania Public Utility Commission
Office of Trial Staff
Commonwealth Keystone Bldg., 2 West
P.O. Box 3265
Harrisburg, PA 17120
josimms@state.pa.us

Steven C. Gray, Esquire
Office of Small Business Advocate
Commerce Building, Suite 1102
300 North 2nd Street
Harrisburg, PA 17101
sgray@state.pa.us

Stephen Keene, Esquire
Office of Consumer Advocate
Forum Place Building, 5th Floor
555 Walnut Street
Harrisburg, PA 17101-1921
skeene@paoca.org

David M. Kleppinger, Esquire
Charis Mincavage, Esquire
McNees, Wallace & Nurick
100 Pine Street
P.O. Box 1166
Harrisburg, PA 17108-1166
cmincavage@mwn.com

Christopher B. Craig, Esquire
Senate Democratic Appropriations
Committee
Room 545, Main Capitol Building
Harrisburg, PA 17120
ccraig@fumo.com

Renardo L. Hicks, Esquire
Anderson, Gulotta & Hicks, PC
1110 N. Mountain Road
Harrisburg, PA 17112
rhicks@aghweb.com

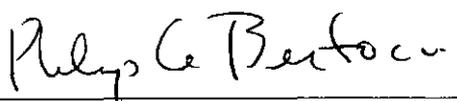
Philip L. Hinerman, Esquire
Fox Rothschild, LLP
2000 Market Street, 10th Floor
Philadelphia, PA 19103-3291
phinerman@foxrothschild.com

BY FIRST CLASS U.S. MAIL, POSTAGE PREPAID

William Kitsch
1233 Stanwood Street
Philadelphia, PA 19111

Barbara Greening, Esquire
1904 Green Street
Philadelphia, PA 19130

Adrienne Glenn
6342 Ardleigh Street
Philadelphia, PA 19138-1002



PHILIP A. BERTOCCHI

212 Locust Street, Suite 300, Harrisburg, Pennsylvania 17101
Tel: (717) 237-7160 ☐ Fax: (717) 237-7161 ☐ www.WolfBlock.com

Daniel Clearfield
Direct Dial: (717) 237-7173
Direct Fax: (717) 237-7161
E-mail: dclearfield@wolfblock.com

ORIGINAL

June 14, 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

RECEIVED
2004 JUN 14 PM 4:20
SECRETARY'S BUREAU

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 Main 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

For WOLF, BLOCK, SCHORR and SOLIS-COHEN LLP

DC/lww

Enclosure

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

DSH:41351.1/PHI211-217982

123

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission,

v.

Philadelphia Gas Works

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

R-00049157 ✓

P-00042090 ✓

ORIGINAL

PHILADELPHIA GAS WORKS' MAIN BRIEF

DOCKETED
JUN 16 2004

**DOCUMENT
FOLDER**

Daniel Clearfield, Esq.
William Mosca, Esq.
Wolf, Block, Schorr and Solis-Cohen LLP
212 Locust Street, Suite 300
Harrisburg, PA 17101
(717) 237-7173

SECRETARY'S BUREAU

2004 JUN 14 PM 4: 20

RECEIVED

Of Counsel:
Gregory Stunder, Esq.
Philadelphia Gas Works
800 West Montgomery Ave
Philadelphia, PA 19122

Date: June 14, 2004

TABLE OF CONTENTS

	Page
TABLE OF AUTHORITIES	iii
I. STATEMENT OF THE CASE.....	1
II. INTRODUCTION & SUMMARY OF ARGUMENT	3
III. ARGUMENT	9
A. The CRRC is Needed to Provide Sufficient Cash to Pay PGW’s Bills and to Provide Assurances to the Bond Ratings Agencies so as to Preserve Its Investment Grade Bond Rating.....	9
1. Background.....	9
a. Uncollectible Accounts Expense	10
b. Cash Working Capital.....	11
2. The Bond Rating Agencies Have Confirmed That PGW’s Cash Levels Are Inadequate and Have Indicated That the Company Will be Downgraded Absent Material Near Term Improvement.	12
3. The Reason For The Crisis: Soaring Natural Gas Prices.....	13
4. PGW and its Owner, the City of Philadelphia, Have Taken All Reasonable Steps to Address its Collections Shortfall	19
a. Grant Back of City Fee and Deferral of City Loan.....	19
b. One-time Gas Storage Payment Deferral.....	19
c. PGW Collections Initiative.....	20
d. Cost Saving Efforts.....	21
e. Offsets to Social Program Costs.....	21
5. Despite PGW’s Efforts to Increase Collections and Cash Working Capital and to Decrease Costs, PGW’s Current Liquidity Has Been Found to be Inadequate to Maintain its Investment Grade Bond Rating.....	21
B. THE CRRC IS SUPERIOR TO ANY OTHER METHOD OF ADDRESSING PGW’S CASH RECEIPTS ISSUES.	24
1. The CRRC Mechanism Provides a Targeted Solution to PGW’s Real Problem – the Potential for a Debilitating Cash Receipts Shortfall.....	24

2.	The Precise Mechanics of the CRRC Demonstrate its Inherent Superiority to Base Rates Proceedings and its Ease of Administration.	27
C.	PGW’s CRRC Is Well Supported By Authority In The Public Utility Code And Consistent With Prior Commission Action.....	29
1.	Introduction.....	29
2.	Pennsylvania Law Recognizes the Appropriateness of Automatic Adjustment Clauses to Reflect Changes in Customer Charges of Specific Rate Components.....	31
3.	PGW’s Proposal Satisfies All of the Elements Required for Section 1307(a) Treatment.....	33
4.	PGW’s E-factor is also justified, and does not constitute retroactive ratemaking.....	35
D.	SUBSTANTIAL LEGAL PRECEDENT FROM OTHER JURISDICTIONS SUPPORTS RECOVERY OF UNCOLLECTIBLE ACCOUNTS EXPENSE THROUGH A FLEXIBLE AUTOMATIC ADJUSTMENT MECHANISM.....	39
1.	Introduction.....	39
E.	The OSBA, OCA And OTS Criticisms Of The CRRC Have No Basis In Reality And Ought To Be Rejected.	41
1.	OSBA.....	42
2.	OCA.....	47
3.	OTS.....	48
IV.	CONCLUSION.....	52

APPENDIX A – Proposed Findings of Fact and Conclusions of Law

TABLE OF AUTHORITIES

CASES

	<u>Page(s)</u>
<i>Columbia Gas of Pennsylvania, Inc. v. Pennsylvania Public Utility Commission</i> , 613 A.2d 74 (Pa. Cmwlth. 1992) <i>aff'd per curiam</i> 636 A.2d 627 (1994)	36-38
<i>Creation and Implementation of a Statewide Consumer Education Program for Natural Gas Competition</i> , 2000 Pa. PUC LEXIS 12	31, 33
<i>National Fuel Gas Distribution Corp. v. Pa. P.U.C.</i> , 473 A.2d 1109 (Pa. Cmwlth. 1984)	31-33, 42
<i>Office of Consumer Advocate v. The Peoples Natural Gas Company</i> , 2003 Pa. PUC LEXIS 53	36-38
<i>Pennsylvania Public Utility Commission v. Consumers Pennsylvania Water Company</i> , 1997 Pa. PUC LEXIS 141	36, 38
<i>Pennsylvania Public Utility Commission v. Philadelphia Thermal Energy Corp.</i> , 1991 Pa. PUC LEXIS 80	32, 33
<i>Pennsylvania Public Utility Commission, et al. v. Jackson Sewer Corporation</i> 2001 Pa. PUC LEXIS 53	32, 34, 37
<i>Pennsylvania Industrial Energy Coalition ("PIEC") v. Pa. P.U.C.</i> , 653 A.2d 1336 (Pa. Cmwlth. 1995)	32, 33
<i>Petition of Pennsylvania-American Water Company for Approval to Implement a Tariff Supplement Establishing a Distribution System Improvement Charge</i> , 1996 Pa. PUC LEXIS 182	31-34
<i>Philadelphia Electric Company v. Pennsylvania Public Utility Commission</i> , 502 A.2d 722 (Pa. Cmwlth. 1985)	37
<i>Pike County Light and Power Company v. Pennsylvania Public Utility Commission</i> , 487 A.2d 118 (Pa. Cmwlth. 1985)	37
<i>Policy Statement on Clean Air Act Emissions Allowances</i> , 1993 Pa. PUC LEXIS 2	31
<i>Popowsky v. Pennsylvania Public Utilities Commission</i> , 695 A.2d 448 (Pa. Cmwlth. 1997) <i>appeal denied</i> 702 A.2d 1062 (1997)	36-38

ADMINISTRATIVE CASES

	<u>Page(s)</u>
<i>In the Matter of the Joint Application of The East Ohio Gas Co. et al.,</i> No. 03-1127-GA-UNC (OH, 2003)	39, 40
<i>Pa. P.U.C. v. Philadelphia Gas Works,</i> R-00005654, R-00005619 (Feb. 22, 2001).....	30
<i>Pa. P.U.C. v. Philadelphia Gas Works,</i> R-00006042.....	11, 24
<i>Pa. P.U.C. v. Philadelphia Gas Works,</i> R-00017034 (Aug. 8, 2002)	24
<i>Petition of Chattanooga Gas Co. et al.</i> No. 03-00209 (TN, 2004)	39
<i>Petition of Philadelphia Gas Works for Extraordinary Rate Relief Pursuant to</i> <i>66 Pa. C.S. § 1308(e), R-00017034F0002 (April 12, 2002)</i>	<i>5, 6, 24, 30, 48</i>
<i>Petition of United Cities Gas Co.,</i> No. 14422 (GA, 2001)	39, 41
<i>Petitions of Atmos Energy Corp. and Roanoke Gas Co.,</i> PUE 2002-00373 and 2002-00002 (VA, 2002)	39, 41

STATUTES

66 Pa. C.S. § 1307.....	<i>passim</i>
66 Pa. C.S. § 1307(a)	<i>passim</i>
66 Pa. C.S. § 1307(e)	33, 35
66 Pa. C.S. § 1307(f).....	9, 25, 28, 38
66 Pa. C.S. § 1308(e)	27, 30, 30
66 Pa. C.S. § 2212(c)	29, 30, 35
66 Pa. C. S. § 2212(e)	11

OTHER

Page(s)

Moody's Investors Service Global Credit Research Rating Update (June 8, 2004)5, 12

Wall Street Journal14

WTRG Energy Economics Newsletter14

I. STATEMENT OF THE CASE

On March 1, 2004, Philadelphia Gas Works (“PGW” or “Company”) filed with the Commission its Proposed 2004 Annual Gas Cost Rate (“GCR”) Adjustment, with supporting testimony and data. On that same date, PGW filed a Petition to Establish a Cash Receipts Reconciliation Clause (“CRRC”), requesting that the Commission implement a flexible automatic adjustment clause mechanism designed to reconcile the dramatic disparity between its cash receipts and billed revenues, caused by spiraling wholesale natural gas costs, and ensure that its receipts reach minimally acceptable, historic levels. PGW also filed a Motion to Consolidate the CRRC and GCR proceedings.

In April 2004, both Standard and Poor’s and Fitches Investment Services downgraded PGW debt to the lowest investment grade level above junk status. The rating agencies based their actions on the Company’s liquidity problems and inability to generate sufficient cash flow from operations to meet its financial commitments. Additionally, both rating agencies warned in public communications that, absent near term, material improvement in the Company’s collections and cash margins, a further downgrade to junk status will occur. In June 2004, Moody’s Investors Service followed suit and placed PGW on its Watchlist.

The Office of Consumer Advocate (“OCA”) filed a complaint as to PGW’s GCR filing, and the Consumers Education Protective Association (“CEPA”)¹ filed a complaint as to the Company’s GCR and CRRC filings. The Office of Small Business Advocate (“OSBA”) and Philadelphia Industrial and Commercial Gas Users Group (“PICGUG”) intervened in the proceedings, and the Office of Trial Staff (“OTS”) actively participated therein. OCA, OSBA, and CEPA filed Answers to the CRRC Petition. On March 17, 2004, Administrative Law Judge (“ALJ”) Charles E. Rainey, Jr., granted the Company’s Motion and consolidated the GCR and CRRC filings.

The ALJ granted leave to intervene to Pennsylvania Senator Vincent J. Fumo, Philadelphia City Council President Anna C. Verna, and City Council members James F.

¹ CEPA was also joined in its complaint by Action Alliance of Senior Citizens of Greater Philadelphia, Association of Community Organizations for Reform Now, and the Tenant’s Action Group (collectively “CEPA”).

Kenney, Frank DiCicco, Michael A. Nutter, David Cohen, Joan L. Krajewski, and Juan F. Ramos. Interventions by the Philadelphia Housing Authority, Philadelphia District Attorney Lynne Abraham, and Pennsylvania Senators Michael Stack and Anthony Williams were also granted.

On May 5, 6 and 20, the Commission held public input hearings on PGW's GCR and CRRC proposals. As would be expected with a proposed rate increase, the consumers who spoke at the hearings were not supportive of the CRRC. Notably, the public was generally unaware that the Company's base rates, which they are required to pay, already contain a provision for uncollectibles expense. Likewise, the speakers were without information detailing the consequences to the Company, the rates they pay, and the service they receive from a downgrading of PGW's bond rating to junk status.

In support of its CRRC Petition, PGW filed direct testimony from Joseph R. Bogdonavage, Senior Vice President of Finance, Douglas Moser, Vice President of Gas Management, Randall Gyory, Vice President of Customer Affairs, and Hugh Gilbert Peach, principal of H. Gil Peach & Associates and a nationally known expert on utility customer payment characteristics and universal service programs. This testimony documented PGW's liquidity crisis, its causes and anticipated duration, the trends in natural gas wholesale prices and the impact on customers of the recent, sustained increases, the uniqueness of PGW's customer base and the unique, negative impact the increases in gas costs have had on them, the steps the Company has and is undertaking to improve its collections and address its cash receipts shortfall, and the rationale behind and workings of the CRRC. The Company also filed direct testimony in support of its GCR filing sponsored by Mr. Moser and Kenneth Dybalski, Manager of Gas Planning.

On April 16, 2004, direct testimony was submitted on behalf of the OCA, OTS, and OSBA as to both the proposed GCR and CRRC. On April 30, rebuttal testimony was served by the OSBA and Messrs. Bogdonavage, Moser, Dybalski and Peach for PGW. Additionally, PGW C.E.O. Thomas E. Knudsen submitted rebuttal testimony regarding the need for and appropriateness of the CRRC. Mr. Knudsen detailed the seriousness of the Company's liquidity crisis, the consequences from an additional downgrading by the rating agencies of PGW debt to

junk status, the need for the CRRC to allay the rating agencies' concerns, and the strenuous efforts by the Company to reduce costs and enhance liquidity.

On May 7, 2004, OCA, OTS and OSBA submitted surrebuttal testimony. On May 11, 2004, an evidentiary hearing was held on the CRRC Petition.² The parties held settlement discussions on the CRRC which proved unfruitful.

On June 3, 2004, PGW, OTS, OCA, and CEPA filed a Joint Petition for Settlement of PGW's 2004-2005 GCR Proceeding. The remaining parties to the proceeding, including OSBA and PICGUG, did not oppose the Settlement.

On June 2, 2004, the Commission entered an order dispensing with the ALJ's Recommended Decision, and directing that the matter be certified directly to it for disposition at the July 8, 2004, Public Meeting. PGW files this Main Brief in support of the CRRC in accordance with the remaining procedural schedule.

II. INTRODUCTION & SUMMARY OF ARGUMENT

Once again, the Commission is faced with a stark choice: it can step up to make a hard decision to approve a limited automatic adjustment mechanism to provide PGW with a backstop level of cash receipts and cash working capital necessary to keep PGW in a position to be able to pay its bills, access the capital markets and, with the additional help of Chapter 56 waivers and modifications, protect its investment bond rating. Or it can fall victim to the rhetoric and refuse PGW's request, likely resulting in a bond downgrade to "junk" status and a cascade of disastrous consequences that will threaten the Company's ability to continue to provide safe, reliable and adequate service to over five hundred thousand customers in the City of Philadelphia.

In considering PGW's Petition for the establishment of a flexible Cash Receipts Reconciliation Clause ("CRRC"), the Commission, the Company and the parties find themselves in familiar territory. PGW is approaching its four year anniversary of being under Commission jurisdiction. During that period, these players, often working together, have achieved significant

² In addition to the presentation of rejoinder and the cross-examination of witnesses, PGW presented testimony from Kenneth S. Dybalski, Manager of Gas Planning, who detailed PGW's final proposed CRRC levels depending upon PGW's realized level of cash receipts. Tr. 396-402.

success in improving PGW's operations, the quality of its service and customer relations, as well as in shepherding the Company through restructuring to choice and competition. Unfortunately, as the evidence in this case and the history of the last four years reveal, similar success in addressing the Company's continuous and very serious cash flow and liquidity problems has proven elusive.

Due to the effects of rising natural gas prices, PGW, again, finds itself in a severe financial crisis, which is imminently threatening to cripple the Company and its ability to pay its bills and to continue to make needed capital improvements. While all gas utilities in Pennsylvania have felt the impact of these higher prices, the record shows that the impact has been much more severe on PGW because of the dramatic difference between PGW's customer base and that of the other Pennsylvania utilities. This crisis is, in reality, a continuation of a condition inherited upon the assumption of PUC jurisdiction is a cash crisis. PGW is a cash flow regulated company. Beyond its fully extended short term commercial paper and a fully utilized loan from its owner, the City of Philadelphia, the Company must recover in rates virtually all of the cash working capital it needs to pay its bills when they come due. But rising natural gas prices have caused havoc with PGW's cash receipts. As gas bills have gone up, PGW has been able to collect less and less of its billings both in absolute and relative terms. The high gas rates in FY 2003 reduced receipts as a percentage of billings to 86.5% – their lowest level ever – robbing the Company of some \$40 million in working capital and increasing its bad debt expense to \$85 million – almost \$30 million more than its current rate allowance (\$55.7 million). The net effect is that if PGW's collections levels do not improve, PGW will not have sufficient cash levels from operations to meet its obligations.

In addition to threatening the Company's ability to pay its bills when due, the cash crisis, exacerbated by these unprecedented levels of natural gas prices (which, because of its demographics, affects PGW's service territory far more than other areas), has resulted in PGW's long term bonds being downgraded. In early April, Standard and Poor's downgraded PGW's bonds to the *lowest* investment grade rating available and stated that further downgrades to junk

bond status *will happen* absent *material* improvement in the Company's cash margins and liquidity.³

PGW must show this material improvement – or the implementation of steps that will lead to such an improvement – by this fall. PGW is in the midst of trying to issue another long term bond by early fall at the latest. A failure to show a positive response to the current cash crisis by that time, will clearly make it harder for PGW to issue the bond.

Moreover, Standard and Poor's is currently scheduled to conduct a review of PGW's financial performance in February 2005. That review will be based upon investigations and discussions in the months leading up to that date. Without material improvement in PGW's cash working capital and collections in the months prior to that fall review, PGW stands to be downgraded to junk status.

As the PUC is well aware, a downgrade to junk status would produce *devastating* results for both the Company and its customers.⁴ If such a downgrade occurs PGW's access to the capital markets will be severely restricted and the cost of any borrowing that is possible will be vastly more expensive, driving rates up still further and threatening all aspects of the Company's operations. Indeed, in the 2002 *Extraordinary Rate Relief Proceeding*⁵, the Commission found the downgrading of PGW's bonds to junk status, and the resultant damage to the Company and its customers, to be so severe that it warranted the virtually unprecedented remedy of extraordinary rate relief in order to forestall its occurrence. In a passage that could well be *déjà vu* all over again, the Commission declared:

³ The Standard and Poor's statement is included in the record as CRRC-5, Exh. TEK-1. Fitch's also downgraded PGW to just above junk status and announced that it has placed PGW on Credit Watch pending review of progress made during the summer. TEK-2. On June 8 Moody's placed PGW's bonds on its Watchlist and made statements similar to those of S&P saying that "PGW has faced a significant cash flow crunch due to slowed payment by customers of record high gas bills. While PGW has demonstrated that management is focused in the problems and the current marginal cash position allows for business to continue to operate further improvement to PGW's liquidity are required to maintain the current rating level." Moody's Investors Service Global Credit Research Rating Update – PGW (June 8, 2004) www.moodys.com/moodys/cust/research/genoa/report/rating%20Update8062.

⁴ PGW St. CRRC 5 at 7-9. OCA witness Lelash agreed that a downgrade to junk status would have "serious impacts." Tr. 447.

⁵ *Petition of Philadelphia Gas Works for Extraordinary Rate Relief Pursuant to 66 Pa. C.S. § 1308(e)*, R-00017034F0002 (April 12, 2002)

Given the current tenor of the markets and the record evidence regarding PGW's liquidity crisis, our responsibility to the residential and business customers of PGW requires that we act now. We simply cannot wait until PGW collapses. Thus, although the OCA, the OSBA and CEPA argue that PGW's claims are speculative, the evidence clearly establishes that PGW's concerns are well founded and imminent.⁶

Today, the situation is eerily similar. The markets have plainly spoken about their concerns over PGW's inadequate liquidity and the imminent threat of further downgrades if the Company's cash receipts shortfall is not sufficiently addressed. As a result, PGW's very real concerns over its cash levels and bond ratings are indeed well founded, despite the familiar refusal to deal with this reality by some of the named parties.⁷ Most importantly, though, is the fact that the Commission faces the *same responsibility* to PGW's customers and the Philadelphia region and simply cannot wait until the Company collapses to assist it in fixing its liquidity problems.

As in the past, all parties concerned about the Company and its ability to continue to provide safe and adequate service to its customers need to step forward to assist. To be sure, major steps have already been taken. For example the Company and the City have taken dramatic action in the face of this current cash receipts shortfall.

- The City of Philadelphia has taken the unprecedented step of foregoing and granting back its statutorily mandated, \$18 million annual payment to PGW, and not just this year but for *five* years for a \$90 million cash infusion.⁸
- The City has agreed to voluntarily defer the due date for its \$45 million line of credit (itself an attempted one time liquidity fix) for two additional years.⁹

⁶ *Id.* at 15.

⁷ Notably, OTS was not among those parties during the extraordinary rate proceeding, and it is not in lockstep with their state of denial now. Rather, OTS has offered honest recognition of the problems behind PGW's request for a CRRC, as well as a good faith, though insufficient, proposal for remedying them.

⁸ PGW St. CRRC-1R at 3.

⁹ *Id.* Significantly, in its extraordinary rate relief order, the Commission urged the City and PGW "in the strongest terms to explore" a grant back of the \$18 million fee and deferment of repayment on the \$45 million loan. *Extraordinary Rate Relief Order*, R-00017034F0002 at 4, *see also Id.* at 28. Despite the fact that such steps literally mean a loss of revenue to the financially strapped City of Philadelphia and its

- PGW has arranged to defer payment for the injection of natural gas into its storage facilities until next fiscal year, preserving \$30 million of needed cash on hand.¹⁰
- The Company has maintained and intensified its efforts to improve its collections, despite long odds created by high natural gas costs, and is on track for a collections rate this year that would reflect historical levels.¹¹

Despite these past and pending efforts and fixes, the Company is simply “not there yet” in terms of remedying its liquidity problems.¹²

PGW has crafted a multi-pronged plan designed to maintain PGW’s investment grade bond rating and sell bonds this fall by seeking to put in place a series of tools designed to convince the investment community that the material improvement has been made or is on the way. The first key component, and the aspect directly at issue here is the establishment of the CRRC mechanism. The CRRC is crucially necessary to create a backstop or failsafe to assure the rating agencies and the investment community that PGW will at least realize revenues reflective of its historic and previously approved collections levels. With the CRRC, PGW will be able to tell the financial community that either its own collections efforts will improve so as to reflect historic levels, or PGW will collect the needed cash through the CRRC mechanism.

To be sure, approving the CRRC alone will not be sufficient, in PGW’s view, to stave off further negative action by the rating agencies. They were quite clear that PGW must do more than merely achieve historic collections levels and cash working capital balances: it must show *a material* improvement in those levels. The Commission must recognize that PGW needs a *package* of tools to produce the material improvement in its cash working capital. For this reason, PGW is in the process of filing a petition requesting waiver or modification of certain Chapter 56 rules or administrative interpretations (and is also advocating before the General

citizens, the City and PGW have not only “explored” such steps, but have actually taken them and done so to an even greater degree than was initially contemplated by the PUC.

¹⁰ PGW St. CRRC-5 at 6-8.

¹¹ PGW St. CRRC-3.

¹² Likewise, the base rate and extraordinary rate increases previously approved by the Commission have proven illusory in terms of addressing the Company’s cash shortfall, as increasing gas costs and the concomitant collections problems have prevented it from realizing the full benefit of those measures.

Assembly for state funding for LIHEAP). Because of the linkage between these two tools, it is crucially important that the Commission simultaneously consider PGW's Chapter 56 Waiver/Modification request and its CRRC petition. Moreover, if the Commission declines to authorize PGW's Chapter 56 Waiver/Modification request in whole or in part, it becomes even more essential to authorize the CRRC mechanism.

This approach is far better than any of the alternatives offered. For example, pursuing PGW's additional cash working capital needs through a base rate or extraordinary increase is not a realistic or reasonable option. Most critically, neither a base rate increase, nor any other possible 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. Further, a base rate increase would entail an exhaustive and burdensome proceeding and result in a remedy that would both potentially overcompensate for the problem and lack desired flexibility. Unlike an increase in base rates which would continue to plague customers even if the cash crisis subsides, PGW's CRRC could result in no increase or charge for customers if collections reach or exceed minimally acceptable levels.

Without the CRRC, the Company can do no more than express its hope that its existing collections efforts will result in a return to historic performance. The consequences if the financial community is not willing to accept mere promises of success, without more, will be devastating.

Far from an extraordinary or unprecedented approach, clauses of a similar nature have been authorized and adopted in a variety of states. More important, this Commission has authorized such automatic adjustment mechanisms when the facts justified them, to recover increases in things as varied as taxes, Clean Air Act compliance costs and sewerage treatment service costs. Contrary to the suggestions of at least some of the parties, a mechanism to address the huge shortfall caused by falling collections and increased uncollectible expense is neither unprecedented nor unreasonable.

In truth, the decision facing the Commission is an easy one: (1) deny PGW's Petition and, if no other action is taken, sit by as PGW's bonds are downgraded to junk status, resulting in a level of devastation to the Company and its customers that the Commission has already

recognized as requiring extraordinary measures to avoid; or (2) approve PGW's CRRC and authorize a flexible surcharge that may result in *no rate increase* for customers at times (if the Company is able to achieve a little better than a 93% cash receipts level rate payers would see no increase from the CRRC starting on September 1, 2004), but will indisputably satisfy the baseline needs of the rating agencies while helping to avert the disaster accompanying a downgrade to junk status and laying a framework that will enable to Company to secure long-term cash sufficiency.

The City has clearly done its part and more by foregoing its annual payment for *five* years and continuing to defer the \$45 million, interest free loan. PGW has done and is doing its part by cutting costs and comprehensively improving its collections policies and programs. The Company respectfully submits that its is now time for the Commission to do its part, by focusing upon the facts, rising above the rhetoric, and approving the CRRC.

III. ARGUMENT

A. **The CRRC is Needed to Provide Sufficient Cash to Pay PGW's Bills and to Provide Assurances to the Bond Ratings Agencies so as to Preserve Its Investment Grade Bond Rating**

1. Background

In order fully to understand the need for the requested automatic adjustment clause, it is necessary to understand PGW's ratemaking methodology and the way in which PGW recovers uncollectible expense in cash working capital as part of its rates. The main drivers of PGW's cost of service are natural gas costs; operating expenses; cash working capital; and the cost of borrowing.¹³ Of these various categories of costs only a tiny percentage (around 11-20 %) are in any way discretionary.¹⁴ As is the case for all natural gas distribution companies in Pennsylvania, PGW recovers its natural gas costs in a separate rate established under Section 1307(f) of the Public Utility Code.¹⁵ The gas cost rate ("GCR") is automatically adjusted

¹³ PGW St. 5, Exh. TEK 4.

¹⁴ *Id.* Excluding labor/benefits; PGW's employee levels, which have decreased year by year, obviously can only be reduced marginally without harming service or safety.

¹⁵ PGW St. CRRC-1 at 3.

quarterly to reflect changes in wholesale prices in natural gas because, historically, natural gas costs have been quite volatile; actually experienced gas costs are largely the function of overall commodity market conditions and outside of the Company's control.¹⁶ While natural gas costs are collected in an automatic adjustment clause that changes as wholesale gas prices change, all of PGW's other costs are recovered in fixed base rates. This includes two key elements of PGW's costs: uncollectible accounts expense and cash working capital.

a. Uncollectible Accounts Expense

Like every company, PGW regularly fails to collect a portion of its billings from customers. When these accounts receivable become permanently uncollectible, PGW has no other alternative but to write them off. Prior to writing off the charges, PGW establishes a provision for uncollectibles which reflects the amount of write-offs it has experienced in the past year plus the amount of additional uncollectibles it anticipates for the coming year. This provision for uncollectibles or uncollectible expense is the basis for a utility's allowance in its base rates.¹⁷ On the basis of dramatically lower levels of natural gas costs, the Commission established PGW's current base rate uncollectible expense allowance of \$55.7 million in the 2001 base rate gas proceeding, based upon an authorized uncollectible expense percentage of 7.616% of *pro forma* gas revenues. This authorized amount implicitly assumed that PGW would collect the remainder of its billed revenues – 92.38%.¹⁸

Historically, PGW's uncollectible expense amount has been in the 7% to 8% level.¹⁹ Since 1999, however, PGW's actual bad debt expense has ranged from 8.1% up to a high of

¹⁶ PGW St. CRRC-1 at 3.

¹⁷ PGW St. CRRC-1 at 4. Both OCA witness Lelash (Tr. 441) and OSBA witness Knecht agreed that PGW's provision for uncollectibles and uncollectible expense was a normal part of utility base ratemaking. OSBA St. 1 at 2.

¹⁸ PGW St. CRRC-1 at 4.

¹⁹ *Id.*

11.2% in 2003.²⁰ For FY 2004, PGW witness Bogdonavage at the initiation of the PGW CRRC filing estimated bad debt expense at 8.6%.²¹

b. Cash Working Capital

While PGW's uncollectible expense is established in a conventional manner, its overall revenue requirement and its provision for cash working capital are determined on a unique "cash flow method" basis. The cash flow method basis, originally used by PGW's predecessor regulatory commission and carried over to this Commission by virtue of the provisions of the Gas Choice Act,²² requires this Commission to establish PGW's rates at a level that will permit the Company to maintain its debt coverage levels required by its bond covenants and to achieve levels of liquidity so that it is able to pay its bills when due. Under this approach, for all intents and purposes, PGW obtains all of its cash working capital from customers in the rates it charges for gas service.²³ PGW has limited sources of short-term borrowing available: a short-term commercial paper line of credit; and a \$45 million City loan. Both vehicles currently are fully extended and are not available to serve their intended purpose: to bridge the gap between PGW expenditures and receipt of revenues to cover those expenditures.²⁴ In past rate proceedings, PGW demonstrated that it needed \$35 to \$40 million in liquidity (i.e., cash and available short-term borrowing) at the end of its fiscal year (August 31st) to provide funding for working capital requirements.²⁵ These year-end balances are crucially necessary so that the Company will have

²⁰ *Id.* at 4, 5.

²¹ PGW Exh. JRB-2.

²² Pa. C.S. § 2212(e). The Commission specifically ruled that the Cash Flow Method was required to be used to calculate PGW's revenue requirement in the 2001 rate proceeding. *Pa. PUC v. PGW*, R-00006042 (Oct. 4, 2001) Opinion and Order at 14-15.

²³ PGW St. CRRC-1 at 7.

²⁴ *Id.* at 8; Tr. at 318. PGW is also able to borrow on a short term basis from its Capital Improvement Fund, the available proceeds of its long term debt which are not as yet used for the capital construction project for which they were borrowed. PGW is required by its bond ordinance, however, to use the funds to make the capital improvement or repay the amounts in the fund by the end of the fiscal year. Accordingly the Capital Improvement Fund does not provide a reliable or regular source of cash working capital for the Company. *See*, PGW St. CRRC-1 at 8. Further, availability of funds for the Capital Improvement Fund depend closely on the availability of revenue from bond sales and, thus, their future availability will be affected by the Commission here.

²⁵ PGW St. CRRC-1 at 7; Tr. at 332.

sufficient funds available to pay its bills in the September – January time frame, when gas sales and revenues start out being very low. As a result of the reduction to its short-term commercial paper line of credit, PGW’s year-end liquidity requirement has now increased to \$60 million.²⁶ This level of end of year liquidity is crucial for PGW to have sufficient cash to pay its gas and other bills through the winter heating season, and must last until the Company is able to garner enough revenues from winter billings to pay its obligations through current receipts.²⁷

2. The Bond Rating Agencies Have Confirmed That PGW’s Cash Levels Are Inadequate and Have Indicated That the Company Will be Downgraded Absent Material Near Term Improvement.

While opposing parties’ claim that PGW’s year end cash projections are really adequate, such claims are patently unbelievable; a company with \$800 million in annual expenses cannot prudently operate with just \$30 million of total cash and borrowing capability available with which to purchase gas, make payroll, pay its long and short-term debt responsibilities and provide for contingencies. Irrefutable proof that PGW’s cash position is in crisis has been provided by objective, unbiased observers – the bond rating agencies. Despite assurances from the City to postpone repayment of short-term debt and to grant back the \$18 million payment for five years, both Standard & Poor’s and the Fitches rating services downgraded PGW debt to just above junk level.²⁸ More disconcerting, the downgrades specifically admonish the Company that if *material* improvement does not occur soon, the Company will be downgraded to below investment grade quality. As stated by Standard & Poor’s:

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 and 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 lower ratings are predicated on the City providing

²⁶ PGW St. CRRC-1R at 4; Exh. JRB-11. This is the amount the bond rating agencies are expecting to see at year end.

²⁷ *Id.*

²⁸ Standard & Poor’s acted on April 9, 2004. Fitch’s followed suit on April 23. On June 8, Moody’s placed PGW on Credit Watch. Moody’s Investors Service Global Credit Research Rating Update – PGW (June 8, 2004) www.moody.com/moodys/cust/research/genoa/report/rating%20Update8062.

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.²⁹

In its downgrade statement, Fitches Investment Service stated as follows:

The rating action primarily reflects PGW's sharply deteriorated liquidity position and the limited ability of its owner, the City of Philadelphia, to provide cash flow support beyond current levels. PGW cannot currently generate sufficient cash from operations to meet all its financial commitment including debt service and has become heavily reliant on external sources for liquidity. While the City appears committed to PGW's success as evidenced by a planned repayment date extension of its \$45 million loan given in 2000 and a proposal to grant back its annual \$18 million payment from PGW in each of the next five years, the City's ability to support the utility's cash flow is more limited than in recent years given it's own financial difficulties . . . for PGW, regaining a Stable Outlook, could be achieved by the successful implementation of planned improvements to revenue collection procedure and/or a strengthening of the City's weakened financial position.³⁰

These ominous statements simply cannot be ignored. Unlike certain parties to this proceeding that have the luxury of blindly focusing on the advocacy of *their* special interests, the Commission is charged with furthering the public interest and cannot turn a deaf ear to these serious warnings.

3. The Reason For The Crisis: Soaring Natural Gas Prices

Because PGW is currently entirely dependent upon customers for its marginal cash working capital, its financial health is uniquely affected by swings in natural gas prices. The main driver of PGW's current financial crisis is high natural gas prices that remain at unprecedented levels. High natural gas costs have not only increased PGW's absolute level of uncollectible expense, but also have reduced PGW's percentage of collections at the same time, affecting its available cash working capital. As PGW witness Moser, Vice President of Gas Management for the Company testified, the prices at which PGW buys natural gas have more

²⁹ PGW St. CRRC-5 at 6; *see also* PGW Exh. TEK-1 (emphasis added).

³⁰ PGW Exh. TEK-2.

than doubled from the range of \$2.00 to \$2.50 in the 1996-1999 timeframe to \$4.50 - above \$6.00 in the 2003-2004 period.³¹

Table One³²

YEAR	PGW FUEL COSTS
2000	\$226,000,000
2001	\$415,000,000
2002	\$315,000,000
2003	\$362,000,000
2004	\$455,000,000

There appears to be no prospects for a near-term reversal of this trend. Mr. Moser also stated (without contradiction) that contract prices for NYMEX futures were projected to be in the \$5.00 - \$6.00 range for the foreseeable future,³³ indeed these levels have already been reached.³⁴

Spiraling natural gas prices have at least two major effects on PGW and its customers, neither of which are good:

First, as one would expect, PGW's purchased gas costs have increased as wholesale natural gas prices have increased. These higher fuel costs are passed directly onto customers through the GCR. For the most part, PGW is permitted (at least in theory) to recover on a dollar for dollar basis these increased wholesale natural gas prices.³⁵

³¹ PGW St. CRRC-2.

³² OCA St. GCR 1 at 24-25.

³³ PGW St. CRRC-2 at 2

³⁴ Indeed, Mr. Moser's prediction now appears to be quite conservative. Since the time he prepared his direct testimony, wholesale natural gas prices have skyrocketed. As of Wednesday, June 9, 2004, natural gas spot prices (Henry Hub) closed at \$6.20 (See WTRG Energy Economics Newsletter, www.wtrg.com/daily/oilandgasspot) and natural gas futures closed at \$6.176. *Wall Street Journal*, June 14, 2004, p. A-2.

³⁵ PGW St. CRRC-1 at 3; St. CRRC-2 Exh. DM-3.

Second, increased fuel expense means higher average bills for customers. The average residential heating bill (assuming 100 Mcf per year per customer) has tracked the increase in PGW's fuel costs:

Table Two³⁶

Year	Average Residential Heating Bill/Year
2000	\$917
2001	\$1,150
2002	\$970
2003	\$1,301
2004 (est.)	\$1,468

These very high levels of billings in turn have two devastating effects on PGW. First, they increase the absolute level of uncollectible expense. Second, they eviscerate PGW's cash receipts, and, in turn, its cash working capital. The following chart depicts the Company's bad debt expense both in absolute terms and as a percentage billed gas revenues:

Table Three³⁷

Year	Bad Debt Expense (000)	Percent
1999	\$39,000	8.1%
2000	\$54,000	10.9%
2001	\$67,633	9.1%
2002	\$51,548	9.2%
2003	\$85,000	11.2%
2004 (est.)	\$70,000	8.6%
Base Rate Allowance	\$55,7000	7.616%

As OTS witness Weakley acknowledged, these high levels of uncollectible expense, directly attributable to higher natural gas costs, have a negative impact on the Company's cash

³⁶ PGW St. CRRC-1, Exh. JRB-3; St. CRRC-2, Exh. DM-3. The lower levels in 2002 was due to lower than normal weather. *Id.*

³⁷ PGW St. CRRC-1, Exh. JRB-2

working capital.³⁸ While PGW's GCR adjusts rates in order to reflect increases (or decreases) in the cost of natural gas PGW procures to serve customers, the effects of higher natural gas prices on uncollectibles and, correspondingly, on cash working capital, are not similarly reconciled.³⁹

As the OTS recognized, this poses a special problem for a Cash Flow company:

[I]f sales were equal to those used to develop base rates and the experienced write-off percentage were unchanged, but gas costs increased above the base rate levels, the Company would be under compensated for uncollectible accounts expense which would negatively affect cash flow. This is due to the fact that the allowance for uncollectible accounts expense would not change from the ratemaking allowance even though revenues would be substantially increased.⁴⁰

As noted, PGW's current base rates contain an allowance for uncollectible expense of just \$55.7 million if calculated based on the Company's last fully litigated base rate proceeding.⁴¹ With historically poor collections rates and gas cost rates in excess of base rate levels, PGW's actual uncollectible expense far exceeds its \$55.7 million quotient by \$15-\$30 million.

Moreover, high wholesale natural gas prices and, correspondingly, high average bills for customers have devastated PGW's collections and, in turn, its cash working capital. The following chart proves that, as PGW's billings have spiraled upward, its receipts as a percentage of these billings have tended to decrease. Correspondingly, in years in which billings have dropped, the percentage of those billings collected by PGW has tended to increase:

³⁸ OTS St. 1 at 11.

³⁹ PGW St. CRRC-1 at 3-4.

⁴⁰ OTS St. 1 at 10.

⁴¹ PGW St. CRRC-1 at 4. PGW settled a base rate proceeding in 2002. The settlement authorized PGW to increase its rates by \$36 million on a "black box" basis, i.e., with no specific items of expense or revenues agreed to in the settlement. Even if that rate increase was considered, PGW's current allowance and base rates for uncollectible expense would be no more than \$58.4 million; Tr. at 422.

Table Four⁴²

Years	Receipts (000)	Billings (000)	Percentages
1997 – 1998	499.9	510.2	97.98%
1998 – 1999	458.0	497.5	92.06%
1999 – 2000	475.1	511.7	92.85%
2000 – 2001	677.4	769.1	88.08%
2001 – 2002	575.3	589.6	97.57%
2002 – 2003	690.3	797.4	86.57%
Average			91.85%
% in base rates			92.38%

This dramatic drop in receipts as a percentage of billings has had a devastating impact on the Company's overall cash working capital, as discussed above.

Mr. Bogdonovage testified that the FY 2003 cash receipts shortfall robbed PGW of some \$40 million in cash working capital.⁴³ If the Company realizes (an improved) 89% rate in FY 2004 it will mean a shortfall of some \$34.3 million.⁴⁴ PGW witness Dr. Peach, a nationally known expert on utility customer payment characteristics with considerable experience with other Pennsylvania utilities,⁴⁵ explained the reasons for the collections difficulties. Dr. Peach conducted a detailed study of PGW residential customer payment patterns, and concluded that PGW's dramatic reduction in collection percentages resulted principally from the combination of very high natural gas bills together with declining real income and increased poverty in the City:

In my opinion, PGW is experiencing these unprecedented levels of uncollectibles as a result of a variety of factors, all related to the persistently high price of natural gas and impact that the high price has on the ability to pay of a very large percentage of PGW customers. Another factor is the continuing decline of the income in the City The situation is exacerbated by the cold weather this winter. The result is that customer bills are increasing because of increased consumption and the rising cost of natural gas at a

⁴² PGW St. CRRC-1, Exh. JRB-1.

⁴³ Tr. 313.

⁴⁴ PGW St. CRRC-1, Exh. JRP-6. Under the CRRC "E-factor" PGW would collect this amount over 3 years.

⁴⁵ PGW St. CRRC-4 (Revised) at 1-2.

time when many customers have increasingly limited ability to pay. . .

Q. HOW HAVE THESE PERSISTENTLY HIGH GAS CHARGES AFFECTED CUSTOMER PAYMENT PATTERNS?

A. They have decimated them. Customers have followed their historic patterns and failed to pay a portion of their now much higher PGW bill. But just as important, the months of very high gas charges have caused them to pay an even smaller amount relative to their total bill.⁴⁶

Dr. Peach further concluded that the recent downturn in collections percentages experienced by the Company has been caused in large part by factors completely outside of PGW's control.⁴⁷ Indeed, while Dr. Peach was hopeful that PGW could stabilize the situation, his overall conclusion, based on observed statistical data, was that collections would remain an issue for the foreseeable future:

Q. FOR BOTH RESIDENTIAL AND SMALL BUSINESS CUSTOMERS, DO YOU HAVE ANY REASON TO EXPECT THAT PGW'S UNCOLLECTIBLE EXPERIENCE WILL IMPROVE DRAMATICALLY IN THE SHORT TERM?

A. I have been informed that PGW is trying to improve its results by increasing and improving collection activity and procedures, as described in the testimony of Mr. Gyory in this proceeding. While I understand that PGW is hopeful that these efforts will produce benefits during the near term, they will take several years to produce dramatic results, if they ever do. The natural gas cost jumps that have caused these decreases in payments didn't happen overnight and even if gas prices return gradually to pre-spike levels it will take many months for customers to see the effects of that mitigation in their retail bills and then pay off any balances accumulated during this period. Nonetheless, it would make sense to permit PGW to track its uncollectible experience in some special mechanism at least until there is consensus that the cost spikes have mitigated for the foreseeable future. . . . The combined forces of increase and real price of gas and [the] decline of real incomes across the board in

⁴⁶ PGW St. CRRC-4 (Revised) at 7-10, 11.

⁴⁷ PGW St. CRRC-4R at 7; Tr. at 405.

the City are strong forces driven by factors outside the City. A special mechanism, such as that proposed by PGW is required to deal with the problem. In my opinion, it will deal with it directly and effectively.⁴⁸

4. PGW and its Owner, the City of Philadelphia, Have Taken All Reasonable Steps to Address its Collections Shortfall

When it realized the depth of its uncollectibles problem, PGW immediately commenced a massive Collections Initiative,⁴⁹ and it and the City took a variety of other steps designed to reduce costs and to increase revenues.⁵⁰ A series of steps designed to allow the Company to hold on by its fingernails were instituted:

a. Grant Back of City Fee and Deferral of City Loan.

The City for the first time agreed to grant back its mandatory \$18 million per year City fee for five years, which would provide the Company with an additional \$90 million over five years. In addition, the City agreed voluntarily to postpone the due date for its \$45 million line of credit for two additional years.⁵¹ These two actions managed to pull PGW from a total cash disaster, pushing its end of year cash – which, as noted, is the traditional measure of the adequacy of PGW’s cash working capital –⁵² to minimally adequate levels, but only when the other “one-time fixes” that PGW was able to arrange are considered.

b. One-time Gas Storage Payment Deferral.

In a further “one time fix” designed to provide assurances that the Company would be able to pay its gas procurement and other bills when due, PGW arranged a “natural gas storage payment deferral” agreement with a counter-party. The transaction essentially permitted PGW to defer the payment for natural gas injected into storage in the fall until the winter months.⁵³

⁴⁸ PGW St. CRRC-4 (Revised) at 23-24.

⁴⁹ PGW St. CRRC-3.

⁵⁰ PGW St. CRRC-5 at 10-12.

⁵¹ PGW St. CRRC-5 at 6, 8; PGW St. CRRC-1R at 3-4.

⁵² PGW St. CRRC-1 at 7.

⁵³ PGW St. CRRC-1R at 3.

This one-time transaction resulted in deferring \$30 million of cash need into the next fiscal year. But, importantly, the arrangement simply transferred the Company's payment obligation from the end of one fiscal year to the middle of the next – producing absolutely no net additional cash or collections.⁵⁴

c. PGW Collections Initiative.

PGW continued and invigorated its efforts to improve collections, even in the face of massively higher gas prices.⁵⁵ Beginning in the summer of 2003, when PGW began to project that its cash receipts were going to fall well below its historical experience, PGW initiated a study of its collections practices to identify a program to reverse the trend, despite the likely negative effects of higher natural gas costs. With the help of Accenture, a nationally known utility collections consultant, PGW completely revised and reinitiated its collections efforts. The study included a review of all of the Company's business processes and metrics, the development of effective work plans and backlog reductions, and the implementation of industry best practices. The specific steps taken as part of the initiative included:

- Review and analyze PGW's current Collections processes, policies and procedures, and technologies.
- Perform collections leading practices Gap Analysis.
- Design, streamline and implement individual programs to improve credit and collections efficiency, and reduce PGW's receivables.
- Develop and assist in implementation of management controls.
- Assign 3, 6, 9 and 12-month recovery goals for individual programs.
- Enhance and provide training to assist the implementation of programs.
- Provide on-going program management consulting for the term of the contract.⁵⁶

In November 2003, PGW launched the new programs and initiatives crafted in consultation with Accenture.⁵⁷

⁵⁴ *Id.* at 2

⁵⁵ *Id.* at 3; Tr. 311-313.

⁵⁶ PGW St. CRRC-3 at 3.

⁵⁷ *Id.*

The results of this massive initiative have been positive. Mr. Bogdanovage testified that as of March 2004, PGW was realizing a 90.46% collections percentage, on a 12 month rolling average basis, and a 7% improvement compared to last year on a month by month basis.⁵⁸ If this improvement continues through the fiscal year, (a considerable achievement considering the level of natural gas prices) PGW's collections experience would be 93%.⁵⁹

d. Cost Saving Efforts.

PGW is evaluating all of its operations, seeking additional cost savings that can be produced without unreasonably affecting PGW's customer service, safety or reliability. But, as PGW has indicated in the past, the Company has only a limited amount of discretionary expenditures that can be reduced or modified in order to produce savings.⁶⁰

e. Offsets to Social Program Costs.

PGW has worked extremely hard in the last 12 months to seek out and develop additional federal and state funding sources to supplement or support the universal service programs now being funded by the Universal Service Charge paid by remaining firm customers.⁶¹ While this effort so far has not produced any supplemental state funding, the Company continues to argue in all fora for concessions that will reduce the subsidy.

5. Despite PGW's Efforts to Increase Collections and Cash Working Capital and to Decrease Costs, PGW's Current Liquidity Has Been Found to be Inadequate to Maintain its Investment Grade Bond Rating.

Even with the various concessions and new cash sources described above, PGW is still far short of the cash position it must attain to ensure its liquidity and to satisfy the bond rating agencies. Mr. Bogdanovage proved as much with a simple math exercise. PGW bills customers in excess of \$800 million per year. The bond rating agencies expect a company of this size to maintain 30 days of average revenue for liquidity purposes in order to be able to retain an

⁵⁸ PGW St. CRRC 1-R at 2.

⁵⁹ *Id.*

⁶⁰ *See*, TEK-5.

⁶¹ PGW St. CRRC-5 at 11-12.

investment grade rating. To meet this requirement, PGW needs fiscal year-end liquidity of \$60 million.⁶²

Despite all efforts, PGW still does not approach the \$60 million target. PGW's Vice President of Finance Joseph Bogdonavage testified that, even when all sources of cash and deferrals are considered, including the one-time, \$30 million gas storage deferral and the City grant-back of the \$18 million payment, PGW shows cash working capital liquidity at the end of FY 2004 of just \$31 to \$36 million,⁶³ still \$24 to \$29 million short of its goal.

But these figures clearly overstate PGW's actual, permanent cash working capital from operations. The \$30 million gas deferral deal is the equivalent of a short-term loan – it merely postpones PGW's financial liability for winter gas injection from fiscal year 2004 to fiscal year 2005 – and serves only as a temporary boost to in-year working capital.⁶⁴ The money must be paid in the next fiscal year, and there is no evidence that this borrowing process will be repeated. If the gas deferral amount of \$30 million is backed out of the financials (because it is one time), and even counting as received the City grant-back of \$18 million, PGW at the end of FY 2004 will have a liquidity balance of only \$6 million – and this figure assumes that PGW can achieve a collection rate of 93%.⁶⁵ If a lower collection rate is assumed – for example its 12 month rolling average as of March 2004 – 90.5%⁶⁶ – then the Company's year end liquidity figure falls from \$6 million to just \$1 million (when the gas storage deferral arrangement is removed)⁶⁷. Clearly, this level is far below the level necessary to sustain its investment grade bond rating.

⁶² PGW St. CRRC 1-R at 4. Additionally, the \$35-40 million end of year cash requirement that PGW established in past cases was at a time when it had a \$100 million short term commercial paper line of credit available. That line has now dropped to \$80 million – meaning that the level of cash it has to produce from rates must be \$20 million greater. Tr. 349, 350-51.

⁶³ *Id.* at 3, 4.

⁶⁴ Tr. 311-13, 348-49.

⁶⁵ Tr. 312. PGW Rejoinder Exh. 1 (JRB).

⁶⁶ Tr. at 364.

⁶⁷ PGW St. CRRC-1R, Exh. JRB-10, pg. 1, Ending Balance-Cash (\$31 million) less effect of the storage deferral (\$30 million).

PGW's opponents in this case seem to suggest that the Company is in fact projecting levels of liquidity for fiscal year end 2004 which are sufficient to obviate the need for the CRRC. This position is obviously and patently false. PGW needs to generate cash working capital for a variety of reasons. The Company must ensure that it can purchase, store and deliver gas to its customers in a safe, adequate and reliable manner. It must also pay down its existing short and long-term debt,⁶⁸ and pay future bond obligations. It must, as well, repay the City Loan and eventually resume its \$18 million payment to the City. In short, PGW has many obligations that it must meet and it plans to meet these obligations. But, in addition, it must sustain a cash reserve to meet unanticipated contingencies.⁶⁹ Finally (and most importantly at the present time), it must have sufficient end-of-year cash to demonstrate to the rating agencies that PGW deserves to keep its investment grade bond rating.⁷⁰

In sum, PGW is at a crossroads. It has vastly improved its collections policies and programs – but even these best efforts are only projected to return PGW to historic collections levels. It has arranged for the City to postpone short-term debt obligations and to grant back the City payment, but even this cash infusion has left PGW with little or no cash working capital on a permanent, sustainable basis. The Company is in the process of arranging a new bond offering, which will be much less costly to ratepayers if PGW maintains its investment grade rating. Now, it seeks the security of the CRRC mechanism to help guarantee cash flow against the uncertainties of volatile gas cost-driven cash receipts shortfalls. The evidence shows that the proposed CRRC is a serious, prudent and responsible approach to assuring that PGW has the cash working capital it needs, both to sustain operations and to satisfy the rating agencies, and therefore, it should be approved.

⁶⁸ These obligations include the \$45 million City line of credit and an \$80 million letter of credit PGW secured through a consortium of banks; both are fully extended. Tr. at 318.

⁶⁹ Tr. at 350-51.

⁷⁰ PGW St. CRRC-5 at 8-9; Tr. at 315-16, 350-51.

B. THE CRRC IS SUPERIOR TO ANY OTHER METHOD OF ADDRESSING PGW'S CASH RECEIPTS ISSUES.

1. The CRRC Mechanism Provides a Targeted Solution to PGW's Real Problem – the Potential for a Debilitating Cash Receipts Shortfall.

The above discussion demonstrates that PGW is in a liquidity crisis that must be addressed to avoid calamitous results. PGW's proposed CRRC mechanism provides one (but not the only) necessary tool to extricate the Company from its precarious position. The key advantage of the CRRC is that it will provide assurances that PGW's cash working capital will at least reflect the Company's historic collections levels. These levels were implicitly reviewed and approved as reasonable in PGW's prior base rate proceedings.⁷¹ If PGW fails to collect at its historic average, the CRRC will be set to charge firm customers an amount to make up the difference. As noted above, PGW's massive Collections Initiative presently appears to be showing success. Even if that success for FY 2004 continues, however, and PGW is able to achieve a collections rate that reflects historic levels, putting in place the CRRC mechanism is nonetheless crucially important to assure the investment community and the rating agencies that PGW's cash working capital levels at least will not fall below historic collection levels. This "backstop," or insurance policy, is vitally important to convince the rating agencies that the Company has been given a reasonable platform or floor from which to attempt to make material cash working capital and collections improvements, as Standard and Poor's has insisted it do to retain its investment-grade rating. Considering the nature of the problem facing the Company and its customers, the CRRC mechanism on balance is the best solution for providing the additional cash working capital support PGW desperately needs.

– The CRRC is self adjusting. The Company's proposed mechanism (described in detail in the next section) is a "make whole" mechanism which self-adjusts based upon PGW's actual collection results. If PGW is able to collect at historic levels (about 93.01% when current rate levels are factored in), the CRRC will be zero and customers will not be charged any additional amount. The CRRC will impose a charge only when the gas costs or other factors

⁷¹ *Pa. PUC v. PGW*, R-00006042 (Oct. 4, 2001); *Petition of Philadelphia Gas Works for Extraordinary Rate Relief Pursuant to 66 Pa. C.S. § 1308(e)*, R-00017034F0002 (April 12, 2002); *Pa. PUC v. PGW*, R-00017034 (August 8, 2002).

result in the Company falling behind its historic levels, and only to the extent necessary to make PGW whole.⁷²

– The CRRC is targeted to the problem. PGW's financial crisis is a cash and liquidity crisis. Because PGW is a cash flow method regulated company its crucial need is to produce sufficient cash from operations to be able to actually pay its bills when they come due. PGW's cash working capital levels are most directly affected by its level of cash receipts (compared to billings). While PGW's uncollectible expense has increased dramatically (from the \$55.7 million level established in PGW's rates in 2001 to \$85 million in 2003, and \$70 million projected for FY 2004), indisputably harming PGW's financial results this has an indirect effect on cash working capital, directly reducing net income and bond overages. But falling cash receipts levels directly affect PGW's cash working capital.⁷³ The CRRC targets the latter.

– The CRRC mechanism mirrors the way in which PGW recovers natural gas cost increases, the principal cause of the Company's current crisis. The CRRC would raise rates temporarily and only in those situations where PGW is unable to improve its collections to minimally acceptable levels. Because high customer bills, and the greater incidence of non-payment of those bills, are driven in substantial part by higher gas costs, the CRRC is particularly suited to a Section 1307(f) type mechanism, which provides for flexible adjustments (including flexible relief) to rates based on circumstances existing at the time. In other words, customers face no permanent rate increases, and the Commission and the utility face no constant need for burdensome base rates proceedings to attempt to deal with the related, volatile gas cost and uncollectibles issues.

The CRRC will give PGW significant incentive to improve collections above historic levels. Under the CRRC as proposed, if PGW is able to exceed its historic collection levels, it will retain the additional cash working capital. This is vitally important in light of the directives of the rating agencies to produce a material increase in collections and cash working capital over and above its historic levels.⁷⁴ By structuring the clause so it can meet these goals, PGW will

⁷² Tr. at 397-98.

⁷³ PGW St. CRRC-1 at 11; 1R at 11-12.

⁷⁴ PGW St. CRRC-5 at 17-18; Tr. at 354.

have enormous incentives to exceed its historic performance. Of course, any additional cash working capital amounts will ultimately benefit customers.

– The CRRC is far superior to increasing PGW’s cash working capital by a permanent base rate increase. A major reason that PGW proposed the CRRC was to seek to avoid having to permanently increase base rates – it is that simple. PGW’s overall rates are already the highest among Pennsylvania utilities. There is no dispute that all parties need to work to avoid additional rate increases to the greatest extent possible, and PGW is committed to trying to do so.⁷⁵ As explained above, the CRRC will only result in an additional increase if all of the Company’s efforts to increase collections and cash working capital are not sufficiently successful.

In contrast, the evidence shows that, if PGW is forced to file a base rate case, its claim will be far more onerous than the potential increase posed by the CRRC. PGW witness Bogdonavage testified that, presently, if forced to file a costly and difficult base rate case, the Company’s claim would be on the order of \$74 to \$94 million.⁷⁶ Once approved, the increase would go into effect and remain in effect until there is another base rates proceeding, irrespective of possible improvements in collections, cash flow, uncollectibles or in other aspects of the company’s business. In short, PGW’s ratepayers would be on the hook for high rates established in a difficult economic setting without the possibility of automatic adjustment to better rates as uncollectibles pressures eased. Perhaps Mr. Bogdonavage said it best:

It makes little sense to drag in every aspect of a company’s finances and operations in a full base rates case simply to address an easily identified and rectified uncollectibles variable.⁷⁷

Moreover, the base rate option simply will not meet the Company’s need to have in place tools to respond to its cash crisis by this fall at the latest in order to stave off a downgrade to junk

⁷⁵ Tr. at 357.

⁷⁶ Statement No. CRRC-1R at 5. With gas costs at historical highs, uncollectible accounts expense also has been at historical highs. A base rates case could establish a large, non-adjustable uncollectibles allowance that could maintain rates at unrealistic and irreversible levels even if gas costs were to decrease. Also, PGW is seeking federal LIHEAP funding of \$10 to \$15 million. If this funding materializes, the CRRC would be adjusted, whereas if base rates were adjusted, customers would not see any benefit. Tr. at 357.

⁷⁷ *Id.* at 6.

status.⁷⁸ A general rate case – or even an emergency rate increase request as part of a general rate case⁷⁹ – simply cannot provide the necessary response in the available timeframe.

2. The Precise Mechanics of the CRRC Demonstrate its Inherent Superiority to Base Rates Proceedings and its Ease of Administration.

The elegance of the CRRC solution to PGW’s cash receipts/cash working capital shortfall lies in its very simplicity. The clause would operate much in the same manner as the section 1307(f) gas cost adjustment mechanism (although it would be authorized under section 1307(a) of that section), and would be established each year at the same time as the GCR. Importantly, the CRRC is a *mechanism* – it is not a fund or a figure in and of itself.⁸⁰ Rather, it is a mechanism that uses a simple calculation to determine whether there is a recoverable revenue shortfall.

The CRRC mechanism has two parts, a pro forma calculation and an E-factor. For the pro forma calculation, each year during the GCR proceedings, PGW will establish a cash receipts factor for the coming fiscal year. The factor initially will be set equal to the projected actual cash receipts percentage for that fiscal year. For instance, if FY 2005 cash receipts was projected to be 90% of billings, the cash receipts factor will initially be set at 10%. The Company will then multiply projected gas billings times the cash receipts factor to determine the expected cash shortfall. If projected gas billings are \$826 million, then the projected cash receipts would be \$826 million x 90%, or \$743.4 million. The projected shortfall is, therefore, \$826 million minus \$743.4 million, or \$82.6 million. The \$82.6 million is then compared to the \$55.7 million uncollectible accounts expense allowance that the Commission established for PGW in the last fully litigated base rates case. To the extent the projected shortfall exceeds the uncollectible expense allowance, PGW will recover that amount via the CRRC mechanism in the coming fiscal year. In the example above, the amount of the CRRC would be \$82.6 minus \$55.7, or

⁷⁸ PGW St. CRRC-5 at 17-18.

⁷⁹ The Public Utility Code permits a Company to file for emergency rate relief but only within the context of a general rate increase request. 66 Pa. C.S. § 1308(e). Considering the standards, the Company would have to show that, absent an immediate base rate increase the Company would start on the road to a complete disruption of normal operations. If the Commission grants PGW’s requests for a CRRC and Chapter 56 waiver it will avoid this brink of disaster.

⁸⁰ *Id.*

\$26.9 million.⁸¹ This amount would then be collected by translating it into a “per Mcf” figure, using total firm sales as the divisor.⁸²

Once the projection is reviewed and approved in the Section 1307(f) proceeding, PGW would update its projections on September 1, to reflect the actual cash receipts and billing information available at that time, just as it does for its GCR.⁸³ Again, the actual cash receipts percentage experienced in the historical fiscal year (for example, FY 2004, September 1, 2003 to August 31, 2004) will be used to establish the projected cash receipts percentage and, in turn, the CRRC for the subsequent fiscal year (e.g., FY 2005, the 12 months ending August 31, 2005).

As noted, if PGW is successful in collections and improves to (or above) historic levels, the CRRC will not impose any additional charge. Again using the above example, and assuming a 94% cash receipts rate instead of 90%, the projected shortfall would be *zero*, and the CRRC for the coming fiscal year would be set at *zero*.⁸⁴ The math works as follows: \$826 million in projected gas billings x 94% equals \$776.4 in projected gas receipts, resulting in a shortfall of \$49.6 million (\$826 - \$776.4). Since the \$49.6 million shortfall is less than the \$55.7 million allowance for uncollectibles expense, there is no recovery under the CRRC.⁸⁵

In fact, PGW believes that its recent collections efforts could cause it to finish the FY 2004 with a 91% collections rate, which would result in a pro forma CRRC of approximately \$18 million to be recovered in fiscal year 2005.⁸⁶ However, if PGW continues its current

⁸¹ PGW St. CRRC-1 at 11-12; Exh. JRB-6.

⁸² *Id.*

⁸³ *Id.* at 12.

⁸⁴ Tr. at 397-98.

⁸⁵ Importantly, PGW is not proposing to credit customers if its cash receipts amount exceeds the target amount. As with current legal requirements that allow it to retain the difference between actual and allowed uncollectibles expense, PGW would retain the difference between its uncollectibles allowance and its total receipts compared to billings and add this amount to cash working capital. This cash would be used to help retire short and long term debt and otherwise aid in meeting operating expenses.

⁸⁶ PGW St. CRRC-1R at 3.

performance, it could finish the 2004 fiscal year with collections of 93% or better, which would result in a CRRC of zero.⁸⁷

Second, the E-factor works in much the same manner as the pro forma calculation. PGW would determine its actual cash undercollection for FY 2004 and compare this figure to its uncollectibles allowance of \$55.7 million. If PGW finishes 2004 with a 93.01% collections rate, there would be no undercollection and the E-factor would be set at zero.⁸⁸ If PGW finishes FY 2004 with a shortfall, then this amount will be amortized and collected in rates over the ensuing three years. The CRRC pro forma and E-factor processes would be repeated at the end of each fiscal year during the life of the clause.⁸⁹ Additional detailed calculations and explanations of how the CRRC will work are set out in Mr. Bogdonavage's testimony.⁹⁰

C. PGW's CRRC Is Well Supported By Authority In The Public Utility Code And Consistent With Prior Commission Action.

1. Introduction.

PGW's request is well supported by the general legal authority in the Public Utility Code, and also by the special authority the PUC has been granted in Section 2212. The Public Utility Code, Section 1307(a), authorizes the PUC to establish a "sliding scale of rates or other method for the automatic adjustment of the rates of the public utility"⁹¹ PGW's CRRC plainly satisfies this statutory requirement. While there are provisions of Section 1307(a) which clearly are not applicable to PGW because of its unique regulatory scheme,⁹² the Commission has the authority to waive such requirements.

⁸⁷ Tr. at 364; Exhibit KSD-2; Tr. at 397.

⁸⁸ Tr. at 397.

⁸⁹ PGW St. CRRC-1 at 12.

⁹⁰ PGW Sts. CRRC-1 and CRRC-1R.

⁹¹ 66 Pa. C. S. § 1307(a).

⁹² Section 1307(a) states that the rates established as part of a "sliding scale" "shall provide a just and reasonable return on the rate base of such public utility. . . ." This provision is not applicable to PGW, and the Commission should waive its application pursuant to 66 Pa. C. S. § 2212(c). Indeed, the Commission did just that in the Company's 2002 extraordinary rate proceeding, finding similar language in Section

Moreover, while PGW's CRRC request is consistent generally with Section 1307(a), if the Commission determines that it does not have the authority to implement all or some aspect of PGW's request, the PUC has been given the authority, upon request by PGW, to alter or revise any aspect of the Public Utility Code (or regulations established pursuant thereto) to customize the regulatory approach to accommodate the special and unique issues and problems raised by PUC regulation of PGW.

Section 2212(c) states in part as follows:

Applicability of other chapters. – Commencing July 1, 2000, to the extent not inconsistent with this section, the provisions of this title, [with certain exceptions not applicable here] shall apply to the public utility service of a city natural gas distribution operation with the same force as if [PGW] was a public utility under section 102 (relating to definitions), provided that, upon request of [PGW] the commission may suspend or waive the application to [PGW] of any provision of this title, including any provision of this chapter other than this section.⁹³

Significantly, the PUC has already utilized its authority to modify or waive standard practices and requirements to permit the automatic adjustment of PGW's uncollectible expense to account for natural gas cost increases. In 2001, the PUC resolved issues associated with PGW's initial rate request before the PUC by approving a settlement which provided in part that "PGW would be permitted to recover \$7 million through its GCR, compressed so as to be collected by August 31, 2001, to account for the additional bad debt expense produced by dramatically higher than projected natural gas costs incurred by PGW."⁹⁴ If ever there was a situation which again justified modifying the legal requirements to establish the best solution for the Company, its employees and its customers, this is it.

1308(e) to be inapplicable to PGW. *Petition of Philadelphia Gas Works for Extraordinary Rate Relief Pursuant to 66 Pa. C.S. § 1308(e)*, R-00017034F0002 (April 12, 2002) Opinion and Order at 18-19.

⁹³ 66 Pa C.S. § 2212(c) (emphasis added).

⁹⁴ *Pa. PUC v. Philadelphia Gas Works*, R-00005654, R-00005619, (Feb. 22, 2001) Order at 4; Tr. at 322.

2. Pennsylvania Law Recognizes the Appropriateness of Automatic Adjustment Clauses to Reflect Changes in Customer Charges of Specific Rate Components.

PGW's requested automatic adjustment clause to recover a special shortfall in cost of service recovery is not at all unusual; many companies have asked for and received authority to recover unanticipated costs via this type of mechanism. Section 1307 affords utilities and the Commission the flexibility to address cost recovery for appropriate expenses via an automatic adjustment clause. The law only requires that resulting rates be just and reasonable. Consistent with its view that the scope of Section 1307's cost recovery is "broad," the Commission historically has "authorized the use of Section 1307(a) automatic adjustment clauses to recover a wide array of expenses, depreciation and capital costs."⁹⁵ Similarly the Commission has also authorized "E-factors," provisions in automatic adjustment mechanisms to account for over or under recoveries in the prior year.

The Commission has approved automatic adjustment clauses for several categories of costs involving all types of utilities. For the electric industry, the Commission has approved clauses involving demand-side management and coal uprating costs. For water utilities, the Commission has approved adjustment clauses involving principal and interest due on PennVEST obligations and distribution system improvements. For natural gas utilities, the Commission has approved clauses involving take or pay costs to pipeline suppliers, costs resulting from Federal Energy Regulatory Commission Order 636, and gas choice customer education initiative costs. Automatic adjustment clauses have also generally been authorized for incremental changes in state taxes and for utilities facing Clean Air Act compliance costs.⁹⁶

Moreover, the Commission has granted requests for Section 1307(a) treatment for utility-specific costs. Such awards have included Philadelphia Electric Company's costs to convert oil-fired units to units that burn natural gas; Philadelphia Thermal Energy Corporation's water and

⁹⁵ *Petition of Pennsylvania-American Water Company for Approval to Implement a Tariff Supplement Establishing a Distribution System Improvement Charge*, 1996 Pa. PUC LEXIS 182, **5, 12-13 (citing *National Fuel Gas Distribution Corp. v. Pa. P.U.C.*, 473 A.2d 1109, 1121 (Pa. Cmwlth. 1984)).

⁹⁶ *Id.* at **5-6, 12; *Creation and Implementation of a Statewide Consumer Education Program for Natural Gas Competition*, 2000 Pa. PUC LEXIS 12, **38-39; *Policy Statement on Clean Air Act Emissions Allowances*, 1993 Pa. PUC LEXIS 2, **7, 17.

sewer costs; and Jackson Sewer Corporation's costs for sewage treatment services provided by a municipal authority.⁹⁷

As these many examples suggest, and as the Commonwealth Court has confirmed, the question of whether to allow the recovery of a particular cost item via an automatic adjustment clause is a matter of sound Commission discretion.⁹⁸ Informing the exercise of that discretion is the recognized purpose behind Section 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 of the broad, costly and time-consuming inquiry required in the case of rate increases generally."⁹⁹ Despite the focus on "one component" of a utility's expenses, and contrary to the positions of the OCA and OSBA in this matter, the doctrine of single-issue ratemaking is inapplicable to automatic adjustment mechanisms authorized under Section 1307.¹⁰⁰

Significantly, Section 1307(a) contains no artificial limitation as to the costs over which the Commission may exercise its discretion. As the Commission has held, Section 1307(a) "has no cost category limitation in its language."¹⁰¹ Rather, as reflected by the Commonwealth Court, the statutory concern is directed more at the procedural aspects of the clause:

[T]he General Assembly did not limit the allowance of automatic adjustment to only fuel costs and taxes which are generally beyond the control of the utility. Instead, the General Assembly specifically allowed the recovery of fuel costs and also allowed the

⁹⁷ *Petition of Pennsylvania-American Water Company*, 1996 Pa. PUC LEXIS 182, *12; *Pa. PUC v. Philadelphia Thermal Energy Corp.*, 1991 Pa. PUC LEXIS 80; *Pa. PUC et al. v. Jackson Sewer Corp.*, 2001 Pa. PUC LEXIS 53, **55-57, 63-64.

⁹⁸ *Petition of Pennsylvania-American Water Company*, 1996 Pa. PUC LEXIS 182, *14 (citing *Pennsylvania Industrial Energy Coalition ("PIEC") v. Pa. PUC*, 653 A.2d 1336, 1349 (Pa. Cmwlth. 1995)).

⁹⁹ *National Fuel Gas Distribution Corp.*, 473 A.2d at 1121; see *Petition of Pennsylvania-American Water Company*, 1996 Pa. PUC LEXIS 182, *13.

¹⁰⁰ *PIEC*, 653 A.2d at 1350.

¹⁰¹ *Petition of Pennsylvania-American Water Company*, 1996 Pa. PUC LEXIS 182, *15.

PUC or the utilities to initiate the automatic adjustment of costs within specific procedures.¹⁰²

These procedural aspects of the adjustment mechanism are intended to ensure that the clause does not “disassemble the traditional ratemaking process.”¹⁰³ To the extent that guidelines have been established for the eligibility of expenses for Section 1307 treatment, the Commission has noted in a non-restrictive fashion that “questions of significance, volatility and control have been used as criteria for the inclusion of items into an automatic adjustment clause.”¹⁰⁴

3. PGW’s Proposal Satisfies All of the Elements Required for Section 1307(a) Treatment.

Certainly, PGW’s proposed CRRC adjustment clause is consistent with Section 1307(a) and the purpose behind it. The clause enables the Company to reflect changes in its cash receipts, resulting from a collections shortfall driven by volatile and significant natural gas costs and exacerbated by the demographics of its customer base, without the need for “the broad, costly and time-consuming inquiry” required under Section 1308 base rate cases.¹⁰⁵ Further, the resulting rate from the CRRC is plainly just and reasonable, as it merely enables the Company to collect previously sanctioned rates at PUC-endorsed collections levels. Those prior determinations were, themselves, just and reasonable.

Likewise, the record reflects that PGW’s cash receipts and collections levels satisfy the Commission’s loose criteria for automatic rate treatment in that they are significant, volatile and beyond the Company’s ability to control.¹⁰⁶ As the testimony reflects, the Company’s

¹⁰² *PIEC*, 653 A.2d at 1349; see *Petition of Pennsylvania-American Water Company*, 1996 Pa. PUC LEXIS 182, **16-17 (focusing on the PUC’s auditing powers and Sec. 1307(e)’s mandatory annual reconciliations).

¹⁰³ *Id.*

¹⁰⁴ *Pa. PUC v. Philadelphia Thermal Energy Corp.*, 1991 Pa. PUC LEXIS 80,*2. Clearly, these criteria are not absolutes. For example, the Commission authorized the recovery of gas choice customer education costs via an automatic adjustment mechanism. Such costs are marginally significant compared to a utility’s overall costs, not at all volatile, and controlled by the utilities. Nonetheless, the Commission approved Sec. 1307(a) recovery treatment. *Creation and Implementation of a Statewide Consumer Education Program for Natural Gas Competition*, 2000 Pa. PUC LEXIS 12. The cash receipts shortfalls proposed to be recovered here, however, are extremely significant, as explained above.

¹⁰⁵ *National Fuel Gas Distribution Corp.*, 473 A.2d at 1121.

¹⁰⁶ See discussion *supra.*, section III (A).

collections shortfall and concomitant cash receipts crisis is primarily driven by dramatically heightened and volatile natural gas costs.¹⁰⁷ Finally, despite the exaggerated claims of the OCA and OSBA, even if PGW was 150% successful in implementing its collections initiative, the parties must acknowledge that such improvements stop far short of “control” over its cash receipts levels. In addition to the volatility of natural gas costs, weather and the customer demographics, income and poverty levels of PGW’s service territory are clearly beyond the Company’s ability to influence or alter.¹⁰⁸

Nor would simply allowing PGW to attain its historic collections percentage on each dollar billed undermine in any way the ratemaking process or enable PGW to achieve “any long-term evasion of a base rate review.”¹⁰⁹ The Company’s proposal is designed to merely enable it to realize its previously authorized revenue requirement. The clause serves as a “make whole” mechanism, and will not account for future, or even present, increases in costs of service generally.

Indeed, PGW’s CRRC proposal is similar to an automatic adjustment mechanism approved by the Commission in *Pennsylvania Public Utility Comm’n, et al. v. Jackson Sewer Corporation*.¹¹⁰ In that proceeding, Jackson Sewer Corporation (“JSC”) requested the implementation of a sewer treatment surcharge adjustment clause to enable it to recover treatment costs incurred by JSC on behalf of its customers for the treatment of sewage by the Jackson Township Sewer Authority.¹¹¹ The Commission approved the automatic adjustment clause, over the protest of the OCA, in part due to the fact that the recommended alternatives

¹⁰⁷ See, section III(A)(3) to this brief, *supra*.

¹⁰⁸ See, PGW St. CRRC-4; CRRC-5 at 16 (69% of PGW’s arrearage at April 1 was associated with customers with family incomes \$30,000 and below); Tr. 405-06 (PGW doing all it can under existing rules, to collect arrearages).

¹⁰⁹ *Petition of Pennsylvania-American Water Company*, 1996 Pa. PUC LEXIS 182, *16.

¹¹⁰ 2001 Pa. PUC LEXIS 53.

¹¹¹ *Id.* at **3-6.

placed the risk of a shortfall in the recovery of the company's costs, *due to customers not paying their bills* or going off the system, on JSC.¹¹²

Here, PGW, like JSC, is facing a significant shortfall in the recovery of its costs of serving its customers, and thereby its cash receipts, due to those customers not paying their bills. As the Commission declared with respect to JSC, “[W]hile the Commission must protect the ‘public interest,’ it also has a responsibility to treat utilities that it regulates fairly. Fairness dictates that JSC should be allowed to recover these uncompensated costs.”¹¹³ PGW deserves no less. The Company has incurred significant costs in order to serve the citizens of Philadelphia and ensure that they have heat to warm their homes in winter, gas to cook their food, and hot water. Refusing to permit the Company to collect at reasonable and historic levels the actual charges it bills, for costs incurred to serve its customers, which it does not recover from those ratepayers due to the circumstances present here, is certainly inconsistent with the Commission’s obligation of fairness.

4. PGW’s E-factor is also justified, and does not constitute retroactive ratemaking.

Similarly, PGW’s request that the CRRC include an E-factor to recover its cash receipts shortfall in FY 2004 (the present fiscal year) is also authorized by section 1307. Section 1307(e) specifically authorizes the Commission, after a 12 month period covered by an automatic adjustment clause, to permit the utility to “recover” an amount equal to that by which such expense or class if expense exceeded the revenue received pursuant to such an automatic adjustment clause.”¹¹⁴

Several parties have also erroneously asserted that this aspect of the Company’s proposal, as applied to the current fiscal year’s cash receipts shortfall, constitutes retroactive ratemaking. To the contrary, Pennsylvania authority clearly permits utilities to recover extraordinary

¹¹² *Id.* at *55-56.

¹¹³ *Id.* at 63.

¹¹⁴ 66 Pa C.S. § 1307(e). The section also indicates that, absent good cause shown to the contrary, a utility should also refund to ratepayers any over-recovery. *Id.* As explained, PGW believes that “good cause” exists to allow the clause to only be reconciled for under recovery. The PUC may also waive this clause pursuant to Section 2212(c).

uncollectible accounts expenses that exceed levels otherwise established in base rates. Although increases in normal uncollectible expenses above those established in base rates is typically disallowed, Pennsylvania law protects utilities that seek timely relief from extraordinary uncollectible accounts expenses.¹¹⁵

Columbia Gas of Pennsylvania, Inc. v. Pennsylvania Public Utility Commission is directly relevant. There, the gas utility sought amortized recovery for a \$4.5 million uncollectible accounts arrearage that had accumulated over a period of years and exceeded its allowance established in base rates. The additional expense was attributed to rules limiting collections and disconnections, which drove up uncollectibles expenses. OCA and OTS objected to the claim on the basis that it would constitute retroactive ratemaking, and the Commission agreed as to past expenses.

Commonwealth Court reversed the Commission and ordered it to allow the utility's full claim, including amortization of amounts for past arrearages. The Court noted the general prohibition against retroactive ratemaking, but decided that the circumstances that led to the increased arrearage, and the utility's diligence in pursuing these expenses, were sufficient to carry the utility's claim within the extraordinary expense exception to the rule.¹¹⁶

Popowsky v. Pennsylvania Public Utility Commission is also on point.¹¹⁷ There, the Court upheld a Commission decision permitting a utility to amortize past expenses associated with an accounting rule change relating to retirement benefits. As to retroactive ratemaking, the

¹¹⁵ *Columbia Gas of Pennsylvania, Inc. v. Pennsylvania Public Utility Commission*, 613 A.2d 74 (Pa. Cmwlth. 1992), *aff'd per curiam* 636 A.2d 627 (1994)(gas utility permitted to recover arrearages of slow-paying customers); *Popowsky v. Pennsylvania Public Utilities Commission*, 695 A.2d 448 (Pa. Cmwlth. 1997), *appeal den.* 702 A.2d 1062 (1997)(electric utility permitted to recover past expenses attributable to changes in retirement plan accounting rules); *OCA v. The Peoples Natural Gas Company*, 2003 Pa. PUC LEXIS 53 (undercollections relating to Sec. 1307 gas cost expenses, though caused by math errors, are recoverable as amortized expenses); *Pennsylvania Public Utilities Commission et al. v. Consumers Pennsylvania Water Company*, 1997 Pa. PUC LEXIS 141(water utility may amortize extraordinary uncollectible accounts expenses associated with customer bankruptcies).

¹¹⁶ As the Court explained: "The money Columbia seeks to recover now as an expense definitely became owing in the past; however, under the peculiar circumstances of this case, the present rate proceeding is the first time that Columbia had an opportunity or a reason to seek recovery of that money in rates. We reverse the Commission's denial of recovery of the full \$4.5 million." *Columbia Gas* at 84.

¹¹⁷ 695 A.2d 448 (Pa. Cmwlth. 1997).

Court initially noted that a utility's relative success or failure accurately to predict its revenues or expenses would not be cause for a refund or a recovery – that would constitute retroactive ratemaking. But, the Court recognized an exception to this rule where the unanticipated expenses, though historic, are extraordinary and non-recurring.¹¹⁸ In those circumstances, the Commission is explicitly authorized to take into account a utility's past extraordinary losses or gains by amortizing them over a period of years without offending the rule against retroactive ratemaking.¹¹⁹

This Commission has followed and applied the teachings of *Columbia Gas* and *Popowsky* in the recent matters of *Office of Consumer Advocate v. The Peoples Natural Gas Company*¹²⁰ and *Jackson Sewer Corporation, supra*. For instance, in *Jackson Sewer*, the Commission flatly rejected the OCA's claim that use of the new automatic adjustment clause to recover treatment costs incurred in the months previous to the surcharge's enactment constituted retroactive ratemaking.¹²¹ The Commission, noting that the prohibition against retroactive ratemaking was intended only to prevent the recalculation of rates to recover surpluses or refund deficits resulting from inaccuracies in prior rate decisions, explained: "JSC's inability to collect the actual charges billed by the Authority, but not recovered from ratepayers, is not a result of either the Company or the Commission seeking to revisit a prior rate authorization."¹²²

PGW's request to recover current extraordinary uncollectibles expense through an E-factor likewise is perfectly consistent with Pennsylvania law, and in fact presents a stronger case for recovery than other approved requests outlined in the published decisions. PGW's cash receipts and cash working capital shortfall – it amounted to \$40 million in FY 2003 and could be \$20-30 million this year – is clearly extraordinary – and is driven in large part by the fact that

¹¹⁸ *Popowsky* at 450 (citing *Philadelphia Electric Company v. Pennsylvania Public Utility Commission*, 502 A.2d 722 (Pa. Cmwlth. 1985)).

¹¹⁹ *Id.* at 452, (citing *Pike County Light and Power Company v. Pennsylvania Public Utility Commission*, 487 A.2d 118 (Pa. Cmwlth. 1985)).

¹²⁰ 2003 Pa. LEXIS 53.

¹²¹ *Id.* at **63-64.

¹²² *Id.* at 64.

PGW's current gas costs are at levels greatly in excess of those established in its base rates.¹²³ PGW seeks recovery only for current fiscal year 2004 shortfall (to be quantified on August 31, 2004) in the E-factor, with those expenses to be amortized over a three year period beginning in fiscal year 2005 (September 1, 2004 through August 31, 2005). The FY 2004 cash receipts shortfall will be fixed and determined as of August 31 of this year. The 2004 shortfall will not recur in future years.¹²⁴

PGW's current undercollections therefore differ favorably from those approved for payment in the *Columbia Gas*, *Popowski* and *OCA* decisions, yet also enjoy similarities with those approved expenses that compel equal treatment in this case. Each of those decisions involved expenses that the utility had incurred for periods of years prior to seeking relief, but relief was granted nonetheless; PGW's claim is for the current fiscal year.¹²⁵ Similar to the utility in *Columbia Gas*, PGW's claim involves extraordinary cash receipts shortfalls attributed to additional unpaid bills. Similar to the utility in *OCA*, PGW's claim involves undercollections directly related to the gas cost rate and involves a Section 1307(f) proceeding. Similar to all three utilities (and *Pennsylvania Water Company*), PGW addressed its problem with the Commission promptly at the first practicable opportunity. It chose to assert its rights, not to sleep on them.

In short, PGW's claim seeking current cash receipts shortfall amortized over the next three years fits comfortably within the exception to the retroactive ratemaking prohibition. The PUC should grant PGW's request as equitable, appropriate, just and reasonable.

¹²³ OTS notes that PGW currently undercollects on its receivables because its current (and expected fiscal year 2005) gas costs are in excess of the gas cost rate used in the base rate case in part to establish the uncollectible accounts expense allowance. See OTS St. 1 at 10; Tr. at 416-420.

¹²⁴ Tr. at 351.

¹²⁵ Fiscal Year 2004 began on September 1, 2003 and concludes on August 31, 2004.

D. SUBSTANTIAL LEGAL PRECEDENT FROM OTHER JURISDICTIONS SUPPORTS RECOVERY OF UNCOLLECTIBLE ACCOUNTS EXPENSE THROUGH A FLEXIBLE AUTOMATIC ADJUSTMENT MECHANISM

1. Introduction

PGW's request for an automatic recovery mechanism is not at all unique. There is additional clear and substantial legal precedent that favors PGW's requested relief mechanism. Other jurisdictions, most notably Ohio, have considered and adopted identical or nearly identical adjustment clauses protecting utilities from rising and substantial gas cost-driven uncollectible expense, or otherwise have provided for recovery of expenses in excess of allotted base rate levels.¹²⁶ Commissions around the country are responding responsibly to the issues created by rising natural gas costs. This Commission should follow suit.

The situation presented in the *East Ohio Gas Co.* case closely mirrors PGW's experience, and the commission decision is particularly on point. In May 2003, several gas companies¹²⁷ petitioned the Ohio Commission for approval of an automatic adjustment mechanism to recover uncollectible expenses associated with rising, volatile gas costs and colder than normal weather. The companies contended that the gas costs and weather were beyond their control, and that they were justified in seeking to recover the resulting higher than normal uncollectibles expenses through an automatic adjustment clause. Despite strenuous objections by the Office of Consumer Counsel and several other parties, the Ohio Commission granted the requested relief. In deciding the need for the clause, the commission quite correctly reasoned:

The fundamental question before us is whether the proposed adjustment mechanism is just and reasonable. We accept the applicants' rationale supporting the proposed adjustment mechanism. There is no doubt gas costs have been volatile during the last several years. We recognize that those gas costs and the weather impact the dollar amounts of customer bills. Additionally, we are aware that gas companies across Ohio, including the

¹²⁶ See, e.g., *In the Matter of the Joint Application of The East Ohio Gas Co. et al.*, No. 03-1127-GA-UNC (OH, 2003); *Petition of Chattanooga Gas Co. et al.*, No. 03-00209 (TN, 2004); *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).

¹²⁷ The petitioning companies included The East Ohio Gas Company, d/b/a Dominion East Ohio; Vectren Energy Delivery of Ohio; Northeast Ohio Natural Gas Corp.; and Oxford Natural Gas Company.

applicants, have experienced difficulty in recovering their bills in full. We are not assigning blame or exculpating anyone for the large uncollectibles they have recently experienced. We agree that weather is not within the applicants' control. We also believe that gas costs are largely outside the applicants' control. . . . We further agree that that the weather and gas costs can substantially impact the dollar amounts of customer bills.¹²⁸

Additionally, the commission noted the inequity in holding gas companies to uncollectible expense allowances determined in times of less volatile gas costs, and acknowledged the reasonableness of the utilities' requested relief:

Yet, when extreme volatility exists, an expense recovery mechanism that moves with the volatility to allow more contemporaneous recovery of expenses or costs is an understandable business approach. In this respect, we disagree with the consumer commenters who claim that the uncollectible proposal is an improper shifting of the risk of volatile gas costs onto consumers.¹²⁹ *Id.* at 11.

The Ohio Commission also analyzed the similarity of the requested uncollectibles clause to other automatic expense recovery mechanisms already in place in the state, concluding:

Moreover, the concept of this proposed adjustment mechanism is not really unique. After all, the applicants' gas costs are recovered through the GCR mechanism, which adjusts based on actual gas cost expenses. Similarly, many gas companies in Ohio recover funds for their gross receipts tax through a distinguishable rider, separate from their base rates. This separation has been approved by the Commission as reasonable. . . . We do not believe that what has been proposed in this application is conceptually different from these other fluctuating recovery mechanisms.¹³⁰

In addition to approving the automatic uncollectibles clause for future expenses, the Ohio Commission also extended recovery to companies with deferred accounts receivable balances,

¹²⁸ *East Ohio Gas Co.* at 10, 11.

¹²⁹ *Id.* at 14.

¹³⁰ *Id.* at 11, 12.

permitting those companies to recover past expenses through a five year amortization program.¹³¹

The Tennessee Commission likewise recently adopted flexible rule changes concerning uncollectible expense, specifically allowing utilities to recover uncollectible expenses in excess of those allowed in their last base rate proceedings.¹³² Like Pennsylvania and Ohio, Tennessee rules permit automatic adjustment of utility bills to account for changes in gas cost expenses. Noting that the rule was designed to permit utilities to recover all of their gas costs, including uncollectible expenses, the Tennessee Commission held that a utility should be able to rely on some degree of revenue continuity in order to provide customers with the same quality of services regardless of the volatility of gas costs or related bad debt.¹³³ The commission noted carefully the circumstances that gave rise to the need for the adjustment clause: harsh, colder than normal weather; dramatic and significantly higher gas costs; and uncollectible expenses far in excess of permitted/tariffed levels.¹³⁴ These same ills have afflicted PGW.

Other commissions, such as those in Virginia and Georgia, have also employed similarly nuanced approaches to the special problems utilities face with rising gas costs, colder than normal weather, and associated rises in customer bills and uncollectible expenses.¹³⁵ Clearly, PGW is not asking this Commission to enter uncharted waters.

E. The OSBA, OCA And OTS Criticisms Of The CRRC Have No Basis In Reality And Ought To Be Rejected.

¹³¹ *Id.* at 13.

¹³² PGW currently has only a transcript of the Tennessee Commission's ruling, and awaits a copy of the written order when it is available.

¹³³ Tr. at 5.

¹³⁴ Tr. at 6. The Tennessee Commission addressed only prospective recovery of expenses, and apparently will approve a rule that also permits for some type of downward adjustment, although the precise mechanism is not apparent from the transcript. Tr. at 14.

¹³⁵ *Petitions of United Cities Gas Co., Atmos Energy Co. and Roanoke Gas Co., supra.* The Virginia and Georgia Commissions decided to cap the initial uncollectibles levels subject to amortization because this approach was new to the states' regulatory scheme, which traditionally relied on base rates.

The OSBA, OCA and OTS all complain, to varying degrees, that the CRRC is flawed and therefore ought to be rejected. Neither the OSBA nor OCA offers any alternative to the CRRC; both state that any issue of cash receipts and cash working capital shortfall, no matter how targeted, ought to be addressed solely within the context of a major base rates case. OTS recognizes the need for a CRRC-like mechanism, yet fails fully to embrace the more comprehensive solution that PGW proposes. The principal criticisms that OSBA, OCA and OTS level against the CRRC, and a thorough refutation of each of them is set forth below.

1. OSBA

Criticism 1: The CRRC is unprecedented and is merely a ploy to avoid a base rates case; it would insulate PGW from a detailed scrutiny of all of its costs and operations.

Response: The CRRC is actually a flexible mechanism targeted to address a recent and extraordinary phenomenon: the sharp drop in cash receipts and the rise in uncollectibles and drop in cash receipts attributable to very high customer bills, which reflect large increases in gas cost rates due to supply volatility and colder than normal weather. As just discussed, there is ample authority in Pennsylvania law and persuasive precedent for CRRC-like mechanisms.¹³⁶ The commissions in Ohio and Tennessee have recently established flexible, automatic adjustment mechanisms for uncollectibles expense that will track gas cost-driven customer rate increases.¹³⁷ These clauses allow affected utilities to recover uncollectibles expenses in excess of the amounts allotted in base rates without having utilities incur the cost and expense of unnecessary, general base rates proceedings. Far from being a “ploy,” these clauses are a “plus” – they permit regulators and utilities to address the real problem without the costly overlay of unnecessary and counter-productive proceedings.¹³⁸

Criticism 2: Adopting the CRRC will weaken PGW’s incentive to collect its bills and establish a precedent in Pennsylvania for other companies to seek similar clauses.

¹³⁶ 66 Pa. C.S. § 1307(a); *National Fuel Gas Distribution Corp.*, 473 A.2d at 1121.

¹³⁷ See discussion of legal points and authorities, section III (C) and (D) *supra*.

¹³⁸ See generally PGW Statement No. CRRC-1R at 5, 6, outlining the heavy additional burden that a base rates case would place on PGW’s customers, and comparing that approach with the more targeted CRRC.

Response: PGW has a strong incentive to collect its bills, and nothing about the CRRC will weaken that incentive. PGW is a cash receipts company, and must match its cash revenues carefully to its expenses. Even relatively small changes in collections percentages can cause large decreases in cash receipts, which PGW must avoid.¹³⁹ Also, as Mr. Knudsen testified with utter conviction, PGW is committed irrevocably to its bill collections initiative; it views the CRRC as a back-stop or insurance policy to assure bond-rating agencies that PGW will have the solvency to meet its obligations. This is important for PGW's customers because it will decrease PGW's costs for borrowing money and avoid a downgrading of its bond rating to junk status.¹⁴⁰ Also, PGW is the only cash receipts regulated utility in Pennsylvania, so its treatment in this case will not spark a rush of copycat filings from other, more traditionally regulated companies.¹⁴¹

Criticism 3: The CRRC is unbalanced and inequitable because it permits PGW to retain any increases in its cash receipts even if its collections improve over allotted levels.

Response: The CRRC is a fair, balanced and proportionate response to the potential of an extraordinary cash receipts shortfall, and does not affect any change in current law or policy relating to retention of uncollectibles expenses. PGW currently has an uncollectibles expense allowance of \$55.7 million, which was established by this Commission in PGW's last fully litigated base rate case.¹⁴² Under current regulatory procedure, to the extent PGW reduces its uncollectible expenses below \$55.7 million, it retains the difference and uses this money for cash working capital.¹⁴³ There is an excellent policy reason for this rule: it incents PGW (or any other utility) constantly to improve its collections in order to generate working capital. In turn, improved collections and additional contributions to utility cash working capital help to keep customer bills reasonable and lower the need/likelihood for costly general base rate cases. If further incentive were required, it has been provided by S&P, which stated that PGW must

¹³⁹ For every 1% decrease in collections, PGW suffers an approximately \$8 million decrease in revenues. PGW Statement No. CRRC-1 at 5; Tr. 313.

¹⁴⁰ Tr. at 359, 360.

¹⁴¹ OTS St. No. 1 at 3.

¹⁴² PGW St. No. CRRC-1 at 4, 6, 11.

¹⁴³ Tr. at 423.

demonstrate material improvement in its cash position in order to maintain an investment grade bond rating.

The CRRC does nothing to upset this policy balance. In years when PGW collections exceed its historical average (and therefore result in a cash receipts shortfall below the current \$55.7 million uncollectible allowance), the CRRC will be set at zero for the next fiscal year and PGW will retain the current year difference as a contribution to its cash working capital reserve. In years when PGW experiences an undercollection, the CRRC will be set at a level to correct for this undercollection.¹⁴⁴ However, PGW will still retain its incentive to improve its collections for the coming year since this improvement is absolutely essential to enable PGW to generate additional the cash working capital it needs to maintain its investment grade bond rating, access the capital markets in the fall, pay down short and long-term debt, repay the City Loan, make its annual City payment, etc. In turn, PGW's collections improvement will result in a lower or a zero CRRC for the following year.¹⁴⁵

Criticism 4: The CRRC is not consistent with cost-causation factors. PGW's residential class is disproportionately responsible for uncollectibles expense, and the CRRC as proposed would shift some of these residential costs onto business customers.

Response: A utility must recover its service costs from its base of ratepayers. All utilities have uncollectible accounts expense, mostly attributable to its residential customers, which must be spread over the entire rate base. This causes business customers to pay somewhat for residential customer costs. Notably, PGW's customer base is disproportionately residential. However, the proper goal of regulatory public policy, however, is not to ensure precise alignment of costs only with the proper category of cost-causers. The proper goal of regulatory public policy is to maximize the public interest. At times, this requires a utility commission to recover greater contributions toward cost from parties with a better ability to pay.¹⁴⁶ Moreover,

¹⁴⁴ PGW St. No. CRRC-1 at 10-12.

¹⁴⁵ Tr. at 398-399.

¹⁴⁶ PGW St. No. CRRC-4R at 10. OSBA's witness Knecht, despite his cost-alignment testimony, does not entirely believe his own rhetoric. On the one hand, witness Knecht argues that PGW's business customers should not subsidize costs caused by residential customers; on the other hand, he also advocates that PGW ought to pursue state and federal funds to subsidize its universal service obligations. In effect, witness Knecht argues that people who do not use PGW's gas services (and therefore are not "cost-causers") should

assisting PGW to continue as a going concern and retain its investment grade bond rating benefits all customers -- not just residential customers. To that extent, PGW's commercial and industrial customers realize benefits that justify the charge to all customers on a equal percentage basis.

Criticism 5: The CRRC will raise customer bills so high that customers will pay even less of the additional charges; since the rate increases will be ineffective, they should not be adopted in the first instance.

Response: This argument is nonsensical and ignores reality. PGW has instituted and is committed to continuing its bill Collections Initiative, which has already increased collections in recent weeks and is on target to have PGW approach its historic collections experience by the end of fiscal year 2004.¹⁴⁷ Therefore, the CRRC mechanism likely will produce rates much lower than those predicted in OSBA's "doomsday" scenarios, which were based on mathematical models assuming continuing extremely high uncollectibles expense. Also, OSBA's argument essentially boils down to this: for every dollar of increased rates, PGW will still realize substantial increased revenues; it may see a couple of percentage points less per dollar than it thought it might attain.¹⁴⁸ Taken to its logical (and absurd) conclusion, OSBA's argument is that no utility should ever raise rates, since higher rates will always cause some customers to pay a bit less of their bills. This is not how utilities operate in the real world, and the Commission should pay no heed to this OSBA fallacy.

Criticism 6: PGW seeks to apply the CRRC to all undercollections, not just those associated with rising purchased gas cost revenues, and therefore is overbroad and inconsistent with other similar proposals adopted by regulators.

Response: PGW is a cash flow regulated municipal utility; it is somewhat different than investor-owned utilities, and requires a more nuanced regulatory approach. PGW's cash undercollections are due in substantial part to volatile, rising gas costs; but they are not due entirely to this cause. It is important to assure PGW of a consistent, earned supply of cash to

nonetheless subsidize those that use PGW gas. His testimony is inherently contradictory and should be discarded.

¹⁴⁷ PGW Statement No. CRRC-4R at 2 (PGW's receipts as a percentage of billed revenue are 90.46% for 12 months ending March 2004; this rate of improvement would yield a 93% rate by end of fiscal year 2004).

¹⁴⁸ OSBA Statement No. 1 at 18.

meet its special needs, including short and long term debt obligations, normal operating expenses, and the eventual reinstatement of its annual commitment to the City. The bond rating agencies have demanded the same – and expect it quickly. The CRRC seeks to ensure PGW’s revenues enable it to meet its many and varied obligations. The clause is entirely consistent with the similar flexible automatic adjustment mechanisms approved in other jurisdictions.

Criticism 7: PGW’s collections problems are not primarily related to its high customer bills or to the demographics of its customers; they are much more likely caused by PGW’s billing problems and by management’s lack of will to collect the bills.

Response: OSBA has again missed the mark, relying on faulty data to produce a flawed conclusion. To support its conclusion, OSBA’s witness Knecht lays out a comparison of Philadelphia and Erie; he notes that NFGD has higher collections than PGW, even though Erie households have lower income (\$28,387 vs. \$30,746).¹⁴⁹ A comparison of Philadelphia to Erie is ridiculous on its face. Significantly, Mr. Knecht failed to correct his income data for the much higher cost of living in Philadelphia. Dr. Peach corrected for this error, demonstrating how Erie household income (\$28,387) actually compared with much lower “real” Philadelphia household income (as low as \$21,768).¹⁵⁰ In reality, Erie residents have over \$6,600 per year (\$550 per month) *more* than Philadelphia residents with which to pay their gas bills. OSBA’s data is flawed; its conclusions flowing from that data are also flawed; and this Commission should reject OSBA’s assertions.¹⁵¹

¹⁴⁹ OSBA Statement No. 1 at 20. In fact, Mr. Knecht highlights the importance of the income differential to his analysis in part by setting it forth as its own, one-sentence paragraph.

¹⁵⁰ PGW Statement No. CRRC-4R at 6, fn. 4. In fact, Mr. Knecht on cross-examination admitted that he had no reason to doubt Dr. Peach’s analysis on this point. Tr. at 481.

¹⁵¹ Witness Knecht also attempted to buttress his NFGD-PGW comparison by purportedly discrediting Dr. Peach’s testimony concerning Pennsylvania gas company write-off rates. Mr. Knecht calculated a “cash basis” write-off rate of 16.7% for PGW, and compared this figure with bad debt expense write-off rates for other gas utilities. But Mr. Knecht was comparing apples and oranges – he was forced on cross-examination to admit that he did not use PGW’s comparable bad debt write-off rate of 8.5 to 9.1% (as calculated by Dr. Peach), and that Dr. Peach’s number might well be correct. Knecht testimony, tr. at 483 - 485; Peach testimony, Tr. at 407, 408. This additional error further erodes the OSBA position, leaving it with no credibility.

2. OCA

The OCA generally echoes the OSBA's criticisms of the CRRC. Specifically, the OCA believes that: (1) the CRRC is unprecedented; (2) PGW should have filed a base rates case; (3) the CRRC would lessen PGW's incentive to collect its bills; (4) the CRRC is inequitable in that it does not provide for customer rate decreases; and (5) the CRRC's E-factor would constitute "retroactive ratemaking."¹⁵² PGW has comprehensively refuted these claims earlier in this brief. However, OCA raises two additional criticisms, that are equally off the mark.

Criticism 1: The CRRC is based on accounts receivable, which do not automatically translate into uncollectibles expense. Also, the base rate allowance for uncollectibles expense is not known because of the effects of the "black box" settlement, and it would be unreasonable to use PGW's claimed \$55.7 million allowance from the last fully litigated base rates case.

Response: The OCA has confused the calculation of PGW's provision for uncollectibles expense and its cash receipts levels. Although OCA correctly notes that any dollar of uncollected cash may or may not become permanently uncollectible, the amount that the CRRC recovers does not depend on that contingency. If, in a future month or year, a customer pays that dollar, it will simply add to PGW's cash receipts level and increase PGW's collections percentage. Customers will receive the benefits of that additional dollar collected automatically in the adjustment of the CRRC.¹⁵³

As for the \$55.7 million allowance, this amount was the last Commission-approved uncollectible accounts expense allowance arising out of PGW's last fully litigated base rates case. OCA has conceded that, if the calculation were adjusted to include the most recent settlement rate increase the uncollectible expense offset at most would increase \$2.7 million to \$58.4 million.¹⁵⁴

¹⁵² These criticisms appear in OCA Statement 1 at 13-21. OSBA, OCA and OTS's retroactive ratemaking claims are refuted in section III(C)(4) of this brief.

¹⁵³ PGW St. CRRC-1R at 9, 10.

¹⁵⁴ *Id.* at 10. Tr. at 422.

Criticism 2: The City's grant back to PGW of the \$18 million annual payment and deferral of the \$45 million loan repayment obviates any need for the CRRC and PGW should withdraw the request.

Response: The grant back and loan deferment help to alleviate somewhat PGW's cash flow difficulties, but it does not come close to eliminating them. The rating agencies still look for PGW to maintain about \$60 million in end of year cash. Moreover, even after recognizing the salutary effects of the City's action, when one-time transactions are backed out, PGW will finish the year with just \$1-6 million in ending cash.¹⁵⁵ they have downgraded PGW's rating and stated unequivocally that PGW **must make further material** improvements in cash working capital and collections or its bond rating will be lowered to junk. PGW must not only have the safety net that the CRRC affords in order to maintain its bond rating and guarantee some measure of liquidity if collections fall, but must go beyond this and take steps that will result in additional improvements in its cash position.¹⁵⁶ Far from eliminating the need for the CRRC, the City's grant back only makes it clear how necessary this additional protection is to PGW's survival.¹⁵⁷

3. OTS

OTS repeats some of the criticisms leveled by OSBA and OCA concerning the CRRC proposal: (1) it is one-sided in that it does not allow for rate reductions when collections improve; (2) it creates a disincentive for PGW to pursue collections; (3) it includes a component (E-factor) that constitutes retroactive ratemaking; (4) it improperly continues to use \$55.7 million as the uncollectible accounts expense, when in fact that number should be higher in light of the black box settlement; and (5) it permits PGW to retain projected undercollections even if actual uncollectibles are lower than what was projected.¹⁵⁸ PGW has already addressed these criticisms.

¹⁵⁵ See section III(A)(5) of this brief, *supra*.

¹⁵⁶ PGW St. CRRC-5 at 9; Tr. at 358-360.

¹⁵⁷ The OCA's failure to take seriously the promised negative action of Standard and Poor's, Fitches and Moody's is not new. The Commission rejected this same attitude by the OCA in the *Extraordinary Rate Relief Proceeding*, and it should do likewise now. *Extraordinary Rate Relief Order*, R-00017034F0002 at 14-17.

¹⁵⁸ OTS St. No. 1 at 4 -9.

However, unlike the other parties, however, OTS recognizes PGW's need to restore its cash receipts position and proposes that this Commission adopt a flexible, automatic adjustment mechanism to account for PGW's receivables undercollection.¹⁵⁹ The OTS proposal recognizes that PGW, as a cash flow company, automatically undercollects on its accounts receivables whenever its gas costs exceed the gas costs that were used to establish PGW's uncollectibles expense allowance in the last fully litigated base rate case. To correct for this undercollection, OTS proposes an adjustment to the receivables bases on a comparison of gas cost rates as part of the GCR process. If gas costs exceed the amount used in base rates, PGW would recover the additional uncollectibles in the coming fiscal year. If gas costs fell below those used in base rates, PGW would refund the difference to ratepayers.¹⁶⁰ Although PGW welcomes OTS' willingness to look at this matter constructively, PGW notes that the OTS proposal is deficient in several respects:

Deficiency 1: The OTS proposal fails to consider the entirety of PGW's cash receipts shortfall.

The OTS proposal focuses solely on the effects that rising gas costs would have on PGW's undercollections. OTS fails to take into consideration that PGW experiences undercollections on its bills for reasons other than gas cost increases, and that these undercollections damage PGW's overall cash position. As a cash flow company, PGW is particularly dependent on collecting its billed revenue, and the OTS proposal would leave PGW with a critical gap in coverage for undercollections.

Deficiency 2: The OTS proposal fails to offer relief to PGW for current undercollections relating to gas costs.

OTS calculates that PGW will undercollect its bills by over \$10 million in fiscal year 2005, and proposes that PGW be permitted to recover this amount through an automatic adjustment to rates.¹⁶¹ OTS also recognizes that the *identical* factor that will drive PGW's FY

¹⁵⁹ Tr. at 415-416.

¹⁶⁰ OTS St. 1 at 9-13.

¹⁶¹ OTS St. 1SR at 5.

2005 undercollection is currently driving a FY 2004 undercollection as well.¹⁶² Inexplicably, OTS believes that PGW should not recover its FY 2004 undercollection.

The OTS position is simply unsustainable, particularly in the face of the threatened downgrade by the rating agencies absent material, near term improvement to cash margins. The Commission cannot expect PGW to achieve such improvement in the near term by placing it in an even deeper hole now. Further, considerations of fairness and equity should compel recovery of PGW's current undercollections as well. As discussed, substantial Pennsylvania and other precedent protects a utility in these circumstances, and permits a utility to recover extraordinary undercollections through amortization over a period of years. PGW's current undercollected expenses are for the not yet concluded fiscal year. These current undercollections arise for the very same reason that will cause the fiscal year 2005 undercollection, which OTS readily admits must be recovered. There is no legal or regulatory stretch required here to do the right thing: permit PGW to recover fiscal year 2004 undercollections through an E-factor amortization over the next three years.¹⁶³

Deficiency 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.

Beyond being inadequate, the OTS proposal could actually harm PGW's liquidity levels. As currently configured, the PUC-established PGW uncollectible expense allowance of \$55.7 million contains a mechanism to encourage PGW to improve collections and add to its capital reserves. Should PGW improve collections such that its actual uncollectibles expense falls below the allotted \$55.7 million, PGW would retain the difference and add that difference to working capital. This money would then be available to PGW to pay off short and long-term debt and improve its infrastructure, an obvious benefit to PGW customers. There is nothing new or unusual about this approach – the Commission employs it for all utilities.

¹⁶² Tr. at 418.

¹⁶³ If the Commission adopts the OTS formulation, it should modify the relief to include recovery of PGW's current undercollections. While that figure was not presented on the record, if the Commission were to adopt this approach, the reasonable approach would be for PGW to be given the opportunity to present as part of its compliance filing the current year shortfall for collection on a 3-year amortized basis. Tr. at 317-18.

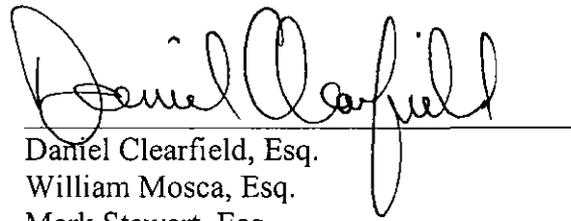
The OTS proposal could do away with PGW's ability to improve collections and meet the S&P requirement of a "material improvement." The proposal requires PGW to refund to customers differences in uncollectible recoveries that PGW will experience if and when gas costs fall below those established in base rates. In other words, revenues that PGW ordinarily would be permitted to retain and add to its cash working capital reserves would now be stripped away and returned to ratepayers. This approach is entirely inconsistent with the Commission's treatment of uncollectibles expense. It is equally inconsistent with any attempt to meet the demands of the rating agencies and avert a second downgrade. The proposal effectively would do away with the Commission's base rates allowance, deprive PGW of necessary working capital, and destroy PGW's incentive to improve bill collections as a method to add to working capital.¹⁶⁴

¹⁶⁴ If approved, the OTS proposal also should be modified to permit PGW to retain any differences in collections generated by a lower-than-base rates gas cost. This change would be in the public interest, as it would incent PGW to continue collections improvement as a method to add to its cash working capital, and thereby be in a much better position to pay down debt, improve infrastructure and avoid future base rates cases.

IV. CONCLUSION

For the reasons stated above, the Pennsylvania Public Utility Commission should grant PGW's request to implement a tariff permitting a Cash Receipts Reconciliation Clause (CRRC) and to file a compliance filing with the specific details of such a clause (and reflecting any variations in the original proposed tariff pages submitted with its March 1 filing).

Respectfully submitted,



Daniel Clearfield, Esq.
William Mosca, Esq.
Mark Stewart, Esq.
Wolf, Block, Schorr and Solis-Cohen LLP
212 Locust Street, Suite 300
Harrisburg, PA 17101
(717) 237-7173

Of Counsel:
Gregory Stunder, Esq.
Philadelphia Gas Works
800 West Montgomery Ave
Philadelphia, PA 19122

Date: June 14, 2004

APPENDIX A

PROPOSED FINDINGS OF FACT

1. PGW is in a severe financial crisis, which threatens to cripple the Company and its ability to provide safe, adequate and reliable service to its customers. PGW St. No. CRRC-1.

2. PGW's financial crisis has resulted in downgrades of its debt by the major bond rating services, Standard and Poor's, Moody's and Fitch's:

(a) In April of this year, Standard and Poor's downgraded PGW's bonds to the lowest available investment grade rating, a level just above junk bond status, and stated that further downgrades to junk bond status will happen absent material improvement in the Company's cash margins and liquidity;

(b) In June of this year, Moody's placed PGW bonds on its Watchlist; and

(c) Fitch's has also downgraded Company bonds to a level just above junk status.

PGW St. No. CRRC-5, Exh. TEK-1 and 2.

3. If PGW's debt is reduced from investment grade to junk bond status, PGW's cost of financing and insuring currently planned bond offerings will increase substantially, to the detriment of PGW's customers, who ultimately must bear this additional expense. Tr. at 356.

4. A downgrade of PGW's debt from investment grade status to junk bond status would produce devastating results both for the Company and for its customers. PGW St. CRRC 5 at 7-9; PGW. St. No. CRRC-1 at 9; Tr. at 360, 447.

5. The main driver of PGW's current financial situation is high natural gas prices that remain at unprecedented levels. PGW's gas costs have more than doubled from the range of \$2.00 to \$2.50 per Mcf in the 1996-1999 timeframe to the range of \$4.50 to \$6.00 in the 2003-2004 period. The Company's actual total fuel costs have increased from \$226 million in the year 2000 to \$455 million in 2004. PGW St. CRRC-2 at 2; OCA St. 1 at 24, 25.

6. There appear to be no prospects for a near-term reversal of the gas cost trend, as contract prices for NYMEX futures have exceeded \$6.00 per Mcf in recent quotes. *Wall Street Journal* (June 14, 2004) p. A-2.

APPENDIX A

7. These high natural gas prices have resulted in higher than normal customer bills, which in turn have produced higher than normal cash undercollections of these customer bills. PGW St. CRRC-1 at 4-6.

8. These higher than normal cash undercollections have increased PGW's absolute level of uncollectible expense and bad debt, and reduced PGW's cash working capital to levels far below what it needs to maintain financial liquidity. PGW St. CRRC-1 at 6-8.

9. PGW is regulated on a unique "cash flow method basis," which was originally used by PGW's predecessor regulatory agency and carried over to this Commission under the provisions of the Gas Choice Act. Pa. C.S. § 2212(e); PGW St. CRRC-1 at 7.

10. The Gas Choice Act requires this Commission to establish PGW's rates at a level that will permit the Company to maintain the debt coverage levels required by its bond covenants, and to achieve levels of liquidity that enable it to pay its bills when due. Under this method of regulation, PGW obtains all of its cash working capital from customers in the rates it charges for gas service. Pa. C.S. § 2212(e); PGW CRRC-1 at 7.

11. The main drivers of PGW's cost of service are natural gas costs; operating expenses; cash working capital; and the cost of borrowing. Only a small percentage of these expenses are discretionary. PGW St. 5, Exh. TEK 4.

12. PGW recovers its natural gas costs in a separate rate established under Section 1307(f) of the Public Utility Code and known as the Gas Cost Rate, or GCR. The GCR is automatically adjusted quarterly to reflect changes in wholesale prices in natural gas because historically, natural gas costs have been quite volatile. PGW St. CRRC-1 at 3.

13. Actually experienced gas costs are largely the function of overall commodity market conditions and are outside of the Company's control. PGW St. CRRC-1 at 3.

14. While PGW collects natural gas costs in an automatic adjustment clause that changes as wholesale gas prices change, all of PGW's other costs and expenses are recovered in fixed base rates. This includes the key cost elements of uncollectible accounts expense and cash working capital. PGW St. CRRC-1 at 3-7.

APPENDIX A

15. Like every company, PGW regularly fails to collect a portion of its billings. When these accounts receivable become permanently uncollectible, PGW has no alternative but to write them off. Before it writes them off, PGW establishes a provision for uncollectibles which reflects the amount of write-offs it has experienced in the past year plus the amount of additional uncollectibles it anticipates for the coming year. This provision for uncollectible expense is the basis for a utility's allowance in its base rates. PGW St. CRRC-1 at 4; OSBA St. 1 at 2.

16. The Commission established PGW's current base rate uncollectible account expense allowance of \$55.7 million in the 2001 base rate gas proceeding, based on an authorized uncollectible expense percentage of 7.616% of pro forma revenues. This authorized amount assumed implicitly that PGW would collect the remainder of its billed revenues -- 92.38%. PGW St. CRRC-1 at 4.

17. Historically, PGW's uncollectible expense amount has been in the 7% to 8% range. Since 1999, PGW's actual bad debt expense has ranged from 8.1% up to a high of 11.2% in 2003. PGW St. CRRC-1 at 4, 5.

18. High levels of gas costs have an especially negative impact on the collections of cash flow companies like PGW. When the Company incurs natural gas expenses higher than those established in base rates, it experiences higher uncollectibles expense and reductions in cash working capital. OTS St. 1 at 11.

19. Historically, as PGW's billings to its customers have increased to reflect the higher costs of natural gas, its receipts as a percentage of billings have tended to decrease. Correspondingly, in years where billings have fallen, PGW's collections have tended to increase. There is a statistically significant correlation between these variables. PGW St. CRRC-4-Supp. at 3.

20. PGW's customer base includes large segments of inner City elderly and poor customers, whose income levels have tended to decline over the years. Combined with the higher bills caused by higher gas expenses and colder weather, these customers have tended to pay less on their bills. PGW St. CRRC-4 (Revised) at 7-10, 11.

21. The recent downturn in PGW's collections percentages was caused in large part by factors such as gas cost, weather-related consumption and declining customer incomes, which

APPENDIX A

are factors outside of PGW's control. Collections stability will remain an issue for the foreseeable future. PGW St. CRRC-4R at 7; Tr. at 405.

22. These factors have taken a heavy toll on PGW's finances. At the time it filed for the CRRC, PGW was collecting only 87 cents for every dollar billed to customers, and was projecting a 2004 fiscal year end cash deficit of \$10.7 million and liquidity (cash plus short-term borrowing ability) of negative \$5 million. The fiscal year 2003 cash receipts shortfall cost PGW \$40 million in reduced cash working capital. PGW Exh. JRB-5 at 2; Tr. at 313.

23. In addition to filing for the CRRC, PGW has taken a series of steps designed to reduce costs and to increase revenues. Among other steps, PGW:

- (a) commenced a massive collections effort, which has improved collections to the point where PGW could end the fiscal year with a 91% to 93% collections rate (PGW St. No. CRRC-3);
- (b) secured a grant-back from the City of the \$18 million per year City fee for the next five years (PGW St. No. CRRC-1R at 3);
- (c) secured an agreement from the City to postpone the due date of a fully extended \$45 million line of credit for an additional two years (PGW St. No. CRRC-1R at 3);
- (d) arranged to defer payment of \$30 million for the purchase of natural gas until fiscal year 2005 (PGW St. NO. CRRC-5 at 6-8);
- (e) evaluated operational costs and discretionary expenditures to determine whether and to what extent these could be reduced (PGW St. No. CRRC-1 at 9-10); and
- (f) sought out new federal and state funding sources to supplement the universal service programs currently funded by the Universal Service Charge. (PGW St. CRRC-1R at 2-5).

24. When the extent of PGW's financial situation first became clear, two of the three primary bond rating agencies, Standard & Poors and Fitches, downgraded the Company's debt to minimum investment grade and clearly indicated that further downgrades could be expected if circumstances did not improve quickly. PGW St. CRRC-5 at 6-7.

25. Bond rating agencies expect a company of PGW's size, with more than \$800 million per year in billings, to maintain 30 days of average revenue for liquidity purposes. This is necessary

APPENDIX A

in order to maintain an investment grade rating. To meet this requirement, PGW needs fiscal year end liquidity of \$60 million. PGW St. CRRC-1R at 4.

26. In past proceedings, PGW has indicated that it needed a minimum of \$35 to \$40 million in fiscal year-end liquidity to meet its disbursements and debt service for the coming months. At the time it gave those estimates, PGW had a \$100 million short term commercial paper line of credit available. That line has now dropped to \$80 million, which means PGW must increase its level of cash produced from rates to make up the additional \$20 million. Tr. at 349-351.

27. Before the recently completed gas deferral deal, PGW faced a fiscal year end cash deficit of \$12 to \$17 million. The gas deferral deal is the equivalent of a short-term loan, since the \$30 million must be paid in fiscal year 2005. There is no guarantee that this procedure can be repeated in the future. PGW St. CRRC-1R at 2-4.

28. PGW's financials show cash working capital for fiscal year end 2004 of \$31 to \$36 million. PGW arrived at this figure only by adding in the \$30 million gas purchase deferral and the \$18 million City grant-back, and by deferring any repayment of the \$45 million City line of credit. PGW St. CRRC-1R at 3-4.

29. Even with the deferral and grant-back included, PGW is \$24 to \$29 million short of its liquidity goal of \$60 million. PGW St. No. CRRC-1R at 3-4.

30. If the \$30 million deferral is removed from its financials, PGW at the end of fiscal year 2004 would have a liquidity balance of only \$6 million. This figure assumes that PGW can achieve a collections rate of 93% for the year. PGW St. CRRC-1R at 2-5.

31. At a more realistic 90.5% collections rate for fiscal year 2004, PGW's liquidity figure falls from \$6 million to \$1 million. PGW's more likely collection rate for fiscal year 2004 will be about 91%. Tr. 364.

32. Even with the City grant-back of the \$18 million and postponement of repayment of the \$45 million line of credit, PGW has insufficient liquidity to meet its obligations and to maintain its bond rating at investment grade level. PGW St. No. CRRC-1R at 3-5.

APPENDIX A

33. PGW must be in a position to operate its business properly. At a minimum, PGW must have sufficient cash to: purchase, store and deliver natural gas to its customers in a safe and reliable manner; pay down its short and long-term debt obligations and preserve its access to financial markets in the future; be able at some point to resume its \$18 million payment to the City; and provide a sufficient reserve to meet anticipated contingencies. Tr. at 350, 351 and 364.

34. Most importantly, PGW must have sufficient end-of-year cash to demonstrate to the bond rating agencies that PGW deserves to keep its investment grade bond rating. PGW St. CRRC-5 at 8-9; Tr. at 315-316, 350-351.

35. The CRRC mechanism that PGW proposes provides a targeted solution to PGW's real problem – the potential for a debilitating cash receipts shortfall. PGW's booked uncollectible expense has increased dramatically from its 2001 rate case allowance of \$55.7 million, to \$85 million in FY 2003 and a projected \$70 million for FY 2004. This cash shortfall has harmed PGW's financial results and significantly affected earnings, bond coverage levels and cash working capital. This shortfall and the potential for future shortfalls can be addressed and remedied by a properly functioning CRRC mechanism. PGW St. No. CRRC-1 at 11 and No. CRRC-1R at 11-12.

36. The key advantage of the CRRC is that it will provide assurances that PGW's cash working capital will at least reflect the Company's historic collection levels. It is therefore an adequate and appropriate backstop or insurance policy to PGW's collection efforts, and will serve to assure the financial markets that the Company has a reasonable opportunity to rebuild its cash working capital. The CRRC mechanism will help PGW to retain its investment bond rating for Company debt. PGW St. No. CRRC-5 at 17-18; Tr. at 316, 354-357.

37. The CRRC also will incent PGW significantly to improve collections. As proposed, the CRRC is a "make whole" mechanism. If PGW exceeds its historic collections levels, it retains any additional cash that the CRRC may have generated. PGW therefore will be in a position to work toward increasing collections in order to generate needed cash working capital. PGW St. No. CRRC-5 at 17, 18; Tr. at 354-358.

APPENDIX A

38. Importantly, the CRRC is also self-adjusting. If PGW meets or exceeds its historic collections percentages, the CRRC automatically adjusts to zero for the coming fiscal year. The CRRC will impose a charge only after those years in which PGW is unable to collect at its historic levels. The charge will then be established equal to the shortfall, in order to make PGW whole. Tr. at 397-398.

39. The CRRC is also particularly suited to mirror the method PGW currently uses to recover increases in natural gas costs, which are the principal reason for the Company's current crisis. Higher customer bills, and the greater incidence of uncollectible expense associated with those bills, are driven in substantial part by higher gas costs. The CRRC, like the GCR, is a suitable 1307(f) mechanism to provide for flexible, temporary, and self-adjusting rate increases. PGW St. No. CRRC-1R at 5-6.

40. The CRRC is far superior to a base rates case to address the particular issue that PGW faces. If PGW was forced to file a base rates case, the Company's claim would be on the order of \$74 to \$94 million. Once approved, these increases would go into effect and remain in effect until there was another base rates case, irrespective of any Company improvements in collections, cash flow, uncollectibles or operations. PGW St. No. CRRC-1R at 5.

41. A base rates case would establish high rates in a difficult economic setting without the possibility of automatic adjustment to better rates as uncollectibles and other expenses improved. A base rates case would only invite future base rates cases to address changes in a cost variable that the CRRC would address automatically. Base rates cases are a non-optimal alternative to the CRRC. PGW St. No. CRRC-1R at 6.

42. The base rates case alternative also will not address PGW's financial crisis in a timely manner. PGW needs to have the CRRC mechanism in place by this fall at the latest in order to stave off a reduction in its bond rating to junk status. PGW St. No. CRRC-5 at 17-18.

43. The CRRC mechanism has two components: a pro forma calculation and an E-factor. Both involve simple calculations. The pro forma calculation compares expected collections of cash receipts with the \$55.7 million uncollectible accounts allowance. The expected collections figure is set at the past fiscal year's collections percentage. If there is a cash shortfall, the CRRC

APPENDIX A

establishes this amount as a surcharge to be collected in the coming fiscal year. If there is no projected shortfall, the CRRC pro forma amount is zero. PGW St. No. CRRC-1 at 11-13; Tr. at 397-398.

44. The E-factor aspect of the CRRC works in the same fashion as the E-factor for the GCR. If there is a cash receipts shortfall at the end of the fiscal year not recovered by that year's CRRC pro forma, the shortfall is recovered through amortization over future years. PGW Statement No. CRRC-1 at 11-13.

45. If PGW finishes fiscal year 2004 with a 91% collections rate, a CRRC mechanism would result in a pro forma CRRC of approximately \$18 million for fiscal year 2005. If PGW completes fiscal year 2004 with a 93% collections rate, the CRRC would be set at zero. Exhibit KSD-2; Tr. at 364, 397.

46. The CRRC as proposed by PGW is a flexible and targeted mechanism that addresses a recent and extraordinary phenomenon: the sharp rise in uncollectible accounts expense attributable to very high customer bills, which reflect large increases in gas cost rates due to supply volatility and colder than normal weather. The CRRC is not a ploy to avoid a base rates case. PGW St. No. CRRC-1R at 5-7.

47. The CRRC has precedent in both Pennsylvania and other jurisdictions. Also, OTS supports the concept of granting PGW a flexible, automatic adjustment mechanism to account for the Company's cash undercollections owing to the unusually high gas cost rate. OTS St. No. 1 at 4-9; Tr. at 415-416.

48. PGW will retain a strong incentive to collect its bills even with the CRRC. It is a cash receipts company and must match its cash revenues closely with its expenses. Even relatively small changes in collections percentages can cause large decreases in cash receipts, which PGW must avoid. PGW St. No. CRRC-1 at 5.

49. The CRRC is a fair, balanced and proportionate response to the Company's cash receipts shortfall issue. It does not effect any change in current Pennsylvania law concerning retention of uncollectibles expense funds. Under current law, PGW is entitled to retain and use as cash

APPENDIX A

working capital any difference between the authorized uncollectible expense allowance and its actual uncollectibles experience. The CRRC preserves this principle. Tr. at 423.

50. The CRRC properly includes an amortization of current fiscal year 2004 cash undercollections, if any, and does not offend any proscription against retroactive ratemaking. OTS admits that the precise mechanism that will cause any undercollections in future years -- gas costs above those established in base rates -- is driving PGW's current undercollections problems. Tr. at 415-418.

51. PGW will realize a substantial collection of any additional sums charged to ratepayers under the CRRC. There is no evidence that the CRRC will be ineffective or otherwise unwarranted because some ratepayers may pay a little less of the increased bill. Tr. at 406.

52. The PGW CRRC as proposed is superior to the OTS partial recovery mechanism. PGW's cash undercollections are due primarily to unusually high gas costs, but are not due exclusively to this cause. The OTS proposed mechanism only corrects for future gas cost effects. The PGW mechanism corrects for current and future gas cost effects and other revenue-affecting expenses. PGW St. No. CRRC-1R at 11-13.

53. PGW's current collection problems are caused primarily by high customer bills and customer demographics. They are not caused by any management lack of will to collect the bills or current billing problems. PGW is in the midst of a massive bill collections effort, which has resulted in some success at raising its collections rates. Also, OSBA's NFGD/Erie data is fundamentally flawed for failing to correct for important cost of living differences between Erie and Philadelphia, and must be rejected along with its faulty conclusions. PGW Statement No. CRRC-4R at 6; Tr. at 481.

54. The "black box" settlement of PGW's last base rates case did not alter PGW's current base rates uncollectibles allowance of \$55.7 million. Even if the effect of that settlement was factored into the current allowance, it would at most increase the \$55.7 million by \$2.7 million to a total of \$58.4 million. PGW St. No. CRRC-1R at 10; Tr. at 422.

55. The grant-back of the City payment of \$18 million annually for the next five years, along with deferral of repayment of the City loan, will somewhat alleviate but not eliminate PGW's

APPENDIX A

cash flow problems. They will not bring PGW close to the \$60 million it needs in liquidity to maintain its bond ratings, and will not constitute in and of themselves the material improvements in cash working capital that PGW needs to maintain its investment bond rating. PGW St. No. CRRC-1R at 9; Tr. at 358-360.

PROPOSED CONCLUSIONS OF LAW

1. PGW's request for the establishment of a CRRC mechanism is a fair, reasonable, just and proportionate approach to the special problems that face a cash flow regulated gas utility in times of rising and sustained high gas costs and the associated difficulties with customer collections.
2. Section 1307(a) of the Public Utility Code authorizes this Commission to establish a "sliding scale of rates or other method for the automatic adjustment of the rates of the public utility..." in order to provide just and reasonable treatment of the particular utility. PGW's request for a CRRC adjustment mechanism is a request very similar to the existing GCR adjustment mechanism authorized by Sec. 1307(f) of the Code. This Commission has the authority under Sec. 1307(a) to authorize the requested CRRC mechanism.
3. Alternatively, this Commission has authority under Sec. 2212(c) of the Code to alter or revise any aspect of the Public Utility Code (including implementing regulations) necessary to customize a regulatory approach to accommodate the special and unique issues and problems inherent in the regulation of PGW as a cash flow company.
4. This Commission has in the past exercised its authority under Sec. 1307(a) of the Code to authorize automatic adjustment clauses involving various categories of costs across an array of utilities. For the electric industry, the Commission has approved adjustment clauses involving demand-side management and coal uprating costs. For water utilities, the Commission has approved adjustment clauses involving principal and interest due on PennVEST obligations and distribution system improvements. For natural gas utilities, this Commission has approved adjustment clauses addressing take or pay costs to pipeline suppliers; costs resulting from FERC Order 636; and gas choice customer education initiative costs. The Commission has also authorized adjustment clauses to deal with incremental changes in state taxes for utilities facing Clean Air Act compliance costs. The Commission has also granted requests for utility-specific

APPENDIX A

costs including PECO's costs to convert oil fired units to gas fired units; Philadelphia Thermal Energy's water and sewer costs; and Jackson Sewer Corporation's costs for sewage treatment services provided by a municipal authority.

5. As these many examples suggest, and as the Pennsylvania Courts have confirmed, the Commission may order an automatic adjustment clause to address a particular area of concern as a matter of sound discretion. Sec. 1307(a) recognizes the salutary purpose of these adjustment mechanisms: "to permit the reflection in customer charges of changes in one component of a utility's cost ...without the necessity of the broad, costly and time-consuming inquiry required in the case of rate increases generally."

6. Sec. 1307(a) contains no artificial limitation as the costs that the Commission may consider appropriate for an adjustment clause. To inform its exercise of sound discretion, the Commission has noted that questions of significance, volatility and control have been used as criteria for the inclusion of items into an automatic adjustment clause. *E.g., Pa. PUC v. Philadelphia Thermal Energy Corp.*, 1991 Pa. PUC LEXIS 80.

7. PGW's proposed CRRC mechanism is fully consistent with the wording of Sec. 1307(a) and its underlying principles. The clause permits the Company to address changes in its cash working capital resulting from collections shortfalls driven by volatile and significant natural gas costs and exacerbated by the demographics of its customer base, without the need for "the broad, costly and time-consuming inquiry" required of Sec. 1308 base rate cases. The rates resulting after application of the clause are just and reasonable, as they merely enable the Company to collect previously sanctioned rates at Commission-endorsed collections levels.

8. The record also establishes that PGW's cash receipts and collection levels satisfy the Commission's loose criteria for automatic rate treatment in that they are significant, volatile and beyond the Company's ability to control. In addition to the volatility of natural gas costs, the Company's customer demographics (including their income and poverty levels, and continued decline in real incomes) and weather-related demand for gas are clearly beyond the Company's control; the Company's broad and partially successful collections effort cannot stave off the effects of the uncontrollable variables.

APPENDIX A

9. In addition to the pro forma aspect of the CRRC mechanism, the E-factor aspect is also justified and in no manner constitutes retroactive ratemaking. Sec. 1307(e) specifically authorizes the Commission, after a 12 month period covered by an automatic adjustment clause, to permit the utility to recover amounts by which the expenses exceeded the revenues generated by the clause.

10. This Commission and the Pennsylvania Courts have on numerous occasions permitted vigilant utilities to recover extraordinary uncollectible accounts expenses that exceeded levels otherwise established in base rates. We have authorized collections in situations involving many years of past expense not otherwise authorized in rates, but justified by the particular circumstances of the case. This favorable treatment has extended to a utility seeking to recover several years' worth of customer uncollectible accounts arrearages exceeding previously established base rate allowances. *Columbia Gas of Pennsylvania, Inc. v. Pa. PUC*, 613 A.2d 74 (Pa. Cmwlth. 1992), *aff'd. per curiam* 636 A.2d 627 (1994). *Accord, Popowsky v. Pa. PUC*, 695 A.2d 448 (Pa. Cmwlth. 1997).

11. PGW's request to recover certain undercollections through an E-factor is perfectly consistent with Pennsylvania law, and in fact presents a stronger case for recovery than those allowed in other cases. PGW's request extends to current uncollectibles expense for the current fiscal year (FY 2004, which concludes on August 31 of this year).

12. Also, the special problems associated with higher gas costs and colder weather are not unique to Pennsylvania. Several jurisdictions have already addressed identical situations where utilities faced significantly decreased cash receipts as a result of much higher uncollectible accounts expense directly associated with much higher customer bills.

13. The Commissions in Ohio and Tennessee, most notably, have recently granted petitioning gas utilities relief from higher uncollectible expenses in the form of automatic adjustment clauses quite similar to the clause that PGW now seeks. Significantly, these Commissions granted this relief only after sharply contested proceedings, and over the strenuous objections of the OCA and OSBA equivalents in those states.

APPENDIX A

14. PGW's requested automatic adjustment mechanism, the CRRC, is just, reasonable and in the public interest.

CERTIFICATE OF SERVICE

I hereby certify that I have this day 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 EMAIL AND FIRST CLASS MAIL

Tanya McCloskey, Esq.
James Mullins, Esq.
Steve Keene, Esq.
Office of Consumer Advocate
5th Floor, Forum Place Bldg.
555 Walnut Street
Harrisburg, PA 17101-1921
E-mail: TmcCloskey@paoca.org
Skeene@paoca.org

Johnnie Simms, Esq.
Richard A. Kanaskie, Esq.
Office of Trial Staff
PA Public Utility Commission
P.O. Box 3265
Harrisburg, PA 17105-3265
E-mail: josimms@state.pa.us

Steven Gray, Esq.
Office of Small Business Advocate
Commerce Building, Suite 1102
300 North 2nd Street
Harrisburg, PA 17101
E-mail: sgray@state.pa.us

Richard Lelash
18 Seventy Acre Road
Redding, CT 06896
E-mail: lelash@sprintmail.com

Greg Stunder, Esquire
Philadelphia Gas Works
800 W. Montgomery Avenue
Philadelphia, PA 19122
E-mail: greg.stunder@pgworks.com

Charis Mincavage, Esquire
McNEES, WALLACE, NURICK
100 Pine Street
P.O. Box 1166
Harrisburg, PA 17108-1166
E-mail: Cmincavage@mwn.com

Philip Bertocci, Esq.
Edward A. McCool, Esq.
Community Legal Services
1424 Chestnut Street
Philadelphia, PA 19102
Fax: (215) 981-0434
E-mail: pbertocci@clsphila.org

Robert D. Knecht
Industrial Economics Incorporated
2067 Massachusetts Avenue
Cambridge, MA 02140
E-mail: rdk@indecon.com

Christopher Craig, Esq.
Senator Fumo's Office
Main Capital
Room B48
Harrisburg, PA 17120
E-Mail: ccraig@fumo.com

SECRETARY'S BUREAU

2004 JUN 14 PM 1: 20

RECEIVED

Renardo L. Hicks, Esq.
Anderson Gulotta & Hicks, PC
1110 N. Mountain Rd.
Harrisburg, PA 17112
Email: rhicks@aghweb.com

Barbara Greening, Esq.
1904 Green Street
Philadelphia, PA 19130

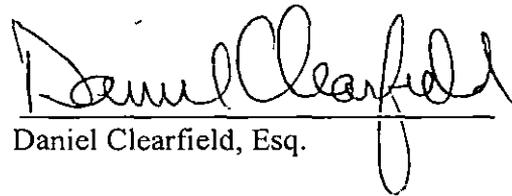
Adrienne Glenn
6342 Ardleigh Street
Philadelphia, PA 19138-1002

Edward Morrison
767 Cinnaminson Street
Philadelphia, PA 19128

Dated: June 14, 2004

Philip L. Hinerman, Esq.
Fox Rothschild LLP
2000 Market Street, 10th Fl.
Philadelphia, PA 19103-3291
E-mail: phinerman@foxrothschild.com

James P. Leonard, Esq.
Cooper Leonard & Schaffer, LLC
1525 Locust St., 13th Fl.
Philadelphia, PA 19102
E-mail: cooperleonardsch@aol.com


Daniel Clearfield, Esq.



McNees Wallace & Nurick LLC
attorneys at law

ORIGINAL

CHARIS MINCAVAGE
DIRECT DIAL: (717) 237-5437
E-MAIL ADDRESS: CMINCAVAGE@MWN.COM

June 14, 2004

James J. McNulty, Secretary
Pennsylvania Public Utility Commission
The Commonwealth Keystone Building
400 North Street, 2nd Floor
Harrisburg, PA 17120

VIA HAND DELIVERY

**DOCUMENT
FOLDER**

**Re: Pennsylvania Public Utility Commission v. Philadelphia Gas Works;
Docket Nos. R-00049157 and P-00042090**

Dear Secretary McNulty:

Enclosed please find the original and nine (9) copies of the Main Brief of the Philadelphia Industrial and Commercial Gas Users Group ("PICGUG") in the above-referenced proceeding.

As evidenced by the attached Certificate of Service, all parties to the proceeding are being served with a copy of this filing. Please date stamp the extra copy of this transmittal letter and kindly return it to our messenger for our filing purposes. Thank you.

Very truly yours,

MCNEES WALLACE & NURICK LLC

By 
Charis Mincavage

Counsel to the Philadelphia Industrial and
Commercial Gas Users Group

Enclosures

CM/lhe

c: Administrative Law Judge Charles E. Rainey (via federal express)
Certificate of Service

RECEIVED
2004 JUN 14 PM 4:06
SECRETARY'S BUREAU

120.

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

ORIGINAL

PENNSYLVANIA PUBLIC
UTILITY COMMISSION

Docket Nos. R-00049157
P-00042090

v.

PHILADELPHIA GAS WORKS

DOCKETED
JUN 16 2004

**MAIN BRIEF OF THE
PHILADELPHIA INDUSTRIAL AND COMMERCIAL
GAS USERS GROUP**

**DOCUMENT
FOLDER**

Apartment Association of Greater Philadelphia
The Building Owners' and
Managers' Association of Philadelphia
Temple University
Thomas Jefferson University/Jefferson Health Systems

RECEIVED
2004 JUN 14 PM 4: 06
SECRETARY'S BUREAU

David M. Kleppinger
Charis Mincavage
McNEES WALLACE & NURICK LLC
100 Pine Street
P.O. Box 1166
Harrisburg, PA 17108-1166
(717) 232-8000
(717) 237-5300 (fax)

Counsel for the Philadelphia Industrial
and Commercial Gas Users Group

Dated: June 14, 2004

TABLE OF CONTENTS

	<u>Page</u>
I. INTRODUCTION	1
II. ARGUMENT	3
A. PGW's Proposed CRRC Is Unjust And Unreasonable Pursuant to the Requirements of the Public Utility Code	3
B. Uncollectible Expenses Must Be Addressed Through a Base Rate Proceeding, Rather Than Through the CRRC Mechanism.....	7
C. The Commission Should Consider Other Solutions to Address PGW's Financial Concern	8
III. CONCLUSION.....	10

I. INTRODUCTION

On January 31, 2004, Philadelphia Gas Works ("PGW" or "Company") made its preliminary Gas Cost Rate ("GCR") filing with the Pennsylvania Public Utility Commission ("PUC" or "Commission"). On March 1, 2004, PGW submitted supporting testimony regarding its GCR filing. In addition, PGW filed a Petition to establish a Cash Receipts Reconciliation Clause ("CRRC"), as a companion to PGW's GCR, in order to reconcile PGW's projected and actual cash receipts with billed revenues on an on-going basis.

On February 18, 2004, the Philadelphia Industrial and Commercial Gas Users Group ("PICGUG") filed a Petition to Intervene in this proceeding. PICGUG is an ad hoc association of energy-intensive industrial and commercial customers receiving service from PGW under various rate schedules. PICGUG members use substantial volumes of natural gas in their businesses, and natural gas costs comprise a significant element of their respective costs of operation. Because a modification to PGW's GCR rates could impact PICGUG member businesses, PICGUG is an active party to this proceeding. The membership of PICGUG is listed on the cover page of this Main Brief.

On March 15, 2004, Administrative Law Judge Charles Rainey, Jr. ("ALJ Rainey") convened a Prehearing Conference, in which the procedural schedule for this proceeding was developed. Pursuant to the procedural schedule, PICGUG received Direct Testimony from the Office of Consumer Advocate ("OCA"), Office of Trial Staff ("OTS"), and Office of Small Business Advocate ("OSBA") on April 15, 2004. On April 30, 2004, PICGUG received the Rebuttal Testimony of PGW and OSBA. On April 7, 2004, PICGUG received Surrebuttal Testimony from OCA, OTS, and OSBA. Evidentiary hearings were held on May 11, 2004, for the purpose of cross-examining witnesses.

Pursuant to the revised procedural schedule and 52 Pa. Code Section 5.502,¹ PICGUG files this Main Brief to address several issues raised in this proceeding regarding PGW's proposed CRRC.² Specifically, PICGUG submits that PGW's proposed CRRC must be rejected by the Commission, as its implementation would result in unjust and unreasonable rates for customers. See Section II. A., infra. In addition, the CRRC should be reviewed, if at all, in a base rate proceeding rather than through a single-issue ratemaking process. See Section II. B., infra. Finally, the CRRC should not be implemented, if at all, without significant and substantive changes that would strengthen PGW's collection process and provide a long-term solution on PGW's fiscal problems. See Section II. C., infra. For these reasons, PICGUG respectfully requests that the Commission deny PGW's proposal to implement a CRRC mechanism.

¹ The parties requested an extension of the procedural schedule in order to provide additional time for continuing settlement negotiations. The ALJ granted this extension pursuant to the parties' request. Because settlement could not be reached, PICGUG now files this Main Brief.

² The parties filed a Joint Petition for Settlement regarding the outstanding GCR issues. Accordingly, the only issues remaining for litigation in this proceeding are related to the CRRC.

II. ARGUMENT

A. *PGW's Proposed CRRC Is Unjust And Unreasonable Pursuant to the Requirements of the Public Utility Code.*

As discussed more fully herein, PGW's proposed CRRC contains many flaws that would result in unjust and unreasonable rates for the Company's ratepayers upon implementation. For example, PGW has failed to provide any precedent for such a reconciliation mechanism. Similarly, the CRRC as proposed by PGW provides for an inappropriate and subjective retroactive collection of costs. Moreover, the CRRC could weaken any efforts by PGW to improve its collection process, especially in light of the fact that the CRRC provides for an inequitable reconciliation to the benefit of PGW and to the detriment of its ratepayers.

The purpose behind the CRRC is to allow PGW to automatically increase rates to firm sales customers whenever the Company undercollects on gas bills by more than \$55.7 million.³ According to PGW, the Company's level of uncollectible receipts has increased, which has decreased PGW's levels of cash receipts. See Petition of Philadelphia Gas Works to Establish a Cash Receipts Reconciliation Clause ("PGW Petition"), Docket Nos. R-00049157 and P-00042090 (March 1, 2004), p. 8. Because PGW is a "cash flow company," PGW claims that this reduction in cash receipts is having a substantial impact on the financial status of the Company, which could result in PGW being unable to pay its obligations due in 2004. Id. at 8-9.

Because PGW claims to have no "cushion" upon which to rely to replace these uncollected receipts, PGW proposes to implement the CRRC. To implement the CRRC, PGW would project its anticipated level of billed revenues and receipts for the twelve months beginning September 1 of each year. That amount, reduced by the \$55.7 million of *pro forma*

³ The \$55.7 million threshold is the allowance that was established in PGW's last base rate case for uncollectibles.

uncollectible expense currently contained in PGW's base rates would constitute the total gas receipts adjustment projected for the CRRC. Id. at 12. The CRRC would also establish a reconciliation for the prior year in order to bridge the gap between projected cash receipts and projected billed revenues and the actual cash receipt shortfall for the year. Id. This additional debit or credit would be added to the total CRRC charge and assigned on a per Mcf basis to all firm customers in the same manner as the GCR. Id. at 12-13.

Pursuant to the Public Utility Code, "[e]very rate made, demanded, or received by any public utility...shall be just and reasonable, and in conformity with regulations or orders of the commission." 66 Pa. C.S. § 1301. Thus, the Commission cannot permit a utility to implement rates that would be unjust and unreasonable. Because PGW's CRRC fails to meet this requirement, the Commission must deny its implementation.

First, PUC precedent provides for the recovery of uncollectible expense through base rates. The CRRC would deviate from this precedent by allowing the Company to carve out a single component of base rates (i.e., the uncollectible expense) in order to subject this expense to annual reconciliation. See OCA Statement No. 1, Direct Testimony of Richard W. Lelash (hereinafter, "OCA St. 1"), p. 15.

In addition, while PGW claims that several states have already established uncollectible adjustment mechanisms to adjust uncollectible expenses, these mechanisms are not comparable regarding their scope of recovery, relationship to customer choice programs, or associated true-up requirements. Id. at 16-17. Moreover, the other states cited by PGW have different definitions of recoverable fuel costs and regulations regarding cost recovery. Rather, the precedent set forth by the majority of states, and most importantly, Pennsylvania, provides that uncollectible expenses must be reviewed within the context of base rate proceedings. Id.

Because PGW has failed to provide any examples contrary to this precedent, implementation of PGW's CRRC would result in unjust and unreasonable rates for the Company's ratepayers.

Second, PGW's proposed CRRC would constitute retroactive ratemaking in that PGW is seeking to recover shortfall for the twelve months ended August 31, 2004. Because rates paid by PGW's customers are collected under tariff provisions, ratepayers are not currently subject to the CRRC. Unless and until the CRRC is authorized by the PUC, the CRRC is not recoverable and not subject to reconciliation. Because customers are entitled to notice and to pay only authorized rates effective from the date they are approved, PGW cannot be permitted to implement the CRRC retroactively, as this would result in unjust and unreasonable rates. See OCA Statement No. 1S, Surrebuttal Testimony of Richard W. Lelash (hereinafter, "OCA St. 1S"), p. 4.

Third, the CRRC would result in an unbalanced and inequitable reconciliation mechanism. Automatic adjustment clauses are typically limited to specifically identified expenses that are not under the control of management and are not subject to true-up mechanisms. See OCA St. 1, p. 14. Because uncollectible levels are largely within the control of PGW, the CRRC does not meet the requirements necessary for an automatic adjustment clause. Moreover, the CRRC is inequitable in that ratepayers will be charged for all undercollections that exceed \$55.7 million; however, if PGW's undercollections are less than \$55.7 million, ratepayers will not be credited for the difference. See OSBA Statement No. 1, Direct Testimony of Robert D. Knecht (hereinafter, "OSBA St. 1"), p. 25. Because of this methodology, the CRRC does not act as a reconciliation mechanism. Rather, the CRRC merely provides an insurance policy to PGW with respect to its uncollectible expenses. Because ratepayers should not be subject to such an inappropriate and inequitable mechanism, the PUC must find that PGW's CRRC would result in unjust and unreasonable rates.

Finally, implementation of the CRRC would weaken PGW's collection efforts. Under the inequitable terms of reconciliation, if PGW's collections are poor, ratepayers must pay for the shortfall. If PGW's collections are strong, PGW is able to retain the "profits." See OSBA St. 1, pp. 11-12. This lack of balance places a serious burden on PGW's ratepayers while limiting any incentive for PGW to improve its collection efforts. The number of customers with uncollectible problems may also increase due to the increase in rates stemming from the CRRC. Because more customers will be unable to pay PGW's higher rates stemming from the CRRC, when PGW increases its rates through the CRRC, PGW's overall collection rate will fall, requiring PGW to further increase its CRRC, which will then further lower the collection rate. See id. at 8.

Moreover, the CRRC could allow PGW to "game" the system. In an instance in which PGW's collection rate is below the "target" but PGW expects a better collection rate in the next year, PGW could have an incentive to not collect bills in the first year because it can recover the undercollections through the CRRC reconciliation mechanism and then aggressively collect bills in the following year when the Company is allowed to retain the cash. Id. at 26.

In light of PGW's history of poor performance with respect to its collectibles, PGW should be required to undertake provisions that will require the Company to more effectively and efficiently lower its uncollectible expense. Providing for an automatic recovery of these expenses would remove any incentive by PGW to pursue a course of action that would improve the Company's uncollectibles. See OCA St. 1, p. 16.

Because of the problems inherent in the CRRC, including the lack of precedent, inappropriate retroactivity, and the inequitable reconciliation, implementation of this mechanism would result in unjust and unreasonable rates for PGW's ratepayers. For these reasons, the PUC must reject the CRRC.

B. Uncollectible Expenses Must Be Addressed Through a Base Rate Proceeding, Rather Than Through the CRRC Mechanism.

As part of its Petition, PGW claims that the effect of volatile natural gas costs on the Company is "uniquely and especially severe" due to PGW's status as a cash flow company. PGW Petition, p. 8. As a cash flow company, PGW claims that the continuing drop-off in cash receipts is having a substantial impact on the financial status of the Company, including PGW's plans for another long-term bond sale in 2004. *Id.* at 9. For that reason, PGW proposes to implement the CRRC to respond to PGW's immediate financial needs without requiring a base rate proceeding. *Id.* at 2.

PGW is correct in that the Company is regulated on a cash flow basis, with its base rates set in order to meet its expenses and cash working requirements. PGW chose to be a cash flow regulated company and supported such regulation to the Commission. Under such a regulatory framework, the appropriate mechanism to address cash flow problems is in a base rate proceeding. As such, any cash flow deficiencies should be addressed within a base rate proceeding or the PUC's overall regulatory oversight will be negated. Because the CRRC would address the Company's deficiencies outside the context of a base rate proceeding, the PUC's regulation of the Company would be disrupted. OCA St. 1, pp. 13-14.

Within the context of a base rate proceeding, the PUC is able to review all elements of a utility's costs and expenses. Through this methodology, the PUC can review an increase in one area while examining whether a resulting decrease in another area acts as an offset. Conversely, the CRRC allows rates to reflect increases in costs in one particular area without recognizing any offsetting reduction in costs that may occur in other areas. *See* OSBA St. 1, p. 11. Because the CRRC does not provide for the detailed scrutiny of a utility's costs that normally occurs in a base rate proceeding, the CRRC should not be implemented in this proceeding.

Moreover, by addressing PGW's collection issues as part of a base rate proceeding, the PUC retains the oversight necessary to ensure that PGW's customers are receiving just and reasonable rates. The use of the CRRC, however, effectively provides PGW with a blank check that ultimately nullifies regulatory oversight by the PUC. See OCA St. 1S, p. 3. Because the PUC has already indicated its willingness to maintain the financial integrity of PGW by providing numerous base rate increases over the past four years, any concerns raised by PGW can be adequately addressed through a base rate proceeding. See id. at 3-4.

Accordingly, because PGW's concerns regarding uncollectible expenses should be addressed in a base rate proceeding, the PUC must reject PGW's proposal and indicate that PGW must file a base rate proceeding if it seeks to address the CRRC issue further.

C. The Commission Should Consider Other Solutions to Address PGW's Financial Concerns.

Throughout the course of this proceeding, PGW has argued that the Company's financial concerns require implementation of the CRRC. For example, PGW has submitted that the CRRC is an attempt to deal "with just one aspect of PGW's overall financial crisis" and that finding a solution to PGW's "financial crises is essential or, the results will be catastrophic for this Company, its employees and, most importantly, its customers." See PGW Statement No. 5, Rebuttal Testimony of Thomas Knudsen (hereinafter, "PGW St. 5"), pp. 2, 4. In addressing these concerns, however, the Commission should seek alternative solutions that would fully address PGW's underlying issues.

For example, the CRRC is just one aspect of PGW's financial crisis. PGW has filed and received numerous base rate increases since the PUC obtained jurisdiction over the Company in 2000, based, in part, on claims by PGW that the Company was facing significant financial issues. Accordingly, PGW's long-standing financial limitations are well known. See OCA St. 1S, p. 7.

In fact, PGW has submitted that the Company has made improvements in its collection process over that past few years, thereby suggesting that PGW's problems are due to liquidity issues rather than collection issues. Id. Accordingly, the CRRC will not address PGW's inherent financial problems nor provide a long-term solution. Rather, the CRRC may do nothing more than place a temporary band-aid over these issues until PGW returns to the PUC requesting additional funding from ratepayers to ensure financial viability. Because ratepayers should not be held accountable for PGW's fiscal problems, the PUC must examine a long-term solution to PGW's issues, rather than implementing an inappropriate and inequitable temporary process.

Similarly, PGW should be required to strengthen its collection process, if, as PGW suggests, the collection problems are to blame for these issues. Unfortunately, the CRRC could result in an increase in the bills of customers currently paying their bills and, thus, rendering these customers unable to pay their bills prospectively. In turn, PGW's uncollectibles will increase while a smaller portion of the Company's ratepayers will continue to shoulder the burden of the Company's fiscal problems. See OSBA St. 1, pp. 17-18. The only way in which to prevent these spiraling problems is for PGW to undertake the necessary steps to improve its collection process. Because the CRRC would only weaken PGW's incentive to improve its collection process, implementation may be especially inappropriate. See Section II., A. supra.

Because of PGW's inherent financial problems, the PUC must look to long-term solutions that will address all of PGW's fiscal concerns rather than allowing the Company to implement a temporary process that would, at best, result in inappropriate and inequitable treatment of the Company's customers and, at worst, exacerbate the problem by adding more customers to those who cannot pay their bills currently. Only by permanently addressing PGW's concerns can the PUC ensure that PGW's financial problems are resolved.

III. CONCLUSION

PGW's proposed CRRC would result in unjust and unreasonable rates in direct contradiction to the requirements set forth in the Public Utility Code. Specifically, the CRRC would contravene PUC precedent, apply retroactive ratemaking, allow for an inequitable reconciliation, and weaken PGW's incentive to improve its collections program. Moreover, if PGW seeks to address its collection issues, the Company should be required to do so as part of a base rate proceeding, which would allow the Commission to account for all issues related to PGW's collection problems, as well as ensure that the PUC retains the necessary regulatory oversight. Finally, in order to ensure a long-term solution to PGW's financial problems, the Commission should examine other avenues by which to resolve these problems, including reviewing PGW's liquidity problems and requiring PGW to strengthen its collection process.

WHEREFORE, the Philadelphia Industrial and Commercial Gas Users Group respectfully requests that the Pennsylvania Public Utility Commission reject Philadelphia Gas Works' request to implement a Cash Receipts Reconciliation Clause.

Respectfully submitted,

McNEES WALLACE & NURICK LLC

By Charis Mincavage

David M. Kleppinger
Charis Mincavage
100 Pine Street
P.O. Box 1166
Harrisburg, PA 17108-1166
Phone: (717)232-8000
Fax: (717)237-5300

Counsel to the Philadelphia Industrial and
Commercial Gas Users Group

Dated: June 14, 2004

CERTIFICATE OF SERVICE

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

VIA E-MAIL AND HAND DELIVERY

Johnnie Simms, Esq.
Office of Trial Staff
Pennsylvania Public Utility Commission
The Commonwealth Keystone Building
400 North Street
Harrisburg, PA 17120
josimms@state.pa.us

Christopher B. Craig, Esq.
Senate Democratic Appropriations
Committee
Room 545, Main Capitol Building
Harrisburg, Pennsylvania 17120
ccraig@fumo.com

Stephen Keene, Esq.
Office of Consumer Advocate
555 Walnut Street, Forum Place - 5th Fl.
Harrisburg, PA 17120
skeene@paoca.org

Steven C. Gray, Esq.
Office of Small Business Advocate
Suite 1102, Commerce Building
300 North Second Street
Harrisburg, PA 17101
sgray@state.pa.us

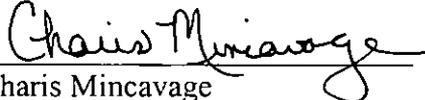
Daniel Clearfield, Esq.
Wolf, Block, Schorr and Solis-Cohen LLP
212 Locust Street
Suite 300
Harrisburg, PA 17101
dclearfield@wolfblock.com

RECEIVED
2004 JUN 14 PM 4:06
SECRETARY'S BUREAU

VIA E-MAIL AND FEDERAL EXPRESS

Philip L. Hinerman, Esq.
Fox Rothschild LLP
2000 Market Street 10th Floor
Philadelphia, PA 19103-3291
phinerman@foxrothschild.com

Philip A. Bertocci, Esq.
Community Legal Services, Inc.
1424 Chestnut Street, 3rd Floor
Philadelphia, PA 19102
pbertocci@clsphila.org


Charis Mincavage

Dated this 14th day of June, 2004, in Harrisburg, Pennsylvania.

COMMONWEALTH OF PENNSYLVANIA



OFFICE OF CONSUMER ADVOCATE

555 Walnut Street, 5th Floor, Forum Place
Harrisburg, Pennsylvania 17101-1923
(717) 783-5048
800-684-6560 (in PA only)

IRWINA. POPOWSKY
Consumer Advocate

FAX (717) 783-7152
consumer@paoca.org

June 14, 2004

James J. McNulty, Secretary
PA Public Utility Commission
400 North Street
Keystone Building
Harrisburg, PA 17105-3265

DOCUMENT
FOLDER

ORIGINAL

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 Main 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)
79748.doc

SECRETARY'S BUREAU
2004 JUN 14 PM 4:07
RECEIVED

22

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

ORIGINAL

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

DOCKETED
JUN 16 2004

OFFICE OF CONSUMER ADVOCATE'S
MAIN BRIEF

**DOCUMENT
FOLDER**

Stephen J. Keene
Senior Assistant Consumer Advocate
Aron J. Beatty
Lori A. Herman
Assistant Consumer Advocates

Counsel for:
Irwin A. Popowsky
Consumer Advocate

Office of Consumer Advocate
555 Walnut Street, Forum Place, 5th Floor
Harrisburg, PA 17101-1923
(717) 783-5048

Dated: June 14, 2004

RECEIVED
2004 JUN 14 PM 4: 07
SECRETARY'S BUREAU

TABLE OF CONTENTS

I.	INTRODUCTION	1
II.	STATEMENT OF THE CASE.....	2
III.	BURDEN OF PROOF	4
IV.	ARGUMENT.....	7
A.	Introduction.....	7
B.	The Record In This Proceeding Demonstrates That There Is No Need For The CRRC.....	9
1.	Introduction.....	9
2.	The Company Will Finish The Current Fiscal Year With More Cash Than In Any Of The Past Four Years.	11
3.	PGW Has Not Demonstrated That It Needs Rate Relief In Order To Avoid A Further Decrease In Its Bond Ratings.	12
4.	The Company’s Collection Renewal Initiative Should Be Given Time To Improve Collections Before Rate Relief Is Considered.....	14
C.	The Proposed CRRC Is Contrary To Established Commission Precedent With Respect To Recovery Of Uncollectible Expense.....	15
1.	Uncollectible Expense Does Not Lend Itself To Recovery Through An Automatic Adjustment Mechanism.	16
2.	The Proposed CRRC Constitutes Impermissible Single-Issue, Retroactive Ratemaking.	17
a.	The CRRC Proposal Constitutes Single-Issue Ratemaking.....	17
b.	The CRRC Proposal Constitutes Impermissible Retroactive Ratemaking.	18
3.	The Proposed CRRC Would Reduce The Incentive For PGW To Maximize Its Collections.	21
D.	The Precedent From Other States Cited By PGW Is Distinguishable From The Instant Case And Should Not Be Followed By The Pennsylvania Public Utility Commission.	22

E.	The Proposed CRRC Will Result In Unjust and Unreasonable Natural Gas Bills For Many PGW Customers.....	25
1.	The Proposed CRRC Will Raise PGW’s Rates Even Higher And Result In Rates That Are Unjust, Unreasonable and Unaffordable.....	25
2.	Public Input Testimony Demonstrates Overwhelming Opposition To PGW’s Proposed CRRC.....	28
a.	Introduction.....	28
b.	Testimony of Philadelphia Public Officials.....	29
c.	Testimony of PGW Customers.....	35
F.	The Office of Trial Staff’s Alternative Proposal Is Also Flawed.	40
V.	CONCLUSION.....	42
Appendix A - In the Matter of the Joint Application of The East Ohio Gas Company d.b.a. Dominion Eat Ohio, Columbia gas of Ohio Inc., Vectren Energy Delivery of Ohio, Northeast Ohio natural Gas Corp., and Oxford Natural gas Company for Approval of an Adjustment Mechanism to recover Uncollectible Expenses. Case No.03-1127-GA-UNC.		
Appendix B - In the Matter of Application of Piedmont Natural gas Company, Inc., for Approval of Special Accounting Procedures. Docket No.G-9, SUB 453.		
Appendix C - Proposed Findings of Fact and Proposed Conclusions of Law		
Appendix D - Proposed Ordering Paragraph		

TABLE OF AUTHORITIES

Cases

<u>Barasch v. Pa.P.U.C.</u> , 507 Pa. 496 A.2d 94 (1985)	17
<u>Berner v. Pa. P.U.C.</u> , 382 Pa. 622, 116 A.2d 738, (1955)	5
<u>Brockway Glass v. Pa. P.U.C.</u> , 63 Pa. Comwlth. 238, 437 A.2d 1067 (1981).....	5
<u>Cheltenham & Abington Sewerage Co. v. Pa.P.U.C.</u> , 344 Pa. 366, 25 A.2d 334 (1942)	17
<u>In the Matter of Application of Piedmont Natural Gas Company, Inc., for Approval of Special Accounting Procedures, North Carolina Utility Commission, Docket No. G-9, Sub 453 (Order entered November 7, 2001)</u>	22
<u>In the Matter of the Joint Application of The East Ohio Gas Company d.b.a. Dominion East Ohio, Columbia Gas of Ohio, Inc., Vectren Energy Delivery of Ohio, Northeast Ohio Natural Gas Corp., and Oxford Natural Gas Company for Approval of an Adjustment Mechanism to Recover Uncollectible Expenses, Public Utilities Commission of Ohio, Case No 03-1127-GA-UNC (Dec. 17, 2003)</u>	20
<u>Lower Frederick Twp. v. Pa. P.U.C.</u> , 48 Pa. Comwlth. 222, 409 A.2d 505 (1980)	5
<u>National Fuel Gas Dist. Corp. v. Pa.P.U.C.</u> , 76 Pa. Comwlth. 102, 464 A.2d 546 (1983)	16
<u>Pennsylvania Industrial Energy Coalition v. Pa.P.U.C.</u> , 653 A.2d 1336 (Pa.Comwlth. 1995)....	16
<u>Philadelphia Elec. Co. v. Pa.P.U.C.</u> , 93 Pa.Comwlth 410, 502 A.2d 722 (1985).....	16, 17, 18
<u>Popowsky v. Pa.P.U.C.</u> , 164 Pa.Comwlth 338, 343, 642 A.2d 648 (1994).....	17, 18
<u>Popowsky v. Pa.P.U.C.</u> , 543 Pa. 733, 673 A.2d 338 (1996).....	17
<u>University of Pennsylvania v. Pa. P.U.C.</u> , 86 Pa. Comwlth. 410, 485 A.2d 1217 (1984).....	5

Administrative Decisions

<u>In Pa. P.U.C. v. National Fuel Gas Dist. Corp.</u> , 83 Pa.P.U.C. 262 (1994)	5
<u>Investigation Into Financial and Collections Issues Regarding the Philadelphia Gas Works, Docket Nos. P-00042090, R-00049157, M-00021612, P-00032061 (Order entered June 2, 2004)</u>	3
<u>Pa.P.U.C. v. Equitable Gas Co.</u> , 57 Pa.P.U.C. 423 (1983).....	5

Pa.P.U.C. v. Pennsylvania Telephone Ass'n., Docket No. P-00981397, 2001 WL 1002753
Pa.P.U.C., *8 (Order entered June 8, 2001) 6

Pa.P.U.C. v. Philadelphia Gas Works, Docket No. R-00017034 (August 8, 2002) 21, 37

Statutes

52 Pa.Code. §53.64 2

66 Pa. C.S. §1308(b) 4, 6

66 Pa.C.S. §1307(f) 2

66 Pa.C.S. §315(a) 4, 6

I. INTRODUCTION

This case involves a request by the Philadelphia Gas Works ("PGW") to implement a first of its kind surcharge mechanism to reconcile uncollectible expense. The surcharge, called the Cash Receipts Reconciliation Clause ("CRRC"), would allow PGW to recover any difference between its actual experienced uncollectible expense and the uncollectible expense rate allowance authorized in PGW's last fully-litigated base rate case in 2001. The OCA submits that PGW's proposal is contrary to basic ratemaking principles and represents unsound public policy. The CRRC should be flatly rejected.

The Company's CRRC proposal has met with unanimous condemnation from ratepayers, consumer groups, state legislators and local officials. No one other than the Company has expressed support for the proposed CRRC. PGW claims that it needs the CRRC mechanism as a back-stop or insurance policy against uncollectible expense. The Company claims that it needs the CRRC in place in order to be able to sell a new issue of capital bonds this coming fall. However, the Company's own financial projections demonstrate that the Company will finish the current fiscal year on August 31, 2004 with between \$31 million to \$36 million in cash. That is more cash on hand than it has had at year end in any year since the Company came under the Commission's jurisdiction in 2000.

Furthermore, PGW's own collections initiative that it has undertaken has produced encouraging results and the Company is already displaying improved collection rates. The Company has reported to the Philadelphia Gas Commission that it expects to finish the current year with a 94% collection rate. That is higher than the 92% collection rate that was utilized in setting PGW's uncollectible expense in the last fully-litigated base rate case. If the

Company continues to collect billed revenues at this rate, the CRRC proposal is not only a terrible ratemaking precedent, but it is completely unnecessary.

II. STATEMENT OF THE CASE

On March 1, 2004, PGW submitted its annual Gas Cost Rate filing (“GCR”) in accordance with Section 1307(f) of the Public Utility Code, 66 Pa.C.S. §1307(f), and the regulations of the Public Utility Commission (“Commission” or “PUC”) at 52 Pa.Code. §53.64 *et.seq.* Concurrently, PGW filed a *Petition to Establish a Cash Receipts Reconciliation Clause* (“Petition”). In its CRRC Petition, the Company seeks to establish a mechanism to reconcile actual uncollectible expense to the allowance for uncollectible expense that the Company claims that it recovers through base rates. Initially, PGW proposes that the CRRC recover \$47 million in additional revenues. Petition at 13. The \$47 million dollars is made up of two components: (1) \$35.2 million for a projected shortfall in cash receipts for FY2005 [September 1, 2004 - August 31, 2005] and (2) \$11.4 million representing a three-year amortization of a \$34.3 million claimed shortfall in cash receipts for FY2004 [September 1, 2003 - August 31, 2004]. The total of these two components equals an initial proposed CRRC of \$46.7 million. PGW St. CRRC-1 at 11-12.

On the same date that it filed the CRRC Petition, the Company also filed a *Motion for Consolidation* (“Motion”), seeking to consolidate the CRRC Petition proceeding with this year’s 1307(f) proceeding. The OCA filed an Answer to the Motion opposing consolidation of the Petition proceeding. At the Prehearing Conference on March 16, 2004, the Motion for Consolidation was granted by Administrative Law Judge Charles E. Rainey, Jr. (“ALJ”).

On April 13, 2004, the OCA filed the Direct Testimony of Richard W. LeLash on the proposed CRRC and other purchased gas cost issues. Other parties filing testimony included

the Office of Trial Staff (“OTS”) and the Office of Small Business Advocate (“OSBA”). PGW filed Rebuttal Testimony on May 3, 2004. A Public Input Hearing was held in Northeast Philadelphia on May 5, 2004. Additional Public Input Hearings were held in Center City Philadelphia on May 6, 2004. The OCA filed its Surrebuttal Testimony on May 7, 2004. A Technical Evidentiary Hearing was held on May 11, 2004. An additional Public Input Hearing was held on May 20, 2004 in Northeast Philadelphia. Prior to the Evidentiary Hearings, the parties were able to reach a stipulation on the contested purchased gas cost issues. A proposed settlement of these issues was submitted to the ALJ on May 28, 2004.

Thereafter, on June 2, 2004, the Commission entered an Order launching an investigation into financial and collections issues regarding the PGW. Investigation Into Financial and Collections Issues Regarding the Philadelphia Gas Works, Docket Nos. P-00042090, R-00049157, M-00021612, P-00032061 (Order entered June 2, 2004)(“June 2 Order”). The June 2 Order consolidated several outstanding proceedings, including: the instant CRRC Petition, PGW’s annual GCR proceeding pursuant to Section 1307(f) of the Public Utility Code, PGW’s Petition for approval of a means-tested Senior Citizen Discount (“SCD”) and the issues described in the Commission’s Secretarial Letter dated May 14, 2004 at Docket No. M-00021612 pertaining to several tariff issues remaining from PGW’s compliance tariff in its restructuring proceeding. June 2 Order at 3-4.

The June 2 Order consolidated these dockets and opened an investigation into issues surrounding PGW’s financial conditions and collections efforts. In particular, those issues set for investigation include:

- (1) adequacy, cost effectiveness and management of PGW’s collection practices;

- (2) whether PGW is entitled to any requested waivers and/or modifications to the Commission's Chapter 56 regulations;
- (3) the reasonableness of implementing a means-tested Senior Citizen Discount program;
- (4) tariff issues arising out of PGW's compliance filing in its restructuring proceeding at Docket No. M-00021612; and
- (5) level of PGW's universal service costs as well as the cost effectiveness, program designs and management of these programs.

June 2 Order at 4-5.

The June 2 Order provides for three separate decisions from the Commission. First, the ALJ will issue a separate Recommended Decision on the GCR issues that will be reviewed by the Commission in accordance with the statutory deadline set forth in Section 1307(f). The Commission also dispensed with the preparation of a Recommended Decision on the CRRC issue and directed that the record on this issue be certified to the Commission for a decision at the Public Meeting of July 8, 2004. Finally, the remaining issues will be part of the larger investigation and will be placed on a procedural schedule that will conclude with a Commission decision at its Public Meeting of September 30, 2004. July 2 Order at 6.

In accordance with the ALJ's Prehearing Order dated May 20, 2004 and the Commission's July 2 Order, the OCA herein files its Main Brief in opposition to the Company's CRRC Petition. The OCA opposes establishment of such a reconciliation mechanism and, for the reasons set forth below, the OCA submits that PGW's CRRC Petition should be denied.

III. BURDEN OF PROOF

The burden of proof to establish the justness and reasonableness of every element of a public utility's rate increase request rests solely upon the public utility in all proceedings under Section 1308(b) of the Public Utility Code. 66 Pa. C.S. §1308(b). The standard to be met by the public utility is set forth at Section 315(a) of the Public Utility Code:

Reasonableness of rates. -- In any proceeding upon the motion of the Commission, involving any proposed or existing rate of any public utility, or in any proceeding upon complaint involving any proposed increase in rates, the burden of proof to show that the rate involved is just and reasonable shall be upon the public utility.

66 Pa.C.S. §315(a).

The Commonwealth Court in reviewing Section 315(a) interpreted the utility's burden of proof in rate proceedings as follows:

Section 315(a) of the Public Utility Code, 66 Pa.C.S. §315(a), places the burden of proving the justness and reasonableness of a proposed rate hike squarely on the public utility. It is well-established that the evidence adduced by a utility to meet this burden must be substantial.

Lower Frederick Twp. v. Pa. P.U.C., 48 Pa. Comwlth. 222, 226-27, 409 A.2d 505, 507 (1980) (emphasis added); *see also* Brockway Glass v. Pa. P.U.C., 63 Pa. Comwlth. 238, 243, 437 A.2d 1067, 1070 (1981).

In rate proceedings, it is well-established at the Commission and in the courts that the burden of proof does not shift to parties challenging a requested rate increase. Rather, the utility's burden of establishing the justness and reasonableness of every component of its rate request is an affirmative one and that burden remains with the public utility throughout the course of the rate proceeding. The courts have held that there is no similar burden placed on

other parties to justify a proposed adjustment to the Company's filing. The Pennsylvania Supreme Court has stated:

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

Berner v. Pa. P.U.C., 382 Pa. 622, 631, 116 A.2d 738, 744 (1955).

The Commission has also addressed this standard in its rate determinations:

The Respondent, Equitable, has the burden of persuasion in the issue of the reasonableness of an expense level. Respondent must affirmatively establish, on the record, that the test year claim is a reasonable and appropriate amount.

Pa.P.U.C. v. Equitable Gas Co., 57 Pa.P.U.C. 423, 471 (1983); *accord*, University of Pennsylvania v. Pa. P.U.C., 86 Pa. Comwlth. 410, 426-27, 485 A.2d 1217, 1226 (1984). The Commission has continued to affirm the utility's burden of proof in base rate proceedings. In Pa. P.U.C. v. National Fuel Gas Dist. Corp., 83 Pa.P.U.C. 262, 266-67 (1994), the Commission stated:

... This matter is a general rate increase pursuant to Section 1308(d) of the Public Utility Code, and we, therefore, agree with the citations of ALJ Kashi and his discussion which placed the burden of establishing the justness and reasonableness of all components of the requested rate increase on the Company. See Section 315(a) of the Public Utility Code, 66 Pa.C.S. §315(a).

Id. at 267. The Commission has applied the same standard to non-general base rate proceedings:

To the extent the OCA filed a Formal Complaint, within the time directed by this Commission, pursuant to our discretion relating to non-general rate changes (66 Pa. C.S. § 1308(b)), it is entitled to have the PTA Companies proceed with the burden of proof.

Pa.P.U.C., *8 (Order entered June 8, 2001).

The OCA submits that, while it has advanced more than a reasonable basis for the recommendations presented by its witness, it remains incumbent upon PGW to affirmatively prove the justness and reasonableness of its proposed CRRC, including the retroactive recovery of historic uncollectible expense, in this proceeding.

IV. ARGUMENT

A. Introduction

Through its CRRC Petition, PGW seeks to implement a first of its kind mechanism in Pennsylvania to reconcile uncollectible expense. The OCA submits that this proposal is unjust and unreasonable in that it seeks to change the way that uncollectible expense has been traditionally treated by the Commission and by the Philadelphia Gas Commission. The proposed CRRC represents a material deviation from the long established precedent for PGW and all Pennsylvania utilities of recovering bad debt expense through base rates. The establishment of a CRRC would constitute impermissible, single-issue ratemaking. Automatic base rate expense adjustments should not be allowed since they fail to recognize the myriad of other expense decreases or revenue increases that may also occur in between base rate cases.

Moreover, such an automatic adjustment clause removes incentives for the Company to limit its level of bad debt expense or pursue proper credit and collection activities. Better uncollectible recovery procedures, more effective gas price hedging strategies, and greater education and enrollment for budget billing plans can all effectively reduce bad debt expense as

they do for other gas distribution companies. The OCA does not dispute that PGW faces challenges in its service territory as gas prices rise and PGW's rates become less affordable for the citizens of Philadelphia. But, imposition of this clause does nothing to incentivize the Company to manage other aspects of its costs and collections. It simply compounds the unaffordability of PGW's rates.

The OCA also submits that a CRRC such as the one proposed by the Company is speculative and subject to manipulation. For instance, in developing a claim for uncollectible expense in a base rate case, PGW sets an allowance for uncollectibles based on a collectibility study. Thus, bad debt expense is a forward-looking estimate determined by the collectibility study. Since it is an estimate, bad debt expense is not a reconcilable amount. Reconciliation mechanisms do not lend themselves to reconciling an estimate with a later estimate. Generally, reconciliation mechanisms reconcile estimated costs with actual, experienced costs. The OCA submits that it would be improper to reconcile one estimate with another estimate. Furthermore, the baseline uncollectible expense allowance that PGW proposes using for calculating its CRRC is from PGW's 2001 base rate proceeding at Docket No. R-00006042. Petition at 6, 13. However, since that case, PGW has been in for another base rate proceeding – done in conjunction with its filing for Extraordinary Rate Relief – in which it was authorized to increase its base rate revenues by \$36 million and was granted a Weather Normalization Adjustment (“WNA”). The OCA submits that it is impossible to determine exactly what the rate allowance is for uncollectible expense in PGW's current rates. To use the uncollectible allowance from the 2001 base rate proceeding to form the baseline, as PGW does in its CRRC filing, assumes that none of the rate increase authorized in the 2002 base rate case was attributed to increased uncollectible expense. The OCA submits that this is unreasonable.

It has also become apparent during the course of this proceeding that PGW's financial condition is not as perilous as the Company contends in its Petition. In fact, PGW's own updated cash flow analysis demonstrates that the Company will have between \$31 million and \$36 million of cash on hand at the end of FY2004 on August 31, 2004. This amount is greater than any of the Company's year-end cash reserves in any year since the Commission assumed jurisdiction over PGW. Given the improvement in collections and the updated cash forecasts for the Company, the OCA submits that PGW does not need the extraordinary remedy it has requested at this time.

Finally, there was extensive public input testimony at the four scheduled public input hearings. It is clear from this testimony that PGW customers are already struggling to pay increased natural gas bills in light of the recent base rate increases and increases in natural gas costs. To further burden these customers with a CRRC will simply make bills largely unaffordable for many people and cause many more PGW customers to fall into arrears. Imposing an additional surcharge on customers already struggling to faithfully pay their bills was seen as fundamentally unfair. Hundreds of people turned out at the hearings in person. Literally thousands of signatures were gathered on petitions in opposition to the proposed CRRC. A very real possibility exists that if this surcharge is approved, the public response would be such that there could be even worse results for the Company's collections. The message at the public input hearings was loud and clear. PGW's customers are angry about the Company's proposed CRRC and many people simply cannot pay it.

B. The Record In This Proceeding Demonstrates That There Is No Need For The CRRC.

1. Introduction

Once again PGW comes to the Commission under the cloak of a financial crisis and seeks an extraordinary regulatory response in order for it to survive its "precarious financial position." Petition at 2. PGW claims that this situation is the result of extraordinarily high natural gas costs that have left customers with an inability to pay. PGW claims that it is experiencing a cash flow crisis due to a drop off in collections over the past 18 months. Petition at 1. In its Petition, the Company states that the "cash collection shortfalls that PGW is experiencing is robbing PGW of cash working capital that is crucial to avoid a financial crisis." Petition at 2.

PGW's senior revenue bonds were also recently downgraded by Standard & Poor's ("S&P") to BBB- from BBB+ PGW CRRC-5, e. Exh. TEK-2. In its April 9, 2004 report, S&P cited PGW's "weakened liquidity position and declining credit measures fueled by collection rates that deteriorated appreciably in the last year" as the reason for the downgrade. POW CRRC-5, TEK-1 at 1. Fitch Rating's also downgraded PGW's bonds to BBB- on April 23, 2004. The Company claims that these reports are indicative of the rating agencies warning that PGW will be downgraded further if PGW's collection rates and cash margins do not improve. PGW St. CRRC-5 at 8.

As a result of these actions, and PGW's collections ineffectiveness during the last 18 months, PGW's solution is to propose the CRRC. The Company has proposed that its uncollectibles expense in base rates should be assumed to be set at the same level as in its last fully litigated base rate case and that it be allowed to bill through the CRRC for any receipts deficiency above that base rate level. Petition at 12-13.

The OCA submits that the CRRC proposal is not a reasonable way to address the Company's uncollectibles and cash flow problems. OCA St. 1 at 13-14. OCA witness LeLash

described why cash flow issues for a Company such as PGW should not be addressed through such a reconcilable mechanism:

As a first observation, the Company is regulated on a cash flow basis. As such, its base rates are set in order to meet its expenses and cash working capital requirements under its bond covenants. Under such a regulatory framework, the logical and appropriate mechanism to address cash flow problems is in a base rate proceeding. Its cash flow method of setting base rates is not a framework that was imposed by the Commission upon the Company, rather it was sought and supported by the Company itself. As such, any cash flow deficiencies should be addressed within a base rate case context or its overall regulatory oversight will be negated. Cash flow deficiencies addressed outside the base rate setting process on an ad hoc basis disrupts the regulation of this Company given its cash flow method of setting rates.

OCA St. 1 at 14.

Therefore, if PGW needs to address its cash flow and cash working capital problems, it should do so within the context of a base rate case. To simply isolate one item of expense that has increased since the last rate case and seek to implement a surcharge to recover that increase as a means of stirring up additional cash working capital violates sound ratemaking tenets.

Furthermore, as demonstrated in the Company's rebuttal case, it appears as though the Company's ongoing collections initiative is having a positive impact on PGW's collections rate already, even though it has only been in place a short while. In addition, since the Petition was filed, the City of Philadelphia has agreed to grant back the \$18 million annual City Payment for each of the next five years. That is a \$90 million injection of cash into the Company over the next five years. With the updated collections forecast and the grant back of the City Payment, the Company projects to end the current fiscal year on August 31, 2004 with between \$31 million to \$36 million in cash reserves. PGW St. CRRC-1R, Sch. JRB-10; Tr. 323.

That is more cash on hand than the Company experienced in any of the past four years. Action Alliance Cross-Exam. Exh. 1. Therefore, the Company's claimed financial crisis as a basis for implementation of an unprecedented uncollectibles surcharge mechanism simply rings hollow.

2. The Company Will Finish The Current Fiscal Year With More Cash Than In Any Of The Past Four Years.

As PGW witness Bogdonavage testified at the hearings, under current projections, the Company expects to finish the fiscal year on August 31, 2004 with between \$31-36 million of cash reserves. PGW St. CRRC-1R, Sch. JRB-10; Tr. 323. This is more cash on hand at year-end than PGW has experienced in any of the past four years. The past four years, PGW finished with the following amount of cash reserves at year-end:

Fiscal Year Ending	Cash Reserves \$\$ million
August 31, 2003	0.1
August 31, 2002	6.0
August 31, 2001	1.7
August 31, 2000	8.4

Source: Action Alliance Cross-Exh. 1.

In its latest forecasts, PGW projects that it will finish with \$36 million of cash at the end of the current fiscal year if it can achieve a 93% collection rate. PGW St. CRRC-1R, Sch. JRB-10 at 1. Even if its collection rate only reaches 90.5% the Company will end the year with \$31 million of cash. PGW St. CRRC-1R, Sch. JRB-10; Tr. 323. While these cash levels reflect the grant back of the \$18 million City Payment, even if the City Payment was backed out,

the Company would conclude the year with between \$13 million and \$18 million – a level higher than in any recent years.

The OCA submits that these projections demonstrate that with improved collections and cooperation from the City, that PGW does not have to turn to its ratepayers and seek additional rate relief at this time.

3. PGW Has Not Demonstrated That It Needs Rate Relief In Order To Avoid A Further Decrease In Its Bond Ratings.

The Company claims that in spite of the improvement in its year-end cash forecasts, 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. 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.

Instead, the best evidence in the record as to the rating agencies' intent is the actual S&P and Fitch reports. An examination of the rating agencies' reports does not indicate any specified required level of cash liquidity at year's end. Instead, the focus of the S&P report seems to be on PGW's collection practices 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. Id. at 1-2. Since then, the forecasts have improved due to improved collections efforts and the City's agreement to grant back the \$18 million City Payment.

PGW witness Bogdonavage testifies that even if PGW's liquidity improves it needs to implement the CRRC as a "backstop" or "fail safe." PGW St. CRRC-1R at 5. The OCA submits that imposing such a surcharge as a backstop to already high rates would be unprecedented. OCA witness LeLash testified about the significance of this update to the Company's forecasts:

Based on these projections, the Commission might well ask why the Company is seeking what amounts to an extraordinary recovery mechanism by proposing a CRRC. Mr. Bogdonavage answers this question on page 3 of his testimony when he states, "Even if PGW were able to improve its collections performance to those levels, it will not have sufficient end of year cash to maintain an investment grade bond rating ..." The issue is not really about cash receipts, it is about PGW's bond ratings and financial profile. Even with a projected year end cash balance of \$31-36 million, Mr. Bogdonavage is of the opinion that the rating agencies are looking for about \$60 million in end of year liquidity. Mr. Bogdonavage fails to mention though that the CRRC will not provide any added liquidity in the current fiscal year, since the proposed mechanism would not start to collect the surcharge until September 1, 2004 – the beginning of the next fiscal year. Rather, with the current year end cash balance, Mr. Bogdonavage characterizes the CRRC as a "back stop" or "fail safe" for PGW.

OCA St. 1S at 3.

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 recovery reasonable operating expenses and meet its bond coverages. There is nothing that requires the Commission to install an additional "backstop" to this process.

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.

4. The Company's Collection Renewal Initiative Should Be Given Time To Improve Collections Before Rate Relief Is Considered.

In June 2003, PGW realized that it was experiencing a significant decline in collections in comparison to its historic 10-year average of 92%. PGW St. CRRC-3 at 2. For the fiscal year ending August 2003, PGW had a collections rate of 86.57% of revenues billed. PGW St. CRRC-1, JRB-1. The Company's five year average for the five years ending August 2003 was 91.85%. Id.

As a result of this decline in collections, in November 2003, PGW launched its Collection Renewal Initiative ("Collections Initiative"). The Collections Initiative has a two-tiered approach to improve collections through (1) enhancing cash flow and containment of uncollectibles and (2) a long-term initiative to improve collections processes and efficiencies. PGW St. CRRC-3 at 3. Although the Collections Initiative commenced in September 2003, the actual effect of the initiative did not start to pay results until the end of March and early April 2004. Tr. 370.

In its rebuttal, the Company updated its forecasted collections. At the time it filed its Petition on March 1, 2004, the Company projected a collections rate of 89% for the fiscal year ending August 31, 2004. PGW St. CRRC-1, Exh. JRB-4; JRB-5 at 2. In his rebuttal testimony, however, PGW witness Bogdonavage testified that collections were improving and that the collections rate for the 12 months ending March 2004 was approximately 90.5%. PGW St. CRRC- 1R at 2. If this improvement continues, PGW is projecting a collections rate of 93%. Id.

Each one percent change in the collections rate results in a change of approximately \$8 million in cash reserves for the Company. PGW St. CRRC-1 at 5.

The OCA submits that if PGW's Collection Initiative continues to result in sustained, improved collections rates, PGW will not need an uncollectibles surcharge. Before the Commission considers such a dramatic departure from traditional ratemaking, PGW's collections initiative should be given time to work. This is especially true in light of the Commission's June 2 Order that opened the investigation into financial and collections issues at PGW. June 2 Order. This investigation may also include consideration of certain, reasonable waivers of Chapter 56 regulations should PGW decide to file a Petition seeking such waivers. June 2 Order at 4-5. Therefore, there may be additional efficiencies to aid PGW's collections arising out of the Commission's investigation.

The OCA submits that before the Commission considers granting a drastic measure such as the CRRC, the effects of the Company's Collections Initiative and any changes that come out of the Commission-sponsored investigation should be allowed to work. These efforts could lead to enhanced collections and improved cash flow for the Company.

C. **The Proposed CRRC Is Contrary To Established Commission Precedent With Respect To Recovery Of Uncollectible Expense.**

1. **Uncollectible Expense Does Not Lend Itself To Recovery Through An Automatic Adjustment Mechanism.**

In Pennsylvania, uncollectible expense has always been an item of expense that was recovered through base rates. PGW's proposed CRRC, however, would allow a portion of

PGW's uncollectible expense to be recovered through a reconcilable surcharge mechanism.¹
The OCA submits that this would set an unsound precedent in Pennsylvania.

Typically, automatic adjustment clauses in Pennsylvania have been limited to recovery of costs that are largely outside the control of the utility, such as natural gas costs or taxes. OCA witness LeLash explained why collection of uncollectibles does not lend itself to recovery through an automatic adjustment mechanism such as the proposed CRRC:

The proposed CRRC represents a material deviation from the long established precedent of providing for recovery of uncollectible expense through base rates. The proposed CRRC is to be "established as a non-bypassable clause to be charged to all firm transportation or sales customers as part of the distribution rate" (CRRC Petition, page 13). Thus, uncollectible expense will still be a component of base rates. However, under PGW's CRRC proposal, the Company wants to carve out a single component of base rates – uncollectible expense – and make it subject to annual reconciliation. This is a clear departure from the way that base rates have historically been treated in Pennsylvania. The establishment of a CRRC constitutes "piecemeal" ratemaking which is not allowed within rate setting. Such automatic base rate expense adjustments should not be allowed.

Automatic adjustment clauses are also typically limited to specifically identified expenses that are not under the control of management, and therefore should be subject to a true up mechanism. In the case of the CRRC, neither of these conditions would be met. Uncollectible levels, while partially affected by variables such as wholesale gas price levels are still largely within the control of the Company. Additionally, the CRRC proposal, while providing for rate increases when collections fall below the specified level, does not provide for rate decreases if collections were to be above the level.

OCA St. 1 at 15-16.

¹ It should be noted, however, that PGW's proposed CRRC is reconcilable in only one direction. If actual, experienced uncollectible expense is greater than the uncollectible expense allowance in current rates, the surcharge will reconcile the difference and allow PGW to fully recover its actual uncollectible expense. If PGW's collections are better, however, experienced uncollectibles are less than the uncollectible expense allowance in current base rates, the difference is not reconciled and PGW gets to keep the difference.

The OCA submits that recovery of uncollectibles through an automatic adjustment mechanism such as the CRRC is not warranted.

2. The Proposed CRRC Constitutes Impermissible Single-Issue, Retroactive Ratemaking.

a. The CRRC Proposal Constitutes Single-Issue Ratemaking.

Another flaw in PGW's CRRC proposal is that carving out one element of PGW's expenses – uncollectible expense – for surcharge treatment in between rate cases violates the rule against single-issue ratemaking. OCA St. 1 at 15. The Commonwealth Court has recognized that there is a general prohibition against single-issue ratemaking in Pennsylvania if a utility seeks “specific recovery of a line-item that traditionally would be requested in rate-making procedure.” Pennsylvania Industrial Energy Coalition v. Pa.P.U.C., 653 A.2d 1336, 1350 (Pa.Comwlth. 1995)(PIEC); *see also*, National Fuel Gas Dist. Corp. v. Pa.P.U.C., 76 Pa. Comwlth. 102, 147, 464 A.2d 546, 567 (1983)(holding that the consideration of expense and revenue items in isolation could result in confiscatory rates); Philadelphia Elec. Co. v. Pa.P.U.C., 93 Pa.Comwlth. 410, 422, 502 A.2d 722, 727-28 (1985)(holding that there should be no line-by-line examination of items in a rate case and “an isolated item of revenue or expense may or may not be, without more, the subject of a refund or recovery.”).

In the PIEC case, the Court stated that:

Single issue ratemaking is similar to retroactive ratemaking and, in general, is prohibited if it impacts on a matter that is normally considered in a base rate case.

PIEC at 1350.

OSBA witness Knecht explained why regulators should refrain from employing single-issue ratemaking:

... it is a policy that is biased against ratepayers and biased in favor of a utility. If a utility is allowed to address only specific issues in a proceeding, it has an opportunity to seek a rate increase for a cost item in which it is under-performing relative to the last base rates case. In such a proceeding, it can do so without addressing other cost areas in which it might be out-performing the revenue requirement basis. For example, if PGW's performance on O&M costs were much better than that provided for in the past base rate case, a full rates proceeding would provide an opportunity for the Commission to offset the good with the bad.

OSBA St. 1 at 23.

In the instant case, PGW is attempting to do just that. The Company seeks to make an adjustment to a single element of base rate expense – uncollectible expense – between base rate cases and without any consideration of changes in other expense items. The OCA submits that this is impermissible single-issue ratemaking and should be denied.

b. The CRRC Proposal Constitutes Impermissible Retroactive Ratemaking.

PGW is also proposing to implement the CRRC clause commencing September 1, 2004. Petition at 12. However, PGW is proposing to recover an under collection realized in FY2004 (12 months ending August 31, 2004) of \$34.3 million. Petition at 13; Exh. JRB-6. The Company proposes to amortize this historic undercollection over a three-year period. Petition at 13. The OCA submits that this constitutes a classic example of retroactive ratemaking. OCA St. 1 at 20.

Under Pennsylvania law, ratemaking is prospective. See, e.g., Popowsky v. Pa.P.U.C., 164 Pa.Comwlth 338, 343, 642 A.2d 648, 650-51 (1994)(Popowsky 1994), *appeal denied*, Popowsky v. Pa.P.U.C., 543 Pa. 733, 673 A.2d 338 (1996). The fundamental principle against inclusion of past costs in future rates was established by the Pennsylvania Supreme Court in Cheltenham & Abington Sewerage Co. v. Pa.P.U.C., 344 Pa. 366, 25 A.2d 334 (1942)(Cheltenham). This prohibition against retroactive ratemaking has been reaffirmed in many cases since. See, e.g., Barasch v. Pa.P.U.C., 507 Pa. 496, 491 A.2d 94 (1985) (Barasch); Philadelphia Elec. Co. v. Pa.P.U.C., 93 Pa.Comwlth 410, 422, 502 A.2d 722, 727-28 (1985) (PECO).

In the PECO case, the Commonwealth Court affirmed an early decision by the Commission to disallow a claim by Philadelphia Electric Company (“PECO”) to recover through a three-year amortization \$41.5 million of deferred costs related to operation of pollution control facilities. Id. at 726-728. The Court agreed with the Commission’s disallowance of the retroactive recovery of these costs and held:

The general rule is that there may be no line by line examination of the relative success or failure of the utility to have accurately projected its particular items of expense or revenue and an excess over the projection of an isolated item or revenue or expense may not be, without more, the subject of the Commission’s order of refund or recovery, respectively, on the occasion of the utility’s subsequent rate increase requests.

An exception to this rule in the case of retroactive recovery of unanticipated expenses has been recognized where the expenses are *extraordinary and nonrecurring* ... We agree with the Commission that the pollution control facilities’ expenses here at issue are clearly neither extraordinary nor nonrecurring. Indeed, PECO here claimed and was granted the *prospective* operating, maintenance, and depreciation expenses associated with these facilities.

PECO, 93 Pa.Comwlth at 422, 502 A.2d at 727-28 (citations omitted; emphasis added).

Therefore, the one exception to the prohibition against retroactive ratemaking is for extraordinary and non-recurring expenses. In Popowsky 1994, 642 A.2d at 652, the Commonwealth Court specifically defined what constitutes an extraordinary expense:

Extraordinary expenses are often described as unanticipated and non-recurring. We believe that any unanticipated, non-recurring, substantial expense to the rate base that would be normalized out if occurring in a test year is “extraordinary.” *Extraordinary cannot mean merely unanticipated, because then every unexpected occurrence or failure to predict an item would be recoverable and the exception would overwhelm the rule, making test years meaningless.* To be extraordinary, it must also be a substantial, one-time expense or a substantial item that will not appear as a continuing expense and could otherwise never be recovered in rates because, like the weather-related expenses, it would be normalized out of the test year as abnormal.

Id. at 652 (emphasis added).

OSBA witness Knecht explained some of the rationale behind the prohibition against retroactive ratemaking:

For sound economic and fairness reasons, costs that are included in rates are usually identified in advance, usually based on reasonable forecast of those costs for a future test period. From an economic efficiency standpoint, by setting base rates that reflect those lower costs in advance, the utility has an incentive to out-perform the forecast. Over the longer term, the lower utility costs that result from these incentives for efficiency are passed on to ratepayers.

From a fairness standpoint, including previously incurred costs in rates is inequitable, because ratepayers had no warning that they were responsible for those costs. Such a practice also results in “intergenerational inequities,” meaning that future ratepayers are paying for costs associated with ratepayers from an earlier period. In addition, by recovering prior costs in current rates, ratepayers are sent inaccurate price signals for current consumption.

OSBA St. 1 at 29-30.

The OCA submits that there is nothing extraordinary or nonrecurring about PGW's claim. This is an expense item that has always been recovered through base rates. PGW has failed to demonstrate that there is any reason to permit retroactive recovery of any uncollectible expense.

3. The Proposed CRRC Would Reduce The Incentive For PGW To Maximize Its Collections.

The OCA submits that recovery of uncollectible expense through an automatic recovery mechanism would reduce the incentive for PGW to maximize its collections. Recovery of uncollectible expense as a non-reconcilable expense allowance in base rates creates an incentive for a utility to maximize the amount of collections that it can recover. The OCA submits that it would be bad policy to remove that incentive for a utility such as PGW where PGW has already demonstrated a poor record with its collection efforts. OCA witness LeLash explained how the incentive to maximize collections would be affected by implementation of an uncollectible expense reconciliation mechanism:

Additionally, an automatic adjustment clause, such as the CRRC, can remove incentives for the Company to limit its level of uncollectibles. This is of a particular concern because PGW has had a history of poor performance when it comes to billing and collections. While the levels of wholesale natural gas prices are beyond the Company's control, better uncollectible recovery procedures, more effective gas price hedging strategies, and greater customer enrollment in budget billing plans and conservation programs can all effectively reduce uncollectibles as they do for other gas distribution utilities. A mechanism for automatic recovery of uncollectibles would remove much of the incentive to pursue such alternative courses of action.

OCA St. 1 at 16.

This concern was echoed by OSBA witness Knecht:

Uncollectibles costs are non-reconcilable for a very good reason. Making uncollectible costs even partially reconcilable, as proposed by PGW, severely weakens PGW's incentives to improve collections. As collections rates are one of PGW's most critical problems, reducing the incentive for it to try to fix the problem is neither appropriate nor timely. Furthermore, allowing PGW to set up such a reconcilable mechanism will set a precedent for other NGDC's, weakening the incentives for bill collection across the Commonwealth.

OSBA St. 1 at 11.

Therefore, the OCA submits that adoption of the CRRC would weaken the incentive for PGW to maximize its collections at a time when PGW should be focused on improving its collection efforts.

D. The Precedent From Other States Cited By PGW Is Distinguishable From The Instant Case And Should Not Be Followed By The Pennsylvania Public Utility Commission.

PGW claims in its Petition that several other states have permitted similar uncollectible expense adjustment mechanisms. Petition at 16. In particular, PGW cites an order from the Public Utilities Commission of Ohio.² As OCA witness LeLash noted, however, the mechanisms that have been authorized in other jurisdictions:

... generally involve the operations of Atmos Energy or operations in Ohio. Second, the mechanisms are not comparable concerning the scope of the recovery, their relationship to customer choice programs or percentage of income programs, and their associated true-up requirements. Third, the jurisdictions' definitions of

² In the Matter of the Joint Application of The East Ohio Gas Company d.b.a. Dominion East Ohio, Columbia Gas of Ohio, Inc., Vectren Energy Delivery of Ohio, Northeast Ohio Natural Gas Corp., and Oxford Natural Gas Company for Approval of an Adjustment Mechanism to Recover Uncollectible Expenses, Public Utilities Commission of Ohio, Case No. 03-1127-GA-UNC (Dec. 17, 2003) [hereinafter "Ohio Order"]. A true and correct copy of this Order is attached hereto and marked "Appendix A".

recoverable fuel costs and the regulations involving such cost recovery differ between utilities and states, and it is unclear that they would be applicable in Pennsylvania. *The long established precedent for the Philadelphia Gas Commission, the Pennsylvania PUC, and the vast majority of other states utility commissions is to set uncollectible and bad debt allowances within the context of base rate or budgeting proceedings.*

OCA St. 1 at 16-17 [emphasis added].

In particular, the one Ohio case cited by PGW is distinguishable from this case in many ways. For instance one of the justifications cited by the Ohio Commission for approval of an adjustment clause for uncollectible expense, in addition to volatile gas prices, was the uncertainty of the weather and the inability of the utilities to control weather. Ohio Order at 11. That justification is not applicable to PGW, since the Company was provided with a Weather Normalization Adjustment (“WNA”) in its last base rate case. See Pa.P.U.C. v. Philadelphia Gas Works, Docket No. R-00017034 (August 8, 2002).

The Ohio Commission also provided another rationale for approval of the adjustment mechanism that is not present for PGW:

... we do not accept that the uncollectible expense amounts allotted in applicants’ rate bases so long ago (and determined at a time with very little gas cost volatility) can be appropriate at this time.

Ohio Order at 11. The Ohio utilities in question had, for the most part, had their base rates established in the late 1980’s or early 1990’s. That is not the case for PGW since it had its rates adjusted in a base rate case in August 2002. At that point, the wholesale gas markets were already going through a state of volatility. Furthermore, as OCA witness LeLash noted:

The current high wholesale gas prices and the overall gas price volatility are not new to the gas industry, nor will today’s prices necessarily continue at this level. During the winter of 2000-2001

wholesale gas prices (as measured by Henry Hub monthly closing levels) were as high as \$9.79 per Dth. However, by October of 2001, wholesale prices were back down to \$1.89 per Dth and they averaged \$2.53 per Dth for the November 2001 to March 2002 period. Similarly, wholesale prices that reached \$9.28 per Dth in March of 2003 fell back to \$4.49 by November of that year.

OCA St. 1 at 17.

Thus, many of the justifications cited by the Ohio Commission for approval of an adjustment mechanism for uncollectible expense simply are not present for PGW.

Other jurisdictions that have addressed similar adjustment mechanisms for uncollectible expense have rejected them. The North Carolina Utilities Commission considered an application filed by a Piedmont Natural Gas Company ("Piedmont") for permission to record to a deferred account the difference between actual uncollectibles experienced and the uncollectible allowance in Piedmont's current rates.³ Piedmont proposed to recover the deferred amount from customers as part of its next purchased gas cost adjustment. This request came after the winter of 2000-2001 when gas prices reached historic highs, weather was colder than normal, and customers experienced significantly higher bills than in previous winters. Piedmont claimed that "as a result of the extended payment arrangements and various Commission rules that limit Piedmont's ability to obtain deposits and to discontinue service for non-payment of gas bills" many customers fell into substantial arrearages. NCUC Order at 1.

The North Carolina Commission rejected Piedmont's proposal. In so doing, the North Carolina Commission held:

³ In the Matter of Application of Piedmont Natural Gas Company, Inc., for Approval of Special Accounting Procedures, North Carolina Utility Commission, Docket No. G-9, Sub 453 (Order entered November 7, 2001)(NCUC Order). A true and correct copy of this Order is attached hereto and marked Appendix "B".

The Commission has considered all of the comments herein, and carefully weighed the equities as well as the law. The Commission concludes that the request for special accounting treatment should be denied. *Piedmont's original petition essentially made an appeal based on equity: gas prices were high, the weather was cold, and uncollectibles went up. There are, however, serious legal obstacles to the special accounting treatment requested by Piedmont, the most fundamental of which is that the proposal focuses solely on one component of rates, without looking at changes in the utility's other expenses and revenues over the same period* and without compliance with the general statutory provisions of G.S. 62-133 as construed in State ex rel. Utilities Commission v. Edmisten, 291 N.C. 451 (1977).

NCUC Order at 2-3 (emphasis added).

The OCA submits that Pennsylvania law requires the same outcome as that in North Carolina. PGW's proposal constitutes impermissible single-issue ratemaking and should be rejected.

E. The Proposed CRRC Will Result In Unjust and Unreasonable Natural Gas Bills For Many PGW Customers.

1. The Proposed CRRC Will Raise PGW's Rates Even Higher And Result In Rates That Are Unjust, Unreasonable and Unaffordable.

In its Petition, PGW proposes an initial recovery of \$47 million per year in additional revenue through the CRRC. Petition at 13. This results in a proposed increase in PGW's rates of \$0.7947/Mcf. PGW St. CRRC-1, Exh. JRB-6. The OCA submits that an increase in PGW's rates of this magnitude would be unjust and unreasonable. PGW already has the highest distribution rates of any NGDC in Pennsylvania. OSBA St. 1 at 9. Such a large rate increase would result in largely unaffordable gas bills for many more PGW customers and force even more of PGW's customers into the category of non-payment. This would simply

exacerbate PGW's collections problems and lead to a greater crisis. As OCA witness LeLash testified:

PGW's rates for gas service are already too high as evidenced by its historical 92% collections percentage which is dramatically lower than the collection percentages for other gas distribution utilities. Adding yet another charge to the Company's distribution rate is only going to exacerbate the situation. If PGW's drop off in collections "can be associated with historically high natural gas rates" (Petition, page 2), it is highly unlikely that the addition of a CRRC will solve the collection problem. Even at current levels, a high percentage of PGW's customers cannot pay their gas bills even with the availability of various assistance programs, and PGW's gas costs may not be as low as they could be if its hedging, supplemental gas supplies, and interstate pipeline resources (including storage) were utilized more effectively.

OCA St. 1 at 19.

The reality is that PGW's collections will fall even further if rates are increased further. As OSBA witness Knecht explained:

... PGW's expert Dr. Peach presents an analysis that shows that PGW's collections rate will decline when rates are increased. Thus, when PGW raises its rates with the CRRC, Dr. Peach's thesis implies that PGW's overall collections rate will fall. When the collections rate is lowered, PGW will then need to increase its CRRC, which will then further lower the collections rate, and so forth. The basic implication of Dr. Peach's thesis is that the initial CRRC that PGW proposes will not produce sufficient cash to stave off financial problems absent some improvement in collections efficiency.

OSBA St. 1 at 8. OSBA witness Knecht did an analysis of the elasticity effect of further rate increases on PGW's rate increases and concluded that the CRRC could explode to as much as \$2.37/Mcf as a result of the downward spiraling collections rate caused by rate increase piled upon rate increase. OSBA St. 1 at 8-9.

OSBA witness Knecht summed up his conclusions about imposing further rate increases on PGW customers through the CRRC:

Based on PGW's own analysis, I conclude that PGW cannot, at this time resolve its financial problems by raising rates. My conclusion applies to any form of rate increase, be it CRRC, base rates increase, or any other rate increase mechanism. Under present collections policies, any increases to PGW's tariff rates will reduce PGW's collections rates, such that some 30 to 40 cents on every dollar of increased billed revenue is never collected. Rate increases may also have the effect of reducing overall demand, either due to conservation efforts, fuel switching or customer flight. These volume losses would further reduce the contribution margin that PGW earns on its sales.

OSBA St. 1 at 10.

In its rebuttal testimony, the Company dampened the magnitude of the proposed increase in rates by providing more optimistic forecasts of its collections rate. PGW witness Bogdonavage provided updated projections for its CRRC proposal based upon improved collections performance since the time it filed its Petition. PGW witness Bogdonavage testified in his rebuttal that if the Company can achieve a collections rate of 90.5%, the proposed CRRC would be set at \$0.49/Mcf. PGW St. CRRC-1R at 2. If the Company's collections rate increases to 93%, the proposed CRRC would be \$0.03/Mcf. Id.

The OCA submits that *any* increase in rates for PGW at this time would result in rates that are unjust and unreasonable and largely unaffordable given the fact that many PGW customers already are struggling to their pay current bills. Piling another rate increase on top of already staggering gas bills will simply push many more customers into the ranks of those that cannot afford to pay.

Furthermore, even if PGW's forecasted improved collections come to fruition, the Company still proposes to increase rates even though it will finish the year with between \$31

million and \$36 million in cash reserves without any rate increase. PGW St. CRRC at 2-3; Exh. JRB-10. The Company's justification is to collect additional working capital. PGW St. CRRC at 2-3. The OCA submits that to ask customers to pay higher rates at a time when they are already struggling to pay historically high gas bills is unjust and unreasonable.

2. Public Input Testimony Demonstrates Overwhelming Opposition To PGW's Proposed CRRC.

a. Introduction

There has been an overwhelming public outcry in opposition to PGW's proposed CRRC. Over one thousand formal complaints have been filed in this proceeding. Four public input hearings were scheduled in PGW's service territory. The first Public Input hearing held at the Double Tree Hotel in Northeast Philadelphia on May 5, 2004 resulted in overflow attendance and many people had to be turned away. Another Public Input hearing was later scheduled in Northeast Philadelphia at George Washington High School on May 20, 2004. Two other Public Input hearings were held at Philadelphia Community College on May 6, 2004. Each was well attended.

There was extensive public input testimony at the four scheduled public input hearings. It is clear from this testimony that PGW customers are already struggling to pay their gas bills in light of the recent base rate increases and increases in natural gas costs. To further burden these customers with another rate increase through the CRRC will simply make bills largely unaffordable for many people and cause many more PGW customers to fall into arrears. Many customers testified to the unfairness of adding an additional surcharge to their bills as they were already struggling to make their payments.

Hundreds of people turned out at the hearings in person. Over 100 PGW customers testified under oath. Literally thousands of signatures were gathered on petitions in opposition to the proposed CRRC. A very real possibility exists that if this surcharge is approved, the public response would be such that there could be even worse results for the Company's collections. The message at the public input hearings was loud and clear. PGW's customers are angry about the Company's proposed CRRC, and many people simply cannot afford to pay it.

Many public officials from Philadelphia also came forward to voice their opposition to PGW's proposal. There was significant public input testimony from state legislators and local officials in opposition to the proposed CRRC. State Senators Anthony Hardy Williams, Michael J. Stack and Allyson Y. Schwartz testified in opposition to the CRRC. Representatives Dwight Evans, Babette Josephs, George T. Kenney, Jr., Angel Cruz, Alan Butkovitz and Mark B. Cohen also testified in opposition to PGW's proposal. City Councilman Brian J. O'Neill of Philadelphia City Council also testified in opposition to the CRRC proposal.

Space and time does not permit a summary of all of the public input testimony. However, a brief summary of selected testimony will highlight the anger and frustration that has been generated by PGW's proposal.

b. Testimony of Philadelphia Public Officials.

Senator Anthony Hardy Williams testified on behalf of his constituents in the 8th Senatorial District and himself as a PGW customer. Senator Williams, who is a member of the Senate Energy Committee, testified that he is troubled by PGW's CRRC proposal and the Company's ability to continue as a solvent entity. He stated that he cannot tolerate a proposal that asks customers to pay an additional \$80 a year through the CRRC and asks that the

Commission flatly reject it. He called the proposal unprecedented and oppressive. In particular, Senator Williams noted that:

Common sense suggests that one of the causes of PGW's collection difficulties is the rapid pace of rate increases. PGW is again gouging its customers. Since 2000, the typical residential customer's bill has shot up 60 percent. My constituents and Philadelphians on the whole simply cannot shoulder another unreasonable rate increase.

Senator Williams also suggested that there needs to be supplemental LIHEAP assistance from the Commonwealth to help PGW customers that are impoverished and unable to pay. Tr. 158-162.

Senator Michael J. Stack testified on behalf of his constituents in the 5th Senatorial District and himself as a PGW customer. Senator Stack testified that he agrees with OCA that the proposed CRRC is unjust and unreasonable. He believes that the PGW filing is "bad policy, bad business, and just plain bad news." He does not find the proposed CRRC to be fair or necessary. Senator Stack cogently summed up his opposition to the proposed CRRC:

The PGW proposal would create a scenario in which normal, everyday hardworking families and retirees who pay their bills on time would be forced to reopen their wallets to pay for services to delinquent customers. Another bewildering aspect of this proposal is that PGW seeks to add this increase to already high rates. A situation that will only serve to diminish the number of customers who can afford to pay their bills. This is especially true, and I think if you look around the room you can see that, for senior citizens and others who are struggling to get by on fixed incomes.

Approval of this rate hike would merely establish a short-term fix for PGW, but it would set a precedent to create a series of long-term hardships for ratepayers. Activating the CRRC would provide absolutely no incentive for PGW to improve its collection system of the overall management of its finances. It would shield management from the consequences of any failed business decisions. The only incentive the CRRC will generate is repeat

PGW requests for additional surcharges in future years and this could easily become an annual ritual.

Senator Stack noted the need to pursue better collection practices, more effective hedging strategies and greater customer education and enrollment in budget billing before considering an increase in rates. He called on the Commission to explore “the maximum range of sound management and financial practices to cure PGW’s maladies before wreaking havoc on our citizens with an ill-advised CRRC.” Tr. 35-40.

Senator Allyson Y. Schwartz testified on behalf of her constituents in the 4th Senatorial District. Senator Schwartz testified about the hardship the proposed CRRC will place on ratepayers:

So the combination of the increasing rates and increasing costs of gas to ratepayers and the fact of the poor collections and the fact that PGW is just not where it should be from a point of view of management, you just cannot punish, and should not punish, responsible ratepayers for that. And I oppose it.

Senator Schwartz concluded by stating that PGW’s proposed CRRC “punishes the wrong people, rewards the wrong people, and is simply bad public policy.” Tr. 514-516.

Representative Dwight Evans testified on behalf of his constituents in the 203rd Legislative District and himself as a PGW customer. Rep. Evans testified that he strongly opposes PGW’s proposed CRRC. He stated:

This is the wrong solution, the wrong policy, and a wrong precedent in rate making, and it is unfair to the decent, hard-working families who do everything that they can to keep up with their expenses and pay their bills.

He noted that Philadelphia has the lowest median income and highest level of poverty in the Commonwealth and noted that PGW has the highest natural gas rates in the Commonwealth. He pointed out the impact this has on PGW customers:

... Philadelphians typically have less income and more people in poverty, but we're saddled with the highest natural gas rates in the state. Now PGW wants to put an automatic surcharge on its gas bills. I point these things out to you because I want you to consider the budgetary context of what PGW is proposing to do.

Is the PUC looking out for the little guy? How much deeper can people reach into their pockets? How much more can decent, honest hard-working families take? The consequence of PGW's request for a Cash Receipts Reconciliation Clause is very clear. It will hurt. PGW is already the most expensive natural gas company in the Commonwealth of Pennsylvania. Now the most expensive wants to become even more expensive, making the unfavorable disparity even worse.

Rep. Evans also noted the impact PGW's proposal would have on small business and industrial customers:

This proposal is not just bad for residential customers but it is also bad for small businesses and industrial customers ... how can the City compete to retain businesses and jobs in the City if its gas rates exceed everybody else's? Businesses will save nearly 18 percent in gas costs just by moving across the city line. We need to keep jobs here in the City.

In conclusion, Rep. Evans produced a petition in opposition to PGW's proposed CRRC with over 3200 signatures. Tr. 162-172.

Representative George T. Kenney, Jr. testified at both Public Input hearings conducted in Northeast Philadelphia. Rep. Kenney testified on behalf of his constituents in the 170th Legislative District and himself as a PGW customer. Rep. Kenney expressed his outrage and opposition to PGW's proposal. He testified:

Responsible customers should not be penalized for PGW's inability to collect from irresponsible customers. Putting an extra burden on good faith paying customers will not fix the problem, it will do nothing to change PGW's current inability to collect from deadbeat customers. In fact, the additional charge could force those who make every effort to pay their gas bills in a timely manner putting them in a position of not being able to pay because of the additional charge. And that is wrong.

In response to the Company's argument that it needs the CRRC as a "backstop" or "insurance policy," Rep. Kenney testified:

I would say to PGW, you're not in the insurance business. You should not be putting insurance policies, or I think you mentioned the term, you were looking for an insurance policy on the back of honest ratepayers just to give you a little comfort level in case you don't collect what you're supposed to collect.

Tr. 47-48, 517-518.

Representative Mark B. Cohen testified on behalf of his constituents in the 202nd Legislative District. Representative Cohen also opposes PGW's proposed CRRC. He testified that PGW needs to help its customers maximize benefits from other sources, such as the Earned Income Tax Credit, Social Security Disability Income and Social Security Supplemental Income, in order to help households meet their budgets. He also criticized PGW's claim that PUC regulations inhibit its ability to collect:

The Gas Works argues that it collects so little because it is legally prohibited from shutting off gas service during the winter months because of the cold weather moratorium. But the cold weather moratorium does not exist to protect delinquent customers who can pay but choose not to. The moratorium exists to protect the vulnerable, low-income persons, the elderly or disabled, those with young children, or the chronically ill from literally freezing to death. The vast majority of people who do not pay their bills during the winter are believed not to be vulnerable; but to be a class of people who have continually and professionally exploited the system at our expense. To the extent that this widespread

belief is accurate, the situation it represents is outrageous and intolerable. Further, the ban on shutting off gas service during the winter months is statewide and does not create an unmanageable problem for other utilities.

Rep. Cohen also encouraged the Commission to consider ordering PGW to examine the best collections practices of other utilities and find a successful collections model for PGW to emulate. Tr. 66-71.

Representative Babette Josephs testified on behalf of her constituents in the 182nd Legislative District. Rep. Josephs testified that she thought the proposed CRRC was very bad precedent for the PUC and that every other utility in the state will ask for the same treatment. She also does not think it is fair to those customers who do pay their bills on a timely basis. Rep. Josephs also expressed concern that an additional increase in rates will result in more people that cannot afford to pay their bills, thus exacerbating PGW's collections problem. Tr. 173-74.

Representative Alan Butkovitz testified on behalf of his constituents in Oxford Circle, Broadhurst and Bustleton and himself as a PGW customer. Rep. Butkovitz also opposes PGW's proposed CRRC. He testified about the hardship that the CRRC proposal would impose upon senior citizens in PGW's service territory. He testified that even a small monthly increase through the surcharge will force seniors to do without something else. Rep. Butkovitz also testified that giving PGW a CRRC will diminish the incentive that the Company has to improve collections. Tr. 519-520.

Representative Angel Cruz testified on behalf of the constituents in his Legislative District. Rep. Cruz suggested that PGW should place liens on property owners' property if they do not pay their gas bills. He also suggested that the salaries of PGW's management should be examined.

City Councilman Brian J. O'Neill testified on behalf of his constituents in Northeast Philadelphia and himself as a PGW customer. Councilman O'Neill also opposes the proposed CRRC. He criticized the proposal for its lack of due process. He stated that it gives PGW a blank check to raise rates whenever its revenues fall short, with no hearings, no accountability, no customer input and no governmental approval. Councilman O'Neill also testified that PGW needs to take more aggressive measures to collect unpaid bills.

c. Testimony of PGW Customers.

Francis Jarrell is a PGW customer, and she testified that she is opposed to the proposed CRRC. Ms. Jarrell is a senior citizen and the type of customer that pays her bill early. She presented a petition that was signed by over 4500 people in opposition to the PGW proposal. She believes that the Company's mismanagement is responsible for allowing customers to run up large arrearages. Tr. 52-56.

Catherine Jackson is a PGW customer, and she testified that she is opposed to the CRRC proposal. Ms. Jackson questions whether PGW follows up with its collections and terminations procedures:

The Cash Receipts Reconciliation Clause is a tax imposed on us paying customers to pay the bills of deadbeats. PGW recently stated they sent 130,000 shut off notices to deadbeats. What really matters is how did they follow up on those letters? Did they receive any payments from the letters that they sent? Did they make any shutoffs? I don't think so. The letters were probably idle threats as they were in the past. PGW never follows through on anything that they say. Except raising rates, yes.

Ms. Jackson also criticized PGW's response time to service calls and the lack of responsiveness by PGW's call center. Tr. 84-85.

Linda Novak is a PGW customer and a Committee Person on the 23rd Board, 14th Division. Ms. Novak also testified that she was opposed to the CRRC proposal. However, Ms. Novak warned against lumping in those who inadvertently fall behind on their bills with deadbeats that make no attempt at all to pay. Tr. 87-88.

Marilyn Chaiken is a PGW customer, and she testified that she is opposed to the CRRC proposal. Ms. Chaiken testified about the hardship that PGW's proposal will place on Seniors in particular:

My husband is retired, I am a housewife ... You are talking about a gas increase, your car gas increase, your water. How is the average senior citizen, my age, 70 years old, and my husband who is 84 who just became ill over the last number of months which has a tremendous increase in medications that I just ordered today was over \$400.00 for three prescriptions, and you expect us to pay that increase and all the other increases?

* * * * *

What's happening to the poor senior citizens who have worked all their life to try to end up with something for themselves, not to leave to their children, but to be able to take care of themselves. We are living longer because of better and more medications but the prices are skyrocketing and it's making it very difficult. I have been in a drugstore where a woman was in tears because of a tremendous medical bill and she had to make a choice between food, her utility bills, and her medicine bill.

Tr. 97-100.

Carol Senske is a PGW customer and also testified in opposition to the proposed CRRC. Ms. Senske's testimony demonstrates that many younger, hardworking families will also be harmed if PGW's CRRC proposal is approved:

My husband and I work hard, we barely get by. We live paycheck to paycheck. Honey, I have to go food shopping, do we have

money in the account? No, hon, there's only \$20.00 in checking, we've got to wait till next week. It's disgusting but we work hard, we pay our bills in full, on time. Tonight my son said to me: Mommy why aren't you coming to my soccer game? I said: Hon, I have to go and I have to stand up. I have to voice for our family that this is unfair. I explained to him that PGW, who helps keep us warm in the winter, wants to charge us extra money so we can pay for the other people that don't pay their bills. And in the wisdom of a seven year old child he said: Mommy, that's just not fair.

Tr. 111-113.

Mark Evans testified in opposition to the CRRC. Mr. Evans is a PGW customer and also a PGW employee who is out on the streets every day. Mr. Evans testified about the outrage he hears from PGW customers during the course of his job:

Now, in 30 years of working at PGW I never have heard the rage tonight and as I hear on the street, because I do work out on the street, I am not one of the people that answers phones, I'm not one of the people that work inside, I am one of the guys on the street that you see out there. In 30 years I have never heard the rage from customers in my daily work expressed as far as this outrage right now. I don't think it's fair. I think there's other means – other ways of attacking the problem.

Tr. 113-116.

Lance Haver testified on behalf of himself as a PGW customer and as the Director of Mayor Street's Office of Consumer Affairs. Mr. Haver testified about how PGW's proposed CRRC would only exacerbate the uncollectibles problem:

If I could I would start my testimony with a scream of pain and anguish. PGW wants to raise the rates of those that are paying to pay for those that are not. If they are allowed to do so without any other change all that will happen is that next year there will be more who can't pay which will lead to another rate increase. Certainly this is the beginning of what economists call the death spiral. Everytime we raise rates more people fall behind, leading

PGW to raise rates even higher until there is no one left who can afford to pay.

Mr. Haver urged the Commission to provide PGW with the tools necessary for it to collect from those customers that are able to pay but don't, while protecting consumers who are simply too poor to keep up. He also urged the General Assembly to provide additional LIHEAP and funding and funding for conservation programs. Tr. 129-134.

Mattie Bridges is a PGW customer and she also testified in opposition to the proposed CRRC. She explained the hardships that a Senior Citizen such as herself endures in Philadelphia:

My reason I'm here today, because I'm very disturbed on what they're asking us to do. I say us because I'm speaking on behalf of all of the other people who pay the gas bill. I'm a retired person. I have been out for ten years. I've had a cost of living once since ten years I have been retired. They tell me my income is too much. I get no help from nobody. I'm a diabetic and insulin dependent. I don't see how in the world, that how I can give anything to anybody that I don't have. The insurance stopped paying. So I have to pay for my medicine. I have to buy it all myself.

Don't feel sorry for me. I worked in the City 36 years and I retired. I went to work every day that I had to go. And I thank god that I could go, that I wasn't sick I could go. I met the retirement age. Everything that I go to ask for it's a block. Your income is too much. I don't know what they think. But I know I have to join the people who are not paying if I'm forced to give them anything ... I want to say to the people and to the gas company especially, it don't make sense. It's not right. Where do you all think that people in this city – you know there are a lot of poor people and it will always be poor people among us. I'm one of them. I do the best that I can. I can't, I will not if you force me to do it I'm telling you in plain English, that I will have to turn like the other people. It don't make sense.

Tr. 174-176.

Mary Winston is a PGW customer and she testified against the CRRC. Ms.

Winston echoed the comments of many others at the Public Input hearings:

I'm here today, because the surcharge they're trying to put on us is ridiculous. I'm 86 years old. I live by myself. I have a house, and everything in it is going up. My insurance is going up. My medicine is going up. Everything is going up. I pay my bills. I cut out a lot of things. I would like to have lobster and steak. But you have to cut down on it to do your bills. I like to travel but I have to stop that. I'm 86 years old. I should be enjoying life. But I can't do it. My budget is \$166 a month for gas. I don't understand why they keep going up.

Tr. 176-177.

Reverend Bruce M. Edwards testified on behalf of the 212 member organizations that make up the Urban Leadership Council. Rev. Edwards criticized PGW's long history of poor management. He also expressed dismay at the effect that PGW's recent rate increases and proposed CRRC has on Philadelphia's Senior Citizens:

Did you see these old senior citizens? You ought to be ashamed of yourself for having our mothers and grandmothers come down here to fuss at you. They've already paid their fair share. And now the people that have paid their share you have the audacity to tell them you will double charge them for some bums that won't pay you ... I pray to God that you take the burden off of our mothers and grandmothers. I'm crying because I can't believe that these old women had to come down here and tell you what I heard here this day. It's unconscionable that we should have to witness – and I never want to see it again, and I will fight to my last breath before I have to see another old woman come down here to fight with you people.

Rev. Edwards also pointed out the need for PGW to enter into reasonable payment arrangements with customers who have fallen into arrears:

But you need to fix, you need to cut out stupid agreements that you make. Let me give you an example. If I owe you already \$2,500 and you send me a regular bill for \$250, and come to make an agreement you say well you pay \$50 on the \$25[00] that you owe, and then the regular bill of 250, how the hell am I going to pay that when I'm not paying you what I owed already. Its absolute

stupidity. You keep on doing it. Why don't you sit the person down and do a means test. Some money is better than none. Why don't you let them make a deal with you that they can hold up to even if it's ten dollars. It's more than what you're getting now.

Tr. 179-186.

Rudolph Tolbert testified on behalf of the Energy Coordinating Agencies (“ECA”). The ECA is a quasi-public nonprofit dedicated to effectively addressing energy problems of low and moderate income people. ECA works with 10 energy centers, who provide services to 30,000 people each year in the area of energy conservation, bill payment assistance and education. One program they work with is PGW’s Conservation Works Program – which has been one of the most effective energy conservation programs in the country. Mr. Tolbert testified that utility service terminations have a very damaging effect on Philadelphia. The number of fires increase as people turn to alternative sources of heating. He urged more energy conservation measures be put in place. He recommended that Philadelphia and Pennsylvania adopt new energy efficiency standards for all new affordable housing, in particular the Energy Star standard. Mr. Tolbert also recommended that energy efficiency standards be incorporated into low income repair and rehab programs. Mr. Tolbert testified about the effect of an increased conservation effort in PGW’s service territory:

If all of these recommendations were implemented, PGW’s uncollectible problems would diminish, which would relieve pressure on the rates for all rate payers. Implementing these recommendations will also create jobs and strengthen the local economy, which is one of the root causes of PGW’s uncollectibles problem.

Tr. 200-204.

F. The Office of Trial Staff’s Alternative Proposal Is Also Flawed.

The Office of Trial Staff (“OTS”) has proposed an alternative adjustment mechanism to PGW’s uncollectible expense in this proceeding. In his direct testimony, OTS witness Weakley made an alternative proposal to adjust the allowance for uncollectible expense upward or downward with each change in the GCR rate. OTS St. 1 at 10. In order to do this, OTS witness Weakley calculated a historic write-off ratio of 7.616% based upon a historic analysis of actual net write-offs to billed gas revenues. OTS St. 1 at 12. He then applies this factor to the change in the cost of gas between the current GCR rate and the GCR rate that was in effect at the time of the last fully-litigated base rate case in 2001.⁴ OTS St. 1 at 12-13; OTS St. 1SR at 3-5. The result is that for every change in the GCR rate, a factor of 7.616% is included. OTS St. 1 at 11-12.

The OCA submits that while the OTS alternative proposal is an improvement over the Company’s CRRC proposal, it is still flawed and should be rejected. For the reasons explained in Section C.2.a above, the OTS alternative proposal constitutes impermissible single-issue ratemaking.

Another flaw in his proposal is that there is no rationale for setting the base GCR rate at the level that was in effect at the time of the last fully litigated base rate proceeding in 2001 – two base rate cases ago. Since that time, PGW has had another base rate case that resulted in a \$36 million increase in base rates as a result of a black box settlement in that case. Pa. P.U.C. v. Philadelphia Gas Works, Docket No. R-00017034 (Order entered August 8, 2002). OSBA witness Knecht explained the problem with the disconnect between OTS’s proposed base GCR rate and the current level of uncollectible expense:

⁴ The OTS alternative proposal compares the GCR rates exclusive of the \$3.18/Mcf of gas costs that was recovered through base rates prior to restructuring. OTS St. 1 at 12-13.

... following the logic of Mr. Weakley's proposal, the base PGC rate should be the PGC rate that was in place at the time of the settlement of PGW's last base rate proceeding. Presumably, at that time, PGW believed that the implicit uncollectibles provision in the base rates was sufficient to provide for gas supply uncollectibles for the PGC rates at the time. My understanding is that the last PGW base rates proceeding was resolved in 2002. In that year, the PGC rate (net of estimated universal service costs) was in the range of \$5 per Mcf, well above the \$3.18 stated by Mr. Weakley. As such, the magnitude of Mr. Weakley's proposed OTS Surcharge significantly exceeds the level of the charge that would result from a logical implementation of his methodology.

OSBA St. 2 at 5.

Therefore, the OCA submits that the OTS alternative proposal is also flawed, single-issue ratemaking and should be rejected.

V. CONCLUSION

For the reasons set forth above, the OCA respectfully requests that the Commission reject the Petition of Philadelphia Gas Works to Establish a Cash Receipts Reconciliation Clause.

Respectfully submitted,



Stephen J. Keene
Senior Assistant Consumer Advocate
Aron J. Beatty
Lori A. Herman
Assistant Consumer Advocates

Counsel for:
Irwin A. Popowsky
Consumer Advocate

Office of Consumer Advocate
555 Walnut Street 5th Floor, Forum Place
Harrisburg, PA 17101-1923
(717) 783-5048
Dated: June 14, 2004

BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Joint Application of The)
East Ohio Gas Company d.b.a. Dominion)
East Ohio, Columbia Gas of Ohio Inc., Vec-)
tren Energy Delivery of Ohio, Northeast) Case No. 03-1127-GA-UNC
Ohio Natural Gas Corp., and Oxford Natural)
Gas Company for Approval of an Adjust-)
ment Mechanism to Recover Uncollectible)
Expenses.)

FINDING AND ORDER

The Commission finds:

- (1) On May 7, 2003, The East Ohio Gas Company d.b.a. Dominion East Ohio (DEO), Columbia Gas of Ohio Inc. (COH), Vectren Energy Delivery of Ohio (Vectren), Northeast Ohio Natural Gas Corp., and Oxford Natural Gas Company (Oxford) jointly filed an application with the Commission. The joint applicants ask the Commission to approve a new mechanism for their respective uncollectible expenses so that they will recover their actual respective uncollectible expenses. This proposal seeks to alter the method by which the joint applicants currently recover uncollectible expenses. Currently, the joint applicants recover uncollectible expenses as one component of their respective base rates. Except for Oxford, each of the joint applicants' uncollectible expenses were determined in the companies' last rate cases, based upon historical test year experiences with uncollectible expenses. Oxford's uncollectible expenses are presumably a component of its base rates, which were established a while ago by City of Oxford Ordinance No. 2433. See, *In the Matter of the Application of Oxford Natural Gas Company for Approval of Contracts Governing the Rates, Terms, and Conditions of Natural Gas Service to Certain Unincorporated Area Customers*, Case No. 98-225-GA-ATA. The cases in which the other joint applicants' base rates were last established are as follows:

<u>Company</u>	<u>Case No.</u>	<u>Decision Date</u>
DEO (East Ohio)	93-2006-GA-AIR	November 3, 1994
(West Ohio)	82-1458-GA-AIR	October 18, 1983
Columbia	94-987-GA-AIR	September 29, 1994 ¹
Vectren	91-415-GA-AIR	February 20, 1992
Northeast Ohio Natural Gas Corp.	97-1724-GA-AIR	March 4, 1999

¹ The Commission issued subsequent decisions altering this initial rate case decision on December 12, 1996, January 7, 1998, and December 2, 1999.

This is to certify that the images appearing are an accurate and complete reproduction of a case file document delivered in the regular course of business
Technician Date Processed 12.17.03

The joint applicants explain that they have experienced volatile and high gas prices and expect such to continue. The joint applicants believe that the uncollectible expenses that they have experienced are driven largely by gas costs² and weather. Additionally, the joint applicants state that, because gas costs and weather are out of their control, a better recovery mechanism for uncollectible expenses is warranted. Besides the benefit of recouping actual uncollectible expenses, the joint applicants contend that their proposal will allow them to agree to expanded enrollment parameters for the gas choice programs (to include customers with delinquent accounts). Similarly, the joint applicants state that, with their proposal, they can make additional purchases of competitive retail natural gas suppliers' receivables and will not have to increase the discount rate. For the above reasons, the joint applicants state that their proposal is reasonable and beneficial.

Next, the joint applicants argue that their proposal is legally permissible. They cite to Section 4929.11, Revised Code, which allows the Commission to approve adjustment mechanisms that fluctuate with changes in costs (similar to the gas cost recovery mechanism and gross receipts tax rider). They state that the proposed adjustment mechanism could be incorporated in their respective percentage of income payment plan (PIPP) riders. The amount would be recovered on a volumetric basis and calculated based upon the actual uncollectible expense experienced the prior year, including that associated with the provision of competitive retail natural gas service. The joint applicants state that, upon effectiveness of this proposal, their base rates will have to be reduced by all components reflecting uncollectible expenses at the time such base rates became effective.³ Annually, the amount would be adjusted to correct for over-/under-collections and include appropriate carrying costs. Additionally, the joint applicants propose that any currently existing deferred accounts receivable balances be recovered over a five-year period. The joint applicants ask for the accounting authority needed to defer the uncollectible expense for future recovery, pending

² The joint applicants subscribe the higher gas prices to the advent of a competitive wholesale gas market, (more entities vying for the same amounts of gas commodity) demand for natural gas by some electric generating facilities, and supply issues in foreign regions. They believe that the competitive retail natural gas programs in Ohio will only increase gas price volatility.

³ Because the amount to be recovered is not known until uncollectible expenses are determined after the end of the fiscal year, the joint applicants also propose that the initial uncollectible rates be established at the same level as the base rate reductions, to ensure that customers will not be affected by the new mechanism.

the establishment of an adjustment mechanism for their respective uncollectible expenses. Furthermore, the joint applicants state that each year's financial audit could include a financial audit of the uncollectible expense mechanism, thereby creating a regular and consistent evaluation of the workings of the mechanism. Lastly, the joint applicants seek an expedited ruling upon the proposal.

- (2) Seven entities filed motions to intervene. On May 9, 2003, Ohio Consumers' Counsel (OCC) filed a motion to intervene in this proceeding on behalf of the residential consumers in the joint applicants' territories. On June 5, 2003, Energy America LLC (Energy America) and Shell Energy Services Company LLC (Shell) jointly filed a motion to intervene in this proceeding arguing that, as competitive retail natural gas suppliers serving customers in DEO's and COH's service territories, the proposal will directly affect the collection of revenues associated with their commodity bad debt. On June 24, 2003, Ohio Partners for Affordable Energy (OPAE) sought to intervene arguing that it has a substantial interest in this proceeding because it is an organization advocating affordable energy policies and its members serve customers to be affected by the proposal. The Commission also received a motion to allow David C. Rinebolt to appear on behalf of OPAE before the Commission in this proceeding.

On July 28, 2003, the Consumers' Coalition (which includes The Empowerment Center of Greater Cleveland and the Coalition for Fair Utility Rates) stated it has an interest in the proceeding because it represents low-income gas consumers who would be affected by the proposed mechanism and any policy change to allow participation in the choice programs by customers with arrearages. The Appalachian People's Action Coalition (APAC) filed its motion to intervene on July 28, 2003, stating that its members (in southeastern Ohio) are affected by the mechanism being proposed. On July 30, 2003, Community Action Partnership (CAP), serving low-income residents of western Ohio in Vectren's service territory, filed to intervene. CAP contends that its members are vulnerable to the mechanism proposed in this proceeding.

- (3) Before summarizing the comments and discussing the substance of the application, we will first address the preliminary motions that are currently pending. The joint applicants have requested an expedited ruling upon their proposal. Over seven months have passed since the application was filed. We have not issued a ruling upon the application in an expedited fashion, nor are we convinced an

expedited decision was warranted. Thus, that request is denied. Next, we grant the motion to allow Mr. David C. Rinebolt to appear on behalf of OPAE in this proceeding.

As for the pending motions to intervene that have been filed in this case, we conclude that they should be denied. Section 4903.221, Revised Code, gives the Commission discretion to grant intervention to persons who may be adversely affected by a Commission proceeding. We find that it is not necessary to grant intervention to the seven movants in order to consider their comments/pleadings on this application. Furthermore, we do not believe that a hearing is necessary for conducting an evaluation of the application.

- (4) Several comments regarding the proposal have also been filed. Energy America and Shell do not oppose the proposed mechanism, so long as the Commission adopts changes related to the gas choice programs of DEO, COH and Vectren. The Gas Marketers' Group (composed of Interstate Gas Supply Inc., Vectren Retail LLC, and WPS Energy Services d.b.a. FSG Energy Services) also supports the proposed adjustment mechanism,⁴ does not believe a hearing is necessary, and advocates that approval occur only with three changes to the gas choice programs. DEO, COH and Vectren filed memoranda contra on the ground that these competitive retail natural gas suppliers' comments relate to issues separate from the joint applicants' proposal. They also addressed the specific suggestions made by the suppliers.
- (5) Since the competitive retail natural gas suppliers' suggestions are largely interrelated, we will summarize them and the utilities' responses together. The suppliers' suggestions are:
 - (a) Elimination of all discounts on commodity receivables. Energy America and Shell advocate the elimination of the discount on commodity receivables because, otherwise, suppliers recover less than 100 percent due to the discount on commodity receivables while competing against

⁴ The Gas Marketers' Group explained why it believes the mechanism is reasonable. The group points out that the cost of gas is a valid factor for justifying the proposal, particularly if the practice of having fewer rate cases continues. Specifically, they state that, even if the percentage of uncollectible sales remains the same with escalating gas prices, the price of commodity used in the base rate component will not adequately cover the price increases for the commodity and the increased dollar amounts of uncollectible expenses. Additionally, the Gas Marketers' Group agrees with the proposal because the gas choice utilities are at risk for 100 percent of a customer's invoice (when providing consolidated billing), even though the utilities' portion of the invoice averages 35 percent. Because of that disparity, the Gas Marketers' Group believes that an established method to recover actual uncollectible expenses is warranted.

the incumbent utility that recovers 100 percent of receivables. The Gas Marketers' Group has a different rationale for this suggestion. The group believes that the amount customers pay to cover those who do not pay should be the same regardless of where they purchase the gas commodity. The group is concerned that, with the proposal and a utility purchasing receivables at a discount, paying choice customers will effectively pay the uncollectible expense and the discount on receivables. According to the group, either the discount should be eliminated or a credit/adjustment equivalent to the discount should be given to those customers who are subject to the receivables reduction.

In response, DEO, COH and Vectren explain that they will offset the amounts that could otherwise be collected through the proposal by the amounts retained from the discount. They do not believe that, with this new mechanism, they will over-collect when purchasing supplier receivables because only the cost of money that goes to delinquent final account status is eligible under the proposal and because they experience substantial carrying costs associated with non-payment before an account is disconnected. In other words, DEO, COH and Vectren believe that the proposed mechanism is not tied to the discount on supplier receivables, particularly because the discount (but not the mechanism) proposes to recover the substantial carrying costs associated with delinquent accounts prior to actual disconnection, along with the delinquent amounts.

- (b) Inclusion of all uncollectible expenses in the mechanism. Energy America and Shell state it will be easier and simpler to track all bad debt costs. Also, Energy America and Shell argue that competitive retail natural gas suppliers should be permitted to do consolidated billing and later disperse the funds among utility and suppliers. The Gas Marketers' Group has a different approach: the utilities should be able to collect from the customer the total amounts owed and be able to shut off for arrearages, regardless of how the natural gas was supplied. Thus, Energy

America, Shell, and the Gas Marketers' Group advocate one collection process by one entity for all arrearages. DEO, COH and Vectren state that proper examination of these two items is in a review of collection practices.

- (c) Expansion of choice enrollment eligibility. Energy America, Shell and the Gas Marketers' Group advocate that customers with arrears be permitted to participate and stay in the gas choice program.⁵ According to the Gas Marketers' Group, the current eligibility policy is difficult to administer and is contrary to the development of the gas choice program (as it bars customers who have difficulty paying gas costs from joining or staying in a lower cost program). Plus, the group contends that the need to financially protect the gas choice utility is eliminated with the proposed mechanism. DEO, COH and Vectren do not agree that the uncollectible mechanism is a "tradeoff" for allowing customers, once enrolled, to stay in the gas choice program when they have arrearages. DEO, COH and Vectren do not believe that customers who accrue arrearages should stay in the gas choice program; in their view, disconnection is the best tool for collecting arrearages. DEO, COH and Vectren explain that only those arrearages associated with a delinquent final account will be included in the proposed mechanism and, therefore, there is no link between the proposal and allowing nonpaying customers to remain in the gas choice programs.

- (6) Additionally, Energy America and Shell advocate that the mechanism be a rider separate from the PIPP rider because it will be easier to track, will readily identify what is being charged, and not confuse allocations among customer classes. Lastly, Energy America and Shell suggest that other costs should be unbundled (such as, billing, customer care, metering, and capacity release). DEO, COH, and Vectren responded to this latter point, arguing that the additional unbundling suggestions are inappropriate for this docket, as they expand the issues beyond the original scope.

⁵ The Gas Marketers' Group states that the joint applicants only referred to allowing customers with arrears to join a gas choice program and did not comment on allowing customers who accumulate 60 days of arrearages while in the program to remain on the gas choice program.

- (7) OCC filed comments on August 8, 2003. OCC argues that volatility in gas prices, in and of itself, is not justification for the proposed mechanism because lower gas prices can also mean less arrearages. Also, OCC states that Section 4929.22(B), Revised Code, requires customers to discharge, or enter into a payment plan to discharge, all existing arrearages *before* being enrolled in a gas choice program. Thus, OCC questions how the proposed mechanism can expand choice enrollment, unless the delinquent customers will all be placed on payment plans. Additionally, the OCC states that, with the proposed mechanism, the levels of uncollectible expenses may increase. For these reasons, OCC suggests approval only with eight mitigation measures.

On August 19, 2003, DEO, COH, and Vectren filed a response to OCC's comments. They ask that the comments be stricken since no procedural schedule was established by the Commission. Additionally, DEO, COH, and Vectren restate the jurisdictional and legal basis for the proposed mechanism. While finding no need to modify the proposal, they do not object to all of OCC's suggestions.

- (8) OCC's eight mitigation items and the companies' responses thereto are as follows:
- (a) Conduct a formal review, with a staff report, of the mechanism and company collection practices after five years. Specifically, DEO, COH, and Vectren do not object to a review of the operation of the mechanism in five years (identifying amounts received and any impact the mechanism has had on credit and collection policies). They do not agree, however, that approval of the proposed mechanism would be contingent upon any such review, arguing that such would "raise concerns for [their] auditors regarding the recoverability of deferred uncollectible expense, which would jeopardize the status of the deferrals as regulatory assets."
 - (b) Reject the joint applicants' request to control the filing of any adjustments to the amount and, instead, require annual filings for adjustments. DEO, COH, and Vectren argue that the Commission should not mandate a yearly adjustment to the amount, but they are willing to annually report the amounts recovered, deferred, and amortized.

- (c) Introduce PIPP arrearage forgiveness for those who are current on the PIPP payments, require annual PIPP rider filings, and audit the PIPP program every two years. DEO, COH, and Vectren state that they have already agreed to implement a PIPP arrearage forgiveness program.⁶
- (d) Disallow any deferrals from approval of the application to the time that it first takes effect. DEO, COH, and Vectren argue that such a moratorium on deferrals would deny the applicants a portion of the relief that they seek. They made this request because the current uncollectible expense balance will not be known until the end of the current fiscal year.
- (e) Reject any recovery through the mechanism of existing, approved deferred account receivables because the deferral accounts were set up for consideration in base rate cases. DEO, COH, and Vectren believe recovery through the mechanism (rather than a rate case that may be filed a number of years in the future) is more appropriate because it will result in a closer match between cost incurrence and cost recovery.
- (f) Require that no customers can "flex" out of the obligation to pay the uncollectible expense. DEO, COH, and Vectren point out that, under the proposal, all customers' arrearages are not recovered. They do not object to the Commission

⁶ This forgiveness program is part of a stipulation that was filed in *In the Matter of the Commission's Review of Chapters 4901:1-17 (Establishment of Credit for Residential Utility Services) and 4901:1-18 (Disconnection of Natural Gas or Electric Service to Residential Customers) of the Ohio Administrative Code*, Case No. 03-888-AU-ORD. The stipulation reflects that, upon approval of the application in this case, DEO, COH and Vectren will institute the stipulated PIPP arrearage forgiveness program. The utilities' pleading in this docket describes the program as follows: a customer's arrearage will be forgiven if he/she makes PIPP payment amounts on time and in full for 36 consecutive months. After the first 12 consecutive months of timely, full payments, the companies will credit the account by 33 percent of the outstanding amount. After the second 12 months of timely, full payments, the companies will credit the account by 50 percent of the outstanding amount. After the third 12 months of timely, full payments, the companies will credit the amount outstanding. If a customer fails to make payment in full or on time in any month, the 36-month period will start over, but the customer does not forfeit any credits received in the prior period. The stipulation in 03-888-AU-ORD also includes a provision that, once a customer completes the 36-month cycle, if the customer continues to make timely, full payments for another 12 months, the company will credit the customer's account for 100 percent of the amount outstanding. Moreover, the stipulation in 03-888-AU-ORD states that Vectren will, in addition, continue its current PIPP arrearage crediting practice, which was approved in Case No. 91-415-GA-AIR (February 20, 1992), and in Case Nos. 88-1115-GE-PIP, 90-705-GE-PIP, and 90-879-GE-ORD (December 2, 1993).

requiring that no customers who arrearages are recovered through the mechanism be exempt from the obligation to pay the amount.

- (g) Conduct an investigation of credit and collection policies as related to the choice programs and the uncollectible expense amount. DEO, COH, and Vectren believe that there is no basis for OCC's concern, stating that, if the joint applicants do not pursue collection efforts, they will be worse off than before the proposed mechanism. They reach this conclusion because they cannot collect any amounts unless the companies first undertake collection efforts.
 - (h) Require the companies to meet with staff and OCC, disclose credit and collection policies, and make appropriate improvements. DEO, COH, and Vectren do not object to meeting with staff and OCC, disclosing credit and collection policies, and making appropriate improvements that do not place an undue burden on the joint applicants or their customers.
- (9) The Consumers' Coalition states that the application does not adequately detail how the proposal will affect low-income consumers. It seeks to have additional areas considered: the elimination of current arrearages, plans for dealing with future arrearages, and weatherization provisions.

Similarly, OPAE, APAC and CAP state that the application is flawed because it shifts the risk of volatile gas costs onto customers and guarantees cost recovery. OPAE, APAC and CAP argue that the proposal is an improper attempt to "single out" one rate base element for adjustment. The three entities also argue that the proposal is a dubious attempt to avoid an evaluation of the overall rate structure of the joint applicants and to avoid filing an alternative rate plan. OPAE posits that the Commission should be skeptical of the proposed tool's guarantee of recovery of uncollectible expenses, while ignoring aggressive disconnection practices, credit counseling, and demand reduction strategies, which have successfully controlled uncollectible expenses. OPAE questions the joint applicant's willingness to allow delinquent customers to participate in gas choice programs, the contention that gas costs and weather directly impact uncollectible expenses, and the soundness of recovering deferred accounts receivable balances. OPAE, APAC and CAP all oppose the idea of

incorporating the uncollectible expenses into the PIPP rider because of the "flawed oversight of PIPP and the lack of any periodic audits of the PIPP rider."

On August 25, 2003, OPAE, The Consumers' Coalition, APAC, and CAP filed a statement of support for the proposal and a withdrawal of their earlier comments in opposition to the application. The pleading reflects that they have reached an agreement with DEO, COH and Vectren regarding a PIPP arrearage crediting program⁷ and additional contributions to new or existing weatherization programs. As a result, OPAE, The Consumers' Coalition, APAC, and CAP state that the application's impact on low-income customers is addressed.

- (10) The joint applicants have filed their application, seeking to implement an adjustment mechanism that is allowed by Section 4929.11, Revised Code. That provision states:

Nothing in the Revised Code prohibits, and the public utilities commission may allow, any automatic adjustment mechanism or device in a natural gas company's rate schedules that allows a natural gas company's rates or charges for a regulated service or goods to fluctuate automatically in accordance with changes in a specified cost or costs. (Emphasis added.)

The plain language of this statute enables the Commission to consider and implement an adjustment mechanism such as that proposed by the joint applicants for their uncollectible expenses. After all, the uncollected amounts become a cost incurred by the joint applicants, a cost for which we have historically allowed recovery through base rates.

- (11) The fundamental question before us is whether the proposed adjustment mechanism is just and reasonable. We accept the applicants' rationale supporting the proposed adjustment mechanism. There is no doubt gas costs have been volatile during the last several years. We recognize that those gas costs and the weather impact the dollar amounts of customer bills. Additionally, we are aware that gas companies across Ohio, including the applicants, have experienced difficulty in recovering their bills in full.⁸ We are not assigning blame or

⁷ The PIPP arrearage crediting program is described in footnote 6.

⁸ We have received pleadings in several different dockets in which various parties have acknowledged the difficulty that consumers have had in paying their gas bills due to the volatile gas market. See, for instance, *In the Matter of the Study of the Current State of the Natural Gas Industry in Ohio*, Case No. 01-152-GA-UNC (Citizens' Parties March 16, 2001 motion to intervene and join in the petition); *In the Matter of*

exculpating anyone for the large uncollectibles they have recently experienced.⁹ We agree that weather is not within the applicants' control. We also believe that gas costs are largely outside of the applicants' control. Certainly, the factors that the joint applicants noted as impacting gas costs (summarized in footnote 2 of this decision) are largely outside of their control. We further agree that the weather and gas costs can substantially impact the dollar amounts of customer bills.

Additionally, we do not accept that the uncollectible expense amounts allotted in applicants' rate bases so long ago (and determined at a time with very little gas cost volatility) can be appropriate at this time. OCC correctly points out that volatile gas prices include both high and low prices (which affect uncollectible levels). Yet, when extreme volatility exists, an expense recovery mechanism that moves with the volatility to allow more contemporaneous recovery of expenses or costs is an understandable business approach. In this respect, we disagree with the consumer commenters who claim that the uncollectible proposal is an improper shifting of the risk of volatile gas costs onto consumers. After all, the GCR rates would have to be considered improper shifting too and we have accepted for many years the benefits that adjusted GCR rates have provided. We believe the concept of an adjustment mechanism has practical merit.

Moreover, the concept of this proposed adjustment mechanism is not really unique. After all, the applicants' gas costs are recovered through the GCR mechanism, which adjusts based upon actual gas cost expenses. Similarly, many gas companies in Ohio recover funds for their gross receipts tax through a distinguishable rider, separate from their base rates. This separation has been approved by the Commission as reasonable because the tax fluctuates directly as the GCR rates fluctuate and, therefore, it is reasonable to have recovery

the Application of The East Ohio Gas Company d.b.a. Dominion East Ohio for Approval, Pursuant to Section 4906.16, Revised Code, of a Payment Matching Program and Other Matters, Case No. 01-2592-GA-UNC (DEO's October 4, 2001 application and October 5 and 16, 2001 supplements); In the Matter of the Application of The Cincinnati Gas & Electric Company for Authority to Modify Current Accounting Procedures for its Cost of Implementing the Commission's Disconnection Moratorium and to Implement Cost Recovery, Case Nos. 01-3227-GA-UNC and 01-3228-GA-UNC (CG&E December 14, 2001 application); and In the Matter of Columbia Gas of Ohio, Inc. for Authority to Modify Its Current Accounting Procedures for its Costs of Implementing the Commission's Moratorium on the Disconnection of Utility Service, Case No. 01-3278-GA-AAM (COH December 20, 2001 application).

⁹ We make this statement in order to point out that the onset of large uncollectible expenses was not, generally speaking, something that the applicants could have avoided altogether or extensively mitigated. We have ongoing gas cost recovery (GCR) proceedings, with audit periods covering some of the recent volatile periods. Nothing in our statements in this docket should be considered to preclude or prevent consideration of any arguments or recommendations in those GCR proceedings about the applicants' actions related to gas procurement and distribution.

of tax funds to fluctuate. We do not believe that what has been proposed in this application is conceptually different from these other fluctuating recovery mechanisms.

As additional reasons for approving the proposal, the joint applicants are willing to allow for expanded enrollments and additional purchases of supplier receivables in the DEO, COH, and Vectren gas choice programs. Many competitive retail natural gas suppliers support the proposed adjustment mechanism (albeit upon condition to change other aspects of the gas choice programs). OP&A, The Consumers' Coalition, APAC and CAP also now support the proposal, following an agreement for a PIPP arrearage forgiveness program and contributions to weatherization programs. These additional items will bring direct benefits to the consumers and competitive retail natural gas suppliers in Ohio. As OCC has pointed out, the expanded enrollment must still comply with Section 4929.22(B), Revised Code. Thus, a consumer with an arrearage can only participate in one of the joint applicants' gas choice programs if the consumer discharges the arrearage or enters into a payment plan. OCC's point that this additional benefit is subject to a statutory restriction is well taken.

- (12) We agree with the concept of the proposed adjustment mechanism package and we have authority to allow the proposed adjustment mechanism. The next question is whether the parameters proposed for the adjustment mechanism should be instituted. Many comments and suggestions were made. We agree with some of the comments made and will require some modifications to the proposed adjustment mechanism. In large part, however, we reject the comments because we feel that they address matters that extend beyond what is necessary for the joint applicants to implement a reasonable adjustment mechanism for uncollectible expenses. We directly address those comments below.

We are not willing to make the adjustments to the gas choice programs in consideration of this proposal, as suggested by Energy America, Shell and the Gas Marketers' Group. Any changes to the gas choice programs will be considered by the Commission in the context of all state gas choice programs, not just those of DEO, COH and Vectren. Nor are we going to redefine the collection process or require further unbundling of other utility costs, in consideration of this proposal. Such action is not a necessary component to the proposed adjustment mechanism.

We do not accept the joint applicants' proposal to include the uncollectible expense in their PIPP riders. We prefer to keep the recovery mechanisms for the two expenses distinguishable. Therefore, the proposed adjustment mechanism should be established through a separate rider.

We believe that it is appropriate for the joint applicants to include carrying costs. Furthermore, each company is granted the necessary authority to defer its respective uncollectible expenses for future recovery under the new mechanism, pending establishment of this new adjustment mechanism. Additionally, the companies are authorized to defer, for subsequent recovery via the uncollectible expense rider, the incremental uncollectible expenses (for the current and subsequent fiscal years) that are associated with disconnected or other final accounts above the amount of uncollectibles expense recovered in current base rates or the uncollectible expense rider once it becomes effective. Uncollectible expenses eligible for recovery via the uncollectible expense rider shall consist of that generated by the class of customers paying the uncollectible expense rider. Eligible uncollectible expenses shall also include the amount associated with the provision of competitive retail natural gas service (because the companies purchase the accounts receivable). Those companies with deferred account receivable balances authorized by the Commission in Case Nos. 01-2592-GA-UNC and 01-3278-GA-AAM are authorized to amortize those balances over 60 months commencing with the first month that the uncollectible expense rider becomes effective and shall include such amounts in the uncollectible expenses eligible for recovery.

OCC suggests that the companies should be required to make yearly filings for adjusting the mechanism. DEO, COH, and Vectren argue that yearly filings should not be mandated. We agree that yearly adjustments should not be mandated. However, the joint applicants' proposed riders should include some parameters under which they must propose to adjust the effective mechanism (e.g., if the level of uncollectibles over the prior "X" period of time is more than "Y" percent different [plus or minus] from the amount being recovered under the effective mechanism). The companies shall annually file with the Commission a report (each May) that identifies amounts recovered, deferred and, as applicable, amortized pursuant to the mechanism. That information may be contained in a request to adjust the rider rate, but must be provided via a separate filing if no adjustment to the rider rate is sought. The

companies shall provide such data as necessary to permit Commission staff and OCC to audit the amounts, validate such amounts, and determine whether the adjustments were made in accordance with the parameters.

Next, we agree that the GCR audit dockets are appropriate for evaluating each company's handling of the new adjustment mechanism. We expect the auditors to address the companies' efforts while the adjustment mechanism is being established and thereafter.

We agree to clarify that no customers whose arrearages are recovered through the mechanism may be exempt from the obligation to pay the amount. We think this is a wise clarification.

DEO, COH, and Vectren have agreed upon a PIPP arrearage forgiveness plan (as well as agreed to make contributions to weatherization programs), if we approve the application in this proceeding. The stipulation involving the PIPP arrearage forgiveness program was not filed in this docket for our consideration. Nor was any agreement related to the weatherization contributions. Therefore, we have no documents to rule upon (accept or reject) in this docket, although the signatory parties have readily acknowledged their existence. We believe that, with our approval of this application, those agreements will be triggered. We expect the parties to "live up" to their obligations in both of those agreements. However, we are not passing on the reasonableness of those agreements. We simply point out the effect our decision will have (providing many citizens of Ohio with other, additional benefits). Aside from this acknowledgement, we will not further address the PIPP program and PIPP forgiveness, as requested by OCC. It is a separate matter.

Likewise, we are not investigating the credit and collection activities of the joint applicants, as a condition under which we will approve the mechanism. We agree that, with our approval of the proposed adjustment mechanism, each of the joint applicants should be required to meet with the staff and/or OCC to disclose credit and collection policies and discuss appropriate improvements and modifications. We intend to closely monitor the companies' collection and disconnection practices and policies given the change to their recovery of uncollectible expenses. We are sensitive to the concern that the approved adjustment mechanism can impact the diligence with which the joint applicants conduct

collection. The companies shall provide credit and collection policies and procedures to staff and OCC within 60 days after Commission approval of the rider. The companies will notify staff and OCC thereafter of any changes in those policies and procedures. The companies will meet with staff and/or OCC to review credit and collection policies and procedures upon request, and will work in good faith to address issues raised by staff or OCC.

The Commission will undertake an investigation of the automatic adjustment mechanism 60 months after its implementation, as suggested by OCC. Among other things, the investigation will identify amounts recovered by the companies pursuant to the mechanism, address the impact of any changes to the companies' credit and collection policies and procedures, and any staff recommendations.

- (13) Lastly, we wish to make it clear that we have, today, approved the proposed adjustment mechanism in concept and made some minor modifications to the proposal. We did elaborate on several specific items. However, each of the joint applicants still must file proposed tariff provisions that are necessary to implement their adjustment mechanisms. We direct the joint applicants to make the tariff amendment filings (in separate dockets). We will evaluate not only whether the proposed tariffs correspond with this decision, but also whether the details of the proposal specific to each applicant are reasonable.

ORDERED, That the joint applicants' request for an expedited ruling is denied. It is, further,

ORDERED, That the motion to allow David C. Rinebolt to appear on behalf of OPAAE in this proceeding is granted. It is, further,

ORDERED, That the motions to intervene filed by OCC, Energy America, Shell, OPAAE, Consumers' Coalition, APAC, and CAP are denied. It is, further,

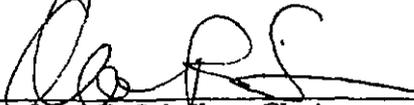
ORDERED, That the application is granted, under the terms discussed in this decision. It is, further,

ORDERED, That the joint applicants make the tariff amendment filings (in separate dockets) to implement the approved adjustment mechanism for their uncollectible expenses. It is, further,

ORDERED, That this case be close of record. It is, further,

ORDERED, That a copy of this finding and order be served upon all parties of record, all commenters and all interested persons of record.

THE PUBLIC UTILITIES COMMISSION OF OHIO



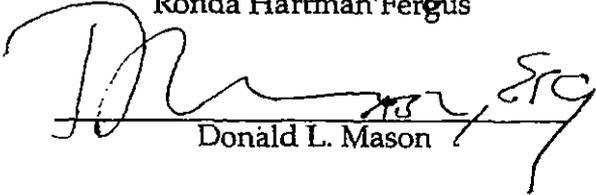
Alan R. Schriber, Chairman



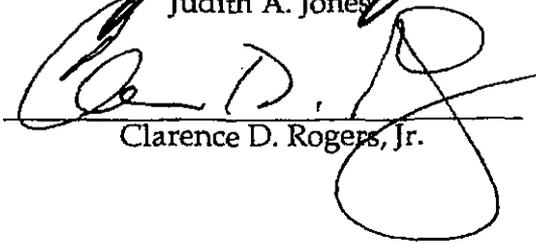
Ronda Hartman Fergus



Judith A. Jones



Donald L. Mason



Clarence D. Rogers, Jr.

GLP;geb

Entered in the Journal

DEC 17 2003



Renee J. Jenkins
Secretary

STATE OF NORTH CAROLINA
UTILITIES COMMISSION
RALEIGH

DOCKET NO. G-9, SUB 453

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of

Application of Piedmont Natural Gas)	ORDER ON REQUEST
Company, Inc., for Approval of Special)	FOR SPECIAL ACCOUNTING
Accounting Procedures)	TREATMENT

BY THE COMMISSION: On September 24, 2001, Piedmont Natural Gas Company, Inc. (Piedmont), filed a request for approval of special accounting treatment of certain costs related to uncollectible accounts during last winter. Piedmont states that high gas prices and colder-than-normal weather during November and December 2000 led to significantly higher gas bills than those for the previous winter. Piedmont took steps to mitigate the impact on customers, but still many customers generated substantial past-due balances "as a result of the extended payment arrangements and various Commission rules that limit Piedmont's ability to obtain deposits and to discontinue service for non-payment of gas bills." In Piedmont's last general rate case, Docket No. G-9, Sub 428, decided in October 2000, a total of \$1,722,278 was included in the cost of service for uncollectibles. During the period September 1999 through August 2000, Piedmont's uncollectibles were \$2,233,344, but they increased to \$5,434,621 for the period September 2000 through August 2001. The uncollectible amount of \$5,434,621 for the twelve months ended August 31, 2001, was \$3,662,343 in excess of the amount allowed in rates. By its request in this docket, Piedmont asks for permission to record a \$3,093,564 charge to its all customers' deferred gas cost account. This represents the difference between the net amount of residential accounts written off as of August 31, 2001, and the amount of residential uncollectibles allowed in rates in Piedmont's last rate case. Any subsequent collections of these written-off accounts will be recorded in the deferred account as offsets against the \$3,093,564 charge. Piedmont proposes that the uncollectibles be assigned to residential rate schedules in a later proceeding, such as the next annual gas cost prudence review.

The Chair issued an Order on October 10, 2001, requesting comments. The Commission has received comments from the Public Staff, the Attorney General, the Carolina Utility Customers Association, Inc. (CUCA), North Carolina Natural Gas Corporation (NCNG), and Public Service Company of North Carolina, Inc. (PSNC).

The Public Staff "does not oppose" the request as long as it is given no precedential effect. The Public Staff generally disfavors special accounting treatment but agrees that some form of relief is appropriate here since the Commission encouraged the LDCs to implement procedures to help residential customers pay their high gas bills last winter.

The Attorney General opposes the request as contrary to existing statutes and case law. The Attorney General says that "gas costs" recoverable under the gas cost adjustment statute, G.S. 62-133.4, do not include uncollectibles and, further, that Piedmont's proposal would amount to improper prospective ratemaking. The Attorney General says that it is not surprising that uncollectibles increased last winter since gas

rates were much higher and the weather was colder than normal. The Attorney General argues that customers bore the brunt of high gas rates last winter and that Piedmont's request would increase that burden even more.

CUCA argues that there are only three ways to modify rates (a rate case, a gas cost adjustment, and a rulemaking) and that neither applies here. Piedmont is not proposing a rate case, and a rulemaking would not be appropriate due to the differences among the LDCs. A gas cost adjustment is not appropriate since uncollectibles "are clearly not costs related to the purchase and transportation of natural gas. . ." Although Piedmont proposes recovery exclusively from residential customers, CUCA opposes any expansion of the gas cost adjustment statute. Further, CUCA argues that Piedmont should be required to show that the flexible payment measures encouraged by the Commission last winter actually caused an increase in uncollectibles before any recovery is allowed.

NCNG supports Piedmont's request and states that it will file a similar request. PSNC supports Piedmont's request as "a balanced approach to the recovery of associated write-offs," but PSNC does not anticipate seeking similar relief.

On October 24, 2001, Piedmont filed reply comments amending its request. In order to address the objections of the Attorney General and CUCA, Piedmont reduces its request for special accounting treatment from \$3,093,564 to \$2,820,028. Piedmont argues that, with this reduction, all of the amount that it now seeks to recover represents gas costs under the gas cost adjustment statute, G.S. 62-133.4.

The Attorney General filed reply comments. Among other points, the Attorney General argues that Piedmont has not shown that the increase in uncollectibles was attributable to the flexible payment measures encouraged by the Commission, that it is unfair to examine one component of rates without examining changes in other components as well, and that Piedmont's request would reverse and return to Piedmont some of the benefits that customers received through the Weather Normalization Adjustment last winter.

CUCA filed reply comments arguing that no special accounting is necessary if the amount Piedmont now seeks to recover is indeed gas costs recoverable under G.S. 62-133.4. The fact that Piedmont is seeking special accounting demonstrates that uncollectibles have never been treated as gas costs under the gas cost adjustment statute.

Piedmont made one last filing, arguing that it just wants to defer these costs now and to litigate recovery in the next gas cost prudence review, where it will bear the burden of proof and all parties will have an opportunity to be heard. Piedmont also argues that the WNA "simply has nothing whatsoever to do with this proceeding."

The Commission has considered all of the comments herein, and carefully weighed the equities as well as the law. The Commission concludes that the request for special accounting treatment should be denied. Piedmont's original petition essentially made an appeal based on equity: gas prices were high, the weather was cold, and uncollectibles went up. There are, however, serious legal obstacles to the special accounting treatment requested by Piedmont, the most fundamental of which is that the proposal focuses solely on one component of rates, without looking at changes in the utility's other expenses and revenues over the same period and without compliance with the general statutory

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

APPENDIX C

PROPOSED FINDINGS OF FACT

1. The proposed CRRC represents a material deviation from the long-standing established precedent of providing for recovery of uncollectible expense through base rates. OCA St. 1 at 15.
2. Automatic adjustment clauses should be limited to specifically identified expenses that are not under the control of management. OCA St. 1 at 15.
3. Uncollectible expense is largely within the control of PGW's management OCA St. 1 at 15.
4. Uncollectible expense does not lend itself to recovery through an automatic adjustment mechanism. OCA St. 1 at 15.
5. The proposed CRRC would reduce the incentive for PGW to maximize its collections. OCA St. 1 at 16; OSBA St. at 23-24.
6. PGW will conclude the current fiscal year on August 31, 2004 with between \$31-36 million in cash reserves. PGW St. CRRC-1R, Sch. JRB-10, Tr. 323.
7. PGW finished the fiscal year ending August 31, 2003 with \$0.1 million in cash reserves. Action Alliance Cross-Exh. 1.
8. PGW finished the fiscal year ending August 31, 2002 with \$6.0 million in cash reserves. Action Alliance Cross-Exh. 1.
9. PGW finished the fiscal year ending August 31, 2003 with \$1.7 million in cash reserves. Action Alliance Cross-Exh. 1.
10. PGW finished the fiscal year ending August 31, 2003 with \$8.4 million in cash reserves. Action Alliance Cross-Exh. 1.
11. PGW's Collection Renewal Initiative commenced in September 2003. Tr. 370.
12. The actual effects of the Collection Renewal Initiative did not start to pay results until the end of March and early April 2004. Tr. 370.
13. PGW has the highest distribution rates in the Commonwealth. OSBA St. 1 at 9.
14. An increase in rates through the CRRC will exacerbate the unaffordability of PGW's rates. OCA St. 1 at 19.
15. An increase in rates will lead to a decrease in PGW's collections rate. OSBA St. 1 at 8.

PROPOSED CONCLUSIONS OF LAW

1. The proposed CRRC will result in rates that are unjust, unreasonable, and otherwise inconsistent with the Public Utility Code and sound ratemaking policy.
2. The proposed CRRC constitutes impermissible single-issue ratemaking.
3. The proposed CRRC constitutes impermissible retro-active ratemaking.
4. The OTS alternative proposal constitutes impermissible single-issue ratemaking, is inconsistent with the Public Utility Code, and would result in rates that are unjust and unreasonable.

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

APPENDIX D

PROPOSED ORDERING PARAGRAPH

IT IS HEREBY ORDERED that the Petition of Philadelphia Gas Works to Establish a Cash Receipts Reconciliation Clause is **DENIED**.

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, the Office of Consumer Advocate's Main 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 14th day of June, 2004.

SERVICE BY E-MAIL and INTEROFFICE MAIL

Richard A. Kanaskie, Esquire
Johnnie E. Simms, Esquire
Pennsylvania Public Utility Commission
Office of Trial Staff
P.O. Box 3265
Harrisburg, PA 17105-3265

RECEIVED
2004 JUN 14 PM 4: 07
SECRETARY'S BUREAU

SERVICE BY E-MAIL and HAND DELIVERY

Daniel Clearfield, Esquire
Alan C. Kohler, Esquire
Wolf, Block, Schorr and Solis-Cohen LLP
212 Locust Street, Suite 300
Harrisburg, PA 17101

David M. Kleppinger, Esquire
Charis Mincavgage, Esquire
McNees, Wallace & Nurick LLC
100 Pine Street
P.O. Box 1166
Harrisburg, PA 17108-1166

Steven Gray, Esquire
Office of Small Business Advocate
Suite 1102 Commerce Building
300 North Second Street
Harrisburg, PA 17101

Christopher B. Craig, Esquire
Main Capitol Building
Room 545
Harrisburg, Pa 17120
Counsel for Senator Fumo, et al
District Attorney Lynne Abraham
Counsel for Senator Stack
Counsel for Senator Williams
ccraig@fumo.org

Renardo L. Hicks
Anderson, Gullotta & Hicks, PC
1110 N. Mountain Road
Harrisburg, PA 17112
Counsel for Senator Fumo, et al.

Daniel P. Delaney, Esquire
James P. Melia, Esquire
Kirkpatrick & Lockhart LLP
240 North Third Street
Harrisburg, PA 170101

SERVICE BY E-MAIL and OVERNIGHT DELIVERY

Gregory J. Stunder, Esquire
Philadelphia Gas Works
800 West Montgomery Avenue
Philadelphia, PA 19122

Mr. Robert D. Knecht
Industrial Economics Incorporated
2067 Massachusetts Avenue
Cambridge, MA 02140

Philip A. Bertocci, Esq.
Laura Moskowitz, Esq.
1424 Chestnut Street
3rd Floor
Philadelphia, PA 19102

Richard Lelash
Financial & Regulatory
18 Seventy Acre Road
Redding, CT 06896

Doreen F. Wrick
Texas Eastern Transmission LP
1284 Soldiers Field Road
Boston, MA 02135

Scott J. Rubin
3 Lost Creek Drive
Selingsgrove, PA 17870

Kent Murphy, Esquire
Amy E. Hamilton, Esquire
Exelon Business Transmission LP
2301 Market Street, S23-1
Philadelphia, PA 19103

Richard J. Kruse, Esquire
Susan Lindberg, Esquire
Texas Easter Transmission LP
P.O. Box 1642
Houston, TX 77251

Anthony R. Francioso, Esquire
Francioso & Francioso
2585 Nottingham Way
Hamilton, NJ 08619

Richard A. Baudino
J. Kennedy & Associates, Inc.
570 Colonial Park Drive, Suite 305
Roswell, GA 30075

SERVICE BY OVERNIGHT DELIVERY

Thomas E. Knudson, President
Philadelphia Gas Works
800 W. Montgomery Drive
Philadelphia PA 19122

James P. Leonard, Esquire
City Council of Philadelphia
Cooper Leonard & Schaffer
1525 Locust Street, 13th Floor
Philadelphia, PA 19102

A. Wesley Bridges, Esquire
Philip Hinerman, Esquire
Fox Rothschild, LLP
2000 Market Street
Tenth Floor
Philadelphia, PA 19103

Helen Richardson
Mondre Energy Inc
1880 John F. Kennedy Boulevard
Suite 1705
Philadelphia, PA 19135

Wendy Beetlestone, Esq.
School District of Philadelphia
Office of General Counsel
2130 Arch Street, 5th Floor
Philadelphia, PA 19103

Lance Haver, Director
Mayor's Office of Consumer Affairs
116 City Hall
Philadelphia, PA 19102

Ms. Adrienne Glenn
6342 Ardleigh Street
Philadelphia, PA 19138

Barbara Greening, Esq.
1904 Green Street
Philadelphia, PA 19130

Mr. William Kitsch
1233 Stanwood Street
Philadelphia, PA 19111

Leslie B. Hope, Esquire
Assistant City Solicitor
One Parkway, 16th Floor
1515 Arch Street
Philadelphia, PA 19102



Stephen J. Keene
Senior Assistant Consumer Advocate
Aron J. Beatty
Assistant Consumer Advocate

Counsel for
Office of Consumer Advocate
555 Walnut Street 5th Floor, Forum Place
Harrisburg, PA 17101-1923
(717) 783-5048
78018

ORIGINAL

Philip L. Hinerman
Direct Dial: (215) 299-2066
Internet Address: phinerman@foxrothschild.com

June 14, ~~2002~~ 2004

VIA FEDERAL EXPRESS

James J. McNulty, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street
Harrisburg, PA 17120

DOCUMENT
FOLDER

RECEIVED

JUN 14 2004

PA PUBLIC UTILITY COMMISSION
SECRETARY'S BUREAU

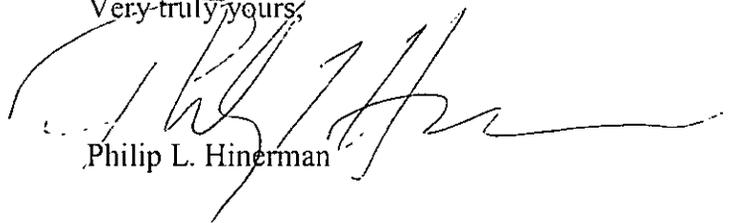
Re: Main Brief of Philadelphia Housing Authority
Docket Numbers: R-00049157 and P-00042090

Dear Secretary McNulty:

Enclosed for filing please find an original and nine (9) copies of the Main Brief of Philadelphia Housing Authority in the above-referenced matter, a copy of which is being served on the other parties. Please date-stamped and return the enclosed extra copy of this letter in the self-addressed stamped envelope provided.

Thank you for your cooperation.

Very truly yours,



Philip L. Hinerman

PLH:jcc
Enclosures

cc: Leigh Poltrock, Esquire (w/ encl., via e-mail)
Distribution List (w/ encl., via e-mail and certified mail)
Judge Charles Rainey, Jr. (w/ encl., via Federal Express)

132

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

PENNSYLVANIA PUBLIC UTILITY :
COMMISSION :

v. :

PHILADELPHIA GAS WORKS :

PETITION OF PHILADELPHIA GAS :
WORKS TO ESTABLISH A CASH :
RECEIPTS RECONCILIATION CLAUSE :

CONSOLIDATED PROCEEDING
Docket Nos. R-00049157 and
P-00042090

ORIGINAL

DOCKETED
JUN 21 2004

MAIN BRIEF OF THE INTERVENOR,
PHILADELPHIA HOUSING AUTHORITY,
TO THE PRESIDING OFFICER

DOCUMENT
FOLDER

PHILIP L. HINERMAN, ESQ.
JOHN C. COLEMAN, ESQ.
A. WESLEY BRIDGES, ESQ.
Fox Rothschild LLP
2000 Market Street, Tenth Floor
Philadelphia, PA 19103
215.299.2066

Attorney for Intervenor, Philadelphia
Housing Authority

TABLE OF CONTENTS

I. STATEMENT OF THE CASE.....1

II. SUMMARY OF ARGUMENT.....2

III. ARGUMENT.....5

IV. CONCLUSION.....15

V. PROPOSED FINDINGS OF FACT.....15

VI. PROPOSED CONCLUSIONS OF LAW.....16

VII. ORDERING PARAGRAPHS.....17

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

PENNSYLVANIA PUBLIC UTILITY :
COMMISSION :
v. :
PHILADELPHIA GAS WORKS :
PETITION OF PHILADELPHIA GAS :
WORKS TO ESTABLISH A CASH :
RECEIPTS RECONCILIATION CLAUSE :

CONSOLIDATED PROCEEDING
Docket Nos. R-00049157 and
P-00042090

RECEIVED

JUN 14 2004

PA PUBLIC UTILITY COMMISSION
SECRETARY'S BUREAU

**MAIN BRIEF OF THE INTERVENOR,
PHILADELPHIA HOUSING AUTHORITY,
TO THE PRESIDING OFFICER**

I. STATEMENT OF THE PROCEEDING

This case arises from recent attempts by Philadelphia Gas Works (“PGW”) to recoup from its paying customers, including the Philadelphia Housing Authority (“PHA”), a cash shortfall caused by a growing group of “customers” who do not pay their gas bills. PGW has continued to provide gas service to those customers for many years without seeking redress. On February 4, 2004, PGW submitted its preliminary Gas Cost Rate (“GCR”) filing to the Pennsylvania Public Utility Commission (the “Commission”), seeking to increase the rate charged to PHA (and all other paying customers). On March 1, 2004, PGW also filed a petition to impose a surcharge, or cash receipts reconciliation (“CRR”), on its customers, including PHA, to compensate PGW for the cash shortfall caused by the continuing failure of certain customers to pay their gas bills. The Administrative Law Judge granted PGW’s motion to consolidate the GCR and CRR actions into the present action. On May 4, 2004, PHA was allowed to intervene because

PHA is a ratepayer and large-scale consumer of natural gas supplied by PGW. On June 2, 2004, the Commission ordered an investigation into PGW's collection practices and finances, and consolidated an action regarding PGW's Senior Citizen Discount ("SCD") into the present action. PHA submits this Brief in accordance with the Prehearing Order of the Administrative Law Judge, dated March 14, 2004.

II. SUMMARY OF ARGUMENT

PGW is taking an unmerited step – asking its very best customers to *compensate* PGW for a financial crisis caused solely by PGW. Astoundingly, PGW hides behind the Public Utility Code (the "Code"), claiming the proposed charges merely reflect its rising cost of doing business. Such a hypothesis, if adopted, would stand the Code on its head.

The Pennsylvania Public Utility Code (the "Code") is based on a simple principle derived from the Constitution: public utilities are entitled to a reasonable rate of return on their investments. The Code actually *requires* PGW to charge for its service; Section 1301 of the Code merely demands that PGW's rate be *just and reasonable*. Whether a rate is "reasonable" involves an analysis of the utility's cost of providing service to groups of customers. Higher costs beget higher rates. Consistent with that logic, Code Section 1304 precludes PGW from discriminating *unreasonably* among customers when charging for service.

Applying that understanding to PGW's proposed charges reveals what thousands of PGW customers, many government officials and even some PGW employees already know: PGW's proposed charges cannot reasonably be construed as "costs of service," and even if they could, the proposed charges would discriminate unreasonably against

customers who consistently pay for service. According to its own website, PGW's uncollected billings approximate \$140,000,000 – equivalent to \$280 past due for *every one* of PGW's 500,000 customers. This sum did not develop overnight; it is the product of PGW's failure to manage the most basic and universal business function: *collections*. Whether sole proprietor or far-flung public company, balancing the need to collect accounts receivable with other business concerns is a fundamental requirement of business. Although it issued the occasional press release threatening to terminate delinquent customers, PGW's management never made serious or effective efforts to curb its losses. Year after year, uncollected billings climbed to ever more crippling heights, while PGW's management stood by.

PGW now asks PHA and other paying customers to fill the void left by PGW's long history of providing service to certain customers, essentially, free of charge. PGW's proposed GCR and CRR charges rest on the premise that its cost of providing service has risen because certain "customers" fail to pay their bills. Because public utilities are entitled to a reasonable rate of return, PGW concludes, the GCR and CRR increases are reasonable and justified, and the Commission, in its broad discretion to set reasonable rates, should grant PGW's requests.

That argument is not only novel in its logic, it is an unabashed effort to ignore a stark fact: the genesis of PGW's nine-digit cash shortfall is its own mismanagement of collections, not any recent rise in business costs. PGW wants the Commission to agree that the adverse financial consequences of mismanagement, left unabated for many years, can metastasize, mystically, into a cost of doing business – akin to payroll expenses or interest payments on debt. In fact, PGW's decision not to react to its problem is not a

cost of service, and therefore, cannot reasonably be passed along to paying customers like PHA. Revenues voluntarily and knowingly squandered are not reasonably construed as costs of service under Section 1301. For that reason, the request for these charges must fail.

Yet, even if the charges could somehow be construed as “costs of service,” PGW’s charges must fail under Section 1304 due to their discriminatory nature. PGW’s claim that the proposed charges will apply to “all ratepayers” is simply bogus. PGW is in this predicament precisely because, for years, PGW allowed the uncollected billings to accumulate without serious efforts to curb losses. The requested charges make paying customers such as PHA responsible for a cash shortfall caused by so-called “ratepayers” who do not pay. In fact, PHA already pays a higher rate than residential customers, whose delinquencies contributed to PGW’s financial predicament. Despite that fact, and despite the fact that PHA’s gas payments are current, PGW seeks to increase PHA’s rate based on a cash shortfall caused by other PGW customers. As the Commission acknowledged, PGW cannot treat paying customers like a bottomless well from which PGW can draw funds owed by other customers. PGW’s attempts to do so unfairly discriminate against PHA in favor of those for whom PGW has continuously provided service, essentially, free of charge. For that reason, the requested GCR and CRR charges, as applied to PHA, violate Section 1301 of the Code.

III. ARGUMENT

A. Introduction.

The record in this proceeding adduces PGW management's ineffective policies and wasteful practices. Based in part on testimony offered in this proceeding, the Commission itself has ordered an investigation into PGW's collection practices and finances. Pa. P.U.C. Opinion and Order of June 2, 2004. By requesting the GCR and CRR charges, PGW seeks compensation for the consequences of its mismanagement. The Code was not designed to reward PGW for such conduct.

Having provided service to tens of thousands of habitually delinquent customers for years, PGW has amassed an uncollected billings account that totals a staggering \$140,000,000. www.philagas.com/mediacenter/pressrelease/2004/040104.htm. That sum is the approximate equivalent of \$280 for every one of PGW's half million customers. Common sense dictates that such a massive figure can arise only where the collector, PGW, has failed to manage collections practices and service terminations. That mismanagement has crippled PGW, which now proposes the GCR and CRR charges to ameliorate the situation. In so doing, PGW implicitly offers two faulty propositions cleverly designed to comply with the Code: *first*, that its proposed charges simply reflect its increasing costs of providing service, and *second*, that the proposed charges apply to all ratepayers.

There is just one problem: the facts in this case demonstrate conclusively that neither of PGW's implied premises is true. Pennsylvania courts have held the Code will not permit PGW to shift these losses to paying customers such as PHA, which, as stipulated, pays its bills. Stipulation of PHA and PGW, Nos. 5 and 6. Code Section 1301

states, “[e]very rate made, demanded, or received by any public utility . . . shall be just and reasonable . . .” *National Utilities, Inc., v. Pennsylvania Public Utility Commission*, 709 A.2d 972 (Pa. Comm. Ct. 1998). However, from a “return on investment” perspective, PGW’s decision, effectively, to give away free gas cannot *reasonably* be construed as a compensable business expense, payable by PHA.

Even if the proposed charges were reasonable under Section 1301, Section 1304 prohibits such discriminatory charges from being applied to PHA. Section 1304 states, “[n]o public utility shall, as to rates, make or grant any unreasonable preference or advantage to any person, corporation, or municipal corporation, or subject any person, corporation or municipal corporation to any unreasonable prejudice or disadvantage. . . .” PGW’s conscious decision continuously to provide \$140,000,000 of gas service, over many years, to a massive group of habitually delinquent customers amounts to unreasonable, baseless discrimination against PHA, in violation of Section 1304.

As the following tables illustrate, PHA already pays a higher rate than PGW’s residential and municipal customers.

Table 1.1 - Present PGW Tariff Rate Comparison (per Ccf)

	Municipal Service (MS)	General Service Residential (GS-R)	Philadelphia Housing Auth. Service (PHA)
Monthly Customer Charge (Per Acct.)	\$18.00	\$12.00	\$18.00
Gas Cost Rate (GCR) *	\$0.76313	\$0.76313	\$0.76313
Delivery Charge	\$0.31470	\$0.42124	\$0.42952
Universal Service Surcharge *	\$0.11136	\$0.11136	\$0.11136
Restructuring & Consumer Education	\$0.00675	\$0.00675	\$0.00675

Surcharge *			
Commodity Total	\$1.19594	\$1.30248	\$1.31076

* Note: May change monthly, but is equivalent for all firm gas rates.

Table 1.3 - Total Modeled PHA Gas Cost

Year	Municipal Service (MS)	General Service Residential (GS-R)	Philadelphia Housing Auth. (PHA)
	2000	\$4,026,738	\$4,164,486
2001	\$5,584,651	\$5,758,705	\$5,915,096
2002	\$5,177,348	\$5,498,573	\$5,672,199
2003	\$5,936,490	\$6,436,757	\$6,545,890

By paying a higher rate for service that is, essentially, residential in nature, PHA already contributes to PGW's efforts to collect from delinquent residential customers. Subjecting PHA, which timely pays its bills, to the additional GCR and CRR charges would shift to PHA the burden of paying for service to other customers. Such a shift of charges is baseless, unreasonably discriminatory and would violate Section 1304 of the Code.

B. The Proposed Charges Violate Section 1301 and Cannot Reasonably Be Construed As Compensable Costs of Service.

Mismanagement is not a business expense, and its adverse financial consequences are not reasonably recoverable by a public utility under the Code. PGW's GCR and CRR proposals may be couched in the language of cost-of-service-based rate increases, but its nine-digit cash shortfall and near-junk debt rating have almost nothing to do with a recent rise in costs.

It is true that PGW is entitled to a reasonable rate of return on its investment under the Fourteenth Amendment to the U.S. Constitution. Pennsylvania codifies that

principle in Section 1301 of the Code, which states that public utility rates must be just and reasonable. 66 Pa. C.S.A. § 1301. However, Section 1301 cuts both ways; it entitles PGW to a reasonable rate of return, but it prohibits unreasonable, unjustifiable charges from being passed to PGW's customers, including PHA.

Pennsylvania courts have considered in the past whether Section 1301 protects the public from unreasonable charges. In *National Utilities, Inc. v. Pennsylvania Public Utility Commission*, the Commonwealth Court reviewed a Commission order denying a water utility's requested rate increase. 709 A.2d 972 (Pa. Comm. Ct. 1998). The court properly referred to Section 1301, reciting the utility's right to a reasonable return. *Id.* at 976. However, the court also considered the mountain of testimony from 133 citizens that National Utilities' services were inadequate and that its product quality was poor. *Id.* at 974. Confronting that evidence, the court made a thorough review of Section 1301's requirements, including United States Supreme Court opinions, Pennsylvania court opinions, and opinions from other jurisdictions. The court concluded that the rate increase was properly denied, noting that "[t]o hold otherwise would mean that regardless of the level of service provided by a utility, or if the utility provided no service, the [Commission] would be required to give the utility a reasonable rate of return solely because it exists." *Id.* at 979. In reaching its conclusion the court relied upon *D.C. Transit System, Inc. v. Washington Metropolitan Transit Commission*, in which the D.C. Transit System, Inc., requested changes in its fares. 466 F.2d 394, (D.C.Cir. 1972), cert. Denied, 409 U.S. 1086, 93 S.Ct. 688. In that case, the Transit Commission denied the fair increases because it found that financial instability caused by poor management decisions had led to inefficient operations. *Id.* at 417. The appellate court agreed,

quoting the Transit Commission's rationale: "[t]his . . . would be calling upon the bus rider to pay a fare to an inefficiently and uneconomically operated transit company without any assurance that the company would remedy those defects. . . . [w]e declined to impose such a one-sided and unjust burden on the bus-riding public." *Id.*

Similarly, the *National Utilities* court relied on *Petition of Valley Road Sewerage Company*, a New Jersey case, in which Valley Road applied for a rate increase. 285 N.J.Super. 2020, 666 A.2d 992 (1995). The New Jersey court denied Valley Road's request because of the company's years of financial mismanagement and failure to rectify its financial problems with proceeds from past increases. *Id.* at 208, 995. In evaluating what constituted a "reasonable" return, the New Jersey court found that the public's interest, as well as the interest of the utility, must be considered. The court found that "neither the constitution nor our state statutes require the public to pay for the consequences of lazy or inefficient management." *Id.* The intertwined nature of service and management is not novel; the *National Utilities* case was relied upon by other jurisdictions, such as Vermont, to deny rate increases where a utility's management was inefficient and its service poor. *In re: Citizens Utilities Company*, 171 Vt. 447, 769 A.2d 19 (2000). In *Citizens*, the Vermont Supreme Court relied on *National Utilities* and a host of other cases to find that Citizens' pattern of mismanagement made its requested rate increase unreasonable. PGW's proposed charges are no different than those found in the above cases. To pass such expenses to PHA and other PGW customers would be unfair, unjust and would violate Section 1301.

The record in this case establishes that PGW's service is terrible, its customer service lax, and its management of collections and service terminations dismal to the tune

of \$140,000,000 outstanding. As the *National Utilities* court and others have found, the adverse consequences of such mismanagement are not reasonably returned to a utility through such charges as the GCR and CRR. In fact, the Commission has recently expressed its grave concern for PGW's mismanagement *and* its unreasonable attempts to pass along its losses to PHA and other customers. In 2000, the Commission granted only \$11,000,000 of a \$52,000,000 rate increase requested by PGW, predicating even that reduced amount on PGW's compliance with certain conditions. *Pennsylvania Public Utility Commission v. Philadelphia Gas Works*, 94, Pa.P.U.C. 479 (2000). As the Commission noted in that proceeding, "we do not believe it is reasonable or appropriate to require ratepayers to make additional financial contributions [r]ather, we are of the view that it is particularly important to refrain from imposing any further burdens on ratepayers, given the fact[] that PGW's current situation is largely one of its own making" The Commission recognized, as recently as 2000, that PGW was mismanaged and that its efforts to pass along the costs were unreasonable. The consequences of PGW's ineptitude are no more reasonably passed to customers now than in 2000.

Most recently, on June 2, 2004, in reliance upon the testimony of witnesses in the present proceeding, the Commission ordered an investigation into PGW's collection practices and finances. Pa. P.U.C. Order dated June 2, 2004. In that Order, the Commission recounted its own "significant action" in trying to help PGW cure its financial problems, but admitted that "it appears PGW continues to face challenges regarding its financial condition and its collections process. *Id.* The Commission also stated, "[s]ome of the witnesses who testified against PGW's [CRR proceeding] argued that PGW's collection process was flawed; this supports placing PGW's collections

efforts – and steps that may be necessary to improve it – at issue in this investigation.”

Id. The scope of the investigation, the Commission ordered, should include investigation of “the adequacy, cost-effectiveness and management of PGW’s collection practices.”

Id. The Commission’s 2004 Order suggests that the problems plaguing PGW’s management in 2000 continue to be the source of PGW’s financial crisis. Nothing has changed in four years. The proposed GCR and CRR charges are mere attempts to shift the consequences of PGW’s ineffective management to its paying customers. As explained above, the Commission, Pennsylvania courts and courts in New Jersey, Vermont in elsewhere have determined that the Code is not designed to compensate PGW for such ineffective management. The GCR and CRR charges cannot reasonably be construed as costs of service, and therefore, under Section 1301, PGW’s request must fail.

C. The Proposed Charges Violate Section 1304 and Are Unreasonably Discriminatory Against PHA.

Even if the GCR and CRR charges were reasonable under Section 1304, Section 1304 prohibits PGW from applying those charges to PHA. In relevant part, Section 1304 states, “[n]o public utility shall, as to rates, make or grant any unreasonable preference or advantage to any person, corporation, or municipal corporation, or subject any person, corporation, or municipal corporation to any unreasonable prejudice or disadvantage. No public utility shall establish or maintain any unreasonable difference as to rates, either as between localities or as between classes of service.” Serving habitually delinquent customers for many years and amassing a \$140,000,000 loss amounts to preferential treatment in favor of those non-paying “customers,” and amounts to establishing and

maintaining unreasonable differences between paying and non-paying customers. That behavior alone violates Section 1303 of the Code, which prohibits any deviation from the rate set forth in PGW's tariff. Yet, PGW now seeks to subject PHA to the burden caused by its careless, yet conscious, discrimination. That request violates Section 1304.

By requesting the proposed GCR and CRR charges, PGW would have the Commission ratify its delivery of \$140,000,000 of free gas service to delinquent customers, and approve the payment of that expense by PHA. Pennsylvania courts have opined on that type of activity. In *Philadelphia Electric Company, v. Pennsylvania Public Utility Commission*, a utility company sought judicial review of a Commission order requiring a surcharge on residential customers using gas for outdoor lights. 79 Pa. Cmwlth 445, 470 A.2d 654 (Pa. Comm. Ct. 1984). While the surcharge in that case did not violate Section 1304, the court's analysis is instructive. The court properly noted that not all differences in rates are unlawfully discriminatory; to be unlawful, the discrimination must be unreasonable. *Id.*, at 450. Quoting a Pennsylvania Superior Court opinion, the court said:

Before a rate can be declared unduly preferential and therefore unlawful, it is essential that there be not only an advantage to one, but a resulting injury to another. Such an injury may arise from collecting from one more than a reasonable rate to him in order to make up for inadequate rates charged to another, or because of a lower rate to one of two patrons who are competitors in business. There must be an advantage to one at the expense of the other.

Id., quoting *Alpha Portland Cement Co., v. Public Service Commission*, 84 Pa. Superior Ct. 255 (1925). In the present matter, imposing any charge on PHA to compensate PGW for its losses resulting from inadequate, mismanaged collections unduly injures PHA to the advantage of those habitually delinquent PGW customers whom PGW elected, for

years, not to call to task. Such discrimination has no basis in cost of service differences, location, usage or any factor, other than PGW's election to provide service to certain customers who should have been terminated ages ago. In fact, PGW employee Joseph Bogdonavage admitted during the evidentiary hearing that PGW undertook no efforts to independently analyze the rate of return, or cost of service or other relevant data applicable to raising rates paid by PHA. Cross Examination of J. Bogdonavage by P. Hinerman, at 348. If PGW had made such an inquiry, it would know that PGW already pays a higher rate than residential customers, even though PHA's service is residential in nature. Stipulation of PHA and PGW, No. 2. Moreover, PHA's account is paid in full. *Id.* at Nos. 5 and 6. To ask PHA, which timely pays a higher rate than customers in the residential rate class, to pay the GCR and CRR charges, simply shifts the costs of service from delinquent customers to PHA. Because there is no basis on which to discriminate against PHA by imposing on it charges greater than the value of the service PHA receives, PGW's requested charges would unreasonably discriminate against PHA, in violation of Section 1304. As the Commission recognized in its Order of June 2, 2004, "customers of PGW who pay their bills cannot be viewed as a bottomless well of funds for [PGW's troubled] programs." Pa. P.U.C. Order, dated June 2, 2004.

The Pennsylvania Commonwealth Court also reviewed unreasonable discriminations under Section 1304 in the recent case, *Philadelphia Suburban Water Company v. Pennsylvania Public Utility Commission*. 808 A.2d 1044 (Pa. Comm. Ct. 2002). In that case, the complainant water company sought judicial review of a Commission order approving the sale of the city of Coatesville's water system to another utility. As part of the sale, the city required the purchaser to donate annually a monetary

amount at least equal to water charges that the city would incur to operate its fire hydrants. The complainant argued that such a rebate effectuated free water service to Coatesville, which deviated from the tariff rate and discriminated against customers that pay the approved rate, in violation of Sections 1303 and 1304 of the Code. *Id.*, at 1046. The court agreed.

Although the court's decision in *Philadelphia Suburban Water Company* was ultimately based on the violation of Section 1303, the court made a thorough review of Section 1304 as well. The court noted that "if the total sum demanded from one customer is illegally high and illegally low for another, there is rate discrimination." *Id.*, at 1059. The court went on to conclude that "free service," such as Coatesville would receive if the purchasing utility's "charges" were not actually collected, but rather rebated to the city, "is necessarily an illegally low charge." *Id.*, at 1061. There, as here, the utility's rate was not actually being demanded of a particular customer. In the case of Coatesville, the water bills would be "paid," but unlawfully, and entirely, reimbursed to the city. Similarly, PGW has allowed its delinquent customers to receive free service, only now seeking to recover the charges – from PHA and other paying customers. In both cases, the burden thereby placed on paying customers, such as PHA, is unfair, and additional charges based thereon, such as the GCR and CRR, are unreasonably discriminatory, in violation of Section 1304.

IV. CONCLUSION

As to PHA, the Commission must deny PGW's proposed GCR and CRR charges because such charges would violate Sections 1301 and 1304 of the Public Utility Code. The proposed charges violate Section 1301 because the adverse financial consequences and poor service resulting from PGW's notorious lack of management acumen are not justly and reasonably passed along to PGW's best customers, such as PHA. Previous opinions of the Commission, and of Pennsylvania courts, demonstrate that the requested charges simply are not reasonable given PGW's historic failure to rectify its financial problems. Furthermore, even if the proposed charges were reasonable, the application of such charges to PHA would violate Section 1304. Having violated Section 1303 of the Code by deviating from its tariff, effectively rendering free service for years to habitually delinquent customers, PGW cannot now shift those costs to PHA, which is not contributing to the delinquent figure. Stipulation of PHA and PGW, No. 6. To do so would award, without any reasonable basis, preferential treatment to PGW's non-paying customers, at the expense of PHA. Thus, Section 1304 precludes PGW from charging PHA for such losses.

V. PROPOSED FINDINGS OF FACT.

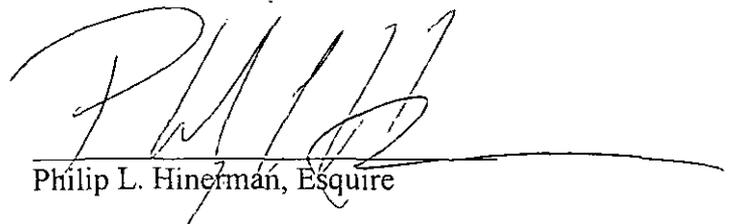
1. The PGW tariff sets the following five firm rates: (1) Residential GS/PHA GS Rate; (2) Commercial GS-MUN GS Rate; (3) Industrial GS Rate; (4) the Philadelphia Housing Authority Rate; and (5) Municipal (MS) Rate.

2. PHA's rate for delivery charge and commodity charge are, per cubic foot, more than the Residential GS/PHA GS and Municipal (MS) Rates.

3. From 2001 to 2003, PHA has paid approximately 18 million dollars for the accounts billed under the PHA rate. This amount does not include scattered sites and/or vendor accounts billed under other rates.
4. PHA receives its financing to pay PGW through the Housing and Urban Development Program ("HUD").
5. PHA has paid in full all of its PGW charges on accounts billed under the PHA Rate as set forth in Paragraph 3.
6. PHA is not contributing to the underlying uncollectible accounts for bills under the PHA Rate on this date.
7. PGW's proposed GCR and CRR charges would be unreasonable and unjust under Code Section 1301.
8. PGW's proposed application of the GCR and CRR charges to PHA are unreasonably discriminatory under Section 1304.

VI. PROPOSED CONCLUSIONS OF LAW

1. PGW's proposed GCR and CRR charges would violate Section 1301 of the Public Utility Code.
2. PGW's proposed application of the GCR and CRR charges to PHA would violate Section 1304 of the Public Utility Code.


Philip L. Hinerman, Esquire

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

PENNSYLVANIA PUBLIC UTILITY	:	
COMMISSION	:	
	:	CONSOLIDATED PROCEEDING
v.	:	Docket Nos. R-00049157 and
	:	P-00042090
PHILADELPHIA GAS WORKS	:	
	:	
PETITION OF PHILADELPHIA GAS	:	
WORKS TO ESTABLISH A CASH	:	
RECEIPTS RECONCILIATION CLAUSE	:	

**ORDER DENYING PHILADELPHIA GAS WORKS GAS COST RATE
REQUEST AND PETITION TO ESTABLISH A CASH RECEIPTS
RECONCILIATION CLAUSE, AS APPLIES TO
THE PHILADELPHIA HOUSING AUTHORITY**

The requests of Philadelphia Gas Works regarding the Gas Cost Rate increase and the petition to establish a cash receipts reconciliation clause, as applied to the Philadelphia Housing Authority, are denied.

DATE: _____, 2004

Charles E. Rainey, Jr.
Administrative Law Judge

CERTIFICATE OF SERVICE

I, PHILIP L. HINERMAN, do hereby certify that service of a true and correct copy of the within Main Brief of the Intervenor, Philadelphia Housing Authority, to the Presiding Officer was made this 14th day of June, 2004, upon the individuals listed below, in conformity with the requirements of 52 Pa. Code § 1.54:

VIA E-MAIL AND HAND DELIVERY:

Johnnie Simms, Esq.
Office of Trial Staff
Pennsylvania Public Utility Commission
The Commonwealth Keystone Building
400 North Street
Harrisburg, PA 17120
josimms@state.pa.us

Stephen Keene, Esq.
Office of Consumer Advocate
555 Walnut Street, Forum Place - 5th Fl.
Harrisburg, PA 17120
skeene@paoca.org

Daniel Clearfield, Esq.
Wolf, Block, Schorr and Solis-Cohen LLP
212 Locust Street
Suite 300
Harrisburg, PA 17101
dclearfield@wolfblock.com

Christopher B. Craig, Esq.
Senate Democratic Appropriations
Committee
Room 545, Main Capitol Building
Harrisburg, Pennsylvania 17120
ccraig@fumo.com

Steven C. Gray, Esq.
Office of Small Business Advocate
Suite 1102, Commerce Building
300 North Second Street
Harrisburg, PA 17101
sgray@state.pa.us

VIA E-MAIL AND FEDERAL EXPRESS

Charis Mincavage, Esq.
McNees Wallace & Nurick, LLC
100 Pine Street
P.O. Box 1166
Harrisburg, PA 17108
cmincavage@mwn.com

Philip A. Bertocci, Esq.
Community Legal Services, Inc.
1424 Chestnut Street, 3rd Floor
Philadelphia, PA 19102
pbertocci@clsphila.org

James J. McNulty, Secretary
Pennsylvania Public Utility Commission
The Commonwealth Keystone Building
400 North Street, 2nd Floor
Harrisburg, PA 17120

Judge Charles E. Rainey, Jr.
1302 Philadelphia State Office Building
1400 West Spring Garden Street
Philadelphia, PA 19130



Philip L. Hinerman, Esquire
Attorney for Intervenor,
Philadelphia Housing Authority

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

PENNSYLVANIA PUBLIC	:	
UTILITY COMMISSION, <u>et. al.</u> ,	:	DOCKET NO. R-00049157
	:	
Intervenor,	:	
	:	
v.	:	
	:	
PHILADELPHIA GAS WORKS	:	
	:	
Defendant,	:	
	:	

STIPULATION

Pursuant to certain provisions of the Pennsylvania Rules of Civil Procedure, Intervenor, The Philadelphia Housing Authority (“PHA”), and Defendant, Philadelphia Gas Works (“PGW”), by and through their undersigned counsel, hereby stipulate to the following:

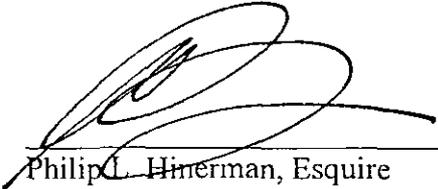
1. The PGW tariff sets the following five firm rates: (1) Residential GS/PHA GS Rate; (2) Commercial GS-MUN GS Rate; (3) Industrial GS Rate; (4) the Philadelphia Housing Authority Rate; and (5) Municipal (MS) Rate.
2. PHA’s rate for delivery charge and commodity charge are, per cubic foot, less than the Commercial GS/MUN GS and Industrial GS Rates, but more than the Residential GS/PHA GS and Municipal (MS) Rates.

3. From 2001 to 2003, PHA has paid approximately 18 million dollars for the accounts billed under the PHA rate. This amount does not include scattered sites and/or vendor accounts billed under other rates.

4. PHA receives its financing to pay PGW through the Housing and Urban Development Program ("HUD").

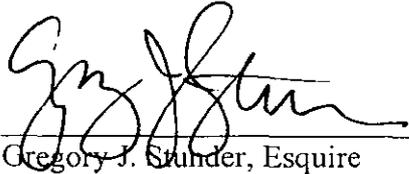
5. PHA has paid in full all of its PGW charges on accounts billed under the PHA Rate as set forth in Paragraph 3.

6. PHA is not contributing to the underlying uncollectible accounts for bills under the PHA Rate on this date.



Philip L. Hinerman, Esquire
John C. Coleman, Esquire
A. Wesley Bridges, Esquire
FOX ROTHSCHILD LLP
2000 Market Street, 10th Floor
Philadelphia, PA 19103-3291

Attorneys for Intervener Philadelphia
Housing Authority



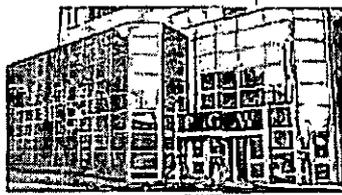
Gregory J. Stunder, Esquire
PHILADELPHIA GAS WORKS
8900 West Montgomery Avenue
Philadelphia, PA 19122

Attorney for Defendant Philadelphia
Gas Works

Dated: June 9, 2004



[Customer Service](#) |
 [Assistance Programs](#) |
 [Requesting Gas Service](#) |
 [Gas Choice](#) |
 [Careers at PGW](#) |
 [Media Center](#)



Media Center

- › [Good Gas News](#)
- › [Media Contacts](#)
- › **Press Releases**
 - 2004 Press Releases
 - 2003_Press_Releases
 - 2002_Press_Releases
- › [Community Service](#)
- › [About Us](#)

[Home](#) > [Media Center](#) > 2004 Press Releases

PGW BEGINS TO SHUT OFF SERVICE

(Philadelphia, PA – April 1, 2004) – The Philadelphia Gas Works (PGW) is now shutting off service to customers who are more than thirty days past due on their gas bills and have not made any effort to contact the company to make payment arrangements. More than 130,000 customers owe in excess of \$140 million in unpaid debt to the company.

PGW urges low-income customers who have received a shut off notice to apply for a LIHEAP and/or CRISIS grant before this year's program ends on April 9.

"With the end of the winter restrictions on turning off customers, we will seek payment and payment arrangements from our customers. We will employ the most aggressive turn-off program in recent memory to get our message across," said Thomas Knudsen, PGW President and CEO.

To prevent shut off, customers who have past due accounts should mail their payments as soon as possible, or make payment arrangements by contacting PGW at 215-235-1777. Customers also may pay by check or with their Visa or MasterCard over the telephone, or make payment arrangements at one of PGW's six customer service centers.

PGW's six Customer Service Centers are normally open from 9 a.m. until 5 p.m. on the designated days as follows:

Center City, 1137 Chestnut Street – Monday, Tuesday, Thursday and Friday.
 Frankford, 4410 Frankford Avenue – Tuesday, Thursday and Friday.
 Germantown, 210 W. Chelton Avenue – Tuesday, Wednesday and Friday.
 North Philadelphia, 1337 W. Erie Avenue – Monday, Wednesday and Thursday.
 South Philadelphia, 1601 S. Broad Street – Monday, Wednesday and Thursday.
 West Philadelphia, 5230 Chestnut Street – Monday, Tuesday, Wednesday and Friday.

Founded in 1836, PGW is the nation's largest municipally owned natural gas utility, serving a half million residential, commercial, and industrial customers in the City of Philadelphia.

[Back to top](#)

OALJ Hearing Report

Please check Those Blocks Which Apply

Docket No.:	R-00049157 & P-00042090	Prehearing Held:	<input type="checkbox"/>	<input type="checkbox"/>
Case Name:	Pennsylvania Public Utility Commission v. Philadelphia Gas Works	Hearing Held:	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Petition of Philadelphia Gas Works to Establish a Cash Receipts Reconciliation Clause		Testimony Taken:	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Location:	Philadelphia, PA	Transcript Due:	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Date:	May 20, 2004	Hearing Concluded:	<input checked="" type="checkbox"/>	<input type="checkbox"/>
ALJ:	Charles E. Rainey, Jr.	Further Hearing Needed:	<input type="checkbox"/>	<input type="checkbox"/>
Reporting Firm:	Commonwealth Reporting	Estimated Add'l Days:		
<p style="text-align: center;">DOCUMENT FOLDER</p>		RECORD CLOSED:	<input type="checkbox"/>	<input type="checkbox"/>
		DATE:		
<p style="text-align: center;">RECEIVED</p> <p style="text-align: center;">JUN 15 2004</p> <p style="text-align: center;">PA PUBLIC UTILITY COMMISSION SECRETARY'S BUREAU</p>		Briefs to be Filed:	<input type="checkbox"/>	<input type="checkbox"/>
		DATE:		
<p style="writing-mode: vertical-rl; transform: rotate(180deg);">RECEIVED OFFICE OF CALJ 04 JUN 14 11:10:49 PA PUC</p>		Bench Decision:	<input type="checkbox"/>	<input type="checkbox"/>
		REMARKS:	<i>Public input hearing held at George Washington High School.</i>	

PLEASE PRINT CLEARLY - Incomplete Information may result in delay of processing.

Name and Telephone Number	Address	Who are you representing?
ANGELA T. JONES Telephone: 717-783-2525	1102 COMMERCE BLDG. 300 N. 2ND ST. City: HBG, State: PA, Zip: 17101	OFFICE OF SMALL BUSINESS ADVOCATE
RENARDO L. HICKS Telephone: 717-541-1194	1110 N. MOUNTAIN RD City: H36, State: PA, Zip: 17112	SENATOR FUMO, ET. AL
Johnnie E. Gimms Telephone: (717) 787-1976	P.O. Box 3265 City: HBG, State: PA, Zip: 17105	Office of TRIAL STAFF
	E-mail Address: anjones@state.pa.us	Fax Number: 717-783-2831
	E-mail Address: rhicks@abtwes.com	Fax Number: 717-541-5452
	E-mail Address:	Fax Number: (717) 772-2677

Check this box if additional parties or attendees appear on back of form.

William J. Hunt
Reporter's Signature

Note: Completion of this form does not constitute an entry of appearance, see 52 Pa. Code §§1.24 and 1.25.

Name and Telephone Number	Address	Who are you representing?
Irwin Popowsky 717-783-5048 Telephone: 717-783-5048	555 Walnut St, 5th Floor, Forum Place City: Harrisburg State: PA Zip: 17101 E-mail Address: ipopowsky@procd.org	PA Office of Consumer Advocate Fax Number: 717-783-7152
Dan Clearfield Wolf Block Telephone: (717) 237-7173	212 Locust St City: Harrisburg State: PA Zip: 17110 E-mail Address:	PCW Fax Number:
Philip A. Bertocci Telephone: 215-981-3902	Community Legal Services 1424 Chestnut St 4th Fl City: Philadelphia State: PA Zip: 19102 E-mail Address: pbertocci@clbphil.org	Teachers Action Group Action Alliance of Senior Citizens ALCORN Fax Number: 215 981-0435
Telephone:	City State Zip E-mail Address:	Fax Number:
Telephone:	City State Zip E-mail Address:	Fax Number:
Telephone:	City State Zip E-mail Address:	Fax Number:
Telephone:	City State Zip E-mail Address:	Fax Number:
Telephone:	City State Zip E-mail Address:	Fax Number:
Telephone:	City State Zip E-mail Address:	Fax Number:
Telephone:	City State Zip E-mail Address:	Fax Number: