OSBA STATEMENT NO. 1

APR 26 2007

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Petition of Duquesne Light Company for Approval of Default Service Plan for the Period January 1, 2008 Through December 31, 2010	: : :	DOCKET NO. P-00072247

Direct Testimony of

BRIAN KALCIC

On Behalf of the

Office of Small Business Advocate

Date Served: March 29, 2007

Date Submitted for the Record: _____

Direct Testimony of Brian Kalcic

Q. Please state your name and business address.

A. Brian Kalcic, 225 S. Meramec Avenue, St. Louis, Missouri 63105.

Q. What is your occupation?

A. I am an economist and consultant in the field of public utility regulation, and principal of Excel Consulting. My qualifications are described in the Appendix to this testimony.

Q. On whose behalf are you testifying in this case?

A. I am testifying on behalf of the Office of Small Business Advocate ("OSBA"), which is representing small business customers served by Duquesne Light Company ("Duquesne" or "Company").

Q. What is the subject of your testimony?

A. I will examine and critique various aspects of Duquesne's proposed Default Service Plan ("Plan") for Small Commercial and Industrial ("Small C&I") customers covering the period from January 1, 2008 through December 31, 2010. In Section I of my testimony, I provide a general overview of the Company's Small C&I default service proposal. In Section II, I critique the primary elements of Duquesne's Small C&I Plan, and explain how and why the Commission should modify it.

Q. Will your testimony provide an evaluation of the Company's proposed Plan as it relates to Duquesne's residential, lighting or large commercial and industrial rate classes?

A. No. However, I will highlight certain important differences in the Company's Plan for residential and Small C&I customers, and explain why such differences are inappropriate.

Q. Please summarize your major findings and recommendations.

A. Based upon my analysis of Duquesne's filing, I find that:

- Duquesne's proposed Market Price Multiplier adjustment mechanism is contrary to Commission policy and fatally flawed;

- The Company's arguments in support of its proposal to adjust only Small C&I rates in 2009 and 2010 are without merit;

- The Commission should order Duquesne to offer Small C&I customers a default service rate that is fixed for three years; and

- The Commission should adopt Duquesne's proposal to phase out its existing Small C&I declining-block energy charges and demand charges over the three-year Plan period.

The specific details associated with my findings and recommendations are discussed below.

I. Small C&I Plan

Q. Mr. Kalcic, please provide a general overview of Duquesne's Small C&I proposal.

A. Duquesne proposes to offer Small C&I customers a fixed-price default service option for the 2008-2010 Plan period. All default service supply would be provided by Duquesne's affiliate, Duquesne Power LP ("Duquesne Power"), under the terms of a full requirements contract entered into by Duquesne Power and the Company. Default service generation rates in 2008 would be based upon the Company's estimate of the prevailing market price to serve Small C&I customers, as determined at the time of Duquesne's filing. The Company's default service rates would subsequently be adjusted annually in 2009 and

2010 based upon a Market Price Multiplier ("MPM") index. The MPM is intended to measure changes in market price levels from the date of the Company's filing.

In addition, Duquesne proposes to modify its current generation-related rate structure. In particular, the Company would phase out its existing declining-block energy charges and demand charges over the three-year Plan period, so that as of January 1, 2010, a single flat-rate energy (i.e., $/kWh) charge would apply to all Small C&I customers who chose to remain on default supply service.

Q. Which rate classes are included in the Company's Small C&I rate group?

A. The Small C&I rate group includes the Rate GS/GM – General Service Small and Medium ("GS/GM") and Rate GMH – General Service Medium Heating ("GMH") classes.[1]

Q. What is the Company's estimate of the prevailing market price to serve Small C&I customers in 2008?

A. Duquesne estimates that the prevailing market price averages 7.083¢ per kWh.

Q. How does this rate compare to the current generation rates paid by Small C&I customers?

A. At present, GS/GM customers taking default service pay an average rate of 6.46¢ per kWh. GMH customers pay an average rate of 5.48¢ per kWh. However, these rates include ancillary services and a PJM surcharge of 0.0708¢ per kWh.

Under the Company's Plan, ancillary services (of 0.2175¢ per kWh) and PJM administrative costs (of 0.0408¢ per kWh) would be recovered via the Company's Transmission Service Charge ("TSC") rather than the generation charge. Therefore, the Company's

[1] Rate GS/GM is limited to non-residential customers with peak loads less than 300 kW. Rate GMH is applicable to non-residential electric heating customers, where the customer's electric heating usage comprises at least 25% of the customer's entire electric energy requirements during the heating season.

equivalent 2008 prevailing market price of "generation" for Small C&I customers would be approximately 7.34¢ per kWh.[2] Accordingly, GS/GM customers would experience an average 2008 generation increase of 13.6% (i.e., 7.34¢ divided by 6.46¢) under Duquesne's Plan.

Q. What would be the increase for GMH customers?

A. Duquesne is proposing to phase in the GMH increase over the course of the Plan. For 2008, the equivalent GMH generation rate would be 6.42¢ per kWh, which is an increase of 17.2%. For 2009, the average GMH generation rate would increase by 7.2% to 6.88¢ per kWh. In 2010, the average GMH generation rate would increase by 6.7% to 7.34¢ per kWh. The effective cumulative GMH increase from 2007 to 2010 would be 33.9% (i.e., 7.34¢ divided by 5.48¢), excluding any changes that may result from Duquesne's proposed MPM adjustment.

II. Assessment of Plan Components

Q. What components of Duquesne's proposed Small C&I Plan will you examine in this portion of your testimony?

A. I will look at the three (3) primary components of Duquesne's Plan: 1) the determination of prevailing market prices; 2) the proposed MPM adjustment mechanism; and 3) the Small C&I rate design.

Prevailing Market Price

Q. Mr. Kalcic, how did Duquesne determine the current prevailing market price of generation for Small C&I customers?

A. In brief, the Company examined the results of thirteen (13) full requirements competitive supply solicitations for Small C&I customers. The solicitations involved eleven (11) utilities located in New Jersey, Maryland, Illinois and Pennsylvania, which occurred over a period

[2] Adding 7.083¢ plus 0.2175¢ plus 0.0408¢ equals 7.3413¢ (per kWh).

from December 5, 2005 through September 9, 2006. In a first step, the Company proceeded to adjust each of the results for known differences in lines losses, network transmission costs, ancillary service costs and taxes.[3] Next, Duquesne further adjusted the solicitation results for its estimate of the differences in the market cost of energy, based upon the region and time period in which the solicitation took place.[4] Finally, the Company averaged its adjusted solicitation outcomes and added a risk premium (to account for alleged differences in asymmetrical risk to be borne by Duquesne Power) to arrive at its estimate of the current prevailing market price of generation applicable to its Small C&I customers.

Q. Have you attempted to replicate the Company's Small C&I prevailing market price analysis?

A. No. While I have reviewed Mr. Fisher's workpapers, the compressed schedule in this proceeding did not allow enough time for the OSBA to replicate Mr. Fisher's analysis or to test the sensitivity of his results to changes in underlying assumptions (i.e., conduct a sensitivity analysis).

Q. Do you have any general comments on Mr. Fisher's market price analysis?

A. Yes. Based upon my review, I conclude that Mr. Fisher's initial adjustments for definitional differences in market prices are both straightforward and appropriate. However, his adjustments for locational and timing differences are more difficult to evaluate.

In general, Mr. Fisher's methodology for measuring locational and timing differences employs large data sets containing, in part, hourly loads and prices applicable to specific utilities and PJM zones, over various time periods. In order to conduct a proper evaluation of the Company's methodology, I would, at a minimum, have attempted to

[3] Duquesne refers to these factors as *definitional* differences.

[4] These *locational and timing* adjustments are intended to reflect the overall change in a given solicitation's result, relative to the Duquesne Delivery Zone, that might be expected due to differences in energy and capacity prices, load shapes (e.g., peak versus off-peak load profiles), delivery periods and the points in time when prices were established.

replicate the Company's results and to perform a detailed sensitivity analysis. However, given the volume of data used in Mr. Fisher's analysis, it was not possible for me to complete such an undertaking in the time allowed to prepare direct testimony. As such, while I agree that one should adjust for the locational and timing differences identified by Mr. Fisher, I am unable to offer an opinion as to whether Mr. Fisher has properly quantified these important factors.

Finally, with respect to Duquesne's proposed asymmetrical risk adjustment, I would note that while Mr. Fisher has identified certain class-specific risk premiums that would be acceptable to Duquesne Power, he has not, in my opinion, justified the absolute levels of those premiums (i.e., shown that they are market based).[5]

Q. Has Duquesne adequately demonstrated that its proposed Small C&I default service rate of 7.083¢ per kWh properly reflects prevailing market prices?

A. In my opinion, it has not.

Market Price Multiplier

Q. Mr. Kalcic, please describe Duquesne's proposed MPM adjustment mechanism in greater detail.

A. The Company's MPM would be used to adjust Small C&I default service rates on January 1, 2009 and January 1, 2010. The 2009 adjustment would be based on a comparison of a measure of wholesale electricity forward prices for 2009, calculated around the time of Duquesne's filing, to a later measure of wholesale electricity forward prices for 2009, taken as of October 1, 2008. For example, if the proposed MPM index shows that 2009 wholesale market prices, as of October 1, 2008, have risen by 10% since the date of Duquesne's filing, the Company would increase its average 2009 Small C&I default

[5] Duquesne Power has agreed to generation rates that include a risk premium of $3.00 per MWh for the Company's residential and lighting classes, and a premium of $1.50 per MWh for Duquesne's Small C&I customers.

service rate by 10%, or from 7.083¢ per kWh (in 2008) to 7.7913¢ per kWh beginning January 1, 2009. Similarly, the 2010 adjustment would be based on a comparison of a measure of the level of wholesale electricity forward prices *for 2010*, calculated around the time of Duquesne's filing, to the level of wholesale electricity forward prices for 2010, measured as of October 1, 2009.

Q. Could Duquesne's proposed MPM adjustment result in a decrease in Small C&I default service rates in 2009 or 2010?

A. Yes, it could.

Q. How does Duquesne propose to measure wholesale electricity forward prices?

A. The Company proposes to average the electricity market prices from twenty consecutive trading days at the PJM Northern Illinois Hub ("NiHub") market, as reported by NYMEX.

Q. Why does Duquesne propose to rely on the NiHub market for price information?

A. The Company states that NiHub represents a liquid trading market located in PJM, and that the historical price differences between NiHub and the Duquesne Zone have been "low and relatively stable."

Q. Are there other liquid trading markets located in PJM?

A. Yes.

Q. Could Duquesne just as easily have chosen an alternative PJM trading hub when developing its proposed MPM?

A. In theory, yes.

Q. Would the resulting MPM adjustment, as calculated by the Company, be the same in such instances?

A. In all likelihood, no. In order for a different trading market to produce the same MPM adjustment as NiHub, the relative change in average

trading prices over time would have to be *exactly* equal across the two trading hubs.

Q. What does this suggest about the Company's proposed MPM adjustment mechanism?

A. It suggests that the MPM adjustment mechanism would produce arbitrary results.

Q. Are there any other problems with the Company's proposed MPM?

A. Yes. Recall that Duquesne is proposing to measure changes in wholesale electricity prices based upon NiHub market activity over 20 consecutive trading days. In essence, Duquesne uses the market activity over these 20 trading days as a proxy for the price that a default supplier would pay for generation if it were to acquire 100% of its default service requirements in that particular market, *within that same 20 day window*. To make matters worse, Duquesne proposes to use the 20 days ending on October 1, 2008 and October 1, 2009, i.e., during the height of the hurricane season, to adjust Small C&I generation rates in 2009 and 2010, respectively.

As evident from Pike County Light and Power Company's ("Pike") experience in 2005, wholesale electricity prices can fluctuate wildly during the hurricane season.[6] As a result, one may conclude that no rational default supplier would propose to acquire 100% of its default service requirement over a twenty-day period in September of each year. Yet, the Company's proposed MPM adjustment mimics just such illogical behavior.

Q. Does the Commission support a policy of acquiring 100% of a utility's default service requirements during one month of the year?

[6] Hurricane Katrina had made landfall as a category 4 storm on August 29, 2005. Subsequently, Pike acquired 100% of its default service requirements in October 2005, which resulted in a total bill increase of approximately 70% to the average Pike customer.

A. I do not believe so. In fact, it is my understanding that the Commission initiated a proceeding to determine what "went wrong" in the 2005 Pike solicitation, so as to avoid a repeat of that outcome in the future. Pike met 100% of its default service requirements on a single day. Although Duquesne proposes to base its MPM on 20 trading days, those 20 days would be consecutive and would fall in the middle of the hurricane season. Therefore, I believe that Duquesne would be as vulnerable to a price spike as Pike was and that the Commission's policy is to avoid a repeat of that problem.

Q. What do you conclude from the above discussion?

A. I conclude that Duquesne's proposed MPM adjustment mechanism is contrary to Commission policy and fatally flawed.

Q. Mr. Kalcic, is Duquesne proposing to use its MPM methodology to adjust the Company's residential generation rates in 2009 and 2010?

A. No, it is not. Instead, Duquesne is proposing to offer its residential customers a fixed default service generation rate of 7.156¢ per kWh in all three years of its Plan.[7]

Q. Historically, has Duquesne always treated its residential and Small C&I customers differently with respect to the frequency of price adjustments?

A. No. In fact, the opposite is true.

Q. Why is the Company proposing to treat its residential and Small C&I customers differently in its proposed Plan?

A. The Company presents two arguments in support of its approach. First, the Company argues that Small C&I customers in the United States "generally have somewhat higher switching levels than residential customers, indicating that Small C&I customers are somewhat more

[7] The Company would phase-in the generation rates applicable to RH and RA customers.

sophisticated about their service options and have more opportunities to shop than do residential customers."[8] Second, Duquesne states that based upon the input it received from electric generation suppliers ("EGSs"), it was deemed important that Duquesne "make further progress toward exposing more customers to shorter-term market price signals."[9] As a result, Duquesne decided to "reset" Small C&I (but not residential) prices in 2009 and 2010 using a market price index.

Q. Do you agree with the Company's first argument?

A. No, I do not. If the Company wishes to argue that customer-switching levels are a valid proxy for inherent differences in customer class "sophistication" levels and shopping opportunities, it should at least look at the customer switching evidence available from its own service territory.

Table 1 below shows the percent of Duquesne's residential and commercial customers served by alternative suppliers over the 2000-2007 time period. In all but one instance (i.e., January 2006), customer-switching rates were higher for residential customers than commercial customers. Using the Company's reasoning, Table 1 would suggest that Duquesne's Plan is exactly backwards, i.e., it is Duquesne's residential customers who should be exposed to shorter term market price signals, not its commercial customers.

[8] See page 11 of Duquesne Statement No. 3 and Duquesne's response to OSBA-I-8.

[9] See page 12 of Duquesne Statement No. 2.

Table 1
Percent of Duquesne Customers Served by Alternative Suppliers,
by Customer Class
2000-2007

For Jan. 200	*Residential*	*Commercial[a]*
2000	22.2%	17.5%
2001	33.6%	15.9%
2002	30.1%	16.7%
2003	26.8%	17.6%
2004	24.9%	20.5%
2005	23.4%	19.5%
2006	19.7%	20.3%
2007	17.3%	15.8%

Source: Pennsylvania Office of Consumer Advocate, at
www.oca.state.pa.us/Industry/Electric/elecstats/instat.htm
a/ Commercial class is not restricted to GS/GM and GMH.

Q. Do you wish to comment on the Company's second argument?

A. Yes. In essence, Duquesne has accepted the EGSs' position that more frequent price changes will result in a greater number of Small C&I customers shopping. In order to examine the validity of that argument, I have prepared Table 2 below which shows the average 2007 generation rate paid by GM customers that are currently taking default service from the Company, by customer size, along with the percent of total GM customers within each customer segment.

Q. What does Table 2 show?

A. Table 2 shows that non-shopping GM customers with peak loads less than 25 kW currently pay 8.00¢ per kWh for generation service, while non-shopping GM customers with peak loads greater than 25 kW currently pay 6.07¢ per kWh. According to Duquesne's estimate of prevailing market prices, the 0-25 kW customers segment is currently paying in excess of the prevailing market price of 7.083¢ per kWh,

while the 25+ kW customer segment is currently paying less than market.

Under Duquesne's Plan, all GM customers would be brought to market (i.e., 7.083¢) by January 1, 2010. However, if approximately 73% of GM customers are currently paying, on average, almost 1¢ per kWh over the prevailing market price of electricity, *and still have not chosen to shop in significant numbers*, it is difficult to imagine that *reducing* their default service rate to market would be likely to cause more of these customers to switch to an alternative supplier, with or without subsequent annual "market price" adjustments. [10]

Table 2
Average 2007 Generation Rates Paid by Non-Shopping
GM Customers, by Customer Segment
(¢/kWh)

GM Customer Segment	*Average 2007 Rate*	*Percent of Customers*
0-25 kW	8.00¢	72.7%
25.1 kW and above	6.07¢	27.3%
Total GM	6.44¢	100.0%

Source: Duquesne response to OSBA-I-2 and OSBA-I-3.

Q. What do you conclude from Tables 1 and 2?

A. I conclude that Duquesne's arguments in support of its proposal to adjust only Small C&I rates in 2009 and 2010 are without merit. Accordingly, Duquesne's proposal to adjust Small C&I prices should be rejected by the Commission.

Q. Is there any other reason to reject the Company's proposal to adjust Small C&I prices?

A. Yes. First, counsel informs me that the Commission has proposed that residential and Small C&I customers be treated equally with regard to

[10] Note that Table 2 pertains only to *non-shopping* GM customers. See the Company's response to OSBA-I-3 for similar information on GM customers that have switched to an alternative supplier.

the frequency of default service price changes.[11] Second, the Company's response to OSBA-I-9 indicates that Duquesne Power's cost of supplying default service load will not move in step with Duquesne's proposed Small C&I price adjustments. As a result, Duquesne's Small C&I default service rates would not be based on the cost incurred by Duquesne Power to acquire default service supply in the open market.

Q. Has the Company proposed to adjust the risk premium applicable to Small C&I customers to reflect the fact that Small C&I generation rates would be adjusted annually under the Company's Plan?

A. Yes. Duquesne proposes to set the Small C&I risk premium at 1.5 mills per kWh, rather than at the 3.0 mills per kWh level proposed for residential customers.

Q. Has the Company explained how it arrived at a Small C&I risk premium of 1.5 mills per kWh?

A. Not to my knowledge.

Q. Given the fact that residential customers would receive a three-year fixed default service rate under Duquesne's Plan, does a residential/Small C&I risk premium differential of just 1.5 mills per kWh seem reasonable?

A. In my opinion, no. If one examines the Company's Plan from the perspective of a residential customer, Duquesne is offering an additional two years' fixed default service rate for the equivalent of an "insurance premium" of approximately 2.1%.[12] If Duquesne were to

[11] See the Commission's recently issued Advance Notice of Final Rulemaking (i.e., "Proposed Regulations") at Docket No. L-00040169.

[12] The Company's proposed residential default service rate of 7.156¢ per kWh includes a risk premium of 0.30¢ per kWh. Assuming that the residential risk premium would be the same as the Small C&I class if residential rates were to be adjusted in 2009 and 2010, the Company's proposed generation rate of 7.156¢ per kWh would decrease by 0.15¢ per kWh (excluding taxes and losses). Dividing 0.15 by (7.156 minus 0.15) equals 2.1%.

offer Small C&I customers a three-year fixed rate option for just 0.15¢ per kWh (excluding taxes and losses) more than the 7.083¢ per kWh contained in its Plan, I expect that many Small C&I customers would choose to purchase the additional two years of fixed price service.

Q. Mr. Kalcic, should the Commission order Duquesne to offer Small C&I customers a default service price that is fixed for three years?

A. Yes.

Q. What rate would you recommend for Small C&I customers under that scenario?

A. Based upon the parameters contained in Duquesne's Plan, I recommend that Small C&I customers be offered a three-year fixed rate of 7.252¢ per kWh.[13]

Q. All else equal, has Duquesne indicated that Duquesne Power would be willing to serve Small C&I customers at a fixed price?

A. Yes, in response to OSBA-I-10, although Duquesne does continue to support its filed proposal for annual adjustments.

Q. All else equal, at what fixed rate would Duquesne Power be willing to serve Small C&I customers?

A. To derive that rate, it would be necessary to begin with the 6.13¢ (excluding associated line losses and GRT) that Duquesne calculated from the observed procurements of other companies. It would then be necessary to add the same 3.0 mill risk premium which is proposed in Duquesne's Plan as the measurement of the risk of fixing Residential rates for three years. Finally, it would be necessary to gross up the

[13] Duquesne's Plan assumes that the Commission will approve Duquesne's estimate of the prevailing market prices for 2008 by comparing those prices to the 13 competitive supply solicitations Duquesne examined. In POLR III, the Commission approved Duquesne's estimate of prevailing market prices for three years, based on record evidence comparing Duquesne's prices to the results of a solicitation in a neighboring jurisdiction in PJM. See Docket No. P-00032071, Opinion and Order, p. 22.

result for losses and taxes. That would produce a three-year fixed rate for Small C&I customers of 7.252¢ per kWh.[14]

Small C&I Rate Design

Q. Mr. Kalcic, please describe the Company's current generation-related rate design for Small C&I customers.

A. At present, GS/GM customers pay a demand charge of $9.28 per kW, on all demand in excess of 5 kW per month. GS/GM customers are also subject to a declining block energy charge wherein the first 1,300 kWhs per month cost 7.9914¢ per kWh, and all monthly usage in excess of 1,300 kWh is priced at 3.4824¢ per kWh.

GMH customers currently pay a demand charge of $9.66 per kW, on all demand in excess of 5 kW per month. In addition, GMH customers are subject to a declining block energy charge, which varies by season. From June through September, GMH customers pay 8.2699¢ per kWh for the 1,300 kWhs of usage, and 3.0442¢ per kWh for all additional usage. From October through May, the corresponding energy charges are 7.2685¢ and 3.0442¢, respectively.

Q. What type of Small C&I generation rate design does Duquesne propose to implement by the end of the Plan period?

A. Assuming that there were no MPM-related changes in average default service rates, all GS/GM and GMH customers would pay a flat rate of 7.083¢ per kWh for generation, beginning January 1, 2010.

Q. Is it appropriate to eliminate Duquesne's generation-related demand charges and declining-block energy charges for Small C&I customers over the course of the proposed three-year Plan period?

A. Yes. These types of complex rate structures are simply a remnant of Duquesne's cost of serving customers with the power plants the

[14] In other words, using the same format as Exhibit NSF-13, the rate would be the sum of 6.130¢ (average of recent solicitations) plus 0.300¢ (risk premium) plus 0.394¢ (line losses) plus 0.428¢ (GRT) or 7.252¢ per kWh.

company used to own and the rate unbundling that took place during restructuring. Generally, such charges produce a wide disparity in the average generation rates paid by individual Small C&I customers. However, such disparities have not been shown to be market-based. Accordingly, it is appropriate to eliminate demand charges and declining-block energy charges for default service.

Q. Are you aware of any Commission action that supports your viewpoint?

A. Yes. It is my understanding that the Commission has proposed to eliminate generation-related demand charges and declining-block energy charges in its Proposed Regulations.

Q. Does the OSBA take issue with the *pace* at which Duquesne is proposing to move toward flat rates?

A. No. Duquesne has proposed a phase-in (rather than a flash cut) to flat rates in order to mitigate the customer bill impacts associated with the rate design change. Counsel informs me that Duquesne's proposal to establish flat rates by January 1, 2010 is acceptable to the OSBA.

Q. What is your recommendation with respect to Duquesne's proposed Small C&I rate design?

A. I recommend that the Commission adopt Duquesne's proposal to phase out its existing Small C&I declining-block energy charges and demand charges over the three-year Plan period.

Q. Does this conclude your direct testimony?

A. Yes.

REFERENCED INTERROGATORY RESPONSES

OSBA I-2
OSBA I-3
OSBA I-8
OSBA I-9
OSBA I-10

Office of Small Business Advocate
Interrogatories Set I

2. *Reference the Rate GM proof of revenue provided in the Company's response to* Item 1. Please provide a (separate) proof of revenue for POLR customers in each of the following Rate GM customer segments:

   a. 0.1 kW to 5.0 kW;
   b. 5.1 kW to 25.0 kW; and
   c. 25.1 kW and above.

   Note that the total or cumulative average supply rate per kWh across the above customer segments should equal the total Rate GM supply rate provided in response to Item 1.

Response:

Please see Attachment OSBA I-2.

An electronic version of this attachment is provided in spreadsheet 'DLC OSBA Set I 1-5 Attachments.xls'.

Attachment OSBA-I-2
Duquesne Light Company
Rate GM Proof of Revenue Calculation - POLR Customers

Segment (1)	2006 Billing Determinants POLR Load	Current Rates	Proposed Supply Rates (Exh. WVP-1) 2008	2009	2010	Current Rate Revenue	Proposed Revenue 2008	2009	2010
GM 0.1 to 5.0 kW									
First 5 kW	39,898	$0.00	$0.00	$0.00	$0.00	$0	$0	$0	$0
Additional kW	0	$9.28	$6.19	$3.09	$0.00	$0	$0	$0	$0
First 1300 kWh	6,501,827	$0.079914	$0.070830	$0.070830	$0.070830	$519,587	$460,524	$460,524	$460,524
Additional kWh	2,079,047	$0.034824	$0.052849	$0.061840	$0.070830	$72,401	$109,876	$128,567	$147,259
Total	8,580,874					$591,988	$570,400	$589,092	$607,783
Average Cents/kWh						6.90	6.65	6.87	7.08
GM 5.1 to 25.0 kW									
First 5 kW	844,568	$0.00	$0.00	$0.00	$0.00	$0	$0	$0	$0
Additional kW	1,054,845	$9.28	$6.19	$3.09	$0.00	$9,788,962	$6,525,975	$3,262,987	$0
First 1300 kWh	204,644,325	$0.079914	$0.070830	$0.070830	$0.070830	$16,353,947	$14,494,958	$14,494,958	$14,494,958
Additional kWh	213,845,604	$0.034824	$0.052849	$0.061840	$0.070830	$7,446,959	$11,301,532	$13,224,108	$15,146,684
Total	418,489,929					$33,589,868	$32,322,465	$30,982,053	$29,641,642
Average Cents/kWh						8.03	7.72	7.40	7.08
GM 25.1 kW and Above									
First 5 kW	431,397	$0.00	$0.00	$0.00	$0.00	$0	$0	$0	$0
Additional kW	4,500,131	$9.28	$6.19	$3.09	$0.00	$41,761,214	$27,840,810	$13,920,405	$0
First 1300 kWh	108,937,026	$0.079914	$0.070830	$0.070830	$0.070830	$8,705,593	$7,716,010	$7,716,010	$7,716,010
Additional kWh	1,695,296,707	$0.034824	$0.052849	$0.061840	$0.070830	$59,037,013	$89,594,784	$104,836,325	$120,077,866
Total	1,804,233,733					$109,503,820	$125,151,604	$126,472,739	$127,793,875
Average Cents/kWh						6.07	6.94	7.01	7.08
GM Total									
First 5 kW	1,315,864					$0	$0	$0	$0
Additional kW	5,554,976					$51,550,176	$34,366,784	$17,183,392	$0
First 1300 kWh	320,083,178					$25,579,127	$22,671,491	$22,671,491	$22,671,491
Additional kWh	1,911,221,358					$66,556,373	$101,006,193	$118,189,001	$135,371,809
Total	2,231,304,536					$143,685,676	$158,044,468	$158,043,884	$158,043,300
Average Cents/kWh						6.44	7.08	7.08	7.08

1/ Customers assigned to each segment based on their peak monthly metered demand in 2006.

Office of Small Business Advocate
Interrogatories Set I

3. Please provide a bill frequency analysis for Rate GM customers taking *POLR service* in 2006, showing a) the numbers of customers, and b) the number of kWhs consumed, for each of the following billing demand ranges: 0.1 to 5.0 kW; 5.1 to 25.0 kW; 25.1 to 100.0 kW; 100.1 to 200 kW; 200.1 to 300.0 kW; and over 300 kW.

Response:

Please see Attachment OSBA I-3.

An electronic version of this attachment is provided in spreadsheet 'DLC OSBA Set I I-5 Attachments.xls'.

Attachment OSBA-I-3
Duquesne Light Company
Rate GM Bill Frequency Analysis

Monthly Metered Demand Range (1)	POLR Customers	POLR kWh	Shopping Customers	Shopping kWh	Total Customers	Total kWh
0 kW Customers (2)	17,014	83,260,735	1,890	12,527,727	18,904	95,788,462
0.1 to 5.0 kW	1,741	8,580,874	430	1,720,549	2,171	10,301,423
5.1 kW to 25.0 kW	17,400	418,489,929	3,598	78,605,990	20,998	497,095,919
25.1 to 100.0 kW	5,720	724,639,002	2,032	210,276,574	7,752	934,915,576
100.1 to 200 kW	971	481,477,121	478	161,980,169	1,449	643,457,290
200.1 to 300 kW	302	289,606,132	150	97,401,186	453	387,007,318
300 kW and Greater	196	308,511,478	100	104,180,615	297	412,692,093
Total	43,345	2,314,565,271	8,678	666,692,810	52,023	2,981,258,081

1/ Customers assigned to each segment based on their peak monthly metered demand in 2006.
2/ Customers assigned to rate GS, Rate Plan 200.

Office of Small Business Advocate
Interrogatories Set I

8. Reference page 11, line 15 through page 12, line 4 of Duquesne Statement No. 3.

a. Does Mr. Fisher consider the 1% difference in residential versus Small C&I shopping shown in Exhibit NSF-1 to be significant? Please explain.
b. Please list all factors, circumstances and/or considerations that Mr. Fisher believes may influence a customer's decision to take electric service from an alternative supplier.
c. Please explain in detail how the information shown in Exhibit NSF-1 supports the conclusion that Small C&I customers "have more opportunities to shop than do residential customers."

Response:

The referenced section of testimony states that, "As Exhibit NSF-1 shows, Small C&I customers in the United States generally have somewhat higher switching levels than residential customers, indicating that Small C&I customers are somewhat more sophisticated about their service options and have more opportunities to shop than do residential customers. As a result, it is appropriate at this stage of market development to provide Small C&I customers with more exposure to market price adjustments, rather than fix their rates for three years. This will further promote retail competition, while not exposing these customers to the same market price movements that Duquesne proposes for Large C&I customers."

a. Mr. Fisher does not rely on the one percentage point difference in residential versus Small C&I shopping in Duquesne's service area shown in Exhibit NSF-1 to support the statement that Small C&I customers in the United States generally have somewhat higher switching levels than residential customers. Therefore, Mr. Fisher does not consider the one percentage point difference as significant to support his testimony.

b. There are numerous factors, circumstances and/or considerations that Mr. Fisher believes may influence a customer's decision to take electric service from an alternative supplier. While developing an exhaustive list of "all" items that may influence a customer's decision is not possible, Mr. Fisher believes such factors, circumstances and/or considerations may include:

1. Dollar amount of the customer's electric bill
2. Potential level of dollar savings that could be realized for the customer by electing service from an EGS (which is affected by the difference between EGS price levels and default service rates)

3. Volatility of the dollar amount of the customer's bill, and the extent to which EGSs can reduce this volatility
4. Whether or not EGSs guarantee savings off of default service rates
5. Degree to which the customer is educated about retail choice (from bill inserts, advertisements, etc.)
6. Amount of time and personnel (e.g., energy or facilities manager) the customer dedicates to the service decision
7. Customer's access to information needed to compare default service rates and EGS offers
8. Number of EGSs offering competitive options
9. Whether or not EGSs offer differentiated services and products (e.g., green products, load management, bundled services, additional price security, bill convenience, etc.)
10. Extent to which messages delivered through the advertising and marketing channels used by EGSs reach the customer
11. EGS affinity programs (e.g., frequent flyer miles programs)
12. Whether or not EGSs avoid serving certain types of customers (e.g., low-income, poor credit, high customer acquisition costs, etc.)
13. Retail access credits provided to the customer if it elects EGS service
14. Exit fees incurred if the customer elects EGS service
15. Loss of customer options if the customer elects EGS service (e.g., the right to return to the default service rate)
16. Customer switching rules and restrictions (e.g., minimum stays, wet signature rules, etc.)
17. Customer assignment programs (opt-out and opt-in)
18. Customer's perceived reliability of EGS service
19. Customer's perceived quality of EGS customer service
20. Extent to which customers are satisfied with the default service offered by the default service provider
21. Customer's education and sophistication
22. Customer's proficiency with the English language
23. Customer's access to a telephone.

Note that this is not an exhaustive list and is in no particular order of importance.

c. Exhibit NSF-1 shows that small C&I customers in the United States generally have somewhat higher switching levels than residential customers. The simple average of the shopping levels for the utilities listed in Exhibit NSF-1 is 27.45% for small C&I customers and 7.78% for residential customers. In other words, the percentage level of small C&I shopping in the United States is on average more than 3.5 times higher than that of residential customers. While the differences in shopping levels may be explained by many factors (as indicated in the response to b above), the overall higher levels of shopping among small C&I customers than residential customers across the United States suggests that EGSs may be more willing to serve small C&I customers and/or small C&I customers may be more willing to switch to an alternative supplier.

In Duquesne's service area, the portion of small C&I customers' load on EGS service exceeds the portion of residential customers' load on EGS service by 9%. Few suppliers are actively marketing to residential customers. While a number of EGSs serving the residential market made an initial foray into the retail market, virtually all but one of the EGSs serving residential customers has exited the market. By comparison, there are currently nine EGSs serving small C&I customers in Duquesne's service area.

Office of Small Business Advocate
Interrogatories Set I

9. Reference page 65, lines 5-24 of Duquesne Statement No. 3. Will the proposed Market Price Multiplier track the changes in cost incurred by Duquesne Power to acquire POLR supply for Small C&I customers in 2009 and 2010? Please explain.

Response:

The Market Price Multiplier will be calculated based on changes in wholesale electricity forward prices. The application of the Market Price Multiplier will allow default service rates to track the changes in market prices each year. The proposed Market Price Multiplier may or may not track the changes in cost incurred by Duquesne Power depending on how and when Duquesne Power chooses to acquire POLR supply. Duquesne Power has discretion regarding how best to assemble a supply portfolio to serve POLR customers at market prices since it assumes the associated costs and risks of such portfolio.

Office of Small Business Advocate
Interrogatories Set I

10. Reference Exhibit NSF-13. All else equal, if the referenced Small C&I regulatory risk premium of $1.50 per MWh were increased to $3.00 per MWh, would Duquesne Power agree to supply Small C&I customers with a three-year (2008-2010) fixed POLR price of $61.30 plus $3.00 or $64.30 (not including associated losses and GRT)? If not, why?

Response:

Yes, Duquesne Power would agree to supply small C&I customers with a three-year fixed POLR price at or about $64.30 (not including associated line losses and GRT). However, Duquesne Light does not believe this would be appropriate at this stage of market development. Duquesne Light supports an annual market price index adjustment to small C&I rates. In developing its Default Service Plan, Duquesne Light undertook an extensive effort to meet with the parties to develop a plan that balances the interests of customers, EGSs, and Duquesne Light. (See Mr. Eichenmiller's testimony at 9-15.) In response to stakeholder input that it was important for Duquesne Light to make further progress toward exposing more customers to shorter-term market price signals, Duquesne Light decided to propose reseting small C&I customer rates in 2009 and 2010 based on a market price index, so that retail rates for these customers (approximately 55,000 customers) would change from current levels for each year of the three year period.

APPENDIX

Qualifications of Brian Kalcic

Mr. Kalcic graduated from Illinois Benedictine College with a Bachelor of Arts degree in Economics in December, 1974. In May, 1977 he received a Master of Arts degree in Economics from Washington University, St. Louis. In addition, he has completed all course requirements at Washington University for a Ph.D. in Economics.

From 1977 to 1982, Mr. Kalcic taught courses in economics at both Washington University and Webster University, including such subjects as Microeconomic and Macroeconomic Theory, Labor Economics and Public Finance.

During 1980 and 1981, Mr. Kalcic was a consultant to the Equal Employment Opportunity Commission, St. Louis District Office. His responsibilities included data collection and organization, statistical analysis and trial testimony.

From 1982 to 1996, Mr. Kalcic joined the firm of Cook, Eisdorfer & Associates, Inc. During that time, he participated in the analysis of electric, gas and water utility rate case filings. His primary responsibilities included cost-of-service and economic analysis, model building, and statistical analysis.

In March 1996, Mr. Kalcic founded Excel Consulting, a consulting practice which offers business and regulatory services.

Mr. Kalcic has previously testified before the state regulatory commissions of Delaware, Kansas, Kentucky, Maine, Massachusetts, Minnesota, Missouri, New Jersey, New York, Ohio, Oregon, Pennsylvania, Texas, and the Bonneville Power Administration.

OSBA STATEMENT NO. 2

APR 26 2007

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Petition of Duquesne Light Company for Approval of Default Service Plan for the Period January 1, 2008 Through December 31, 2010	: : : :	DOCKET NO. P-00072247

Rebuttal Testimony of

BRIAN KALCIC

On Behalf of the

Office of Small Business Advocate

Date Served: April 13, 2007

Date Submitted for the Record: _____

Rebuttal Testimony of Brian Kalcic

Q. Please state your name and business address.

A. Brian Kalcic, 225 S. Meramec Avenue, St. Louis, Missouri 63105.

Q. Have you previously submitted direct testimony in this proceeding?

A. Yes, I have.

Q. What is the subject of your rebuttal testimony?

A. My rebuttal testimony responds to certain points raised in the direct testimony of the following witnesses: 1) Mr. Thomas J. Butler on behalf of Dominion Retail, Inc. ("Dominion"); 2) Mr. Frank Lacey on behalf of Direct Energy Services, LLC and the Retail Energy Supply Association ("Direct/RESA"); 3) Mr. Richard J. Hudson Jr. on behalf of Strategic Energy, LLC ("Strategic");[1] and 4) Mr. Steven W. Ruback on behalf of Constellation NewEnergy, Inc. ("Constellation").

Dominion

Q. On page 3 of his direct testimony, Mr. Butler comments on Duquesne's proposed POLR rate of 7.156¢ per kWh for residential customers. Mr. Butler concludes that Duquesne's proposed residential rate is at the lower end of his estimate of a range of reasonable market prices, and that "Duquesne appears to be absorbing significant market risks with minimal compensation." Do you have any comment?

A. Yes. Mr. Butler does not comment directly on Duquesne's proposed POLR rate of 7.083¢ per kWh for Small C&I customers. However, as I discussed in my direct testimony, the Company's proposed Small C&I generation rate of 7.083¢ per kWh includes annual price adjustments, but reflects a risk premium discount of just 0.15¢ per kWh compared to residential customers. If Duquesne is willing to absorb significant market risk, with minimal compensation, by offering a three-year fixed rate of 7.156¢ per kWh to

[1] While Mr. Hudson has submitted direct testimony on behalf of both Strategic and RESA, my rebuttal testimony addresses only Part II of his testimony, which was submitted on behalf of Strategic only.

residential customers, it should also be required to offer a three-year fixed rate, at an equivalent risk level, to Small C&I customers.[2]

Direct/RESA & Strategic

Q. On pages 11-12 of his direct testimony, Mr. Lacey recommends that Duquesne implement a quarterly auction for its residential and Small C&I customers. Similarly, on pages 17-18 of his direct testimony, Mr. Hudson recommends that Duquesne conduct quarterly competitive solicitations for the supply needs of residential and Small C&I customers, in order to produce "market-reflective and responsive pricing" for such customers. Do you have any comment?

A. Yes. Both witnesses recommend quarterly solicitations for 100% of Duquesne's residential and Small C&I default service load so that default service rates reflect market prices as closely as possible. However, the Commission did not specify that quarterly solicitations covering 100% of default service load would be required in its Advance Notice of Final Rulemaking (i.e., "Proposed Regulations") at Docket No. L-00040169. Instead, the Commission indicated that default service providers should use a mix of procurement strategies, with varying contract lengths, in order to mitigate price volatility. Using quarterly solicitations to acquire 100% of default service requirements would expose residential and Small C&I customers to unnecessary price volatility.

In addition, neither Mr. Lacey nor Mr. Hudson acknowledges the higher transaction costs that would be associated with constantly running quarterly auctions. Presumably, such costs would be recoverable from default service customers and result in higher default service rates.

Q. On page 13 of his direct testimony, Mr. Lacey states that while all default service customers would ultimately benefit from a monthly (or more frequent) price adjustment, he believes "that the small C&I customers can act in a much more deliberate manner already and should be entitled to benefit from monthly-priced auctions." How do you respond?

[2] Based upon the parameters contained in Duquesne's Plan, the equivalent three-year fixed rate for Small C&I customers would be 7.252¢ per kWh. See pages 13-15 of OSBA Statement No. 1.

A. I find it hard to believe that Small C&I customers would welcome monthly default service price adjustments. However, leaving that aside, Mr. Lacey's comment is entirely inappropriate in that it attempts to distinguish between the type of default service offerings that should be made available to residential versus Small C&I customers. In its Proposed Regulations, the Commission has stated that all Small C&I customers with peak demands less than or equal to 25 kW should be treated the same as residential customers. Therefore, at a minimum, there should not be any difference between the frequency of default service price adjustments applicable to residential and (less than 25 kW) Small C&I customers over the course of Duquesne's Plan.

Q. On pages 15-16 of his direct testimony, Mr. Lacey discusses a study performed by Intelometry Inc. ("Intelometry") on Direct's behalf that purports to compare the Company's *POLR III* tariff rates for residential and Small C&I customers to PJM clearing prices for the Duquesne zone. Mr. Lacey concludes, in part, that "in all but five of the 23 months analyzed, a typical small C&I customer would have paid less had Duquesne procured power on a monthly basis." Do you have any comment?

A. Yes. There are a number of limitations in the Intelometry study that call Mr. Lacey's conclusion into question. First, the study assumes that all market-related energy costs are derived by purchasing 95% of a Small C&I customer's electricity requirement in the day-ahead market with the remaining 5% purchased in the real-time market. However, the study does not include any adjustment to cover the transaction costs that would be associated with such daily purchases. Moreover, the study does not appear to include any allowance for differences in actual versus expected customer usage, which could necessitate additional real-time purchases (or energy sales) at prices that deviate from those included in the study.

Second, the study looks to measure the costs associated with serving a "typical" Small C&I customer, not the Small C&I class as a whole. Since Duquesne's *POLR III* rates for Small C&I customers contain demand charges, the actual POLR III tariff rate for the Small C&I *class* as a whole will likely differ from that of the typical Small C&I *customer* used in the Intelometry study. Therefore, even if one accepts Mr. Lacey's conclusion

regarding a "typical" customer, the study provides no information regarding how Duquesne's overall Small C&I class would have fared over the period studied. Finally, it should be noted that since the Intelometry study examines only a 23 month period during POLR III, the reported results, at best, apply only during that particular period and cannot be generalized to apply to other time periods and/or default service providers.

Constellation

Q. On page 3 of his direct testimony, Mr. Ruback recommends that Duquesne's existing declining block rate design for Small C&I customers be eliminated immediately (rather than phased out over two years as under Duquesne's Plan). However, Mr. Ruback does not appear to offer any opinion on the Company's proposal to phase out its existing Small C&I demand charges. Assuming that the Commission were to adopt Mr. Ruback's recommendation, would there be any problem with combining a "flash-cut" elimination of the Company's Small C&I declining block energy charges with a phase out of Small C&I demand charges?

A. It would depend on how the hypothetical "hybrid" rate design was carried out. Under the Company's Plan, GM and GMH customers would be subject to a flat rate energy charge of 7.083¢ per kWh beginning January 1, 2010, with *no* demand charge. Obviously, if the energy charge applicable to GM and GMH customers were to be set at 7.083¢ per kWh sometime earlier than January 1, 2010, then the demand charges applicable to these customers would also have to be eliminated at that same time. Otherwise, the GM and GMH classes would be paying an overall generation rate in excess of the Company's estimate of prevailing market prices.

Stated differently, as long as GM and GMH customers are subject to demand charges, the average energy charge paid by these customers must be lower than market.

Q. What do you recommend?

A. If the Commission chooses to adopt Mr. Ruback's recommendation to eliminate Duquesne's declining block energy charges for Small C&I customers immediately, I recommend that the applicable Small C&I rate

design be conducted on a revenue neutral basis, by rate class, in order to maintain the proposed overall class average generation rates shown in each year of Duquesne's Plan.

Q. Does this conclude your rebuttal testimony?

A. Yes.

OSBA STATEMENT NO. 3

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Petition of Duquesne Light Company for Approval of Default Service Plan for the Period January 1, 2008 Through December 31, 2010	: : : :	DOCKET NO. P-00072247

Surrebuttal Testimony of

BRIAN KALCIC

On Behalf of the

Office of Small Business Advocate

Date Served: April 20, 2007

Date Submitted for the Record: _____

Surrebuttal Testimony of Brian Kalcic

Q. Please state your name and business address.

A. Brian Kalcic, 225 S. Meramec Avenue, St. Louis, Missouri 63105.

Q. Have you previously submitted direct and rebuttal testimony in this proceeding?

A. Yes, I have.

Q. What is the subject of your surrebuttal testimony?

A. My surrebuttal testimony responds to various points raised in the rebuttal testimony of the following witnesses: 1) Mr. Frederick J. Eichenmiller and Mr. Neil S. Fisher on behalf of Duquesne; 2) Mr. Frank Lacey on behalf of Direct Energy Services, LLC and the Retail Energy Supply Association ("Direct/RESA"); and 3) Mr. Steven W. Ruback on behalf of Constellation NewEnergy, Inc. ("Constellation").

Duquesne

Q. On pages 3-4 of his rebuttal testimony, Mr. Eichenmiller characterizes the Company's Plan as having fairly balanced the desire of Small C&I customers for stable rates with the expressed desire of marketers for more frequent price changes. Do you have any comment?

A. Yes. Mr. Eichenmiller expresses satisfaction with having balanced the interests of Small C&I customers and marketers, while at the same time ignoring the fact that the Company's Plan chooses *not* to balance those same interests with respect to the frequency of residential default-service price changes. As I pointed out in my rebuttal testimony, various marketers are interested in more frequent adjustments in residential default-service rates than Duquesne has proposed. However, Mr. Eichenmiller offers no explanation as to why it is appropriate that marketers' interest in more frequent price changes should be accommodated with respect to Small C&I default service but not residential default service.

Q. On pages 4-5 of his rebuttal testimony, Mr. Eichenmiller notes that more EGSs are actively serving Small C&I customers in Duquesne's service area than are serving residential customers. Mr. Fisher makes the same point on pages 51-52 of his rebuttal testimony. Based upon this observation, both witnesses conclude that Small C&I customers have greater opportunities to shop than residential customers, and therefore annual price changes are more appropriate for Small C&I customers than residential customers. How do you respond?

A. If Small C&I customers do indeed have greater opportunities to shop than residential customers, those opportunities have not translated into more Small C&I customers switching to an alternative supplier.[1] As I indicated in my direct testimony, if customer-switching levels are to be used as a proxy for the inherent differences in shopping opportunities available to various customer groups, the Company's Plan should be targeting residential customers for more frequent default service price changes, not Small C&I customers.

Q. On page 5 of his rebuttal testimony, Mr. Eichenmiller argues that it would be inappropriate to adjust residential rates either quarterly or annually at this time, since such rate changes would be inconsistent with: a) how residential rates were designed in Duquesne's POLR III Plan; b) the capped rates that will be in effect through 2009 or 2010 for residential customers served by the Commonwealth's other major electric utilities; and c) the proposed 2010 residential bridge plan sponsored by PPL Electric Utilities Corporation ("PPL"). Do you have any comment?

A. Yes. Mr. Eichenmiller is correct that Duquesne's Plan for residential customers is consistent with the above precedents. However, Mr. Eichenmiller fails to mention that the Company's Plan for Small C&I customers, if adopted, would be totally *inconsistent* with the same precedents, namely: 1) how Small C&I rates were designed in Duquesne's POLR III Plan; 2) the capped rates that will be in effect through 2009 or 2010 for Small C&I customers served by the Commonwealth's other major electric utilities; and 3) the proposed 2010 Small C&I bridge plan sponsored by PPL Electric

[1] See Table 1 of OSBA Statement No. 1.

Utilities Corporation ("PPL"). Specifically, in all of the precedents cited by Mr. Eichenmiller, Small C&I rates are adjusted no more frequently than are residential rates.

Q. On page 6 of his rebuttal testimony, Mr. Fisher suggests that Duquesne's Plan should not be measured against the Commission's Proposed Regulations, since such regulations are not yet final and may change. Instead, on pages 10-12 of his rebuttal testimony, Mr. Fisher claims that Duquesne's Plan should be appropriately viewed as being modeled after its prior default service plans, which have been tested and "proven" to be successful. Mr. Kalcic, is Duquesne's Plan consistent with its prior default service plans?

A. No. The Company's Plan is inconsistent with its prior plans in at least two (2) important respects: a) the Plan would not offer Small C&I customers a three-year (i.e., 2008-2010) fixed default service rate; and b) the Plan would treat the Company's Small C&I customers differently than its residential customers with respect to the frequency of default service price changes.

Q. On page 13 of his rebuttal testimony, Mr. Fisher notes that RESA has taken the position that EGSs would not have sufficient incentive to commit the resources necessary to develop the competitive retail electric market in the Commonwealth under the Commission's Proposed Regulations. From this, Mr. Fisher concludes that he is "even more convinced that small customers require a default service now that provides these customers stable rates." Do you have any comment?

A. Yes. If it is important that small customers be offered stable rates, Duquesne should offer a three-year fixed rate to its Small C&I customers, not just to its residential customers.

Q. On page 26 of his rebuttal testimony, Mr. Fisher states that since you employed his market price analysis to arrive at a recommended Small C&I three-year fixed rate of 7.252¢ per kWh, the "OSBA must believe that Duquesne's proposed rate meets the prevailing market test." Is Mr. Fisher's assertion correct?

A. No. As I indicated in my direct testimony, I do not believe that Duquesne has adequately demonstrated that its proposed Small C&I default service rate of 7.083¢ per kWh properly reflects prevailing market prices. However, I continue to recommend that the Commission order Duquesne to offer Small C&I customers a default service rate that is fixed for three years. My recommendation that Duquesne offer Small C&I customers a specific three-year fixed rate of 7.252¢ per kWh is premised upon the Commission accepting the Company's estimate of prevailing market prices. For example, if the Commission were to accept Duquesne's estimate of the prevailing market price for residential customers, it should also adopt the Company's estimate for Small C&I customers, since the relative difference between the two classes is consistent with that observed in recent market solicitations (e.g., Penn Power).

Q. On page 27 of his rebuttal testimony, Mr. Fisher states that the OSBA does not believe that the proposed Small C&I default service rate is too high. Is that correct?

A. No. As I explained in my direct testimony, the Company has not shown that the absolute levels of its proposed class-specific risk premiums are market based. Absent such information, one cannot conclude that a residential risk premium of 3.0 mills per kWh is adequate compensation for a three-year fixed rate (compared to a 1.5 mills per kWh risk premium for Small C&I rates that would be adjusted annually). However, if the Commission determines that the 3.0 mills risk premium for residential customers is adequate, then one would have to conclude that the 1.5 mills risk premium for Small C&I customers is too high and, therefore, that Duquesne's proposed Small C&I default service rate of 7.083¢ is too high.

Q. On pages 50-51 of his rebuttal testimony, Mr. Fisher discusses the Company's proposed MPM. In response to the OSBA's criticism that measuring changes in wholesale electricity prices based upon the market results taken from the 20 consecutive trading days ending October 1 (2008 and 2009) would expose Small C&I customers to unnecessary price volatility, Duquesne has offered to amend its Plan by moving the 20 day

trading period back one or two months.[2] Would such a change be sufficient to protect Small C&I customers?

A. No.

Q. Why not?

A. While moving the trading period back one or two months would arguably lessen Small C&I customers' exposure to the price volatility inherent in the hurricane season, it would not correct the fundamental flaw in the Company's methodology.

Q. What is that flaw?

A. The fundamental flaw stems from the Company's proposal to use a single 20-day window to measure market prices. Such an approach is equivalent to a default service provider acquiring 100% of its default service requirements within that same short time period. As I discussed in my direct testimony, the Commission is seeking ways to avoid unnecessary price volatility for default service customers. As long as Duquesne's proposed MPM is based upon a single 20-day trading window, it would fail to comport with the Commission's stated goal.

Q. Mr. Kalcic, assume that the Commission were to adopt the Company's proposal to adjust Small C&I prices annually, based upon an MPM-type mechanism. How should such a mechanism be implemented?

A. Similar to what the Commission ordered in the recent Penn Power default service case, I would recommend that the MPM be based upon at least two (2) hypothetical solicitations (i.e., two distinct trading periods). For example, if the Commission were to adopt Duquesne's offer to use market information from the 20 trading days ending November 1, it should also require Duquesne to combine that information with the market information taken from the 20 trading days ending May 1 (i.e., six months earlier). Specifically, Duquesne should be ordered to average the May 1 and November 1 outcomes, giving equal weight to each, *just as if Duquesne Power were going to market for 50% of its POLR requirements in each of those trading periods.* This

[2] In other words, Duquesne is now willing to use either the 20 consecutive trading days ending November 1, or the 20 consecutive trading days ending December 1 in place of its original October 1 proposal.

blended outcome would then be used to adjust Small C&I prices beginning January 1 of the following year.

Q. On page 52 of his rebuttal testimony, Mr. Fisher states that while he recognizes "that there is considerable diversity among small C&I customers, I believe it is appropriate at this stage of market development in Duquesne's service area to provide small C&I customers with more exposure to market price adjustments, rather than fix their rates for three years." Do you have any comment?

A. Yes. If Duquesne really wishes to balance diversity and "market development" considerations, it would be much better to offer Small C&I customers with peak demands less than 25 kW a three-year fixed price option (and adjust the default service rates applicable to Small C&I customers with demands in excess of 25 kW) rather than simply adjust the rates of all Small C&I customers. As I pointed out in my previous testimony, shopping by Small C&I customers with peak demands less than 25 kW is surprisingly low given the fact that these customers face default-service rates significantly above what Duquesne represents to be the market price.

Direct/RESA

Q. On pages 5-6 of his rebuttal testimony, Mr. Lacey references the discussion presented on page 12 of OSBA Statement No. 1, wherein you conclude that the frequency of default service price changes would likely have little impact on the probability of certain GM customers switching to an alternative supplier. Mr. Lacey responds that the reason such customers have not shopped is "because there are few competitive suppliers in the market that are serving this market segment – and this lack of market penetration is directly related to POLR design flaws." Specifically, Mr. Lacey claims that it is too risky for EGSs to invest in markets where the default service price is disconnected from the market price. Do you have any comment?

A. Yes. Duquesne states that there are currently nine (9) EGSs serving Small C&I customers, despite the fact that POLR III rates for Small C&I customers

have been fixed for three years.[3] Apparently, these nine suppliers subscribe to a different business model than that espoused by Mr. Lacey. More to the point, either these nine EGSs are not marketing to enough Small C&I customers, or a large number of customers have received offers and chosen to ignore them. Either way, Small C&I customers as a group are not shopping in any greater numbers than residential customers, despite the larger number of EGSs serving the Small C&I market in Duquesne's service area.

If Mr. Lacey is correct that Small C&I customers are not shopping because only nine EGSs are serving the Duquesne market, one may wonder whether the majority of Duquesne's Small C&I customers would ever switch to an alternative supplier, even if more EGSs were to enter the market.

Constellation

Q. On page 2 of his rebuttal testimony, Mr. Ruback states that the proper way to eliminate declining block rates for Small C&I customers without violating principles of gradualism is to establish more homogeneous sub-classes within Duquesne's existing GM and GMH rate schedules. Such an approach would purportedly allow Duquesne to eliminate declining block rates in one-step, rather than over a "three-year phase-out" period. Do you have any comment?

A. Yes. First, Duquesne proposes to eliminate its Small C&I declining block rate design in three steps over *two* (not three) years. Thus, the Company's Plan is more aggressive than Constellation suggests. Second, Mr. Ruback recommends that Duquesne's Small C&I customers be grouped into more homogeneous rate classes. However, Mr. Ruback gives no guidance as to the number of new rate classes that should be created or how such a process could be implemented at the conclusion of this proceeding. Finally, I would note that the whole process needed to establish more homogeneous rate classes (with separate default service rates) would come to naught on January 1, 2010, since Constellation's proposal, like Duquesne's Plan, would result in a single flat rate of 7.083¢ per kWh for *all* Small C&I customers at that time.

[3] Duquesne states that there are currently two (2) EGSs serving its residential customers.

Q. Does this conclude your surrebuttal testimony?

A. Yes.